COURT OF CHANCERY
OF THE
STATE OF DELAWARE

DONALD F. PARSONS, JR.
VICE CHANCELLOR

New Castle County Courthouse
500 N. King Street, Suite 11400
Wilmington, Delaware 19801-3734

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Re: *KL Golf, LLC v. Frog Hollow, LLC*
Civil Action No. 001-N

Dear Counsel:

Pending before the Court is KL Golf, LLC's ("KL Golf") complaint and motion to confirm an arbitration award and Frog Hollow LLC's ("Frog Hollow") counterclaim to vacate parts of that award. For the reasons stated below, the Court will confirm the award.

I. BACKGROUND

KL Golf and Frog Hollow are parties to a Golf Course Development and Operation Agreement (the "Development Agreement") and a Ground Lease Agreement

(the "Lease") at a golf course (the "Premises") in Middletown, Delaware. Under the Development Agreement, KL Golf was generally responsible for constructing, operating and maintaining the golf course. Frog Hollow was to construct a multi-use building to house golf related activities and act as a sales center and community building. The building was to include a clubhouse with a grill room/lunch counter with a liquor license.

Disputes developed concerning the parties' respective obligations. Section 41 of the Lease contains an arbitration clause (the "Arbitration Clause") that provides in relevant part:

> All claims, demands, disputes, controversies, and differences that may arise between the parties, concerning any issue related to or generated by this Lease . . . shall be resolved by the resolution process set out in this provision . . . .
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> * * * *
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> (e) It is expressly understood and agreed by the parties that the provisions of this provision . . . shall be construed by a court of competent jurisdiction as preventing any party from maintaining an action at law or in equity in any court of competent jurisdiction to obtain any remedy to which such party may be entitled in the event of any breach or violation of this Lease.[1]

On April 6, 2001, the parties began what evolved into an extended arbitration process, including separate, but related, awards pertaining to Frog Hollow's obligations regarding a grill in the clubhouse and KL Golf's failure to pay Frog Hollow $25,000 towards the construction of the clubhouse.

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[1] The Development Agreement contains a similar provision (Section 7).

The arbitrator issued two documents on April 19, 2002: (1) a 30-page Arbitrator's Award, comparable to an opinion; and (2) a 7-page Final Award, analogous to a judgment. The Final Award required, among other things, that:

> On or before June 1, 2002, Frog Hollow shall, at its sole expense, construct and open a grill operation of substantially the same kind and quality as grill operations at comparable golf courses. On or before June 1, 2002, Frog Hollow shall also secure a liquor license for the grill operation. For <u>each</u> day after June 1, 2002, that Frog Hollow does not operate a grill with a liquor license, it shall pay to KL Golf $500.[2]

The arbitrator also ordered KL Golf to pay within 45 days $25,000 that it owed to Frog Hollow for construction of the clubhouse.[3] "To encourage timely payments and completion of the remaining work, and to discourage the previous dilatory conduct, [the arbitrator] attached financial consequences if either party did not comply with certain of their obligations under the Final Award."[4]

The Final Award, however, did not end the disputes between the parties. KL Golf claimed that Frog Hollow failed to meet its obligations under the Lease and the duties imposed by the Final Award. The parties agreed that a grill was constructed and opened by June 1, 2002, but disputed whether it was of "substantially the same kind and quality

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[2] Appendix to Frog Hollow's Opening Brief ("FHOP App.") Ex. A at 5-6 (emphasis in original). The answering brief of KL Golf and reply brief of Frog Hollow are cited herein as KLAB and FHRB, respectively.

[3] The parties stipulated to confirmation of the Final Award with one exception, which was later withdrawn. KLAB Ex. B.

