# JAMS ARBITRATION NO. 1425028131

JESSICA REZNICK, et al.,

Claimants,

-against-

BRIAN SCHULTZ,

Respondent.

## AMENDED FINAL ARBITRATION AWARD

The Undersigned Arbitrator, having been designated in accordance with the dispute resolution procedures set forth in a Settlement Agreement entered into as of July 23, 2018, but actually signed several months later on October 5, 2018 ("Settlement Agreement"), hereby issues the following Amended Final Arbitration Award ("Award").

In doing so, the Arbitrator wishes to acknowledge the excellent performance of counsel for both sides throughout the hearing and subsequent post-hearing briefing. The outcome of this proceeding thus is not a reflection on the quality of either side's presentation, but, rather, is based on a review of the evidentiary record in light of the applicable New York law.

### I. Introduction

In this arbitration, Claimants Jessica Reznick (Reznick"), Emma Rathe ("Emma"), Magnetic Collaborative LLC ("Magnetic" or the "Company"), Richard Rathe ("Richard"), Montana Rathe 2015/2017 Trust, and Emma Rathe 2015/2017 Trust (collectively, "Claimants") seek to recover the damages allegedly arising out of multiple breaches of the Settlement Agreement by Respondent Brian Schultz ("Schultz"). Schultz, in turn, asserts several

counterclaims against the Claimants. The claims and counterclaims arise out of Schultz's former relationship with Magnetic, by which he was employed and of which he was a member.

## II. Relevant Procedural History

In April 2018, Magnetic commenced an action against Schultz in New York State court in which it sought declaratory relief and money damages because of Schultz's alleged breaches of his employment agreement with Magnetic and the Magnetic operating agreement, both of which are dated June 1, 2012. The parties settled that lawsuit following a full-day mediation before me on July 23, 2018. The key terms of the settlement were summarized in a Memorandum of Understanding ("Memorandum") signed that day, which later was superseded by the Settlement Agreement. The Settlement Agreement provides that "[a]ny disputes or disagreements between the parties concerning the terms or implementation of this Agreement shall be resolved in arbitration by the Honorable Frank Maas of JAMS, or if he is not available by another single member of JAMS, to be selected pursuant to the JAMS Commercial Arbitration Rules, and thereafter conducted pursuant to such rules."

On or about November 8, 2018, the Claimants commenced this arbitral proceeding by filing their Demand for Arbitration and Statement of Claim with JAMS. Schultz responded and filed counterclaims on or about November 28, 2018. Thereafter, the parties amended their pleadings twice. The Claimants' Second Amended Statement of Claim was served on July 18, 2019; Schultz's Second Amended Response and Counterclaims was served on July 26, 2019.

The arbitral hearing took place over the course of four days on October 16-18, and November 13, 2019. During the hearing, the Claimants called four witnesses: Reznick, Richard, Emma, and Charles Raiche ("Raiche"). Schultz testified on his own behalf and also

called four other witnesses: Joseph ("J.J.") Jones ("Jones"), Mark Billik ("Billik"), Scott Dickerson ("Dickerson"), and Frank Hentic ("Hentic). Billik, Dickerson, and Raiche testified by electronic means from remote locations.

Following the hearing, by agreement, the Claimants submitted their post-hearing brief on December 18, 2019, Schultz submitted his opposition brief on January 22, 2019, and Claimants submitted their reply brief on February 14, 2020.[1]

With the consent of the parties, the deadline to submit an award was extended until April 15, 2020. This Award is therefore timely.

## III. Relevant Facts

Rule 24(h) of the JAMS Comprehensive Arbitration Rules & Procedures ("JAMS Rules") provides that, unless the parties agree otherwise, an award shall "contain a concise written statement of the reasons for the Award." Accordingly, this Award recites only those facts necessary to establish the basis for my conclusions. I nevertheless have considered all of the evidence and arguments proffered by the parties. To the extent there is any discrepancy between my findings and any exhibits, testimony, or contentions of a party, that is the result of my determinations regarding credibility, relevance, burden of proof, and the weighing of the evidence.

### A. Magnetic

Magnetic is an experiential marketing agency. The company creates physical environments with which consumers can interact. One example of their work is a re-creation of

[1] By letter dated January 24, 2020, Schultz's counsel drew to my attention a First Department decision issued the week before their opposition brief was due, which first came to their attention two days after the brief was filed. Counsel contended that the decision constituted controlling authority with respect to one of the legal issues in this case. To permit Claimants to address that contention without being prejudiced, I increased the page limit for their reply brief by two pages.

the Seinfeld set for Hulu, which had bought the rights to televise the Seinfeld reruns. Visitors to the set could pose for photographs while pretending to be Kramer coming through the Seinfeld apartment entryway or Jerry sitting on his couch – what Reznick described as "shareable moments."

Magnetic's motto is "From Render to Reality," which is intended to explain that Magnetic has the ability to handle every aspect of creating such an experience, from design to construction to actual operation of the environment. At times, however, Magnetic is retained only for certain aspects of that continuum, such as securing permits from relevant authorities. As Reznick explained, Magnetic is proud that it "can plug in anywhere in the process."

Although Magnetic employs nearly 100 people with expertise in such diverse fields as architecture, engineering, lighting design, and construction, it typically does not build the environments it designs. Instead, Magnetic hires others to do the construction work, with Magnetic serving in an oversight role as the project manager or general contractor. Nevertheless, when projects run behind schedule, the operating principle appears to be "all hands on deck," with Magnetic employees called upon to perform work outside their usual job duties, such as painting walls, laying floors, and installing railings.

The Company was formed on June 1, 2012, with four members, two of whom were Richard and Schultz. That same day, Schultz also signed an employment agreement, pursuant to which he served as Magnetic's Director of Engagement Strategy and Business Development reporting to Richard, the Company's Managing Member. Subsequently, two of the original four members left the Company, which increased the equity interests of Richard and Schultz. Because Richard purchased some of the former members' interests, he eventually owned 66-2/3 percent of the membership interests, with Schultz owning the other 33-1/3 percent.

