FILED: NEW YORK COUNTY CLERK 08/21/2014 05:55 PM
NYSCEF DOC. NO. 110

INDEX NO. 600592/2010
RECEIVED NYSCEF: 08/21/2014

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

--x

MAZEL CAPITAL, LLC, on its own behalf, and derivatively on behalf of HEARTWATCH, LLC

Plaintiffs,

-against -

FRANKLYN LAIFER,

Defendant.

--x

Index No.: 600592/10

Motion #6

DEFENDANT'S MEMORANDUM OF LAW IN SUPPORT OF HIS MOTION FOR SUMMARY JUDGMENT

INTRODUCTION

Plaintiff Mazel Capital, LLC ("MC"), a disgruntled investor in Heartwatch, LLC ("Heartwatch"), bases its claims against defendant Franklyn Laifer ("Laifer") on actions to which it did not previously object, despite being fully informed about them years ago. Moreover, MC's challenges to Laifer's decisions - which were indisputably within the scope of Laifer's authority as managing member of Heartwatch and in which he had no personal interest - cannot overcome the business judgment rule. *See* N.Y. Limit. Liab. Co. Law, §409.

MC's Amended Complaint[1] alleges, as part of a derivative claim on behalf of Heartwatch (which ceased operations in 2008), that Laifer received compensation for his work beyond that which he was contractually permitted under Heartwatch's May 24, 2006 operating agreement (the "Agreement"). MC further alleges, again derivatively, that Heartwatch breached a letter

---

[1] Hereinafter the "AC", annexed, along with defendant's Answer, as Exhibit A to the accompanying affidavit of Franklyn Laifer (the "FL Aff.".) All references herein to Exhibits ("Ex.") refer to Exhibits to the FL Aff.

agreement between them signed the same day (the "Letter Agreement"), by spending more than allowed thereunder [2]. Finally, MC alleges, as a direct claim, that Laifer fraudulently induced it to invest additional monies in Heartwatch (the "Additional Investments") by allegedly failing to disclose the "breaches."[3]

Numerous documents, however, as well as undisputed testimony (including that of MC's principals), establish that MC, prior to making its Additional Investments, was not only sent regular written updates reciting every detail of Heartwatch's operations (including schedules of actual, and projected expenditures setting forth the compensation paid Laifer and consulting fees paid others), but also had numerous telephone and face to face conversations with Laifer and other Heartwatch employees about every aspect of Heartwatch's operations. Thus, in addition to the many Heartwatch financial documents with which MC was regularly supplied, MC's principal ("Jedwab") testified that:

---

[2] See Agreement and Letter Agreement, collectively Ex.B. The AC could be construed as alleging that ***Laifer*** breached par.5 of the Letter Agreement. If so, such claim must be dismissed as Laifer is not a party to the Letter Agreement; it was ***Heartwatch***, not ***Laifer personally***, which undertook to limit its spending for 6 months. To the extent that MC's theory is that Laifer breached the Agreement's requirement of reasonable care and prudence (Agreement, par.7[g]) by causing Heartwatch to pay "excess consulting ... fees ... ." (AC, par. 16[c]), such claim likewise lacks merit. Again, MC was fully informed of these payments throughout the relevant period. Moreover, as demonstrated by the curricula vitae of the "consultants" at issue, their compensation was commensurate with their qualifications. See FL Aff., pars. 13-14 and Ex.G. Moreover, the Agreement expressly authorized Laifer, as Manager, to incur such obligations on Heartwatch's behalf (Agreement, Article III, pars. 1 and 7) and, as Laifer had no personal interest in the compensation paid to others, his decision as to what Heartwatch should pay its employees (the "consulting fees" were actually, as testified to by Heartwatch's accountant, Henry Grant [Ex.F, 48:9-50:9] employees' salary; nevertheless, for simplicity's sake, they will be referred to herein as "consulting fees) must be afforded a presumption of propriety under the business judgment rule, a presumption which MC cannot overcome.

[3] Laifer has asserted a counterclaim for the Heartwatch obligations which he paid.

i) Laifer was also in constant communication with another of MC's principals ("Wolf", now deceased), who discussed those communications with Jedwab;

ii) MC complained to Laifer that Heartwatch's expenditures, including Laifer's compensation and consulting fees, were too high and questioned Laifer about them; and

iii) MC knew that Laifer was receiving compensation from Heartwatch. Significantly, when asked at his deposition what Laifer had intentionally concealed from MC (as alleged in the AC, par. 31), ***Jedwab never claimed that Laifer had concealed any information relating to Laifer's compensation or the consulting fees paid by Heartwatch.*** See transcript of deposition of Richard Jedwab ("RJ"), Ex.C, 178:6 through 181:7.

Nevertheless, MC never asserted any claims against Laifer until three years after the Additional Investments and two years after Heartwatch had ceased to operate, thus belying its claims that the expenditures were in breach of the Agreements, and, in any event, waiving any breach. MC's *ex post facto* reinterpretation of the agreements cannot create breaches which it never before claimed, and which do not exist. "When one party performs under the contract and the other party accepts his performance without objection it is assumed that this was the performance contemplated by the agreement." *Nomura Sec. Int'l, Inc. v. E*Trade Sec., Inc.*, 280 F. Supp. 2d 184, 204 (S.D.N.Y. 2003)(applying New York law)(citations omitted.)

Even if MC had not been informed of the acts of which it now complains, it certainly had ready access to all the information it needed to learn about them. Jedwab admits that he questioned Laifer about Heartwatch's expenditures, including Laifer's compensation, and that MC never requested any information which Laifer, or another Heartwatch representative, did not

supply. (*See* RJ, 108:10-18).[4] Indeed, although both the Agreement and New York statutes gave MC the right to all of Heartwatch's financial information, MC admits that it never made any written request for information from Laifer or Heartwatch until after Heartwatch was out of business. See accompanying Joint Statement of Material Undisputed Facts (the "Statement".) "Where a party has the means to discover the true nature of the transaction by the exercise of ordinary intelligence, and fails to make use of those means, he cannot claim justifiable reliance on defendant's misrepresentations." *Stuart Silver Associates, Inc. v. Baco Development Corp.*, 245 A.D.2d 96, 98-99, 665 N.Y.S.2d 415, 417 (1st Dept. 1999) (citations omitted)(reversing lower court and granting summary judgment dismissing fraud claims by limited partner against general partner.)

