To Be Argued By:
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New York Supreme Court

APPELLATE DIVISION — FIRST DEPARTMENT

ROBERT SHAPIRO,

Plaintiff-Appellant,

against

GABRIEL ETTENSON and DAVID NEWMAN,

Defendants-Respondents.

BRIEF FOR DEFENDANTS-RESPONDENTS

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Defendants-Respondents Gabriel Ettenson ("Ettenson") and David Newman ("Newman") (together, "Respondents") respectfully submit this memorandum of law in opposition to the appeal of Plaintiff-Appellant Robert Shapiro ("Shapiro" or "Appellant") from the August 16, 2015, Decision, Order and Judgment (the "Decision") of the Supreme Court (the "IAS Court") which entered summary judgment in favor of Respondents pursuant to CPLR 3212.

PRELIMINARY STATEMENT

Appellant and each of the Respondents are one-third members of ENS Health, LLC ("ENS" or "Company"), a New York Limited Liability Company formed in January 2012. Appellant commenced this action in November 2014, contesting the validity of an operating agreement (the "Operating Agreement") and amendment to the Company's articles of organization that were approved by a majority of the members of the Company (Respondents) nearly a year earlier, in December 2013.[1] Appellant also challenged Respondents' majority determinations in October 2014 to reduce Appellant's salary and, separately, to issue a ten-thousand dollar ($10,000) capital call to all members of the Company. Appellant contended that these and "any other actions for or on behalf of ENS" are invalid without the unanimous consent of all members. Respondents, by their

[1] In his appellate papers, Appellant abandons his challenge to the amendment of the articles of organization, and challenges only the adoption of the Operating Agreement. *See* September 6, 2016 Brief for Plaintiff-Appellant ("App. Br.") at 3-4 (Questions Presented); 20-23.

Counterclaims, sought a declaration that all of these actions were valid and binding decisions made by the vote of a majority of the members of the Company, under the controlling provisions of the New York Limited Liability Company Law, N.Y. Ltd. Liab. Co., §101, et seq. (the "LLC Law").

The parties agreed that the material facts relevant to a resolution of their claims were not in dispute, and stipulated to proceeding immediately to summary judgment. The IAS Court agreed with Respondents that, in the absence of a *written* operating agreement providing otherwise (or an applicable provision in the LLC Law or articles of organization specifically requiring unanimous consent) the LLC Law expressly authorized Respondents to act by majority vote. Finding that no such agreement or provision requiring unanimous consent existed, and with it being undisputed that Respondents together comprise a majority of the Company, the IAS Court held that Respondents' actions were authorized and binding.

As was the case before the IAS Court, the cornerstone of Appellant's argument on appeal is his claim that there exists some oral agreement among the parties requiring unanimity in connection with the governance of ENS. On appeal, Appellant contends that because there was some factual dispute between the parties as to this oral agreement's terms, summary judgment was improper. However, this argument is a red-herring because, as the IAS Court correctly concluded, any such oral agreement – assuming it even existed at all – is unenforceable as a matter of

law. Indeed, controlling law is unequivocal that (a) an operating agreement must be in writing to be enforceable, and (b) if there is no such written operating agreement, the default, majority-rules provisions of the LLC Law control.

As further detailed below, Appellant's other assorted arguments fare no better, and the fact that he relies on virtually no legal authority speaks volumes of their credibility. Several of Appellant's arguments were never even made to the IAS Court. Regardless, whether made to the IAS Court or not, every one of Appellant's arguments is bereft of legal support because they are all belied by controlling law, including the plain and unambiguous provisions of the LLC Law.

In short, the IAS Court's well-reasoned Decision should be affirmed.

COUNTER-STATEMENT OF QUESTIONS PRESENTED

1. Is Appellant precluded from relying on the terms of a purported oral agreement regarding the conduct of the members and governance of ENS? The IAS Court correctly held that he is, because any such oral agreement is unenforceable under the LLC Law.

2. Do the provisions of the LLC Law provide the default governing terms, conditions, and requirements for the for the governance and operation of the Company in the absence of any written operating agreement, or controlling provision in a written operating agreement or articles of organization? The IAS Court correctly held that they do.

3. In the absence of a written operating agreement providing to the contrary, were Respondents, as a majority in interest of the members, authorized under § 402(c)(3) to adopt an operating agreement for the Company in December 2013? The IAS Court correctly held that they were.

4. Were Respondents, as a majority in interest of the members, authorized to issue a voluntary capital call to all members of the Company in October 2014? The IAS Court correctly held that they were.

5. Were Respondents, as a majority in interest of the members, authorized to reduce Appellant's salary in October of 2014? The IAS Court correctly found that they were.

6. Given that the LLC Law prohibits oral operating agreements, was the IAS Court correct when it dismissed Appellant's causes of action for breach of contract and breach of the covenant of good faith and fair dealing based upon a purported oral operating agreement? Yes, the IAS Court was correct.

7. Did the IAS Court properly dismiss Appellant's cause of action for breach of fiduciary duty by the Respondents as insufficient in light of its other findings and § 409 of the LLC Law? Yes, it did.

STATEMENT OF UNDISPUTED MATERIAL FACTS NECESSARY TO DECIDE THIS APPEAL

Contrary to Appellant's assertions, the IAS Court properly concluded that the material facts necessary to decide the parties' motions for summary judgment are not in dispute. *See* RA 13-16 (summarizing material undisputed facts).

A. The Company and Its Members

ENS is a limited liability company that was formed in January 2012 by Appellant and Respondents under the LLC Law. RA 13; RA 46-47 at ¶¶ 4-5, 9; RA 59 at ¶ 4. Generally stated, the Company engages in the marketing, sale, and distribution of the HyperVibe Whole Body Vibration Machine, which is used for exercise, therapeutic, and performance enhancement purposes. RA 412, ¶ 4. The Company's primary asset is an exclusive distributorship agreement it has with HyperVibe Pty. Ltd. ("HyperVibe"), the manufacturer of the HyperVibe Whole Body Vibration Machine. *Id.*; App Br. at 4.

ENS was initially established as a member-managed limited liability company by default, because the Company's original articles of organization ("Articles of Organization") did not specifically provide for management of the Company by managers. RA 13; RA 412 ¶ 5; App. Br. at 5.[2] However, the original

[2] Under the LLC Law, a limited liability company may be member-managed or manager-managed. To be manager-managed, the articles of organization must state that the management is vested in managers. *See* LLC Law §§ 401(a), 408(a). If it does not, as was the case here in connection with the Company's original Articles of Organization, the company is deemed to be member-managed. *Id.*

Articles of Organization did not require the Company to be member-managed; they were silent on the issue altogether and provided only for the name of the Company, the location of its office, and designated an agent and address for service of process. RA 423-426; LLC Law § 401(a).

At formation, the Company did not have any "operating agreement," which is defined in the LLC Law as a "*written* agreement of the members concerning the business of a limited liability company and the conduct of its affairs … ." LLC Law § 102(u) (emphasis added); RA 13 ("[u]ntil December of 2013, ENS had no written operating agreement"). At all times since formation, Appellant and Respondents have been the only members of the Company, and each has been an equal one-third member of the Company, with equal one-third management rights and rights to one-third of the profits of the Company. RA 13; RA 46, ¶ 4; RA 59, ¶ 4.

B. The Approval of the Parties' Salaries in September 2013

In September 2013, the parties convened for a meeting (the "September 2013 Meeting") at the office of the Company's attorney. RA 241, ¶ 10; RA 414, ¶ 12; RA 556, ¶ 7. At the time, the Company still had no written operating agreement and the Articles of Organization were the same as originally filed. RA 13; RA 240, ¶ 7; RA 414, ¶ 15; RA 556, ¶ 7. Among the topics discussed at the September 2013 Meeting was the payment of salaries to the members, and the members voted unanimously to approve monthly salaries to be paid to them by the

Company, depending upon the cash needs of the business, on the basis of the following annualized rates: Shapiro, $50,000, Ettenson, $100,000, and Newman, $100,000. RA 50, ¶ 26; RA 63, ¶ 26.

