Supreme Court of New Jersey

Docket No. 088645

LAURENCE J. RAPPAPORT, Individually and as a Member of Rapad Real Estate Management, LLC, KABR Management, LLC, KABR Management II, LLC, KABR Management III, LLC and KABR Management IV, LLC, *Plaintiff-Respondent,* – vs. – KENNETH PASTERNAK, Individually and as a Member of Rapad Real Estate Management, LLC, KABR Management, LLC, KABR Management II, LLC, *(For Continuation of Caption See Inside Cover)*	CIVIL ACTION ON PETITION FOR CERTIFICATION FROM THE FINAL JUDGMENT OF THE SUPERIOR COURT OF NEW JERSEY, APPELLATE DIVISION DOCKET NOS. A-000491-21 and A-000492-21 Sat Below: HON. RICHARD J. GEIGER, J.A.D. HON. RONALD SUSSWEIN, J.A.D. HON. MARITZA B. BYRNE, J.A.D.

SUPPLEMENTAL BRIEF IN SUPPORT OF DEFENDANTS-PETITIONERS

HOWARD W. SCHUB
KASOWITZ BENSON TORRES LLP
One Gateway Center, Suite 2600
Newark, New Jersey 07102
(973) 645-9462
hschub@kasowitz.com

STUART REISER
SHAPIRO, CROLAND, REISER, APFEL & DIIORIO, LLP
Continental Plaza II
411 Hackensack Avenue
Hackensack, NJ 07601
(201) 488-3900
sreiser@shapiro-croland.com

Attorneys for Defendants-Petitioners

On the Brief:
HOWARD W. SCHUB, ESQ.
Attorney ID# 045381990
STUART REISER, ESQ.
Attorney ID# 015051980

Date Submitted: June 24, 2024

CP COUNSEL PRESS (800) 4-APPEAL • (330785)

KABR Management III, LLC and KABR Management IV, LLC; ADAM ALTMAN, Individually and as a Member of Rapad Real Estate Management, LLC, KABR Management, LLC, KABR Management II, LLC, KABR Management III, LLC, and KABR Management IV, LLC; MICHAEL GOLDSTEIN, Individually and as a Member of KABR Management III, LLC, and KABR Management IV, LLC; JUDE MASON, Individually and as a Member of KABR Management III, LLC, and KABR Management IV, LLC; RAFFI AYNILIAN, Individually and as a Member of KABR Management IV, LLC; THE SARA PASTERNAK 2008 IRREVOCABLE TRUST, as a Member of KABR Management, LLC, KABR Management II, LLC and KABR Management III, LLC; THE RACHAEL PASTERNAK 2008 IRREVOCABLE TRUST, as a Member of KABR Management, LLC, KABR Management II, LLC and KABR Management III, LLC; THE DANIEL PASTERNAK 2008 IRREVOCABLE TRUST, as a Member of KABR Management, LLC, KABR Management II, LLC, KABR Management III, LLC and KABR Management IV, LLC; THE KABR GROUP, LLC; JOHN DOES 1 through 20 and XYZ CORPORATIONS 1 through 20,

Defendants-Petitioners.

LAURENCE J. RAPPAPORT, Individually and as a Member of KABR Management, LLC and KABR Management II, LLC,

Plaintiff-Respondent,

– vs. –

KENNETH PASTERNAK, Individually and as a Member and Manager of KABR Management, LLC and KABR Management II, LLC; ADAM ALTMAN, Individually and as a Member and Manager of KABR Management, LLC and KABR Management II, LLC; THE SARA PASTERNAK 2008 IRREVOCABLE TRUST, as a Member and Manager of KABR Management, LLC and KABR Management II, LLC; THE RACHAEL PASTERNAK 2008 IRREVOCABLE TRUST, as a Member and Manager of KABR Management, LLC and KABR Management II, LLC; and THE DANIEL PASTERNAK 2008 IRREVOCABLE TRUST, as a Member and Manager of KABR Management, LLC and KABR Management II, LLC,

Defendants-Petitioners.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Other Authorities

PRELIMINARY STATEMENT

The sophisticated parties in this case entered into a broadly worded arbitration agreement, delegating to the arbitrator the authority to resolve issues related to both Plaintiff Rappaport's termination from his employment with Defendant real-estate management companies and the value of Plaintiff's management and membership interest in those companies. The parties conferred on the arbitrator the power to rule on his jurisdiction and the scope "of the arbitration agreement or to the arbitrability of any claim or counterclaim."

The parties chose as their arbitrator Chief Justice James Zazzali (ret.) ("Arbitrator"), who held thirteen days of hearings and additional days of oral argument. He reviewed a record of almost 10,000 pages of pleadings, transcripts, briefs, exhibits, and correspondence. He concluded that Defendants wrongly terminated Plaintiff and awarded Plaintiff $4.9 million for both his membership and management interests ("Arbitration Award"). In rendering the Arbitration Award, the Arbitrator found that Rappaport had failed to prove by a preponderance of the evidence that he was entitled to carried interest.

The record is replete with evidence that Plaintiff's membership and management interests were within the scope of the arbitration agreement. The Arbitrator repeatedly found that the parties submitted for his determination the value of those interests. The Chancery Division confirmed the Arbitration

Award. The Appellate Division reversed based on a non-deferential, de novo review of the record, finding the valuation issue was not before the Arbitrator.

The Appellate Division erred by not recognizing that the parties were free "to delegate to [the] arbitrator the issue of whether they agreed to arbitrate a particular dispute." See Morgan v. Sanford Brown Inst., 225 N.J. 289, 303 (2016). It also erred by not affording a heightened level of judicial deference to the findings of the Arbitrator in this private-sector arbitration.

The parties opted out of the civil justice system in favor of deciding their dispute through arbitration. They chose an arbitrator and delegated to him the discretion to decide what claims were before him and the authority to resolve those claims. As Chief Justice Wilentz stated in his concurrence in Perini Corp. v. Greate Bay Hotel & Casino, Inc., "[t]he very purpose of committing a dispute to arbitration is to get away from the judiciary" and to avoid the "litigation wringer." 129 N.J. 479, 519, 542 (1992).

