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

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SBE 44 WALL, LLC and BARUCH 44 WALL, LLC,

Index No.: 654038/2012

Plaintiffs,

-against-

NEW 44 WALL STREET, LLC and KOMMERSIELLA FASTIGHETER IN NY 3 CORP and PAUL ELLIOTT,

Defendants.

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MEMORANDUM OF LAW IN OPPOSITION OF DEFENDANTS' MOTION TO DISMISS

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Cases **Page**

Statutes

INTRODUCTION

Plaintiffs commenced this action for equitable relief, consistent with leading case law from the Court of Appeals, authorizing a minority member of a limited liability company to challenge prejudicial, self-serving, unauthorized, or fraudulent actions by the majority member. The first paragraph of the Complaint identifies this authority: *Walter J. Schloss Associates v Arkwin Industries*, 61 N.Y. 2d 700 (1984), and *Hall v Wood Wentworth*, 2011 N.Y. Slip Op 30631(U) (Supreme Court, Nassau Cty. 2011).

In an attempt to avoid this established law and Plaintiffs' clear right to seek equitable relief for their misconduct, Defendants Kommersiella Fastigheter in NY 3 Corp. ("KFS") and its principal, Defendant Paul Elliot ("Elliot") present this baseless motion to dismiss. KFS and Elliot seek to profit from a "squeeze out" merger, deprive Plaintiffs' of their substantial investment and equity in real estate, and unreasonably limit Plaintiffs to an appraisal proceeding of limited liability company member interests.

The motion to dismiss has no basis in fact or law. KFS and Elliot are engaged in a scheme to merge 44 Wall, LLC ("44 Wall") into New 44 Wall, LLC ("New 44 Wall") (the "Merger") for no legitimate purpose. As alleged in great detail in the Verified Complaint, the Merger was effected in violation of 44 Wall's Operating Agreement, and for no purpose other than to eliminate Plaintiff, Baruch 44 Wall, LLC's and Plaintiff, SBE 44 Wall, LLC's valuable 21.8% minority membership interest in 44 Wall. In short, KFS and Elliott are engaged in theft: they purported to use their power as managing member to cancel Plaintiffs' valuable minority membership interests for no consideration. Accordingly, Plaintiffs dissented from the Merger and now seeks equitable remedies.

Consistent with a squeeze out, Defendants never intended to compensate Plaintiffs. They connived to rush to Court with an appraisal proceeding ("Special Proceeding" Index No. 652768/2012) to obtain some form of seeming Court-approval for their scheme. They alleged that Plaintiffs should be paid "zero" and sought a Court order to that effect. Plaintiffs herein are respondents in that proceeding. Defendants deprived Plaintiffs of the alleged appraisals and documents establishing value of the limited liability interests. Plaintiffs requested discovery in the Special Proceeding, which KFS and Elliot opposed. Plaintiffs have moved to stay or dismiss the maliciously-conceived Special Proceeding.

Plaintiffs bring this plenary action to adjudicate their equitable claims to, *inter alia*, set aside the Merger, enjoin the contribution of further assets to New 44 Wall and divestiture of assets from 44 Wall, enjoin the recordation of a deed transferring any real estate between New 44 Wall and 44 Wall, direct the Defendants to execute and file a termination of the Agreement of Merger, direct Defendants' specific performance of the Operating Agreement, and impress a constructive trust upon the membership interests and real estate of New 44 Wall. Ancillary to this broad equitable relief, this action seeks money damages for Defendants' fraud and breach of fiduciary duty.

Defendants, ignoring the Court of Appeals' explicit approval, attempt to avoid being before a Court of Equity. They attack this action on a bevy of inapplicable procedural grounds. They falsely argue that "documentary evidence" contradicts the allegations in the complaint. In point of fact, their documentary evidence consists of nothing more than unproven and false allegations that failed to secure a judgment years ago in a prior 2009 action that was ultimately settled. Finally, they argue that Plaintiffs cannot bring this action in their individual capacities,

even though Defendants breached fiduciary duties they owed to Plaintiffs individually as shareholders, not to 44 Wall.

