To be Argued by:
EDWARD B. SAFRAN
(Time Requested: 15 Minutes)

New York Supreme Court

Appellate Division—Second Department

RONALD MIZRAHI, individually and as a 50% member of and in the right of 372-376 Avenue U Realty LLC, a New York limited liability company,

Docket No.: 2012-02021

Plaintiff-Appellant-Respondent,

– against –

EZRA COHEN,

Defendant-Respondent-Appellant.

BRIEF FOR PLAINTIFF-APPELLANT-RESPONDENT

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thereafter prevented Cohen from meeting the particular demand, "but the obligation to fund was not questioned" [R. 10-11]. Cohen never opposed or question the need for a capital call. His sole response when asked for a contribution was that "financially, things were tough and that he ... needed some time" [R.345].

For the foregoing reasons the Court below erred when holding that the Operating Agreement was not breached due to Cohen's failure to make equal capital contributions with Mizrahi. The clear intent and expectations of the parties was that each make equal contributions. The parties implemented that intent for a number of years after executing the contract. The Operating Agreement was accordingly breached by Cohen when he failed to do so.

IV

A BUY-OUT SHOULD HAVE BEEN ORDERED

The equities of this case, as well as the provisions of the Operating Agreement, should have resulted in an order permitting Mizrahi to buy Cohen's interest in the Company rather than reserving the right to appoint a receiver and have

a public sale of the Company's property as a means of liquidation.

A. The Operating Agreement contemplates a buy-out on dissolution.

The Court below held that §7.2 of the Operating Agreement somehow precludes a buy-out. It doesn't. All §7.2 provides is that, on dissolution and following payment to creditors, "the assets of the Company shall be distributed ... to the Members and Economic Interest Holders in accordance with Section 4.4 of this Agreement" [R. 710].

§ 4.4.2 of the Operating Agreement contemplates a buy-out rather than an auction upon dissolution. It provides in relevant part that "[I]f any assets of the Company are distributed in kind to the Economic Interest Holders, those assets shall be valued on the basis of their fair market value ... Unless the Members otherwise agree, the fair market value of the assets shall be determined by an independent appraiser who shall be selected by the Members..."[R. 705] Nothing in the Operating Agreement mandates either a public or private sale on liquidation. Accordingly, looking to the Operating Agreement for guidance, ordering a buy-out is appropriate.

The "distribution in kind" provision of the

operating agreement is essentially a buy-out provision. It provides for an appraisal to be performed by an independent appraiser selected by the Members. The Court ordered such an appraisal, which demonstrated a fair market value for the property of $4,550,000, barely more than the principal due on the mortgage.

Not a single provision of the Operating Agreement requires a public sale, or an auction, of the company's assets on dissolution. The simple fact is that the only language in the contract regarding disposition of the company's assets is distribution in kind to a member at fair market value.

The Court below erred in finding that Sections 7.2 and 4.4 of the Operating agreement precludes the possibility of a buy-out. The Court below further erred in finding that the personal liability which the parties have on the mortgage precludes a buy-out [R. 22]. The language of Section 7.2 taken together with Section 4.4.2 expressly contemplates that a member may receive his interest "in kind" on liquidation, provided the fair market value is determined.

The Court's footnote [R.22] regarding tenancy in common distribution did not consider that tenants in common have an absolute right of partition.

In justifying its finding, the Court below referred

to Section 3.2 of the Operating Agreement, which provides that "No Member shall have any personal liability for any obligation of the Company." [R.22] However, the personal liability on the mortgage which the parties have devolves not from their membership in the Company, but pursuant to collateral guarantees which each signed in his personal capacity. Anyone could have issued personal guarantees on the mortgage whether or not they were members in the Company. The Court below misconstrued Section 3.2, which is a standard clause in limited liability operating agreement providing that no person, solely by reason of his membership in the limited liability company, has personal liability for the company's debts.[13] Section 3.2 of the Operating Agreement is a common provision used to define member's rights so as to preclude personal liability under LLCL §609(b).

