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Matter of Ryan (Integra Networks Inc.)
2013 NY Slip Op 51030(U)
Decided on June 11, 2013
Supreme Court, Albany County
Platkin, J.
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Decided on June 11, 2013

Supreme Court, Albany County

In the Matter of the Application of Eugene W. Ryan, TRUSTEE OF THE SARAH A. RYAN 2503(C) TRUST and PAUL RYAN, Petitioners, For the Judicial Dissolution of Integra Networks, Inc., Respondent, - and - DAVID PRESCOTT and MELISSA PRESCOTT, Respondents.

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Richard M. Platkin, J.

Petitioners Eugene W. Ryan, as Trustee of the Sarah A. Ryan 2503(c) Trust (the "Trustee" and "Trust" respectively), and Paul Ryan ("Ryan") move pursuant to Business Corporation Law ("BCL") § 1116 for an order granting them leave to voluntarily discontinue this proceeding. Respondents Integra Networks, Inc. ("Integra"), David Prescott and Melissa Prescott oppose the motion and cross-move for an order: (1) vacating any temporary restraints issued in this proceeding; and (2) granting respondents the rights to purchase the Trust's shares of Integra pursuant to BCL § 1118 in accordance with their fair value as of August 11, 2011. Further, in the event the Court denies the requested BCL § 1118 relief, Integra seeks to ensure that the dismissal of this proceeding shall be with prejudice. Petitioners oppose the cross-motion.

BACKGROUND

In their verified petition, petitioners allege six causes of action: (1) judicial dissolution of Integra pursuant to BCL § 1104-a; (2) return of assets pursuant to BCL § 626; (3) inspection of books and records pursuant to BCL § 624; (4) judicial dissolution of Integra pursuant to BCL § 1104; (5) indemnification of Ryan under Integra's by-laws; and (6) payment to Ryan of a certain accrued bonus he allegedly is due. According to the verified petition, David Prescott is the owner of 51.25% of the voting stock of Integra, and the Trust is the owner of the remaining 48.75%.

The petition was brought on by an Order to Show Cause ("OTSC") dated August 12, 2011. The signed OTSC (Connolly, J.) included a temporary restraining order that, among other things, prohibited the amendment of Integra's by-laws to add directors or to otherwise diminish the Trust's shareholder rights. During the pendency of the application, Gregory Streeter commenced a third-party action by Order to Show Cause dated October 24, 2011 that sought specific performance of an alleged barroom agreement granting Streeter a five percent ownership interest in Integra. Streeter's request to join the two cases was granted upon consent. By Order to Show Cause dated November 13, 2011, petitioners then sought additional injunctive relief against Prescott and Integra.

Following submission of the foregoing applications, Prescott advised the Court in writing of his intention to withdraw his opposition and to join in so much of the petition as sought the judicial dissolution of Integra based upon director deadlock under BCL § 1104. In response, the Trustee advised that it wished to withdraw without prejudice this cause of action on the ground that the Trust holds less than fifty percent of Integra's outstanding shares. The Trustee further [*2]advised that he was not withdrawing the Trust's claim for dissolution under BCL § 1104-a and suggested that prompt resolution of Streeter's claim to an ownership interest in Integra may facilitate resolution of that issue and the numerous other issues raised by this proceeding. Ryan joined in the Trust's request for a judicial determination of Streeter's claim, but declined to withdraw his cause of action under BCL § 1104. Both the Trust and Ryan further requested that the temporary relief previously granted in the Order to Show Cause dated August 12, 2011 remain in effect pending the resolution of Streeter's claim.

In a Decision & Order dated March 14, 2012, the Court accepted the Trustee's withdrawal of the cause of action for dissolution under BCL § 1104. The Court further ruled that Ryan could not maintain such a cause of action in his own right because he is not a fifty

percent shareholder of Integra. The Court also decided that "prompt determination of Streeter's claim to a five percent ownership in Integra may: provide clarity regarding the control of Integra; potentially facilitate a consensual resolution of some or all of the issues raised in this proceeding; establish which party or parties may pursue a petition for dissolution under BCL § 1104; and allow the Court to fully assess whether and to what extent to which dissolution would benefit Integra's shareholders." Finally, the Court directed that the temporary restraints of the August 12, 2011 OTSC remain in effect.

