SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY : CIVIL TERM : PART 54

DANIEL SHATZ, suing individually and derivatively on behalf of VAST VENTURES VI LLC,

Plaintiffs,

-against-

Index No. 655620/2018

DOUGLAS CHERTOK, VAST VENTURES LLC, VAST VENTURES V LP and VAST VENTURES GP LLC,

Defendants,

PROCEEDING

-and-

VAST VENTURES VI LLC,

Nominal Defendant.

June 18, 2019

60 Centre Street
New York, New York

B E F O R E:

HON. JENNIFER G. SCHECTER, Justice

A P P E A R A N C E S:

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Anne Marie Scribano
Senior Court Reporter

THE COURT: All right. Were you all here for the last argument?

I'm going to do this one differently. Meaning, I read all the licenses, I read all of your papers thoroughly, I want to cut straight to the chase here.

Having looked at the 19 -- 19? -- causes of action, there's going to be some good news and bad news for everybody.

After taking a close look at the LLC agreement for Vast Ventures VI, accompanied by reading the complaint, there is no basis to dismiss a breach of fiduciary duty claim as against Chertok and Vast Ventures LLC, the managing member of Vast Ventures VI LLC, which I'll just refer to as Vast Ventures VI.

Looking at the Vast Ventures VI LLC agreement, in particular section 1.4, it sets forth that:

"The purpose of the LLC is to carry on any business approved by the LLC in accordance hereof and consistent with the Act of any other business or activity related thereto or arising therefrom and to carry on anything incidental, convenient or necessary to the foregoing."

The following sentence is:

"Specifically, the LLC's objective shall be to identify and invest in private equity funds whose primary focus is to invest in technology companies. The LLC may invest in as many such private equity funds as the managing member elects in its sole and absolute discretion; provided, however, that no investments shall be made in funds or other accounts in which the managing member has an ownership interest outside of the LLC."

And the section goes on.

I do not find that this section unambiguously prohibits the nature of the investment in Ripple. Meaning just because it specifies that the objective shall be to identify and invest in private equity funds, that's not to the exclusion of other technology-related investments.

And the fact is, I have to give the complaint every benefit of the doubt in this motion to dismiss at the pleading stage.

And in the pleading it sets forth -- and I have to accept the factual allegations as true -- in paragraph E that:

"In August of 2013, Chertok notified Shatz by e-mail that, as they had discussed earlier" -- and this is a purported quote of the e-mail -- "per Article 3 of the Vast VI operating agreement, Vast Ventures VI LLC is making a capital call of $75,000 for an investment in OpenCoin Inc."

It's one word, OpenCoin, Inc., which is Ripple.

So that certainly is indicative of a reading of the section that would be consistent with the investment.

Now, in addition, my problem here in terms of breach of fiduciary duty is the allegation of an actual misrepresentation here of the opportunity. Meaning the $75,000 check, I believe, according to the complaint, was ultimately returned with the representation made that the investment wasn't possible. Whether it was or wasn't at that particular time, I don't necessarily know. But we have allegations here as well that Mr. Shatz continued to inquire about the possibility of the investment and was told -- and the allegation is that it was inaccurate -- that the investment was not a possibility due to Ripple not seeking investors.

Based on those allegations, I find that the complaint is sufficient in terms of establishing the potential breach of fiduciary duty and conduct not in good faith in terms of the opportunity.

There is no case law here that establishes for me definitively that this was not of a nature of a corporate opportunity or a potential. Meaning having explicitly been offered to Shatz as part of -- as an opportunity for Vast Ventures VI.

That said, the individual claims do not survive. Meaning everything here, to the extent that there was a breach of fiduciary duty, the duty was owed to Vast Ventures VI, not to Shatz individually in any capacity.

Moreover, the other claims -- and the other claims being 18 -- the other claims are all either dismissed as improperly seeking individual recovery or duplicative of the breach of fiduciary duty claim.