Thus, as set forth more fully below, MC's AC should be dismissed in its entirety[5].

FACTS

Background

In the Spring of, 2006, Laifer formed Heartwatch for the purpose of marketing a heart monitoring device in tandem with a live 24-hour call center staffed by cardiologists and other medical professionals. On May 24, 2006, Laifer, as 91% owner, and MC, as 9% owner, entered into the Agreement, which provided that Laifer would be the managing member of Heartwatch. See Agreement, Art.III, par.1. The Agreement expressly provides that "[e]ach Manager's liability to this Company or to its members for damages for any breach of duty in such capacity is

---

[4] Also see deposition transcript of Brian Jedwab ("BJ"), relevant pages annexed as Ex.D, 95:25- 96:6.

[5] As set forth more fully in Point Four, *supra*, MC's fraud claim, even if sustained, cannot support its demand for punitive damages.

eliminated, except if there is a final judgment or adjudication adverse to the Manager that establishes that his acts of omissions involved intentional misconduct or a knowing violation of law or that he personally gained in fact a financial profit or other advantage to which he was not legally entitled." Agreement, Art. III, par. 7(g).

Laifer, a cardiologist, was also the Medical Director of Heartwatch. As set forth more fully in the FL Aff., pars.9-11 and testified to by Jay Lichtenstein, (Ex.E ["JL"], 38:22-40:9) Heartwatch's former President and Chief Financial Officer, this position entailed completely different services than the management services Laifer also performed for Heartwatch.

In May and October, 2007, MC made its Additional Investments in Heartwatch ($120,000 and $180,000 respectively.) Heartwatch's other major investor was South Ferry Building Co. ("South Ferry") which invested a total of $500,000, some invested before and some after the Additional Investments were made; Laifer's son, Alan, and Seymour Kramer invested $100,000 and $50,000, respectively, both before and after the second of the Additional Investments. Ultimately, Laifer owned 80% of Heartwatch, MC 12%, South Ferry 6.5%, Alan Laifer 1%, and Kramer .5%. See Statement.

The principals of MC are (or were, in Wolf's case) sophisticated business professionals. Jedwab had formed, and was the managing member of, approximately a dozen limited liability companies. (RJ,182:14; 185:4; 188:4 -196:6) His son, Brian ("Brian"), through whom Jedwab communicated with Heartwatch and who also acted on MC's behalf, was, at the time of the events at issue, a practicing attorney, general counsel "to a conglomerate", and a portfolio manager. RJ 181:22-182:14; Brian's transcript, ("BJ"), Ex.D, 14:5-10; 15:5-16:20; 19:5-7.

The Agreement provides that "[e]ach member may inspect and copy ... the Articles of

Organization, the Agreement, minutes of any meeting of members and all tax returns or financial statments of this Company for the three years immediately preceding his inspection, and other information regarding the affairs of this Company as is just and reasonable." Agreement, Article III, par. 4. Nevertheless, MC never made any written request for any Heartwatch documents until September, 2009, long after Heartwatch had ceased operations. See Statement. Shortly thereafter, MC commenced this action as a books and records proceeding, and then based the AC on the very documents it received in response, thus demonstrating that information relating to Laifer's supposed wrongdoing was always available to it. Further, MC admits that Laifer or another Heartwatch employee responded to every request for information that MC ever made. RJ 108:10-18; BJ 95:24- 96:6.

Plaintiff's Claims

Plaintiff claims that Laifer breached the Agreement's provision which provides that "the Manager shall not be entitled to any compensation ***for serving as manager to [Heartwatch]*** ... ." See Agreement, par.7(a) and AC, par. 16. The compensation Laifer received from Heartwatch was not for his management services, but rather for his services as Medical Director. See FL Aff., pars.8-11 and JL 41:15-42:10. Laifer had previously been the medical director of E.K. Guard, Inc. ("EKG"), a very similar medical technology business in which MC had also invested[6]. Laifer had no equity in EKG, and no management responsibilities, but nevertheless received the identical compensation from Heartwatch as he received for his services as medical

---

[6] MC received a 4% interest in Heartwatch in exchange for its interest in EKG, which had essentially ceased operations by that time and was the defendant in a lawsuit filed by Laifer and Lichtenstein alleging EKG's breach of their employment agreements. The agreement settling that action is confidential.

director of EKG.[7] See FL Aff., par.8. Moreover, Laifer's compensation was fully disclosed in documents provided to MC (described more fully below), which, prior to instituting this action, never contended that such compensation breached the Agreement (or constituted corporate waste), even though it knew about and specifically discussed Laifer's compensation with him. See RJ 81:22-24;95:23-98:2.

MC also claims that Heartwatch breached the Letter Agreement, which provides in pertinent part that "Heartwatch hereby undertakes that ... it will not use in excess of $50,000 per month for each of the first two months, and $37,500 per month for each of the following four months ... (so that [MC's] Investment will not be fully expended for a period of at least six (6) months from the date of [MC's] Investment." See AC, pars. 16-17, and Letter Agreement, par.5. Although the target spending for some months was exceeded, Heartwatch spent less than the designated $250,000 in the six months from MC's investment (see Statement), and MC did not claim that Heartwatch was in breach. Thus, the parties' performance establishes that Laifer's interpretation of this provision is correct. In any event, MC waived any claim that overpayment during some of the constituent months constituted a breach, and (given that Heartwatch complied with the $250,000 over 6 month requirement) can show no damages from any such breach.