Consequently, the fact that the parties have independently guaranteed the mortgage on the Company's property has no relevance to their rights and liabilities as member of the Company or under the Operating Agreement.

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[13]LLCL Sec. 611 distinguishes between acts taken not as a member (such as guarantor) and acts taken as a member.

B. The Court below should have exercised its equitable power to order a buy-out.

Matter of Superior Vending, LLC, 71 AD3d 1153 (2nd Dept. 2010) stands for the proposition that although the Limited Liability Company Law does not expressly authorize a buyout in a dissolution proceeding, the Supreme Court has that authority where it is determined to be "the most equitable method of liquidation." It is submitted that the Court below misconstrued the intent of the Second Department when issuing its decision in *Matter of Superior Vending* in distinguishing that case by highlighting the fact that one of the two members in *Superior Vending* remained active and the other did not. Although the facts are different in certain respects, the equities are not.[14] Due to Cohen's failure to abide by his agreements and fiduciary duties, Mizrahi needed to invest about $1 Million more than Cohen to forestall foreclosure and protect the integrity of both his and Cohen's separate, and substantial, investments in their respective professional suites.

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[14]In the Decision/Order the Court below distinguished *Matter of Superior Vending* by emphasizing that the members consented to dissolution. In the proceedings of July 11, 2011, immediately before testimony was taken, Cohen's attorney agreed to a dissolution upon a "fair accounting." [R.307]

Matter of Superior Vending, LLC implemented long-standing New York law holding that the mere fact that a case is novel and is not brought plainly within the limits of some previously judged case is not enough to preclude equity from taking jurisdiction and exercising equitable powers to furnish a remedy. *Millspaugh v. Cassidy,* 191 AD 221 (2nd Dept. 1920); *Lewis v. Jones,* 107 AD2d 931 (3rd Dept. 1985)[leaving a party without an adequate remedy is "a circumstance abhorrent to the common law"];*New York and Brooklyn Suburban Inv. Co. of New York v. Leeds,* 100 Misc.2d 1079 (N.Y. Sup. 1979).

Mizrahi (and Cohen) have established businesses at the location. The cost of uprooting Mizrahi's dental practice, moving it to another location, and building a new dental suite, would be no less than what he spent to construct his existing suite. So, in addition to losing the ±$452,000 investment in his dental suite, he would be required to spend at least an additional ±$500,000 to reestablish and replicate a dental suite at another location, with the concomitant disruption in his professional practice and almost certain loss of income. That loss, of ±$2 Million, is not recoverable under the terms of the Decision/Order, although directly attributable to Cohen's breaches and defalcations.

If the property were to be sold at public sale, the

Company would incur expenses well in excess of $525,000 for brokerage fees (±5%), receiver's fee (5%), transfer taxes (±2%) and attorney's fees. The property has recently been appraised pursuant to order of the Court below at a market value of $4,550,000 [R.306]. The principal balance due on the mortgage is about $4.4 Million [Trial Exh. 6, R. 306, 883]. There is virtually no equity in the property, and Mizrahi will suffer a substantial cash loss if the Company were required to sell the property at public sale.[15] It is unlikely that Cohen has the ability to fund any portion of such a shortfall, since he has not even returned the $230,000 which he took in 2006. More significant, however, is that the Company will have no cash after such a sale to reimburse Mizrahi for the ±$1 Million he is owed as a creditor of the Company pursuant to the Decision/Order.

Accordingly, the most equitable method of liquidation is to permit Mizrahi to purchase Cohen's economic interest in the Company at fair market value, subject to the accounting provided for in the Decision/Order.[16]

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[15]There is insufficient equity in the property to pay a receiver's statutory fee of 5% and satisfy the existing mortgage.

[16]It appears that the personal liability of the parties on the mortgage loan was a significant factor in arriving at that branch of the Decision/Order denying a request for a buyout. To