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

CULLIGAN SOFT WATER COMPANY, et al.,

Plaintiffs,

vs.

CLAYTON, DUBILIER & RICE, LLC, et al.,

Defendants.

Index No.: 651863/12

IAS Part 48

Justice Andrea K. Masley

Motion Sequence No. 19

PLAINTIFFS' MEMORANDUM OF LAW IN OPPOSITION TO NOMINAL DEFENDANT CULLIGAN LTD.'S MOTION TO SUBSTITUTE PURSUANT TO CPLR 1017 AND 1021, AND MOTION TO DISMISS UNDER CPLR 3211(a)

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Plaintiffs Culligan Soft Water Company, *et al.* ("Plaintiffs"), respectfully submit this Memorandum of Law in opposition to the motion of nominal Defendant Culligan Ltd. in Members' Voluntary Liquidation ("Culligan Ltd." or "Defendant") for an order to substitute Michael W. Morrison and Charles Thresh, liquidators of nominal defendant Culligan Ltd. in Members' Voluntary Liquidation (the "Bermuda Liquidators"), as plaintiffs in place of the shareholder Plaintiffs pursuant to CPLR 1017 and 1021, and to dismiss for Plaintiffs' failure to make demand on the liquidators pursuant to CPLR 3211.

PRELIMINARY STATEMENT

Culligan Ltd.'s motion is baseless on multiple levels. It purports to seek relief under CPLR 1017 and 1021, requesting substitution to replace Plaintiffs in this action for the purpose of ending the lawsuit. CPLR 1017 is contingent upon a receiver being appointed under New York law. Defendant is not a receiver under New York law, and has made no attempt to be appointed as a receiver, despite being active in the lawsuit for five years.

CPLR 1021 is a permissive statute, and Defendant has failed after over five years to seek such relief. ("A motion for substitution may be made by the successors or representatives of a party or by any party.") Defendant, despite not qualifying as a receiver, seeks such appointment to dismiss the suit pursuant to CPLR 3211.[1] Defendant failed to raise these arguments in prior

[1] Defendant's Notice of Motion does not specify which section of the CPLR under which it seeks relief, and as such the notice is defective. "A notice of motion to dismiss pursuant to 'CPLR's 3211(a) . . . . (5)' is not a compliance with the requirement of CPLR's 2214(a) that the notice of motion shall state 'the grounds therefor.'" *Rubin v. Rubin*, 72 A.D.2d 536, 537 (1st Dept. 1979). Further, Defendant's Memorandum of Law ("Defendant's MOL," NYSCEF Doc. No. 376) does not even cite CPLR 3211, but seemingly makes a claim that Plaintiffs failed to make a demand under BCL 626(c) -- but again those grounds were not included in the Notice of Motion, nor even mentioned in Defendant's MOL. Defendant's notice therefore fails to specify the grounds for the motion as required under CPLR 2214.

motions to dismiss, and as such are waived.

More telling is that Defendant completely ignores BCL 1006. It does cite myriad Federal cases, applying Delaware and Federal Bankruptcy statutes, but neglects to address directly applicable New York statutes and case law. New York law is clear: Shareholders are specifically allowed to pursue their rights, despite dissolution, and the corporation may sue or be sued in its name for any right or claim existing or any liability incurred before such dissolution.[2] Plaintiffs have specifically brought claims under New York BCL 510, 719-720. What may or may not be the standard in Bermuda or Delaware is not relevant here, where the underlying claims are specifically authorized under New York statutes and made applicable to foreign corporations doing business here.

Beyond that, even if BCL 1006 was somehow not applicable, Defendant's motion fails as a matter of law as:

1. The Bermuda Liquidators are not receivers under New York Law, and have not made any attempt to comply with the requirements imposed upon a receiver under BCL 1202, 1204, or 1311.

2. The opening lines of Defendant's MOL recite a simple fact that is fatal to its own motion: This action was commenced on May 31, 2012; the Company did not enter liquidation proceedings according to Defendant until April 29, 2013. (Defendant's MOL: 1, 2) Despite participating in this case for five years, Defendant never sought substitution. The burden is not on Plaintiffs to substitute them as a party. *See* CPLR 1021.