And to the extent that there is any aiding and abetting allegations or allegations as to Vast Ventures V, or Vast Ventures GP LLC, which I think was the general partner of Vast Ventures V, there is no allegation that any of those entities did anything distinct from what Chertok did. Meaning Chertok, again, is going to remain as a defendant for breach of fiduciary duty, but there is nothing independent that would allow for liability as to the other entities distinct from Chertok.

So on that basis, the complaint will proceed as to breach of fiduciary duty, a derivative claim.

And I understand that you have a discovery conference today, is that correct, preliminary confluence?

MR. WEINBERGER: Yes, that's correct.

MR. BOWMAN: That's correct, your Honor.

THE COURT: All right. Very good. So we'll give you a few moments and Mr. Rand will proceed with your conference.

MR. WEINBERGER: May I ask one question, your Honor?

THE COURT: Yes, you can.

And before I forget, the movant is to e-file a copy of the transcript within 45 days.

MR. WEINBERGER: On the individual claims, does that include the failure to disclose material information?

THE COURT: It does. Because there is only a duty here to Vast Ventures VI, the fiduciary duty. There was no individual duty that would run from -- that would run directly to Shatz individually.

In addition -- I'm sorry -- was that Mr. Weinberger who asked the question?

MR. WEINBERGER: Yes.

THE COURT: Mr. Weinberger, to be clear, too, looking at the nature of the agreement here, the Vast Ventures VI agreement. Meaning the investments were to be made -- well, the managing -- the only entity that had the power to make the investments was the managing member and that was Vast Ventures LLC. So to the extent that there would have been any disclosure, Shatz really couldn't have done or wouldn't have done anything individually on that basis in any event.

So, again, based on the LLC agreement here, the only claim that survives is the derivative claim for breach of fiduciary duty.

MR. BOWMAN: Your Honor, it's Philip Bowman.

I know that you've read our briefs and have considered this carefully, but I wanted to know if I could just respond to a couple of things that you said.

THE COURT: Go right ahead.

MR. BOWMAN: Okay. First, your Honor, we absolutely agree that the LLC agreement permitted the investment in Ripple as a technical matter. And to the extent that argument was misinterpreted, I think the other side tried to say that we were arguing that it couldn't make an investment in Ripple. Of course we agree that it could.

And you mentioned Section 1.4 of the operating agreement, but you didn't mention --

THE COURT: 4.1?

MR. BOWMAN: 4.1.

THE COURT: Okay.

MR. BOWMAN: So I just wanted to draw the Court's attention to that provision if your Honor has it in front of you.

THE COURT: I do. I have it highlighted, in fact.

And, in fact, I was aware of that section in the followup that I did to Mr. Weinberger's question, yes. Meaning I appreciate that the managing member has the sole and exclusive control of the management. However, once the investment opportunity was presented to Vast Ventures VI and then there was, according to the complaint, inaccurate information about the possibility of that investment, despite inquiries, there still is an issue in terms of breach of fiduciary duty.

To the extent, by the way, that there may be causation issues in terms of damages, that will have to be addressed down the pike.

But there is enough in the complaint for the claim for breach of fiduciary duty.

MR. BOWMAN: And the point about the sole and exclusive control as it relates to this claim and the reason why we believe it precludes the claim is because, essentially, Mr. Shatz' claim is that he had a voice or some role in making a decision about what investments could be made. That has to be his claim. In other words, he's saying "I wanted to invest in Ripple and, therefore, the company should have invested in Ripple." But what 4.1 says is that only Mr. Chertok and Vast Ventures get to decide what the company does. Mr. Shatz could never have chosen to invest in Ripple. It wasn't his decision. And, you know, it's sort of been, you know, twisted and contorted a little bit, but essentially that's what he's claiming. He's saying "I want a role. I want a decision-making role with respect to the investments the company made." He never had that.

THE COURT: It's interesting because I read it as "A decision was made. There was a capital call. I put in the money." And, yes, you know, Chertok said it's not going to work right now. And, again, he said it's not going to work right now. Shatz then follows up "When is it going to work? When is it going to work?"

