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

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DANIEL KOCH and DEREK KOCH,

Index No. 650519/2014

Petitioners,

-against-

HC HOSPITALITY PARTNERS, LLC
PCG DGHP, LLC, and DUAL GROUPE
HOSPITALITY, LLC (nominally),

Respondents.

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PETITIONERS' MEMORANDUM OF LAW IN OPPOSITION TO MOTION TO DISMISS VERIFIED PETITION FOR JUDICIAL DISSOLUTION AND APPOINTMENT OF A RECEIVER

Petitioners Daniel Koch and Derek Koch (together, "Petitioners"), by and through their undersigned attorneys, respectfully submit this memorandum of law in opposition to the motion (the "Motion") of respondents HC Hospitality Partners, LLC ("HC"), PCG DGHP, LLC ("PCG") and Dual Groupe Hospitality, LLC (the "Company" and, together with "HC" and "PCG", "Respondents") to dismiss the Verified Petition for the judicial dissolution of, and the appointment of a receiver concerning, the Company (the "Petition"), pursuant to §§702 and 703 of the Limited Liability Company Law.

BACKGROUND

Briefly[1], the impetus for Petitioners' filing of their Petition for judicial dissolution of the Company is the readily apparent existence of substantial irreconcilable disputes and differences between the Company's "50/50" membership groups and the apparent financial unfeasibility of the

1 A detailed statement of the underlying facts relevant to the Motion is set forth in the accompanying Affidavit of Derek Koch, sworn to on March 31, 2014, submitted in opposition to the Motion (the "Koch Aff.").

Company. As a result thereof, it is not reasonably practicable to carry on the business of the Company as intended within the purview of §702 of the Limited Liability Company Law. Dissolution of the Company is the only appropriate remedy under the circumstances.

Specifically, it is not disputed that Petitioners hold a combined 50% ownership interest in the Company, which was formed in October 2012 for the purpose of operating and developing hospitality-related ventures such as restaurants, bars and/or nightlife venues. The remaining 50% is held by PCG (an entity owned/controlled by Michael Wainstein ("Michael") which holds 30% of the Company's membership interests) and HC (an entity owned/controlled by Andreas Huber ("Andreas") which holds 10% of the Company's membership interests). On or about October 12, 2012, the members entered into a written operating agreement (the "Operating Agreement").

Reflective of the substantially equal distribution of the Company's membership interests among its four members, the Company was always intended to be, and it was mutually understood by the members to be, a collaborative effort and was to be operated with the active involvement of all of the members (*i.e.*, there were no "passive" members, no members who were mere "stakeholders" and no members who held only nominal/*de minimis* membership interests). As such, although Michael and Andreas were designated as the "Managers" of the Company under the Operating Agreement, the unanimous approval of all of the members was required for certain enumerated "Major Decisions". In the absence of such unanimous consent, certain "Deadlock" protocols are triggered under the Operating Agreement. Along with the Operating Agreement, Petitioners, Andreas and Worth Capital LLC (an entity owned/controlled by Michael) entered into separate "Consulting Agreements" (together, the "Consulting Agreements") with the Company concerning each member's designated duties to be performed in furtherance of their collaborative operation of the Company as "independent contractors" and setting forth the manner and amount in which they would be

compensated for performing those duties on behalf of the Company.

Unfortunately, following the formation of the Company, it became apparent that the "Managers" of the Company (*i.e.*, Michael and Andreas) viewed Petitioners more like employees than their 50% co-owners of the Company which resulted in multiple disputes between Petitioners and Michael and Andreas concerning the Company's operations and outlook. By way of example, under Michael and Andreas' stewardship, the Company was generally unable and/or unwilling to pay its debt obligations as they came due, was unprofitable and lacked any real prospects of financial improvement, and was otherwise mismanaged. Throughout this time, the Company was not making any of the payments required to be made to Petitioners under their Consulting Agreements which raised tensions further between the two ownership groups. The infighting came to a head in September 2013 when HC and Worth Capital LLC made demands upon the Company for payment under certain alleged promissory notes which Petitioners were not previously aware of and the issuance of which would have constituted a breach of the Operating Agreement. It became apparent to Petitioners that Respondents were attempting to wrest full control of the Company away from Petitioners without any consideration therefor and without giving a second thought to their fiduciary duties to Petitioners as 50% co-owners of the Company. As such, Petitioners were left with no alternative but to part ways with Respondents.

