SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

DEBORA WARNER,	
Plaintiff,	Index No.: 654714/2018
-against-	
WILLIAM HEATH, DAVID KUZMANICH, KIM TABET, ROBERT NUELL, DAVID ROBINSON,	
Defendants.	

MEMORANDUM OF LAW IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS PLAINTIFF'S SECOND AMENDED COMPLAINT

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Defendants William Heath, David Kuzmanich, Kim Tabet, Robert Nuell, David Robinson (collectively, "Defendants"), by and through their undersigned counsel, respectfully submit this memorandum of law in support of their motion to dismiss the Second Amended Complaint pursuant to CPLR 3211(a)(1), (3), and (7). Accompanying this Memorandum of Law is the Affirmation of Marc A. Lebowitz, Esq., dated March 29, 2019 (the "Lebowitz Aff.") and the Affidavit of William Heath, sworn to March 28, 2019 (the "Heath Aff.").[1]

PRELIMINARY STATEMENT

This is now the fourth, flawed pleading in this matter. The Court provided Plaintiff with a roadmap to remedy the conflation of direct and derivative claims which marked her first amended complaint ("First Amended Complaint"), as well as extensive time to replead these claims. Plaintiff has elected to recast all of her claims as direct claims, regardless of the substance of those claims, or whether they are, in fact, direct or derivative in nature.

Thus, the Second Amended Complaint ("SAC") asserts a repetitive, hodge-podge of "group pled" allegations, all asserted on a direct and individual basis only against the Defendants. Even though most of the allegations assert injuries to a corporate entity, rather than the Plaintiff, and as such must be brought as derivative claims, if at all. The SAC also suffers from other pleading infirmities throughout, including a lack of required particularity for claims

[1] For the convenience of the Court, a copy of the SAC is attached to the accompanying Affirmation of Marc A. Lebowitz ("Lebowitz Aff.") as Exhibit A. References to the SAC herein are in the form of "SAC ¶ __."

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sounding in fraud, duplication of other claims, including claims for breach of contract, and an overarching failure to meet even the most basic of pleading standards despite the voluminous nature of the allegations.

For these reasons, as set forth below, Plaintiff's SAC should be dismissed in its entirety.

STATEMENT OF FACTS

A full description here of the factual allegations pled within Plaintiff's 63-page, 326 paragraph SAC would be lengthy and, because of the prolix and contradictory nature of the allegations, not easily summarized. Instead, specific allegations pulled from the SAC, as they relate to Plaintiff's twelve causes of action and this motion to dismiss, are set forth at length within the argument section below. Additionally, documentary evidence that "fact checks" and definitively contradicts certain allegations within the SAC are included within, and annexed to, the Heath Affidavit.

I.

ARGUMENT

A. General

1. Standards for Motion to Dismiss

Dismissal pursuant to CPLR 3211(a)(1) is warranted where "documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law." Leon v Martinez, 84 N.Y.2d 83, 88 (1994). Moreover, when the moving party "offers matter extrinsic to the pleading the court need not assume the truthfulness of the pleaded allegations, the criterion to be applied in such a case

being whether the opposing party actually has a cause of action or defense, not whether he has properly stated one." O'Donnell, Fox & Garter, P.C. v R-2000 Corporation, 198 A.D.2d 154 (1st Dep't 1993).

Although for purposes of a motion to dismiss pursuant to CPLR 3211(a)(7), a Court must accept as true the well-pleaded allegations within a complaint, a Plaintiff must still allege all the material elements of a cause of action. See CPLR § 3013; see also East Hampton Union Free School Dist. v. Sandpebble Builders, Inc., 66 A.D.3d 122, 125 (2d Dep't 2009). Indeed, a court is not required to accept factual allegations "that do not state a viable cause of action that consist of bare legal conclusions, or that are inherently incredible or clearly contradicted by documentary evidence." Skillgames LLC v. Brody, 1 A.D.3d 247, 250 (1st Dep't 2003); see also Kamhi v. Tay, 244 A.D.2d 266, 266 (1st Dep't 1997) ("A complaint, replete with legal conclusions and devoid of factual allegations of the underlying wrongful conduct is not entitled to the benefit of favorable inferences usually accorded on a pre-answer motion to dismiss.") Where, as here, Plaintiffs fail to allege material elements of a claim, the allegation should be dismissed.

2. Warner Continues to Conflate Individual and Derivative Claims

Warner has mistakenly plead derivative claims as individual claims. Warner lacks standing to assert these derivative claims because to the extent these claims even exist, they belong to MHRC, and not to Warner individually.

Under New York law, members of a limited liability company have

no greater rights to present claims belonging to the limited liability company than do shareholders to present claims belonging to a corporation. Tzolis v. Wolff, 10 N.Y.3d 100 (2008). In determining whether a claim is direct or derivative, the First Department adopted the test developed by the Supreme Court of Delaware. See Yudell v. Gilbert, 99 A.D.3d 108, 114 (1st Dep't 2012) (citing Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031, 1039 (Del. 2004). Pursuant to the Tooley Test, a court must consider (1) who suffered the alleged harm and (2) who would receive the benefit of any recovery or other remedy. Id. In New York, "[a] complaint the allegations of which confuse a shareholder's derivative and individual rights will ... be dismissed." Yudell v. Gilbert, 99 A.D.3d 108, 115 (1st Dep't 2012) (citing Abrams v. Donati, 66 N.Y.2d 951, 953 (1985)).

Applying these principles here, the Court should dismiss Warner's purportedly direct Claims II, III, VI, VII, and X for lack of standing both because (1) her claimed injuries flow from alleged breaches of duties that Defendants owed to MHRC, not Warner individually; and (2) the SAC makes clear that Warner could not prevail on any of these claims without first showing an injury to MHRC (and then her recovery, derivatively, as a member).

3. The Business Judgment Rule Warrants Dismissal of the Complaint

Even apart from Warner's infirmities in pleading, the Defendant Board Members decision to decline an acquisition offer, as discussed in more detail below, may not be challenged or second-guessed by Warner.