Plaintiff further conclusorily alleges that "Laifer had Heartwatch pay unjustified, unsupported and excessive consulting and [sic] fees of over $310,000 over a two-year period " (AC, par. 16[c]), and appears to contend that such fees constituted either a breach of Laifer's contractual obligation to manage Heartwatch with reasonable care and prudence (Agreement,

---

[7] Moreover, Laifer's compensation was, at least in part, a "pass through" of monies Heartwatch could have paid to Remote, and from Remote from Laifer. FL.Aff., fn.3.

par.7[g]) or a breach of Laifer's fiduciary duty to Heartwatch not to waste corporate assets. Either way, MC was fully informed about all consulting fees paid by Heartwatch at the time they were made, but did not assert a claim about them. Moreover, plaintiff does not dispute that the Agreement conferred authority upon Laifer to engage consultants or employees on Heartwatch's behalf[8], nor does it allege that Laifer had any personal interest in the compensation received by these "consultants." ***To the contrary, the person who had the greatest interest in ensuring that Heartwatch did not pay excessive employee compensation was Laifer, who (depending on the time period) owned 80% or more of Heartwatch***[9]. Moreover, the employees' compensation was commensurate with their experience and qualifications, as established by the curricula vitae with which MC was furnished. FL Aff., par. 14. Accordingly, MC's unsupported challenge to these transactions is barred by the business judgment rule.

Finally, MC claims that Laifer defrauded it into making its Additional Investments without informing it of his "wrongdoing". To the contrary, however, MC was informed fully (both in writing and in oral communications) before it made its Additional Investments. In any event, even if it had not been expressly informed, MC had the means of discovering the

---

[8] Par. 7(e) of the Agreement provides that "[e]xcept as otherwise provided herein, a Manager shall have the power and authority on behalf of this Company to do all things as set forth in Sec. 202(a)-202(q) of the New York Limited Liability Company Law." Among many other powers, those sections of the Limited Liability Law authorize limited liability companies to "make contracts" and "elect or appoint managers, employees and agents of the limited liability company, define their duties and fix their compensation." Sections 209(e) and 209(h), respectively.

[9] Laifer originally owned 100% of Heartwatch, but transferred 9% of it to MC in May, 2006 in exchange for MC's investment in Heartwatch (and prior interest in EKG), and, over the next year and a half, approximately, transferred an additional 11% to MC and others in exchange for their investments in Heartwatch, leaving him with an 80% share of Heartwatch. The full consideration for the purchases went to Heartwatch, not Laifer personally. FL Aff., par.3.

information it now claims was withheld - the amount of Heartwatch's spending (including "consultants' fees") and of Laifer's compensation - had it simply reviewed Heartwatch's financial documents which fully disclose such information.

Information Provided to Plaintiff

During the period between MC's initial investment in Heartwatch, in May, 2006, and its Additional Investments in May, 2007 and October, 2007, it was provided with regular written reports, approximately quarterly (in addition to other documents, meetings, and other communications) about Heartwatch's operations, including financial analyses. Examples of such reports (two from July, 2006, one each from April and August, 2007) are annexed as Ex.G. Each contain a "Financial Analysis", which include both actual and projected compensation to be paid "management and sales execs" and "advisors", and also projections of compensation for "Mgmt and Operations Salaries" and "Advisors" for 2007 through 2011. At deposition, Jedwab acknowledged that Mazel knew that these terms included Laifer. (RJ113:7-12.)

In actuality, the compensation paid by Heartwatch ***was less than had been projected***; because Heartwatch was having financial difficulties, Laifer and other Heartwatch employees agreed to reduce their compensation. This fact was also well-known to MC, which received schedules showing Heartwatch's deposits and withdrawals, as well as a summary of the amounts being paid to Laifer and other Heartwatch employees monthly. Schedules covering 5/15/06-8/1/06, and 5/15/06-2/22/07 annexed as Ex.H. These schedules expressly set forth the checks Heartwatch wrote to Laifer and other Heartwatch executives (Jay Lichtenstein and Don Andrews, referred to in the AC as "consultants") during those periods. In addition, the first schedule contains a "Monthly Expense Run Rate" listing the monthly compensation Heartwatch was

paying Laifer, Lichtenstein, and Andrews, and the second carries that information through 2/07.[10]

Prior to its second Additional Investment, MC was also provided with three draft versions of offering materials (the "Offering Materials") dated March 2007 relating to a contemplated $2 million private placement (example annexed as Ex. I), each of which disclosed that $260,000 of the contemplated $2 million raised would be used for "salaries of employees, officers, and directors" (par.2) and also that "Laifer will have sole control over the management, operations and policies of the Company" (par.5.)

The Offering Materials also disclosed that Laifer would be managing a medical staffing company ("Remote"), and would receive compensation for such services. Offering Materials, par.7(i). The Offering Materials also provided that all documents pertaining to Heartwatch were made available to potential investors (par.8[d]), who had had the opportunity to ask questions and receive answers from Heartwatch representatives, and to verify the information contained in the Offering Materials (8[f]). Indeed, Jedwab confirmed that MC had had "the opportunity to ask and receive whatever [information MC] needed." RJ 108:10-18; BJ 95:24-96:6.

In addition to these documents, Laifer and other Heartwatch personnel had substantial correspondence and "numerous meetings"[11] and other oral communications with MC. For example, in an August, 2006 email (part of Ex.J) transmitting one of Heartwatch's periodic update reports, MC was advised that "our burn rate[12] is now $33,500 per month plus any amount

---

[10] This schedule is appended to a larger report (dated August 7, 2006) sent to MC which included updates, CVs of personnel and financial data (Ex. G).

[11] *See* e.g. RJ 40:2-21;49:23-50:6;55:18-56:11.