In Tretina Printing Inc. v. Fitzpatrick & Associates, Inc., the Court adopted the "views expressed in [Chief Justice Wilentz's] Perini concurrence" and pronounced that a heightened standard of deference would apply to private-sector arbitration awards. 135 N.J. 349, 358-59 (1994). In the wake of Tretina, such awards would be "final, not subject to judicial review absent fraud, corruption, or similar wrongdoing on the part of the arbitrators." Id. at 357

(quoting Perini, 129 N.J. at 519 (Wilentz, C.J., concurring)). Chief Justice Wilentz indicated in his concurrence that, under N.J.S.A. 2A:23B-23 and -24, only errors that went beyond "gross or ordinary" factual errors and only errors of law that were patently "egregious" would result in vacation or modification of a private-sector arbitration award. Perini, 129 N.J. at 542.

The Appellate Division did precisely what Tretina forbids -- it conducted a de novo review of the record, weighed witness testimony, and afforded no deference to the Arbitrator's finding that the value of Plaintiff's membership interest (and a right to any carried interest) was indisputably within the scope of the Arbitration Agreement and submitted to him. The opinion of the Appellate Division is in conflict with the fundamental tenets of Tretina and undermines the integrity of private-sector arbitration awards, and therefore cannot stand.

Additionally, if the Appellate Division believed that the Arbitrator wrongly based Plaintiff's $4.9 million award on the value of his combined management and membership interests, the panel should have vacated the entirety of the award instead of permitting the entire $4.9 million award to stand solely on Plaintiff's management interest. That ruling directly violated the directive in N.J.S.A. 2A:23B-24(a)(2).

This Court should reverse the judgment of the Appellate Division and reinstate the Chancery Division's confirmation of the Arbitration Award.

FACTS AND PROCEDURAL HISTORY

A. KABR and Rappaport's Business Relationship and Its Rupture.

Laurence Rappaport is a former member and officer of the KABR Group, LLC, ("KABR"), a real estate management and development business. (See Pa114 ¶ 13, Pa116 ¶ 24, Pa117 ¶ 33, Pa118 ¶ 38, Pa119 ¶ 45, Pa120 ¶ 51, Pa121 ¶ 59, Pa122 ¶ 65, Pa123 ¶ 73.) KABR includes KABR Management, L.L.C. ("KABR I"), KABR Management II, LLC ("KABR II"), KABR Management III, LLC ("KABR III"), KABR Management IV, LLC ("KABR IV"), and Rapad Real Estate Management, L.L.C. ("Rapad"). (Pa130 ¶ 85.) KABR also manages several funds that invest in real estate. (Pa950 ¶ 3.) From 2008 until his departure, Rappaport served as an officer and member of those entities and was an investor in the funds. (See, e.g., Pa112; Pa117 ¶ 33, Pa119 ¶ 45, Pa121 ¶ 59, Pa123 ¶ 73; Pa951 ¶ 7.) Rappaport and his wife invested approximately $3 million in the funds. (Pa857.)

Rappaport earned compensation from KABR in several different ways. (7a.) As an officer of KABR, Rappaport received distributions from KABR's management and development fees and distributions from the KABR entities' investment fees. (Ibid.) As an attorney, Rappaport billed KABR for the legal work he and his firm did for KABR. (Ibid.)

Rappaport was also eligible to receive carried interest. (See Pa1319.) Carried interest is a performance fee rewarding KABR for profitable management of the KABR entities' investments on behalf of the KABR entities' investors. (See Pa1319 n.60.) After KABR's managers are paid their fees and the entities' investors receive not only the return of their capital but also a preferred return, then KABR and the KABR entities and their members split any excess returns -- carried interest. (Ibid.) In addition, Rappaport had a capital account with each of the KABR entities. Rappaport's capital accounts were, in essence, records of how much each of the entities owed him as a member. (See, e.g., Pa540-42 (Rapad Operating Agreement provisions governing capital accounts).)

In 2018, Rappaport and Kenneth Pasternak, the primary investors in the KABR entities and Rapad, had an acrimonious falling out that led to mutual recriminations. (Pa131 ¶ 91; Pa132 ¶¶ 93, 98; Pa138 ¶¶ 136, 140; Pa139 ¶ 144; Pa390-93.) On January 29, 2019, Rappaport was terminated as an officer and member of KABR and the KABR entities. (Pa134 ¶¶ 112-13, Pa136 ¶ 123; Pa139 ¶ 143.) Rappaport's severance from the entities had no impact on his wife's and his approximate $3 million dollar investment in the funds.

B. The Parties Agree to Arbitrate all Disputes Related to Rappaport's Departure from KABR, and the Arbitrator Denies Rappaport's Claim of Carried Interest.

On March 25, 2019, Rappaport, filed a 23-count complaint against Defendants, alleging that he was wrongly terminated as an officer and member of KABR ("the 2019 Action"). (See Pa111-83.) Defendants moved to compel arbitration pursuant to operating agreements with enforceable arbitration clauses.

Rappaport then agreed to dismiss the complaint, and the parties entered into an Arbitration Agreement with very broad terms. (Pa184-87; Pa197-205.) The Arbitration Agreement clearly stated that the parties were agreeing to arbitrate any disputed issues regarding Rappaport's rights as a manager and member of the KABR entities:

> Whereas, the Parties wish to fully and finally resolve their dispute related to the Claim and Counterclaim, and related matters, including but not limited to, any claims that could be asserted by any Party as part of the Claim or the Counterclaim or with respect to the dissolution or disassociation of Rappaport from, or Rappaport's employment with, Rapad Real Estate Management, LLC; KABR Management, LLC; KABR Management II, LLC; KABR Management III, LLC; KABR Management IV, LLC (collectively, the "KABR Management Companies") by submitting their claims and defenses to arbitration.
>
> [(Pa197) (emphasis added).]

The Arbitration Agreement provided that it would be governed by the Commercial Arbitration Rules of the American Arbitration Association ("AAA Rules");[1] the New Jersey Arbitration Act (NJAA), N.J.S.A. 2A:23B-1 to -36; and New Jersey law. (Pa198.) AAA Rule 7(a) provides that "[t]he arbitrator shall have the power to rule on his or her own jurisdiction, including any objections with respect to the existence, scope, or validity of the arbitration agreement or to the arbitrability of any claim or counterclaim." (Pa1644.)

The parties also agreed that any conflict between those governing rules would be decided by the Arbitrator. (Pa198.) Finally, the Arbitration Agreement provided that the Arbitrator would render a reasoned award and that his ruling would be final and binding, except as provided by the NJAA. (Pa199.)

