SURROGATE'S COURT : NEW YORK COUNTY

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New York County Surrogate's Court

November 8, 2017

In the Matter of the Application of Jenny Mui, as Administrator of the Estate of

File No. 2009-3859/A

PETER MUI,

Deceased,

for, Inter Alia, the Dissolution of Yellow River, Inc.

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A N D E R S O N, S .

This is a proceeding by the administrator of the estate of Peter Mui seeking, inter alia, the dissolution of Yellow River, Inc. ("Yellow River" or the "Company"), a clothing importer and wholesaler in New York City in which the estate holds a 49% interest. Two motions are pending. In the first, the administrator moves for summary judgment on its dissolution claim, as well as the summary dismissal of the counterclaims of respondents, Yellow River and Tungtex (U.S.A) Inc. In the second motion, Yellow River and Tungtex cross-move for summary dismissal of the dissolution claim.

Peter Mui died intestate on August 18, 2009, survived by his wife (petitioner) and five children. From 1988 until his death in 2009, decedent owned 49% of Yellow River and was the Company's Chief Executive Officer. Tungtex owned the other 51% of Yellow River. According to the president of Tungtex, Lam Yiu On Alan ("Lam"), decedent was the "creative force" behind Yellow River and "irreplaceable in terms of his value to the Company."

As the CEO of Yellow River, decedent received a substantial salary, reimbursement for documented expenses and, for at least four years prior to his death, dividend payments. The parties dispute whether Yellow River ceased paying such dividends before decedent's death, but there is no dispute that no dividends were paid after his death. There is also no dispute that, for years prior to decedent's death, Yellow River paid Tungtex "management fees" and those payments continued after Yellow River ceased paying dividends.

Decedent also devoted some of his time to two other companies he had formed during his tenure as Yellow River's CEO, namely Fine Print, a graphic design company, and Yellow Man, a specialty clothing wholesaler and retailer. By all accounts, neither of these two companies competed directly with Yellow River.

After decedent's death, Yellow River and/or Tungtex loaned funds to petitioner to cover some of her family's expenses. Lam also discussed with petitioner the possibility of a buy-out of decedent's interest in Yellow River. Eventually, however, petitioner's relationship with the principals of Tungtex/Yellow River soured. Believing that Tungtex had caused Yellow River to cease paying "dividends to the Estate or to provide other substantial funds while, at the same time, deriving economic benefits from its control of the Company," petitioner brought the instant proceeding seeking the dissolution of Yellow River under New York's Business Corporation Law ("BCL") Section 1104-a.[1] Yellow River and Tungtex asserted various counterclaims based upon alleged misconduct by decedent as Yellow River's CEO. The instant motions followed.

Discussion

The standards for summary judgment are clear. Summary judgment is available only where no material issues of fact exist (*see e.g. Alvarez v Prospect Hosp.*, 68 NY2d 320 [1986]). The party seeking summary judgment "must make a prima facie showing of entitlement to judgment as a matter of law, tendering sufficient evidence to demonstrate the absence of any material issues of fact" (*id.* at 324 [citations omitted]). If such a showing is made, the party opposing summary judgment must then come forward with proof establishing a genuine issue of material fact or must provide an acceptable excuse for the failure to do so (*see e.g. Zuckerman v City of New York,* 49 NY2d 557 [1980]).

The party attempting to resist summary judgment is entitled to every favorable inference that can reasonably be drawn from the evidence (*see e.g. Branham v Loews Orpheum Cinemas, Inc.*, 8 NY3d 931 [2007]). The opposing party may use evidence that includes hearsay as long as it is not the only proof offered *(see*

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[1] Petitioner also seeks other relief, including the appointment of a receiver, but neither petitioner nor respondents address such relief in their motions.

e.g Bishop v Maurer, 106 AD3d 622 [1st Dept 2013]). In addition, evidence that might be barred at trial under CPLR § 4519 (Dead Man's Statute) can be used to oppose summary judgment (*Phillips v Joseph Kantor & Co.*, 31 NY2d 307 [1972]). However, "mere conclusions, expressions of hope or unsubstantiated allegations or assertions are insufficient" to raise an issue of fact (*Zuckerman v City of New York*, 49 NY2d at 562, *supra* [citations omitted]).