Under New York law, the business judgment rule shields the duly

designated Managers' business judgments from judicial second-guessing where the Managers have exercised their business judgment within the scope of their authority, in the interests of the Company, and in good faith. See Levandusky v. One Fifth Ave. Apt. Corp., 75 N.Y.2d 530, 537-38 (1990); see also Kassover v. Prism Venture Partners, LLC, 53 A.D.3d 444, 450 (1st Dep't 2008) (challenge to decision dismissed under business judgment rule where decision was authorized). At the pleading stage, it is Plaintiff's burden to plead facts sufficient to overcome the deference to be accorded to the Managers' business judgment. See, e.g., Jones v. Surrey Coop. Apts., Inc., 263 A.D.2d 33, 36 (1st Dep't 1999).

Warner has not done so. Nowhere in the SAC does Warner even allege that the Managers acted outside the scope of their authority in determining to turn down an offer of acquisition and continue to develop MHRC rather than sell it. The gravamen of this action is that the decision not to sell to Xpo was such a bad decision that MHRC should be dissolved. This case is nothing more than an improper attempt to prevent MHRC from pursuing its chosen path. Warner is working at a competitor who unsuccessfully tried to buy MHRC, and working with that competitor to prevent MHRC from raising funds and pursuing its chosen path of organic growth through investment. Xpo has inserted itself into every stage of the process, has been party to confidential settlement communications, and has been gathering MHRC's financial information while propping up Warner's lawsuit and crippling MHRC.

B. Warner's Claim For Judicial Dissolution Should Be Dismissed (Count I)

Section 702 of the New York Limited Liability Company Law ("LLCL") provides that:

> On application by or for a member, the supreme court in the judicial district in which the office of the limited liability company is located may decree dissolution of a limited liability company whenever it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement

New York courts have interpreted this standard to mean that for judicial dissolution of an LLC, a petitioner must "establish, in the context of the terms of the operating agreement or articles of incorporation, that (1) the management of the entity is unable or unwilling to reasonably permit or promote the stated purpose of the entity to be realized or achieved, or (2) continuing the entity is financially unfeasible." 1545 Ocean Ave., LLC, 72 A.D.3d 121, 131 (2nd Dep't 2010); Barone v. Sowers, 128 A.D.3d 484, 484-85 (1st Dep't 2015). Warner does not properly plead either of these criteria here and has failed to provide this Court with the requisite showing to be afforded such the "drastic remedy" of dissolution. 1545 Ocean Ave., 72 A.D.3d at 131.

First, Warner alleges that dissolution is appropriate because "she has been completely excluded from the business and improperly removed from the Board of Managers without cause, it is no longer possible to carry on the business of (sic) as contemplated by the OA." SAC ¶ 139. This allegation is unrelated to a dissolution claim. Rather it supports a claim for breach of the Operating Agreement, unrelated to the dissolution standard. See Section I(A)(2), *Supra*.

On point is Doyle v. Icon LLC, 103 A.D. 3d 440 (1st Dep't 2013), wherein, the First Department reversed the Supreme Court's grant of dissolution under LLCL § 702, stating:

> Plaintiff's allegations that he has been systematically excluded from the operation and affairs of the company by defendants are insufficient to establish that it is no longer 'reasonably practicable' for the company to carry on its business as required under LLCL § 702. The allegations do not show that "the management of the entity is unable or unwilling to reasonably permit or promote the stated purpose of the entity to be realized or achieved, or that continuing the entity is financially unfeasible"

Warner's allegations, that she was removed from the Board or excluded from the operation and affairs of MHRC, are unrelated to the standard and do no go to whether it is no longer "reasonably practicable" to carry on its business or that the current managers of MHRC are unable to permit or promote the stated purpose of MHRC to be realized or achieved.

MHRC continues to own and operate indoor treadmill studios and has opened a third studio during the pendency of this litigation. This is consistent with the purpose for which MHRC was established--i.e. "to engage in any activity for which limited liability companies may be organized in the State of New York" Operating Agreement § 1(f).

Next, Warner alleges - in sum - that MHRC "was established to develop and operate running studios and distribute profits to its members" and; "[t]hat purpose is no longer practicable because Mile High is currently insolvent" and "has no prospect of recovery because its business has lost revenue year-over-year and it is currently operating at 95% cost as a percent of its monthly sales." SAC ¶ 144-45. As previously established and contrary to Warner's allegations

above, the express purpose of MHRC is "to engage in any activity for which limited liability companies may be organized in the State of New York" (Operating Agreement § 1(f)).

The Operating Agreement includes a section providing for "Distributions," however distributing profits on Warner's schedule is not the "purpose" of MHRC and if she believes the "Distributions" section is being breached that would be a different claim. Notably, a Court "will not dissolve an LLC merely because the LLC has not experienced a smooth glide to profitability or because events have not turned out exactly as the LLC's owners originally envisioned; such events are, of course, common in the risk laden process of birthing new entities in the hope that they will become mature, profitable ventures". A "hair-trigger dissolution standard" would "thwart the expectations of reasonable investors..." 1545 Ocean Ave, 72 A.D. 3d at 130-131 (quoting Matter of Arrow Inv. Advisors, LLC, 2009 WL 1101682, at *2 (Del. Ch. 2009).

Finally, to the extent Warner is claiming that Defendants' alleged breaches of fiduciary duty somehow warrant dissolution (SAC §§ 148 - 156), the remedy for such conduct is not found in LLCL § 411. See 1545 Ocean Ave, 72 A.D. 3d at 132 (holding that a fair reading of LLCL § 702 demonstrates an application to dissolve an entity does not flow from a claim under LLCL § 411); see also Widewaters Herkimer Company, LLC v. Aiello, 28 A.D.3d 1107, 1108 (4th Dep't 2006) ("In alleging that the majority members breached their fiduciary duty to defendants and engaged in unlawful or oppressive conduct toward them, defendants 'did not plead the requisite grounds for dissolution of a

limited liability company'") quoting Artigas v. Renewals Arts Realty Corp. 22 A.D.3d 327 (1st Dep't 2005), citing LLCL § 702.

In sum, the SAC falls short of supporting a judicial dissolution claim and Warner's first cause of action should be dismissed.