This action is specifically authorized by Business Corporation Law § 623, Limited Liability Company Law 1002(g), and every decision interpreting these statutes. Defendants fail to address this authority in their moving papers, and in sum, fail to establish why this Court should not hear Plaintiffs' meritorious equitable claims.

ARGUMENT

I. THIS PLENARY ACTION IS NOT DUPLICATIVE OF THE SPECIAL PROCEEDING

Defendants argue that this plenary action is duplicative of the Special Proceeding because Plaintiffs' claims herein can be brought as counterclaims in the Special Proceeding. (Def. Br. p. 8) This argument fails both legally and practically.

Practically, Plaintiffs' claims require discovery, which is why Plaintiffs have brought this plenary action. Plaintiffs herein (Respondents therein) moved for discovery in the Special Proceeding. (Resp. Mem. of Law in Support of Mtn. to Dismiss, Dated Nov. 9, 2012 p.18) Defendants opposed it, arguing that discovery must be "limited... to the valuation of the fair value of the shares." (Resp. Opp. Br. to Motion to Dismiss p. 14) Thus - to put Defendants' arguments together - they are arguing that there should be no discovery on Plaintiffs' causes of action in the Special Proceeding, and that there should be no discovery in this plenary action either. Defendants are not actually offering a solution to the Court – they are simply trying to strip Plaintiffs of their right to adjudicate their claims.

Legally, Defendants' argument fails as well. The Business Corporation Law states that any shareholders dissenting from a merger may "bring or maintain an appropriate action to obtain relief on the ground that such corporate action will be or is unlawful or fraudulent as to

him." Business Corporation Law § 623. The appellate decisions interpreting this provision uniformly hold that this "appropriate action" is an action for primarily equitable relief, where ancillary monetary damages may also be demanded.

In *Walter J. Schloss Assoc. v Arkwin Indus.*, Inc., 61 NY2d 700 (1984), for example, the Court of Appeals overturned a ruling of the Second Department, adopting the reasoning of the Second Department's dissenting opinion by Justice Mangano. In so doing, the Court of Appeals held that "the right of appraisal is the exclusive remedy for dissenting stockholders, except that (and that is a narrow exception) an action or proceeding in the nature of a suit in equity will be permitted as an appropriate action to attack fraudulent or illegal corporate activity." *Walter J. Schloss Assoc. v Arkwin Indus., Inc.*, 90 A.D.2d 149, 158 (2d Dep't 1982) rev'd, 61 N.Y.2d 700 (1984). Though "there must be a request for equitable relief which... must be the primary relief sought" money damages are also available so long as they are "ancillary or incidental to such equitable relief." *Id.* citing *Breed v Barton*, 54 N.Y.2d 82 (1981)

Again, in *Klurfeld v Equity Enterprises, Inc.*, 79 A.D.2d 124 (2d Dep't 1981), majority stockholders of a corporation concocted a merger to freeze out the minority shareholders. The minority shareholders brought an action for primarily equitable relief. The Appellate Division, applying BCL § 623, upheld the action.

Trial Courts have followed this reasoning as well in permitting plenary actions for primarily equitable relief to proceed under similar facts. In *Hall v. Wood Wentworth*, Ltd., 2011 WL 997180 (Sup. Ct. Nassau Cty 2011), in the context of a limited liability company, the Supreme Court applied Justice Mangano's reasoning in *Schloss*. The Court found that, aside from an appraisal proceeding to value a minority interest in the company, an "appropriate action" seeking primarily equitable relief was warranted.