[12] Jedwab testified that he understood the term "burn rate" to mean how much a business is expending on a weekly, monthly, or yearly basis. RJ 168:2-7.

spent on non-recurring items. Also note that we have just under $100,000 [of the $250,000 initial MC investment] remaining. *** Please let me know if you would like additional details on our July overage." Similarly, in a December, 2007, email (part of Ex. J), MC was advised that HeartWatch's monthly burn rate for management compensation was $130,000. Moreover, as Jedwab acknowledges, Laifer was in constant communication with Wolf about all aspects of Heartwatch's business, and Wolf reported back to Jedwab about those conversations. RJ98:14-20; 101:18-102:21; 40:5-21; 55:8-23.

Laifer also had many direct communications with Jedwab and his son, Brian, about Heartwatch's operations and finances. *See, e.g.*, RJ 40:2-21; 55:9-56:11. At least one of these conversations, which took place before the Additional Investments, involved Laifer's compensation and Heartwatch's other expenses. Thus, Jedwab testified that he asked Laifer for a breakdown of Heartwatch's expenses and that Laifer "then explained to us who is making what. To a certain extent he gave us some of those answers of people who were earning money." RJ 132:7-10. Jedwab further testified on this subject as follows:

> Q At the time investments were made in May 2007 of $120,000 and October [2007] of $180,000 had you spoke to Dr. Laifer about what his activities were and whether he was being compensated for these activities?
>
> A At some of the meetings that Frank came to us or Hirsch for additional funds both Hirsch and myself and even my son said, "Frank we need to control the expenses" and we were promised they would be.
>
> Q Mr. Jedwab my question was during the time that you invested in May [2007] and October [2007] did you say to, Frank Laifer. Frank 'you should not be getting paid for anything you are doing' in words or substance.
>
> A Again that needs an explanation. We wanted them to adhere to the Agreement whatever the Agreement calls for that salaries would not exceed a certain amount ***whether it was for him or other people*** combined we should operate according to

the Agreement.
Again it was brought out to Frank that we cannot keep coming back to investors and taking money after money to run offices, consultants and yet we haven't made a product, sold a product, marketed a product.

Q I am sorry, you said officers consultants. Would that include salaries in that categorization?

A What I basically meant was all expenses, whether it was lunches, travel, and entertainment.

Q At that point you were aware of what expenses were you not?

A I may have been.

See RJ 80:11-81:24 (emphasis added.); See also 84:24-85:3.[13]

In light of all the information with which MC was provided before it completed its Additional Investments, MC's allegation that Laifer "intentionally concealed" that he was receiving compensation from Heartwatch and had agreed to "excessive, unjustified, and unreasonable payments to consultants" (AC, pars. 31-34), is demonstrably false. It is thus no wonder that Jedwab, when asked about that allegation at his deposition, retreated from it and did not contend that Laifer had concealed any information on those subjects. RJ 178:6-23;179:3-20; 180:15-181:7.

---

[13] Jedwab also testified: "So at the time you made the [Additional Investments] had you spoken to Dr. Laifer about what his activities were and whether he was being compensated?" ... "Yes." (RJ 80:11- 81:4.)

POINT ONE

HAVING BEEN FULLY INFORMED ABOUT ALL ACTIONS ABOUT WHICH IT NOW COMPLAINS, AND/OR HAVING FULL ACCESS TO ALL RELEVANT INFORMATION ABOUT THOSE ACTIONS, MC CANNOT AS A MATTER OF LAW, PROVE ITS REASONABLE RELIANCE AS REQUIRED TO MAKE OUT A FRAUD CLAIM

It is hornbook law that reasonable reliance is a required element of a fraud cause of action. *Stuart Silver Associates, supra.* "To prevail on a claim of fraud, a plaintiff must show that it actually relied on the purported fraudulent statements and that its reliance was reasonable or justifiable." *KNK Enterprises, Inc. v. Harriman Enterprises, Inc.*, 33 A.D.3d 872, 824 N.Y.S.2d 307 (1st Dept. 2006)(citation omitted.) *Accord Assured Guaranty Municipal Corp. v. DLJ Mortgage Capital, Inc.*, 44 Misc.3d 1206(A) (Sup.N.Y. 2014)(Kornreich, J.) Here, MC cannot possibly show reasonable reliance on any representation about Laifer's compensation or Heartwatch's expenditures (including consulting fees) since Heartwatch provided it with numerous documents, as well as discussions in meetings, emails, and other communications, which clearly set forth the facts about these matters.

Moreover, even if MC had not been provided with the many documents and other communications described in detail above, it always had access to that information. Indeed, it formulated the AC based on documents it received from Heartwatch! Thus, as a matter of law, it cannot have reasonably relied on any misrepresentation relating to Heartwatch's expenditures or Laifer's compensation. "Reasonable reliance is a condition which cannot be met where, as here, a party has the means to discover the true nature of the transaction by the exercise of ordinary intelligence, and fails to make use of those means." *Arfa v. Zamir*, 78 A.D.3d 56, 59, 905

N.Y.S.2d 77, 79 (1st Dept. 2010), *aff'd* 17 N.Y.3d 737, 929 N.Y.S.2d 11 (2011)(citations, internal quotations, omited.)[14]

As demonstrated above, before making its Additional Investments, MC was provided with a plethora of documents showing Laifer's compensation and Heartwatch's expenditures, both actual and projected. It admitted that it had had the opportunity to ask questions and get answers before its Additional Investments, and even admitted discussing Heartwatch's expenditures, including Laifer's compensation, with Laifer. If it was not aware that Laifer was receiving compensation from Heartwatch and of the amount of consulting fees (which it was, since it questioned Laifer about these issues), it can only be because it did not read the documents with which it was provided regularly. Willful ignorance does not a fraud claim make.