Cross-Motions for Summary Judgment: Dissolution Claim

Petitioner contends that dissolution is warranted because, as a matter of law, Tungtex engaged in "oppressive actions" toward the estate within the meaning of BCL § 1104-a. This statutory provision was enacted to enable minority shareholders who own 20% or more of a close corporation to petition for its judicial dissolution under certain circumstances such as where the majority shareholders are engaged in "illegal, fraudulent or oppressive actions toward the complaining shareholders" (BCL § 1104-a[a][1]). Courts have defined "oppressive actions" as conduct that "substantially defeats the 'reasonable expectations' held by minority shareholders in committing their capital to the particular enterprise" (*Matter of Kemp & Beatley, Inc.*, 64 NY2d 63, 72 [1984][citations omitted]). Whether to order dissolution of a closely held corporation "is a matter of discretion and should not be undertaken lightly" (*see e.g. Matter of Harris*, 118

AD2d 646, 647 [2d Dept 1986] [citations omitted]). In exercising such discretion, courts are required to take into account whether liquidation is 1) "the only feasible means" by which petitioners can "obtain a fair return on their investment," and 2) "reasonably necessary" to protect the interests of the shareholders (BCL § 1104-a[b]).

To support her prima facie case for summary judgment, petitioner offers evidence that Tungtex systematically denied the estate the benefit of its minority ownership in Yellow River. According to petitioner, after decedent's death, Tungtex caused Yellow River to stop paying dividends to the estate and instead diverted its "accrued savings and earnings to Tungtex in the form of 'management fees' and other charges." Petitioner further claims that while she was still grieving the loss of her husband and in need of funds to support decedent's family, Tungtex pressured her, albeit unsuccessfully, to sell the estate's 49% interest in Yellow River to Tungtex for $1,000,000, an amount far below what she believed to be the Company's fair market value.

Although these facts, if undisputed, could be a basis for the court to exercise its discretion and direct the dissolution of Yellow River under BCL § 1104-a, Yellow River and Tungtex have offered sufficient evidence to create multiple fact issues. For example, according to Lam's affidavit, Tungtex did not cause Yellow River to stop paying dividends to the estate after decedent's death. Rather, he claims that Yellow River stopped paying dividends to all of its shareholders, *i.e.*, decedent **and** Tungtex, almost a year prior to decedent's death for economic reasons after the company's revenues and profits had substantially decreased. Lam further avers that, contrary to petitioner's contention, Yellow River did not divert funds to Tungtex after decedent's death through the payment of management and other fees. Yellow River had paid management fees to Tungtex with decedent's approval for many years prior to his death. The payments continued after decedent's death in amounts that, according to Lam, were necessary and appropriate under the circumstances.

In response to petitioner's contention that Lam and others attempted to coerce her into selling Yellow River to Tungtex at less than its fair market value, respondents offer a sharply different version of the substance and tone of the conversations at issue. According to Lam, he discussed the possibility of a sale not to pressure petitioner but "to help and work with [her] during a difficult time ...." He claims that the loans to petitioner are evidence of Tungtex's good will and intention to help her financially, thus undermining petitioner's claim that she was pressured to sell decedent's interest in Yellow River.

In view of the record, petitioner is not entitled to a summary determination that Tungtex engaged in "oppressive actions" within the meaning of BCL § 1104-a. Petitioner's efforts to salvage her motion by recasting arguments belied by respondents' papers are plainly insufficient. For example, faced with evidence that, for economic reasons, Yellow River had ceased paying dividends to its shareholders prior to decedent's death, petitioner argues that the dividends that she claims were "abruptly" stopped were not regular dividends at all. Rather, they were informal or *de facto* ones paid in the form of reimbursement for "personal and family expenses from time to time." At best, however, this new argument creates a fact issue about whether those payments were informal dividends that should have continued after decedent's death as she contends, or reimbursement for purported business expenses related to decedent's services as CEO of Yellow River, as Tungtex and Yellow River contend.

For these reasons, petitioner's motion for summary judgment on her dissolution claim is denied for failure to establish as a matter of law that Tungtex engaged in "oppressive actions" within the meaning of BCL § 1104-a.

As for respondents' cross-motion for summary judgment, they have failed to establish, as a matter of law, that the dissolution claim should be dismissed. Although respondents have met their initial burden on summary judgment, the record is replete with factual disputes about their conduct after decedent's death. Respondents contend, for example, that there was no pressure put on petitioner to sell the estate's interest in Yellow River, but petitioner's sworn statements are to the contrary and this court, on a motion for summary judgment, cannot assess the credibility of the witnesses (*see e.g. S. J. Capelin Associates, Inc. v Globe Mfg. Corp.*, 34 NY2d 338 [1974]).