Following the September 2013 Meeting, the Company's attorney circulated by e-mail for the members' consideration a proposed Unanimous Written Consent of the Members of the Company (the "Proposed Consent"). RA 415, ¶ 17; 427-428. The Proposed Consent provided that the members' salaries would "be reviewed by the Members of the Company at the end of the ninety (90) day period commencing as of the date of this Unanimous Written Consent [October 1, 2013] and may be extended or modified at such time by the unanimous consent of the Members." *Id.* None of the parties ever signed the Proposed Consent. RA 77, ¶ 55; RA 415, ¶ 17; RA 556, ¶ 9. However, in accordance with the parties' votes at the September 2013 Meeting, salaries were paid by ENS to all members – including in months following the expiration of the suggested ninety day period set forth in the unsigned Proposed Consent. RA 77, ¶ 57; RA 91, ¶ 57. Appellant, accepted his salary and never objected to the payment of salaries to Respondents. *Id.*

C. The Operating Agreement and Amendment to the Company's Articles of Organization

In connection with the September 2013 Meeting, and particularly in light of increasing acrimony among the members relating to Appellant's non-participation in the Company's business, the Company's attorney recommended that the

members of ENS get an operating agreement in place and, later, circulated a draft. *See* RA 241-243, ¶¶ 11-17; RA 415-418, ¶¶ 18-30; RA 557, ¶¶ 10-12. Although other drafts and e-mails were exchanged on the subject, Respondents were unable to secure Appellant's participation in that process.[3] As of December 13, 2013, the Company still had not finalized any operating agreement, despite the advice of the Company's attorney and Respondents' efforts. RA 13, 16; LLC Law § 102(u). *See also* App. Br. at 5 (it is "undisputed that no written operating agreement was adopted [by the parties] … until December 13, 2013"); RA 47, ¶ 11; RA 61, ¶ 11.

Thus, on December 13, 2013, Respondents, acting as a majority of the members of the Company, voted under the LLC Law to approve and adopt the Operating Agreement for the Company. RA 13; RA 47, ¶ 8; RA 60, ¶ 8; RA 195-226. Respondents also authorized an amendment to the Company's Articles of Organization to provide for the management of the Company by one or more managers. Newman thereafter signed and caused to be filed with the New York Secretary of State a Certificate of Amendment of the Company's Articles of

[3] While not material to this appeal, Respondents are constrained to correct the misleading picture of reality painted by Appellant, as the record is actually quite clear that Appellant had been asked as far back as *July 2013* to move the operating agreement process along with the Company's attorney. *See* RA 34, ¶ 8, RA 98. Yet noticeably absent from the record is any evidence (because there is none) that Appellant ever actually did anything to participate in that process. To the contrary, the record is unrebutted that Appellant has been totally absent from the Company's business for years, and that he did nothing except obstruct Respondents' efforts to get an operating agreement in place cooperatively, including by ignoring the drafts that were circulated as far back as November 12, 2013, and by failing to ever provide any feedback on Respondents' comments to those drafts. RA 415-418, ¶¶ 18-30.

Organization (the "Amendment") on behalf of the Company, which added a new Article FOURTH to the Articles of Organization, providing that the Company "shall be managed by one or more managers." RA 228-231.

Neither the Operating Agreement nor the Amendment changed the parties' ownership interests in ENS or their entitlement to equal one-third shares of the current profits of the Company. RA 534; RA 546. Moreover, each of Shapiro, Ettenson, and Newman was designated as a manager of the Company, meaning that management of the Company continued to be vested in equal one-thirds among the members. RA 511, § 6.01. Consistent with the LLC Law, the Operating Agreement provided that, except as otherwise provided in the Operating Agreement or as required by the LLC Law, any action requiring the approval of the managers or members could be approved by a majority of the members or managers. RA 14; RA 541, § 6.03.[4] All of the requisite notices and consents relating to Respondents' actions were duly delivered to Appellant in accordance with the LLC Law. RA 15; RA 227.[5]

[4] The Operating Agreement includes some exceptions to the default majority-rules provision that are not at issue here. In some cases these exceptions actually provides the members with even greater protections than they would otherwise have under the default provisions of the LLC Law. For example, it includes unanimity requirements for a material change in the purposes or nature of the Company's business, the admission of new members or the issuance of additional membership interests, a merger or consolidation with another entity, the disposition of all or substantially all of the Company's assets, or a dissolution, liquidation or winding up of the Company. RA 511-512.

[5] In his brief, Appellant goes to great lengths to detail the "negotiating history" of the Operating Agreement – in reality, drafts circulated by the Company's attorney with comments from Respondents – all without any feedback from Appellant, despite the Company's attorney's admonition that each of the members should "consult independent counsel" to advise them. *See*

Appellant initially objected through counsel to Respondents' actions by letter dated December 24, 2013. RA 536-539. Appellant claimed that the Operating Agreement was "without legal force and effect" and requested that Respondents "immediately rescind the actions taken and withdraw the … Operating Agreement." RA 538. Respondents responded through counsel by letter dated January 2, 2014, declining to rescind the Operating Agreement because it "is valid, binding, and consistent with the [LLC] Law in all respects." RA 542. Appellant did not respond or take any further action to challenge the Operating Agreement (or Amendment). RA 70, ¶ 18; RA 419, ¶ 33; RA 557, ¶ 12. To the contrary, Appellant began to participate from time to time in a regular Tuesday meeting that was put in place by § 6.09 of the Operating Agreement. *Id.*

D. The October 2014 Capital Call and Salary Reduction

The parties all participated in the Company's regular Tuesday meeting held on October 14, 2014 (the "October 2014 Meeting"). Prior to that meeting, Newman circulated an e-mail to all members detailing the Company's financial

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App. Br. at 9-15. Whatever the reasoning for his discussion of earlier drafts, the simple fact is that Appellant concedes elsewhere that none of these drafts were ever approved by the members. *See* App. Br. at 5 ("It is undisputed that no written operating agreement was adopted [by the parties] … until December 13, 2013[.]") Respondents have freely admitted that they endeavored to secure Appellant's cooperation in the process of adopting an operating agreement, but were consistently stonewalled by Appellant's inaction – leaving them with no choice but to act as a majority in December 2013. *See, e.g.*, RA 413 – 419; RA 555-557. In other words, whatever was discussed prior to Respondents' approval of the Operating Agreement is ultimately irrelevant, and certainly not a material fact, with respect to the narrow question before the Court: whether Respondents were within their rights to adopt the Operating Agreement.

status and indicating that ENS had a shortfall of approximately $31,000 that needed to be made up. RA 553. Respondents therefore voted at the October 2014 Meeting – in Appellant's presence – to request from each of the members an additional capital contribution of ten thousand dollars ($10,000). Respondents also voted at that meeting to reduce Appellant's salary to zero dollars ($0), because of his ongoing dereliction of his duties to ENS. RA 15, RA 232.[6] The reduction in Appellant's salary did not impact Appellant's rights to distributions of profits as a one-third member of the Company.

Immediately following the October 2014 Meeting, Respondents signed and delivered to Appellant a Notice of Action Taken at Meeting Held on October 14, 2014 (the "Notice of Action"), confirming their votes at the October 2014 Meeting to "(i) reduce the salary of Robert Shapiro to zero dollars ($0), for the reasons discussed at the meeting held on October 14, 2014; and (ii) request of each of the Members an additional Capital Contribution of ten thousand dollars ($10,000.00) each." RA 15; RA 232. Enclosed with the Notice of Action was a Notice of Call for Additional Capital Contributions from Members, dated October 15, 2014 (the "Capital Call"). RA 233. The Capital Call formally requested, but did not

[6] In addition to Appellant's general failure to carry out his responsibilities, Appellant's dereliction of his duties included a failure over the course of at least a year to prepare a business plan for HyperVibe. That business plan is required pursuant to the Company's exclusive distributorship agreement with HyperVibe, and a failure to provide HyperVibe with the business plan could have authorized HyperVibe to terminate the Company's exclusive distributorship agreement. RA 419-420, ¶¶ 34-39.

require, from each of the members of the Company an additional capital contribution of ten thousand dollars ($10,000) by November 21, 2014. *Id.* Appellant filed the underlying action slightly more than a month later, on November 17, 2014. RA 44.