Within the rule articulated by the BCL and confirmed by *Schloss*, *Hall* and *Klurfeld*, this action asserts seven claims. Six are for equitable relief seeking to, *inter alia*, set aside the Merger, enjoin the contribution of further assets to New 44 Wall and divestiture of assets from 44 Wall, enjoin the recordation of a deed transferring any real estate between New 44 Wall and 44 Wall, direct the Defendants to execute and file a termination of the Agreement of Merger, direct Defendants' specific performance of the Operating Agreement, and impress a constructive trust upon the membership interests and real estate of New 44 Wall. The Complaint also seeks equitable relief in the form of a declaratory judgment and an accounting. Ancillary to this sweeping equitable relief, this action seeks money damages for Defendants' fraud and breach of fiduciary duty. As such, this action is specifically authorized by not only statutory, but also judicial precedent. It is not "duplicative" of the Special Proceeding.

II. THE LIMITED SPECIAL PROCEEDING DOES NOT PRECLUDE THIS PLENARY ACTION

Defendants argue that the Special Proceeding should bar this plenary action because the Special Proceeding was filed first. They rely on CPLR 3211(a)(4), which states:

> A party may move for judgment dismissing one or more causes of action asserted against him on the ground that...there is another action pending between the same parties for the same cause of action in a court of any state or the United States; the court need not dismiss upon this ground but may make such order as justice requires

This argument fails for two independent reasons. First, there is no action pending between the same parties for the same cause of action. Second, if any index number should be dismissed, it should be the limited, Special Proceeding, not this plenary action.

A. There is No Action Pending Between the Same Parties for the Same Cause of Action

CPLR 3211(a)(4) requires that there be "another action pending between the same parties for the same cause of action." This is clearly not the case here. There is no other action pending between the parties for the same cause of action. The Special Proceeding, though commenced prior to the instant plenary action, is not an action at all. To the contrary, it is a limited special proceeding that will only adjudicate a single, limited issue: the value of the minority shareholders' stake in 44 Wall.

The court in *Alegria v Metro Metal Products, Inc.*, 29 Misc.3d 591 (Sup. Ct. 2010) faced a similar situation. A worker filed a special proceeding for pre-action disclosure against his employer seeking an inspection of machinery that had allegedly caused injury to the worker. He then filed a plenary action against the lawyer seeking damages for spoliation of evidence. When faced with a motion to dismiss the new plenary action, the court found that the two cases were related. Nonetheless, they sought different relief and so were not "for the same cause of action" as required by CPLR 3211(a)(4). The court denied the motion to dismiss.

There is only one cause of action in the Special Proceeding: an appraisal. There is no such cause of action at issue here. This plenary action seeks primarily equitable relief: an injunction, a declaratory judgment and specific performance of the Operating Agreement. Moreover, the factual issue in the limited Special Proceeding is the dollar value of the Minority Members' ownership interest. That is not at issue in this special proceeding. To be sure, the Defendants here may make it an issue by counterclaiming, but this only emphasizes why this Plenary Action is preferable to the limited Special Proceeding, and demonstrates why this Plenary Action should not be dismissed: All causes of action may be adjudicated here, in this

special proceeding. In no way does the instant motion satisfy the "same cause of action" requirement of 3211(a)(4). For this reason alone, the Court should deny it.

B. Justice Requires that the Limited Special Proceeding be Dismissed, not this Plenary Action

CPLR 3211(a)(4) does not require the dismissal of any action, let alone the subsequent action. To the contrary, it permits the court to make "such order as justice requires." Permitting the limited Special Proceeding to determine the rights of the parties instead of this plenary action would not do justice. It would ignore the abundance of relevant, determinative facts that will be raised in this action. Specifically, the Majority Shareholders have brought the limited special proceeding to appraise the Minority Shareholders' rights at zero dollars, eliminating without consideration their 21.8% interest in 44 Wall. The factual and legal issues in this plenary action, will demonstrate their myriad breaches of fiduciary dutyand contractual duties as parties to their Operating Agreement. There would be no opportunity to assert these claims in the limited Special Proceeding. Specifically, it will demonstrate that the Merger triggering the limited special proceeding was a sham, concocted to steal Plaintiffs' equity interest in the company. Thus, the factual and legal findings in this broad plenary action will determine whether the limited special proceeding ought to even move forward in the first instance.

