

MFB Realty LLC v Eichner

2016 NY Slip Op 31242(U)

June 24, 2016

Supreme Court, New York County

Docket Number: 653549/2014

Judge: Saliann Scarpulla

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 39

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MFB REALTY LLC, individually and derivatively
on behalf of T. PARK CENTRAL, LLC, and
JOSEPH LIPARI, as Executor of the ESTATE OF
JAY M. FURMAN, individually,

Plaintiffs,

-against-

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IAN BRUCE EICHNER, LESLIE EICHNER,
STUART EICHNER, SCOTT L. LAGER,
O. PARK CENTRAL LLC, PARK CENTRAL
MANAGEMENT LLC and NEW YORK URBAN
OWNERSHIP MANAGEMENT LLC,

Defendants.

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Scarpulla, J.

Defendants Ian Bruce Eichner, Leslie Eichner, Stuart Eichner (“the Eichners”),
Scott L. Lager, O. Park Central LLC (“O. Park”), Park Central Management LLC (“Park
Central”), and New York Urban Ownership Management LLC (“Urban Ownership”)
(collectively, “defendants”) move, pursuant to CPLR 3211 (a) (1), (3), (7), and (10), to
dismiss the complaint in its entirety and with prejudice.

In the complaint, plaintiffs MFB Realty LLC (“MFB”), suing individually and
derivatively on behalf of T. Park Central, LLC (“T. Park”), and Joseph Lipari (“Lipari”),
as executor of the Estate of Jay M. Furman (“Estate”) (collectively “plaintiffs”), allege
that defendants misused and diverted T. Park's corporate assets for the benefit of O. Park,

a company wholly owned by defendants, to transform O. Park into a timeshare project in direct competition with T. Park and to drain T. Park's sales.

In 1995, the Eichners, Park Central, Jay M. Furman ("Furman"), now deceased, and nonparties Richard Birdoff ("Birdoff") and Alexis Promuto ("Promuto") created T. Park, a New York limited liability company, to be a timeshare residential condominium project, known as the Manhattan Club, in the Park Central Hotel building located at 870 Seventh Avenue in Manhattan.

In 1996, they entered into an amended and restated operating agreement for T. Park (the "T. Park operating agreement") which lists Park Central as the T. Park managing member having a 1% membership interest, and the Eichners as T. Park non-managing members holding a combined membership interest of 88%. The T. Park operating agreement also lists Promuto and Birdoff as non-managing members, each holding a 1% membership interest, and Furman as a non-managing member, holding a 9% membership interest.

Plaintiffs allege that the Eichners, Park Central, and Promuto created O. Park to be an office space project in the building. Plaintiffs further allege that, eventually, the Eichners, Park Central, and Promuto determined that the office space project was not financially viable, and converted the project to a timeshare project, in direct competition with T. Park.

Plaintiffs allege that defendants intended to continue operating the Park Central Hotel on some of the floors of the building through nonparty H. Park Central LLC (H.

Park). Plaintiffs also allege that defendants developed a retail space project at the building through nonparty R. Park Central LLC (R. Park).

Plaintiffs allege that Park Central is wholly owned by defendants, and is the managing member of O. Park, as well as T. Park. Park Central, in its capacity as managing member of T. Park, is authorized to dispose of T. Park's property in any manner, provided that such disposition "shall be done in conjunction with [T. Park's] primary purpose of offering Timeshare Units in the Timeshare Project in accordance with the [T. Park] Offering Plan" (T. Park operating agreement § 5.3 [d]). Park Central is also authorized "to borrow money for [T. Park] purposes and, if security is required therefor, to pledge, mortgage" T. Park's assets as collateral for such loans (*id.* § 5.3 [e]).

Plaintiffs allege that MFB became a T. Park member on January 1, 2006, when Furman and Birdoff assigned their combined 10% membership interest in T. Park to MFB, pursuant to an agreement entitled Assignment and Assumption of Limited Liability Company Interests [T. Park Central L.L.C.] Agreement (the Assignment Agreement"). Furman executed the assignment agreement in his capacity as manager of MFB.

