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

JEAN BARMASH, an individual, for himself and derivatively on behalf of nominal defendant ENERGYSCORECARDS, INC.,

Plaintiff,

- against -

JEFFREY PERLMAN and BRIGHT POWER, INC.,

Defendants,

and

ENERGYSCORECARDS, INC.,

Nominal Defendant.

Index No. 650417/2013

DEFENDANTS' MEMORANDUM OF LAW IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS THE VERIFIED COMPLAINT

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Dated: New York, New York
March 18, 2013

Defendants Jeffrey Perlman ("Perlman"), Bright Power, Inc. ("BP") and EnergyScoreCards, Inc. ("ESC") (collectively "Defendants") submit this memorandum of law [1] in support of their motion pursuant to CPLR 3211(a)(7) to dismiss the verified complaint filed February 5, 2013 (ECF Doc. # 1, the "Complaint") filed by plaintiff Jean Barmash ("Plaintiff") individually and derivatively as a shareholder on behalf of ESC.

PRELIMINARY STATEMENT

In this action, Plaintiff improperly seeks to bring derivative claims on behalf of ESC, a Delaware corporation, after threatening ESC (the very entity he seeks to represent as fiduciary) with litigation challenging ESC's use and ownership of its principal asset (computer software) and seeking to improperly extort a buy-out of his interest in ESC. Plaintiff's threats, extortionate tactics and failure to comply with the very agreement through which he was issued ESC's shares make him directly adverse to ESC and completely inadequate to serve as a derivative plaintiff. Indeed, in his Verified Complaint, Plaintiff brazenly *admits* that he used the threat of filing this very action to attempt to extort personal benefits through a settlement, by way of a buy-out of his interest in ESC. Moreover, the relief Plaintiff seeks in this case would actually harm ESC, the very entity he purports to represent derivatively. Finally, because there are direct claims between Plaintiff and ESC in this litigation, Plaintiff is in a directly adverse position *vis-à-vis* the entity he seeks to represent in this case -- and, therefore as no standing to sue derivatively as a stockholder in ESC.

Given these circumstances -- under applicable case law in both Delaware and New York law, Plaintiff is inadequate to be a derivative action plaintiff and cannot proceed with this

[1] The Court is also respectfully referred to the accompanying moving affidavit of Jeffrey Perlman sworn to on March 18, 2013 ("Perlman Aff."). A copy of the Complaint is attached as Exhibit A thereto.

derivative action. Moreover, although Plaintiff attempts to also assert "direct" claims against defendants Perlman and BP, those claims are in fact all derivative because (i) they allege harm to only ESC and not to plaintiff personally, and (ii) any relief afforded would be relief for ESC and not for Plaintiff personally. Once again, all of the authority on point -- in both Delaware and New York -- hold that such claims are "derivative" and are not "direct" claims, regardless of how Plaintiff has attempted to style such claims in his Complaint. Thus, because *all* of the claims Plaintiff has asserted are, in substance and reality, "derivative" claims, they should all be dismissed on the ground that Plaintiff is an inadequate and improper derivative action plaintiff.

Finally, Plaintiff is estopped from bringing his current claims -- whether styled as derivative or direct -- because, through those claims, he is seeking to challenge corporate policy and actions that he agreed to and affirmatively approved as a shareholder, officer and director of ESC. As a matter of law, Plaintiff cannot challenge those corporate actions and policies in order to attempt to extort a personal buy-out of his stock interest. The cases uniformly recognize the impropriety of such claims and uniformly estop a plaintiff from pursuing such claims.

STATEMENT OF FACTS

The Court is respectfully referred to the accompanying Perlman Aff., which sets forth certain documentary evidence and facts appropriately considered on a motion to dismiss.

Perlman is the President and majority shareholder of BP, a company which, among other things, conducts energy audits and provides energy management consulting services to owners of buildings in New York City and in other locations. Complaint at ¶¶ 27-29 and Perlman Aff., ¶ 2. BP has been in business since December 2004. Perlman Aff., ¶ 2.

As the Complaint alleged, in or about 2008, Perlman and Plaintiff, a software developer, began discussions regarding the development and implementation of software designed to monitor the energy usage and water consumption of buildings (the "Software"). Complaint at ¶¶ 2-3. Perlman was aware of the potential need and market for the Software based on his prior experience in the energy business, and the software prototypes his team had already created and their reception in the marketplace. *Id.* at ¶ 29. In or about April 2009, Perlman and Plaintiff entered into a letter agreement outlining the terms and conditions upon which Perlman and Plaintiff would pursue the development and marketing of the Software (the "Agreement"). Perlman Aff., ¶ 3.