Courts regularly favor a complete adjudication of the merits of a dispute over the limited determination reached in a special proceeding. Indeed, Defendants' own cases make this clear. In *Maroney v. Hawkins*, like the case at bar, the same parties brought a limited special proceeding, and then subsequently brought a broader plenary action. The court refused to dismiss the plenary action, instead choosing to dismiss the limited special proceeding, even though the proceeding was filed first. The court chose to let the action proceed that was broader

in scope – the action that would permit the parties to fully litigate their claims. This is the opposite of what Defendants are demanding the court do in the case at bar.

Likewise, in *Clarity Connect v AT&T*, also cited by Defendants, an internet service provider demanded a declaratory judgment against a vendor setting the dollar amount it owed to the client. The vendor then filed a broader action demanding a money judgment against the internet service provider. The trial court dismissed the prior-filed action seeking the limited declaratory judgment. The Third Department affirmed, finding that the broader plenary action should proceed instead of the limited declaratory judgment action, because the plenary action permitted all of the parties to fully litigate their claims.

Defendants remaining authorities, *Chang v Zapson*, and *North Fork Bank v Grover*, do not dismiss a subsequent plenary action in favor of a prior limited special proceeding. To the contrary, they affirm the dismissal of a plenary action because there was a prior pending *plenary action*, not a prior pending special proceeding, asserting the same cause of action as the subsequent action.

In *Clarity Connect*and in *Maroney,* just as in the case at bar, dismissing the broader action would strip one of the litigants of the right to adjudicate its dispute. It would allow one party to obtain relief in the limited proceeding that the plenary action might reveal to be unwarranted. Specifically, here, it would permit the Defendants to use the Merger to freeze out the Plaintiffs before this Plenary Action can demonstrate that the Merger was a sham. Plaintiffs herein, the Respondents in the Plenary Action, have already moved to dismiss the Special Proceeding for just this reason. That motion is fully briefed and currently before the Court.

III. DEFENDANTS HAVE NOT "CONCLUSIVELY ESTABLISHED" THEIR RIGHT TO DISMISSAL ON THE BASIS OF "ESSENTIALLY UNDENIABLE" DOCUMENTARY EVIDENCE

The standard on a motion to dismiss based on CPLR 3211(1) is critical in this case. Under CPLR 3211 (a)(1), a dismissal may be granted only if the documentary evidence submitted by the movant "conclusively establishes a defense to the asserted claims as a matter of law." *Held v Kaufman*, 91 N.Y.2d 425, 671 N.Y.S.2d 429 (1998). The contents of the documents themselves must be "essentially undeniable". *Fontanetta v Doe*, 73 A.D.3d 78, 85 (2d Dep't 2010) citing *Matter ofCasamassima v Casamassima*, 30 A.D.3d 596 (2d Dep't 2006). For the purposes of CPLR 3211(a)(1), "documentary evidence" is a strict category, including "mortgages, deeds, and contracts." *Midorimatsu, Inc. v Hui Fat Co.*, 99 AD3d 680, 682 (2d Dept 2012) citing *Fontanetta*, 73 A.D.3d at85. Letter correspondence, such as those submitted herein by Defendants are generally not "documentary" under the rule. *See, e.g., Integrated Const. Services, Inc. v. Scottsdale Ins. Co.*, 82 A.D.3d 1160, 920 N.Y.S.2d 166 (2d Dep't 2011); *Granada Condominium III Ass'n v. Palomino*, 78 A.D.3d 996, 913 N.Y.S.2d 668 (2d Dep't 2010); *Frenchman v. Queller, Fisher, Dienst, Serrins, Washor&Kool*, LLP, 24 Misc. 3d 486, 884 N.Y.S.2d 596 (N.Y.CTY. 2009). Defendants herein have presented the court with no "essentially undeniable" documents that "conclusively establish" their right to dismissal, nor do Defendants explain how any of the documents they have submitted rebut any of the allegations in the Complaint.