3. Neither Defendant nor the Bermuda Liquidators ever raised this issue in prior motions to dismiss and they are thereby waived. *See Sanchez v. L.L.H. Recycled Aggregates*, 147 Misc.2d

[2] BCL 1006; Subject to limitations not relevant here.

41 (Queens Cty. Sup. Ct. 1990); *Addesso v. Shemtob*, 70 N.Y.2d 689 (1987); CPLR 3211(e).

4. There is absolutely no requirement that a further demand, or allegations of futility, need be pleaded with regard to foreign liquidators appointed after the commencement of the action. The time to make demand or determine if a demand would be futile is ***before an action is commenced.*** BCL 626(c); *Bansbach v. Zinn* 1 N.Y.3d 1, 8 (2003). The only case on point specifically found as "meritless" an argument that demand would have to be made on a receiver that had not been appointed as of the time the action was filed. *Gunzburg v. Gunzburg*, 152 A.D.2d 537, 538 (2d Dept. 1989).

ARGUMENT

A. Plaintiffs Are Specifically Authorized To Maintain This Action In Any Dissolution.

New York law applies to this case, period. Plaintiffs bring claims under BCL 510, 719, and 720, which are applicable to foreign corporations pursuant to BCL 1317 and 1319. *See Culligan Soft Water Co. v. Clayton Dubilier & Rice LLC,* 118 A.D.3d 422 (1st Dept. 2014). To maintain a derivative action, Plaintiffs needed to make the allegations required by BCL 626(c), which this Court has already determined Plaintiffs have done. (Decision and Order dated January 2, 2019 ("Order"); NYSCEF Doc. No. 327) The applicable time for determining whether demands were made or excused was prior to the commencement of the action, and such allegations needed to be pled in the complaint per BCL 626(c). Defendant itself recites that the action commenced May 31, 2012, and the Bermuda Liquidators were not appointed until eleven months later. (Defendant's MOL: 2.) No further demand or futility need be pled per the express wording of the statute. *See* BCL 626(c); *Bansbach,* 1 N.Y.3d at 8. This effectively ends the analysis.

Notwithstanding, Defendant tries to blur the issues with a discussion based on what a foreign liquidator, which is "akin" to a receiver under New York law (Defendant's MOL: 1), may

or may not do under Bermuda law. This argument has no support under New York law.

1. BCL 1006 Specifically Authorizes This Action, Notwithstanding Dissolution.

Even if the Bermuda Liquidators' appointment after this action commenced was relevant, it would not affect Plaintiffs' ability to maintain this action. Again, the threshold question regarding derivative standing is whether or not Plaintiffs met the requirements of BCL 626(c), which they have. Derivative standing aside, BCL 1006, cited in relevant part, unequivocally decides this issue in Plaintiffs' favor:

> (a) A dissolved corporation, its directors, officers and shareholders may continue to function for the purpose of winding up the affairs of the corporation in the same manner as if the dissolution had not taken place, except as otherwise provided in this chapter or by court order. In particular, and without limiting the generality of the foregoing:
>
> . . . .
>
> 4) The corporation may sue or be sued in all courts and participate in actions and proceedings, whether judicial, administrative, arbitrative or otherwise, in its corporate name, and process may be served by or upon it.
>
> (b) The dissolution of a corporation shall not affect any remedy available to or against such corporation, its directors, officers or shareholders for any right or claim existing or any liability incurred before such dissolution, except as provided in sections 1007 (Notice to creditors; filing or barring claims) or 1008 (Jurisdiction of supreme court to supervise dissolution and liquidation).

BCL 1006.

Summed up: once a derivative action, always a derivative action. Even the appointment of a legitimate receiver under New York law does not deprive shareholders of their ability to maintain a derivative action if the requirements of BCL 626(c) are met (and which is specifically applicable to foreign corporations per BCL 1319(a)(2)). Even if Culligan Ltd. had entered dissolution or liquidation prior to the commencement of this action, BCL 1006 would still permit a derivative action by shareholders in the name of the corporation itself. *See Ind. Inv. Protective League v.*

Time, Inc., 50 N.Y.2d 259, 264 (1980) (Dissolution of corporation does not affect shareholder standing to maintain derivative action.) This action was commenced almost a year before the purported liquidation, which has not even been authenticated, nor have Culligan Ltd. or the Bermuda Liquidators pursued any of the required actions to constitute a dissolution required in New York. Liquidation simply has no effect upon Plaintiffs' right to maintain this action.