C. Warner's Claim For Breach of Fiduciary Duty Should Be Dismissed (Count II)

To state a breach of fiduciary duty claim, a plaintiff must allege that (i) defendants owed a fiduciary duty, (ii) defendants committed misconduct, and (iii) damages were caused by that misconduct. Burry v. Madison Park Owner LLC, 84 A.D.3d 699, 699-700 (1st Dep't 2011).

Here, Warner's cause of action for breach of fiduciary duty requires dismissal because this claim: (i) improperly seeks derivative relief; (ii) is not plead with the requisite particularity; and (iii) impermissibly duplicates Warner's claims for breach of contract

1. Warner's Breach of Fiduciary Duty Claim Improperly Seeks Derivative Relief for Warner Individually

Those allegations Warner purports to plead as a direct claim for breach of fiduciary duty (e.g., stripping the value of her equity (SAC ¶¶ 165, 184); self-dealing and damages to Mile High's finances and reputation (SAC ¶¶ 170-172); failure of Defendants to evaluate an offer (SAC ¶¶ 173-177, ¶¶ 178-180, ¶ 188) are all classic derivative claims which assert harm to MHRC; not Warner. See Section I(A)(2), *Supra*.

The Court need look no further to dismiss this improperly pled individual claim. However, this breach of fiduciary duty claim is deficient in other material respects worth addressing.

2. The Breach of Fiduciary Claim is also not Plead with Required Particularity

Under New York law, breach of fiduciary duty claims must be pleaded with particularity. CPLR 3016(b). This requires that the "the circumstances constituting the wrong shall be stated in detail." CPLR 3016(b); see also Berardi v. Berardi, 108 A.D.3d 406, 406-07 (1st Dep't 2013). "[I]n order to survive a motion to dismiss under CPLR 3211, each element of a cause of action for breach of fiduciary duty must be supported by particularized factual allegations, as opposed to mere legal or factual conclusions." Singh v. PGA Tour, Inc., 42 Misc. 3d 1225(A) (Table), 2014 WL 641311, at *6-7 (Sup. Ct. N.Y. Cnty. 2014). In particular, "when a cause of action is pled against multiple defendants, the plaintiff must make factual allegations as to the time frame and particular acts attributable to each defendant." Epic Sports International, Inc. v. Frost, 2013 WL 705527, at *7 (Sup. Ct. N.Y. Cnty. Feb. 21, 2013) (dismissing breach of fiduciary duty claim for failing to meet this heightened standard).

The SAC falls far short of this standard, impermissibly employing group pleading to allege a stream of alleged "bad acts" indiscriminately against all Defendants. See e.g., SAC ¶ 164 and the nearly identical type of group pleading employed to allege a nearly identical stream of allegations against Defendants under the heading "Co-Founding Member Defendants Collectively" (SAC ¶¶ 182-183).

3. Warner's Breach of Fiduciary Duty Claim Impermissibly Duplicate Warner's Breach of Contract Claims

Warner has also failed to allege that each Defendant is in breach of a separate and independent "fiduciary" duty to her - i.e., sounding

in tort - instead she predicates her fiduciary claims on allegations going to a breach of the Operating Agreement.

Warner cannot recast claims sounding in breach of contract as a tort claim for breach of fiduciary duty. See, e.g., LaSalle Hotel Lessee, Inc. v. Marriott Hotel Servs., Inc., 29 A.D.3d 464, 465 (1st Dep't 2006) (dismissing cause of action for breach of fiduciary duty "based on the same allegations as for breach of contract"); Kaminsky v. FSP Inc., 5 A.D.3d 251, 252 (1st Dep't 2004) (dismissing fiduciary claim for failure to distinguish between conduct constituting breach of contract and conduct constituting a breach of alleged fiduciary duty); and William Kaufman Org., Ltd. v. Graham & James LLP, 269 A.D.2d 171, 173 (1st Dep't 2000) (same).

Thus, Warner's breach of fiduciary duty claims which are predicated on the same set of operative facts covered by the Operating Agreement should be dismissed. And as discussed at the outset, any fiduciary duty claims that are not impermissible, would be derivative claims.

D. Warner's Claim for Aiding and Abetting Breach of Fiduciary Duty Should Be Dismissed (Count III)

First, this is a derivative claim, improperly brought individually by Warner. See Section I(A)(2), *Supra*.

Second, like Warner's breach of fiduciary duty claims, this claim must also be pleaded with particularity under CPLR 3016(b). Warner's claim for aiding and abetting fails because the SAC does not sufficiently allege an underlying breach of fiduciary duty. OFSI Fund II, LLC v. Canadian Imperial Bank of Commerce, 82 A.D.3d 537, 540 (1st

Dep't 2011) ("As there is no breach of fiduciary duty claim, there can be no claim for aiding and abetting breach of fiduciary duty."); Fiala v. Met. Life Ins. Co., 6 A.D.3d 320, 323 (1st Dep't 2004) (dismissing aiding and abetting claim where the underlying breach of fiduciary duty claim dismissed).

For the same reasons, Warner's aiding and abetting breach of fiduciary duty claim should be dismissed.

E. Warner's Claim for Rescission of the Operating Agreement Should be Dismissed (Count IV)

Warner's Fourth Cause of Action seeks rescission of the Operating Agreement and IP Agreement, however the allegations plead in support of this claim (e.g., "Defendants wrongfully induced Warner by false promises and representations to execute an IP Agreement and the Operating Agreement" (SAC ¶ 209); "Defendants also falsely represented that they would pay for their equity in Mile High, in addition to bringing in investors (SAC ¶ 212), etc.) are more appropriately described as a claim for fraudulent inducement.

To plead a cause of action for fraudulent inducement, plaintiff must allege with particularity a "representation of a material existing fact, falsity, scienter, deception and injury." New York Univ. v. Continental Ins. Co., 87 N.Y.2d 308, 318 (1995), quoting Channel Master Corp. v. Aluminum Ltd. Sales, Inc., 4 N.Y.2d 403, 407 (1958).

In cases, as here, of fraudulent misrepresentation alleged to have occurred in the context of contract discussions and/or performance, courts require that the plaintiff allege a misrepresentation of a "then-present fact, which would be extraneous

to the contract and involve a duty separate from or in addition to that imposed by the contract and not merely a misrepresented intent to perform." See Hawthorne Group, LLC v. RRE Ventures, 7 AD3d 320, 323-324 (1st Dep't 2004), citing Deerfield Communications Corp. v. Chesebrough-Ponds, 68 N.Y.2d 954 (1986).