Thereafter, and rather than trying to resolve the member disputes in conformity with or in adherence to the Operating Agreement, Respondents commenced an lawsuit against Petitioners asserting that Petitioners had breached the Operating Agreement and/or the Consulting Agreements and seeking money damages, as well as a permanent injunction restraining Petitioners from engagement in business activities competing with the Company(the "Action"). The commencement of the Action constituted a breach of the Operating Agreement as it constituted a "Major Decision"

requiring the approval of all of the members, which Respondents never sought or obtained. The allegations made and the relief sought by Respondents in the Action further evidences that the rift between the "50/50" ownership groups of the Company is vast and that Respondents only believe that the Operating Agreement applies when it suits their own, self-serving purposes.

Faced with the foregoing circumstances, and fearing the potential complete loss of any value or compensation on account of their extensive contributions to and work on behalf of the Company, Petitioners commenced this special proceeding by filing the Petition with this Court on February 17, 2014 seeking the judicial dissolution of the Company and the appointment of a receiver to protect the interests of *all* members of the Company. By way of the instant Motion, Respondents now seek to dismiss the Petition based upon Respondents' incorrect assertions that the Petition lacks evidentiary support and allegedly fails to sufficiently state a valid claim for judicial dissolution of the Company.

DISCUSSION

A. Standard on Motion to Dismiss for Failure to State a Cause of Action

CPLR §3211(a)(7) provides that a party may move the court for an order dismissing one or more causes of action asserted against it if the pleading fails to state a cause of action. In determining whether a pleading is sufficient to withstand a motion to dismiss pursuant to §3211 of the CPLR, the court is required to afford the pleading a liberal construction. *See Leon v. Martinez*, 84 N.Y.2d 83, 97 (1994); *see also* CPLR §3026 ("Pleadings shall be liberally construed. Defects shall be ignored if a substantial right of a party is not prejudiced."). As the Court of Appeals stated in *Leon*, in considering a motion to dismiss:

> We accept the facts as alleged in the complaint as true, accord plaintiffs the benefit of every possible inference, and determine only whether the facts as alleged fit within any cognizable legal theory (*Morone v. Morone*, 50 N.Y.2d 481, 484; *Rovello v. Orofino Realty Co.*, 40 N.Y.2d 633, 634). Under CPLR 3211(a)(1), a dismissal is warranted only if the documentary evidence submitted conclusively establishes a

> defense to the asserted claims as a matter of law (*See, e.g., Heaney v. Purdy*, 29 N.Y.2d 157). In assessing a motion under CPLR 3211(a)(7), however, a court may freely consider affidavits submitted by the plaintiff to remedy any defects in the complaint (*Rovello v. Orofino Realty Co., supra*, at 635) and 'the criterion is whether the proponent of the pleading has a cause of action, not whether he has stated one.' (*Guggenheimer v. Ginzburg*, 43 N.Y.2d 268, 275; *Rovello v. Orofino Realty Co., supra*, at 636)."

84 N.Y.2d at 87-88.

In keeping with the notion that pleadings are to be construed liberally and afforded the benefit of every inference, §3211(e) of the CPLR provides that, to the extent that a motion to dismiss may be granted, the court may permit the plaintiff/petitioner to plead again to remedy any defect. The decision as to whether to grant a party leave to plead again is soundly within the discretion of the trial court. *Martell Realty v. Vanderveer-Oakdale Assocs.*, 265 A.D.2d 384, 385 (2d Dep't 1999).

B. Judicial Dissolution and Appointment of a Receiver Under the Limited Liability Company Law

Section 702 of the LLC Law, titled "Judicial Dissolution", provides, in pertinent part, as follows:

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

While the question of whether or not to issue an order of dissolution with respect to a limited liability company lies within the sound discretion of the court hearing the petition, judicial dissolution is appropriate where the petitioning member establishes "in the context of the terms of the operating agreement or articles of organization that (1) the management of the entity is unable or unwilling to reasonably permit or promote the stated purpose of the entity to be realized or achieved, or (2) continuing the entity is financially unfeasible." *In re 1545 Ocean Avenue, LLC*, 72 A.D.3d 1212, 131 (2d Dep't 2010); *Matter of Extreme Wireless*, 299 A.D.2d 549, 550 (2d Dep't 2002). A

petitioning member need not demonstrate that carrying on the business of the limited liability company in conformity with its operating agreement would be impossible, but rather only that it would "not [be] reasonably practicable." *See, e.g.*, *Matter of Youngwall v. Youngwall Realty, LLC*, 2008 N.Y. Slip Op. 30811[U] (Sup. Ct. Nassau County 2008); Limited Liability Company Law §702.