[4] Supplemental Award (FHOB App. Ex. B) at 2.

as grille operations at comparable golf courses."[5] In addition, KL Golf put the $25,000 into escrow, rather than paying it to Frog Hollow as ordered by the arbitrator. The parties copied the arbitrator with their complaints about noncompliance with the Final Award. On June 24, 2002, the arbitrator wrote to the parties and offered to assist in determining compliance with the Final Award, provided both parties approved. KL Golf responded four days later and asked the arbitrator to intervene; Frog Hollow did not respond.[6] In June 2003, however, both parties did contact the arbitrator and began further proceedings before him. Both parties requested the imposition of financial consequences for noncompliance and other relief.

On August 26, 2003, the arbitrator conducted an evidentiary hearing. On October 8, 2003, he issued a Supplemental Award reconfirming KL Golf's obligation to pay the $25,000 due under the Lease. He also awarded KL Golf $182,000 as a result of Frog Hollow's failure to comply with the substance of the Final Award and awarded KL Golf possession of the clubhouse grill.[7]

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5 *Id.* at 5.

6 *Id.* at 3. The arbitrator noted that, "[h]ad Frog Hollow responded in June 2002, it may have avoided the substantial financial liabilities it has incurred under th[e] Supplemental Award." *Id.*

7 Of the amount awarded to KL Golf, $172,000 was for Frog Hollow's failure to provide a grill "of substantially the same kind and quality as grill operations at comparable golf courses" by June 1, 2002. Supplemental Award at 9-10.

On October 15, 2003, Frog Hollow requested the arbitrator to reconsider the same parts of the Supplemental Award that are in issue before this Court. In a written decision dated October 29, 2003, the arbitrator denied those aspects of the motion for reconsideration.[8]

KL Golf filed this action to confirm the Supplemental Award. Frog Hollow counterclaimed to have parts of that Award vacated. After KL Golf moved for confirmation of the Supplemental Award, the parties briefed and argued their respective positions. This is the Court's opinion on the issues presented.

II. ANALYSIS

Section 5713 of Title 10, Delaware Code, provides:

> The Court [of Chancery] shall confirm an award upon complaint or application of a party in an existing case made within one year after its delivery to the party unless within the time limits hereinafter imposed grounds are urged for vacating or modifying or correcting the award, in which case the Court shall proceed as provided in §§ 5714 and 5715.

Frog Hollow applied to have parts of the Supplemental Award vacated pursuant to § 5714. The Court must vacate an arbitration award under § 5714 if there was "evident partiality" that prejudices the rights of a party or the arbitrator "exceeded [his] powers, or

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[8] FHOB App. Ex. E.

so imperfectly executed them that a final and definite award upon the subject matter submitted was not made."[9]

A. Was the arbitration tainted by evident partiality?

Upon a thorough review of the Final and Supplemental Awards, the decision on reconsideration, and the parties' submissions, the Court finds that there was no evident partiality on the part of the arbitrator. Frog Hollow's attempt to characterize the arbitrator's frustration with its failure to comply with the substance of the Final Award, and his response to that noncompliance, as reflecting evident partiality is not persuasive.

The arbitrator accepted the parties' invitation to visit the clubhouse and grill and compared the grill to other golf clubs in the area. He found that:

> Frog Hollow's grille is not even close [to comparable to the grills at two admittedly comparable clubs, Back Creek and Patriot's Glen]. The construction is of lesser quality materials. There is no bar area. The food service is more akin to a pool snack bar than a grille inviting to golfers following a round of golf. The food and drink selection is more of a snack variety as opposed to a wider selection at Patriot's Glen. There is no cooking at all, only a food preparation area. There is no readily apparent well-stocked bar with spirits. The décor is minimalist at best.[10]

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[9] 10 *Del. C.* § 5714(a)(2), (3). Frog Hollow also seeks to have the Court modify the Supplemental Award pursuant to § 5715(a) to reflect the vacation of parts of it. Because the Court has decided to deny Frog Hollow's counterclaim to vacate parts of the Award, there is no need to address its request for modification.

[10] Supplemental Award at 9.