And, allegedly, yes, misleading information -- it never -- this is not what Vast Ventures did, is going to do, because the Vast Ventures LLC or Chertok has made the determination that it is not going to invest. But it presented the opportunity, did the capital call, gave misleading information and, you know, the next thing Vast Ventures knows is that Chertok did invest in the venture without any disclosure, without saying -- you know, and the allegations are that Chertok kept saying or not denying or not discussing that the opportunity was unavailable, meaning stringing along Shatz or providing misleading information.

And again, under -- as alleged, that's sufficient for breach of fiduciary duty.

MR. BOWMAN: And then, your Honor, the other point that I didn't hear you address explicitly is the separate argument that's not based on the contract, which is that the complaint simply doesn't allege a diversion of a corporate opportunity.

In particular, there's really three prongs to that claim, right? The first is that there is an opportunity that belongs to the corporation. The second is that it be diverted. And the third, that it be for the benefit of the defendant.

With respect to the first prong, the complaint does not properly allege that that opportunity belongs to Vast VI as opposed to any of the other Vast entities that Mr. Chertok controlled. In other words, it was an investment idea. In fact, Vast V was already an investor in Ripple. Mr. Chertok was on the board of Ripple by virtue of that investment. How can it be that the invest -- that that opportunity, such as it is an opportunity -- and we've argued in our briefs that it's not an opportunity at all, it's just an investment idea -- but how could that belong to Vast VI as opposed to Vast V? What about the dozens of other investors that Mr. Chertok had who might also very much want to invest in Ripple? How does it become Mr. Shatz's investment because they had a conversation about it?

THE COURT: I don't know -- well, I think it went further than just a conversation. Meaning there was a capital call for this very purpose. And then, again, I don't know whether it was misinformation at the time in terms of ability to invest in Ripple at that time. I don't know.

But the point is, I don't know if Mr. Chertok presented the same opportunity to other LLCs or to other individuals to whom he had a fiduciary duty or with whom he had this relationship.

MR. BOWMAN: And, in a sense, your Honor, that brings me to my next point, which is the question of diversion. The complaint doesn't allege adequately that the opportunity was actually diverted; i.e. taken from the company and given to some other company or entity. That would have to have happened for there to be a diversion.

In other words, just failing to cause Vast VI to invest in Ripple -- let's assume for a moment that there was an agreement or there was -- some sort of some state of affairs had arisen whereby Vast VI had some expectation that that would happen. Simply not investing in Vast VI wouldn't be -- in Ripple wouldn't be a diversion, it would just simply be failing to invest. And there's no claim for failing to invest. Shatz would have to show that he took that opportunity, took it away from Vast VI and gave it to someone else. And he never did that. There's no allegation that he did that, let along for his own benefit.

THE COURT: There is an allegation that he denied Vast Ventures VI the opportunity and then went ahead and invested in it himself or for other entities that he is affiliated with.

MR. BOWMAN: Certainly not for himself.

And, in fact, Vast Ventures VI was 50 percent owned by him, so he took the opportunity away from himself and --

at best, at the best reading of the complaint -- and presented it to another investment entity, as to which there's no allegation that he had a greater or equal interest.

There's nothing in the complaint from which one could draw the conclusion that Mr. Chertok benefited from this, other than the conclusory statement that it was for his benefit.

THE COURT: Well, he denied the benefit to Vast Ventures VI and then his entity took advantage of that same venture or that same opportunity, I should say, in terms of investing in Ripple.

Which, again, my reading of the complaint is that that's sufficient to invoke the corporate opportunity doctrine and allege a breach of fiduciary duty.

Is there anything else you wanted to add?

MR. BOWMAN: No, thank you, your Honor.

THE COURT: Thank you very much.

Go ahead with your PC.

Don't forget to e-file the transcript.

MR. WEINBERGER: Sorry? We should file the transcript?

THE COURT: The movant.

Have a great day.

MR. BOWMAN: Thank you, your Honor.

MR. WEINBERGER: Thank you.

(Proceedings adjourned)

Certified to be a true and accurate transcript of the foregoing proceedings

Anne Marie Scribano

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