Matter of MGI Repetti LLP v Klueg
2014 NY Slip Op 31054(U)
April 22, 2014
Supreme Court, New York County
Docket Number: 650740/14
Judge: Melvin L. Schweitzer

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK : PART 45

Application of MGI REPETTI LLP f/k/a GRAF REPETTI & CO., LLP, Petitioner, For an Order Pursuant to Article 75 of the CPLR Staying Arbitration of A Certain Controversy,	
Petitioner,	Index No. 650740/14
-against-	DECISION AND ORDER
GEORGE L. KLUEG, and GEORGE L. KLUEG, C.P.A., P.C.,	Motion Sequence No. 001
Respondents.	

MELVIN L. SCHWEITZER, J.:

This is a motion by petitioner, MGI Repetti, LLP, an accounting firm (petitioner or MGI/GRC), to stay an arbitration proceeding before the American Arbitration Association (AAA) which petitioner *itself* commenced on December 3, 2013. Petitioner asks that the stay remain in place until the court issues a declaratory judgment as to whether the parties are required to arbitrate their dispute before the AAA or whether the court is the proper forum to resolve the dispute.

According to petitioner, its petition arises out of numerous breaches by respondent George L. Klueg (respondent or Klueg) of the parties' Revised Partnership Agreement (RPA) dated March 9, 2010. Respondent is a signatory to the RPA in his individual capacity and was formerly an equity partner of petitioner. Petitioner contends that Klueg continues to be bound by the terms of the RPA which survived his decision to withdraw as a partner from MGI/GRC and to establish his own CPA firm, George L. Klueg, C.P.A., P.C. (Klueg, P.C.). Petitioner believes that collections of accounts receivable and work in progress owned by MGI/GRC have been

improperly collected and deposited by Klueg into one or more accounts under the name and control of Klueg, P.C. and that clients of MGI/GRC who were improperly solicited and serviced by the Klueg, P.C. firm subsequent to Klueg's withdrawal from MGI/GRC are currently being serviced and billed by Klueg and Klueg, P.C. without MGI/GRC receiving compensation as required under the RPA.[1]

On December 3, 2013, MGI/GRC started the arbitration proceeding pursuant to Article 11 of the RPA. Respondents' answer to the demand specifically asserts that the AAA and the arbitrator do not have jurisdiction over the dispute. Respondent argues that MGI/GRC is not a signatory to the RPA and cannot enforce it because the RPA was only signed by each of MGI/GRC's equity partners *individually* but not by MGI/GRC as a firm. Respondents further allege that because Klueg PC is not a signatory to the RPA it need not arbitrate disputes with MGI/GRC and that the AAA lacks jurisdiction to adjudicate the dispute with Klueg, PC.[2]

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[1] Section 8.16 of the RPA provides that each partner, including Klueg, agrees that all clients are clients of the partnership as a whole and that in dealing with any client the partner, including Klueg, does so solely on behalf of the partnership. RPA 8.16 precludes a partner from communicating with firm clients in order to solicit business from them in anticipation of terminating the partner's relationship with the partnership. In addition, any partner who leaves the partnership must assist the partnership in collecting fees due to the partnership for services rendered by the partnership before the disassociation of the partner.

RPA 8.17 (a) prohibits former partners from soliciting firm clients or performing accounting services for them for a period of two years after the partner has withdrawn. RPA 8.17 (b) states that a former partner like Klueg who violates 8.17 (a) and solicits firm clients during the two year period is required to pay the firm an amount equal to 120% of the firm's average annual billings for each such client during the prior three year period. In addition, the violating partner agrees that the first dollars of any amount otherwise due to that partner under the RPA are offset 100% by any amount due to the firm as a result of violations of RPA 8.17 (a).

Under RPA 8.13 (a), the firm is entitled to offset amounts which are owed to the withdrawing partner by amounts owed by that partner to the firm.

[2] Petitioner counters that the financial affairs of Klueg concerning his current practice of accounting are inextricably intertwined with the financial affairs of Klueg, P.C. and that most, if not all, of the assets which Klueg has taken from MGI/GRC without compensating the firm are currently under the possession, custody and control of Klueg, P.C.

MGI/GRC argues that it is entitled to enforce the RPA provisions against signatories of the RPA on behalf of the other equity partners who executed the RPA including Klueg.

MGI/GRC argues that, in light of respondents' position in the arbitration, it will suffer prejudice were it to go forward in the arbitration and obtain an award against the respondents only to have the respondents later seek a judicial declaration that the award is unenforceable because they, i.e. Klueg, PC, are not bound by the RPA, or that MGI/GRC, i.e. the partnership entity as opposed to the individual partners who signed the RPA, cannot enforce the RPA.

Respondents counter that at this juncture the court has no discretion to extend the 20-day time period under CPLR 7503 (c) within which MGI/GRC could have applied for a stay of the arbitration. An untimely stay application is barred by the existence of an agreement to arbitrate. Respondents argue that petitioner is attempting to circumvent the 20-day time period by couching its untimely stay application as challenging the very existence of an agreement to arbitrate. Yet, according to respondents, petitioner's argument actually challenges the *scope* of the arbitration provision rather than its existence, and thus is time barred under CPLR 7503 (c).