E. The Underlying Action

The cornerstone allegation of Appellant's Verified Complaint was his claim that there was some oral agreement among the members of ENS relating to its governance. In particular, Appellant alleged that:

> In connection with the formation of ENS, Ettenson, Newman and Shapiro, expressly agreed that ENS would be member managed, that all material decisions would be by unanimous vote of all the members and that in the event of a capital call, that no members inability or decision not to make any payment on account of a capital call, would result in any diminution of that member's membership interest.

RA 47, ¶ 6.[7] On the basis of this claim, Appellant asserted causes of action for declaratory relief, breach of fiduciary duty, and breach of contract seeking the following relief: (1) a declaratory judgment that the Operating Agreement is invalid, (2) a declaratory judgment that the Capital Call is invalid, (3) a declaratory judgment that "no capital call can be made unless all the terms thereof are agreed to by all the members of ENS," (4) a declaratory judgment "that no member of

[7] In other words, Appellant's core contention is that the parties coincidentally had the prescience to specifically discuss, but not reduce to writing (despite having Company counsel available to advise them) each of the specific issues that eventually developed among them *years* after the formation of ENS.

ENS may receive any salary that is not consented to by all the members of ENS"; (5) a declaratory judgment "that no actions for or on behalf of ENS Health, LLC be taken absent the unanimous consent of the members," and (6) damages "in the amounts, if any, of any salary paid to [Respondents] Ettenson and Newman which was in excess of any salary paid to [Appellant] Shapiro other than what was agreed to for the period October 1, 2013 through December 31, 2013." RA 53-54.

Respondents filed a Verified Answer, Affirmative Defenses, and Counterclaims on January 23, 2015. RA 59-81. The Counterclaims sought a declaratory judgment as follows: (1) that Respondents were authorized to adopt the Operating Agreement for the Company, that the Operating Agreement was duly and properly adopted in accordance with the LLC Law, and that the Operating Agreement and each of its provisions are valid and binding on the Company and all of its members, (2) that Respondents were authorized to amend the Company's original Articles of Organization, that the Amendment was duly and properly authorized in accordance with the LLC Law, and that the Amendment is valid and binding on the Company and each of its members, (3) that the default provisions of the LLC Law are the governing terms, conditions, and requirements for the conduct of the members of the Company for the operation of the Company in the absence of any controlling provision of the Operating Agreement or valid and binding written operating agreement for the Company, (4) that Respondents were

authorized to issue the Capital Call, and that the Capital Call is valid and binding on all members in all respects, and (5) that the payment of salaries to the members of the Company beyond December 2013 was and is authorized, that Respondents were authorized to reduce Appellant's salary to zero dollars ($0) by majority vote, and that the reduction of Appellant's salary to zero dollars ($0) is valid and binding.

THE DECISION BELOW

Agreeing that no discovery was necessary in view of the undisputed facts detailed above, the parties stipulated to proceeding immediately to summary judgment. RA 57-58. After briefing and oral argument, the IAS Court issued its Decision granting summary judgment in favor of Respondents on August 16, 2015. *See* Decision (RA 10-26).

The IAS Court began its analysis by recognizing that the validity of the Operating Agreement is at "the heart of the parties' dispute[.]" RA 16. With respect to the Respondents' majority vote to adopt the Operating Agreement, the IAS Court held that:

> Where an operating agreement … does not address certain topics, a limited liability company is bound by the default requirements set forth in the Limited Liability Company Law. *Matter of 1545 Ocean Ave. LLC*, 72 AD3d 121, 129 (2d Dept 2010). The LLC Law defines "[o]perating agreement" as "any written agreement of the members concerning the business of a limited liability company and the conduct of its affairs and complying with section four hundred seventeen of this chapter." LLC Law § 102(u). As discussed above, it is undisputed that ENS had no

> written operating agreement prior to the Operating Agreement. Therefore, the LLC Law governs the issue of whether Newman and Ettenson properly adopted the Operating Agreement pursuant to the LLC Law.

See RA 16.

The IAS Court then proceeded to analyze the relevant provisions of the LLC Law, including §§ 102, 401, 402, and 408. RA 17-18. The IAS Court concluded that, in accordance with "section 401(a) of the LLC Law, prior to the Operating Agreement, management of ENS was vested in its three members" and that under sections "402(a), (c) (3), and (f), Shapiro, Ettenson, and Newman, were each entitled to vote in proportion to their one-third ownership interests" to "adopt, amend, restate or revoke the articles of organization or operating agreement." RA 18. Because Respondents "clearly constitut[ed] a majority sufficient, under the LLC Law, to adopt the Operating Agreement and amend the articles of organization" the IAS Court concluded that Respondents had made a prima facie showing that the Operating Agreement and Amendment were "valid and enforceable." RA 18-19.

The IAS Court then rejected each of Appellant's arguments seeking to rebut Respondents' prima facie showing that the Operating Agreement was validly adopted. RA 19-20. First, the IAS Court rejected Appellant's attempt to read a unanimity requirement into § 417 of the LLC Law – as well as his attempt to argue that those voting requirements changed once ninety days had passed after the filing

of the initial articles of organization – as "not supported by the plain language of the LLC Law." *See* RA 19-20 ("Nothing contained in section 417 requires 'all' of the members of a limited liability company to enter into an operating agreement."). Second, the IAS Court rejected Appellant's reliance on the terms of the purported oral agreement as contrary to § 102(u) of the LLC Law, which provides that only a *written* operating agreement may override the default provisions of the statute. RA 20 ("Prior to the Operating Agreement, there was no 'written' operating agreement, and, therefore, the default provisions of the LLC Law controlled.")

With respect to the Capital Call, the IAS Court held that its issuance was "consistent with both the LLC Law and section 7.01 [of] the Operating Agreement." RA 20-12. The IAS Court rejected Appellant's argument that the Capital Call was improper under two inapplicable provisions of the LLC Law, § 502 (applicable to mandatory capital calls) and § 417(b) (applicable to amendments of an operating agreement). RA 20-21. With respect to the former, the IAS Court found that § 502 of the LLC Law was not implicated because "the capital call was not obligatory[.]" *Id*. *See also* RA 233. With respect to the latter, the IAS Court held that § 417(b) was facially inapplicable because it only applied to *amendments* to an existing operating agreement. RA 21.

The IAS Court also rejected Appellant's challenge to Respondents' decision to reduce his salary. RA 21-22. First, the IAS Court properly found that § 411 of

the LLC Law, known as the "interested manager" provision, was inapplicable because Respondents had not "derived a personal benefit" from the decision to eliminate Appellant's salary. RA 21. Second, the IAS Court found that Appellant failed to raise an issue with respect to Respondents' compliance with § 9.01 of the Operating Agreement, which applies only to "Management Fees and Expenses," not salaries. RA 22.

The IAS Court further sustained the Capital Call and reduction of Appellant's salary based on the majority-rules default provisions of the LLC Law as an alternative ground for granting relief. RA 22. It dismissed Appellant's other claims for (1) breaches of the parties' oral agreement; (2) breaches of the implied covenant of good faith and fair dealing; and (3) breaches of fiduciary duties, and entered summary judgment in favor of Respondents. RA 22-26.