1. Warner's Fraudulent Inducement Allegations Are Not Plead With the Specificity Required By CPLR 3016(b)

CPLR 3016(b) provides that where a cause of action is based on fraud or misrepresentation, "the circumstances constituting the wrong must be set forth in detail." Dragon Investment Co. II LLC v. Shanahan, 49 A.D.3d 403 (1st Dep't 2008); Fink v. Citizens Bank Mortgage Ltd., 148 A.D.2d 578, 578 (2d Dep't 1989) ("plaintiff must allege each of the elements of fraud with particularity and must support each element with an allegation of fact").

2. Warner's Fraudulent Inducement Claim Does Not Plead Scienter

Warner's fraudulent inducement allegations are fatally deficient under CPLR § 3016(b) because they are not supported by "facts with sufficient specificity to permit an inference of fraudulent intent." Stuart Lipsky, P.C. v. Price, 215 A.D.2d 102, 104 (1st Dep't 1995).

Warner must allege facts demonstrating that each of the Defendants made false statements knowingly or recklessly and, further, that the misrepresentations were made with the intent to deceive. Zaref v. Berk & Michaels, 192 A.D.2d 346, 348 (1st Dep't 1993). The SAC must, at a minimum, state concrete facts from which scienter may be inferred. Giant Group, Ltd. v. Arthur Andersen, LLP, 2 A.D.3d 189, 190 (1st Dep't 2003).

Here, Warner's fraudulent inducement claim fails to plead sufficient factual detail to demonstrate that any one of the Defendants made representations with the intent to deceive. In order to show an intent to deceive, Warner "must [plead facts] that defendant knew, at the time they were made, that the representations were false." Abrahami v. UPC Const. Co., 224 A.D.2d 231, 233 (1st Dep't 1996). Instead, Warner's SAC merely asserts the conclusory allegation that "Defendants wrongfully induce Warner by false promises and representations to execute an IP Agreement and the [Operating Agreement"] (SAC ¶ 209); the "Defendants also falsely represented that they would pay for their equity in Mile High, in addition to bringing in investors" (SAC ¶ 212); and "using false representations and the pretense that they were there to help her" (SAC ¶ 214)

These bare legal conclusions of intent do not meet CPLR § 3016(b) because Warner provides no rational explanation, supported by facts, for why Defendants would bear any intent to deceive. See Zanett Lombardier, Ltd. v. Maslow, 29 A.D.3d 495, 495-96 (1st Dep't 2006) (holding that "conclusory statement of intent did not adequately plead sufficient details of scienter").

3. Warner's Fraudulent Inducement Claim Fails to Specify Which Defendant Made What Alleged Misrepresentation

Warner's fraudulent inducement allegations make virtually no attempt to distinguish among the Defendants; instead, the SAC lumps them together by making allegations against "Co-Founding Member Defendants" (SAC ¶¶ 210-214).

Under New York law, this sort of group pleading is inadequate to state a fraud claim because each defendant has not been put on notice

of which of the alleged misrepresentations is attributable to him or her. See Raytheon Co. v. AES Red Oak, LLC, 37 A.D.3d 364, 365 (1st Dep't 2007) (dismissing claim of fraudulent misrepresentation that "did not particularize when or by whom it had been made"). Neither particularity nor scienter can exist with such generalized group pleading.

4. Defendants' Contractual Promises Are Not Actionable as Fraud

"A failure to perform promises of future acts is merely a breach of contract to be enforced by an action on the contract. A cause of action for fraud does not arise when the only fraud charged relates to a breach of contract." Tesoro Petroleum Corp. v. Holborn Oil Co. Ltd., 108 A.D.2d 607, 607 (1st Dep't 1985). Warner and the Defendants' respective rights and obligations are set forth in the Operating Agreement. Because these alleged fraudulent acts are merely alleged failures to carry out contractual promises, they cannot sustain a fraud claim.

F. Warner's Claim for Rescission of the Contribution Agreement Must be Dismissed (Count V)

Warner's Fifth Cause of Action seeks to rescind a contribution agreement she entered into with Mile High on August 31, 2017. For this claim, Warner simply alleges that "[she] was fraudulently induced by the Co-Founding Member Defendants into signing a Contribution Agreement…" (SAC ¶ 219).

As an initial matter, under New York law, a rescission "is to be invoked only when there is lacking complete and adequate remedy at law and where the status quo may be substantially restored." Sokolow,

Dunaud, Mercadier & Carreras v. Lacher, 299 A.D.2d 64, 71 (2002), quoting Rudman v. Cowles Communications, 30 N.Y.2d 1, 13 (1972). In this case, Plaintiff cannot and has not made any indication that a complete and adequate remedy at law is unavailable to her for her claims against Defendants. Furthermore, years later, after millions in invested an operating the business based on this contribution agreement the status quo manifestly cannot be restored with a rescission.

This allegation also fails to assert a claim for fraudulent inducement, plead with particularity. Fink v. Citizens Bank Mortgage Ltd., 148 A.D.2d 578, 578 (2d Dep't 1989) ("plaintiff must allege each of the elements of fraud with particularity and must support each element with an allegation of fact").

Accordingly, Warner's rescission claim should be dismissed.

G. Warner Fails to State a Claim for Breach of the Operating Agreement Confidentiality Requirements Contract (Count VI)

For this claim, Warner knits together a variety of elements including the (i) duty of loyalty and care owed by Kuzmanich to Mile High (SAC ¶ 229); (ii) the fiduciary duties owed by the Defendants to Warner including the duty to keep confidential offers received by Mile High (SAC ¶ 230); (iii) a confidentiality provision in the Operating Agreement (SAC ¶ 231); (iv) the alleged violation of these duties of confidentiality by Kuzmanich and Heath (SAC ¶ 232); (v) the remaining Defendants violating their own fiduciary duties by ignoring Kuzmanich and Heath's confidentiality breaches (SAC ¶ 235); and together, Defendants breaches resulted in substantial damage to Warner (SAC ¶ 236).