The parties selected former Chief Justice Zazzali (ret.) to serve as the Arbitrator. (Pa198.)

Throughout the arbitration proceedings, Rappaport made clear that he was seeking compensation for his membership interests, which included his claim to carried interest.

Rappaport asserted twenty-five arbitral claims against Defendants, seeking damages for his termination as both a manager and a member of KABR. (Pa306-84). Rappaport specifically alleged that (1) "Pasternak began a

[1] The AAA Rules can be found at Pa1632-77.

systematic campaign to circumvent Rappaport's interests in [KABR], as both a member, chief executive officer, and a manager of" the KABR entities, (Pa327 ¶ 97 (emphasis added)), and (2) that there was "an actual controversy between Rappaport, on the one hand, and the [Defendants], on the other hand, concerning the improper attempt to terminate or change Rappaport's obligations -- as an owner of [KABR]" under the KABR operating agreements (Pa339 ¶ 171 (emphasis added)).

In addition, in several causes of action, Rappaport alleged that the Defendants' conduct was "deliberately designed to deprive Rappaport of the reasonable expectations of his membership interests in [KABR], thereby frustrating Rappaport's reasonable expectations with respect to his membership interests." (Pa374 ¶ 332 (emphases added); see also Pa376 ¶ 343 (same); see also Pa359-372 ¶¶ 249, 265, 276, 287, 298, 309, 320.) Rappaport's total monetary demand came to $69,000,000. (Pa208.)

Defendants submitted counterclaims against Rappaport for $11,000,000, alleging that he acted in an exploitive, abusive, negligent, and fraudulent manner and that he engaged in incompetent behavior as a manager, officer, and director of KABR. (Pa387-93). Defendants also sought a declaration that Rappaport "has properly been or may be terminated from all of the KABR Entities and is

not entitled to any further compensation" or distributions from KABR. (Pa393 ¶ 13.)

In his pre-hearing brief, Rappaport explained that he sought "a judgment requiring that various compensation due him as a member of [KABR] continue to be paid pursuant to the terms of the operating agreements." (Pa1025.) He also filed a motion seeking a declaration that as "a member" he was "entitled to the profits, losses, and distributions set forth in Articles 3, 4, and 5 of the operating agreements[,]" and was "entitled to such compensation going forward." (Pa1093.)

In January and February 2020, the Arbitrator held a 13-day evidentiary hearing, during which he heard witness testimony, examined hundreds of exhibits, and allowed the attorneys to present opening and closing arguments. (See Pa1881 ¶ 8.) During the hearing, Rappaport twice asserted his membership claim for carried interest.

While engaged in a colloquy with his attorney, Rappaport was asked the value of his "current carried interest." He responded: "aggregated with the monies that my wife and I owned in the investment, I think, it came out -- I'm trying to think. I guess somewhere in the 20 -- in the low 22 to $25 million would have been where it came out with just the carried interest." (Da4.)

Second, Rappaport also testified about carried interest during his direct examination:

> [RAPPAPORT'S COUNSEL]: With respect to this . . . arbitration, are you asserting any claims with respect to your carried interest?
>
> [RAPPAPORT]: I'm asserting the fact that I am entitled to that and I am fully vested in the carried interest.
>
> . . .
>
> [RAPPAPORT'S COUNSEL]: And what do you estimate your carried interest to be?
>
> [RAPPAPORT]: Last time that it was valued, which was I think 2018, the total carried interest was somewhere in the $25 million neighborhood. I'm not a hundred percent sure.
>
> [(Pa1440 (emphasis added).)]

Rappaport decided not to call an expert to testify regarding the value of any carried interest and submitted no documentary support for his alleged valuation of his carried interest claim. Defendants took the position that Rappaport had failed to prove an entitlement to carried interest or the amount with sufficient certainty. (Pa1319-23.)

In his closing remarks, Rappaport's counsel told the Arbitrator,

> [S]ection 6.3 of the operating agreements all clearly state that any member that leaves the company for whatever reason is entitled to . . . the carried interest in perpetuity, as he would receive as a member.
>
> . . .

> Mr. Rappaport is fully vested in the management companies, including KABR Management I through IV and Rapad. We ask that the monies outlined in the independent expert report of EisnerAmper be awarded, there be a full award of all future carried interests, all monies distributed of the operating income until dissolution in perpetuity . . . .
>
> [(Pa1101; Pa1104 (emphases added.)]

After the arbitration hearings concluded, the parties filed post-hearing briefs. In his brief, Rappaport argued that he "is fully vested and entitled to carried interest." (Pa1197; see also Pa1203 n.2 ("The value of Rappaport's carried interest is $25 million dollars.").) He also submitted a proposed form of Award that included a declaration that Rappaport is a member of KABR who "is entitled to the carried interest paid by the KABR Funds . . . ." (Pa1237-39.)

In their brief, Defendants argued that Rappaport was, at most, entitled to his capital accounts. (Pa1243-330.) Defendants also argued that under the Operating Agreements, a dissociated member or a member forced to withdraw was not entitled to carried interest and, in any event, Rappaport failed to prove the value of any carried interest. (Pa1319-21.)

On July 31, 2020, the Arbitrator issued his Interim Final Arbitration Award ("Initial Award"). (Pa207-42.) Discussing the factors set forth in the New Jersey Revised Uniform Limited Liability Act (RULLCA), N.J.S.A. 42:2C-1 to -94, the Arbitrator found Rappaport was wrongfully terminated. The

Arbitrator, however, denied Rappaport's request for a declaration (1) nullifying his termination, (2) reinstating him as chief executive officer, and (3) entitling him to compensation in perpetuity under the various operating agreements. (Ibid.) The Arbitrator observed that it would not be in the legitimate interest of KABR, its owners, investors, and clients to reinstate Rappaport due to a toxic atmosphere prevailing among the parties. (Pa239.)

Although he denied Rappaport's request for reinstatement and compensation in perpetuity, the Arbitrator awarded Rappaport damages in the amount of $4,900,000. (Pa240.) In explaining his decision, the Arbitrator stated that he disagreed with Rappaport's expert on economic damages and "made [his] own independent judgment on damages" regarding Rappaport's wrongful termination claim. (Ibid.) He awarded Rappaport $4,900,000 on that claim and subtracted $1,048,853, which was credited to Defendants for a management-fee counterclaim. (Pa240-41.). The Arbitrator also found that Rappaport was entitled to a return of his capital account, valued at $13,455. (Pa237.) The Rappaports' $3 million investment in the KABR funds was not touched by the Arbitrator's decision.