Prior to *1545 Ocean Avenue*, courts held that allegations of "internal 'deadlock' impeding [the company's] smooth operation" substantiate a petitioning member's request for judicial dissolution. *Schindler v. Niche Media Holdings*, 1 Misc.3d 713, 716 (Sup. Ct. New York County 2003). In keeping therewith, when there is "intense personal animosity between the members…[a] lack of any proof of the current profitability of the LLC, [and an] apparent inability to function as intended, dissolution is appropriate." *Youngwall*, *supra* (citation and quotation omitted); *see also 1545 Ocean Avenue* at 133 (Fischer, J. concurring in part and dissenting in part) ("[I]t is 'not reasonably practicable' for a limited liability company to carry on its business in conformity with its articles of organization or operating agreement when disagreements or conflict among the members regarding the means, methods, or finances of the company's operations is so fundamental and intractable as to make it unfeasible for the company to carry on its business as originally intended."); *Matter of Natanel v. Cohen*, 2014 WL 37887, Index No. 502760/13, Decision and Order (Sup. Ct. New York County January 2, 2014) ("[P]etitioner's testimony is that the two 50% members of the LLC are not on speaking terms and that decision-making has been seriously frustrated, raising questions of fact as to the feasibility of continuing the LLC.") (decision appended)

C. An Alleged Lack of Evidence is Not a Basis for Dismissal Under CPLR §3211(a)(7)

Respondents' contention that the Court may dismiss the Petition under CPLR §3211(a)(7) based upon any alleged lack of evidence submitted by Petitioners in support of the Petition is improper. Specifically, CPLR §3211(a)(7) states that a party may move to dismiss a cause of action if "the pleading fails to state a cause of action." With regard to pleadings in special proceedings, CPLR §402 provides, in pertinent part that: "There shall be a petition, *which shall comply with the requirements for a complaint in an action*, and an answer where there is an adverse party…The court may permit such other pleadings as are authorized in an action upon such terms as it may specify…" (emphasis added) As such, and contrary to Respondents' assertions, "lack of evidence" is not a basis for dismissal as a failure to state a cause of action under CPLR §3211(a)(7). In fact, *Matter of Trustco Bank, N.A. v. Strong*, 261 A.D.2d 25 (3d Dep't 1999), cited by Respondents in support of their assertions that, unlike complaints in plenary actions, a petition must include evidentiary support in order to properly state a cause of action, only discussed the submission of "competent evidence" in support of a petition as it concerned the court's summary consideration of the petition under CPLR §409(b) and/or its ability to refer any factual issues for trial under CPLR §410, and not with regard to whether the petition therein stated a valid claim for purposes of CPLR §3211(a)(7).

Notwithstanding the defects in Respondents' position, Petitioners respectfully submit that sufficient evidence has been submitted in support of the Petition. In this regard, the Petition was duly verified by both Petitioners as being true and correct to the best of their knowledge and belief. Additionally, attached to the Petition as Exhibit "A" is a copy of the Summons and Complaint filed in connection with the Action commenced by Respondents, individually, and the Company, by Respondents, against Petitioners. Attached to said Complaint as Exhibit "A" is a full and complete

copy of the Operating Agreement and the Consulting Agreements. Said documents were submitted in connection with the allegations made in the Petition concerning the terms and provisions of the Operating Agreement and Consulting Agreements, as well as Petitioners' contention that the Action was commenced in derogation of the Operating Agreement (and thereby substantiating Petitioners' assertion that judicial dissolution is appropriate).