To the extent Warner bases this claim on damages resulting from Defendant alleged breach of a confidentiality provision in the Operating Agreement, then such a claim is a derivative claim and concerns harm to MHRC; not Warner. See Section I(A)(2), *Supra*. To the extent Warner fashions this claim to be premised on Defendants alleged breach of fiduciary duties, this claim is duplicative of Warner's second and third cause of action and should similarly be dismissed.

H. Warner Fails to State a Claim for Breach of Operating Agreement Undertaking Requirements (Count VII)

For this claim, Warner alleges that "Defendants have a fiduciary obligation not to engage in self-dealing or appropriate Mile High's fund for personal use or expenses" (SAC ¶ 241); "have an obligation only to permit advancement in accordance with the specific provisions of the [Operating Agreement]" (SAC ¶ 242); and "in violation of their duties and contractual obligations, the Defendants have misappropriated Mile High's … funds to pay for their legal expenses, as well as those of Defendant Kuzmanich" (SAC ¶ 243). Warner also complains that "[n]one of the Defendants has provided the legally required undertaking, despite Warner's repeated requests that the (sic) do so" (SAC ¶ 244).

Here, Warner's breach of contract claim fails and must be dismissed on the grounds of documentary evidence: the indemnification provision within Operating Agreement and the undertakings filed with the Court.

Section 4(g) of the Operating Agreement titled Indemnification of the Managers and Others, provides that:

> (1) The **Managers**, the Officers **and agents acting on behalf of the Company**, if any (each, an "Indemnitee"), **are hereby indemnified and held harmless by the Company from and against any manner of claim, demand, proceeding, suit and action** () and any liability (), loss, damage, expense, or injury of any nature suffered or sustained by such party (**including** any judgment, award, settlement, and **any reasonable attorneys' fees and disbursements and other costs or expenses incurred in connection with the defense of any actual or threatened action, proceeding, or claim**) ("Loss"), **arising out of or incidental to the business, activities or operations of, or relating to, the Company**.
>
> (emphasis added).

Here, both the claims against Defendants Heath, Nuell, Tabet, Robinson and Kuzmanich, and Defendants defense against these claims, all arise out of or are incidental to the business, activities or operation of MHRC. Moreover, Warner's claims concern the business decisions and activities of Heath, Nuell, Tabet, Robinson (each as a Manager) and Kuzmanich (as Agent) while acting on behalf of MHRC.

Moreover, contrary to Warner's unfounded claim, each of the Defendants have submitted a form of legally required undertaking to Mile High; a copies of which was electronically filed with the Court at D.E. No. 33.

Additionally, Warner's allegations that she "has the right to enforce the contractual provisions of the [Operating Agreement]; is entitled to "an injunction barring Defendants" from receiving any further advancement of legal fees (SAC ¶ 246); "has been damaged by Defendants' misappropriation and conversion of Mile High's funds for their personal use" (SAC ¶ 247); and can "hold Defendants jointly and severally liable for the damage they caused by their misconduct, including by requiring them to make restitution…, plus interest (SAC ¶

249), all state derivative claims. See Section I(A)(2), *Supra*.

I. Warner Fails to State a Claim for Breach of the Operating Agreement – Removal of Warner from the Board (Count VIII)

Warner asserts that in breach of the Operating Agreement, she was wrongfully removed from Board, without cause and without an opportunity to cure (SAC ¶ 253).

Warner is incorrect. Effective December 21, 2018, Warner was removed as a Manager of MHRC pursuant to § 4(a)(iii) of the Operating Agreement. That provision concerns the "Term of Managers" and provides that "[e]ach Manager will serve until the earlier of the following events:

(1) the Manager withdraws from management (by resignation, death or disability);
(2) the Manager is removed from office by a Board Supermajority;
(3) the Manager's successor has been duly elected and qualified.

Here, Warner was removed by a Board Supermajority. See Heath Affidavit at §§ 46 -47.

Notably, The Board Supermajority also reserved all rights to determine at a later date if "[Warner's] removal shall be deemed for Cause as set forth in §3(b) of the Operating Agreement."

Section 3(b) of the Operating Agreement provides that:

> The Board (excluding the vote or consent of the affected Member in all respects), at its sole discretion at any time, may remove or force a mandatory withdrawal from membership in the Company, the Board, … as a Manager …, of any Founding Member for Cause if such Member meets any of the conditions for removal for Cause.

To remove "for cause" a supermajority is not required, it is simply a Board vote, excluding the Member at issue.

However, if there is cause, as the Board is considering, then

upon a unanimous vote (excluding Warner) Warner can be forced to withdraw as a Member and be bought out at book value. See Operating agreement at sections 3(b)(c) & (e). Thus, if and when the Board determines cause and Ms. Warner is bought out at book value, then her claims regarding the sufficiency of cause and whether an opportunity to cure must be provided becomes relevant.[2] Not before.

The documentary evidence establishes that Warner was properly removed from the Board by a supermajority pursuant to section 4(a)(iii)(2) of the Operating Agreement, and this claim should be dismissed.[3]

J. Warner Fails to State a Claim for Defamation (Count IX)

Warner alleges that Heath defamed her by "publish[ing] to third parties false and defamatory statements about Warner's professional ability and conduct as Mile High's CEO, which statements constitute libel per se under New York law." (SAC ¶ 261).[4]

The defamation claim is fundamentally flawed in ways that mandate its dismissal.

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[2] Notably the definition of "Cause" provided for in Exhibit A to the Operating Agreement does not allow a Founding Member an opportunity to cure.
[3] Despite her baseless claim, Warner refers to Section 15(o) of the Operating Agreement in support of her alleged entitlement to "immediate specific performance" (SAC ¶ 256). However, § 15(o) of the Operating Agreement refers to a remedy held by "the Company" (not Warner) and pertains to specific performance as a remedy for MHRC in case of a breach of § 10 (Confidentiality) or § 11 (Non-Solicitation) of the Operating Agreement.
[4] It is worth noting that truth is an absolute defense to defamation, and everything stated about Warner, in any of Heath's communications, is demonstrably true. Dillon v. City of N.Y., 261 A.D.2d 34, 39 (1st Dep't 1999).