The Complaint alleges that the Defendants concocted a merger between 44 Wall and New 44 Wall not for any legitimate purpose, but solely to eliminate Plaintiffs' valuable minority interest in 44 Wall. The Complaint alleges that the Merger was an act ultra vires, and invalid under the 44 Wall Operating Agreement. It alleges that Defendants failed to call the required meeting and vote of members prior to the Merger. The Complaint further alleges that the written

consent, executed solely by KFS, was void *ab initio*, and could not have duly authorized the Merger.

In rebuttal, Defendants insist that "It was the very actions of SE Wall and Baruch in misappropriating corporate assets which caused the dire financial condition of the Company when KFS assumed control." (Def. Br. p. 10). To support this position, Defendants do not present a judgment they secured against Plaintiffs for that misappropriation. They do not even present any evidence that such misappropriation occurred. To the contrary, they present only *allegations*: "KFS was compelled to institute [a 2009 action] against, inter alia, SE Wall and Baruch for their obvious failures to follow proper procedures in dealing with the Company and their misappropriation of corporate assets for themselves." (Def. Br. p. 9) And so, their argument goes, SE Wall and Baruch "cannot now contend that they did appropriate [sic] such assets for themselves as this issue was previously litigated against them in the [2009] action." (Id.)

In point of fact, KFS failed to secure a judgment – or any factual findings at all – against Plaintiffs in that 2009 action. As Defendants conceded by affidavit in the Special Proceeding, it was resolved pursuant to a settlement agreement. (Miltenberg Aff. Dated January 4, 2013 Ex. 1; Franzino Aff. Dated Jan. 9, 2013, ¶¶8-10) Defendants are presenting their unfounded allegations in the 2009 action as "evidence" to support more unfounded allegations in this action. This is a far cry from the "essentially undeniable" documents that Defendants are required to submit in order to "conclusively establish" their right to dismissal at this early stage.

First, Defendants have submitted an Order to Show Cause in the 2009 action, but this order only sets a briefing schedule. This order does not "conclusively establish" that defendants misappropriated corporate assets. In fact it does not even suggest it. *Second*, they have submitted an Agreement of Merger and Written Consent of Merger. These documents might

demonstrate that there was a merger, but it does not "conclusively establish" that the merger was not, as alleged, a sham. In fact, the documents undermine Defendants position, and suggest that the merger was illegitimate: the Written Consent's signature block was signed by a nonexistent "sole member" of 44 Wall. *Third*, they submit their own letters demanding capital calls, but do not explain how they conclusively establish that the capital calls were legitimate, and not part of a scheme to freeze out Plaintiffs. To the contrary, Plaintiffs' own letters in response to Defendants' letters (also submitted by Defendants) rebut each and every accusation contained in Defendants letters. None of these documents are "essentially undeniable", nor do they "conclusively establish" defendants right to dismissal.

IV. THE COMPLAINT CLEARLY PLEADS A CAUSE OF ACTION FOR FRAUD

To state a cause of action for fraud, a plaintiff must allege a representation of material fact, the falsity of the representation, knowledge by the party making the representation that it was false when made, justifiable reliance by the plaintiff and resulting injury. *Kaufman v Cohen*, 307 A.D.2d 113, 119 (1st Dep't 2003) citing *Monaco v. New York Univ. Med. Ctr.*, 213 A.D.2d 167, 169, 623 N.Y.S.2d 566, lv. denied 86 N.Y.2d 882, 635 N.Y.S.2d 944; *Callas v. Eisenberg*, 192 A.D.2d 349, 350, 595 N.Y.S.2d 775 (1st Dep't 1993). Alternatively, instead of an affirmative misrepresentation, a fraud cause of action may be predicated on acts of concealment where the defendant had a duty to disclose material information. *Id.* citing *Swersky v. Dreyer and Traub*, 219 A.D.2d 321, 326, 643 N.Y.S.2d 33 (1st Dep't 1996). Thus, where a fiduciary relationship exists, the mere failure to disclose may constitute actual fraud. *Id.* citing *Whitney Holdings Ltd. v. Givotovsky*, 988 F.Supp. 732, 748 (S.D.N.Y. 1997); and *American Baptist Churches v. Galloway*, 271 A.D.2d 92, 100, 710 N.Y.S.2d 12 (1st Dep't 2009).