Following joinder of issue and expedited disclosure, a trial on Streeter's claim was held before the Court. In a Decision & Order dated February 14, 2013, the Court rejected Streeter's claim to an ownership interest in Integra.

The Court then wrote the parties on or about February 19, 2013 to advise of its intention to schedule a conference in this proceeding. The Court stated that prior to scheduling such conference, it was "requesting that counsel and their clients meet and confer in good faith in an effort to settle the outstanding litigation." While recognizing that "prior settlement efforts have been unsuccessful", the Court expressed the view that the parties "would be well served by resolving their disputes concerning Integra without the need for further judicial intervention." Ultimately, additional settlement efforts proved unsuccessful, and the instant motion practice ensued.

THE PARTIES' ARGUMENTS AND CONTENTIONS

In arguing that the application for leave to voluntarily discontinue this proceeding should be granted, petitioners embrace the statement made in the Court's February 19, 2013 correspondence, which urged the parties towards a business solution of their differences. Petitioners' motion papers further observe that no other parties to this proceeding have asserted any claims or counterclaims, and respondents did not exercise a right of election pursuant to BCL § 1118 within the period in which they could do so as of right..

In opposition to the motion and in support of the cross-motion to compel a buy-out of the Trust's minority interest pursuant to BCL § 1118, Integra argues that while the company is viable and healthy, its corporate governance has been rendered dysfunctional due to the ongoing animosity and dissension between Prescott and Ryan, the corporation's two directors. In an affidavit submitted in support of Integra's filing, Prescott emphasizes the

inability of the board of directors to transact business unrelated to litigation matters. According to Prescott, "there is [*3]clear distrust" between himself and Ryan that leaves them unable to "work or exist together anymore" (Affidavit of David Prescott, ¶¶ 7-19). And the same holds true for the relationship between Prescott and the Trust, since, "it is clear that there is really no distinction between Ryan and the Trust. They are one and the same" (*id.* ¶ 26).

The solution, according to Prescott and Integra, is for the Court to grant the cross-motion under BCL § 1118 so as to allow respondents to purchase the Trust's shares at their value as of August 11, 2011, the day prior to commencement of this proceeding. In this connection, Prescott emphasizes that Ryan would receive a fair price for his shares and Integra would be free from the "threat of future acrimony, litigation and Dissolution Proceedings" (*id.* ¶ 28).

Integra further argues that petitioners' motion for leave to discontinue is a strategic device that would only lead to further future litigation. According to counsel, petitioners' motion represents "a disingenuous attempt by the Trust (and Ryan) to reset' the valuation date" governing a BCL § 1018 election." Indeed, counsel argues that petitioners' papers are devoid of any assurance that the petitioners will not simply recommence a new dissolution proceeding after Prescott proceeds with his stated intention of calling a shareholder's meeting to reorganize the board of directors and remove Ryan as a director and officer. With regard to the issue of timeliness, Integra argues that the Court should exercise its discretion to allow a late election due to the unique circumstances of this case, including the "effective stay" of this proceeding while Streeter's claim to an ownership interest in Integra was adjudicated. Addressing the prospect that the Court may decline to allow an untimely BCL § 1118 election, Integra argues in the alternative that petitioners' motion should be granted, but only with the clear understanding that the dismissal is with prejudice and encompasses all claims that were or could have been raised in this proceeding.[FN1]

In further support of petitioners' motion and in opposition to the cross-motions, the Trustee submits a supplemental affidavit in which he offers the following averments:

The Trust is not an active participant in the business of Integra. Its ownership interest in Integra is its primary asset, and it holds its shares for the benefit of Sarah A. Ryan. While it originally was intended that Paul Ryan would serve as the Trust's representative with regard

to the management of Integra, that objective is no longer possible. Due to the continuing conflict between Prescott and Paul Ryan, the Trust has determined that its efforts are best served by the discontinuance of any efforts to ensure Paul Ryan's continued participation in the management of Integra (Aff. of Eugene Ryan, ¶ 10).