It was agreed by the parties that an entity would be formed for purposes of developing and marketing the Software: namely ESC. *Id.* at ¶ 4. BP was to hold 80% of ESC's shares and Plaintiff was to receive 20% of ESC's shares in exchange for his software development services. *Id.* The parties further agreed that, despite the disparity in ownership, during the first two years of ESC's existence, Perlman and Plaintiff would be the only two Directors and would have equal voting rights. *Id.* After the initial two year period, and so long as Plaintiff remained working for ESC, Perlman and Plaintiff (through BP) would have voting rights in proportion to their

ownership of ESC. *Id.*

The parties also agreed that Perlman would be the CEO of ESC and that Plaintiff would be the Chief Technology Officer of ESC. As CEO of ESC, Perlman agreed to "set overall direction, product definition, and [] be the chief salesperson." As Chief Technology Officer, Plaintiff agreed to create the Software, "operate and maintain the software, expand its features as needed, and direct other technology aspects of the business." *Id.* Perlman and Plaintiff also agreed that BP would "provide the idea, spreadsheets, and early prototypes of the product, insights into the energy and buildings industries, connections to potential customers, business structuring and development, sales, testing and quality control, and marketing." *Id.* Finally, Perlman and Plaintiff expressly recognized and agreed that BP would be a customer of ESC and would be purchasing the right/ability to use the Software directly from ESC: thus, the Agreement defines gross revenue as "revenue from product sales, *including sales to Bright Power itself*, although sales to Bright Power may not constitute more than 50% of gross revenue for purposes of milestone or clawback provisions or calculations." *Id.* (emphasis added).

Pursuant to the terms of the Agreement, Plaintiff worked on developing the Software and Perlman incorporated ESC in or about February 2010. *Id.* at ¶ 5.[2] Even though the Software remained in Beta release and was not complete, Perlman and the Bright Power team also set out to market and sell the Software. Ultimately, Perlman and BP were able to secure customers for the Software. *Id.* at ¶ 7. At all times, and pursuant to the Agreement, BP employees provided sales, support, product definition, testing, quality control and marketing for the Software. Moreover, and as specifically agreed to by Perlman and Plaintiff, BP developed a significant and steady flow of customers and revenue for ESC by referring its own customers to ESC, marketing

[2] Plaintiff renegotiated his initial holdings and was issued 25% of ESC's shares in exchange for his promise to develop the Software. Thereafter, Plaintiff was diluted to approximately 19% based on agreed-to buy-back provision enabling ESC to buy back some of his shares after he ceased working for ESC. Perlman Aff., ¶ 6.

ESC and incorporating the Software into BP's package of services provided to its customers. *Id.* at ¶ 8. In exchange for BP's use of the Software in this manner, BP paid ESC a licensing fee that was often greater than the fees collected by ESC through direct licenses to individual customers. *Id.* at ¶ 9.

Plaintiff, as one of only two shareholders, one of only two directors and one of only two officers of ESC was fully aware of and agreed to BP's involvement in both the direct marketing and sale of the Software to ESC's direct customers and the indirect marketing and sale of the Software through the incorporation of the Software into BP's broader package of services provided to its customers. *Id.* at ¶ 10. Plaintiff was aware that BP compensated ESC for use of the Software in connection with its own customers and that ESC compensated BP for BP's sales, support, testing, quality control and marketing for the Software and Plaintiff never complained about or objected to this arrangement. *Id.* at ¶ 11.

In or about November 2011, Plaintiff notified Perlman of his decision to resign from ESC. Plaintiff continued to work with Perlman, BP and ESC through May 2012, to transition his technical responsibilities relating to the Software to others (mainly employees of BP). *Id.* at ¶ 12. In discussing Plaintiff's departure from ESC, Perlman and Plaintiff agreed in principle that BP would buy Plaintiff's interest in ESC for reasonable compensation. In May 2012, Perlman approached Plaintiff with an offer to exchange Plaintiff's stock in ESC for a combination of cash and stock in BP. In July 2012, Plaintiff responded, through his counsel at the time, with an exorbitant counter-offer that well exceeded the value of Plaintiff's interest and failed to account for the costs associated with completing and fixing the Software. *Id.* at ¶ 13. In fact, the Software remains in Beta release form and has not yet been fully developed. *Id.* at ¶¶ 14-15. Indeed, BP and ESC have spent in excess of $650,000.00 working to fix problems in the

Software that existed at the time Plaintiff abandoned ESC and trying to finally complete the Software so it can be taken out of Beta release. *Id.* at ¶ 14.