The Complaint gives a detailed factual account of Defendants' misrepresentations and concealments. Among others, Defendants represented to Plaintiffs that they would manage 44

Wall for the benefit of its members, including its minority members and concealed from Plaintiffs their intention to cause a merger and to squeeze out Plaintiffs from 44 Wall and its ownership interest of the real estate and rental income. Defendants further concealed from Plaintiffs that they would lie in wait for a time when they could characterize Plaintiffs' minority interest in 44 Wall as worth "zero dollars" and freeze them out of the company for no consideration. As members of a closely-held company – especially as that company's managing member – Defendants owed Plaintiffs fiduciary duties Burnett v Pourgol, 83 A.D.3d 756, 757 (2d Dep't 2011). As set forth in *Kaufman*, *Whitney* and *American Baptist Church*, supra, these duties impose upon them an obligation to disclose this relevant, material information.As alleged in the Complaint, Plaintiffs reasonably relied on these misrepresentations and concealments by agreeing KFS' assumption of the role of sole managing member of 44 Wall and in entering into the Second Amendment to the Operating Agreement that gave Defendants broad control over the company.

Defendants, citing *East End Cement*, argue that the relevant information was not in Defendants' "peculiar knowledge" because Plaintiffs "were not denied access to corporate accounts and were given the appropriate financial documents and the appraisals." (Def. Br. p. 12) Defendants even annex appraisals to their moving papers. This argument misses the mark: The Complaint does not allege that Defendants concealed appraisals. The complaint does contain, however, abundant allegations that prior to the Merger, Defendants withheld financial documents and information to which KFS and Paul Elliot – as managing, majority members of 44 Wall – had sole access.

Defendants further argue: "The fact that SE Wall and Baruch have failed to annex an alternate appraisal showing that their interests were worth more than the zero propounded by

New Wall, demonstrates that there is no fraud here." (Def. Br. p. 13) It is difficult to understand why Defendants' submission of an appraisal to this court would insulate them from liability for acts that they undertook months and even years to the commissioning or submission of that appraisal. Stranger still is Defendants' conclusion that Plaintiffs' submission of their own appraisal would create a fraud claim where one would not otherwise exist. Neither proposition contradicts any element of a fraud cause of action. The appraisal is neither relevant nor persuasive. It is a red herring.

V. THE COMPLAINT CLEARLY PLEADS DIRECT, NOT DERVIATIVE, CLAIMS

Defendants argue that all of Plaintiffs' claims – save the fraud claim – are derivative claims for which, under New York law, demand must be made up on the board of directors of the company, or such demand must be futile. Both the Business Corporation Law and every appellate decision interpreting it has held that these very same claims are direct, not derivative.

A. Plaintiffs' Claims are Direct

Generally, a claim is direct, not derivative, where the alleged misconduct "effects a separate and distinct wrong to the plaintiff, which is independent of any wrong to the corporation" *Burnett v Pourgol*, 83 A.D.3d 756, 757 (2d Dep't 2011); see *Knox v. Estate of Sprague*, 293 A.D.2d 451, 739 N.Y.S.2d 644 (2d Dep't 2002).

For example, in *Lazar v Robinson Knife Mfg. Co., Inc.*, 262 AD2d 968, 969 (4th Dep't 1999) the managers of the company dissented from a transaction, brought an appraisal proceeding and also commenced a separate action alleging fraud, overreaching and breach of fiduciary duties by the individual defendants. The Appellate Division considered whether the action ought to be direct or derivative, and found that it was a direct action because "the complaint alleges that plaintiffs' ownership interest in defendant corporation was diminished because of the breach by defendants of their fiduciary duties... Because plaintiffs allege that

defendants breached a duty owed to them individually, this is not a derivative action brought on behalf of defendant corporation." *Id.* Likewise, here, the Complaint does not allege, and Plaintiffs are not seeking redress for, Defendants' violation of their fiduciary duties to the company. They are seeking redress for Defendants' violation of their independent fiduciary duties to themselves, as minority members of the company.