ARGUMENT

I THE STANDARD FOR SUMMARY JUDGMENT

A party is entitled to summary judgment if, "upon all the papers and proof submitted, the cause of action or defense shall be established sufficiently to warrant the court as a matter of law in directing judgment." CPLR 3212(b). The proponent of summary judgment must make a prima facie showing of entitlement to judgment as a matter of law, supported by evidence in the record demonstrating the absence of a material issue of fact. *See Alvarez v. Prospect Hospital*, 68 N.Y.2d 320, 324

(1986). In contrast, a party opposing summary judgment must establish by admissible evidence the existence of a genuine material issue of fact. *See W.W.W. Assoc. v. Giancontieri*, 77 N.Y.2d 157, 164 (1990). Mere "conclusions, expressions of hope or unsubstantiated allegations or assertions are insufficient." *Zuckerman v. City of New York*, 49 N.Y.2d 557, 562 (1980) (internal citations omitted).

Summary judgment was appropriate here because the parties' respective claims, which effectively mirror each other, are all centered on the application of unambiguous provisions of the LLC Law to material facts that are not in dispute. Appellant himself acknowledged that there were no material issues that required a trial, and stipulated to proceed immediately to a determination of the issues in this case by way of summary judgment. RA 57. Having received an unfavorable decision, Appellant reverses course on appeal, arguing for the first time that briefing of the motions revealed "material disputed issues of fact." App. Br. at 17. However, as detailed below, the "disputed facts" upon which Appellant's argument is based – namely, the terms of a purported oral agreement between the parties – are in fact completely immaterial and insufficient to preclude summary judgment in Respondents' favor. *See* RA 16; LLC Law § 102(u).

II THE PROVISIONS OF THE LLC LAW CONTROL OVER ANY ALLEGED UNENFORCEABLE ORAL AGREEMENT

The central theory of Appellant's case is his claim that there was some "express agreement" among the parties "in connection with the formation of ENS" regarding the governance of the Company, providing (according to Appellant):

> [T]hat ENS would be member managed, that all material decisions would be made by unanimous vote of all the members, and that in the event that the members unanimously agreed to make a capital call, that no members inability or decision not to make any payment on account of a capital call, would result in any diminution of that member's membership interest.

App. Br. at 6; *see also* RA 47, ¶ 6; RA 50, ¶¶ 24-25; RA 52-53 ¶¶ 39, 43-44; RA 240, ¶ 5. Appellant, however, admits that this agreement was never reduced to writing. *See* App. Br. at 5 (admitting that it is "undisputed that no written operating agreement was adopted … until December 13, 2013"); RA 47, ¶ 11; RA 240, ¶ 7. On appeal, Appellant contends that, in the IAS Court, Respondents disputed his account of the terms of this purported oral agreement, and that there exists a "factual dispute as to the content" of the parties' "verbal agreement," precluding summary judgment. *See* App. Br. 6-8, 23. Appellant misses the point.

The "content" of the supposed "verbal agreement" being claimed by Appellant is irrelevant and immaterial because any such agreement – whatever Appellant claims the terms to be – is unenforceable as a matter of law. Indeed, the LLC Law requires that a New York limited liability company be operated in

accordance with its provisions, subject to any provisions that may be contained in the company's articles of organization or an operating agreement. *See* LLC Law §§ 401(a), 408(a). An operating agreement, however, must be in writing to have any force or effect. *See* LLC Law § 102(u) (defining an "operating agreement" as a "written agreement of the members concerning the business of a limited liability company and the conduct of its affairs[.]") (emphasis added).[8] In the absence of any such written operating agreement, the default provisions of the LLC Law "become the terms, conditions, and requirements for the conduct of the members for the operation of the limited liability company." *Spires v. Lighthouse Solutions, LLC*, 778 N.Y.S.2d 259, 266 (Sup. Ct. Monroe Co. 2004). *See also* LLC Law §§ 401(a) and 408(a) (requiring that member-managed and manager-managed companies, respectively, be managed "in accordance with this chapter"); *Ross v. Nelson*, 54 A.D.3d 258, 259 (1st Dept. 2008) (recognizing the applicability of the default provisions of the LLC Law in the absence of a "specific mechanism in the operating agreement"); *In re 1545 Ocean Ave. LLC*, 72 A.D.3d 121, 129 (2nd Dept. 2010) ("Where an operating agreement … does not address certain topics, a limited liability company is bound by the default requirements set forth in the Limited

[8] This requirement is analogous to New York's statute of frauds, General Obligations Law § 5-701, which requires certain agreements to be in writing to be enforceable. As the Court of Appeals has observed, the purpose of this requirement is to decrease uncertainties, litigation, and opportunities for fraud and perjury. *See William J. Jenack Estate Appraisers and Auctioneers, Inc. v. Rabizadeh*, 22 N.Y.3d 470, 476 (2013). In other words, this policy targets precisely the kinds of "he said, she said" claims that LLC Law § 102(u) was carefully crafted to avoid.

Liability Company Law."); *Manitaras v. Beusman,* 56 A.D.3d 735, 736 (2nd Dept. 2008) (holding that, where "the operating agreement … is silent" the "default provisions of the Limited Liability Company Law apply."); *Man Choi Chiu v. Chiu,* 71 A.D.3d 646, 647 (2nd Dept. 2010) (holding that "the default provisions of the Limited Liability Company Law apply, as neither the articles of organization nor the alleged operating agreement of the LLC contain a provision concerning expulsion of members."); *Overhoff v. Scarp, Inc.*, 812 N.Y.S.2d 809, 816 (Sup. Ct. Erie Co. 2005) (holding that it is "clear … that the [LLC Law] statute provided default procedures for LLCs, which will apply to LLC proceedings unless the operating agreement of the particular LLC clearly provides otherwise.").

Thus, Appellant's reliance on the existence of a supposed oral agreement among the parties is ineffective, and certainly not a material fact precluding summary judgment, because as a matter of law only a written operating agreement can override the default provisions of the LLC Law. *See* RA 16 ("[I]t is undisputed that ENS had no written operating agreement prior to the Operating Agreement. Therefore, the LLC Law governs the issue of whether Newman and Ettenson properly adopted the Operating Agreement pursuant to the LLC Law."). In other words, in the absence of such an agreement – which Appellant admits was the case here prior to December 13, 2013 – the only issue to be resolved is whether Respondents' actions were authorized under the LLC Law. *See Jones v. Bill*, 10

N.Y.3d 550, 554 (2008) ("[a]s a general proposition, we need not look further than the unambiguous language of the statute to discern its meaning").[9] As detailed further below, the IAS Court correctly concluded that they were. RA 18-19.

III THE OPERATING AGREEMENT WAS ADOPTED IN BY A MAJORITY IN ACCORDANCE WITH THE LLC LAW

As majority of the members of the Company, and in the absence of a written operating agreement providing to the contrary, Respondents were expressly authorized under § 402(c)(3) of the LLC Law to adopt the Operating Agreement. RA 18-19 ("Together, Ettenson and Newman owned two-thirds of ENS, clearly constituting a majority sufficient, under the LLC Law, to adopt the Operating Agreement and amend the articles of organization.")[10]

[9] Although he continues on appeal to cling to his claim that there existed some oral operating agreement among the members, and that the terms of that oral agreement are somehow material to the issues in this case, Appellant elsewhere actually admits both that (a) it is "undisputed that no written operating agreement was adopted [by the parties] … until December 13, 2013" (App. Br. at 5), and (b) "if the members do not cover a particular concept in their operating agreement, the relevant LLC Law default provision for such concept would then govern their entity" (App. Br. at 20-21). And though this admission ends the inquiry as a legal matter, Respondents are nevertheless constrained again to respond to Appellant's incorrect assertion that Respondents "agree that there was a verbal arrangement, [but] dispute [his] version of it." App. Br. at 6. Notably, Appellant's claim is not supported by a citation to the record which, in truth, actually makes clear Respondents' view that "it was never agreed (or even discussed) that unanimity was required for this decision or that unanimity would be required for any salary (or other) decisions in general.") *See* RA 413, ¶ 8; RA 415, ¶ 16.