The Supplemental Award compensated KL Golf for Frog Hollow's failure to comply with the Final Award using exactly the financial consequences the arbitrator specified in the Final Award.[11] In addition, the arbitrator gave KL Golf the ability to make the necessary changes on its own to avoid the likelihood of continuing problems in the future. These actions were reasonable in the circumstances. The Court therefore finds that the Supplemental Award was not tainted with evident partiality and declines to vacate the challenged parts of the Supplemental Award on that basis.

B. Did the arbitrator exceed his authority?

The party moving to vacate an arbitration award on the ground that the arbitrator exceeded his authority must show by "strong and convincing evidence" that the arbitrator "clearly exceeded" his authority.[12] The sources of the arbitrator's authority include: "1) the underlying agreement between the parties in which they agree to submit their disputes to arbitration and 2) the document containing the submission to the Arbitrator of the issues to be decided."[13] In this case, due to the extensive procedural history of the arbitration, there is a third source of authority – namely, the arbitrator's Final Award, which was confirmed by stipulation of the parties. The Supplemental Award at issue

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[11] Frog Hollow's argument that the financial consequences specified in the Final Award should be limited solely to any failure to provide "a grill room/lunch counter with a liquor license" is discussed *infra*, pp. 8-10.

[12] *Baltimore Barn Builders v. Jacobs*, 1990 Del. Ch. LEXIS 214, at *4 (Dec. 17, 1990); *Malekzadeh v. Wyshock*, 611 A.2d 18, 21 (Del. Ch. 1992).

[13] *Malekzadeh*, 611 A.2d at 21.

involves questions of compliance with the Final Award and the remedies imposed for noncompliance. If the arbitrator had decided an issue outside the scope of the parties' submission, or if his actions were in direct contradiction to the express terms of the Development Agreement or Lease Agreement, when viewed in the context of the Final Award, he would have exceeded his authority.[14]

In the proceedings that led to the Supplemental Award, the parties stipulated that the issues submitted to the arbitrator included: "[w]hether Frog Hollow opened the Grille Room/Lunch Counter ("Grille") on or before June 1, 2002, and whether the Grille is of substantially the same kind and quality as grille operations at comparable golf courses."[15] Frog Hollow claims that the arbitrator considered or ruled on issues outside the scope of the parties' submittal letters. Specifically, Frog Hollow argues that the arbitrator exceeded his authority and the scope of the Final Award by (1) ordering Frog Hollow to pay KL Golf damages of $500 per golf day for their noncompliance with the requirement in the Final Award to provide a grill of a certain "kind and quality," and (2) awarding KL Golf the use of the grill rent free.

1. $500 per golf day damages

In the Final Award, the arbitrator ruled as quoted above (p. 3) regarding the grill. Frog Hollow's primary argument is that all the Final Order required it to do to avoid

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14 *See id.*, citing cases.

15 Supplemental Award at 5.

incurring a $500 a day obligation to KL Golf was to "operate a grill with a liquor license" by June 1, 2002. In making that argument, Frog Hollow focuses on the last sentence of paragraph 10 of the Final Award, and all but ignores the earlier sentence that required Frog Hollow "to construct and open [on or before June 1, 2002] a grill operation of substantially the same kind and quality as grill operations at comparable golf courses." According to Frog Hollow, the Final Award did not tie the comparability or quality requirement to the $500 per day charge for noncompliance. Indeed, because there is no dispute that Frog Hollow met the lesser standard of simply providing a grill with a liquor license (without regard to comparability) by June 1, 2002, it contends that the entire grill-related financial award of $172,000 should be vacated.