Again, in *Klurfeld v Equity Enterprises, Inc.*, 79 A.D.2d 124 (2d Dep't 1981), majority stockholders of a corporation concocted a merger to freeze out the minority shareholders from the corporation. The minority shareholders brought a direct action in their individual capacities (the parties were pled as *Klurfeld and Del Giorgio, Individually*) for primarily equitable relief.

Again, in *Venizelos v Oceania Maritime Agency, Inc.*, 268 AD2d 291 (1st Dep't 2000), the managing shareholder of the closely-held corporation "managed the business in a manner intended to divest plaintiffs... of their interests therein." The Appellate Division, First Department, found that "clearly, Defendant breached fiduciary duties he owed to plaintiffs independent of the duties he owed to the holding company... and the sole purpose and effect of his transactions with respect to the holding company... was to steal from plaintiffs." Likewise, the Complaint herein exhaustively details Defendants' scheme to steal Plaintiff's interests in 44 Wall. As the Complaint alleges at length, the Merger was a sham transaction concocted solely to divest Plaintiffs of their 21.8% of the company.

Again, in *Benedict v Whitman Breed Abbott & Morgan*, 282 AD2d 416, 418 (2d Dep't 2001) the Appellate Division held that "individual plaintiffs have standing to assert claims for diminution of the value of their stock" where"the wrongs alleged were not only wrongs to the corporations, but were violations of an independent fiduciary duty owed by the appellants to the plaintiff stockholders."

Finally, in *Bernstein v. Kelso & Co., Inc.*, 231 A.D.2d 314, 659 N.Y.S.2d 276 (1st Dep't 1997) The Appellate Division, First Department, held that a minority shareholder of a corporation had standing to bring a direct action for breach of fiduciary duty and inducing breach of fiduciary duty against the management of the corporation and a leveraged buy-out firm that purchased his stock in a subsidiary of the corporation. The complaint alleged that the management of the corporation secretly conspired to orchestrate a buyout with the firm at an unfairly low price, thereby breaching its independent fiduciary duty to the minority shareholder. Similarly, here, Plaintiffs are suing for Plaintiff's elimination of their valuable stake in the company, not for any damage Plaintiff might have caused to the company itself. Accordingly, the claims herein are direct, not derivative.

B. Even if Plaintiffs' Claims were Derivative, Demand would be Excused as Futile

Even if a claim is derivative, the plaintiff is not necessarily required to make a demand upon the board of the corporation. In the context of a corporation, if making such a demand would be futile, the doctrine of Demand Futility excuses the plaintiff from making one. A demand would be futile if either (i) a majority of the directors are interested in the transaction, or (ii) the directors failed to inform themselves to a degree reasonably necessary about the transaction, or (iii) the directors failed to exercise their business judgment in approving the transaction, then any demand would be futile, and the doctrine of Demand Futility excuses the Plaintiff from making one. *Marx v Akers*, 88 NY2d 189, 198 (1996). The same rule applies to managing members of limited liability companies as to directors of a corporation. *See, e.g., Segal v Cooper*, 49 AD3d 467 (1st Dep't 2008).

Curreri v Verni, 156 A.D.2d 420, 421 (2d Dep't 1989) is instructive. In *Curreri*, the defendants moved to dismiss, arguing that the plaintiffs' derivative claims required a demand on

the company's board. The Appellate Division affirmed the trial court's denial of the motion, noting that merely naming the company's managers as defendants is insufficient for a finding of futility. However, the complaint had alleged "that the appellants were in exclusive control of the corporation" and, as such, "set forth sufficient details from which it may be inferred that the making of a demand would indeed be futile."

Likewise, the Complaint alleges that Defendant KFS was in exclusive control of the corporation, and concocted the Merger to take for itself Plaintiff's valuable interests in 44 Wall. Transmitting a demand to the Corporation would be asking defendants to sue themselves for their own unlawful conduct. Thus, the Complaint clearly pleads that KFS was interested in the transaction. Under *Curreri* and the first prong of *Marx*, any demand made upon the company would be futile.