Ust, *supra*, in which corporate investors sued investment bankers alleging that they had

---

[14] *Accord Waterscape Resort LLC v. McGovern*, 107 A.D.3d 571, 967 N.Y.S.2d 368 (1st Dept. 2013)(same, granting summary judgment dismissing fraud claim); *Rosenblum v. Glogoff*, 96 A.D.3d 514, 946 N.Y.S.2d 167 (1st Dept. 2012)(same, granting summary judgment dismissing fraud claim); *Miller v. Icon Grp. LLC*, 77 A.D.3d 586, 911 N.Y.S.2d 3 (1st Dept. 2010)(same, granting summary judgment to plaintiff on contract despite defense of fraudulent inducement); *Dragon Investment Co. II LLC v. Shanahan*, 49 A.D.3d 403, 404, 854 N.Y.S. 2d 115, 117 (1st Dept. 2008)("The fraud claim is also defective because as a matter of law, a sophisticated plaintiff cannot establish that it entered into an arm's length transaction in justifiable reliance on alleged misrepresentations if that plaintiff failed to make use of the means of verification that were available to it.")(citations, internal quotations, omitted); *UST Private Equity Investors Fund, Inc. v. Salomon Smith Barney*, 288 A.D.2d 87, 88-89, 733 N.Y.S.2d 385, 386 (1st Dept. 2001)(same, dismissing fraud claim on the pleadings); *Stuart Silver Associates, supra* (same, granting summary judgment dismissing fraud claims); *Holzer v. Mondadori*, 40 Misc.3d 1233(A) (Sup.N.Y. 2013)(Kornreich, J.)(same, citing *Stuart Silver Associates, supra,* and *Rosenblum, supra*, and dismissing fraud claim on the pleadings); *Wong v. May*, 23 Misc.3d 1114(A), 2009 WL 1099466, *3 (Sup.N.Y. 2009)([P]laintiff has failed to demonstrate that he justifiably relied on the alleged misrepresentation. Notably, [plaintiff] does not claim to have reviewed the [business's] books and records or to have undertaken any other due diligence to determine the profitability of the business prior to entering into the [investment] agreements with [defendant]. Plaintiff's second cause of action [for fraud] must, therefore, also be dismissed.)(citations omitted.)

been fraudulently induced into investing by misrepresentations concerning whether the corporation's sole product had been cleared for marketing, is directly on point. In *Ust*, the Appellate Division, First Department, affirmed the dismissal of plaintiffs' complaint on the pleadings, holding that plaintiffs could not demonstrate reasonable reliance because, like MC (which was expressly informed of the true facts through documents and other communications), they could have discovered the alleged misrepresentations through the exercise of ordinary intelligence:

> As a matter of law, a sophisticated plaintiff cannot establish that it entered into an arm's length transaction in justifiable reliance on alleged misrepresentations if that plaintiff failed to make use of the means of verification that were available to it, such as reviewing the files of the other parties. *** If plaintiffs had requested and carefully reviewed these documents during their due diligence, they would have been apprised of the clearance issue before making their investment decision. Accordingly, plaintiffs cannot claim to have justifiably relied on the [alleged misrepresentations.]

288 A.D.2d at 88-89, 733 N.Y.S.2d at 386 (citations omitted.)

Similarly, in *Stuart Silver Associates, supra*, limited partners in a real estate development partnership sued their general partners for fraud. Plaintiffs claimed that the general partners had misrepresented the expenses, profits, and risks of the venture in oral representations and in offering materials on which plaintiffs had relied in making their investment, just as MC claims that it made its Additional Investments in reliance on Laifer's misrepresentions as to Heartwatch's expenses, including his own compensation. The Appellate Division, First Department, reversed the Court below and granted summary judgment dismissing plaintiffs' fraud claim on the ground that plaintiffs could not demonstrate that they had reasonably relied on the alleged misrepresentations:

> [E]ven if we assume that [the general partner] made all of the disputed statements and intended to induce reliance thereupon, plaintiffs have failed to state a fraud claim because they cannot show that their alleged reliance was justified. Plaintiffs were relatively sophisticated investors who should have understood the risks of investing in a real estate venture without conducting a 'due diligence' investigation or consulting their lawyers and accountants. In fact, [one of the plaintiffs] did not even read the [offering materials], the implication being that she entered into this venture based on [one general partner's] alleged oral promises alone. As such reliance is no reasonable, the existence of a dispute as to whether [the general partner] made such promises does nto create a triable issue on the fraud claim.

245 A.D.2d at 99, 665 N.Y.S.2d at 418.

Equally instructive is Your Honor's own decision in *Holzer*, *supra*, 980 N.Y.S.2d at *4, in which Your Honor held that "[t]he Complaint and documentary evidence indicate that defendants lied about myriad facts ... . However, the fraud claim is dismissed for failure to plead reasonable reliance." Your Honor noted that plaintiffs had "thrown caution to the wind [by investing] without conducting the most basic of inquiries that would have revealed [the misrepresentations][15], and had ignored an "obvious red flag"[16] when making a further investment, exactly as MC (assuming that it never read the documents it received and forgot its other communications with Heartwatch as soon as they concluded) made the Additional Investments without conducting the most basic of inquiries and ignored the red flags prominently displayed in the many financial documents Heartwatch provided to it. Like the *Holzer* fraud claim, therefore, MC's fraud claim should be dismissed.

---

[15] 690 N.Y.S.2d at *5.

[16] *Id.*

POINT TWO

MC'S CLAIM THAT LAIFER BREACHED THE AGREEMENT BY APPROVING EXORBITANT CONSULTING FEES IS BARRED BY THE BUSINESS JUDGMENT RULE

The business judgment rule "bars judicial inquiry into actions of corporate directors taken in good faith and in the exercise of honest judgment in the lawful and legitimate furtherance of corporate purposes." *Zuckerbrod v. 355 Co., LLC*, 113 A.D.3d 675, 676, 979 N.Y.S.2d 119, 120 (2d Dept. 2014)(citations, internal quotations, omitted.) It applies equally to the managers of a limited liability company. N.Y. Limited Liab. Co. Law §409.