B. Schultz's Employment with Magnetic

As Magnetic became successful, Schultz's compensation grew. For example, for his last year at Magnetic, Schultz's total income was approximately $1.2 million, six times his starting salary. Over time, however, Schultz and the rest of the Magnetic executive staff grew increasingly disenchanted with one another. Magnetic contends that Schultz was creating problems because of his excessive use of recreational drugs, work ethic, and relations with clients. Schultz denies these allegations and contends that Magnetic was trying to force him out of the Company. He notes that in or around the spring of 2018, Richard sought to have him spend considerable time in London overseeing the office there, which was not feasible because of issues in Schultz's family life, including the fact that Schultz's wife was pregnant with their second child.

In April 2018, Magnetic filed an action against Schultz in Supreme Court, New York County, in which the Company alleged that Schultz had been terminated for cause for violations of his employment agreement and the Magnetic operating agreement. Schultz denied that his termination was justified, contending that he had been constructively discharged and therefore had resigned with "good reason." Pursuant to the operating agreement, if Schultz was terminated for cause, the Company could purchase his interest in Magnetic for book value, which Magnetic contends was a negative number. Alternatively, if Schultz was not terminated for cause, the Company was obligated to purchase his interest for its higher appraised value.

C. Settlement of the State Court Suit

As noted above, the parties resolved the state court suit on July 23, 2018. At that time, they both signed the Memorandum which provided for Schultz to be paid a total of $2,150,000 for his membership interest in Magnetic. Of that sum, $1 million was to be paid

within thirty days, $575,000 was to be paid on July 23, 2019, and the remaining $575,000 was to be paid on July 23, 2020. In exchange, Schultz agreed that for a period of three years commencing on July 23, 2018, he would not "solicit or provide services to any of the Magnetic client's [sic] identified on the attached Exhibit A, unless approved in writing by Magnetic."

Exhibit A to the Memorandum actually listed both clients and competitors of Magnetic (the "Proscribed Entities"). Among the Proscribed Entities that Schultz could not do business with were two potential Magnetic competitors known as "Rebel & Rogue" and "BeCore." Rebel & Rogue is an experiential marketing agency owned by Schultz's brother-in-law, Jones. BeCore is a West Coast experiential marketing agency owned by Billik. The Memorandum contemplated that the parties also would enter into a formal settlement agreement containing additional terms.

After protracted discussions, the parties eventually signed the Settlement Agreement which provided that it was entered into as of July 23, 2018, the date of the JAMS mediation. Pursuant to the Settlement Agreement's terms, the first $1 million payment was to be made on October 5, 2018, when a closing would take place at Claimants' counsel's offices. The two subsequent payments were to be made as set forth in the Memorandum, but the Agreement provided that Reznick and Emma would each be liable for half of each payment, (i.e., $287,500) and that Richard would guarantee those payments.

In the Settlement Agreement, Schultz represented that he was fully aware of Magnetic's past and proposed business affairs, including its assets and liabilities, as well as certain expressions of interest regarding possible purchases of the Company, such that he was able to reach an informed decision regarding his decision to sell his membership interest for a total of $2,150,000. The Settlement Agreement further provided, insofar as relevant, that for a

period of three years beginning on July 23, 2018, Schultz would not "solicit business from or provide experiential marketing services or any other services that are competitive with the services provided by Magnetic as of the date of the Memorandum . . . to any of the entities identified on the attached Exhibit E, unless approved in writing by Magnetic" (the "Noncompete Provision"). Exhibit E listed the same Proscribed Entities as had been set forth on Exhibit A to the Memorandum. Thus, BeCore and Rebel & Rogue were both Proscribed Entities to which Schultz could not provide competitive services for the three-year period.

The Settlement Agreement also provided that, because a determination of Magnetic's actual damages would be "difficult and speculative," Schultz would pay Magnetic liquidated damages in the amount of $900,000 in the event he breached the Noncompete Provision. The Agreement further permitted Magnetic, at its option, to assign the right to recover the liquidated damages in the event of a breach to Reznick and Emma, who could then each deduct $450,000 from the amount due under their promissory notes.[2]

The Settlement Agreement further recited that the Noncompete Provision was a "material and essential term" necessary for the "protection of Magnetic's legitimate business interests, and that the Claimants would not have purchased Schultz's membership interest absent its inclusion. In addition, the Agreement provided that if "Schultz's actions result[ed] in two or more breaches of [the] Agreement," any parties that had made payments to Schultz pursuant to the Agreement would be entitled to a refund and would have "no further obligation to tender any remaining payments" in respect of the $2.1 million purchase price.

[2] Prior to the arbitral hearing, the Claimants' counsel represented to the Arbitrator and opposing counsel that such an assignment had in fact been made. (See letter from Steven J. Shore to the Arbitrator, dated July 30, 2019, at 1-2).

Finally, the Settlement Agreement contained a Default Notice provision, which required that a party intending to declare a default provide the adverse party with a written notice "specifying the default" and a ten-day cure period before instituting any mediation, litigation, arbitration, or other remedy.

D. The Trolls Experience

In 2017, Feld Entertainment ("Feld") secured the rights to produce a paid customer experience in midtown Manhattan based on the "Trolls" movie. Feld hired an experiential marketing firm to design the project, but eventually replaced that firm with BeCore in the spring of 2018. An architectural firm then translated BeCore's plans into drawings which were sent to contractors seeking to bid. The responsive bids, however, were so high that Feld feared it might not be able to complete the project. Additionally, many prospective bidders had backed out of the process because of the tight time frame for construction, which called for the The Trolls Experience to open in October 2018.