B. Neither KPMG Bermuda, Nor the Bermuda Liquidators, Are Receivers.

Defendant's request for substitution depends on its status as a "receiver" under New York law, which it is not. It has not been appointed by the Court, has not met substantive requirements of New York law governing receivers, and has not even attempted to do so. CPLR 1017 states: "[i]f a receiver is appointed for a party, or a corporate party is dissolved, the court shall order substitution of the proper parties." The Bermuda Liquidators ***were not*** appointed as a receivers. Defendant tries to gloss over this very important point by stating that the appointment of Messrs. Morrison and Thresh was "akin" under New York and Bermuda law to the appointment of a receiver." (Defendant's MOL: 1) "Akin" does not a receiver make. New York has specific requirements for the appoint of a receiver.

1. The Bermuda Liquidators Were Not Appointed By The Court Pursuant to BCL 1202.

BCL 1202 provides, in relevant part:

> (a) A receiver of the property of a ***corporation can be appointed only by the court, and in one of the following cases:***
> . . .
> (4) An action to preserve the assets in this state, of any kind, tangible or intangible, of a foreign corporation which has been dissolved, nationalized or its authority or existence otherwise terminated or cancelled in the jurisdiction of its incorporation or which has ceased to do business, brought by any creditor or shareholder of such corporation or by one on whose behalf an order of attachment against the property of such corporation has been issued.

> (b) A receiver shall be subject to the control of the court at all times and may be removed by the court at any time.

BCL 1202 *(emphasis added*).

2. The Bermuda Liquidators Did Not Comply With BCL 1204.

BCL 1204 provides for very specific criteria and duties for a New York receiver:

> (a) A receiver, before entering upon his duties, shall:
>
> > (1) Take and subscribe an oath that he will faithfully, honestly and impartially discharge the trust committed to him, and the oath shall be filed with the clerk of the court in which the action or special proceeding is pending.
> >
> > (2) File with the clerk of such court a bond to the people, with at least two sufficient sureties or a bond executed by any fidelity or surety company authorized by the laws of this state to transact business, in a penalty fixed by the court appointing him, conditioned for the faithful discharge of his duties as receiver. The court may at any time direct a receiver to give a new bond with new sureties and with like condition.

BCL 1204.

3. The Bermuda Liquidators Did Not Comply With BCL 1311.

Regarding foreign corporations, BCL 1311 imposes yet additional requirements on dissolving foreign corporations, including filing of notices with the Secretary of State. *Id.*

4. Defendant's Cited Authorities Have Nothing To Do With This Case, And Actually Contradict Defendant's Position.

O'Keefe v. Coreless, 231 A.D. 58 (1st Dept. 1930) has nothing to do with this case. First, it is a half page First Department decision from 1930, which has no subsequent citations or supporting authority, and was seemingly superseded by current statutes. Second, the receiver in that case had been previously approved and appointed as a receiver for a U.S. corporation by a New York Court. Third, the case involved whether or not a temporary receiver could be substituted out in favor of a permanent receiver. Finally, it was the defendant/appellant in that case that

opposed the substitution of receivers, which were apparently approved by the derivative plaintiffs. That is the exact opposite of the case at bar.

More intriguing is Defendant's citation to *SNR Holdings, Inc. v. Ataka Am., Inc.*, 54 A.D.2d 406 (1st Dept. 1976). That was a bankruptcy case where the trial court had approved a substitution of a bankruptcy trustee as the derivative plaintiff in an action. Although the court recognized that due to comity, and the Bankruptcy Court having jurisdiction over the matter, there would be no distinction between a receiver and a Bankruptcy trustee. In that case though, the trustee had been appointed by the court, and promptly moved to be substituted. The First Department overturned the appointment, however, due to the fact that (as in this case) the trustee had been named as a defendant. As that court noted: "[The Trustee] could not reasonably be expected to sue or enter a judgment against itself." *SNR Holdings, Inc.*, 54 A.D.2d at 409.

In short, the Bermuda Liquidators complied with none of the statutory requirements to even be considered receivers. If they want to be treated as receivers under New York Law, then they needed to comply with New York law. In any event, they are not entitled to the relief here sought, and BCL 1006 would render their appointment moot *vis a vis* an attempt to deprive Plaintiffs derivative standing anyway.