Then, beginning in September 2012, after resigning from ESC, leaving it with faulty software that had not been fully developed (which was the very basis of Plaintiff's receipt of stock in ESC) and failing to agree to a reasonable buy-out of his interest in ESC, Plaintiff began a campaign aimed at coercing, through various threats, a buy-out of his interest in ESC at his exorbitant price. *Id.* at ¶ 16. First, Plaintiff threatened to sue ESC directly over ownership of the copyrights and other intellectual property rights associated with the Software if it did not accede to his unreasonable buy out demand. *Id.* at ¶ 17-18. The allegation underlying the threat plainly lacked merit -- the Agreement specifically stipulated that ESC owned the Software and it is undisputed that Plaintiff developed the Software while employed by ESC (*Id.*) -- thereby exposing Plaintiff's extortionate motive. Thus, using the threat of litigation regarding ESC's principal asset, Plaintiff sought to coerce a *personal* buy-out of his interest in ESC, the very entity he seeks in this litigation to represent as a fiduciary. *Id.* at ¶ 19.

After the foregoing threats failed to secure Plaintiff the buy-out he sought, Plaintiff engaged litigation counsel and changed course. At the end of January 2013, Plaintiff threatened to file the instant derivative action as an additional extortionate attempt to obtain a buy-out of his stock interest -- thus, misusing this derivative action to further his own, personal financial interests on the pretext of seeking to represent ESC in a derivative action. *Id.* at ¶ 21 and Complaint at ¶ 163. Indeed, as Plaintiff brazenly admits in his Verified Complaint, prior to filing this action, Plaintiff sent Perlman a draft of the Verified Complaint with a letter indicating that if his buy-out demands were not met, the Verified Complaint would be filed. *Id.* While Perlman and BP sought to negotiate in good faith, Plaintiff maintained demands for a buy-out of his

interest in ESC that were completely unrealistic and unreasonable. Perlman Aff., ¶ 22. Furthermore, the significant counterclaims that BP and ESC have asserted in response to Plaintiff's Verified Complaint demonstrate that Plaintiff is directly adverse to the very company (ESC) that he improperly seeks to represent in this derivative action (and establish that Plaintiff's very standing as a stockholder of ESC is in serious doubt). *Id.* at ¶ 15.

Plaintiff's conduct in (1) seeking to extort a buy-out through threatened litigation directly against ESC, (2) filing the instant action, and (3) failing to fulfill his obligations to completely develop the Software creates an irreconcilable conflict of interest between Plaintiff and ESC, the very entity he seeks to represent as a fiduciary in this derivative action. Indeed, there is a direct economic antagonism between Plaintiff -- who is pursuing this litigation only for personal gain - and ESC and BP. For these, and other reasons, Plaintiff cannot adequately represent ESC or its shareholders and Plaintiff's derivative claims should be dismissed.

LEGAL ARGUMENT

A. Motion To Dismiss Standard

CPLR 3211 (7) CPLR permits the court to dismiss a complaint where the pleading fails to state a cause of action. When determining a motion under CPLR § 3211(a)(7), the court should accept as true the facts alleged in the complaint. As applicable here, however, "factual allegations that do not state a viable cause of action, that consist of bare legal conclusions, or that are inherently or clearly contradicted by documentary evidence are not entitled to such consideration." *Skillgames, LLC v. Brody*, 1 A.D. 3d 247, 250, 767 N.Y.S. 2d 418, 421 (1st Dep't 2003), *Shariff v. Murray*, 33 A.D. 3d 688, 690, 823 N.Y.S. 2d 96, 98-99 (2d Dep't 2006) ("Although the narrow question presented on review of a motion to dismiss is not whether a plaintiff should ultimately prevail in the action, but whether the complaint states cognizable

causes of action, vague and conclusory allegations will not suffice."); *accord Stoianoff v. Gahona*, 248 A.D. 2d 525, 526, 670 N.Y.S. 2d 204, 205 (2d Dep't 1998).