BeCore's principal, Billik, was aware that Schultz had left Magnetic and suggested that Dickerson, Feld's senior vice president for operations, reach out to him for advice when he learned that the Trolls project schedule appeared to be in jeopardy. After Billik and Schultz spoke, Schultz made a site visit, after which he advised Dickerson that he was willing to submit a bid. As he explained to Dickerson in an email, "This project fits our core capabilities and we are excited to jump into the estimation process." Although earlier emails between the two used Schultz's personal email address, Schultz sent this email using the email address of Voxel Supply LLC ("Voxel"), which is the entity that ultimately bid on the project.

Over the next week, Schultz prepared Voxel's bid with the assistance of Jones, a former Magnetic employee, and Patrick Maranzino ("Maranzino"), a Magnetic employee who was in

the process of leaving the Company. Voxel did not intend to construct the work using its own forces since it lacked the necessary license. Instead, after being awarded the job, Voxel subcontracted the construction work to Bindner Spencer Partners ("BSP"), a licensed general contractor. BSP further subcontracted portions of the work to other specialty trades such as plumbers.

According to Schultz, Voxel's role was to oversee BSP's work to ensure that it was completed on the tight time schedule that Feld required. This necessitated close coordination not only among the various trades, but with BeCore as well. BeCore therefore was charged with maintaining, and revising as needed, the overall project schedule. To ensure that the work would be properly sequenced, there were frequent jobsite meetings, attended by BeCore, Voxel, and others. Jones was the primary Voxel employee at the worksite, but Schultz was also there frequently, at least until his second child was born.

During the course of the work, certain change orders resulted in modifications of the Voxel contract price. In addition, at several points during the construction, BeCore requested that Voxel perform construction work at its behest. First, on September 21, 2018, BeCore requested eight custom electrical panels which were eventually billed to Feld. Second, on or before September 26, 2018, BeCore requested some additional painting work, noting in an email to Jones that BeCore could "keep a running list of these charges and invoice at the end if that works for you guys." Third, during a "recap" of "hot items" on October 3, 2018, BeCore noted that Voxel had cut down a door at its request, the cost of which was to be "added to BeCore['s] running tab," which "currently only include[d]" the painting work. Finally, on or about October 4, 2018, BeCore asked Voxel, inter alia, to drill a hole in a ceiling for audio and to cut holes in walls for touch panels. Responding to this last request for work, Jones sent an email to BeCore

asking, "as this work is direct with BeCore[,] can you let me know who we should send an invoice through to?

On November 1, 2018, BeCore renewed its request to Jones for an invoice for "the (2) items that were direct charges from Voxel," i.e., the additional painting work and cutting down of the door." Jones then forwarded that email to Schultz, asking whether he should "handle this over a call." At Schultz's instruction, Jones then spoke directly with Ariel Pratt, the BeCore employee overseeing The Trolls Experience project. A few days later, Pratt sent an email to Jones asking him to disregard the request for an invoice. Pratt apologized "for the miscommunication," stating that she now understood "that all payments to Voxel are being handled directly by Feld per your agreement with them." In keeping with this email, BeCore never paid Voxel any money for its work on The Trolls Experience project.

Voxel ultimately completed the construction work required by the architectural plans on or close to schedule. That work had to be completed so that BeCore and other companies could then install the experiential aspects of the project, with which Voxel had no involvement. Although Voxel bid approximately $1.1 million for its work on the project, Voxel's gross profit was only about $60,000 and its net profit was only about $26,000; Schultz individually realized no money from the project.

E. Claimant's Knowledge of Voxel's Role in the Troll Experience

On September 21, 2018, before the Settlement Agreement was signed, Magnetic received an email that Billik had mistakenly sent to Schultz's legacy email address at the Company. In that email, which concerned "The Trolls Team," Billik reported to his "fellow Trollers" that Dickerson was "really happy with everything going on with the team and how we are jumping through any last-minute hurdles or hoops." This email raised concerns at Magnetic

that Schultz might be doing business with BeCore in violation of the Settlement Agreement. Magnetic responded by arranging for its counsel to retain a private investigator to visit The Trolls Experience site to determine what Schultz was doing. There, at some point between October 16 and 22, 2018, the investigator interviewed Hentic, who was a BSP employee. In a recorded interview, Hentic explained that NBCUniversal owned the rights to the Trolls, but granted a license to Feld for the Troll Experience, that Feld in turn "hired BeCore to help with the production," that "BeCore hire[d] Voxel," and that Voxel hired BSP. Hentic's job at BSP was to source products such as brass electrical cover plates for floor outlets. Accordingly, there is no indication that he had any personal knowledge of the contractual arrangements among the parties. In fact, to the extent that he suggested that "BeCore hire[d] Voxel," he plainly was wrong.

On October 23, 2018, Claimants' counsel wrote to Schultz's counsel to request a copy of any agreements that Schultz had entered into in connection with The Trolls Experience project and the amount of consideration Schultz would receive. Claimants' counsel made this request based on Magnetic's "understanding that [Schultz] ha[d] been working on behalf of BeCore" at The Trolls Experience site. The following day, Schultz's counsel responded that Voxel had been retained by Feld, an entity unrelated to BeCore, contending that the fact that Feld may also have engaged BeCore to work side-by-side with Voxel did not constitute a breach of the Settlement Agreement. Schultz's counsel further represented that the services that Schultz had provided to Feld were "merely general contracting services, namely overseeing the installation of drywall, HVAC units, fire sprinkler, painting and electrical work, not experiential marketing services, and not competitive with Magnetic's services." Counsel noted that Schultz had learned of Magnetic's retention of the private investigator, arguing that the attempt to hold

Schultz in default without affording him notice and an opportunity to cure any alleged infraction showed that Magnetic's real purpose was not to protect its market share, but rather, simply, to "create a windfall event whereby . . . Schultz would stand to forfeit a Million Dollars."