The Trustee further emphasizes that the Trust has not interfered with Integra's management, and that the instant application is being made by the Trustee solely in his role as a responsible fiduciary protecting the interests of the Trust and its beneficiary. Notably, petitioners' reply papers do not take issue with Integra's request that any voluntary discontinuance of this proceeding be with prejudice.

Both the Trustee and Ryan further assert that the untimely BCL § 1118 election [*4] represents an inappropriate effort by respondents to obtain a windfall from the significant appreciation of Integra during the pendency of this litigation. Ryan submits a supplemental affidavit that emphasizes Integra's growth in revenues throughout the litigation and his alleged contribution to that growth, including the identification of a purchaser willing to pay more than $10 million for the company. Ryan further argues that adopting respondents' position would provide them with an inequitable windfall.

Finally, Integra replies that respondents were not "dilatory" in exercising their BCL § 1118 election rights, though the company acknowledges that neither respondent "technically elected the BCL § 1118 remedy within 90 days of the filing of the Dissolution Petition." Integra further maintains that its election rights should not be denied merely because the company increased in value during the litigation. And Prescott insists that petitioners brought this proceeding in bad faith and are the ones seeking a windfall from the success of Prescott's efforts at Integra over the two years.

ANALYSIS

The motion and cross-motions implicate two sections of the BCL that establish means by which a dissolution proceeding may be terminated without an adjudication of the claim for dissolution.

The motion for voluntary discontinuance is made pursuant to BCL § 1116, which authorizes discontinuance of a "special proceeding for the dissolution of a corporation . . .

when it is established that the cause for dissolution did not exist or no longer exists." Upon such a showing, the Court may exercise its discretion to authorize discontinuance of the proceeding "upon terms and conditions, as the court deems proper" (CPLR 3217 [b]; *see Matter of Astoria Sports Complex, Inc.*, 5 AD3d 681, 681 [2d Dept 2004]). A voluntary discontinuance generally is without prejudice, but a court may order a discontinuance with prejudice in special circumstances, including cases where the substantial rights of another party would be adversely affected (*see* CPLR 3217 [c]; *Wells Fargo Bank, N.A. v Fisch*, 103 AD3d 622 [2d Dept 2013]; *Brenhouse v Anthony Indus.*, 156 AD2d 411 [2d Dept 1989]).

Respondents' cross-motions are made pursuant to BCL § 1118, which allows the corporation or majority shareholders to respond to a claim for dissolution under BCL § 1104-a by making a binding election to purchase the petitioner's shares at their fair value. Such an election may be made as of right within ninety days after the filing of the dissolution petition or at such later time as the Court in its discretion may allow (BCL § 1118 [a]). The fair value of the corporation shall be determined as of the day prior to the date on which such petition was filed (*id.* [b]). "The buyout election accommodates the interests of the respective parties in ensuring the continued functioning of the business, while also protecting the financial interest of the shareholders and creditors"(*Ferolito v Vultaggio*, 99 AD3d 19, 25-26 [1st Dept 2012] [internal quotation marks omitted]).

In considering whether "the cause for dissolution . . . no longer exists" (BCL § 1116), the Court begins by examining the allegations of the petition, which fall into two general categories. First, petitioners allege that Prescott has wasted or diverted Integra funds by, *inter alia*, over-billing Integra for inventory (Petition ¶¶ 23-25), over-billing Integra for airplanes and related expenses (*id.* ¶¶ 26-33), acquiring the 4 Airline Drive property (*id.* ¶¶ 34-42), engaging in interested financial transactions involving Cable Acquisition Company, LLC and CNC [*5]Microtech, Inc. (*id.* ¶¶ 43-48) and using Integra funds for personal expenses (*id.* ¶¶ 49-53). The second category of grievances concern the role of Ryan in the company and the alleged frustration of petitioners' reasonable expectations. Specifically, the petition takes issue with Prescott's efforts to enlarge the board of directors (*id.* ¶¶ 55-57), divest Ryan from having input, direction and control over Integra (*id.* ¶¶ 57-58), the suspension of Ryan as an officer of Integra (*id.* ¶¶ 60-61) and the failure to pay Ryan his accrued bonus (*id.* ¶¶ 103-105).