The Court finds Frog Hollow's argument unpersuasive for several reasons. First, when considered in the context of paragraph 10 of the Final Award as a whole, the Court finds it more reasonable to read the reference to a grill in the last sentence to incorporate the comparability requirement. Second, the most relevant inquiry is what the arbitrator meant when he issued the Final Award. In this case, there is no need for speculation on that score. Frog Hollow squarely raised that issue when it sought reconsideration of portions of the Supplemental Award. The arbitrator denied reconsideration and expressly held that if Frog Hollow failed to comply with the comparability requirement, "it was responsible for payment of $500 for each day it was not in compliance."[16] Finally,

[16] FHOB App. Ex. E at 2, 7-8.

having stipulated in December 2002 to the confirmation of the April 2002 Final Award, Frog Hollow has waived any argument that the arbitrator exceeded his authority by enforcing paragraph 10 of the Final Award exactly as he intended it.[17]

Because the quality component was part of Frog Hollow's obligations under the Final Award, the arbitrator had every right to consider it in determining whether Frog Hollow complied with the Final Award. Frog Hollow, in fact, "devoted a great deal of the [Supplemental Award] hearing" to its arguments that the grill met that standard.[18] After visiting the grill and the facilities at comparable courses, the arbitrator found that Frog Hollow indeed had a grill with a liquor license, but that it was "not even close" to the "same kind and quality as grille operations at comparable golf courses."[19] The

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[17] In denying Frog Hollow's request for reconsideration of the Supplemental Award, the arbitrator stated:

> The definition of "grill" used in the last sentence of paragraph 10 refers to the grill described in the preceding sentence. Frog Hollow has also been on notice since June, 2002, that KL Golf took the position that the monetary award was accruing as a result of Frog Hollow's failure to comply with the Final Award. Again, to the extent there was any question, Frog Hollow could have resolved the issue in June, 2002.

FHOB App. Ex. E at 8.

[18] Supplemental Award at 5.

[19] *Id.* at 9.

arbitrator recognized that the quality standard was subjective, but noted that he had taken his own subjectivity into account in framing the Supplemental Award.

> Although the standard for compliance requires a subjective evaluation of aesthetics, for which there can be differences of opinion, I have given more than a reasonable allowance for this margin of error . . . . One would have thought that, given the significant financial consequences of non-compliance, Frog Hollow would have agreed to resolve the compliance issue promptly in June or July 2002. One would also have thought that Frog Hollow would have given the Final Award a wide berth and constructed a grille that did not flirt with a determination that it failed to comply with the Final Award. It did neither.[20]

In reviewing the arbitrator's Supplemental Award, this Court may not pass on the merits of the issues submitted to the arbitrator.[21] Rather, the Court need only conclude, as it does in this case, that the arbitrator did not exceed his powers or so imperfectly execute them that a final award upon the issue of compliance was not made.

The arbitrator noted KL Golf's dependence on Frog Hollow's compliance with its obligations under the contract and imposed financial consequences of $500 per *golf* day (not calendar days as KL Golf had sought) for 344 days from June 1, 2002 until the date of the Supplemental Award for their failure to comply with the Final Award. Frog Hollow argues that the $500 per day charge constitutes an impermissible penalty. The time for challenging that provision of the Final Award, however, has passed. In fact, the

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[20] *Id.* at 8-9.

[21] *Malekzadeh*, 611 A.2d at 20-21.

parties stipulated to its confirmation. The Court declines Frog Hollow's invitation to revisit the Final Award and rejects its contention that the "financial consequences" are an improper form of liquidated damages. The Court therefore finds that Frog Hollow has not shown that the arbitrator clearly exceeded his authority by awarding KL Golf $172,000 for Frog Hollow's failure to comply with the Final Award.

2. Grill space

Frog Hollow contends that by providing for financial consequences in the Supplemental Award, the arbitrator limited the possible remedies that he could grant to KL Golf as a result of Frog Hollow's continued failure to respect its contractual obligations. Frog Hollow also argues that neither party argued to the arbitrator in the supplemental proceedings that the Final Award even permitted an award of space to KL Golf. As this Court has previously held, however, "the award of relief not previously conceived of by the parties is not grounds for vacating an Arbitrator's award."[22]