F. The Parties' Claims

In their Second Amended Statement of Claim, the Claimants assert two claims for relief. First, the Claimants contend that Schultz breached the Noncompete Provision of the Settlement Agreement by, "inter alia, engaging Jones and Maranzino to work at Voxel and provide services for BeCore in connection with The Trolls Experience." Second, the Claimants maintain that Schultz breached the Agreement "by retaining property of Magnetic that should have been returned, and by continuing to use Magnetic's property and making unauthorized charges to Magnetic's corporate American Express credit card after the Closing."

In his Response to the Second Amended Statement of Claim, Schultz asserts four counterclaims. First, Schultz seeks a declaratory judgment that the noncompete provision does not bar him from: (1) working on projects on which the Proscribed Entities identified in the Settlement Agreement also are working, so long as Schultz does not violate the plain language of the Noncompete Provision; (2) "providing general contracting services" to the Proscribed Entities because those services "do not constitute 'experiential marketing services' and are not competitive with" services that Magnetic was providing as of July 23, 2018; (3) "creating a new entity with, or partnering with any of the principals" of most of the Proscribed Entities;[3] and (4) "engaging the services of, and having services provided from" any of the Proscribed Entities or their principals.

[3] Schultz excluded three of the Proscribed Entities from this aspect of his request for declaratory relief because the line of Exhibit E to the Agreement on which they are identified contains the words "or any additional business they set up." The other Proscribed Entities were not described in that manner.

Schultz's second counterclaim alleges that the Claimants breached the Settlement Agreement by (1) failing to give him a notice to cure, (2) retaining a private investigator whose presence at The Trolls Experience jobsite damaged his reputation and caused other damages, (3) adding a clause to Magnetic's agreements that bars its vendors from working with Schultz, and (4) demanding that Magnetic's vendors not do business with Schultz.

In his third counterclaim, Schultz seeks to recover the attorneys' fees and costs he has incurred in connection with this arbitration.

Finally, in his fourth counterclaim, Schultz seeks to recover the $575,000 that was to have been paid to him on July 23, 2019, pursuant to the Settlement Agreement.

## IV. Discussion

### A. Claimants' Breach of Contract Claims

The Settlement Agreement provides that it is governed and shall be construed under New York law. Accordingly, to prevail on any of their breach of contract claims, the parties must prove "(1) a contract; (2) performance of the contract by one party; (3) breach by the other party; and (4) damages." Williams v. Time Warner, Inc., No. 09 Civ. 2962 (RJS), 2010 WL 846970, at *6 (S.D.N.Y. Mar. 6, 2010) (quoting Terwilliger v. Terwilliger, 206 F.3d 240, 245-46 (2d Cir. 2000)). Each of these elements must be established by a preponderance of the evidence. Ward v. N.Y. Life Ins. Co., 225 N.Y. 314, 322 (1919).

As the Claimants accurately observe, their breach claims primarily turn on "one question: Did Schultz provide 'experiential marketing services, or any other services that are competitive with the services provided by Magnetic' to BeCore on The Trolls Experience" project. Building on the fact that Magnetic often oversees the construction of experiential marketing projects by subcontractors for its clients as part of its "Render to Reality" services, the

Claimants argue that Schultz was providing "experiential marketing services" to BeCore, in violation of the Settlement Agreement, through Voxel's work on The Trolls Experience project. The evidence makes clear, however, that Feld retained BeCore to design the experiential aspects of the project, and that Voxel and Schultz played no role in that design. Indeed, by the time that BeCore and others began to install the experiential aspects of the project at the site, Voxel's construction work was largely completed.

Nevertheless, the Agreement does not bar Schultz merely from providing experiential marketing services to the Proscribed Entities. Rather, the Agreement also precludes Schultz from providing those Proscribed Entities with "any other services that are competitive with the services provided by Magnetic." There is no question that those services on other prior Magnetic experiential marketing projects included general contracting services that were furnished by subcontractors that Magnetic would oversee.

At The Trolls Experience project, Schultz, through Voxel and BSP, unquestionably provided general contracting services. While those services were mostly furnished to Feld, with which Voxel had a contract, on a handful of occasions Voxel also provided those services to BeCore at its request, even if Voxel eventually refused to accept payment from BeCore or the cost of the work was billed to Feld. In doing so, Schultz violated the Noncompete Provision of the Settlement Agreement by providing services to BeCore that were competitive with services that Magnetic had provided to its other clients on or before July 23, 2018. The Settlement Agreement provides that in such circumstances Schultz is liable for the payment of liquidated damages.

The Settlement Agreement further provides that the Claimants need not pay Schultz any more money, and can recoup the $1 million already paid, if Schultz commits two or

more breaches of the Agreement. Perhaps not surprisingly, the Claimants therefore contend that BeCore also breached the Settlement Agreement in other ways, none of which withstands scrutiny.

First, the Claimants argue that because Rebel & Rogue was on the list of Proscribed Entities, and Jones is one of the three principals of Rebel & Rogue, Schultz violated the Noncompete Provision by hiring Jones to help formulate Voxel's bid and to oversee the work of BSP and its subcontractors. As Jones testified, however, Rebel & Rogue is an experiential marketing company that does not do construction. Moreover, Jones performed his construction oversight work for Voxel through JJ the Producer LLC, another company that he owns. The clear intent of the Memorandum and Settlement Agreement was to prevent Schultz from working with Rebel & Rogue, a competitor in the experiential marketing space. Had the Claimants wanted to prevent Schultz from working with his brother-in-law Jones on any aspect of the work that Magnetic typically performs, they could have identified him individually on the list of Proscribed Entities. Having failed to do so, they cannot establish that Schultz's retention of Jones or JJ the Producer to oversee construction work at The Trolls Experience site violated the Settlement Agreement's prohibition against working with Rebel & Rogue.