Respondents point to the Court of Appeals decision in *Matter of Lane v Abel-Bey*, 50 NY2d 864 (1980) in which the Court held that "[w]hether the corporation was bound by the arbitration agreement of all its shareholders was a threshold question. Inasmuch as this question was not raised by the corporation in a timely application for a stay, that issue may not now be raised by the corporation or by anyone on its behalf." 50 NY2d at 866. Respondents argue that the question raised by MGI/GRC's not having signed the RPA, as included in petitioner's stay application is barred for failure to comply with the 20-day time period under CPLR 7503 (c) because the RPA was signed by the MGI/GRC *partners*. Thus, whether the arbitration provision

extends to MGI/GRC, the partnership entity, is an issue that had to have been raised within the 20-day time period. According to respondents, MGI/GRC admittedly failed to comply with CPLR 7503 (c) and, as such, it is precluded from having the issue addressed by the court. *See Matter of Woodcrest Fabrics, Inc. v Taritex, Inc.*, 98 AD2d 52 (1st Dept 1983); *Aetna Life & Cas. Co. v Stekardis*, 34 NY2d 182 (1974).

Respondents also point out that not only did MGI/GRC commence the arbitration and fail to timely move for a stay, but it also continued to participate in the arbitration without any reservation of rights. *See Matter of Infinity Ins. Co. v Daily Med. Equip. Distrib. Ctr., Inc.*, 39 Misc 3d 582 (2013), holding that a party to an arbitration proceeding, even one who never executed an arbitration agreement, who participates in the arbitration waives its right to a judicial determination on the issue of arbitrability. Once a party has taken part in the arbitration proceeding "they no longer are entitled to stay further progress of the arbitration proceeding, even if they are not subject to any arbitration agreement." *Ibid.* at 587.

Respondents point out that petitioner's active participation in the arbitration after the 20-day time period included, for example, submitting to the AAA a checklist for conflicts and a ranking of potential arbitrators; participating in the selection of the initial arbitrator; submitting correspondence and communications opposing respondents objection to the appointment of the initial arbitrator; requesting a new panel of arbitrators following the recusal of the initial arbitrator; participating in the selection of a new arbitrator; and filing a reply to counterclaims. This, of course, is in addition to MGI/GRC's commencement of the arbitration by filing a Demand for Arbitration and a Statement of Claim in the first instance.

Finally, petitioner characterizes respondents' Answering Statement with Affirmative Defenses and Counterclaims in the arbitration, as alleging that "the RPA and its arbitration provision are a product of pervasive, far reaching fraud" (*see* ¶¶ 16, 126-136) and, as a result, it is this court which must rule on whether there is a valid arbitration agreement between the parties and whether they are required to arbitrate their dispute. But respondents counter that they make "no claim that the Arbitration Provision is invalid or does not exist." The fraud alleged, say respondents, is not the type of claim that would invalidate the arbitration provision. *See O'Neill v Krels Comm. Corp.*, 16 AD3d 144 (2d Dept 2005). As such, say respondents, the arbitration provision is broad enough to encompass a claim that the RPA was procured by fraud. *See Prima Paint Corp. v Flood & Conklin Mfg. Co.*, 388 US 395, 18 L. Ed. 2d 1270, 87 Sup Ct 1801 (1967) (a claim of fraud in the inducement of a contract may be determined in arbitration).

Several important points must be made in addressing petitioner's argument which seeks the intervention of this court. First, it is not the petitioner who seeks to invalidate the RPA and its arbitration clause on grounds of fraud. Indeed, in commencing its arbitration, petitioner seeks to rely on its agreement to vindicate its rights *viz* respondents. Second, what petitioner characterizes as respondents allegations of "pervasive fraud" for the court to evaluate is so general and non-specific as to never be able to pass muster under CPLR 3016 (b)'s specificity requirements. In contrast, petitioner on Sur-Reply cites a bevy of cases where fraud allegations were made with clear specificity, e.g. forgery, unconscionable arbitration fees, denial of having signed the contract, usurious loan agreement, no agreement to arbitrate. Arbitrators are more than capable of dealing with the amorphous allegations they are presented with here. *See Stellmack Air Conditioning and Refrigeration Corporation v Contractors Management Systems*

of NH, Inc., 293 AD2d 956 (3d Dept 2002). Third, when petitioner encountered those assertions of fraud, even though they were made more than 20 days after petitioner had filed its Demand for Arbitration, *that* was the time to raise this jurisdictional point. But petitioner did not do that. Rather, it filed its Reply to respondents' counterclaims which was confined to a series of denials of fraud without once challenging the jurisdiction of the arbitrators to hear and decide the issue (*see* Petitioner's Reply, ¶¶ 16, 82-92).

It is the opinion of the court that, notwithstanding the conundrum with which petitioner ostensibly finds itself, it is one of petitioner's own making. Petitioner admits that it commenced the arbitration in the name of MGI Repetti, LLP which is an unconditional waiver of any right to seek a stay. Petitioner admits that its stay application is untimely. Petitioner's participation in the arbitration also bars the stay application. And, finally, petitioner's fraud argument is to no avail since it failed to make a jurisdictional objection as soon as the issue of fraud was raised, but rather continued to participate in the arbitration proceeding on its merits. *N.J.R. Associates v Nicole Tausend*, 19 NY3d 597 (2012); *Matter of Infinity Insurance Company v Daily Medical Equipment Distribution Center, Inc.*, 39 Misc 3d 582 (Sup Ct, Kings Cnty, 2013).

Accordingly, it is

ORDERED that petitioner's motion is denied and the Petition is dismissed.

Dated: April 22, 2014

ENTER:

J.S.C.

MELVIN L. SCHWEITZER