C. Even If The Bermuda Liquidators Were Proper Receivers, They Step Into the Shoes of the Board.

As Defendant itself professes, even if the Bermuda Liquidators had been appointed and could legitimately serve as receivers under New York law, they would stand in the shoes of Culligan Ltd. *See* Affidavit of Peter A. Singler, filed concurrently ("Singler Aff."), ¶3; Exhibit 1 (Morrison Aff.¶ 4; NYSCEF Doc. No. 146). Actual demand was made upon Culligan Ltd.'s Board ("Complaint;" NYSCEF Doc. No. 332, ¶¶155-162; annexed as Exhibit 1 to Defendant's motion); demand was nonetheless futile as the Board was self-interested. (Complaint, NYSCEF Doc. No.

332, ¶¶136-154) This Court has already determined that Plaintiffs adequately pled self-interest and lack of independence. (Order, NYSCEF Doc. No. 327, at 7)

Simply stated, even if appointed as receivers, the Bermuda Liquidators would not be entitled to receive independent notice after the commencement of the action, or supplant Plaintiffs' ability to maintain this action once Plaintiffs have adequately pled demand and demand futility prior to the commencement. They step into the shoes of Culligan Ltd. and its former Board, and would be no more entitled to additional relief or rights than the original Board at the time the action commenced in 2012.

1. BCL 626(c) Establishes When A Demand Is To Be Made, Or Futility of Demand Is Determined.

The time to make a demand or determine if a demand would be futile is before an action is commenced. "In any such [derivative] action, the complaint shall set forth with particularity the efforts of the plaintiff to secure the initiation of such action by the Board or the reasons for not making such effort." BCL 626(c); *Bansbach*, 1 N.Y.3d at 8. If this were not the case, the "demand" requirement would be an ever moving target; every time a director changed, a company entered into any type of reorganization, a receiver is appointed or amendment made to the complaint, a new demand would have to be made, which would open the court to never-ending motions to dismiss. That is not what the statute says, and would lead to absurd results.

2. The Only Case On Point Specifically Refutes Defendant's Demand Argument As "Meritless."

Defendant can cite no case where repeated demands have ever been required. It would fly in the face of the statute and defeat the very purpose of making a demand in advance or pleading futility, while completely defeating legitimate derivative claims by self-interested directors. The only case on point holds the exact opposite: That a demand need not be made on a receiver

appointed after the commencement of an action. "The claim [lack of demand on the receiver] as it pertains to the receiver, while properly before this court, is meritless because the receiver had not yet been appointed at the time the complaint was filed." *Gunzburg,* 152 A.D.2d at 538.

All defendants in this case have done everything they can to cause delay and avoid the inevitable and undisputed conclusion that Culligan Ltd. violated BCL 510 (a) and (b), and the other defendants breached their fiduciary duties. This current motion is a last ditch effort to try to pose a last procedural challenge now that this Court has ruled that Plaintiffs' claims are adequately pled and the directors were self-interested in the transactions. (Order, NYSCEF Doc. No. 327, at 7) These findings establish that Plaintiffs have standing, and the Business Judgment Rule is inapplicable.

> Demand is excused because of futility when a complaint alleges with particularity that a majority of the board of directors is interested in the challenged transaction. Director interest may either be self-interest in the transaction at issue (*see*, *Barr v Wackman, supra,* at 376 [receipt of "personal benefits"]), or a loss of independence because a director with no direct interest in a transaction is "controlled" by a self-interested director.

Marx v. Akers, 88 N.Y.2d 189, 200 (1996). *See also Bansbach,* 1 N.Y.3d at 11.

3. Defendant's Argument That The Complaint Does Not Relate Back Is Meritless.

Defendant cites myriad Federal cases, applying inapplicable foreign law or Federal Bankruptcy statutes, but wholly neglects applicable New York Law. Two New York cases upon which Defendant does heavily rely are miscited and/or inapplicable. Defendant's reliance on *O'Keefe* is inapplicable, as discussed above. Relative to its relation back argument, Defendant relies on *Korinsky v. Winkelreid*, 143 A.D.3d 427 (1st Dept. 2016). That too is a case that has nothing to do with the case at bar, and Defendant cannot point to an authority that supports its position.