Next, the Claimants maintain that Schultz violated the Settlement Agreement because Maranzino helped Voxel prepare its bid for the proposed construction work on The Trolls Experience. According to the Claimants, Maranzino worked for Magnetic as a detailer, assisting in the assembly of technical drawing packages, until late August 2018. On August 22, 2018, Schultz sent Maranzino a copy of floorplans for The Trolls Experience that had been sent to him by Billik. The following day, Maranzino responded with an order of magnitude estimate of the construction work, suggesting that it would be "about a $3MM price tag.' In his email

containing that estimate (which proved to be wildly inaccurate), Maranzino also volunteered that he had taken a look at the cost of a recent Magnetic project for Netflix, and he provided information about the size of that project, the fabrication and construction costs, and the expenses per square foot. The Claimants contend that this constituted the misappropriation of confidential Magnetic information because Schultz had left Magnetic before the firm undertook the Netflix project.

To prevail on their breach allegation concerning Maranzino, the Claimants must show that Schultz's receipt of the information volunteered by Maranzino violated some provision of the Settlement Agreement. Maranzino, however, is not mentioned in the schedule of Proscribed Entities. Although the Settlement Agreement also prohibited Schultz from inducing Magnetic employees to leave the Company, it is undisputed that Maranzino had given notice of his intent to resign long before Schultz offered him an opportunity to assist with the preparation of The Trolls Experience bid. Schultz therefore did not violate the non-solicitation provision of the Settlement Agreement.

During his testimony, Schultz conceded that the Netflix costs were "confidential information." It nevertheless seems doubtful that the rather general information that Maranzino volunteered to Schultz rises to the level of a confidential trade secret. In any event, even if the information did constitute a trade secret and Maranzino's employment agreement prohibited him from furnishing it to Schultz, the Claimants have not pointed to any provision of the Settlement Agreement that Schultz violated by receiving the information and not notifying Magnetic that it had been given to him. Moreover, even if one were to assume that this exchange of information violated employment agreements that both Maranzino and Schultz previously had signed as a condition of their employment, the Claimants have failed to establish that their alleged

misconduct would be arbitrable before this tribunal. It follows that the Claimants have failed to prove that Schultz should be held liable in this forum for a contractual breach arising out of his dealings with Maranzino related to The Trolls Experience.

Finally, the Claimants argue that Schultz breached the Settlement Agreement by using his Magnetic credit card to purchase an airline ticket long after he had resigned from the Company. The Claimants suggest that they were injured because they had to incur legal fees to recover this unauthorized expenditure. The Claimants gave Schultz's counsel notice of the problem by letter dated December 17, 2018, but Magnetic was not reimbursed until January 15, 2019. The Claimants also allege that Schultz breached the Settlement Agreement because he and Jones failed to return certain Magnetic equipment when they left the Company.

As Schultz explained, the improper charge was inadvertent. When booking a flight after he had left Magnetic, Schultz used his cellphone to pay and mistakenly selected the Magnetic credit card, which was identified only by its last four digits, as the means of payment. Schultz testified that he reimbursed Magnetic "immediately once [he] found out about this mistake."

During his testimony, Jones conceded that he was aware that Magnetic wanted him to return his cellphone following his departure from the Company. Instead, he took it to a Verizon store, where he turned it in after learning that it had been locked, presumably by Magnetic.

In paragraph 13 of the Settlement Agreement, Schultz acknowledged that he "ceased to be a Member or an officer or hold any other positions, titles, duties, authorities and responsibilities with Magnetic . . . , including without limitation, as Director effective as of January 1, 2018." The Claimants contend that Schultz breached this provision through his

mistaken use of the credit card. Schultz, however, has never claimed that he continues to be associated with Magnetic in any way. Consequently, even if Schultz's representation in paragraph 13 gave rise to rights enforceable in this arbitration (itself a dubious proposition), the Claimants have failed to establish that Schultz breached its terms through his inadvertent use of the Magnetic credit card account. They also obviously have not established that Jones' failure to return his phone constitutes a breach by Schultz of any contractual undertaking.

In sum, of the various breaches alleged in the Second Amended Statement of Claim, the Claimants have established only that Schultz violated the Noncompete Provision by furnishing certain services competitive with services that Magnetic previously has provided to its clients at The Trolls Experience worksite at BeCore's request.

B. Notice of Default

Schultz contends that even if he breached the Settlement Agreement, the Claimants cannot recover damages because they failed to give him timely notice of his default and an opportunity to cure. He further maintains that the Claimants were aware of his work on The Trolls Experience by October 5, 2018, but chose to sandbag him by failing to raise their breach concerns before he signed the Settlement Agreement containing the liquidated damages clause.

Prior to the closing of the Settlement Agreement, Magnetic unquestionably was aware of Billik's email dated September 21, 2018, to the members of the Trolls Team, including Schultz. Indeed, the Claimants' preliminary inquiries heightened their suspicion to the degree that they contacted an investigator whom their counsel subsequently retained. Following her retention, the investigator traveled to New York City, where she apparently observed The Trolls

Experience worksite from October 16 to 22, 2018. She also interviewed Hentic during this period.