Petitioner also offers evidence sufficient to create a fact issue concerning whether Tungtex, as majority shareholder, influenced Yellow River to act for the benefit of Tungtex to the detriment of the estate by causing it to pay Tungtex unwarranted management fees. Indeed, Tungtex admits that, despite the economic downturn, which it contends began in 2008-2009, Yellow River first cut the "management fees" it paid Tungtex in fiscal year 2012 in order "to assist with reducing the Company's expenses during difficult financial times." These issues and others cannot be determined summarily on the conflicting evidence in the record.

None of the cases cited by petitioner or respondents in their cross-motions compels a different result. Given the nature of dissolution proceedings, the cases cited which apply BCL § 1104-a are very fact-specific and easily distinguishable. Moreover, these cases make clear that courts frequently require a hearing before dissolving a corporation under BCL § 1104-a (*see e.g. In re Kemp & Beatley, Inc.*, 64 NY2d 63 [1984]; *In re*

Charleston Square, 295 AD2d 425 [2d Dept 2002]; *In re Mintz*, 113 AD2d 803 [2d Dept 1985]). And when a court does not require a hearing as in *Matter of Schlacter* (154 AD2d 685 [2d Dept 1989]), the undisputed facts unequivocally demonstrate that the majority shareholder did or did not engage in conduct that defeated the minority shareholder's reasonable expectations of ownership. Here, there are myriad fact issues surrounding whether, after decedent's death, the estate received the full benefit of its ownership interest in Yellow River as a result of the conduct of Tungtex.

For these reasons, the cross-motion of Yellow River and Tungtex for summary judgment on the dissolution claim is denied.

Summary Judgment on Yellow River's Counterclaims

Breach of Duty of Loyalty/Faithless Servant

Yellow River's first counterclaim alleges that decedent, as an employee of Yellow River, had a duty of loyalty to the Company which he violated by, among other things, diverting Yellow River's resources and funds to his other businesses and to himself individually to support his "lavish lifestyle." The law is clear that corporate officers, in the performance of their duties, stand in a fiduciary relationship to their corporation (*see e.g. Matter of Vogel [Lewis]*, 25 AD2d 212 [1st Dept 1966], *affd* 19 NY2d 589 [1967]), and thus owe the corporation their undivided loyalty (*see Limmer v Medallion Group*, 75 AD2d 299 [1st

Dept 1980]; *Foley v D'Agostino*, 21 AD2d 60 [1st Dept 1964]).

In seeking summary dismissal of this counterclaim, petitioner does not argue that, as a matter of law, decedent's alleged conduct did not amount to a breach of his duty of loyalty to Yellow River. Instead, she argues that Yellow River's counterclaim is without merit because all of the conduct at issue was "expressly approved" by Yellow River and therefore cannot be considered a breach of any duty of loyalty decedent may have had to the Company (*see e.g. Board of Managers of Soho Green Condominium v Clear Bright and Famous LLC*, 106 AD3d 462 [1st Dept 2013]). Petitioner has submitted admissible evidence that Yellow River was aware that decedent was involved with Yellow Man and Fine Print while CEO of Yellow River and that this fact had not been raised as an issue during decedent's lifetime. She has also submitted evidence that Yellow River reimbursed decedent in full for his claimed expenditures after decedent's submission of documentary support.

According to Yellow River and Tungtex, however, the extent of decedent's involvement with Fine Print and Yellow Man did not become apparent until petitioner commenced this proceeding and respondents obtained discovery revealing that 1) decedent had spent a significant amount of his time working for the benefit of those companies instead of Yellow River, and 2) decedent's representations that all his expenses were related to Yellow

River's business were inaccurate. Thus, whether Yellow River "expressly approved" the conduct at issue is disputed.

For these reasons, petitioner's motion as it relates to Yellow River's first counterclaim for breach of duty of loyalty is denied.

Breach of Contract

Yellow River has asserted two breach of contract counterclaims, one involving decedent's purported employment contract and the other involving the 1988 Shareholder's Agreement between decedent and Yellow River and Tungtex. With regard to the employment contract (the second counterclaim), Yellow River alleges that decedent breached the agreement by engaging in conduct that benefited him and his family at the expense of Yellow River. The elements of a breach of contract claim are (1) the existence of a contract, (2) plaintiff's performance thereunder, (3) defendant's breach, and (4) resulting damages (*see e.g. Harris v. Seward Park Hous. Corp.*, 79 AD3d 425 [1st Dept 2010]).