[10] As noted above, although Appellant challenged in the IAS Court Respondents' authority under the LLC Law to adopt the Amendment to the Company's articles of organization, he has abandoned that claim on appeal. Indeed, there can be no serious argument that the Amendment was not authorized, because the LLC Law specifically authorized Respondents to do so by majority vote. *See* LLC Law §§ 211, 213, 402(c)(3).

Appellant concedes that each of the parties to this litigation is an equal one-third member of ENS. RA 46, ¶ 4. Any two members of the Company therefore comprise a "majority in interest of the members" of the Company. RA 18-19; LLC Law § 102(o) ("Majority in interest of the members means, unless otherwise provided in the operating agreement, the members whose aggregate share of the current profits of the limited liability company constitutes more than one-half of the aggregate of such shares of all members."). As Appellant also concedes, the Company had no written operating agreement prior to December 13, 2013. *See* App. Br. at 5 (it is "undisputed that no written operating agreement was adopted [by the parties] … until December 13, 2013"); *see also* RA 13. Thus, at least before December 13, 2013, the default provisions of the LLC Law governed the parties' rights to adopt an operating agreement.

Section 402(c)(3) of the LLC Law provides, in relevant part, as follows:

> Except as provided in the operating agreement**,** whether or not a limited liability company is managed by the members or by one or more managers, the vote of a majority in interest of the members entitled to vote thereon shall be required to … adopt**,** amend, restate or revoke the articles of organization or operating agreement …

LLC Law § 402(c)(3) (emphasis added). In other words, unless there is a written operating agreement providing otherwise, a "majority in interest of the members" is all that is necessary to "adopt" an operating agreement. It is undisputed that this

is precisely what occurred on December 13, 2013, when Respondents acted without a meeting (as permitted under § 407 of the LLC Law[11]) to adopt the Operating Agreement. Appellant did not offer any basis below, and presents no viable argument on appeal, for departing from the IAS Court's holding that the Operating Agreement was properly adopted under § 402(c)(3).

In particular, Appellant contended in the IAS Court that Respondents' actions were contrary to § 417 of the LLC Law. Appellant claimed that, pursuant to that section, (1) "an operating agreement is to be entered into by all but not less than all of the members, and certainly not just a majority," and (2) an operating agreement could only be entered into by the members before, at the time of or within ninety days after the filing of the articles of organization. *See, e.g.*, RA 19-20. However, Appellant's assertion that § 417 requires an operating agreement to be approved by "all of the members" is simply not supported by the plain text of § 417. The word "all" appears nowhere in § 417(a), which refers only to the requirement of members generally to "adopt a written operating agreement" and says nothing whatsoever about there being any unanimity requirement. In fact, the *only* reference in the LLC Law to the quorum required to adopt an operating

[11] Section 407 of the LLC Law provides that, whenever the members of a limited liability company are permitted to take action by vote, "such action may be taken without a meeting, without prior notice and without a vote" by "the members who hold the voting interests having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting." LLC Law § 407. Appellant does not take issue with or challenge the procedure utilized by Respondents under § 407.

agreement is set forth in § 402(c)(3), which states quite clearly that the vote of "a majority in interest of the members" is all that is required to "adopt**,** amend, restate or revoke the … operating agreement." *See* LLC Law § 402(c)(3) (emphasis added).[12] Thus, the IAS Court correctly concluded that "[n]othing contained in section 417 requires 'all' of the members of a limited liability company to enter into an operating agreement" nor does "section 417 prohibit a majority of the members from entering into an operating agreement." RA 19.

With respect to Appellant's contention that the Operating Agreement was unenforceable pursuant to § 417(c) because it was not entered into either before, at the time of or within the ninety day period after the filing of the articles of organization, Appellant similarly misread the statute. Read in full, § 417(c) provides as follows:

> An operating agreement may be entered into before, at the time of or within ninety days after the filing of the articles of organization. Regardless of whether such agreement was entered into before, at the time of or after such filing, such agreement, may be effective upon the formation of the limited liability company or at such later time or date as provided in the operating agreement; provided, however, under no circumstances shall an operating agreement become effective prior to the formation of such company.

[12] In fact, the LLC Law is actually clear that that the default rule throughout is majority rules, unless the statute, the articles of organization, or a written operating agreement specifically provide otherwise. *See* LLC Law § 402(f) (providing that "[w]henever any action is to be taken … by the members or a class of members," the default rule is majority, "except as otherwise required or specified by this chapter or the articles of organization or the operating agreement.")

LLC Law § 417(c) (emphasis added).

Thus, read in context, § 417(c) merely permits (but does not require) the members of an LLC to adopt an operating agreement within a certain window of time, and if done within that window of time allows for it to be deemed effective retroactively (up to, and including, the formation date of the company). Section 417(c) does not, however, curtail in any way the rights of a majority of the members to adopt an operating agreement at a later date (although, admittedly, such an agreement could not be retroactively effective). That right remains intact under §402(c)(3). This was in fact the precise conclusion reached by the court in *Spires v. Lighthouse Solutions, LLC*, which held that "[t]here is no provision in the Limited Liability Company Law imposing any type of penalty or punishment for failing to adopt a written operating agreement" within the time frame set forth in § 417, and found that the members of the limited liability company at issue had validly adopted two separate (but temporary) operating agreements more than two and a half years after the company's articles of organization were filed. 778 N.Y.S.2d at 262-265. Thus, the IAS Court also correctly concluded that Appellant's interpretation of § 417 was simply "not supported by the plain language of the LLC Law." RA 20, *citing Matter of Rosenblum v. New York State Workers' Compensation Bd.*, 309 A.D.2d 120, 123 (1st Dep't 2003) ("interpretation of the statute" should "comport[] with its plain language"); *Matter of Cortland-*

Clinton, Inc. v. New York State Dept. of Health, 59 A.D.2d 228, 231 (4th Dep't 1977) ("the plain language used in a statute … should be construed in its natural and most obvious sense.").[13]

On appeal, Appellant now shifts to two new, but equally unsound, arguments never posited below: (1) that the parties were not "members" of the Company; and (2) that the relevant provisions of the LLC Law should in essence be re-written by this Court so as to eliminate the majority-rules provision. *See* App. Br. at 20-23.[14] These arguments too are unavailing, and contrary to the rule that a statute must be interpreted and applied in accordance with its plain meaning.

[13] Appellant also appears to have abandoned an argument he made to the IAS Court that, based on his counsel's experience, it is common practice and a requirement for all parties to sign an operating agreement. As Respondents argued to the IAS Court, whatever counsel's personal practice may be is irrelevant, because it is the provisions of the LLC Law control. As set forth above those provisions specifically authorize an operating agreement to be adopted by a majority and include no signature requirement. New York case law has recognized that an operating agreement approved by a majority is binding even if it has not been signed by all members. *See Bobrow v. Liebman*, 839 N.Y.S.2d 431, 2007 N.Y. Slip Op. 50795(U) at *8 (Sup. Ct. N.Y. Co. 2007) (relying on provision of an operating agreement that was signed by only three of four members of New York limited liability company). Indeed, there is nothing in the LLC Law at all that makes *signing* a prerequisite to the validity or enforcement of an operating agreement. *Id.* Rather, the LLC Law authorizes an operating agreement as long as it is "adopt[ed]" by a "majority in interest of the members." LLC Law §§ 402(c)(3), 402(f).

[14] Appellant also suggests in his brief, without legal support, that he cannot be bound by all of the provisions of the Operating Agreement, including its expulsion and arbitration clauses. *See* App. Br. at 15, 21. Not so. Appellant chose to become a member of a Company formed under the LLC Law, and he chose to do so without bargaining for rights different than the default, majority-rules provisions of the LLC Law. As noted above in footnote 13, if the Operating Agreement was validly adopted by a majority then Appellant is bound by it, whether or not he signed it. This Court has specifically recognized that operating agreements may include expulsion and arbitration clauses. *See Ross*, 54 A.D.3d at 259 (expulsion clause); *SSM Realty Group, LLC v. 20 Sherman Assoc., LLC*, 101 A.D.3d 433 (1st Dep't 2012) (arbitration clause).