The arbitrator found that Frog Hollow had continuously flaunted its obligations and violated the Final Award by failing to construct an adequate clubhouse and grill. The financial consequences were retrospective. In view of the continuing qualitative deficiency of the grill, however, the arbitrator decided to impose a prospective remedy as well. He noted three possible alternative remedies: "(1) order Frog Hollow to renovate the grill room to be substantially the same as Patriots Glen; (2) allow KL Golf to contract

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[22] *Malekzadeh*, 611 A.2d at 22 (citing *United Steelworkers of America v. Enterprise Wheel & Car Corp.*, 363 U.S. 593, 597 (1960)).

for and complete the renovations, and charge Frog Hollow for the expense; or (3) continue the financial consequences until Frog Hollow renovates the grill so that it complies with the Final Award."[23] The arbitrator found none of these alternatives appealing because they failed to provide any finality to the parties' inability to cooperate and pervasive mistrust.

Instead, the arbitrator decided to relieve KL Golf of its dependence on Frog Hollow's cooperation for the construction and operation of an adequate grill. He found that "it is an appropriate remedy for breach of the Final Award that Frog Hollow turn over the grille operation to KL Golf" rent-free for a term co-extensive with the lease agreement already in place between the parties.[24] By so doing, the arbitrator also transferred to KL Golf the costs of completing the construction and operating the grill, including the utility expenses.

Frog Hollow argues that the arbitrator exceeded his authority when he awarded KL Golf the space rent free. Yet, Frog Hollow admits that it probably never would have received any rent from KL Golf under the Lease. KL Golf's rent obligation begins when 30,000 rounds of golf are played in a year. Since the course opened, according to Frog Hollow, the rounds played have not "even come close" to that threshold.[25] Frog

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23 Supplemental Award at 10.

24 *Id.* at 11.

25 FHOB at 12.

Hollow's claim that by being precluded from operating the grill it has lost its only source of income also rings hollow. Frog Hollow continues to own and operate the remainder of the clubhouse, including a banquet facility and the adjacent swimming pool, and most substantially, is selling the residential lots in the surrounding community. The arbitrator (and KL Golf) saw the inadequacy of the grill as contributing to the lack of golfers and sought to remedy that situation. The costs of upgrading the grill to one of an appropriate quality and operating it have now been shifted to KL Golf. These new expenses (and Frog Hollow's lack thereof) offset any potential lost rent and operating income of Frog Hollow. Thus, the Court does not agree with Frog Hollow's contention that by awarding possession of the grill for the duration of the lease period to KL Golf, the arbitrator gave KL Golf a windfall.

Furthermore, the Court finds that the arbitrator derived the essence of this aspect of his award from the contractual relationship between the parties.[26] Thus, Frog Hollow has not shown that the arbitrator exceeded his authority in awarding KL Golf possession of the grill premises as a prospective remedy for Frog Hollow's continued failure to comply with the Final Award.

III. COSTS

KL Golf also requested an award of the costs of this application. The Court has discretion under 10 *Del. C.* § 5716 to award the costs of an application to confirm an

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[26] *Malekzadeh*, 611 A.2d at 22 (noting that it is the arbitrator's obligation to draw the "essence of the award" from the underlying contractual relationship).

arbitration award. Frog Hollow failed to comply with the Final Award, necessitating the Supplemental Award, unsuccessfully sought reconsideration of the Supplemental Award, and failed in its efforts to vacate parts of that Award. Frog Hollow also filed an action to evict KL Golf from the premises while this proceeding was pending, forcing KL Golf to seek and obtain a preliminary injunction against that proceeding. Based on this history, the Court finds that an award of costs is appropriate, but notes that the award does not include attorneys fees.

IV. CONCLUSION

For the reasons stated above, Frog Hollow's counterclaim to vacate portions of the Supplemental Award is DENIED. KL Golf's motion to confirm the Supplemental Award is GRANTED. Frog Hollow shall pay the costs of this proceeding. After conferring with Frog Hollow's counsel, KL Golf shall submit a conforming order.

IT IS SO ORDERED.

Sincerely,

/s/Donald F. Parsons, Jr.

Vice Chancellor

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