Rappaport received a net award of $3,851,147. (Pa241-42.) The Arbitrator expressly denied Rappaport's request for carried interest, concluding that he failed to prove the claim and that the $4.9 million damages award was a

"fair and just result." (Pa237, Pa241.) In closing, the Arbitrator "urge[d] the parties to put these events behind them and continue on with their professional and personal lives." (Pa241.)

C. The Arbitrator Reiterates that Rappaport Failed to Prove His Entitlement to Carried Interest.

Dissatisfied with that ruling, Rappaport requested that the Arbitrator reconsider the Initial Award. (Pa1332-44.) Rappaport again argued that he was entitled to future carried interest payments in his capacity as a member. (Pa1336-44.) The Arbitrator issued his second award ("Final Arbitration Award") and affirmed his denial of any carried interest to Rappaport. (Pa244-63.) In so doing, he stated:

> In the original Award, I denied Claimant's request for $25M in carried interest but awarded $13,455, the total value of his capital account in KABR I through IV. Claimant nonetheless pursues his request for carried interest although he is "not looking for a number amount to replace on the carried interest at this point." . . . I will entertain Claimant's application. But that is all I do.
>
> I previously denied the Claimant's request of $25M. That decision stands. I denied the claim in an exercise of discretion after a review of the entire record. I did so for the reasons set forth by [Defendants] in their original brief submitted before the prior Award, in their current brief filed in connection with this Award, and in their correspondence of September 8, 2020. Rather than leave it at that, and although the Arbitrator is not obligated to speak further on the issue, I emphasize that apart from all of the above, I find that Claimant has not established by a preponderance of the credible evidence

> that he has proven carried interest. I specifically find that he has not established by a preponderance of the credible evidence the value of his current interest at the time of his termination.
>
> Although not determinative of the above or any issue, I have awarded Claimant almost $3.9M in this matter. I also award interest. In the aggregate, that sum represents a reasonable result. I believed at the time of issuance of the original Award, and am even more convinced now after consideration of all the circumstances, that it is a just remedy. To make the point abundantly clear, even if I had awarded carried interest, the amount would be de minimis.

[(Pa247-48) (emphases added)].

Defendants paid the full amount awarded to Rappaport. (Pa276.)

D. The Chancery Division Remands the Matter to the Arbitrator.

Rappaport did not accept the results of the arbitration. On December 21, 2020, Rappaport commenced a second action against Defendants in the Superior Court, Chancery Division, Bergen County ("2020 Complaint"). (Pa1679-714.) The 2020 Complaint raised ten separate counts for relief against Defendants, all of which were already fully litigated in the arbitration. (Ibid.) For the most part, Rappaport repeated his claims that Defendants owed him carried interest under the operating agreements for the KABR entities. (Pa1698 ¶ 114.)

Defendants responded by filing a motion in the 2019 Action to confirm the Final Arbitration Award. (Pa188-90.) Rappaport likewise moved to confirm the Final Arbitration Award in the 2019 Action, but only to the extent that it did

not deprive him of his status as a member of KABR, or, alternatively, he moved to vacate or modify the Award to retain his membership interest. (Pa1383-84.)

Defendants moved before the Chancery Division to dismiss the 2020 Complaint and for sanctions for the bad-faith second filing. (Pa1876-78.) The Chancery Division stayed the 2020 Complaint and remanded to the Arbitrator for the limited purpose of "clarify[ing] . . . whether the $4.9 million award in damages was intended to represent full, just, and complete compensation to Plaintiff for his damages against Defendants both as a manager and member of the KABR Entities." (Pa2.)

E. The Arbitrator Holds for a Third Time that Rappaport Failed to Prove His Entitlement to Carried Interest.

On remand, the parties submitted briefs and presented oral argument on the issue of whether the Award fully compensated Rappaport for his damages both as a manager and member of the KABR entities. (See Pa2084; Pa2089-113.) During oral argument before the Arbitrator, Rappaport's counsel stated "that 'carried interest' is 'the only item' he is seeking and that the carried interest is $2.6 million." (See Pa2288.)

The Arbitrator answered the limited remand question, stating that he "intended that the $4.9 million Award represent full, just and complete compensation to [Rappaport] for his damages against [Defendants] both as a manager and member of the KABR Entities." (Pa2286-98 (emphasis added).)

In his decision, the Arbitrator noted that "[a]t least twice I have denied carried interest," and he lamented that "[a]rbitration, long trumpeted as an expeditious path to resolution, sometimes comes up short in meeting that goal." (Pa2287-88.)

When the matter returned to the Chancery Division, the court rejected Rappaport's arguments that the Arbitrator had exceeded his authority or misapplied New Jersey law. (2T60-19 to 61-8.) The court opined that it did not believe that the parties "could have really presented much more of a record," and that "the arbitrator carefully reviewed and considered the record." (2T55-21 to 56-2.)

In reviewing the Arbitrator's decisions, the Chancery Division explained that its role was limited: "I am not here to be an Appellate Court . . . to see if I agree or disagree with [the Arbitrator's] conclusions, but once the parties go to arbitration there is very limited grounds to disturb, or vacate, or modify." (2T58-17 to 58-23.)

The Chancery judge found that carried interest was repeatedly raised throughout the arbitration and that the Arbitrator had, on multiple occasions, ruled on it squarely. "[I]t was argued by [Rappaport] . . . that carried interest was never discussed and never a part of this. I just didn't understand that. I mean, [the Arbitrator] obviously ruled on it, there was a reconsideration. Even

on this remand, carried interest is really the only thing that is being discussed." (2T59-17 to 59-24 (emphasis added).)

Indeed, the court emphasized that Rappaport's membership interest and right to carried interest were central to the arbitration and fully litigated:

> And the case really was about, you know, his role in this company as a member, or owner, or CEO, and whether he is due his interest, his carried interest, which he would get as a member, and whether he is entitled to this carried interest.
>
> And the Chief Justice ruled on it. So, you know, in the end I think that there was full consideration of all the issues.
>
> [(2T62-2 to 62-11.)]