Where extrinsic evidence is introduced on a motion to dismiss pursuant to CPLR 3211(a)(7), "the motion should be granted where the essential facts have been negated beyond substantial question by the affidavits and evidentiary matter submitted." *Biondi v. Beekman Hill Apt.*, 257 A.D.2d 76, 81, 692 N.Y.S. 2d 304 (1st Dep't 1999); *see also Taylor v. Pulvers, Pulvers, Thompson & Kuttner*, 1 A.D. 3d 128 (1st Dep't 2003) (dismissing complaint where affidavits submitted on the motion to dismiss "conclusively established that plaintiff had no cause of action"); *Fields v. Leeponis*, 95 A.D. 2d 822 (2d Dep't 1983) (same). The standard of review, where extrinsic evidence is used, is "whether the proponent of the pleading has a cause of action, not whether he has stated one." *Id.* quoting *Guggenheimer v. Ginzburg*, 43 N.Y.2d 268, 275 (1977).

Here, as discussed more fully in the following sections, the Complaint on its face demonstrates that Plaintiff is inadequate to bring derivative claims on behalf of ESC and, as all of Plaintiff's claims are in fact derivative in nature, the Complaint should be dismissed. A review of the extrinsic evidence presented herewith further demonstrates that Plaintiff's *sole motive* for filing this suit is to coerce an unreasonable buy-out of his interest in ESC. Finally, in his capacity as shareholder, officer and director of ESC, Plaintiff has agreed to much, if not all, of the activity he now complains about – BP's use of the Software and BP's role in supporting the Software -- and, thus is estopped from bringing a cause of action based on that legitimate business relationship.[3] All of these reasons, as set forth in detail below, mandate dismissal of Plaintiff's Verified Complaint.

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[3] Under Delaware law, "[t]ransactions between a controlling shareholder and the company are... perfectly acceptable if they are entirely fair, and so plaintiff must allege facts that demonstrate a lack of fairness." *Monrow Cnty. Emps.' Ret. Sys. v. Carlson*, 2010 WL 2376890, *2 (Del. Ch. June 7, 2010).

B. The Complaint Should Be Dismissed Because Of Plaintiff Is Not a Legally Adequate Representative Of ESC And Is Not Qualified To Bring Derivative Claims On ESC's Behalf

In order to qualify as a derivative plaintiff, a shareholder must demonstrate that he can act as a fiduciary for, and fairly and adequately represent the interests of, the company and all of its other shareholders. *See Gilbert v. Kalikow*, 272 A.D.2d 63, 707 N.Y.S.2d 100 (1st Dep't 2000) (affirming dismissal of a derivative action where "plaintiff has failed to demonstrate that he will fairly and adequately represent the interests of the limited partnership"). This requirement is "intended to prevent shareholders from suing in place of the corporation in circumstances where the action would disserve the legitimate interest of the company or its shareholders." *See Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 532, n.7 (1984); *see also* The Business Judgment Rule, Vol. II, Chap. IV.A.5 at 3746 (6th Ed. 2009) ("These considerations are important because 'a shareholder may bring a derivative action to gain leverage by which to settle an unrelated dispute, to advance the shareholder's primary interests as an employee, creditor...or for other reasons not shared by the holders as a class,' and '[w]here courts have discerned conflicts between the real interests of the plaintiff and the interests of the class the shareholder purports to represent, they have been ready to deny standing.'" quoting 2 Principles of Corporate Governance: Analysis and Recommendations § 7.02 Comment at 38 (1994, as reprinted in 2008)).

In order to determine whether a plaintiff meets the legal requirement that he be an adequate representative of the derivative class, Delaware and New York courts review the following factors[4]:

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[4] ESC is a Delaware corporation and, therefore, Delaware law governs the issue of Plaintiff's legal qualification as a derivative action on behalf of ESC here. In deciding whether a shareholder is a legally adequate derivative action representative, New York State courts look to authority from Delaware and the New York Federal Courts. *See e.g. In re Comverse Technology, Inc.*, 56 A.D. 3d 49, 56, 866 N.Y.S. 2d 10 (1st Dep't 2008) (Delaware

1. economic antagonism between the representative and the other shareholders;

2. the remedy sought by the plaintiff in the derivative action;

3. indications that the named plaintiff is not the driving force behind the litigation;

4. plaintiff's unfamiliarity with the litigation;

5. other litigation between the plaintiff and the company and/or other shareholders;

6. the relative magnitude of the plaintiff's personal interests as compared to his interest in the derivative action itself;

7. plaintiff's vindictiveness toward the company and/or its other shareholders; and,

8. the degree of support for plaintiff's claims from the shareholders he purports to represent.

