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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA  
SECOND APPELLATE DISTRICT  
DIVISION EIGHT

FUNDAMENTAL CREDIT RECOVERY  
FUND LP et al.,

Plaintiffs and Respondents.

v.

CEREF GENERAL PARTNER I, LLC,

Defendant and Appellant.

B265462

(Los Angeles County  
Super. Ct. No. BS150925)

APPEAL from a judgment of the Superior Court of Los Angeles County.  
William F. Fahey, Judge. Affirmed.

Miller Barondess and James Goldman for Defendant and Appellant.

Law Offices of Todd D. Thibodo and Todd D. Thibodo for Plaintiffs and  
Respondents.

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Appellant CEREF General Partner I, LLC (general partner) appeals from a judgment confirming an arbitration award entered in favor of respondents Fundamental Credit Recovery Fund LP and Shekels Group Investments LLC (limited partners). The general partner contends the arbitrator failed to consider an issue that was properly tendered for decision. We affirm the judgment.

### **FACTUAL AND PROCEDURAL BACKGROUND**

On January 5, 2010, the general partner and the limited partners entered into a Side Letter Agreement, where the general partner made certain assurances to secure the limited partners' investment in Series B of the CEREF Partners I, LP limited partnership. The limited partners were to invest \$3 million, representing approximately 15 percent of the total capital invested in the Series B partnership. In exchange for their investment, the Side Letter Agreement provided that the general partner would pay the limited partners a preferred return of 12 percent on their investment; the general partner would subordinate repayment of its own invested capital to the limited partners; and the general partner would fund its own capital account with at least \$1.3 million, among other assurances. Series B did not perform as expected, and the general partner failed to comply with the Side Letter Agreement. The general partner did not invest \$1.3 million of its own capital, never paid the preferred return on the limited partners' investment, and never repaid the limited partners' initial investment.

The Series B Partnership Agreement (partnership agreement) contained an exculpation provision, which provided that “[t]he General Partner . . . shall have no liability to the Partnership or to any Partner for any claims, costs, expenses, damages, or losses suffered by the Partnership which arise out of any action or inaction of [the General Partner, if the General Partner’s] course of conduct or omission was undertaken . . . in good faith and in belief that such . . . conduct or omission was in . . . the best interests of the Partnership, and . . . such course of conduct did not constitute fraud, willful misconduct or gross negligence. [The General Partner will not be liable] to the Partnership or any Partner for any claims or losses due to circumstances beyond its control. . . . [The General Partner shall not be liable] to the Partnership or any Partner for

any action or omission which such [General Partner] reasonably believed to be consistent with the advice of attorneys, accountants or other professional advisers . . . selected in good faith.”

## **I. The Arbitration**

On February 19, 2013, the limited partners filed a demand for arbitration with the American Arbitration Association (AAA), seeking \$920,000, and describing the dispute as follows: “[Limited partners] invested funds with [general partner] pursuant to a written contract in which [general partner] agreed (1) to pay a preferred return on investment and (2) to establish safeguard mechanisms to ensure payment of the preferred return. Despite repeated demands, [general partner] has refused to establish the safeguard mechanisms. [General partner’s] Chief Executive Officer also expressly repudiated [general partner’s] promise to pay the preferred return.”

On March 13, 2013, the general partner filed an answering statement, generally denying the allegations in the limited partners’ demand, and asserting “that various affirmative defenses bar [limited partners’] claim in whole or in part.” The general partner set forth its affirmative defenses, and also asserted that it “may have other separate and additional defenses of which it is not aware, and hereby reserves the right to assert them by amendment to this answering statement . . . .” The general partner did not mention the exculpation provision contained in the partnership agreement.

On May 31, 2013, the arbitrator issued a Report of Preliminary Hearing and Scheduling Order No. 1. On June 7, 2013, in response to the arbitrator’s preliminary hearing report, the limited partners filed a detailed 12-page amended claim. The general partner filed a 24-page response to the amended claim on June 24, 2013. The response included numerous affirmative defenses, but did not mention the exculpation provision.

On December 3, 2013, the parties filed their pre-hearing briefs. The general partner’s brief discussed the exculpation provision for the first time, and did not characterize it as an affirmative defense. The brief argued that the partnership agreement provides that “the General Partner is insulated from liability so long as it acts in good faith and in the best interests of the Partnership, and its conduct does not involve fraud,

willful misconduct or gross negligence. Alternatively, so long as the General Partner reasonably bases its conduct on the advice of a professional selected in good faith, and does not engage in bad faith, it will have no liability to any Partner – including [limited partners]. Accordingly, [limited partners] must show ‘bad faith,’ a ‘failure to act in the best interests of the Partnership [the Fund], or fraud, willful misconduct or gross negligence on the part of the General Partner.’ ”