The business judgment rule mandates summary judgment dismissing a claim against a manager for waste where, as here, the manager makes a prima facie showing that the complained of acts were within his or her authority and were made in good faith to serve proper business purposes, and the plaintiff fails to submit evidence demonstrating that the manager acted in bad faith. *Carroll v. Radoniqi*, 105 A.D.3d 493, 494, 963 N.Y.S.2d 97, 98 (1st Dept. 2013) (dismissing breach of fiduciary claim on summary judgment holding that "the [defendant] made a prima facie showing that its board of directors' decisions and actions ... were within the scope of its authority and were made in good faith, and therefore are entitled to deference under the business judgment rule. Plaintiff failed to raise a triable issue of fact, as he failed to submit any evidence to substantiate his allegations of bad faith.")(citations omitted.)[17]

---

[17] *Accord Zuckerbrod, supra*, 113 A.D.3d at 676, 979 N.Y.S.2d at 121 ("In opposition to defendants' prima facie showing ... the appellant failed to adduce evidence to substantiate her allegations of fraud, bad faith, or breach of fiduciary duty and, thus, failed to raise a triable issue of fact.") (citations omitted); *North Fork Preserve, Inc. v. Kaplan*, 68 A.D.3d 732, 733, 890 N.Y.S.2d 93, 95 (2d Dept. 2009)("[T]he defendants established, prima facie, that there were entitled to judgment as a matter of law based on the business judgment rule .... Inasmuch as the plaintiffs failed to produce any evidence to substantiate their allegations of fraud, bad faith, the

Moreover, in case after case over the past century, New York Courts have uniformly recognized that managers' decisions regarding the compensation to be paid to employees and others providing services to a business entity are entitled to the deference and presumption of validity afforded by the business judgment rule. Thus, the New York Court of Appeals held that:

> The statements of conclusions which express no more than a difference of opinion between a stockholder and directors as to the value of an employee's services or the expediency of his employment whether it will advance the corporation's interests will not serve in a complaint as sufficient in law to put a director on the defensive. Nor may judicial process be invoked to challenge the judgment of directors except when fraud is alleged or conduct so oppressive as to be its equivalent, and facts are pleaded which afford a basis for such allegations.
>
> ***
>
> [T]he question whether the corporation's interests will be advanced by employment contracts ... which were based in part on incentive compensation, are matters for the judgment of the directors with which the courts will not interfere in the absence of a factual showing of misconduct amounting to bad faith.

---

waste of corporate assets, or the breach of fiduciary duty, the Supreme Court properly granted the defendants' motion for summary judgment ... .")(citations omitted); *Hui v. Ho*, 1 A.D.3d 274, 767 N.Y.S.2d 582, 583 (1st Dept. 2003)("The complaint was properly dismissed since the challenged conduct of defendants ... did not violate the Shareholders' Agreement, and was otherwise shielded from judicial scrutiny under the business judgment rule. Plaintiffs failed to meet their burden to demonstrate that defendants acted in bad faith or to serve interests other than those of the corporation.")(citation omitted); *Bennett v. Instrument Systems Corp.*, 66 A.D.2d 708, 709, 411 N.Y.S.2d 287 (1st Dept. 1978)(granting summary judgment dismissing a derivative claim for breach of fiduciary duty against corporate directors holding that "[t]he defendants ... made a factual showing of the legality, propriety and fairness of their actions ... . Under these circumstances, the plaintiff was required to come forward with some factual showing to indicate that the Directors were not following their sound business judgment but were acting in bad faith. *** [P]laintiff [has not] come forward with any affidavit to substantiate the charges of waste, fraud and breach of fiduciary duty as alleged in the complaint.")

Kalmanash v. Smith, 291 N.Y. 142, 155-56 (1943)(citations omitted.)[18]

Here, Laifer has made the requisite showing that it was within his authority to agree to consulting fees on Heartwatch's behalf. The Agreement provides that Laifer, as Manager, "shall have the power and authority on behalf of this Company to do all things as set forth in Sec. 202(a)-202(q) of the New York Limited Liability Company Law[19] which includes the power to "elect or appoint managers, employees and agents of the limited liability company, define their duties and fix their compensation." N.Y. Limited Liab. Co. Law §202(h).

Laifer has also made the requisite showing that his decisions to pay consulting fees were made in good faith. Laifer had no personal interest in the compensation paid to others. Further, as set forth more fully in the FL Aff., the individuals who received consulting fees provided necessary services to Heartwatch, and were paid commensurate to their qualifications. In

---

[18] *Accord Sandfield v. Goldstein*, 33 A.D.2d 376, 380, 308 N.Y.S.2d 25, 29 (3d Dept. 1970)("The amount of compensation to be paid corporate officers is properly a matter for the business judgment of the board of directors. Their judgment in this respect is final and subject to interference by the court only in cases of clear abuse[,] bad faith or fraud ... .")(citation, internal quotations, ellipses, omitted); *Wellington Bull & Co. v. Morris*, 132 Misc. 509, 512, 230 N.Y.S. 122, 128 (Sup.N.Y. 1928), *aff'd* 226 A.D. 868, 235 N.Y.S. 906 (1st Dept. 1929)("Subject to interference by the Courts in cases of clear abuse, the directors of a corporation ... have the right to fix the compensation of executive officers for services rendered to the corporation. The directors are the persons chosen by the stockholders to pass upon such matters, and ordinarily their decision as to the amount of compensation is final."); *Ferguson v. Fergus Enterprises, Inc.*, 13 Misc.2d 235, 239, 175 N.Y.S.2d 974, 977 (Sup. N.Y. 1958)("The business judgment rule is that stockholders may not question the judgment of directors who have the right to fix the compensation of executive officers for services rendered and to be rendered to the corporation, escept when fraud is alleged or conduct so oppressive as to be its equivalent and facts are pleaded which afford a basis for such allegations.")(citations, internal quotations, omitted); *Mautner v. Hirsch*, 1992 WL 106318, *6 ("Under New York law, when an independent majority of a Board of Directors approves an officer's compensation, the business judgment rule precludes a stockholder from challenging the amount of the compensation in the absence of bad faith.")(citations omitted.)