See Priestley v. Comrie, No. 07 CV 1361, 2007 WL 4208592, *5 (S.D.N.Y. Nov. 27, 2007) (motion to dismiss derivative claims granted because of several impermissible conflicts of interest with the shareholder class); *see also Youngman v. Tahmoush*, 457 A.2d 376, 379-80 (Del. Ch. 1983) ("a Court...should examine any extrinsic factors, that is, outside entanglements which make it likely that the interests of the other stockholders will be disregarded in the prosecution of the suit"); *Zamer v. Diliddo*, No. 97-CV-328, 1999 WL 606731, *3 (W.D. N.Y. March 23, 1999) ("to find adequacy of representation...the courts have required that the representative plaintiff demonstrate...absence of 'either a conflict of interest which goes to the forcefulness of the prosecution or the existence of antagonism between the plaintiff and other shareholders arising from difference of opinion concerning the best method of vindicating the corporate claim.'" quoting *Sweet v. Bermingham*, 65 F.R.D. 551, 554 (S.D.N.Y. 1975)).

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law found instructive on issue New York courts had not yet addressed); *Matakov v. Kel-Tech Const., Inc.*, 84 A.D. 3d 677, 679, n. 1, 924 N.Y.S. 2d 344 (1st Dep't 2011) ("Federal jurisprudence is an appropriate guide when analyzing CPLR article 9 issues, because article 9 has much in common with Federal rule 23, the federal class action provision," *citing City of New York v. Maul*, 14 N.Y. 3d 499, 510 (2010)); *see also* 4B N.Y. Prac., Com. Litig. Section 82:30 (3d ed. 2010) (analyzing a derivative plaintiff's adequacy under federal case law and noting that the New York state corollary to Fed. R. Civ. P. 23.1 is codified at Section 901 of the CPLR.).

A court need not find all of these factors to disqualify a plaintiff as a legally adequate derivative representative. Indeed, a sufficient showing of just one of the above factors can disqualify a plaintiff. *Priestley, supra*, 2007 WL 4208592 , *5, *citing Youngman, supra*, 457 A.2d at 380 ("Although these elements have been frequently combined to provide the basis for a court's decision to dismiss, often a strong showing of one factor which is actually inimical to the class, will permit the same conclusion."). Here, several of the applicable disqualifying factors are established in the existing record as follows. Thus, Plaintiff is not a legally adequate representative of the ESC shareholders or ESC's interests. Accordingly, his derivative action should be dismissed[5].

1. Economic Antagonism Between The Purported Derivative Representative And The Other Shareholder.

As set forth in the Perlman Aff. and above, Plaintiff quit as CTO of ESC in 2011 without having completed development of the Software. Since that time, Plaintiff's singular interest regarding ESC has been to secure a high priced buy-out of his minority stock holding. For the past six months, Plaintiff has sought to influence the negotiations by making a series of litigation threats against ESC. First, Plaintiff threatened to sue ESC directly for alleged copyright infringement, and pursue relief that would deprive ESC of its principal asset (the Software). Of course, that threatened litigation would have been devoid of merit because document evidence and undisputed fact establishes ESC's ownership of the intellectual property. Perlman Aff., ¶¶ 17-19. The fact that Plaintiff is threatening plainly meritless litigation against ESC -- obviously for the sole purpose of enhancing his personal interest in coercing a buy-out -- is irreconcilable with his now alleging legal qualification to represent ESC in a fiduciary capacity.

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[5] As demonstrated in Point C below, all of Plaintiff's claims are derivative in nature. Thus, the Complaint should be dismissed in its entirety.

The initial litigation threat was followed with another one after Plaintiff engaged litigation counsel. *Id.* at ¶ 21. While the nature of the litigation threat changed with counsel, the fact remained that Plaintiff was using the threat to serve his personal interest of coercing a buy-out. Indeed, the Complaint contains Plaintiff's admission that the buy-out of his ESC stock by using the threat of litigation was his objective. *See* Complaint at ¶163.

Plaintiff's litigation threats against ESC in pursuit of his personal goal of a vastly overpriced buy-out are especially egregious when viewed in light of his failure to satisfy his contractual obligations to fully develop the Software. Perlman Aff., ¶¶ 14-15. Indeed, Plaintiff's failure in this regard places in question Plaintiff's very ownership of his stock in ESC (a precondition to bringing a derivative action)[6]. *See Youngman*, 457 A.2d at 379 ("the only explicit standing requirement for maintaining a derivative suit is that the plaintiff be a stockholder of the corporation at the time of the transaction of which he complains."). Plaintiff's intractable negotiation position vis-à-vis a buy-out, the threatened claims against ESC and the claims made in the Complaint, place Plaintiff in a position directly adverse to ESC, the company he purports to represent.

