

<b>SM Sydell Hotels LLC v Yucaipa U.S. Hospitality Partners Holdings, Inc.</b>
2019 NY Slip Op 30918(U)
March 26, 2019
Supreme Court, New York County
Docket Number: 656028/2017
Judge: Barry Ostrager
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SUPREME COURT OF THE STATE OF NEW YORK  
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART IAS MOTION

-----X  
SM SYDELL HOTELS LLC

INDEX NO. 656028/2017

Petitioner,

MOTION DATE Mar. 22, 2019

- v -

YUCAIPA U.S. HOSPITALITY PARTNERS HOLDINGS, INC.,

MOTION SEQ. NO. 005 & 007

Respondent.

**DECISION AND ORDER**

-----X  
The following e-filed documents, listed by NYSCEF document number (Motion 005) 178, 179, 180, 181, 182, 183, 184, 185, 186, 187, 188, 189, 190, 191, 196, 202, 203, 204, 205, 206, 207, 208, 209, 210, 211, 212, 213

were read on this motion to/for CONFIRM/DISAPPROVE AWARD/REPORT

The following e-filed documents, listed by NYSCEF document number (Motion 007) 197, 198, 199, 200, 201

were read on this motion to/for STAY

HON. BARRY R. OSTRAGER:

Petitioner SM Sydell Hotels LLC (“Sydell”) moves to confirm the findings of a valuation proceeding, pursuant to CPLR § 7510, and to compel Respondent Yucaipa U.S. Hospitality Partners Holdings, Inc. (“Yucaipa”) to close on a contractual buyout in accordance with the determination of the valuation proceeding. Respondent Yucaipa opposes and cross moves for an order staying proceedings in this Court pending a separate JAMS arbitration that was initiated by Yucaipa to determine whether Sydell’s alleged misconduct during the valuation proceeding renders the result in the valuation proceeding invalid. For the reasons stated herein, Petitioner’s motion is denied and Respondent’s cross motion is granted.

## Background

Sydell and Yucaipa are the two sole members of Sydell Holdings LLC (the “Company”) pursuant to a September 15, 2011 Operating Agreement (the “Agreement”). In the Agreement, the parties agreed that Sydell would serve as the Managing Member and manage and direct the affairs of the Company. The parties further purportedly agreed that Andrew Zobler, the CEO of Sydell, would serve as CEO of the Company and would remain in that position unless and until a court or arbitral panel made a final determination that Sydell had engaged in gross negligence, fraud, willful malfeasance, or a material breach of the Agreement.

In September 2017, Ronald Burkle, Yucaipa’s principal, allegedly threatened to breach the Agreement by, *inter alia*, terminating Zobler. In response, Sydell initiated a JAMS arbitration pursuant to Section 13.4 of the Agreement, which specifically provides for the arbitration of all disputes before JAMS in California.

Immediately thereafter, Petitioner Sydell commenced a special proceeding before this Court to enjoin Respondent Yucaipa from replacing Zobler as CEO of the Company during the pendency of the JAMS arbitration.<sup>1</sup>

On or about October 2, 2017, Sydell invoked its right under Section 10.6 of the Agreement to cause the Company to buy out Yucaipa’s 50% interest. Section 10.6 of the Agreement makes provision for the Managing Member (Sydell) to initiate a buyout procedure. The provision contemplates the appointment of a valuation arbitrator with specialized knowledge who is authorized to conduct an expedited proceeding to determine the buyout price. Once the buyout price is determined, Yucaipa is presumably obligated to close on the buyout, although

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<sup>1</sup> It appears that Sydell ultimately opted to withdraw that arbitration request after Sydell invoked its contractual buyout rights.

Sydell retains the power to cancel the buyout proceeding even after determination of the buyout price.

On October 3, 2017, Yucaipa stipulated, on the record in this Court, not to replace Zobler as CEO and the parties further agreed to continue to act in good faith with respect to the contemplated buyout. (*See* Oct. 3, 2017 Transcript [NYSCEF Doc. No. 43]). Thus, the special proceeding was resolved on consent and this Court agreed to retain jurisdiction in the event of any further disputes. *Id.*

Shortly thereafter, the parties selected a valuation arbitrator, in compliance with Section 10.8 of the Agreement, and commenced valuation proceedings. Section 10.6 contemplates that, shortly after a neutral arbitrator's valuation determination, Yucaipa will close on the sale of its interests in the Company.

In November 2018, toward the end of the valuation proceeding, Yucaipa allegedly communicated to Sydell that Yucaipa had no intention to close on the buyout. On November 27, 2018, Yucaipa sent a letter to the buyout arbitrator asserting that Yucaipa would no longer participate in the proceedings and that the process should be considered void. Yucaipa's argument was based on allegations concerning purportedly undisclosed deals, concealed third-party valuations, and misallocated expenses that may have corrupted the neutral valuation process.

In December 2018, Yucaipa commenced a separate arbitration proceeding with JAMS in California (the "California Arbitration"). In the California Arbitration, Yucaipa seeks, *inter alia*, a declaration that the contractual buyout process was procedurally and substantively flawed. The California Arbitration was purportedly initiated pursuant to Section 13.4 of the Agreement which

provides for JAMS arbitration of “[a]ll disputes, claims and controversies arising out of or relating to this Agreement.”

Sydell moved by order to show cause for an order compelling Yucaipa to participate in and close on the buyout. Sydell also moved to enjoin the California Arbitration. The Court directed the parties to complete the valuation proceeding, however, the Court stayed a final closing of the buyout pending further order from the Court. The Court also denied Sydell’s motion to enjoin the California Arbitration from proceeding.

On February 19, 2019, the valuator issued a final determination of the fair market value of Yucaipa’s interests in the Company.