1. The Pleading Requirements to Assert A Claim for Defamation Have Not Been Met

The elements of a cause of action for defamation are: a false statement, published without privilege or authorization to a third party, constituting fault as judged by, at a minimum, a negligence standard, and it must either cause special harm or constitute defamation per se. Dillon v. City of New York, 261 A.D.2d 34, 38 (1st Dep't 1999).

Specifically, under C.P.L.R. § 3016(a), when pleading a defamation action, "the particular words complained of shall be set forth in the complaint." Accordingly, it is black-letter law that for a defamation claim to survive dismissal, the complaint must set forth the actual words complained of, not merely a paraphrase, and specify the persons to whom the defamatory statements were made. CSI Group, LLP v. Harper, 153 A.D. 3d 1314, 1320 (2d Dep't 2017) (dismissing defamation claim where pleading only said it was published to "certain clients"); Gill v. Pathmark Stores, 237 A.D.2d 563, 564 (2d Dep't 1997) ("Failure to state the particular person or persons to whom the allegedly defamatory comments were made also warrants dismissal"). These rules are strictly enforced, and any paraphrasing or qualification of the statement renders the complaint defective. Erlitz v. Segal, Liling & Erlitz, 142 A.D.2d 710, 712 (2d Dep't 1988); Gardner v. Alexander Rent-A-Car, Inc., 28 A.D.2d 667 (1st Dep't, 1967).

The pleading requirements include attaching the email to the

complaint so that the challenged statements can be construed within the context of the entire publication as a whole. Dillon, 261 A.D.2d at 38; Garfinkel v. Twenty-First Century Publishing Co., 30 A.D.2d 787, 788 (1st Dep't 1968).

Additionally, Warner's reference to a December 21, 2018 letter "Heath caused to be published" to undisclosed third parties, the contents of which Warner paraphrased in her pleadings, is even more lacking in the particularity requirements set forth in CPLR § 3016(a) (SAC ¶ 277).

Here, the complaint neither presents the allegedly defamatory statements in full context, nor identifies the individuals to whom the statements allegedly were published. Thus, the requirements of C.P.L.R. § 3016(a) are not satisfied, and this claim must be dismissed.

2. The "Letter" is Mischaracterized, Withheld, and Non-Actionable

As set forth above, Warner alleges that "on December 21, 2018, Heath caused to be published a letter containing numerous false statements…" (SAC ¶ 277).

Here, Warner asserts defamation by "Heath" by blatantly mischaracterizing (and outright lying) about the substance of a letter that MHRC (not Heath) sent to Xpo after Warner continued to refuse to disclose to the Board the substance of her employment with the competitor, Xpo. In order to mischaracterize both the sender of the letter and the substance of the letter, Warner has kept the actual letter from the Court. Warner's summary of this alleged defamation is at ¶ 277 of the SAC. The actual letter is found at ¶ 45 of the Heath

Aff., Exhibit G. It is hard to imagine a more deficient and disingenuous claim for defamation, save for the claim Warner also makes regarding Heath's statement of opinion, to an investor, that the decision to remove Warner "was necessary due to a lack of alignment and discord with the Board."

3. The Email To An Investor Is A Non-Actionable Statement of Opinion

Even if the Court were to excuse the severe procedural defects, the defamation claim still would fail. The "false" statements Warner alleges are two snippets from a Heath email which Warner quotes as "lack of alignment and discord with the board" and "pushing [the members] to sell [Mile High] to Purchaser for a price and terms that did not make sense." Whether words are defamatory presents a legal question. Golub v. Enquirer/Star Group, Inc., 89 N.Y.2d 1074, 1076 (1997). "Generally, a written statement may be defamatory 'if it tends to expose a person to hatred, contempt or aversion, or to induce an evil or unsavory opinion of him in the minds of a substantial number of the community." Id. (quoting Mencher v. Chesley, 297 N.Y. 94, 100 (1947)). Alternatively, a written statement may be actionable as defamatory if it "impugn[s]... any particular talent or ability needed to perform [the allegedly defamed party's] profession. Id.

The allegedly defamatory statement here satisfies neither standard. A statement within an email regarding Warner and her "lack of alignment and discord with the board" or that she was "pushing [the members] to sell [Mile High] to Purchaser for a price and terms that did not make sense" are not the kind of statements that have been

recognized as tending to elicit a strong negative reaction from the community at large.

The two statements were nothing more than non-actionable opinion. Steinhilber v. Alphonse, 68 N.Y.2d 283,289 (1986). ("An expression of pure opinion is not actionable. It receives ... protection accorded to the expression of ideas, no matter how vituperative or unreasonable it may be.")

Moreover, Heath's email (see Heath Aff., ¶ 33) was sent to one person - Leo Keonig; a single investor whom Warner had personally introduced to MHRC during the "friends and family" round, and one not likely to be induced - by Heath's written opinions - to develop an evil or unsavory opinion of Warner. Nor could Koenig alone, form a substantial number of the community.

4. The Email To A Member Investor Is Subject to A Common Interest Privilege

Warner alleges that Heath sent an email to at least one investor. (SAC ¶ 262). As set forth above, that single investor was Leo Koenig (Heath Aff., ¶ 33). That communication - with an investor - would also be protected by the Common Interest Privilege.

Courts have long recognized that the public interest is served by shielding certain communications, though possibly defamatory, from litigation, rather than risk stifling them altogether. Liberman v. Gelstein, 80 N.Y.2d 429, 437 (1992). Liberman explains that the common interest privilege extends to: a communication made by one person to another upon a subject in which both have an interest" (citation omitted Stillman v Ford, 22 NY2d 48, 53 (1968)). This "common interest" privilege has been applied, for example, to employees of an

organization (see, Loughry v Lincoln First Bank, 67 NY2d 369, 376 (1986)), members of a faculty tenure committee (Stukuls v State of New York, 42 NY2d 272 (1977)) and constituent physicians of a health insurance plan (Shapiro v Health Ins. Plan, 7 NY2d 56, 60-61 (1959)). The rationale for applying the privilege in these circumstances is that so long as the privilege is not abused, the flow of information between persons sharing a common interest should not be impeded. Liberman, 80 N.Y.2d at 437. The privilege clearly applies to any statements of opinion Heath may have delivered to MHRC's members or investors; including Leo Koenig.

