To be Argued by:
ROBERT J. SLYE
(Time Requested: 5 Minutes)

New York Supreme Court

Appellate Division—Fourth Department

Docket No.:
CA 19-02290

In the Matter of

JOHN L. YEHLE,

Petitioner-Appellant,

– against –

JON T. RICH, JR.,

Respondent-Respondent.

BRIEF FOR PETITIONER-APPELLANT

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QUESTIONS INVOLVED

1. Question: Whether a limited liability company member's misrepresentation of his financial contributions to the company constitute the type of "fraud" entitling the other member to set aside a stipulation calling for the auction of company property prior to a hearing on the respective contributions of the members.

Answer: The Court did not address the member's purposeful, sworn misstatements of fact concerning his financial contributions to the company.

2. Question: Whether a member's knowledge concerning the other member's actual financial contributions to the limited liability company is important at the time of auctioning the company's property.

Answer: The Court below failed to recognize the importance of relative positions of the parties at the time of the sale, and the effect those positions have on the willingness to bid at the sale.

3. Question: Whether the stipulation calling for the sale was entered into as the result of the good-faith member's unilateral mistake induced by Respondent's fraudulent misrepresentations.

Answer: The Court below did not address this issue.

NATURE OF THE MATTER

The underlying Petition is for dissolution of a limited liability company pursuant to Section 702 of the New York Limited Liability Company Law. (R9 – 38). This appeal lies from a Memorandum Decision and Order of the Jefferson County Supreme Court (Hon. James P. McClusky, J.S.C. presiding) denying Petitioner's Cross-Motion to vacate a Stipulation and Order requiring an auction of Company property prior to the Court's determination of the relative contributions of the members. (R6 – 8). Petitioner's claim is that the Stipulation was obtained due to his reliance on the fraudulent testimony of the Respondent concerning his claimed contribution to the Company in the form of claimed value of work performed by Respondent's separate construction company. (R58 – R174).

STATEMENT OF FACTS

Petitioner John L. Yehle ("Yehle") and Respondent Jon T. Rich, Jr. ("Rich") formed a Limited Liability Company known as Wellesley Island Storage, LLC ("Wellesley Island Storage" or the "Company") for the purpose of constructing and operating storage units for rental to the general public. (R11 - 12; R39 - 40). Within two years of the commencement of operations, both Yehle and Rich became involved in a monetary dispute regarding the financial status of the Company and management responsibilities. (R13; R39). Ultimately, the parties determined that they could not continue business in the Company. (R13; R39).

During the course of the dissolution proceedings, Rich was deposed concerning his claimed financial contributions to the Company. According to his testimony on March 15, 2017, Rich claimed that he was entitled to claim a personal contribution to the Company of over $310,000.00. (R62). This amount was described by him as representing 1/2 of claimed construction work performed by Rich's separate construction company, Jon T. Rich Construction, LLC ("JTRC") (including 20% in overhead and profit) in the physical construction of the storage facility itself. (R79). In contrast, Yehle's contribution to the Company was in cash, which Rich has admitted is in the amount of $271,000.00. (R63 – 64; R156 – 157). Indeed, Yehle's cash was the only cash infused into the Company, and $178,000.00 of that cash was used by Rich to pay JTRC at a time when he was responsible for the Company's checkbook. (R63; R135; 138; R142).

As the dissolution proceeding progressed, Yehle requested proof of JTRC's work, timecards, foreman reports, and paystubs related to claims for straight time and overtime for employees. (R67 – 75). These items were sought by way of a Notice for Discovery and Inspection to enable Yehle's accounting firm, Bowers & Company, CPA, PLLC, to conduct a forensic accounting of Rich's claimed financial contribution to the Company. (R159 – 167). Rich did not respond to the Notice for Discovery and Inspection until compelled to do so by the Court Order

dated March 26, 2019, months after the Notice for Discovery and Inspection had been served (R75 – 78) and then as late as April 23, 2019 (R169 – 174).

Rich's ultimate response to the Notice for Discovery and Inspection was that he is not in possession of documents from JTRC which support that company's claims for labor hours performed; equipment hours; proof of certain purchases by JTRC, and invoices for the substantial payments to JTRC ($178,000.00) made to JTRC by Rich when he controlled the Wellesley Island Storage checkbook. (R168 – 174).

According to Yehle's forensic accountant, Rich cannot then prove $250,000.00 of JTRC's claimed input to the project, reducing JRTC's claim to $264,000.00 and, thereby, at best reducing Rich's claim of 1/2 to $132,000.00. (R159 – 168).

Notwithstanding this development, a Stipulation and Order granting partial summary judgment and directing the sale of the real property, which had previously been agreed-upon, calls for the auction of Company property prior to a determination of the relative contributions of the members. (R50 – 51).