Based on these facts and circumstance, there is substantial direct economic antagonism between Plaintiff and ESC. This factor alone is enough to defeat Plaintiff's adequacy to serve as a derivative Plaintiff. *See Youngman*, 457 A.2d at 380 ("A major type of antagonism requiring denial of certification is clear economic antagonism between representative and class." quoting *Katz v. Plant Industries, Inc.*, Del.Ch., C.A. # 6407-N.C., 3-4 (October 27, 1981) (internal quotations and citations omitted)); *see also Canadian Commercial Workers Industrial Workers Pension Plan v. Alden*, No. Civ.A. 1184-N, 2006 WL 456786, *8 (Del. Ch. Feb. 22, 2006) ("[A]

[6] ESC stock was issued to Plaintiff in good faith anticipation that he would fulfill contractual requirement to complete the Software (Perlman Aff., ¶ 6).

strong showing as to one factor is sufficient if that factor involve[s] some conflict of interest between the derivative plaintiff and the class. The primary factor in this inquiry is whether there is an economic conflict between the plaintiff and the other stockholders making it likely that the interests of the other stockholders will be disregarded in the prosecution of the suit." (internal quotations and citations omitted)).

2. The Remedy Sought By Plaintiff Would Harm ESC Economically.

Plaintiff seeks to enjoin BP from using the Software in any manner. See Complaint generally and WHEREFORE clause C at p. 32. This relief is in derogation of the parties' Agreement, which expressly contemplated that BP would be a significant customer of ESC and authorized the sale of the Software to it. Indeed, the revenue ESC derives from BP purchasing the right to use the Software is significant and the fees paid by BP often exceed the fees paid by ESC's direct customers. Perlman Aff., ¶¶ 8-9. Thus, a request for such injunctive relief would harm ESC economically.

In addition to being a significant customer, BP is funding the continued development of the Software and is responsible for marketing and servicing the Software. *Id.* at ¶ 8. Thus, there is a strong likelihood that such injunctive relief would interfere and retard the development and marketing of the Software. As such, ESC stands to suffer substantial and immediate harm -- irreparable harm -- through lack of revenue and lack of marketing and support for the Software if BP were enjoined from using it. Indeed, the remedy Plaintiff seeks presents a strong risk of causing irreparable harm to ESC. Accordingly, while perhaps of interest to Plaintiff for the purpose of coercing a buy out of his stock interest, the remedy he seeks is incompatible with ESC's best interests and further demonstrates Plaintiff's legal inadequacy to serve as a derivative plaintiff.

Finally, while Plaintiff has styled his Verified Complaint, in part, as a Derivative Action and he claims to seek relief on behalf of ESC, his actions over the past six months demonstrate conclusively that the remedy he truly seeks is a buy-out of his interest in ESC. This remedy will not inure to the benefit of ESC at all and will only serve to line Plaintiff's own pockets *at the expense of ESC.*

3. The Relative Magnitude of the Plaintiff's Personal Interests As Compared To His Interest In the Derivative Action Itself.

As set forth in the Perlman Aff. and above, Plaintiff currently owns only approximately 19% of ESC's outstanding stock. BP, on the other hand, owns the remaining 81% of ESC's outstanding shares. Accordingly, even assuming *arguendo* Plaintiff's claims had any validity, which is expressly denied, substantially all the benefit of the relief afforded to ESC will inure to the benefit of BP. In contrast to this minor alleged interest in this case, Plaintiff has demonstrated that his primary and major interest is the personal one of securing a buy-out or individual relief on the individual claims he asserts against Perlman and BP herein. Additionally, as set forth above, Plaintiff has exhibited indifference to ESC's interest by threatening meritless litigation over its intellectual property that is in derogation of the Agreement between Perlman and Plaintiff, seeks remedies that will interfere with development and marketing of the Software, and will alienate one of ESC's most important customers. Based on the foregoing, Plaintiff's personal interests substantially outweigh any interest he has in pursuing derivative claims on behalf of ESC.