5. The Defamation Claim Fails To Plead Special Damages

Finally, Warner's defamation claim must also be dismissed for failure to plead special damages. Warner claims that "Defendant William Heath published to third parties false and defamatory statements about Warner's professional ability and conduct as Mile High's CEO, which statements constitute libel *per se* under New York law (SAC ¶ 261).

While Court's have found that false statements regarding a person's professional ability and conduct may rise to the level of libel *per se*, a statement regarding Warner's "lack of alignment and discord with the Board" most certainly does not. Since Warner's allegations are insufficient to sustain a per se claim, she was required to plead special damages, and her failure to do so is a fatal error. Garfinkel, 30 A.D.2d at 788 ("Plaintiff does not plead special damages, so unless the language is libelous *per se* the complaint cannot withstand defendants' motion to dismiss pursuant to CPLR 3211

(subd. [a], par. 7) for failure to state a cause of action).

Accordingly, Warner's defamation claim is inadequate and must be dismissed.

K. Warner Fails to State A Cause Of Action For Tortious Interference With Prospective Business Advantage (Count X)

Warner asserts a claim for tortious interference with prospective business advantage against Defendants Heath and Kuzmanich asserting that these two Defendants "used unlawful means," including "fraudulent misrepresentations and other misconduct" to "vote down the sale of Mile High to the prospective purchaser" (SAC ¶¶ 286-288).

This claim is dismissible for a multitude of reasons. First, the proposed business relations with a third party at issue here - the acquisition of Mile High - did not belong to Warner. Rather, the proposed business relations belonged to Mile High and all of her Members, including Warner, Heath and Kuzmanich. If such a claim does indeed exist, it belongs to Mile High; not Warner. Warner asserts this claim directly, on her own behalf, and for that reason, this claim must be dismissed. See Section I(A)(2), *Supra*. Second, the claim is dismissible on the grounds of the Business Judgement Rule. See Section I(A)(3), *Supra*. Finally, the claim must be dismissed due to infirmities in pleading.

In order to succeed on such a claim, Warner must show that but for the intentional and wrongful acts of a defendant, a known third party was prevented from entering into a business relationship with a plaintiff. Levy v. P & R Dental Strategies, Inc., 302 A.D.2d 255, 756 (1st Dep't 2003). Thus, the required elements are: (1) that the defendant must have known of the proposed business relations between

the plaintiff and a third party, (2) that the defendant must have intentionally interfered with the proposed business relations, (3) that the proposed business relations would have been entered into but for the defendant's interference, (4) that the defendant acted with wrongful means, and (5) injury to the business relationship. See Carvel v Noonan, 3 N.Y.3d 182 (2004); NBT Bancorp Inc. v Fleet/Norstar Fin. Group, Inc., 87 N.Y.2d 614, (1996); Guard-Life Corp. V. S. Parker Hardware Mfg. Corp., 50 N.Y.2d 183 (1980). It is black-letter law that the level of culpable conduct necessary to state a cause of action is comparably high when viewed against other business torts, and must rise to the level of a criminal act or an independent tort. Carvel, 3 N.Y.3d at 190.

Even if Warner had properly brought this claim derivatively and on behalf of Mile High, the claim would still require dismissal because Warner failed to plead that Heath and Kuzmanich engaged in the type of wrongful conduct that would support a claim for tortious interference. That type of wrongful conduct is limited to culpable conduct that amounts to a crime or an independent tort, or conduct for the sole purpose of inflicting intentional harm on the plaintiff. Carvel, 3 N.Y.3d at 190. Here, In addition, the wrongful act must be aimed at third parties, not the plaintiff. RXR WWP Owner LLC v. WWP Sponsor, LLC, 132 A.D.3d 467, 469 (1st Dep't 2015). Not that the defendants, in their judgment, decided not to accept a buyout offer.

The allegations plead here do not satisfy this standard, and this cause of action must be dismissed.

L. Warner's Claim for Indemnification and Advancement Must Be Dismissed (Count XI)

Section 4 (g) of the Operating Agreement - titled Indemnification of the Managers and Others - provides that:

> (1) **The Managers**, the officers and agents **acting on behalf of the Company**, if any (each, an "**Indemnitee**"), **are hereby indemnified and held harmless by the Company from and against any manner of claim, demand, proceeding, suit and action** (whether civil, criminal, administrative or investigative,) **and any liability** (joint or several), loss, damage, expense, or injury of any nature **suffered or sustained by such party** (**including** any judgment, award, settlement, and any **reasonable attorneys' fees and disbursements and other costs or expenses incurred in connection with the defense of any actual or threatened action, proceeding, or claim**) ("Loss"), **arising out of or incidental to the business, activities or operations of, or relating to, the Company**, regardless of whether or not the Indemnitee continues to be a Manager, agent, officer, or Affiliate thereof at any time any such liability or expense is paid or incurred (emphasis added).

Warner argues that "the Co-Founding Member Defendants have wrongfully denied Warner's request for advancement and indemnification to defend against threats and demands that have been made against her by reason of her role at Mile High" (SAC ¶ 302) and that the "mandatory advance and indemnification provisions" in §4(g) (SAC ¶ 304) "requires the Co-Founding Member Defendants to agree to provide Warner the advancement she requested". (SAC ¶ 305).

Warner misapprehends the plain meaning of the indemnification provision in the Operating Agreement and when and how it is triggered. First, it is the Company - MHRC - who provides indemnification to an appropriate indemnitee under § 4(g)(1) of the Operating Agreement; not the Defendants. As Warner failed to name MHRC - the putative "Indemnitor" - as a defendant in this action, Warner's claim for

indemnification fails and should be dismissed.

Second, even if Warner had named MHRC as a defendant in this action, she would not be entitled to indemnification and advancement of funds because she does not fit the definition of an **Indemnitee** set forth in § 4(g)(1) of the Operating Agreement.