Plaintiffs claim that Furman, as an individual, retained the right under the T. Park operating agreement to select an accountant for T. Park, even after transferring his interest in T. Park to MFB, and exercised that right years later, by letter dated July 16, 2014. In the July, 16, 2014 letter, Furman requested that T. Park appoint nonparty Berdon LLC ("Berdon") as its accountants. Plaintiffs further claim that the Estate now holds the authority to enforce that right.

Prior to the execution of the Assignment Agreement, by consent letter dated December 19, 2005, the Eichners consented to "any transfer by either or both of you of any of your direct or indirect interests in [T. Park] to MFB." Plaintiffs allege that such consent by the Eichners, who hold a combined 88% membership interest in T. Park, constitutes consent to a transfer of the membership interests of Furman and Birdoff, and that, as a result, MFB became a full T. Park member, in accordance with the terms of the T. Park operating agreement.

Plaintiffs claim that defendants improperly acted against the best interests of T. Park by obtaining tens of millions of dollars in loans, largely secured by T. Park's assets, resulting in a significant decrease in T. Park's sales between 2011 and 2013. Plaintiffs allege that defendants secured financing for the O. Park timeshare project by leveraging T. Park's assets, and used T. Park as a guarantor on O. Park's obligations. Plaintiffs also allege that, at the same time, defendants focused their efforts on developing O. Park, while allowing T. Park's sales to fall precipitously.

As a result, plaintiffs allege, while T. Park's operating expenses substantially remained the same, T. Park's interest expenses, intercompany lending, and receivables increased significantly. Plaintiffs further allege that, despite the drop in T. Park's sales, defendants, through their ownership of Park Central, have failed to adjust the allocated costs between T. Park and O. Park.

Plaintiffs also allege that defendants rejected Furman's demand to appoint Berdon, on the ground that Furman lost the right to appoint the corporate accountant when he transferred his interest in T. Park to MFB in 2006.

In the complaint, MFB sues individually and derivatively on behalf of T. Park, and Lipari sues as executor of the Estate. Plaintiffs assert causes of action for breach of fiduciary duty, reckless disregard of fiduciary duty, corporate self-dealing, corporate waste, diversion of corporate assets, interference with corporate opportunity, misappropriation of corporate assets, aiding and abetting breach of fiduciary duty, and breach of the T. Park operating agreement, and seek an accounting. On these claims, plaintiffs seek to recover at least \$1 million, together with interest, costs, and attorneys' fees.¹

Defendants now seek to dismiss the first through eighth causes of action and the tenth cause of action, first, on the ground that MFB lacks standing to bring this action derivatively on behalf of T. Park, a limited liability company (LLC), because MFB was never a member, but is merely a transferee, or, assignee, of membership interests in T. Park. In opposition, plaintiffs contend that MFB was a member of T. Park at the time

¹ With respect to the claims denominated as derivative, plaintiffs claim that a demand on Park Central, T. Park's managing member, would have been futile because Park Central, whom they accuse of significant wrongdoing, is exclusively controlled by the individual defendants, whom they also accuse of significant wrongdoing. Plaintiffs also allege that a demand would have been futile because Park Central has complete control over T. Park's business affairs, pursuant to the T. Park operating agreement, and because MFB is a minority member of T. Park. Plaintiffs further allege that, based on their past experience with defendants, a demand would have been futile.

that defendants allegedly committed the improper acts and at the time that this action was commenced.

As a threshold matter, I note that plaintiffs allege that they are suing both in their individual capacities as well as in MFB's alleged derivative capacity. However, a reading of the complaint demonstrates that the first through eighth and the tenth causes of action are solely derivative in nature. A derivative claim is a claim brought to vindicate a wrong inflicted upon the company, rather than a wrong inflicted on an individual shareholder or member. See *Glenn v Hoteltron Sys.*, 74 NY2d 386, 392 (1989). Any recovery under a derivative claim inures directly to the company, and the individual members share in that recover only indirectly, to the extent of their ownership interests in the company. *Id.* Allegations of misuse of corporate assets, usurpation of corporate opportunities, waste, and similar claims belong to the corporation, and must be brought derivatively, on the corporation's behalf. *Abrams v Donati*, 66 NY2d 951, 953 (1985); *Serino v Lipper*, 123 AD3d 34, 39-40 (1st Dep't 2014).