Accordingly, the Chancery Division confirmed the Final Arbitration Award and dismissed the 2020 Complaint with prejudice. (Pa3-8.) Rappaport appealed.

F. The Appellate Division Misconstrues the Record, Makes Its Own Evidential Findings, and Modifies the Award without Deferring to the Arbitrator.

The Appellate Division reversed the Chancery Division's confirmation of the Final Arbitration Award and its dismissal of the 2020 Complaint. (5a.)

The panel did not apply a standard of deference to the Arbitrator's award, conducted a de novo review of the record, and made findings of fact diametrically opposite from those of the Arbitrator. (4a-5a.) The panel specifically found that "Rappaport's interests as a member of the entities was

not raised as a claim by either party in arbitration," (4a), despite the plethora of evidence indicating otherwise.

The panel also mistakenly attributed a colloquy between Rappaport and his counsel as one between Rappaport and the Arbitrator. The panel erroneously stated that "there was no claim submitted for future carried interest" and "the only testimony regarding [carried interest] came in response to a sua sponte question posed to Rappaport by the arbitrator." (27a.) The panel then reproduced the colloquy, misnaming the interlocutor as the Arbitrator when, in fact, the questioner was Rappaport's attorney:

> [THE ARBITRATOR]. With respect to this litigation -- or, rather, this arbitration, are you asserting any claims with respect to your carried interest?
>
> [RAPPAPORT]. I'm asserting the fact that I am entitled to that, and I am fully vested in the carried interest.
>
> [THE ARBITRATOR]. Do you remember [defense counsel] going through some numbers about the damages that you assert in this case? Do you recall him speaking today about that?
>
> [RAPPAPORT]. Yes.
>
> . . . .
>
> [THE ARBITRATOR]. And what do you estimate your carried interest to be?
>
> [RAPPAPORT]. Last time that it was valued, which was I think 2018, the total carried interest was

> somewhere in the $25 million neighborhood. I'm not a hundred percent sure.
>
> [(27-28a.)]

Where "Arbitrator" appears in brackets should have been the name of Rappaport's attorney. When Chief Justice Zazzali interjected during Rappaport's direct examination, the transcript labeled the interlocutor as "THE COURT." (See, e.g., Pa1436.) Otherwise, when Rappaport's attorney was conducting his direct examination, the questions begin with the letter "Q." (Ibid.) A review of the transcript leaves no doubt that Rappaport's attorney, not the Arbitrator, was the questioner in the above exchange. (See Pa1440.)

The panel erroneously rejected the Arbitrator's ruling that Rappaport submitted a $25 million claim for carried interest, concluding that "Rappaport's membership interest in the KABR entities was not an issue presented to the [A]rbitrator as a claim to be ruled upon." (26-27a.) In addition, despite the Arbitrator's expressed intent to allocate the award of $4.9 million in damages to cover both Rappaport's management and membership interests, the Appellate Division reallocated the $4.9 million damages award to cover only Rappaport's management interest -- thus making an evidential finding of its own not supported by the record. (5a.)

The panel also misapprehended the law, stating that "[a]s the decision to vacate an arbitration award is a decision of law, this court reviews the denial of

a motion to vacate an arbitration award de novo." (20a (quoting Manger v. Manger, 417 N.J. Super. 370, 376 (App. Div. 2010)).) As will be discussed, that overbroad statement is at complete odds with decisional law of this Court relating to private-sector arbitration agreements.

Although the appellate court acknowledged that "the Arbitration Agreement specifically references dissociation," it incongruously found that "neither party had notice [that] Rappaport's fair value or fair market value interest after dissociation would be included in the arbitration award." (31a; 37a.) Last, the panel disregarded the standard of deference that applies to private-sector arbitration agreements, as articulated in Tretina. (38a.)

ARGUMENT

I. Judicial Deference to Private-Sector Arbitration Awards Is the Hallmark of New Jersey Jurisprudence.

"[T]he affirmative policy of this State, both legislative and judicial, favors arbitration as a mechanism of resolving disputes." Atalese v. U.S. Legal Servs. Grp., L.P., 219 N.J. 430, 440 (2014) (alteration in original) (quoting Martindale v. Sandvik, Inc., 173 N.J. 76, 92 (2002)). Parties choose arbitration because it "can be an effective means of resolving a dispute in a low cost, expeditious, and efficient manner" and because the parties get "to choose a skilled and experienced arbitrator in a specialized field to preside over and decide the dispute." See Delaney v. Dickey, 244 N.J. 466, 493 (2020).

The parties also can decide, as they did here, what issues are proper for the arbitrator to resolve -- including whether a claim was submitted to the arbitrator. "Thus, a delegation clause in an arbitration agreement can provide that an arbitrator, rather than a judge, will decide such 'threshold issues' as whether the parties agreed to arbitrate a legal claim brought by a plaintiff." Morgan, 225 N.J. at 303 ("Parties to an arbitration agreement can agree to delegate to an arbitrator the issue of whether they agreed to arbitrate a particular dispute.") (citing Rent-A-Ctr. W., Inc. v. Jackson, 561 U.S. 63, 68-69 (2010)). Here, the parties agreed that "[t]he arbitrator shall have the power to rule on his or her own jurisdiction, including any objections with respect to the existence, scope, or validity of the arbitration agreement or to the arbitrability of any claim or counterclaim." (See Pa198 (incorporating AAA Rule 7(a) (Pa1644)).)

The parties chose the Arbitrator to determine whether Rappaport's membership interest, including carried interest, was an issue submitted to his jurisdiction. The Arbitrator was charged with the responsibility of not only determining what claims were before him but also the responsibility of resolving them. The Chancery Division afforded great deference to the Arbitrator's determinations. The Appellate Division did not and diverged from the commands of our jurisprudence. Because, in the exercise of the authority delegated to him, the Arbitrator found that the parties placed the issue of carried

interest before him, the Appellate Division was duty-bound to give heightened deference to that decision.