A. The Parties Are "Members" Of the Company

Appellant's first argument to attack the plain words of § 402(c)(3) is that the parties are not "members" of the Company. *See* App. Br. at 20-21. Appellant arrives at this conclusion by torturing the definition of "Member" set forth in § 102(q), and his conclusion is plainly wrong.

First, the definition of "Member" in § 102(q) is not limited to a person who is "admitted in accordance with the 'operating agreement' and who has the rights and obligations specified in the 'operating agreement.'" App. Br. at 20. Section 102(q) actually defines a "Member" as follows:

> [A] person who has been admitted as a member of a limited liability company in accordance with the terms and provisions of this chapter and the operating agreement and has a membership interest in a limited liability company with the rights, obligations, preferences and limitations specified under this chapter and the operating agreement.

LLC Law § 102(q) (emphasis added). Obviously, if there is no operating agreement then there is no way to be admitted in accordance with one since, as stated, the absence of an operating agreement merely means that the default provisions of the LLC Law (*e.g.*, "the terms and provisions of this chapter") control. *See, e.g.*, *Ross*, 54 A.D.3d at 259; *In re 1545 Ocean Avenue, LLC*, 72 A.D.3d at 129; *Manitaras*, 56 A.D.3d at 736; *Man Choi Chiu*, 71 A.D.3d at 627; *Spires*, 778 N.Y.S.2d at 266; *Overhoff*, 812 N.Y.S.2d at 816.

Lest there be any doubt, Appellant's argument is belied specifically by § 602(a), titled "Admission of members." That provision provides as follows:

> A person becomes a member of a limited liability on the later of: (1) the effective date of the initial articles of organization; or (2) the date as of which the person becomes a member pursuant to this section or the operating agreement; provided, however, that if such date is not ascertainable, the date stated in the records of the limited liability company.

LLC Law, § 602(a). In other words, contrary to Appellant's argument, the statute itself confirms that each of the parties became "members" when the Company was formed by the filing of its original articles of organization with the Secretary of State on January 11, 2011. RA 423; RA 46, ¶5.[15]

Moreover, beyond § 602(a), Appellant's argument simply cannot be squared with common sense or his own admissions. For example, under the LLC Law, only "members" can adopt an operating agreement in the first place. *See* LLC Law § 402(c)(3) ("the vote of a majority in interest of the members entitled to vote thereon shall be required to … adopt … [the] operating agreement … .") (emphasis added); LLC Law § 417(a) ("the members of a limited liability company shall adopt a written operating agreement … .") (emphasis added). Yet, under Appellant's theory, this would be impossible to achieve because, according to

[15] *See* § 203(d) ("[t]he filing of the articles of organization shall … be conclusive evidence of the formation of the limited liability company as of the time of filing or effective date if later, except in an action or special proceeding brought by the attorney general.")

Appellant, there are no "members" *unless* there is an operating agreement. In any event, Appellant's argument is belied by his own pleadings, which admit that all parties have been "members" of the Company since its formation. RA 46, ¶ 5 ("ENS had and for all times since the formation to present, been managed by the same three members, Ettenson, Newman and Shapiro") (emphasis added).

B. Section 402(c)(3) Must Be Read and Applied As Drafted, And May Not Be Re-Written

Appellant also attempts to avoid the plain language of § 402(c)(3) by arguing that the introductory clause used in that section and throughout the statute, "Except as otherwise provided in the operating agreement," creates a requirement for such an agreement to exist before § 402 (and, *a fortiori,* every other provision of the statute using this phrase) can be applied. *See* App. Br. at 21. This argument is not only unsupported by *any* case law, it is actually contrary to the unanimous legion of case law holding that the default provisions of the LLC Law apply *in the absence* of a written operating agreement. It also contradicts the definition of "except," which includes "other than." *See Oxford English Dictionary*.

Appellant seemingly recognizes the weaknesses in his position when, for his last argument, he asks this Court to re-write §402(c)(3) and limit the word "adopt" to only the articles of organization. App. Br. at 21-22. The Court should decline Appellant's invitation, as it is only the legislature that can re-write a statute. *See*

Chemical Specialties Mfrs. Ass'n v. Jorling, 85 N.Y.2d. 382, 394 (1995); McKinney's Cons. Laws of NY, Book 1, Statutes § 94, at 190.

IV Respondents Were Authorized to Issue the Capital Call and to Reduce Appellant's Salary

Appellant also challenged Respondents' majority determination in connection with the October 2014 Meeting to approve the Capital Call and reduce Appellant's salary. Respondents' Counterclaims, in turn, sought a declaratory judgment holding (1) that Respondents were authorized to issue the Capital Call, and that the Capital Call was valid and binding on all members in all respects; and (2) that the payment of salaries to the members beyond December 31, 2013, was authorized, that Respondents were authorized to reduce Appellant's salary by majority vote, and that the reduction of Appellant's salary was valid and binding.

The IAS Court found that the Capital Call was authorized and consistent "with both the LLC Law and section 7.01 [of] the Operating Agreement." *See* RA 21. The IAS Court further found that both the LLC Law and the Operating Agreement authorized the Respondents to reduce Appellant's salary. *See* RA 21-22. Appellant argues for reversal based primarily on the purported terms of the same unenforceable oral agreement, and incorrect interpretations of §§ 411(a), 411(e), and 417(b) of the LLC Law. *See* App Br. at 24-25; 26-28.

A. The Capital Call Was Authorized

Section 7.01 of the Operating Agreement authorizes "a Majority of the Members" to "determine if additional Capital Contributions are necessary to conduct the Company's business activity." RA 207. If such a determination is made, notice must be given to all members of the Company, "specifying the due date, which shall not be less than thirty (30) days from the date of the notice, of any additional Capital Contributions which may be required." *Id.* Members are not required to make the additional Capital Contribution, but if they do not do so their interests in the Company may be adjusted if Capital Contributions are made by other members. *Id.*

As detailed above, these provisions were followed by Respondents to the letter. The Operating Agreement had been validly adopted – and in place with Appellant's knowledge – for ten months at the time of the October 2014 Meeting. Prior to the October 2014 Meeting, Newman circulated an e-mail to all members detailing the Company's financial status and indicating that the Company had a shortfall of approximately $31,000. RA 553. Respondents then voted at that meeting, in Appellant's presence, to request of each of the members an additional $10,000 Capital Contribution. RA 232. The day after the meeting, the Company issued the Capital Call, which was duly served on all members and specified a due date that was thirty-seven days from the date of the notice. RA 233.

Appellant argued before the IAS Court that the Capital Call was not authorized because (1) the Operating Agreement was not validly adopted (and therefore § 7.01 did not apply), and (2) it was prohibited by §§ 502(a) and (b) of the LLC Law. *See* RA 20-21. Respondents, in turn, argued that the Capital Call was validly issued pursuant to a binding Operating Agreement, and did not run afoul of §§ 502(a) or (b) of the LLC Law.

Indeed, § 502(a) simply sets forth the requirement that "a member is obligated to the limited liability company to perform any promise" to make a "required" capital contribution, regardless of "death, disability or any other reason." LLC Law § 502(a) (emphasis added). And § 502(b) merely provides, in relevant part, as follows:

> the obligation of a member to make a contribution or to return money or other property paid or distributed in violation of this chapter may be compromised only by consent of all the members. Notwithstanding the compromise, a creditor of a limited liability company who extends credit in reliance on the obligation of any member may enforce the original obligation to the extent he or she reasonably relied on such obligation after the member signed a writing which reflects the obligation and the creditor extended credit before the compromise…

LLC Law § 502(b). As commentators have recognized, these sections of the LLC Law largely exist to protect (a) lenders of a limited liability company who extend credit in reliance upon members' existing obligations to make contributions to the company, and (b) the other members of a limited liability company who frequently

may be held personally liable to creditors under loan agreements. *See* 1 N.Y. Prac., New York Ltd. Liab. Cos. and Partnerships, §16:4 (Liability of members – Liability for distributions and contributions). Under these circumstances, a member may be compelled under §502(a) to make a contribution of capital *that he has already promised to make*, and *that obligation* may not under §502(b) be compromised without the consent of the other members or a creditor that has relied on that obligation.