The Memorandum containing the key settlement points to which the parties had agreed does not contain a notice and cure requirement. Accordingly, the obligation to give notice of an alleged breach first arose when the Settlement Agreement was signed on October 5, 2018. As the Claimants correctly observe, by that date Voxel's work at The Trolls Experience site was "99%" complete. It follows that even if the Settlement Agreement required notice of a default and an opportunity to cure, sending the notice at that point would have been a futile exercise. Under New York law, strict compliance with a notice and cure provision is not necessary, where, as here, affording an opportunity to cure would have been "useless." Bank of N.Y. Mellon Trust Co., N.A. v. Morgan Stanley Mortg. Capital, Inc., 821 F.3d 297, 312 (2d Cir. 2016). The Claimants' failure to provide notice of a potential default therefore is not a basis on which Schultz can avoid the consequences of performing work for one of the Proscribed Entities.[4]

C. Damages

The Agreement provides that Schultz will pay Magnetic liquidated damages in the amount of $900,000 if he breaches the terms of the Noncompete Provision. This is an astonishingly large amount in relation to Voxel's total profit on the job. Nevertheless, Schultz made the determination to skate close to the line by working at a jobsite where he knew one of

[4] Schultz maintains that he could have cured any breach, despite the late stage of Voxel's work, through other means, such as disgorging his profits. Disgorgement, however, is not a remedy that the Settlement Agreement contemplates in the event Schultz breaches the Noncompete Provision.

the Proscribed Entities would also be working, without first advising Magnetic and seeking its consent or raising the issue with the Arbitrator.[5]

A liquidated damages provision is enforceable if the damages likely to be suffered by the party seeking to enforce it are difficult to determine when the contract is entered into and the stipulated amount constitutes a reasonable estimate of the probable harm. See BDO Seidman v. Hirshberg, 93 N.Y.2d 382, 396 (1999); City of Rye v. Public Serv. Mut. Ins. Co., 34 N.Y.2d 470, 473 (1974). "If, however, the amount fixed is plainly or grossly disproportionate to the probable loss, the provision calls for a penalty and will not be enforced." Truck Rent-A-Center, Inc. v. Puritan Farms 2nd, Inc., 41 N.Y.2d 420, 425 (1977). "Whether a contractual provision represents an enforceable liquidation of damages or an unenforceable penalty is a question of law. . . ." Bell v. Abadat, 08 Civ. 8965 (RJS), 2009 WL 1803835, at *2 (S.D.N.Y. June 16, 2009) (quoting Bates Adv. USA, Inc. v. 498 Seventh, LLC, 7 N.Y.2d 115, 120 (2006)). "[A]ny doubt with respect to whether the relevant provision is an unenforceable penalty or a permissible liquidated damages clause should be resolved in favor of a construction which holds that the provision is a penalty." Id. (quoting Bristol Inv. Fund, Inc. v. Carnegie Int'l Corp., 310 F.Supp.2d 556, 566 (S.D.N.Y.2003) (applying New York law)). Nonetheless, "[t]he burden is on the party seeking to avoid liquidated damages . . . to show that the stated liquidated damages are, in fact, a penalty." JMD Holding Corp. v. Cong. Fin. Corp., 4 N.Y.3d 373, 380 (2005).

The Memorandum executed by the parties makes no mention of liquidated damages, which first were referenced in the more detailed Settlement Agreement. As the

[5] In his post-hearing brief, Schultz notes that he consulted with counsel before Voxel entered into its agreement with Feld, thereby allegedly entitling him to assert an advice of counsel defense. The Claimants contend that this defense is inapplicable because the record is silent as to the advice that Schultz's counsel rendered. There is no need to resolve this issue because neither intent nor scienter is an element of a breach of contract claim under New York law. Thus, Schultz could have acted in complete good faith and still be liable for his breach of contract.

Agreement recites, both sides were represented by counsel during its negotiation. Counsel's zealous representation of Schultz at every stage of his negotiations regarding his departure from Magnetic confirms that the liquidated damages provision that was incorporated into the final Agreement is not a contract of adhesion.

As part of his argument against the imposition of liquidated damages, Schultz notes that Voxel's gross profit on the work that it did for Feld was "about $60,000," resulting in a net profit of "about $26,000" after the payment of various expenses, including $46,000 paid to Jones, $3,000 paid to Maranzino, and $7,800 paid for insurance. Additionally, Schultz himself received no remuneration from Voxel for the job. The issue, however, is not what Schultz or Voxel actually earned, but whether the damages that Magnetic would suffer if Schultz breached the Noncompete Provision were ascertainable at the time the Settlement Agreement was signed and, if not, whether $900,000 was a reasonable estimate of the likely damages it would sustain.

At the hearing, Richard testified without contradiction that he and Schultz negotiated the liquidated damages amount through a series of telephone conversations. Richard explained that Magnetic previously had completed a number of projects for Facebook and others for which the contract amounts were in the neighborhood of $5 million. Since the profitability of those projects often exceeded 35 percent, Richard initially suggested to Schultz that the agreed liquidated damages amount should be $1,750,000. Eventually, however, he and Schultz agreed on a "much lower amount." In arriving at the $900,000 figure, Schultz clearly did not have to rely solely on Richard's representations concerning Magnetic's past performance. Indeed, in the Settlement Agreement, Schultz expressly agreed that he was "aware of the past and proposed business, affairs, assets, liabilities, operations, and results of operations of Magnetic and the businesses thereof."

Clearly, Magnetic's expectation at the time the parties negotiated the Settlement Agreement was that if Schultz violated the Noncompete Provision it would be by seeking employment with a Magnetic competitor or stealing one of Magnetic's important clients. Had he done so, the agreed liquidated damages amount would unquestionably have been reasonable in light of Magnetic's past experiential marketing work and profitability. As it happens, Schultz breached the Noncompete Provision through an arguably less egregious violation. There is no suggestion, however, that either side anticipated a breach of the Noncompete Provision that would entail Magnetic suffering significantly less damage. Indeed, had that been the case, Schultz, who was represented by able counsel, presumably would have negotiated a more elaborate liquidated damages clause covering that circumstance. His failure to seek some sort of graduated liquidated damages formula, covering losses less than $900,000, confirms that Schultz did not anticipate a breach of the sort that now has exposed him to liquidated damages. It follows that the $900,000 amount set forth in the Settlement Agreement, rather than constituting a penalty, was a reasonable attempt to estimate the Claimants' likely losses in the event of a breach.