Parties select arbitration "to get away from the judiciary" and to avoid the "litigation wringer." Perini, 129 N.J. at 519, 542 (Wilentz, C.J., concurring). "[F]or arbitration to achieve its goal of speedy, economical and final determinations, courts must minimize their interference with arbitrators' decisions." Apex Realty, Inc. v. Schick Realty, Inc., 242 N.J. Super. 494, 497 (App. Div. 1990). To that end, "there exists a strong preference for judicial confirmation of arbitration awards." Borough of E. Rutherford v. E. Rutherford PBA Loc. 275, 213 N.J. 190, 201 (2013) (quoting Middletown Twp. PBA Loc. 124 v. Twp. of Middletown, 193 N.J. 1, 10 (2007)).

"Judicial review of an arbitration award is very limited." Bound Brook Bd. of Educ. v. Ciripompa, 228 N.J. 4, 11 (2017) (quoting Linden Bd. of Educ. v. Linden Educ. Ass'n ex rel. Mizichko, 202 N.J. 268 (2010)); see also Fawzy v. Fawzy, 199 N.J. 456, 470 (2009) ("[T]he scope of review of an arbitration award is narrow."). That is because an expansive, searching review would "severely undermine[]" "the purpose of the arbitration contract, which is to provide an effective, expedient, and fair resolution of disputes[.]" Fawzy, 199 N.J. at 470 (emphasis added).

The NJAA provides lists of criteria for the vacation and modification of private-sector arbitration awards with the preamble words, "the court shall vacate an award made in the arbitration proceeding if," N.J.S.A. 2A:23B-23, and "the court shall modify or correct the award if," N.J.S.A. 2A:23B-24. "Notwithstanding the apparently broad scope of the court's powers to alter an arbitrator's award as described in the statutory language, our courts have not traditionally interpreted the statutory language broadly." Kimm v. Blisset, LLC, 388 N.J. Super. 14, 29 (App. Div. 2006) (citing Tretina, 135 N.J. at 355). In the seminal case of Tretina, this Court made clear that the highest level of deference would be afforded to private-sector arbitration awards.

In Tretina, the Court adopted Chief Justice Wilentz's concurrence in Perini, in which he expounded on the limited scope of judicial review in private-sector arbitration awards. 135 N.J. at 357-58. In that concurrence, Chief Justice Wilentz asserted that "[a]rbitration awards should be what they were always intended to be: final, not subject to judicial review absent fraud, corruption, or similar wrongdoing on the part of the arbitrators. . . . They can be corrected or modified only for very specifically defined mistakes as set forth in [the arbitration statute]." Perini, 129 N.J. at 519, 548

In adopting Chief Justice Wilentz's concurrence in Perini, Tretina announced that a heightened standard of deference would apply to private-sector

arbitration awards. The Tretina Court rejected the formulation announced by the plurality in Perini -- that "in private-sector arbitration an arbitrator's determination of a legal issue should be sustained as long as the determination is reasonably debatable." Tretina, 135 N.J. at 357 (quoting Perini, 129 N.J. at 493). The reasonably debatable standard is the one that applies in public-sector cases. PBA Loc. 160 v. Twp. of N. Brunswick, 272 N.J. Super. 467, 473 (App. Div. 1994).[2] Accordingly, in Tretina, the Court charted a different course in overturning the Perini plurality's approach which "would allow a court to vacate an award when an arbitrator makes a mistake in respect of an undebatable point of law." Tretina, 135 N.J. at 357.[3]

This Court in Tretina "join[ed] the Chief Justice in the views expressed in his Perini concurrence." Id. at 359. According to those views, judicial

---

[2] Note that Perini and Tretina, and this case, arose in the private-sector context, while several of the cases cited above arose in the public-sector context. Review of arbitration awards in the private-sector context are given greater deference than in the public-sector context. See Kearny PBA Loc. No. 21 v. Town of Kearny, 81 N.J. 208, 217-18 (1979); PBA Loc. 160 v. Twp. of N. Brunswick, 272 N.J. Super. 467, 472-73 (App. Div. 1994).

[3] Chief Justice Wilentz was referring to what is today enumerated as N.J.S.A. 2A:23B-23(a)(1): "[T]he court shall vacate an award made in the arbitration proceeding if: (1) the award was procured by corruption, fraud, or other undue means." Since Tretina was decided, the Legislature has amended the NJAA several times. E.g., L. 2003, c. 95, § 24. Notably, the provisions that Tretina cited as N.J.S.A. 2A:24-8 and N.J.S.A. 2A:24-9 have been reformulated as N.J.S.A. 2A:23B-23 and N.J.S.A. 2A:23B-24. Compare ibid., with Tretina, 135 N.J. at 355.

correction of factual errors is so limited that neither "gross" nor "ordinary" errors will result in vacation or modification of an award. Perini, 129 N.J. at 542 (Wilentz, C.J., concurring). And with regard to "errors of law," he noted that such errors "had to be so egregious that one need only look at the cover page, at the award, to know that a horrible mistake had been made." Ibid. In other words, the error had to be "so horrible that without getting involved at all with the merits of the proceeding, with the thousands of pages of transcripts . . . , one could say that there was fraud or corruption or some similar wrongdoing that requires vacating the arbitrators' award." Ibid.

Additionally, the Tretina Court explained that "[t]he clear implication from [N.J.S.A. 2A:23B-24] is that the Legislature intended that courts correct mistakes that are obvious and simple-errors that can be fixed without a remand and without the services of an experienced arbitrator." 135 N.J. at 360.

As a result, the Court in Tretina rejected both the Chancery Division's modification of the arbitration award and the Appellate Division's vacation of the award -- an award it vacated after "conducting a detailed analysis of the contract and of the arbitration proceedings." Id. at 354. Instead, the Court entered "a judgment confirming the arbitration award in all respects," id. at 365, noting that the record had "not even a hint of misconduct by the arbitrator and .

. . no statutory ground exist[ed] for invalidating or modifying the award," id. at 358.

The panel in this case paid lip service to the principles in Tretina as it conducted a de novo review of the Arbitrator's findings. It appears that the panel may have misconstrued language in Manger, 417 N.J. Super. at 376, which stated that "[a]s the decision to vacate an arbitration award is a decision of law, this court reviews the denial of a motion to vacate an arbitration award de novo." (See 20a (quoting Manger).) That proposition of law may be applicable to certain provisions of N.J.S.A. 2A:23B-23 and -24, but it is not applicable to issues properly submitted to the discretion of the arbitrator. Those matters submitted to the arbitrator's discretion are governed by the super-deferential standard of Tretina.