Sydell moves to confirm the valuation and compel Yucaipa to close on the buyout. Yucaipa cross moves for a stay of this Court’s proceedings and for an order compelling Sydell to participate in the on-going California Arbitration.

### **Discussion**

The central issues before the Court are: (1) whether the buyout procedures of Section 10.6 of the Agreement are subject to the broad arbitration provisions contained in Section 13.4; and (2) whether such an issue should be determined in the California Arbitration or by this Court.

If the buyout procedures of Section 10.6—whereby the parties select a neutral arbitrator to determine the value of Yucaipa’s interests in the Company—are not further subject to Section 13.4’s broad, general arbitration provision purporting to govern all disputes arising under the Agreement, then Sydell’s motion to compel a closing should be granted. If, however, the broad arbitration provisions of Section 13.4 govern disputes arising out of Section 10.6’s potentially

separate valuation arbitration, then a closing should be stayed and the parties compelled to participate in the California Arbitration.

Sydell argues that Section 10.6 of the Agreement provides a streamlined valuation arbitration procedure in the event that Sydell exercises its right to redeem Yucaipa's interest in the Company and the parties disagree about the valuation. Thus, Sydell argues that Section 10.6 contains its own arbitration process that is not subject to further JAMS arbitration under the Agreement's broader dispute resolution provisions in Section 13.4.

Yucaipa, in its opposition and cross motion, asserts that the issue of whether disputes arising from the valuation arbitration—specifically, Yucaipa's allegation that Sydell corrupted the valuation proceeding—is an issue of arbitrability that the California arbitrator, and not this Court, must determine. Thus, Yucaipa argues that the threshold issue of arbitrability must be determined in the California Arbitration.

It is undisputed that Section 13.4 of the Agreement provides:

*All disputes, claims and controversies arising out of or relating to this Agreement, including any and all disputes, claims or controversies arising out of or relating to (i) the Company, (ii) any Member's rights and obligations hereunder, (iii) the validity or scope of any provision of this Agreement, (iv) whether a particular dispute, claim or controversy is subject to arbitration under this Section 13.4 and (v) the power and authority of any arbitrator selected hereunder, that are not resolved by mutual agreement shall be submitted to final and binding arbitration before JAMS pursuant to the Federal Arbitration Act. (emphasis added).*

Thus, as Yucaipa asserts, the threshold issue of arbitrability must be decided by the California arbitrator before this Court can resolve the issue of whether the valuation should be confirmed and Yucaipa compelled to close on the buyout.

Ordinarily, “a gateway dispute about whether the parties are bound by a given arbitration clause raises a ‘question of arbitrability’ for a court to decide.” *Howsam v. Dean Witter*

*Reynolds, Inc.*, 537 U.S. 79, 84 (2002). However, “a court must defer to an arbitrator’s arbitrability decision when the parties submitted that matter to arbitration.” *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995). This exception to the rule applies only when the parties’ arbitration agreement “clearly and unmistakably” provides that the question of arbitrability is to be determined by the arbitrator. *Howsam*, 537 U.S. at 83. Thus, “[the Federal Arbitration Act] allows parties to agree by contract that an arbitrator, rather than a court, will resolve threshold arbitrability questions as well as underlying merits disputes.” *Henry Schein, Inc. v. Archer and White Sales, Inc.*, 139 S. Ct. 524, 527 (2019).

Here, it is clear that Section 13.4 of the Agreement provides that “any and all disputes, claims and controversies arising out of or relating to ... whether a particular dispute, claim or controversy is subject to arbitration” must be determined by a JAMS arbitrator. Thus, the California Arbitration must determine whether Yucaipa’s claims are arbitrable.

Passing over the fact that the California Arbitration must decide the threshold arbitrability issues before the Court, Yucaipa would have an exceedingly heavy burden to succeed on any claim with respect to the propriety of the buyout arbitrator’s decision given the extraordinary amount of time and effort expended by the buyout arbitrator in addressing the issues before him.

Nevertheless, given the particularly broad language of the arbitration provision in the Agreement, it would be inappropriate for this Court to “confirm” the buyout arbitrator’s valuation in the face of Yucaipa’s challenge to the validity of the buyout process and the parties’ contractual obligation to submit threshold arbitrability issues to a JAMS arbitrator.

The Court notes that Yucaipa declined the Court’s offer to hold an evidentiary hearing on Yucaipa’s challenge to the buyout proceeding. In any event, because the parties—perhaps inadvertently—agreed in Section 13.4 to arbitrate *all* arbitrability issues arising under the

Agreement with a JAMS arbitrator, it is not for this Court to determine the threshold arbitrability issues raised by Yucaipa in the California Arbitration.

Accordingly, it is hereby

ORDERED that Sydel's motion is denied without prejudice to renewal following the California Arbitration's determination of arbitrability; and it is further

ORDERED that Yucaipa's motion to stay this action is granted pending the California Arbitration's determination of arbitrability.

3/26/2019

DATE

CHECK ONE:

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CASE DISPOSED

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GRANTED

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DENIED

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SETTLE ORDER

APPLICATION:

CHECK IF APPROPRIATE:

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INCLUDES TRANSFER/REASSIGN

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NON-FINAL DISPOSITION

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GRANTED IN PART

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OTHER

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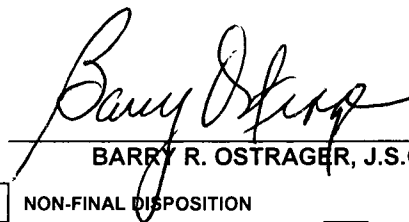
SUBMIT ORDER

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FIDUCIARY APPOINTMENT

☐

REFERENCE



BARRY R. OSTRAGER, J.S.C.