Under § 4(g)(1), Indemnification is provided to:

> Managers … acting on behalf of the Company … are [] indemnified [] by the Company from [] any [] claim [] and any [] expense [] sustained by such party (including [] any reasonable attorneys' fees and disbursements and other costs or expenses incurred in connection with the defense of any actual or threatened action, proceeding, or claim), arising out of or incidental to the business, activities or operations of, or relating to, the Company

Warner is the plaintiff in an action she commenced against the Defendants. Any expenses Warner has incurred to date are a direct result of her role as plaintiff, her retention of counsel, and her counsel's chosen course of litigation. Warner is not incurring any legal expenses in connection with the defense of any actual, or even threatened, action.[5]

As Warner is not incurring any expense in connection with her defense of a claim or threatened claim, this claim should be dismissed.

M. Warner's Claim for Production of Books and Records Should Be Dismissed (Count XII)

Warner alleges that "as a Manager and Co-Founding Member" she "has a right of access to books and records of Mile High". Complaint ¶

[5] Moreover, Warner's argument that she should be indemnified for fees to non-parties for discovery Warner has decided to engage in prior to party discovery is simply nonsensical. See SAC at ¶ 307, ¶ 310, and ¶ 311.

317. Warner then refers to § 2(g) of the Operating Agreement, titled "Access to Records," which provides:

> *Access to Records*. **After giving reasonable advance *written notice to the Company stating under oath the purpose thereof in accordance with Section 1102(b) of the Act*,** any Member may inspect and review the Company's books and records for any proper purpose and may, at the Member's expense, have the Company make copies of any portion or all of such books and records. A proper purpose means a purpose reasonably related to such person's interest as a Member (emphasis added).

SAC ¶ 318.

First, Warner has not followed the specific procedures in § 2(g) of the Operating Agreement and has not even alleged that she has done so. To be clear -- no formal written requests for access to record - submitted under oath - has been received or refused. On the contrary, Warner's informal, improper requests have been honored. Second, Warner seeks MHRC's books and records yet neglected to include MHRC as a defendant. This is a fatal error and Warner's cause of action for books and records should be dismissed.

II.

THE DEMANDS FOR PUNITIVE DAMAGES SHOULD BE STRICKEN

Plaintiff's requests for punitive damages -- appended to the Second Amended Complaint's claims for breach of fiduciary duties (Count II), aiding and abetting breach of fiduciary duties (Count III), breach of Operating Agreement confidentiality requirements (Count VI), defamation (Count IX), and tortious interference with prospective business advantage (Count X) -- should be dismissed because this action is a private dispute and plaintiff has not pled

sufficiently culpable conduct on the part of Defendants.

In New York punitive damages awards are based upon allegations of a "high degree of moral culpability" affecting a "public right." Rose Lee Mfg., Inc. v. Chemical Bank, 186 A.D.2d 548, 550-51 (2d Dep't 1992) (dismissing claim for punitive damages for failure to allege facts demonstrating "a high degree of moral culpability"); see also Holoness Realty Corp. v. New York Prop. Ins. Underwriting Ass'n, 75 A.D.2d 569, 570 (1st Dep't 1980) (punitive damages claim against insurer is cognizable only on allegations of "a fraudulent and deceitful scheme in dealing with the general public" which "impl[ies] a criminal indifference to civil obligations"); Tevdorachvili v. Chase Manhattan Bank, 103 F. Supp.2d 632, 645 (E.D.N.Y. 2000) (in New York, "punitive damages 'are available only in those limited circumstances where it is necessary to deter defendant and others like it from engaging in conduct that may be characterized as 'gross' and 'morally reprehensible,' and of 'such wanton dishonesty as to imply a criminal indifference to civil obligations.") (citing New York Univ. v. Continental Ins. Co., 87 N.Y.2d 308, 315-16 (1995).

Even in cases of fraud, punitive damages are recoverable only when the fraud is "aimed at the public generally." M.S.R. Associates v. Consolidated Mutual Insurance Company, 58 A.D.2d 858, 859 (2d Dep't 1977) (quoting Walker v. Sheldon, 10 N.Y.2d 401, 405 (1961)); see also Diker v. Cathray Constr. Corp., 158 A.D.2d 657, 658 (2d Dep't 1990) (same); Maravex Processing & Finishing Corp. v. Allendale Mut. Ins. Co., 398 N.Y.S.2d 464, 466 (Sup. Ct. 1977) (punitive damages not available for an "isolated transaction although claimed to be

fraudulent, incident to the otherwise legitimate business" of a defendant).

Even accepting all of plaintiff's allegations, a request for punitive damages in this case, by plaintiff, is completely inappropriate, and the punitive damages claims in the Second Amended Complaint should be dismissed.

CONCLUSION

For the all of the foregoing reasons, Defendants respectfully request the Court grant their motion in its entirety, together with such other and further relief that the Court may deem just, proper and equitable.

Dated: March 29, 2019
New York, New York

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

DEBORA WARNER, Plaintiff, -against- WILLIAM HEATH, DAVID KUZMANICH, KIM TABET, ROBERT NUELL, DAVID ROBINSON, Defendants.	Index No.: 654714/2018

KEITH M. GETZ, an attorney duly licensed to practice law in the State of New York, subscribing and affirming as true, under penalties of perjury, states as follows:

1. I am Of Counsel to Lebowitz Law Office, LLC, attorneys for Defendants William Heath ("Heath"), David Kuzmanich ("Kuzmanich"), Kim Tabet ("Tabet"), Robert Nuell ("Nuell"), and David Robinson ("Robinson" and together with Heath, Kuzmanich, Tabet, and Nuell, collectively "Defendants").

2. On March 29, 2019, I electronically filed the within Memorandum of Law in Support of Defendants' Motion to Dismiss Plaintiff's Second Amended Complaint.

3. As set forth in Rule 17 of the Rules of the Commercial Division of the Supreme Court (22 NYCRR 202.70(g)), I certify that the word count for Defendants' Memorandum of Law totals **8323** words.

4. I further certify that on March 29, 2019, Defendants' were granted, by the Court, an enlargement of the word limit from 7000 words to 9000 words.

I affirm under penalty of perjury that the foregoing is true and correct.

Dated: March 29, 2019
New York, New York

Keith M. Getz, Esq.