If the waste and diversion claims were voluntarily discontinued with prejudice, these

potential causes for dissolution would no longer exist. A discontinuance with prejudice would represent a binding election by petitioners to abandon any claims of wrongdoing by Prescott and Integra with respect to the transactions and occurrences that form the basis of the Petition, even if based upon different legal theories or seeking different remedies. In contrast, a voluntary discontinuance without prejudice would leave these potential grounds for dissolution in existence and leave respondents facing the prospect of successive dissolution actions, which would substantially prejudice them. Likewise, any claim concerning Ryan's role in the management and affairs of Integra would no longer exist following discontinuance with prejudice. And going forward, the Trustee has squarely and unequivocally renounced under oath "any efforts to ensure Paul Ryan's continued participation in the management of Integra" (Affidavit of Eugene Ryan, ¶ 10). Based upon the foregoing, the Court is satisfied that petitioners have established that the causes for dissolution of Integra would no longer exist following a voluntary discontinuance with prejudice, thereby allowing the Court to exercise its discretion under BCL § 1116 and CPLR 3217 (c) to authorize such a discontinuance.

In exercising this discretion, the Court must consider respondents' cross-motions, which propose to terminate this proceeding through a buy-out of the Trust's shares in Integra. As respondents did not make a BCL § 1118 election by November 10, 2011, ninety days after the filing of the instant Petition, the decision whether to allow an election rests in the Court's sound discretion.

In support of their contention that leave for voluntarily discontinuance under BCL § 1116 should be denied and a late election under BCL § 1118 permitted, respondents cite and discuss *Matter of Musilli* (134 AD2d 15 [2d Dept 1987]), the only reported decision to address the interplay between the two statutes. In *Musilli,* the Second Department held that a petitioner for dissolution may not use voluntary discontinuance under BCL § 1116 as a device to circumvent a respondent's election of its statutory buy-out right under BCL § 1118 (134 AD2d at 19-20).

The Court does not find respondents' reliance on *Musilli* to be availing. In *Musilli*, the application for leave to voluntarily discontinue the dissolution proceeding came in response to respondent's timely election to purchase petitioner's shares (*id.* at 17-18). Here, in contrast, respondents made no attempt at a BCL § 1118 election until after the filing of petitioners' motion to discontinue, which came some 19 months after the commencement of

this proceeding. Moreover, respondents' attempt at election comes after Integra received a buy-out offer from a third party that assigns a value to the company substantially in excess of the value of the corporation immediately prior to commencement. Thus, insofar as petitioners are said to be guilty of invoking BCL § 1116 as a strategic tool for "resetting" the valuation date, respondents are equally guilty of strategically holding back their BCL § 1118 election until Integra's current value was substantially in excess of the value as of the commencement of this proceeding. [*6]

Further, *Musilli* concerned a corporation organized in a manner that gave the petitioner, a 35% shareholder, an effective veto over all shareholder and director actions (134 AD2d at 16). The present record discloses no reason why Prescott cannot proceed with his stated intention of amending Integra's by-laws, altering the composition of the corporation's board of directors and removing Ryan from the company — particularly in light of the Trust's explicit renunciation of any efforts to intervene in Integra's management or to secure or maintain a role for Ryan. Thus, this has not been shown to be a case where the denial of a BCL § 1118 remedy would adversely affect the corporation.