First, *Korinsky* applies Delaware law. There, the plaintiff did not have contemporaneous share ownership and could not have maintained a derivative action on those grounds alone. Second, the court found that the plaintiff could not plead demand futility, because he still would have been unable to satisfy the independent prong of contemporaneous ownership, thus the amended complaint could not state a cause of action. There was nothing factually or logically that could have revived the complaint—the plaintiff there could not re-make the past and satisfy the contemporaneous requirement for derivative standing under Delaware law.

In the current case, the original complaint did survive. The trial court erroneously dismissed based on application of Bermuda Law, which the First Department modified with regard to all but one claim against one of the defendants, finding that New York law applied to the standing analysis. *See Culligan Soft Water Co.,* 118 A.D.3d 422. In ruling on the defendants' motion to dismiss the Third Amended Complaint, the trial court found that Plaintiffs did make multiple demands, but erroneously ruled that Plaintiffs had failed to "plead around" the refusal of those demands. The First Department confirmed that the trial court had applied the incorrect standard and overturned the trial court's denial of Plaintiffs' motion for leave to amend, granting Plaintiffs the opportunity to plead according to the proper standard. *See Culligan Soft Water Co. v. Clayton Dubilier & Rice, LLC,* 139 A.D.3d 621, 622 (1st Dept. 2016)[3].

This Court has now thoroughly reviewed the amended complaint and found that it has

[3] The First Department noted that Plaintiffs had made demands, but held that they did not wait a reasonable amount of time before filing, citing *MacKay v. Pierce,* 86 A.D.2d 655 (2d Dept. 1982). In *MacKay,* the plaintiff made a demand, and with no sound reason, filed immediately, yet it was found to be reasonable in that case. In the present case, Plaintiffs made several demands over several months, and waited until the last possible day before Culligan was to enter bankruptcy. The demand issue was not actually a subject of the appeal, only whether or not Plaintiffs had to "plead around" a refused demand. These additional facts are pled in the Fourth Amended Complaint, and were not at issue when the First Department made its prior finding. (Singler Aff. 5)

adequately pled demand futility, thus satisfying the requirements of BCL 626(c). (Order, NYSCEF Doc. No. 327)

4. Defendant And The Bermuda Liquidators Have Been Completely Dilatory In Seeking Substitution And Have Waived The Ability To Seek Dismissal Now.

Defendant Culligan Ltd. has had counsel and actively participated in this case since its inception. It has never sought dismissal on the grounds, as ambiguous as they may be, stated in this present motion. While no authority supporting dismissal is cited in Defendant's MOL, its notice generically refers to CPLR 3211. Failure to assert a basis for seeking dismissal in a prior motion to dismiss waives that ability. *See Sanchez,* 147 Misc.2d 41 (Defense under 3211(a) cannot be asserted in amended answer if it was not asserted in original answer); *Addesso,* 70 N.Y.2d 689 (Plain language of statute mandates waiver of defense if not brought in earlier motion to dismiss); CPLR 3211(e) ("Any objection or defense based upon a ground set forth in paragraphs one, three, four, five and six of subdivision (a) is waived unless raised either by such motion or in the responsive pleading.")

The Bermuda Liquidators have also asserted themselves in this case for some time, but never sought to be substituted for Plaintiffs or even sought to appoint a proper receiver to enable them to do so.[4] Additionally, the Bermuda Liquidators attempt to stress that they are separate from KPMG Advisory Ltd., and that they serve in their individual capacity. (Defendant's MOL: 1, 5, 6) However, the authority they cite for that proposition is anything but unequivocal. Paragraph 2 of Mr. Morrison's Affirmation (NYSCEF Doc. No. 146) states:

[4] Culligan Ltd. and/or the Bermuda Liquidators have actively participated in this case, including but not limited to: Culligan Ltd. filed CPLR 3211 motion 12/3/13 and did not raise substitution issue; Culligan Ltd. and Bermuda Liquidators opposed partial settlement (NYSCEF Doc. Nos. 145, 146); Appealed trial court's approval of the partial settlement (NYSCEF Doc. No. 168); Culligan Ltd. motion to compel discovery (NYSCEF Doc. No. 272); Opposed motion for leave to amend (NYSCEF Doc. No. 312). (Singler Aff. 6)

> In connection with the members' voluntary liquidation, Charles Thresh and I, Managing Directors at KPMG Advisory Limited in Bermuda, were appointed as joint and several liquidators ("Liquidators") of Culligan by the Company's shareholders on April 29, 2013. Independent appointed liquidators act as trustees of the assets of the Company for the benefit of the creditors and the shareholders.