[19] Agreement, Art. III, par. 7(e).

addition, of course, the consulting fees were all disclosed fully to MC in the many financial documents which Heartwatch provided to it.

Accordingly, Laifer had demonstrated that his decisions to pay consulting fees fall within the protection of the business judgment rule, and are therefore presumptively valid. Absolutely no evidence has come to light which would in any way negate this presumption. Moreover, the Agreement expressly provides that Laifer can have no liability to Heartwatch or its members "except if there is a final judgment or adjudication adverse to the Manager that establishes that his acts of omissions involved intentional misconduct or a knowing violation of law or that he personally gained in fact a financial profit or other advantage to which he was not legally entitled." Agreement, Art. III, par. 7(g). MC cannot establish intentional misconduct, and does not even allege that Laifer committed a knowing violation of law or personally gained from the consulting fees paid to unrelated third parties. Accordingly, Laifer should be granted summary judgement dismissing MC's claim that he breached the Agreement by agreeing to excessive consulting fees.

POINT THREE

MC'S FAILURE TO OBJECT TO LAIFER'S SUPPOSED BREACHES ESTABLISHES THAT LAIFER DID NOT BREACH ANY AGREEMENTS, AND IN ANY EVENT, MC WAIVED ANY CLAIM OF BREACH

The Agreement does not bar Laifer from receiving compensation for his services as medical director of Heartwatch, and that is no doubt why MC, although it complained about the amount of Heartwatch's expenses including Laifer's compensation, never previously claimed that Laifer had breached the Agreement by accepting compensation from Heartwatch. Similarly,

Heartwatch did not breach the Letter Agreement, and MC never previously claimed such a breach, because, although Heartwatch expended more than was contemplated during some months, it did not spend MC's $250,000 initial investment in the six month period covered by the Letter Agreement, which was expressly stated to be the intent of the Letter Agreement's restriction on expenditures[20].

MC's acceptance of Laifer's and Heartwatch's performance under the Agreement and Letter Agreement, respectively, demonstrates that Laifer's interpretation of those agreements, and not MC's retroactive reinterpretation of them, is the correct one. "There is no surer way to find out what parties meant, than to see what they have done." *Brooklyn Life Ins. Co. of New York v. Dutcher*, 95 U.S. 269, 273 (1877). Thus, "[w]hen the parties to a contract of doubtful meaning, guided by self-interest, enforce it for a long time by a consistent and uniform course of conduct, so as to give it a practical meaning, the courts will treat it as having that meaning, even if as an original proposition they might have given it a different one." *Brooklyn Pub. Library v. City of New York*, 250 N.Y. 495, 501 (1929)(citation, internal quotations, omitted.)

During the entire course of performance under the Agreement, Laifer, with MC's knowledge, received compensation from Heartwatch. During the course of the six month restriction on Heartwatch's spending, it, with MC's knowledge, spent more than the monthly guidelines on more than one occasion. Yet MC did not claim either of these actions constituted a

---

[20] The Letter Agreement expressly provided that Heartwatch's spending would be restricted during the six months following MC's initial investment "so that [MC's] Investment will not be fully expended for a period of at least six (6) months from the date of [MC's] Investment." Letter Agreement, par.5. Since it is undisputed that Heartwatch did not spend $250,000 during the specified six month period, MC cannot show any damages from any overage during any of the constituent months, even if the Letter Agreement is construed, contrary to the parties' practical interpretation, to place binding limits on spending during individual months.

breach of contract, ***which establishes that they did not.*** *William C. Atwater & Co. v. Panama R. Co.*, 255 N.Y. 496, 501 (1931)("The courts in determining the obligations of a contract should, when possible, apply the same measure as the parties have applied in performing their obligations."); *Benevento v. RJR Nabisco, Inc.*, 1994 WL 577010 (S.D.N.Y. 1994)(granting *in limine* motion which was "in substance ... a motion for summary judgment"[21] based on interpretation given to contract by parties holding that "[w]hen one party performs under the contract and the other party accepts his performance without objection it is assumed that this was the performance contemplated by the agreement."[22]) (citations, internal quotations, omitted); *Nomura, supra* (same)(applying New York law.)[23]

If MC felt that Laifer's receipt of compensation, and Heartwatch's payment of consulting fees, were breaches of contract, than it waived those breaches by failing to object and accepting Laifer's and Heartwatch's performance, respectively. *Madison Ave. Leasehold, LLC v. Madison Bentley Associates LLC*, 30 A.D.3d 1, 3, 811 N.Y.S.2d 47, 49, *aff'd*, 8 N.Y.3d 59 (2006)(granting summary judgment dismissing landlord's complaint against lease guarantors holding that

---

[21] 1994 WL 577010 at *1.

[22] 1994 WL 577010 at *2.

[23] *Accord In Re Field's Will*, 11 A.D.2d 774, 775, 204 N.Y.S.2d 947, 949 (2d Dept. 1960)(holding that an informal pledge was a binding obligation because "[t]he [parties], by their acts and declarations after ... the pledge, interpreted decedent's subscription as binding. The interpretation given by the parties themselves, as shown by their acts, will be adopted by the Court ... .")(citations, internal quotations, omitted); *S. Ferry Bldg. Co. v. J. Henry Schroder Bank & Trust Co.*, 114 Misc. 2d 1045, 1049, 453 N.Y.S.2d 563, 566 (N.Y.C. Civ. Ct. 1982), *aff'd as modified*, 122 Misc. 2d 595, 473 N.Y.S.2d 94 (App. Term 1983)("[T]he doctrine of practical construction [applies] *** where [tenant] has never raised any objection to the form of certification furnished each year by [landlord]. It is evident then that certification required by the lease did not have to track the words of the lease in haec verba, so long as the statement was certified to be in accordance with the terms of the lease.")