I note that within days after Schultz served his post-hearing brief, his counsel submitted a letter calling attention to the First Department's recent decision in Rubin v. Napoli Bern Ripka Shkolnick, LLP, 118 N.Y.S.3d 4 (1st Dep't 2020). There, the court affirmed the denial of summary judgment to the defendant law firm, which sought liquidated damages for the breach of a confidentiality agreement, observing that "the party seeking to enforce [a liquidated damages] provision must necessarily have been damaged for the provision to apply." Id. at 7 (citing J. Weinstein & Sons, Inc. v. City of New York, 35 N.Y.S.2d 530 (1st Dep't 1942)).

It is, of course, black letter law that a claimant alleging a contractual breach claim must prove damages as an element of the claim. Williams, 2010 WL 846970, at *6. In Rubin, because the defendants had moved for summary judgment on their breach of contract claim, relying on the liquidated damages clause without explaining how they were damaged, the motion court did not have an opportunity to consider whether the liquidated damages amount was "plainly or grossly disproportionate" to the probable loss when the contract was drafted. Accordingly, the Appellate Division affirmed the denial of summary judgment on the defendants' breach of contract claim. This is consistent with the decision in Weinstein, upon which the Appellate Division relied, which stated simply that "[a]greements to pay fixed sums characterized as liquidated damages which plainly have no reasonable relation to any probable damage that may follow a breach will not be enforced." 35 N.Y.S.2d at 532 (emphasis added).

As noted previously, in advancing the argument that the Claimants failed to provide him with the required default notice, Schultz contended that any harm to Magnetic caused by Voxel's work on The Trolls Experience could have been cured by disgorging Voxel's profits on the project. This possibility, posited by Schultz himself, underscores that Magnetic was damaged by Schultz's breach, even if, as appears likely, the damages that it actually suffered were relatively slight. Indeed, any work that Schultz performed that improved BeCore's standing with its client arguably worked to Magnetic's detriment since BeCore had in the past sought to poach Facebook, one of Magnetic's premier clients, and hoped to establish a greater presence on the East Coast. Accordingly, even if Rubin requires that a claimant suffer actual damages for liquidated damages to be awarded, there is no question that the Claimants have satisfied this element of their breach of contract claim.

D. Schultz's Counterclaims

In his first counterclaim, Schultz seeks a declaratory judgment regarding the scope of the activities that he can undertake in the future despite the Noncompete Provision of the Settlement Agreement. Under New York law, a "court may render a declaratory judgment having the effect of a final judgment as to the rights and other legal relations of the parties to a justiciable controversy whether or not further relief is or could be claimed." N.Y. C.P.L.R. § 3001 (emphasis added). If a court declines to issue a declaratory judgment it must state its grounds. Id. The use of the word "may" in the declaratory judgment rule underscores that the remedy is discretionary. Bower & Gardner v. Evans, 60 N.Y.2d 781, 783 (1983). Moreover, the rendering of a declaratory judgment is inappropriate when any decree that might be issued would "become effective only upon the occurrence of a future event that may or may not come to pass." Employers' Fire Ins. Co. v. Klemons, 645 N.Y.S.2d 849, 850 (2d Dep't 1996) (quoting NYPIRG, Inc. v. Carey, 42 N.Y.2d 527, 531(1977) (quoting 3 J. Weinstein, H. Korn & A. Miller, N.Y. Civil Practice ¶ 3001.09b)); accord Combustion Eng'g, Inc. v. Travelers Indem. Co., 428 N.Y.S.2d 235, 237 (1st Dep't 1980).

Schultz seeks a declaration that the Settlement Agreement does not bar him from: (1) working alongside the Proscribed Entities, so long as he does not violate the plain language of the Noncompete Provision; (2) providing general contracting services to those Proscribed Entities because those services do not constitute experiential marketing services and are not competitive with services that Magnetic was providing as of July 23, 2018; (3) "creating a new entity with, or partnering with any of the principals" of most of the Proscribed Entities; and (4) "engaging the services of, or having services provided from any of" the Proscribed Entities or their principals.

For the reasons set forth above, I have found that general contracting services of the type that Voxel furnished to BeCore and Feld are competitive with the services that Magnetic was providing to its clients as of July 23, 2018. Accordingly, there is no basis for a declaration that the provision of such services to the Proscribed Entities would not violate the noncompete provision.

Turning to the remaining branches of Schultz's first counterclaim, it is clear that, rather than asking for an interpretation of contractual language that will have a present-day application, Schultz is instead asking for an advisory opinion as to what the outcome would be if he engages in further business activities involving the Proscribed Entities or their principals. In each instance, however, the declaration that he seeks is contingent upon the occurrence of a further event, such as a new contractual relationship between Shultz or a company that he controls and a Proscribed Entity or one of its principals. It is conceivable that Schultz could enter into an arrangement along the lines that he describes that would pass muster. For example, using a variant on the facts of this case, Schultz could conceivably agree to serve as a construction supervisor on a future Feld project for which BeCore had agreed to furnish the experiential marketing components. If, however, the agreement with Feld provided that Voxel's work would be completed before BeCore's work began, and Voxel and BeCore consequently never interacted, the mere fact that Voxel and BeCore both were working on the same experiential marketing project might not give rise to a breach of the Settlement Agreement because Voxel would not be providing any services to any of the Proscribed Entities. As this case demonstrates, however, such determinations are necessarily fact bound. It therefore would be inappropriate to grant declaratory relief at this juncture in the form of the broad advisory pronouncements that Schultz seeks. Schultz's first counterclaim is therefore denied.

In his second counterclaim, Schultz contends that the Claimants violated Paragraph 14.C of the Agreement by sending a private investigator to The Trolls Experience worksite and causing persons who do business with Magnetic not to do business with him. That paragraph provides that:

> The Parties agree not to make, or cause to be made, at any time after the date hereof, any negative or disparaging statements about another Party hereto (including any of the circumstances or allegations giving rise to the Complaint), or to intentionally do anything that damages the other or any of Magnetic's affiliates or any of their respective services, reputations, financial status, businesses, members, directors, officers or employees.