The arbitration hearing was conducted on December 12, 13, and 30, 2013. On January 17, 2014, the general partner submitted its post-hearing brief, in which it again asserted the exculpation provision “insulated [the general partner] from liability so long as it acts in good faith and in the best interests of the Partnership, and its conduct does not involve fraud, willful misconduct or gross negligence. Accordingly, [limited partners] must show ‘bad faith,’ a ‘failure to act in the best interests of the Partnership, or fraud, willful misconduct or gross negligence on the part of the General Partner.’ None of this is shown by the evidence, and [the exculpation provision] supports a denial of [limited partners’] claims. [¶] Alternatively, [the exculpation provision] provides that so long as the [general partner] reasonably bases its conduct on the advice of a professional selected in good faith, and does not engage in bad faith, it will have no liability to any Partner.” (Fn. omitted.)

On May 12, 2014, the arbitrator issued a “Partial Final Award” finding in favor of the limited partners. Concerning the Exculpation Provision, the arbitrator found that: “[General Partner] relies for exculpation upon ¶ 2.4 of the [partnership agreement], which provides that if the General Partner acts in good faith and the best interests of the Partnership, and its conduct does not involve fraud, willful misconduct or gross negligence, or so long as it reasonably bases its conduct on the advice of an attorney selected in good faith, and does not engage in bad faith, the General Partner shall have no liability to any Partner. [¶] While [the General Partner’s CEO] relied strategically on [counsel] for legal advice, it was never proven that he fully disclosed to [counsel] the extent of the representations he made to [limited partners] during negotiations of the [s]ide [letter agreement], so that any reliance on advice of counsel as a defense is

misplaced. [¶] Fraud and willful misconduct constitute exceptions to the exculpatory clause. While I am not making such a finding against the [General Partner], I do not rule them out in this case. [¶] Notwithstanding the filing of a 24-page Response to Amended Claim, [General Partner] nowhere raised the defense of the exculpatory clause as an affirmative defense until it raised it for the first time in its prehearing brief, and because that is too late to raise a new affirmative defense, I need not proceed further with analysis of potential fraud or willful misconduct. [General Partner's] exculpatory clause defense is without merit.”

The partial award left open the issue of which remedies were available to the limited partners. In subsequent proceedings, the parties filed briefs addressing the remedies to be provided in the final award. The general partner's brief stated that the general partner had urged the arbitrator to reconsider her finding that the exculpation provision was an affirmative defense. The brief also argued that the arbitrator had erroneously concluded the defense had been waived, and that the provision was not an affirmative defense, but imposed a burden on the claimants to prove bad faith. The arbitrator found she was not “ ‘empowered to redetermine the merits of any claim already decided.’ ”

The arbitrator issued her final award on August 13, 2014, awarding the limited partners specific performance and money damages.

## **II. Superior Court Action**

The limited partners filed a petition to confirm the arbitration award. The general partner filed a consolidated opposition to the petition to confirm the arbitration award, and a cross-petition to vacate the arbitration award. The cross-petition argued that the “arbitrator imperfectly executed her powers” by failing to “properly and fully adjudicate issues relating to the applicability of the exculpation provision.”

With leave of the court, the parties submitted supplemental briefs in support of their positions. The general partner argued that the arbitrator “intentionally and inappropriately ignored the exculpation provision” of the partnership agreement, and that the arbitrator “exceeded her jurisdiction” by ignoring the exculpation provision. The

court granted the petition to confirm the arbitration award. Judgment was entered on May 22, 2015. This timely appeal followed.

## DISCUSSION

When parties agree to arbitrate their disputes, the scope of judicial review is strictly limited to give effect to the parties' intent "to bypass the judicial system and thus avoid potential delays at the trial and appellate levels . . . ." (*Moncharsh v. Heily & Blase* (1992) 3 Cal.4th 1, 10 (*Moncharsh*)). Generally, a court may not review the merits of the controversy, the validity of the arbitrator's reasoning, or the sufficiency of the evidence supporting the arbitration award. (*Id.* at p. 11.) " '[I]t is within the power of the arbitrator to make a mistake either legally or factually. When parties opt for the forum of arbitration they agree to be bound by the decision of that forum knowing that arbitrators, like judges, are fallible.' " (*Id.* at p. 12.)