Notably, Manger did not cite to Tretina or Perini. In any event, the Manger court correctly stated that its "review is informed by the authority bestowed on the arbitrator by the Arbitration Act." 417 N.J. Super. at 376. The court described this authority as "broad" and affirmed the arbitration award. Id. at 376, 377.

Similarly, in Sanjuan v. School District of West New York County, a public-sector arbitration case, the Court recognized an arbitrator's "broad discretion to fashion remedies long recognized in decisional law." 256 N.J. 369,

385 (2024). There, in reversing the Appellate Division, the Court found that the arbitrator did not exceed his powers in demoting rather than terminating a teacher. Ibid.

II. The Appellate Division Erred by Not Deferring to the Arbitrator's Determination that the Parties Submitted the Issue of Carried Interest for His Consideration.

The Appellate Division was wrong to second-guess the Arbitrator's finding that the parties had submitted for his determination the issue of whether Rappaport was entitled to carried interest.

N.J.S.A. 2A:23B-24(a)(2) provides that "the court shall modify or correct the award if: . . . the arbitrator made an award on a claim not submitted to the arbitrator and the award may be corrected without affecting the merits of the decision upon the claims submitted." But here the parties selected the Arbitrator to determine whether an issue was before him and, if so, whether to confer an award. Working within the framework of the NJAA, Morgan clearly expressed that "[p]arties to an arbitration agreement can agree to delegate to an arbitrator the issue of whether they agreed to arbitrate a particular dispute." 225 N.J. at 303. That is what the parties did here -- they agreed "that an arbitrator, rather than a judge, [would] decide such 'threshold issues' as whether the parties agreed to arbitrate a legal claim brought by a plaintiff." See ibid.

In their Arbitration Agreement, they incorporated the AAA Rules, including Rule 7(a). (Pa198.) Rule 7(a) unmistakably says that "[t]he arbitrator shall have the power to rule on his or her own jurisdiction, including any objections with respect to the existence, scope, or validity of the arbitration agreement or to the arbitrability of any claim or counterclaim." (Pa1644.)

The parties delegated to Chief Justice Zazzali the power to determine which claims had been submitted to him. The parties chose him -- not a court -- to make that determination. As the record in this case makes clear, he was in the best position to decide whether the parties had submitted the issue of carried interest for his determination. First, the broad language of the Arbitration Agreement allowed for consideration of that issue. That Agreement provided for the disposition of "any claims that could be asserted by any Party as part of the Claim or the Counterclaim or with respect to the dissolution or disassociation of Rappaport from" KABR. (Pa197 (emphases added).) Second, the parties' briefs, the testimony, and the oral arguments all raised the issue. The Arbitrator could reasonably have found that Rappaport's claim to carried interest was submitted to him.[4]

[4] In Rappaport's second action, the 2020 Complaint, Rappaport raised the same carried-interest arguments that failed before the Arbitrator. The entire controversy doctrine required him to advance his carried interest claim in the first proceeding. See Oliver v. Ambrose, 152 N.J. 383, 394 (1998). And, in

It is understandable that Rappaport, having his arguments rejected multiple times by the Arbitrator, would seek to draw our courts into the fray and put Defendants through the "litigation wringer." That is an invitation the Appellate Division should not have accepted. Because the parties had delegated to the Arbitrator the power to determine which claims were before him, Tretina deference applied to the Arbitrator's Award in deciding the merits of the claim. The panel had no business scouring the record as though it were the court of first instance. Even outside of arbitration, deference applies to a trial court's factfindings because our "judicial system . . . assigns different roles to trial courts and appellate courts." See State v. S.S., 229 N.J. 360, 379 (2017). Greater deference applies to an arbitrator's findings of fact.

Because the Arbitrator -- not the court -- was empowered by the parties to determine whether the carried-interest issue was properly before him, the panel's role was merely to rule on whether the Arbitrator made a "gross" or egregious error in determining not to award Rappaport carried interest. See Perini, 129 N.J. at 542 (Wilentz, C.J., concurring). Or, if the panel thought that it was reviewing a legal determination, it was only supposed to determine whether there was an error "so egregious that one need only look at the cover

---

fact, he did. But that did not stop Rappaport from seeking a second bite at the apple.

page, at the award, to know that a horrible mistake had been made," without reviewing "the thousands of pages of transcripts" the arbitration generated. Ibid.

Under any standard of review, much less the most rigorous one presented in a private-sector arbitration, Rappaport asserted his carried-interest claim multiple times. How did the Appellate Division go awry? Not only did it not respect the high standard of deference afforded to private-sector arbitration awards, but it also misread the record. The panel wrongly concluded that the Arbitrator, not Rappaport's attorney, raised the issue of carried interest during testimony. Perhaps the "Q." and "A." headings in the transcript confused the court. In context, it is clear that the questions came from Rappaport's attorney. (See, e.g., Pa1436 (illustrating that questions from Chief Justice Zazzali were labeled as coming from "THE COURT" while questions from counsel were labeled as coming from "Q.").)

It was in response to his own attorney's questioning that Rappaport declared, "I'm asserting the fact that I am entitled to that and I am fully vested in the carried interest." (Pa1440.)

The panel also incorrectly found that "defendants made representations on the record specifically acknowledging Rappaport's membership interests were not at issue in the arbitration." (4a.) Defendants argued that Rappaport's removal as an officer in January 2019 had "nothing to do with his status as an

equity owner." (Pa1904.) But that was simply an argument that Defendants' removal of Rappaport as an officer did not adequately establish his claim for "minority member oppression," not a concession that Rappaport's membership interest was not part of the arbitration.[5]

No one understood the history of the dispute between the parties and the issues submitted to arbitration better than the Arbitrator, who conducted lengthy and thorough arbitration proceedings over many days of hearings and reviewed thousands of pages of pleadings, briefs, and other relevant documents. (See Pa2287 ("After thirteen days of hearings and additional days of oral arguments, I issued an Award. . . . [T]he undersigned, until now, has not endured a record of almost 10,000 pages of pleadings, transcripts, briefs, exhibits, and correspondence.").)