Petitioner first argues that this counterclaim must be dismissed as a matter of law because it is undisputed that decedent and Yellow River had no written employment contract. However, a written employment contract is not required for a breach of contract claim because an employment contract can be oral (*see e.g. Gold v Benefit Plan Adm'rs,* 233 AD2d 421 [2d Dept

1996][oral employment contract upheld]) or implied in fact (*see e.g. Western Electric Co. v Brenner*, 41 NY2d 291, 295 [1977] [noting that "the employer-employee relationship is one of contract, express or implied"). Petitioner concedes as much in her reply papers, but then argues, based upon *Julian J. Studley, Inc. v New York News, Inc.* (70 NY2d 628, 629 [1987]), that the parties' Shareholder Agreement precludes an implied contract because it is "an express contract covering the subject matter involved."

This argument also fails. First, it ignores the possibility of an oral contract. Second, to the extent that the Shareholder Agreement covers any of decedent's employment obligations, its scope was specifically limited to decedent's 1) "Apply[ing] his designs during his tenure of employment exclusively to articles of clothing sold by Yellow River under labels, trade names and related trademarks owned by Yellow River," and 2) "rendering his best efforts in promoting such labels, trade names and trade marks." Consequently, the Shareholder's Agreement cannot be reasonably interpreted to cover all of the conduct that forms the basis for Yellow River's second counterclaim. Because petitioner has failed to establish, as a matter of law, that decedent and Yellow River did not have an enforceable employment contract, her motion for summary judgment with respect to this counterclaim is denied.

With regard to Yellow River's sixth counterclaim that decedent breached the Shareholder's Agreement, summary judgment is also unwarranted. Yellow River alleges that decedent's efforts on behalf of Yellow Man breached the above-quoted provisions of the Shareholder's Agreement. Petitioner, relying on the undisputed fact that Yellow Man did not compete directly with Yellow River, asserts that, as a matter of law, there was no breach. However, that Yellow Man did not compete directly with Yellow River has no bearing on whether decedent breached the Shareholder's Agreement. What bears on this issue is, instead, whether decedent "appl[ied] his designs" under labels and trademarks owned by Yellow River to clothing sold by any company other than Yellow River and "rendered his best efforts in promoting [Yellow River's] labels, trade names and trade marks." As to this issue, respondents, based upon the deposition testimony of various employees of Yellow River and Tungtex, have offered sufficient evidence to preclude summary judgment. For these reasons, the motion is denied with respect to Yellow River's sixth counterclaim as well.

Conversion

In its third counterclaim, Yellow River alleges that decedent converted "monies belonging to Yellow River [for] his own use to [its] detriment." To prevail on a claim for conversion, Yellow River must establish that decedent, without authorization, exercised ownership over property belonging to it (*see e.g. State of New York v Seventh Regiment Fund*, 98 NY2d 249 [2002]). Petitioner offers evidence that decedent substantiated all of his expenses to Yellow River before he was reimbursed. According to petitioner, Yellow River "expressly authorized" all of the expenses at issue, thereby negating any claim for conversion. Again, however, there is a fact issue as to whether decedent misled Yellow River about the nature of his expenses and sought reimbursement for items unrelated to his services as CEO. Since the use of corporate funds to pay for non-business-related expenses supports a claim for conversion (*see e.g. Lemle v Lemle*, 92 AD3d 494 [1st Dept 2012]), the motion is denied with respect to Yellow River's third counterclaim.

Unjust Enrichment

In order to prevail on their fourth counterclaim for unjust enrichment, Yellow River must show that decedent was enriched at its expense and that it would be "against equity and good conscience to permit [petitioner] to retain what is sought to be recovered" (*Mandarin Trading Ltd. v Wildenstein*, 16 NY3d 173 [2011] [internal quotation marks and citation omitted]). Petitioner argues that summary judgment is warranted because the Shareholder's Agreement is an enforceable contract that "governs the subject matter of Yellow River's claim" and thus precludes the equitable remedy of unjust enrichment. Alternatively, petitioner argues that decedent did not receive any payments to Yellow River's detriment.