Here, even in the absence of the Operating Agreement, §§ 502(a) and (b) would not bar the Capital Call because, by its terms, the Capital Call was *voluntary*, and did not seek to *require* or impose any enforceable *obligation* on any member of ENS to make a contribution of capital. *See* RA 207, § 7.01 ("Each Member may, <u>but shall not be required</u> to, provide additional Capital Contributions to the Company in proportion to his Participation Interest.") (emphasis added). As Respondents do not contend that Appellant has made any promise or has any obligation to make any contribution of capital pursuant to the Capital Call, §§ 502(a) and (b) have no application.

The IAS Court therefore correctly found that § 502 was not "trigger[ed]" because the "capital call was not obligatory" and that, more broadly, the "capital call was consistent with both the LLC Law and section 7.01 [of] the Operating Agreement." RA 20-21. On appeal, Appellant does not seriously contest this

finding, merely stating in a conclusory manner that the IAS Court's finding that the Capital Call was voluntary was "not well founded." App. Br. at 25.

As an alternative ground, Appellant also argued in the IAS Court that § 417(b) of the LLC Law, which by its terms applies only to *amendments* of an operating agreement, prohibited Respondents from adopting an operating agreement that contained capital call provisions that "adversely affected" Appellant without his consent. That section provides, in pertinent part, as follows:

> The operating agreement of a limited liability company may be amended from time to time as provided therein; provided, however, that, except as otherwise provided in the operating agreement or the articles of organization, without the written consent of each member adversely affected thereby, (i) no amendment of the operating agreement … shall be made that (i) increases the obligations of any member to make contributions ...

LLC Law § 417(b) (*emphasis added*). As the IAS Court correctly held, § 417(b) is facially inapplicable because "that provision applies only to 'amended' operating agreements, and it is undisputed that ENS had no operating agreement prior to the Operating Agreement." RA 21.

On appeal, Appellant concedes that § 417(b) applies only to an amendment to an already existing operating agreement. App. Br. at 25. Nevertheless, Appellant again asks the court to re-write the statue, requesting that the language of § 417(b) be extended to the adoption of the Operating Agreement because of an "important legislative policy" that "no member may be required to make additional

capital contributions without his assent to an operating agreement providing for such additional capital calls." App. Br. at 26. Respondent provides no support for this argument, which is actually counter-intuitive since one would expect that an "important legislative policy" of this type would be codified in the statute. Regardless, the statute is clear and reflects a conscious decision by the legislature to limit § 417(b) to amendments to operating agreements.

As noted above, it is only the legislature that can re-write a statute. *Chemical Specialties Mfrs. Ass'n*, 85 N.Y.2d. at 394; McKinney's Cons. Laws of NY, Book 1, Statutes § 94, at 190 Moreover, Appellant's policy argument overlooks an actual policy codified in the LLC Law that has also been recognized in case law – that a member is free to negotiate the terms of his participation in an LLC at the time of his decision to enter into it, and that if he chooses not to do so then he is choosing to be subject to the statute's default, majority-rules provisions. This well-founded policy is based on the bedrock principle embraced by the drafters of the LLC Law not to permit a minority member to stonewall the will of the majority. *See, e.g., Overhoff*, 812 N.Y.S.2d at 816 (upholding majority-rules provision because "[t]o rule otherwise would permit a minority member to stonewall any action by the members merely by refusing to attend meetings, as happened here").

B. Respondents Were Authorized To Reduce Appellant's Salary

Like the Capital Call, the determination to reduce Appellant's salary was made by majority vote at the same meeting held in Appellant's presence on October 14, 2014. That determination was undertaken after Appellant failed (yet again) to live up to his obligations, including most recently one of the critical tasks he was directly responsible for: the preparation of the HyperVibe business plan. RA 419-420, ¶¶ 34-39. The reduction in Appellant's salary did not, however, impact his rights as a one-third owner of ENS to distributions of Company profits.

As stated, unless otherwise provided in the LLC Law, the articles of organization, or a written operating agreement, the default rule is that whenever any action is to be taken by members or managers it is authorized to be taken by a determination of a *majority* in interest of the members or managers. *See* LLC Law §§ 402(f), 408(a). Here, there is no provision in the LLC Law, the Company's Articles of Organization, or the Operating Agreement concerning salaries – meaning that Respondents' determination as a majority is valid and binding.

In his Verified Complaint, Appellant conceded that the members' salaries were authorized pursuant to a unanimous vote, but argued that the parties had agreed to these salaries only for ninety days (October 1, 2013 to December 31, 2013) and that they could only be "extended or modified by unanimous consent." RA 50, ¶¶ 26-27. In other words, he again claimed that the parties had orally agreed to modify

the default, majority-rules provisions of the LLC Law. Aside from the legal ineffectiveness of any such purported oral modification, his claim is belied by the undisputed fact that none of the members of the Company – including Appellant himself – agreed to the Proposed Consent circulated by the Company's attorney that would have required "the unanimous consent of the Members" for salary determinations. His claim is even further belied by his admission that salaries were paid by ENS to all members (including Appellant) in the months following the expiration of the suggested ninety day period set forth in the Proposed Consent. RA 415, ¶17; RA 427. Appellant also admits that he was aware of, and never once objected to, those payments of salaries. RA 77, ¶ 57; RA 91, ¶ 57.

Appellant also argued to the IAS Court that, in addition to being a violation of an unenforceable oral agreement, Respondents' determination to terminate Appellant's salary a year later while keeping their own in place was barred by § 9.01 of the Operating Agreement, which applies to "Management Fees" for "the Managers for their services in arranging transactions contemplated by the Company and managing the Company." RA 517, § 9.01. As Respondents pointed out, Appellant was attempting to play on both sides of the net with this argument, because he contends elsewhere in his brief that the Operating Agreement is invalid, while also attempting to rely on that same Operating Agreement to argue that the members' salaries were not permitted. Regardless, Appellant's argument is wrong

because the undisputed record is clear that the salaries paid to the parties were plainly not "Management Fees" under § 9.01. Indeed, it is undisputed that they were approved at the September 2013 Meeting, three months *before* the Company had any managers at all (it was still member-managed) or an Operating Agreement.

Appellant finally argued that § 411 of the LLC Law, the interested manager provision, prohibited Respondents from voting in favor of the salary termination. As an initial matter, Appellant did not present to the IAS Court (and does not present here) any authority holding that salary decisions even fall within the ambit of § 411.[16] More fundamentally, however, Respondents' actions plainly did not implicate the interested-manager rule.

Indeed, Appellant specifically concedes that the members' salaries were *unanimously* approved at the September 2013 Meeting. RA 50, ¶ 26. Thus, as to the approval of the members' salaries, there is certainly no issue with respect § 411. And Respondents' votes over a year later, at the October 2014 Meeting, to reduce Appellant's salary due to his continual and ongoing dereliction of his duties could not be an interested manager transaction under § 411 because it was not a

[16] Appellant's argument that § 411 of the LLC Law applies to salary decisions is actually contrary to the statutory scheme of the LLC Law. For example, § 414 of the LLC Law authorizes members to remove or replace "any or all managers of a limited liability company … with or without cause by a vote of a majority in interest of the members entitled to vote thereon." LLC Law § 414. If Respondents had simply voted at the October 2014 to remove Appellant as a manager of ENS for non-performance, he clearly would not have been entitled to continue to receive a salary for any management services. In other words, if Appellant's argument that § 411 were to be accepted, it would mean that Respondents could easily do under § 414 that which they could not do under § 411.