That Rappaport was pursuing carried interest was not a figment of the Arbitrator's imagination. Rappaport testified to the value of his carried interest in response to his attorney's -- not the Arbitrator's -- questioning. (Pa1440.) In his post-hearing arbitration brief, Rappaport argued that he "is fully vested and

---

[5] Moreover, in connection with his "minority member oppression" claim, Rappaport asked for "a remedy other than dissolution." (See, e.g., Pa377 ¶ 349.) As a result, the Arbitrator had the "discretion" to "order the sale of all interests held by a member" if he thought that such a forced dissociation "would be fair and equitable to all parties under all of the circumstances of the case." N.J.S.A. 42:2C-48(b). The Arbitrator did exactly that, valuing Rappaport's membership stake as the worth of his capital account, but denying him carried interest.

entitled to carried interest," (Pa1197), and that "[the] value of [his] carried interest is $25 million dollars," (Pa1203 n.2). Rappaport, moreover, sought a declaration from the Arbitrator that Rappaport "is a member of KABR" and is "entitled to the carried interest paid by the KABR Funds . . . ." (Pa1237-39.)

Only after Rappaport lost repeated rulings from the Arbitrator on the issue of carried interest did Rappaport turn to his contrived argument that the issue of carried interest was never submitted to the Arbitrator. Rappaport filed his 2020 Complaint to tee up that issue. To the extent that there is a dispute about whether carried-interest issue was submitted to the Arbitrator, the parties chose the Arbitrator -- not a court -- to resolve that issue.

Accordingly, Tretina's heightened standard of deference applies to the Arbitrator's finding that the membership/carried interest issue was properly subject to arbitration. Absent malicious wrongdoing or egregious error, the panel should have deferred to the Arbitrator's determination. Not unlike other cases, in the present case the Court may find that the parties are presenting different versions of the facts. Ultimately, the function of the Arbitrator is to decide between the differing accounts. That is what the Arbitrator did here.

The Arbitrator's Final Arbitration Award could not have been clearer. "I find that Claimant has not established by a preponderance of the credible evidence that he has proven carried interest. I specifically find that he has not

established by a preponderance of the credible evidence the value of his current interest at the time of his termination." (Pa248 (emphasis added).) However the Arbitrator's determination may be cast, whether as a legal conclusion or a factfinding, the Appellate Division was obliged to defer to that determination in accordance with the dictates of Tretina.

Even if Tretina were to be erased from the books, a de novo review of the record would still support the Arbitrator's findings.

The Arbitrator fulfilled his charge under the AAA Commercial Rules, the NJAA, and our jurisprudence -- he fashioned a remedy he deemed just and equitable within the scope of the Arbitration Agreement. See AAA Rule 47(a) ("The arbitrator may grant any remedy or relief that the arbitrator deems just and equitable and within the scope of the agreement of the parties."). (Pa1659.) The Appellate Division assumed a power that it did not possess in reversing the Chancery Division's confirmation of the Arbitration Award and in paying no deference -- much less the deference required under Tretina -- to the findings of the Arbitrator. Accordingly, this Court should reverse the judgment of the Appellate Division and reinstate the Final Arbitration Award.

III. The Appellate Division Erred by Modifying the Award.

Even if the Appellate Division did not think that the Arbitrator had the authority to deny Rappaport's claim for carried interest, the panel did not have the power to mold the judgment as it did.

Although N.J.S.A. 2A:23B-24 states that an award can be modified or corrected where an arbitrator renders "an award on a claim not submitted to" him, a reviewing court may do so only if "the award may be corrected without affecting the merits of the decision upon the claims submitted." N.J.S.A. 2A:23B-24(a)(2). Regardless of whether the Appellate Division thought the carried-interest issue was before the Arbitrator, the fact remains that the Arbitrator awarded Rappaport $4.9 million as compensation "for his damages both as a manager and member of the KABR Entities." (Pa2289.)

Nevertheless, the Appellate Division "modified" the Final Arbitration Award by allowing the entire $4.9 million Award to stand as damages solely for Rappaport's interest as a manager. This "modification" altered the merits of the Arbitrator's decision. The Appellate Division made its own finding of fact, determining that KABR owed Rappaport $4.9 million in damages only as a former manager of the KABR entities. Such a rewriting of an award -- a rewriting that goes to the heart of the underlying arbitral decision -- is not the kind of "modification" contemplated by N.J.S.A. 2A:23B-24(a)(2). The panel

exceeded the scope of review provided by the NJAA. For that reason too, this Court should reverse the judgment of the Appellate Division and reinstate the Final Arbitration Award.

CONCLUSION

Parties choose arbitration because they can secure an arbitral forum that can resolve a dispute in a low cost, expeditious, and efficient manner. Within the arbitral setting, the parties can select a skilled and experienced arbitrator and delegate to him broad powers to decide what issues are before him and the merits of those issues. Our jurisprudence assures the parties that they can rely on the finality of the arbitrator's decision -- that the arbitrator's decision is not the first round in a litigation war that will be waged in the courts.

If the benefits of arbitration are illusory, then who will turn to arbitration as a forum for alternative dispute resolution? Morgan instructs that, when the parties agree, the arbitrator, not a court, decides which claims are subject to arbitration. Tretina instructs that the courts should keep in their lane and respect the heightened standard of deference afforded to private-sector arbitrations. The Appellate Division's meddling in the Arbitrator's determination is at complete odds with Morgan, Tretina, and with New Jersey's public policy favoring arbitration.

Here, the Arbitrator determined that the issue of carried interest was within the scope of the Arbitration Agreement and was submitted to him by the parties. The Arbitration Agreement provided that the Arbitrator would render a reasoned award and that his ruling would be final and binding, with limited exceptions. The Arbitrator fulfilled his obligation by rendering a reasoned award. This Court must now hold that it is final and binding.

For the reasons expressed, Defendants respectfully request that the Court reverse the judgment of the Appellate Division and reinstate the Arbitration Award and its confirmation by the Chancery Division.

Respectfully Submitted,

Dated: June 24, 2024
New York, New York

KASOWITZ BENSON TORRES LLP

By: */s/ Howard W. Schub*
Howard W. Schub (045381990)

1633 Broadway
New York, New York 10019
(212) 506-1700
hschub@kasowitz.com

SHAPIRO, CROLAND, REISER, APFEL & DI IORIO, LLP
Stuart Reiser (015051980)
Continental Plaza II
411 Hackensack Avenue, 6th Floor
Hackensack, NJ 07601
Tel.: 201-488-3900
Fax: 201-488-9481

Attorneys for Defendants-Petitioners