Additionally, Respondents' contentions in this regard are disingenuous because, as Respondents are undoubtedly aware, as the Managers of the Company, *Michael and Andreas are solely in possession, custody and control of all of the Company's books and records, financial statements, documents and the like concerning its financial affairs and have refused to share those records with Petitioners*. As a result, Petitioners have been forced to rely on the limited documents that they have in their personal possession and those that Petitioners have been able to obtain from third-party sources (such as former employees, vendors, and the like) concerning the Company's financial affairs and other matters in order to formulate a response to the Motion. Put simply, Respondents should not be heard to complaint that Petitioners failed to submit sufficient evidence in support of their request for judicial dissolution of the Company knowing full well that they are in sole possession of such evidence.

D. The Petition Sufficiently States a Valid Claim for Judicial Dissolution of the Company

It is respectfully submitted that Respondents have failed to demonstrate their alleged entitlement to the dismissal of Petitioner's claim for judicial dissolution of the Company pursuant to CPLR §3211(a)(7) of the CPLR.

As discussed above, judicial dissolution of a limited liability company is appropriate when *either* the management of the entity is unable or unwilling to reasonably permit or promote the stated

purpose of the entity to be realized or achieved *or* continuing the entity is financially unfeasible." *1545 Ocean Avenue*, 72 A.D.3d at 131; Limited Liability Company Law §702. By way of the Petition (both in its present form and particularly as supplemented by way of the Koch Aff. and the exhibits annexed thereto which Petitioners respectfully request that the Court include as part of the record in support of the Petition as permitted under CPLR §402), Petitioners have sufficiently plead that the Company cannot continue to operate in the manner and for the purpose intended by the members as a result of the irreconcilable differences that exist between the two equal ownership groups and that continuing the operations of the Company is not financially feasible within the purview of §702 of the Limited Liability Company Law. In this regard, the Petition alleges that Respondents commenced the Action against Petitioners in derogation of the Operating Agreement and have continued to operate the Company's business without Petitioners' involvement or participation and without regard to their status as 50% co-owners of the Company. (See Petition at ¶¶14-17; Ex. A) The Petition further alleges that the Company is not paying its debts as they come due, is insolvent, has insufficient revenues to meet its ongoing obligations and has insufficient assets to carry on its operations as intended. (Petition at ¶17)

The aforementioned allegations set forth in the Petition are expanded upon in exhaustive detail and are further substantiated by documentary evidence by way of the Koch Aff. Specifically, even though Michael and Andreas are the sole "Managers" of the Company, the Company was always intended to be operated with the active involvement and participation of all of the members, who each held a relatively equal stake in the Company, with "Major Decisions" requiring the affirmative approval of each member. (Koch Aff. at ¶7) However, once material disputes arose between Petitioners and Respondents concerning, among other things, the Company's apparent

inability and/or unwillingness to generally pay its obligations, its unprofitability and lack of any real prospects of financial improvement, its overall mismanagement by Michael and Andreas and Michael's attempt to exert complete control over the Company, and rather than attempting to resolve said disputes in accordance with and under the procedures set forth in the Operating Agreement, Respondents abandoned their fiduciary duties to Petitioners as 50% co-owners of the Company by demanding payment from the Company under certain previously undisclosed promissory notes and unilaterally commencing the action against Petitions. (Koch Aff. at ¶¶9, 10, 13) Additionally, it is readily apparent that the Company cannot pay its debts as they come and has insufficient assets/capital to make it a viable entity going forward. (Koch Aff. at ¶¶18-27) Such facts strongly support Petitioners' claim that the Company cannot continue to operate in accordance with its intended purpose and is financially unfeasible and, thus, have adequately stated a valid claim for judicial dissolution of the Company.

CONCLUSION

Affording Petitioners the benefit of every possible inference, and assuming, as the Court must, that the facts and circumstances set forth in the Petition and Koch Aff. are true, it is clear that Petitioners' claim for judicial dissolution of the Company has been adequately plead and has sufficient merit to allow it to proceed. Accordingly, the Motion should be denied in its entirety. To the extent that the Court perceives any deficiencies with regard to the allegations set forth in the Petition, Petitioners respectfully submit that they should be granted leave to re-plead as may be necessary and appropriate. Petitioners further request that the Court refer any perceived disputed issues of material fact for an immediate trial in accordance with CPLR §410.

WHEREFORE, Petitioners respectfully request that the Motion be denied and that the Court enter an Order: (a) decreeing that the Company be dissolved; (b) appointing a receiver to wind up the affairs of the Company; and (c) granting such other and further relief as may be just and proper.

Dated: New York, New York
April 4, 2014

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