(Singler Aff. 3; Ex.1)

It is hardly clear who serves in the capacity of liquidator – Messrs. Thresh and Morrison, in their individual capacity, or as Managing Directors of KPMG Advisory Ltd.? If as individuals, then why even bother to mention KPMG Advisory Ltd.?

The final sentence of this Affirmation is also telling. If they have the duty to serve as trustees for the benefit of the Culligan Ltd. shareholders, then why would they be adverse to this action? It seeks recovery from self-interested directors of hundreds of millions of dollars. The only "shareholders" that benefit from dismissal are the defendants in this case, and the fund and entities they control. Maybe this is allowable in Bermuda. However, the statutory protections of New York law specifically apply to this case, and specifically confer upon Plaintiffs the ability to maintain this derivative action, even if a proper receiver had been appointed under New York law.

Although it would have had no substantive effect because of CPLR 1006, the Bermuda Liquidators could have sought substitution at any time. "A motion for substitution may be made by the successors or representatives of a party or by any party." CPLR 1021. Their attempt to do so now, for the singular purpose of dismissing Plaintiffs' valid derivative action, is a self-evident expression of both the prejudice and impropriety of the relief sought. This is a last ditch effort to avoid discovery and the ultimate finding that the other defendants in this case made illegal dividends and distributions, and committed breaches of various fiduciary duties. The fact that KPMG Advisory Ltd. is now a defendant in this case underscores the lack of independence, inherent conflicts, and the fact that neither KPMG Advisory Ltd. nor Mr. Thresh nor Mr. Morrison

could ever be approved to serve as trustees for all of Culligan Ltd.'s Shareholders. *See Gunzburg, supra.*

D. Request For Discovery.

In the event that the Court finds any merit to Defendant's argument, Plaintiffs respectfully request the motion be denied and Plaintiffs be allowed to conduct discovery pursuant to CPLR 3211(d)). Pertinent facts as to the appointment of the Bermuda Receivers, their obligations, duties and rights are all in Defendant's knowledge, as well as any efforts to be appointed a receiver in New York. (Singler Aff. 4.) Further, Plaintiffs are entitled to know of the interrelationships between the Bermuda Liquidators, KPMG Advisory Ltd. and the other defendants in this action to evaluate whether or not conflicts exist and the Bermuda Liquidators can represent the interests of all shareholders, including Plaintiffs.

Lastly, Plaintiffs are entitled to discovery and the Court cannot dismiss a derivative action when information is solely available to defendants without affording Plaintiffs an opportunity to perform discovery. *See, Parkoff v. Gen. Tel. & Electronics Corp.*, 53 N.Y.2d 412 (1981)*; Byers v. Baxter*, 69 A.D.2d 343, 348 (1st Dept. 1979), *citing Udoff v. Zipf*, 44 N.Y.2d 117, 122 (1978). Plaintiffs have outstanding requests for production, which are the subject of a forthcoming motion to compel.

CONCLUSION

Defendant's motion is fatally flawed on virtually every conceivable level. From a defective notice and no cited authority to support dismissal of this case, to a complete disregard of the fact that the Bermuda Liquidators were not, and cannot be, appointed as receivers to even qualify to be substituted as Plaintiffs. Defendant's motion must fail. As for dismissal, even if the Bermuda Liquidators could be substituted, they still would not have the ability to dismiss the complaint and

Plaintiffs' rights to continue to purse a derivative action are expressly unaltered by a dissolution. Plaintiffs have now adequately pled self-interest by Culligan Ltd.'s Board. This establishes standing under BCL 626(c), negates the Business Judgment Rule at this stage of the proceeding, and the case now needs to move forward. The only case on point specifically holds that a derivative plaintiff need not make a demand on a receiver appointed after the filing of the action. Defendant's last ditch effort to further delay and confuse this case should be rebuked, and its baseless motion denied.

Dated: New York, New York
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