Plaintiffs assert claims for breach of fiduciary duty by misuse of T. Park's assets, reckless disregard of fiduciary duty, corporate self-dealing, corporate waste, diversion of corporate assets, interference with corporate opportunity, misappropriation of corporate assets, and aiding and abetting breach of fiduciary duty, and they seek an accounting from T. Park's inception in 1996 through the present. Those claims belong solely to T. Park, and not to MFB, and, therefore, are derivative in nature.

Only a member of an LLC at the time of the alleged wrong to the LLC has standing to bring a derivative claim on behalf of that company. *See Cordts-Auth v. Crunk, LLC*, 815 F. Supp 2d 778, 786-787(SD NY 2011) (citing New York law), *affd* 479 Fed Appx 375(2d Cir 2012). Further, both applicable law and the T. Park operating agreement draw a bright line distinction between members of an LLC and the assignees of membership interests.

The New York Limited Liability Company Law provides, in relevant part, that "[e]xcept as provided in the operating agreement . . . an assignment of a membership interest does not . . . entitle the assignee to participate in the management and affairs of the limited liability company or to become or to exercise any rights or powers of a member." Limited Liability Company Law § 603 (a) (2). That section further provides that "the only effect of an assignment of a membership interest is to entitle the assignee to receive, to the extent assigned, the distributions and allocations of profits and losses to which the assignor would be entitled." Limited Liability Company Law § 603 (a) (3).

The Limited Liability Company Law accords the members of an LLC the right to choose their fellow members, and provides that, "[e]xcept as provided in the operating agreement, an assignee of a membership interest may not become a member without the vote or written consent of at least a majority in interest of the members, other than the member who assigned or proposes to assign such membership interest." Limited Liability Company Law § 604 (a).

In addition, the T. Park operating agreement imposes certain restrictions on the transfer of membership interests, and distinguishes between assignees, or, transferees or permitted transferees, who hold only economic rights, and substituted members, who hold full rights under that agreement and applicable law. *See* T. Park operating agreement §§ 7.1, 7.2. The T. Park operating agreement provides that no member may transfer an interest without the prior written consent of members owning 95% of the T. Park membership interests. *Id.* § 7.1. The T. Park operating agreement additionally provides that, "[n]otwithstanding anything contained in this Agreement to the contrary, no Permitted Transferee or any other transferee shall become a Member without the written consent of Members owning . . . 95% . . . of the Membership Interests, which may be arbitrarily withheld." *Id.* § 7.2.

Thus, under the T. Park operating agreement two steps are required to obtain T. Park member status. First, a T. Park interest may be transferred only with the prior written consent of members owning at least 95% of the membership interests in T. Park. Second, member status in T. Park may be transferred only with the written consent of members owning at least 95% of T. Park's membership interests.

The documentary record submitted demonstrates that, while MFB obtained the necessary consent to become a transferee under section 7.1 of the T. Park operating agreement, it never obtained the written consent required to become a substituted member under section 7.2 of that agreement. In the December 19, 2005 consent letter, the Eichners, who together hold an 88% membership interest, consented to "any" transfer

of T. Park interests by Furman or Birdoff, who together hold a 10% interest.

Significantly, however, the consent letter is completely devoid of any express (or implied) reference to the transfer of a membership interest in T. Park, and nothing in that letter may be interpreted as a consent to the transfer of membership.

Defendants' contention that MFB became a permitted transferee and holds member status because its members are lineal descendants is irrelevant. A lineal descendant is defined by the T. Park operating agreement as a descendant of the parents of the T. Park members and the spouses of such descendants. *See* T. Park operating agreement § 1.1. Whether or not MFB's members qualify as lineal descendants, prior written consent to the transfer of member status by members owning at least a 95% membership interest in T. Park is nevertheless required to confer member status on any entity or natural person *Id.* § 7.2.