New York Courts have embraced the majority view that "a plaintiff who asserts substantial direct (whether as a representative of a class or individually) as well as derivative claims cannot adequately represent the interests of the corporation/limited partnership for purposes of the derivative action." *JFK Family Ltd. Partnership v. Millbrae Natural Gas*

Development Fund 2005, L.P., 21 Misc.3d 1102(A), 873 N.Y.S.2d 234, 2008 WL 4308289, *15 (N.Y. Sup. Sept. 16, 2008) (citations omitted); *Baker v. Andover Assoc. Management Corp.*, 30 Misc.3d 1218(A), 924 N.Y.S.2d 307, 2009 WL 7400085, *13 (Sup. Ct., Westch. Co. Nov. 30, 2009) ("courts have held that a plaintiff is an inappropriate representative for a derivative action if that plaintiff is asserting direct claims along with derivative claims."); *see also St. Clair Shores Gen. Employees Ret. Sys. v. Eibeler*, Case No. 06 Civ. 688, 2006 U.S. Dist. Lexis 72316, *23 (S.D. N.Y. Oct. 4, 2006) ("[c]ourts in [the Second] Circuit have long found that plaintiffs attempting to advance derivative and direct claims in the same action face an impermissible conflict of interest."); *Tuscano v. Tuscano*, 403 F.Supp.2d 214, 223 (E.D. N.Y. 2005) ("Any individual claims raised by a shareholder in a derivative action present an impermissible conflict of interest"); *Wall Street Sys., Inc. v. Lemence*, No. 04 Civ. 5299, 2005 WL 292744, at *3 (S.D.N.Y. 2005) (stating that an individual shareholder cannot simultaneously bring direct and derivative claims in the same action); *Ryan v. Aetna*, 765 F.Supp. 133, 136-37 (S.D. N.Y. 1991) (explaining that a plaintiff would be "subject to a conflict of interest in pursuing both direct and derivative claims" in the same action). Thus, where, as here, Plaintiff has muddled individual claims and derivative claims, the Complaint should be dismissed. *See Id.; see also Abrams v. Donati*, 66 N.Y. 2d 951, 953, 498 N.Y.S.2d 782 (1985) ("A complaint the allegations of which confuse a shareholder's derivative and individual rights will...be dismissed"); *Jones v. Citigroup, Inc.*, No. 570210/10, 28 Misc.3d 132(A), 958 N.Y.S.2d 61, 2010 WL 2944224 (App. Term, 1st Dep't July 27, 2010) ("Even assuming the fraud claim could otherwise be asserted by plaintiff as an individual claim, the intermingling of derivative and individual claims requires dismissal of the entire complaint." *citing Abrams,* 66 N.Y. 2d 951; *Balk v. 125 W. 92nd St. Corp.*, 24 AD 3d 193, 806 N.Y.S. 2d 31 (1st Dep't 2005); *Barbour v. Knecht*, 296 A.D. 2d 218, 743

N.Y.S. 2d 483 (1st Dep't 2002)).

Based on the foregoing, Plaintiff's personal interests outweigh his interests in pursuing the derivative claims -- as shown particularly by combining direct claims with his purported derivative claims -- and, thus, he is legally inadequate to represent ESC's interest.

4. The Plaintiff's Vindictiveness Toward Perlman, BP and ESC.

Plaintiff's vindictiveness towards Perlman, BP and ESC is demonstrated by all of his conduct over the past six months discussed above in Points B(1-3) and the Perman Aff. Without limitation, it is demonstrated by Plaintiff's disregard of express provisions in the Agreement authorizing BP to engage in the activity of which Plaintiff now complains, his indifference to the adverse consequences to ESC (the entity he seeks to represent) of the injunctive relief sought, including the loss of substantial revenue and interference with the development and marketing of the Software.

5. Plaintiff Is Not a Legally Adequate Representative Because He Has No Support From Shareholders He Purports To Represent.

As set forth above, Plaintiff is one of ESC's two shareholders, with BP being the other. BP does not support this action. In addition, both of the individuals holding options to purchase ESC shares-- Conor Laver and Jonathan Braman -- have indicated that they do not support Plaintiff's action in any way. Perlman Aff., ¶ 23.

* * *

Based on the foregoing, these factors, individually and collectively, establish plainly that Plaintiff is a legally inadequate derivative representative to maintain derivative claims on behalf of ESC and, thus, all such claims should be dismissed.