Rich's misrepresentations of material fact had led Yehle to believe that Rich's contributions to the Company were at least comparable to his own, such that Yehle had agreed to the stipulation. Given the subsequent revelation that Rich's claim to 1/2 ownership cannot withstand scrutiny, Yehle is of the view that, to the extent that the stipulation calls for a sale of the property prior to knowing the

relative contributions, the stipulation was either procured by fraud or a unilateral mistake induced by Rich's knowing misrepresentation. (R60 – 65). As a result, Yehle believes it would be inappropriate to conduct the auction prior to the establishment of each party's contributions so that they will each know whether, and/or how much, to bid at the sale of the Company assets. (R64).

ARGUMENT

POINT I
Good Cause Exists to Annul the Stipulation based upon Rich's Knowing Misrepresentations of Material Fact

The Court of Appeals has held that a "stipulation is generally binding on parties that have legal capacity to negotiate, do in fact freely negotiate their agreement and...reduce their stipulation to a properly subscribed writing...." McCoy v. Feinman, 99 N.Y.2d 295, 302 (2002). Accordingly, the McCoy Court held that "courts should not disturb a valid stipulation absent a showing of good cause such as fraud, collusion, mistake or duress....or unless the agreement is unconscionable...or contrary to public policy...or unless it suggests an ambiguity indicating that the words did not fully and accurately represent the parties' agreement." Id. (citations ommited).

A common definition of "fraud" is that of a material misrepresentation of fact, with knowledge of its falsity by the maker, designed to induce a party's reliance, which then does induce justifiable reliance, and which causes harm. See,

for example, Ambac Assurance Corporation v. Countrywide Home Loans, Inc., 31 N.Y.3d 569, 578-579 (2018) and Southwestern Investors Group, LLC v. JH Portfolio Debt Equities, LLC, 169 A.D.3d 1510, 1511 (4th Dep't 2019). Such a misrepresentation clearly occurred here. Based upon Rich's sworn testimony of the value of his separate construction company's (JRTC's) work, Yehle justifiably believed that Rich's contribution was equivalent to Yehle's proven, and admitted, cash contribution of $271,000.00. Thus, he proceeded to sign the stipulation.

Separately, the type of "mistake" which could justify any rescission or reformation of the stipulation is the establishment "[by] clear and convincing evidence, that the contract was executed under mutual mistake or a unilateral mistake induced by the other party's fraudulent misrepresentation...." Yakobowicz v. Yakobowicz, 142 A.D.3d 996, 997-998 (2nd Dep't 2016), citing Yu Han Young v. Chiu, 49 A.D.3d 535, 536 (2nd Dep't 2008). See, also Mooney v. Manhattan Occupational Physical and Speech Therapies, PLLC, 166 A.D.3d 957, 960 (2nd Dep't 2018). Here, there is no claimed mutual mistake; the mistake was solely Yehle's in believing Rich's testimony to the effect that he had personally invested over $310,000.00 in the Company. Yehle's decision to agree to a sale, prior to judicial determination of relative contributions, was induced by Yehle's reliance upon Rich's untruthful deposition testimony and his inability to obtain Rich's timely responses to the forensic accountant's inquiry.

The stipulation should be annulled, with an order that the sale should abide a hearing on the parties' respective contributions.

POINT II
It Would be Unjust or Inequitable to Enforce the Stipulation Calling for Sale of the Property Prior to Each Party Knowing the Other's Relative Contributions to the Business

The Second Department has made clear that:

> Under almost any given state of facts, where to enforce a stipulation would be unjust or inequitable to permit the other party to gain an unconscionable advantage, courts will afford relief.

Goldstein v. Goldsmith, 243 App. Div. 268, 271-272 (2nd Dep't 1935), cited in favor as recently as 2018 in the case of RCS Recovery Services, LLC v. Mensah, 166 A.D.3d 823, 825 (2nd Dep't 2018).

In this case, it is tempting to conclude, as did the Court below, that it essentially makes no difference what the relative contributions of the parties have been when ordering a limited liability company's sale of its assets. It is respectfully submitted, however, that such a conclusion ignores the reality that there will be no magical third party who or which will appear and bid enough funds at auction to cover both parties' claims. When one party has contributed over $270,000.00 in cash, and the other party has not only been paid from that cash (to a separately-owned and operated construction company), but cannot apparently

provide competent proof of that claimed work, it becomes impossible for the cash-equity partner to determine how much, if at all, he should bid at the sale. If he is to bid at the sale, and commissions to the auction house get paid on the bid amount, must he bid the entire total claimed amount so as to assure the full set-off for himself and then fight over another claimed amount in excess of $300,000.00? Or if he does not bid, and a third party bids in, how is he to know, at any given bid amount, whether he should also join in the bidding process? Finally, if Rich is to bid at the sale, how is Yehle to know what his break-even point is?

All of these questions lead to one simple response: Rich's misrepresentation of a material fact during the course of his Examination Before Trial placed the advantage at the auction in the hands of the person who did not tell the truth, and inures to the detriment of the good-faith owner whose contribution is not only easily provable, but admitted. Goldstein v. Goldsmith, supra.

CONCLUSION

The Stipulation and Order dated November 21, 2018 should be annulled or reformed to require a hearing on relative contributions before the assets of the Company are sold at auction.

Dated: February 20, 2020
Watertown, New York

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