"landlord's acceptance of the tendered rent with knowledge of the lease violation extinguishes the default as a matter of law."); *Fantigrossi v. Brannon Homes, Inc.*, 77 A.D.3d 1413, 1414, 909 N.Y.S.2d 240, 241 (4th Dept. 2010)(granting summary judgment dismissing breach of contract claim holding that "plaintiffs are deemed to have waived the right to assert that defendant breached the parties' contract based on defendant's deviation from that contractual specification inasmuch as such a deviation would have been obvious during plaintiffs' pre-closing inspection of the home.") *Scavenger, Inc. v. GT Interactive Software, Inc.*, 273 A.D.2d 60, 61, 708 N.Y.S.2d 405, 406 (1st Dept. 2000)("[A]s a matter of law ... defendant's claim that plaintiff breached the parties' agreement ... had been waived by ... defendant's acceptance and marketing of the games without objection.")(citation omitted); 22A N.Y.Jur.2d *Contracts*, §382 ("If a performance differing from that required by the contract is approved or accepted, such action may constitute a waiver of performance in accordance with the contract.")(citations, footnote, omitted.) Thus, assuming *arguendo* that Laifer's receipt of compensation and Heartwatch's payment of consulting fees differed from the performance required by the Agreement and Letter Agreement, respectively, MC's acceptance of such performance waived its right to assert claims for breach of contract.

POINT FOUR

MC'S DEMANDS FOR PUNITIVE DAMAGES AND ATTORNEYS' FEES SHOULD BE STRICKEN

MC seeks punitive damages of $2 million predicated on Laifer's alleged fraud. As MC's fraud claim should be dismissed for the reasons set forth in Point One, *infra*, its demand for punitive damages should likewise be stricken. Even if MC's fraud claim survived summary

judgment, however, it will not support an award of punitive damages.

"Punitive damages are not available in the ordinary fraud and deceit case, but are permitted only when a defendant's wrongdoing is not simply intentional but evinces a high degree of moral turpitude and demonstrates such wanton dishonesty as to imply a criminal indifference to civil obligations." *Hoeffner v. Orrick, Herrington & Sutcliffe LLP*, 85 A.D.3d 457, 458, 924 N.Y.S.2d 376, 377 (1st Dept. 2011)(affirming striking of demand for punitive damages)(citations, internal quotations, brackets, omitted.) At most, MC has alleged nothing more than "an ordinary fraud and deceit case." It has not alleged that Laifer's "fraud" was part of a pattern of wrongdoing, or that it was aimed at the public generally, or even that Laifer personally profited from his alleged fraud. Such allegations, even if taken at face value, simply do not evidence the "high degree of moral turpitude" necessary to sustain a demand for punitive damages. *Howard S. v. Lillian S.*, 62 A.D.3d 187, 193-94, 876 N.Y.S.2d 351, 355 (1st Dept. 2009) *aff'd*, 14 N.Y.3d 431 (2010)(affirming grant of motion limiting possible recovery for fraud by excluding punitive damages, holding that "punitive damages are inappropriate here, in that such damages have been limited to conduct evincing a high degree of moral turpitude and demonstrating such wanton dishonesty as to imply a criminal indifference to civil obligations. A wife's infidelity and her alleged concealment from her spouse of their child's paternity does not rise to such a high degree of moral turpitude.")(citations, internal quotations, brackets, omitted); *Baxter v. Javier*, 109 A.D.3d 493, 495, 970 N.Y.S.2d 567, 569-70 (2d Dept. 2013)(affirming summary judgment dismissing demand for punitive damages predicated on alleged fraud holding that "the plaintiff failed to raise a triable issue of fact as to whether the defendants' alleged conduct was so gross, wanton, or willful, or of such high moral culpability, as to warrant an

award of punitive damages.") (citations omitted); *Princes Point, LLC v. AKRF Eng'g, P.C.*, 94 A.D.3d 588, 944 N.Y.S.2d 493, 494 (1st Dept. 2012)(affirming denial of leave to amend to assert, *inter alia*, fraud claim and demand for punitive damages holding that "the [punitive] damages sought ... are unavailable to plaintiff on the claims asserted. *** [P]unitive damages are not warranted since plaintiff has not alleged wrongdoing evincing a high degree of moral turpitude that demonstrates such wanton dishonesty as to imply a criminal indifference to civil obligations.")(citations omitted.) Thus, MC's demand for punitive damages should be stricken.

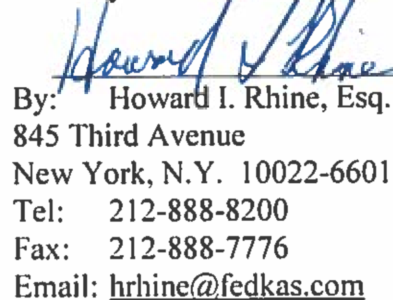
Mazel's demand for attorneys' fees should also be stricken. MC does not allege that an award of attorneys' fees is authorized by either statute or agreement between the parties. Absent that, the demand cannot stand. *Hooper Associates, Ltd. v. AGS Computers, Inc.*, 74 N.Y.2d 487, 491, 549 N.Y.S.2d 365, 366 (1989); *Mt. Vernon City Sch. Dist. v. Nova Casualty Co.*, 78 A.D.3d 1028, 1030, 912 N.Y.S.2d 98, 100-01 (2d Dept. 2010).

CONCLUSION

For all the foregoing reasons, as well as those submitted in the FL Aff. Laifer's motion seeking summary judgment dismissing plaintiff's claims should be granted in its entirety.

Dated: New York, New York
August 21, 2014

Feder Kaszovitz, LLP
Attorneys for the Defendant



By: Howard I. Rhine, Esq.
845 Third Avenue
New York, N.Y. 10022-6601
Tel: 212-888-8200
Fax: 212-888-7776
Email: hrhine@fedkas.com