Schultz alleges that the investigator's inquiries caused others to contact him to advise him that he was under investigation, which in turn "damaged [his] reputation, interfered with his work and caused him financial damages." Suffice it to say, there was no testimony during the arbitral hearing about any statements that others made to Schultz concerning the investigator's work, much less any monetary damages that the inquiry may have caused. Indeed, apart from certain details of the investigator's retention and billing, the only evidence that was adduced with respect to her was that she spoke with Hentic briefly at the jobsite – an event so benign that Hentic was unable to recall it, even after he heard a recording of a brief portion of the interview when he testified.

Turning to the second aspect of this counterclaim, Schultz contends that Richard required that vendors and freelancers doing business with Magnetic sign agreements not to do business with Schultz as a condition of being awarded work. Despite that assertion, Schultz introduced no evidence of any such agreements at the hearing. Richard did testify that he asked both his long-term accounting firm and his insurance broker not to do business with Schultz, but there is no evidence that this request caused Schultz to suffer anything other than some

inconvenience. There also has been no showing that his request was accompanied by negative or disparaging statements about Schultz.

Moreover, Raiche, the founding partner of the Raiche Ende accounting firm, testified that he independently made the decision to cease doing business with Schultz because of the "situation" involving Magnetic, Richard, and Schultz, and because he was a trustee for the Montana Rathe 2015/2017 Trust, one of the Claimants bringing claims against Schultz in this arbitration. According to Raiche, this led to an "untenable situation."

For the foregoing reasons, Schultz has failed to establish any violation of paragraph 14.C of the Settlement Agreement. His second counterclaim is therefore denied.

Schultz's third counterclaim seeks the recovery of his attorneys' fees and expenses. This counterclaim is discussed – and denied – in the next section of this Award.

Schultz's fourth counterclaim alleges that Emma and Reznick violated the payment terms of the Settlement Agreement by failing to make a payment in the amount of $575,000 for Schultz's membership interest in Magnetic or before July 23, 2019. Schultz further alleges that Richard did not honor his personal guaranty of that payment obligation. By failing to remit the $575,000, despite due demand therefor, Emma, Reznick, and Richard gambled that Schultz would be found liable for an amount greater than what they owed him. For the reasons set forth above, the Claimants have established that Schultz owes Magnetic $900,000 as liquidated damages for his breach of the Settlement Agreement. Moreover, the Agreement gave Magnetic the right to assign its claim for liquidated damages to Emma and Reznick. It follows that Emma, Reznick, and Richard did not have an obligation to pay Schultz money last July that he would then have been required to return by virtue of this Award**.** See, e.g., Matter of Midland Ins. Co., 79 N.Y.2d 253, 264 (1992) ("Contracting principals, who are debtors and creditors of

each other by virtue of entry into a contract or contracts, have the same legal capacity and may set off debts against each other.").

E. Attorney's Fees and Costs

The Settlement Agreement provides that, "[i]n addition to all other remedies available hereunder, the non-prevailing Party shall pay the cost and expenses, including reasonable attorneys' fees and expenses, of the prevailing party." Based on this provision, both sides seek to recover their costs and expenses.

Although the Claimants prevailed with respect to their entitlement to liquidated damages, Schultz was the victor with respect to the Claimants' efforts to establish that he had committed two or more breaches of the Settlement Agreement, thereby entitling them not to pay any further monies and to recoup the $1 million that they had already paid. Schultz also prevailed with respect to the Claimants' second claim for relief which alleged, inter alia, that he breached the Settlement Agreement by using the Magnetic corporate credit card and failing to return (or cause Jones to return) certain Magnetic equipment after he left Magnetic's employ. Thus, both sides prevailed with respect to aspects of their claims in this arbitration. It follows that neither side is a "prevailing party" entitled to recover its attorneys' fees and expenses.

Both sides also have incurred expenses related to JAMS' administration of this arbitration, including the fees for my time. Rule 24(f) of the JAMS Rules provides that "[t]he Award of the Arbitrator may allocate Arbitration fees and Arbitrator compensation and expenses, unless such an allocation is expressly prohibited by the Parties' Agreement." In the Settlement Agreement, the parties essentially adopted that standard, providing that "each side shall initially share equally in the fees payable to JAMS, subject to reimbursement as determined by the

[A]rbitrator." For the reasons set forth above, I find that it is equitable that both sides share equally in the cost of this JAMS arbitration.

V. Award

For the foregoing reasons, the Claimants are awarded the sum of $325,000 ($900,000 - $575,000) to be paid by Schultz within thirty days. All remaining relief requested by the parties, including their requests to recover their legal fees and expenses, are denied. Additionally, the parties shall share equally the JAMS charges related to this arbitration, including the Arbitrator's compensation.

SO ORDERED.

Dated: New York, New York
April 15, 2020

_____
Frank Maas
Arbitrator

I, Frank Maas, do hereby affirm upon my oath as Arbitrator that I am the individual described in and who executed this instrument, which is my Final Arbitration Award.

_____ April 15, 2020
Frank Maas
Arbitrator

**PROOF OF SERVICE BY E-Mail**

Re: Reznick, Jessica, et al vs. Schultz, Brian
Reference No. 1425028131

I, Shakiya Wright-McDuffie, not a party to the within action, hereby declare that on April 16, 2020, I served the attached Amended Final Arbitration Award on the parties in the within action by electronic mail at New York, NEW YORK, addressed as follows:

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Brian Schultz

I declare under penalty of perjury the foregoing to be true and correct. Executed at New York, NEW YORK on April 16, 2020.

_____

Shakiya Wright-McDuffie
JAMS
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