The existence of the Shareholders' Agreement does not foreclose Yellow River's unjust enrichment claim as a matter of law. While "the existence of a valid and enforceable written contract governing a particular subject matter ordinarily precludes recovery in quasi-contract for events arising out of the same subject matter" (*see e.g. Clark-Fitzpatrick, Inc. v Long Is. RR. Co.*, 70 NY2d 382, 388 [1987][citations omitted]), if there is a bona fide dispute as to the existence of a contract or the contract does not cover the dispute in issue, a petitioner is not required to elect his or her remedies (*see e.g. Joseph Sternberg, Inc. v Walber 36th St. Assocs.*, 187 AD2d 225 [1st Dept 1993]). Here, the Shareholder's Agreement, to the extent it covers any of decedent's employment obligations, does not govern the subject matter of Yellow River's claim. For example, the conduct Yellow River alleges as a basis for its unjust enrichment claim includes obtaining reimbursement for non-business-related expenses. However, the Shareholder's Agreement does not cover the issue of expenses. Consequently, that contract cannot be a basis to dismiss Yellow River's unjust enrichment claim and petitioner's motion to summarily dismiss Yellow River's fourth counterclaim for unjust enrichment is therefore denied.

dealings with it" (citation omitted)]). Here, petitioner has offered evidence that decedent received the funds at issue in his individual capacity and not as a fiduciary, *i.e.*, he was not holding the funds to pay or manage them on Yellow River's behalf. Thus, an accounting by petitioner would not serve its intended purpose, namely, to give a statement as to the monies decedent received and disbursed on behalf of Yellow River. Moreover, Yellow River does not refute petitioner's contention that the Company has an adequate remedy at law because it seeks damages for breach of contract and breach of fiduciary duty/loyalty arising out of the same conduct.

Under these circumstances, the motion for summary judgment is granted with respect to Yellow River's fifth counterclaim seeking an accounting.

Summary Judgment on Tungtex's Counterclaims

Breach of Duty of Good Faith

Tungtex's first counterclaim alleges that decedent, as a shareholder of Yellow River, had a duty to act in good faith. Petitioner argues that Tungtex lacks standing to assert this claim because it seeks to vindicate alleged wrongs to Yellow River and therefore must be brought derivatively. Generally, a shareholder has no individual cause of action for a wrong committed against a corporation (*see e.g. Wolf v Rand*, 258 AD2d 401 [1st Dept 1999]). Petitioner argues that the allegations here, namely, decedent's diversion of corporate assets for his own benefit, cannot be prosecuted by Tungtex as a matter of law.

Tungtex's argument in opposition is relegated to a single footnote in which it cites *Casata v Brewster-Allen-Wichert, Inc.* (248 AD2d 710 [2d Dept 1998]) for the proposition that "shareholders of a close corporation have a duty to each other to act in good faith" (*id.* at 711 [citations omitted]). However, that case did not involve a majority shareholder bringing an independent action for breach of a duty of good faith against a minority shareholder, as is the case here. Rather, it involved a dissolution proceeding under BCL § 1104-a. The issue of a shareholder's good faith (or lack thereof) arose only as a defense by the majority shareholder who claimed that certain actions of the minority shareholder had been undertaken in bad faith to force an involuntary dissolution. The court held only that the minority shareholder's conduct raised fact issues that precluded summary judgment on its dissolution claim.

Tungtex concedes that its counterclaim is based on decedent's "covert and improper use of funds of Yellow River." It does not argue, let alone demonstrate, a basis for an independent claim by it as majority shareholder of Yellow River *(see e.g. Herbert H. Post & Co. v Sidney Bitterman, Inc.*, 219 AD2d 214 [1st Dept 1996]). Under these circumstances, petitioner is entitled to summary judgment on Tungtex's first counterclaim.

Accounting

Finally, petitioner is entitled to summary judgment on Tungtex's second counterclaim for an accounting "for all monies [decedent] diverted from Yellow River." Tungtex's counterclaim is based upon essentially the same allegations as Yellow River's claim for an accounting. To the extent that Tungtex, as a majority shareholder, would even have standing to seek an accounting from decedent for funds diverted from Yellow River, the claim suffers from the legal deficiencies discussed above.

In sum, the parties' cross-motions for summary judgment on petitioner's dissolution claim under BCL § 1104-a are denied. Petitioner's motion for summary judgment is granted with respect to Yellow River's fifth counterclaim and Tungtex's first and second counterclaims, and denied with respect to Yellow River's first, second, third, fourth and sixth counterclaims.

This decision constitutes the order of the court.

Dated: November 8, 2017

S U R R O G A T E