In reaching the foregoing conclusions, the Court is mindful of the unusual procedural circumstances of this action, particularly with regard to Streeter's third party action claiming an ownership interest in Integra. Moreover, the fact that a BCL § 1118 election comes in response to a BCL § 1116 application for leave to discontinue is not necessarily determinative. But respondents here took no overt steps towards a BCL § 1118 election during the critical ninety day period following the filing of the petition, and the issue of election was raised by respondents for the first time almost 21 months after the date of commencement and only in response to a lucrative buy-out offer from a third-party and a motion for voluntary discontinuance by petitioners.

Under all of the facts and circumstances of this case, the Court determines, in the exercise of its discretion, that it would be inequitable to require the Trust to sell its shares to respondents for their fair value as of almost two years ago where a dismissal with prejudice of this proceeding and the formal change in position by the minority shareholder have eliminated the causes of dissolution and there are no proven impediments to the successful operations of the corporation going forward. Accordingly, petitioners should be given leave to voluntarily discontinue this proceeding with prejudice, and respondents' cross-motion for a BCL § 1118 election should be denied.

In addition to its power to order that the discontinuance be with prejudice, the Court may further condition the granting of leave to discontinue "upon terms and conditions, as the court deems proper" (CPLR 3217 [b]). While *res judicata* will bar any claim arising out of the transactions and occurrences alleged in the petition, as well as any other claims that could have been litigated herein, the Court recognizes that the bulk of the petition concerns a claim for non-monetary relief: the dissolution of Integra. The Court can envision circumstances in which the effective functioning of Integra and the financial interests of the corporation's shareholders and creditors may be jeopardized by internal disputes and new litigation that might technically fall within the bar of claim preclusion. Accordingly, as a condition of granting petitioners' motion and ordering discontinuance of this proceeding, the Court reserves the right to apply the August 11, 2011 valuation date to any future BCL § 1118 election made in a BCL § 1104-a dissolution proceeding brought by petitioners where the grounds for dissolution were or could have been raised in this proceeding or the new proceeding effectively constitutes a foreseeable continuation of this proceeding.

Accordingly,[FN2] it is [*7]

ORDERED that petitioners' motion for voluntary discontinuance is granted in accordance with the foregoing; and it is further

ORDERED that the petition is dismissed with prejudice and without costs or fees; and finally it is

ORDERED that respondents' cross-motions are granted to the limited extent that any injunctions or restraints entered herein are hereby vacated and the foregoing dismissal is made with prejudice, and the cross-motions are denied in all other respects.

This constitutes the Decision & Order of the Court. The original Decision & Order is being transmitted to the Trust's counsel for filing and service; all other papers are being transmitted to the Albany County Clerk. The signing of this Decision and Order shall not constitute entry or filing under CPLR Rule 2220. Counsel is not relieved from the applicable provisions of that Rule respecting filing, entry and Notice of Entry.

Dated: Albany, New York

June 11, 2013

Richard M. Platkin

A.J.S.C.

Papers Considered:

Notice of Motion, dated March 14, 2013;

Affirmation of Donald T. Kinsella, Esq., dated March 14, 2013, with attached exhibits A-N;

Notice of Cross-Motion, dated May 15, 2013;

Affirmation of Peter A. Lauricella, Esq., dated May 15, 2013, with attached exhibits A-L;

Notice of Cross-Motion, dated May 15, 2013;

Affidavit of David Prescott, sworn to May 15, 2013, with attached exhibits A-H;

Affirmation of Donald T. Kinsella, Esq., dated May 22, 2013, with attached exhibits A-D;

Affirmation of F. Charles Dayter, Esq,. dated May 15, 2013, with attached exhibits A-N;

Reply Affirmation of Peter A. Lauricella, Esq., dated May 31, 2013, with attached exhibits A-D;

Reply Affidavit of David Prescott, sworn to May 31, 2013, with attached exhibit A;

Reply Affirmation of F. Charles Dayter, Esq., undated, with attached exhibits A-C.

Footnotes

Footnote 1: Prescott offers similar arguments and proof in the submissions filed in connection with his own opposition to the motion and his separate cross-motion.

Footnote 2: The Court has considered the parties' remaining contentions, but finds them unavailing or unnecessary to disposition of the instant motions.

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