VI. PAUL ELLIOTT IS DIRECTLY LIABLE FOR HIS ACTIONS IN FREEZING OUT PLAINTIFFS FROM 44 WALL

The Complaint seeks to hold Paul Elliott individually liable for (i) his fraudulent misrepresentations to Plaintiffs, set forth in greater detail in Section IV, above, and (ii) his use of KFS and New 44 Wall to steal Plaintiffs' valuable minority interest in 44 Wall. Defendants do not distinguish between these two acts, and argue that both should be dismissed because the corporate form of KFS insulates him from liability for both.

Generally, a plaintiff seeking to pierce the corporate veil must show that complete domination was exercised over a corporation with respect to the transactions attacked, and that such domination was used to commit a fraud or wrong against the plaintiff which resulted in plaintiff's injury.*Matter of Morris v. New York State Dept. of Taxation & Fin.*, 82 N.Y.2d 135, 141, 603 N.Y.S.2d 807 (1993); see *TNS Holdings v. MKI Sec. Corp.*, 92 N.Y.2d 335, 339, 680 N.Y.S.2d 891 (1998). In addition, the corporate veil will be pierced to achieve equity, even

absent fraud, when a corporation has been so dominated by an individual or another corporation and its separate entity so ignored that it primarily transacts the dominator's business instead of its own and can be called the other's alter ego. *Matter of Island Seafood Co. v. Golub Corp.*, 303 A.D.2d 892, 893, 759 N.Y.S.2d 768 (3d Dep't 2003), quoting *Austin Powder Co. v. McCullough*, 216 A.D.2d 825, 827, 628 N.Y.S.2d 855 (3d Dep't).

The Complaint alleges that Elliott controlled, managed and directed KFS and New 44 Wall. It alleges that he used this control, management and direction to exercise complete domination over KFS and New 44 Wall in creating and consummating the sham Merger that divested Plaintiffs of their valuable minority interests in the company for his own benefit. Indeed, he is the only person who would have benefitted from this act, and is properly named as a defendant. His incorporation of KFS cannot insulate him from liability.

VII. THIS ACTION SHOULD NOT BE STAYED, AS IT MAY RENDER THE LIMITED SPECIAL PROCEEDING UNNECESSARY

Defendants argue, in the alternative to dismissal, that this plenary action should be stayed pending the determination of the Special Proceeding. They believe that the Special Proceeding "will determine all of the rights of the parties thereby eliminating any need to litigate" this plenary action. This is nonsensical.

As set forth in Section I, supra, Plaintiffs' maintaining of this plenary action is authorized by statute (BCL § 623(k)) and expressly approved-of by every case that has interpreted it. Delaying it in favor of a Special Proceeding will not "determine all of the rights of the parties." To the contrary, the Special Proceeding is a limited adjudication that can determine one – and only one – issue: the value of the minority members' shares in 44 Wall. If that value is determined, Plaintiffs claims herein will be remain unexamined. This plenary action, on the other hand, will be a broad investigation into the respective rights of the parties subsequent to the

Merger and the liability of the Defendants in freezing out Plaintiffs from 44 Wall. A limited special proceeding would not adjudicate any of these rights and remedies.

Most importantly, one of Plaintiff's primary equitable demands herein is to unwind the Merger that triggered the Special Proceeding. If this relief is granted, then there would be no dissent from the Merger, no need to appraise the minority interests in 44 Wall, and no need for the limited Special Proceeding. It would be entirely unnecessary. Adjudicating this plenary action first not only preserves the rights of the parties, it may do away with any need for further litigation over the value of the minority's shares.

CONCLUSION

Defendants have not carried their burden to "conclusively establish" their right to dismissal of this action on the basis of their documentary evidence. To the contrary, many of their own cases describe with particularity why this action is authorized, legally, and advisable, practically. Defendants' motion to dismiss should be denied.

Dated: New York, New York
February 19, 2013

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