"contract or other transaction between a limited liability company and one or more of its managers" in which those managers "have a substantial financial interest." LLC Law § 411(a). Respondents did not vote to increase their own salary; they merely voted to reduce Appellant's salary. In other words, because Respondents derived no personal financial benefit from the decision, which concerned only the elimination of Appellant's salary, there is no § 411 issue at all.

Based on the foregoing, the IAS Court correctly found that (a) § 9.01 of the Operating Agreement was not implicated because Appellant "does not allege that [Respondents] are receiving 'Management Fees' in violation of the Operating Agreement"; and (b) § 411 of the LLC Law was not implicated because Appellant "does not allege that [Respondents] derived a personal benefit from the decision to eliminate his salary[.]" RA 21-22. The IAS Court also found that, as an alternative, Respondents' acts were authorized under the default provisions of the LLC Law. *See* RA 22 ("Under section 402, Ettenson and Newman held a combined majority interest, thereby permitting them to reduce Shapiro's salary and issue the capital call."). Appellant largely recycles his arguments on appeal, and they fail for the same reasons. *See* App. Br. at 26-28.

First, the purported oral agreement Appellant relies upon is still unenforceable under § 102(u) of the LLC Law. The argument is not strengthened by his reliance upon the Proposed Consent – an equally unenforceable agreement. To the contrary,

the very existence of that draft is an indication that the Company's attorney knew that it needed to be approved in writing to be enforceable. And in the absence of any such writing, the default majority-rules provisions, in both the Operating Agreement and the LLC Law, authorized Respondents to reduce Appellant's salary.

Second, Appellant simply misses the mark in arguing that the IAS Court misinterpreted § 9.01 of the Operating Agreement because it "construed the prohibition against 'compensation' as not including 'salary.'" App. Br. at 27-28. The IAS Court did no such thing. Instead, it correctly found that salaries – which all parties began to draw months *before* the Company adopted the Operating Agreement or had any managers – were just that, salaries, that were by definition not "Management Fees" for "services in arranging transactions contemplated by the Company and managing the Company."

Finally, relying on § 411 of the LLC Law, Appellant argues that Respondents "continued to receive a personal benefit of paying themselves salary" as result of the salary decision, and consequently the IAS Court "erroneously held that defendants did not derive a personal benefit from the salary action." *See* App. Br. at 28. Appellant, however, ignores that this "benefit" was already in place and is one that he concedes approving, and avoids the IAS Court's *actual* holding, which is that he fails to allege that Respondents "derived a personal benefit from the decision to eliminate his salary[.]" RA 21.

V THE IAS COURT PROPERLY DISMISSED APPELLANT'S OTHER CLAIMS

The IAS Court also properly entered summary judgment in Respondents' favor with respect to Appellant's claims for breaches of the "parties' [oral] agreement, the implied covenant of good faith and fair dealing, and fiduciary duties." RA 22.

Appellant can have no claim for breach of contract or breach of the implied covenant of good faith and fair dealing because the supposed agreement upon which these claims rest – *i.e.*, the purported oral agreement among the members – is unenforceable as a matter of law. *See* RA 22-23. *See also, Harris v. Seward Park Hous. Corp.*, 79 A.D.3d 425, 426 (1st Dept's 2010) (breach of contract claim requires the existence of an enforceable contract); *Jacobs Private Equity, LLC v. 450 Park LLC*, 22 A.D.3d 347, 347-348 (1st Dep't 2005) (dismissing breach of the implied covenant of good faith and fair claim as "duplicative of the insufficient breach of contract claim.").

Appellant also can have no claim for breach of fiduciary duty in the absence of any evidence of bad faith or self-dealing – particularly in light of the fact that all of Respondents' actions were expressly authorized under the LLC Law. *See* LLC Law § 409 (barring breach of fiduciary duty claims when a manager has acted "in good faith and with that degree of care that an ordinarily prudent person in a like position would use under similar circumstances."). While Appellant may disagree

with Respondents' decisions, they are not the proper basis for a claim. At best, they are "business disagreements" which under the business judgment rule "should not be questioned by the courts where, as here, there is no evidence of bad faith or self-dealing on the part of the individual defendants." *See Van Der Lande v. Stout*, 786 N.Y.S.2d 515, 516 (1st Dep't 2004); *see also Auerbach v Bennett*, 47 N.Y.2d 619, 630-631 (1979) ("[B]y definition the responsibility for business judgments must rest with the corporate directors; their individual capabilities and experience peculiarly qualify them for the discharge of that responsibility. Thus, absent evidence of bad faith or fraud (of which there is none here) the courts must and properly should respect their determinations.").

In briefing before the IAS Court, Appellant sought to oppose dismissal of these claims by arguing that Respondents' decision to cut off his salary, and to issue the Capital Call, could reasonably be considered to be bad faith or self-dealing on the part of the Respondents. However, as the IAS Court held, Appellant's pleading "contains only conclusory allegations of breach of fiduciary duties, without alleging bad faith, self-dealing, or any other conduct that would constitute a breach of fiduciary duty." RA 23. That is simply not enough to overcome Respondents' showing that they acted appropriately. *See id.*, *citing* LLC Law § 409 (a) and (c); *TPZ Corp. v. Reddington*, 239 A.D.2d 301, 301 (1st Dep't 1997) (finding "conclusory allegations of … breach of fiduciary duties"

insufficient); *Steinberg v. Carey*, 285 App. Div. 1131, 1131 (1st Dep't 1955) ("charges must be supported by factual assertions of specific wrongdoing rather than conclusory allegations of breaches of fiduciary duty," and "[m]atters depending on business judgment are not actionable.").

On appeal, Appellant still does not identify any actual breaches of fiduciary duties by Respondents. *See* App. Br. at 23 (arguing in summary fashion that it "was both a breach of fiduciary duty, and a breach of the parties' oral agreement here, for [Respondents] to impose upon [Appellant] an initial Operating Agreement which was materially different from the one they had last prepared and were negotiating, and to do so in response to [Appellant's] notice that he would obtain independent counsel."). Thus, his argument should be rejected for the same reasons identified by the IAS Court.[17] *See* RA 23. Indeed, the simple fact is that Respondents acted as authorized by the LLC Law. As one of the original members of the Company, Appellant could have negotiated for different terms at the time he made his

[17] *Pokoik v. Pokoik,* 115 A.D.3d. 428 (1st Dept. 2014), the only case to which Appellant cites, actually bars his breach of fiduciary duty claim. Under New York Law any breach of fiduciary duty claim lies only, if at all, against managing or controlling members. *Id*. at 428-429. *See also Cottone v. Selective Surfaces, Inc.*, 68 A.D.3d 1038, 1039 (2nd Dept. 2009); *Kalikow v. Shalik,* 43 Misc.3d 817, 823-24 (Sup. Ct. Nassau Cty. 2014). Here, as each of the parties is a one-third member and manager, there can be no claim of breach of fiduciary duty against either or both of them together. *See Marino v. Grupo Mundial Tenedora, S.A.*, 810 F.Supp.2d 601, 608-609 (S.D.N.Y. 2011) (rejecting argument that a breach of fiduciary duty claim would lie where "multiple members … combine to over 50% of the voting interests" because such a rule "would, in effect, impose fiduciary duties upon minority members … for purposes of a specific transaction because they voted with the majority in regards to that transaction.").

investment in the Company, but chose not to do so. Thus, he chose to bound by the default provisions of the law the parties chose to govern their Company.

CONCLUSION

For the foregoing reasons, the IAS Court's Decision granting summary judgment in favor of the Respondents pursuant to CPLR 3212 should be affirmed.

Dated: October 5, 2016
New York, NY

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