Because it has failed to show that 95% of the members of T. Park gave written consent to MFB becoming a substituted member of T. Park, MFB lacks standing to sue on T. Park's behalf. Therefore, that branch of the motion to dismiss the first through eighth causes of action and the tenth cause of action, MFB's derivative claims, is granted, and those claims are dismissed without prejudice, on the ground that MFB lacks standing. *See* CPLR 3211 (a) (3).

Defendants next seek to dismiss the ninth cause of action, in which plaintiffs allege that defendants breached section 5.5 of the T. Park operating agreement by refusing to replace T. Park's accountant with the accountant designated by Furman in his

July 29, 2014 letter. Defendants contend that the claim is fatally defective on the ground that, when Furman assigned his interest in T. Park to MFB in 2006, he ceased to be a T. Park member, and lost any rights and powers that he might otherwise have been granted pursuant to the terms of the T. Park operating agreement.

In opposition, plaintiffs contend that Furman properly exercised his individual right on July 29, 2014, when he wrote to Ian Bruce Eichner, and demanded the appointment of Berdon as T. Park's accountant, effective immediately, that defendants' refusal to appoint Berdon was a breach of the T. Park operation agreement, and that the Estate is has the authority to enforce Furman's right.

When Furman transferred his interest in T. Park to MFB in 2006, he did not retain any rights he may otherwise have had under the T. Park operating agreement. "Except as provided in the operating agreement, . . . a member ceases to be a member and to have the power to exercise any rights or powers of a member upon assignment of all of his or her membership interest." Limited Liability Company Law § 603 (a) (4); *see Verderber v. Commander Enters. Centereach, LLC*, 85 AD3d 771, 772 (2d Dep't 2011).

The assignment agreement provides, in section 1, that: "[e]ach Assignor [Furman or Birdoff] hereby assigns and transfers to Assignee [MFB] all of each Assignor's interests . . . in T. Park . . . together with *all such Assignor's right, title and interest in and to [T. Park]* in respect of the Assigned Interest, including, without limitation, such Assignor's capital account therein, to have and to hold the same unto Assignee forever" (emphasis added).

Nothing in the assignment agreement, or any other relevant document, provides that Furman reserved any individual rights, such as the right to designate T. Park's accountant, when he assigned his rights and interests in T. Park to MFB in 2006.

To the extent that plaintiffs contend that the Estate holds the power to exercise Furman's individual rights granted by the T. Park operating agreement, that contention is without merit. The T. Park operating agreement provides, in relevant part, that, upon the death of a member, the member's executor becomes only a "Decedent's Transferee," with expressly limited economic rights (*see* T. Park operating agreement § 7.4). That agreement further provides that an executor, as a "Decedent's Transferee," may become a member only if all the T. Park members unanimously approve such admission, and the transferee executes such instruments as the managing member requires (*see id.*).

Thus, pursuant to the express terms of the assignment agreement, and in accordance with the applicable statutory law, Furman transferred all his rights, including the right to designate T. Park's accountant, and interests to MFB in 2006. Inasmuch as Furman's letter demanding the appointment of an accountant was written July 29, 2014, some eight years after Furman transferred the right to make such a demand, the demand was without effect.

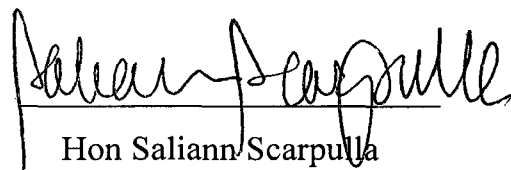
Therefore, the branch of the motion to dismiss the ninth cause of action is granted, and that claim is dismissed.

In accordance with the foregoing, it is

ORDERED that defendants' motion to dismiss the complaint is granted, and the complaint is dismissed in its entirety without prejudice as against all defendants, with costs and disbursements to defendants as taxed by the Clerk of the Court, and the Clerk is directed to enter judgment accordingly.

This constitutes the decision and order of the Court.

Dated: June 24, 2016

A handwritten signature in black ink, appearing to read "Hon Saliann Scarpulla", written over a horizontal line.

Hon Saliann Scarpulla

J.S.C.