C. All Of Plaintiff's Claims Are, In Fact And Substance, Derivative In Nature

While Plaintiff purports to assert "direct" claims against Perlman and BP for alleged

breach of fiduciary duty and misuse of ESC's Software, those claims are in substance derivative in nature and cannot be asserted as directs claims by Plaintiff. Indeed, all of Plaintiff's claims (direct or derivative) are based upon allegations regarding BP's use (or misuse) of ESC's Software and diversion of assets and opportunity away from ESC. *See* Complaint at ¶¶ 98-120. These clams are derivative because any damages resulting from the alleged wrongful actions would flow to ESC and not to Plaintiff directly. *See Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1033 (Del. 2004) (whether a claim is direct or derivative depends "solely on the following questions: (1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of any recovery or other remedy (the corporation or the stockholders, individually)?"); *Benihana of Tokyo v. Benihana, Inc.*, 891 A.2d 150, 155, n.3 (Del. Ch. 2005) (holding that claims of unfair dealing, breach of fiduciary duty and self-dealing transactions were derivative and not direct), *aff'd on other grounds*, 906 A.2d 114 (Del. 2006); *see also Abrams v. Donati, supra*, 66 N.Y.2d at 953 (1985) (finding New York law to be consistent with Delaware and holding that "allegations of mismanagement or diversion of assets by officers or directors to their own enrichment, without more, plead a wrong to the corporation only for which a shareholder may sue derivatively but not individually"); *Fisher v. Big Squeeze (N.Y.), Inc.*, 349 F. Supp.2d 483, 488-89 (E.D.N.Y. 2004) ("New York courts have held that, on a claim for breach of fiduciary duty, the fact that a corporation is closely held and the defendant fiduciaries own a large share does not provide a basis for departure from the requirement that the claim be brought derivatively.").

Here, the purported waste and diversion alleged by Plaintiff would only affect ESC as an entity, and not Plaintiff individually as a stockholder of ESC. Any relief that Plaintiff could possibly obtain from the claimed wrongful conduct would inure to the benefit of ESC alone and

not to Plaintiff individually. Accordingly, all of the claims asserted by Plaintiff are derivative and not direct and the direct claims should be dismissed.

D. Plaintiff's Claims Are Barred By Estoppel

"A shareholder is estopped to challenge a corporate policy which he or she affirmatively approved, or of which the shareholder had knowledge but to which no objection was interposed." *Winter v. Bernstein*, 149 Misc.2d 1017, 1020, 566 N.Y.S.2d 1012(Sup. Ct., N.Y. Co., 1991) *citing Diamond v. Diamond*, 307 N.Y. 263, 120 N.E. 2d 819 (1954); *Kranich v. Bach*, 209 App. Div. 52, 204 N.Y.S. 320 (1st Dep't 1924); *Jacobson v. VanRhyn*, 127 A.D. 2d 743, 512 N.Y.S. 2d 135 (2d Dep't 1987); *Greenberg v. Acme Folding Box Co., Inc.*, 84 Misc. 2d 181, 374 N.Y.S. 2d 997 (Sup. Ct. Kings Co. 1975); *Wellington Bull & Co., Inc. v. Morris*, 132 Misc. 509, 513, 230 N.Y.S. 122 (Sup. Ct., N.Y. Co. 1928). This is especially true in a closely held corporation like ESC:

> Furthermore, it is to be noted that this is a family corporation, and it is a fair inference that the members knew each other intimately and presumably had a more intimate knowledge of the corporation and its affairs than would be the case in a large corporation where the stockholders are widely scattered and know nothing of what is transpiring. All of the stockholders are chargeable with notice of what takes place at meetings of the stockholders regularly convened, whether they appear or not.

Kranich, 209 App. Div. at 54.

Here, as set forth above and in the Perlman Aff., Plaintiff was one of only two shareholders, officers and directors of ESC from the time of its formation in February 2010 to the time he resigned. In addition, Plaintiff had equal voting rights with BP from its inception until the time he resigned. In those capacities, Plaintiff is charged with knowledge of how ESC conducted its business. Yet, during this period, Plaintiff never once objected, protested or complained about BP's use of the Software or BP's role in providing services to ESC. Perlman

Aff., ¶ 11. Indeed, any such objection, protest or complaint would be in derogation of the parties' Agreement that expressly provided for BP being a customer of the Software and providing technical, marketing and sales support to ESC. *Id.* at ¶ 4. Defendants relied on Plaintiff's acquiescence in the propriety of all of those activities by, inter alia, funding the development of the Software in an amount exceeding $650,000. *Id.* at ¶ 14. Accordingly, Plaintiff should be estopped from maintaining this action by his own participation in, acquiescence and consent to the actions taken by the closely held business for a substantial period of time.

CONCLUSION

For the foregoing reasons, Defendants Perlman, BP and ESC respectfully request that the Court grant this motion to dismiss this action in its entirety, along with such other and further relief as the Court deems necessary and proper.

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