Judicial review of an arbitration award is limited to "circumstances involving serious problems with the award itself, or with the fairness of the arbitration process." (*Moncharsh, supra*, 3 Cal.4th at p. 12.) Grounds on which a court may vacate an award are set forth in Code of Civil Procedure section 1286.2, subdivision (a), such as the award was procured by "undue means."<sup>1</sup> Moreover, an award may be vacated when an award fails to determine "all the questions submitted to the arbitrators the decision of which is necessary in order to determine the controversy." (§ 1283.4; see also *Safeway Stores, Inc. v. Brotherhood of Teamsters* (1978) 83 Cal.App.3d 430, 439-440, fn. 4.) "There is a

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<sup>1</sup> Code of Civil Procedure section 1286.2, subdivision (a) provides, "the court shall vacate the award if the court determines any of the following: [¶] (1) The award was procured by corruption, fraud or other undue means. [¶] (2) There was corruption in any of the arbitrators. [¶] (3) The rights of the party were substantially prejudiced by misconduct of a neutral arbitrator. [¶] (4) The arbitrators exceeded their powers and the award cannot be corrected without affecting the merits of the decision upon the controversy submitted. [¶] (5) The rights of the party were substantially prejudiced by the refusal of the arbitrators to postpone the hearing upon sufficient cause being shown therefor or by the refusal of the arbitrators to hear evidence material to the controversy or by other conduct of the arbitrators contrary to the provisions of this title. [¶] (6) An arbitrator making the award . . . failed to disclose within the time required for disclosure a ground for disqualification . . . or . . . was subject to disqualification . . . ."

presumption favoring the validity of the award, and [the party challenging the award] bears the burden of establishing [a] claim of invalidity.” (*Betz v. Pankow* (1993) 16 Cal.App.4th 919, 923.)

We review de novo a trial court’s order confirming an arbitration award. (*Malek v. Blue Cross of California* (2004) 121 Cal.App.4th 44, 55.)

The general partner contends the arbitrator’s award failed to decide all issues submitted to her, and that the award was procured by undue means. Specifically, the general partner contends the arbitrator erroneously failed to reach the merits of its claim that the exculpation provision barred the limited partners’ claims, an issue that had been properly tendered to her. The general partner also contends the award was obtained by “undue means” because the arbitrator sua sponte decided that the exculpation defense had been waived, without notice to the general partner, and the arbitrator erred in finding that the defense had been waived. We find no merit in these contentions.

The general partner contends the arbitrator expressly declined to make a finding on the application of the exculpation provision. However, the arbitrator *did* decide the issue of exculpation provision, and decided it against the general partner. The arbitrator decided the general partner could not be excused by its reliance on counsel under the exculpation provision. The arbitrator also decided that the general partner raised the defense for the first time in its pre-hearing brief, and that was too late to raise a new affirmative defense. Essentially, the general partner is arguing that the arbitrator misconstrued the law in finding waiver. An arbitrator’s decision cannot be reviewed for errors of law. (*Moncharsh, supra*, 3 Cal.4th at p. 12.)

The cases cited by the general partner are distinguishable, because in each of those cases, the arbitrator completely failed to address a material issue which was essential to the resolution of the parties’ claims. (*Banks v. Milwaukee Ins. Co.* (1966) 247 Cal.App.2d 34, 39-40 [arbitrator failed to decide the issue of general damages in an automobile accident case, and submitted a declaration averring that he did not consider general damages]; *M. B. Zaninovich, Inc. v. Teamster Farmworker Local Union* 946

(1978) 86 Cal.App.3d 410, 415 [arbitrator found an amount was owed for breach of contract but did not decide what amount was owed].)

The general partner also contends the award resulted from a process lacking “procedural due process or fundamental fairness” because the arbitrator sua sponte decided that the defense was waived without affording the general partner an opportunity to challenge the arbitrator’s finding. Therefore, the general partner contends the award was procured through “undue means.” (§ 1286.2, subd. (a)(1) [an arbitrator award may be vacated if “[t]he award was procured by corruption, fraud or other undue means”].) The general partner cites *Pacific Crown Distributors v. Brotherhood of Teamsters* (1986) 183 Cal.App.3d 1138, where the prevailing party in the arbitration waited until its post-arbitration brief to argue that language in a newly revised labor contract entitled the employee to an award of back pay, *after the parties had agreed before the arbitration that the new contract did not apply*. The trial court vacated the award of back pay and the appellate court affirmed, finding that the award was procured by “corruption, fraud or undue means.” The tactic of raising an issue in a postarbitration brief, without an opportunity for the opponent to respond, “ ‘intentionally and fraudulently deprived [the losing party] of its opportunity to present evidence in arbitration concerning the nonexistence of the [contractual provision] . . . .’ ” (*Pacific Crown Distributors, supra*, at p. 1149.)

Here, the general partner raised the exculpation provision in its pre-hearing and post-hearing briefs. Evidence was presented concerning the exculpation provision at the arbitration. The arbitrator addressed and discussed the exculpation provision in the award and expressly found the defense was without merit. The arbitrator did not rule out a finding that the general partner committed fraud and willful misconduct but concluded it was unnecessary to make those findings because the general partner waived the defense of the exculpation provision. There was no denial of due process or fundamental fairness. Notably, the general partner never claimed that it was denied a fair hearing or due process to the arbitrator in any of its post-arbitration filings.



**DISPOSITION**

The judgment is affirmed. Respondents are awarded their costs on appeal.

GRIMES, J.

WE CONCUR:

BIGELOW, P. J.

FLIER, J.