Short Form Order

NEW YORK SUPREME COURT - QUEENS COUNTY

Present: **HONORABLE MARGUERITE A. GRAYS** IAS PART 4
Justice

x

FELIX GLAUBACH, derivatively on behalf of PERSONAL TOUCH HOLDING CORP.,

Plaintiff(s)

-against-

DAVID SLIFKIN, TRUDY BALK, ROBERT MARX, JOHN L. MISCIONE, JOHN D. CALABRO, LAWRENCE J. WALDMAN, ROBERT E. GOFF, JACK BILANCIA, ANTHONY CASTIGLIONE, NANCY ROA and JOSEPHINE DIMAGGIO,

Defendant(s)

PERSONAL TOUCH HOLDING CORP., PT INTERMEDIATE HOLDING, INC. and PERSONAL TOUCH HOME CARE OF N.Y. INC.

Nominal Defendant(s)

x

Index Number: 702987/2015

Motion Date: April 24, 2018

Motion Cal. Number: 7

Motion Seq. No: 15

The following papers numbered 1 to 8 read on this motion by defendant David Slifkin and defendant Trudy Balk for summary judgment dismissing the first, second, third, fourth, tenth, and eleventh causes of action asserted against them.

	Papers Numbered
Notice of Motion - Affidavits - Exhibits	1-2
Answering Affidavits - Exhibits	3
Reply Affidavits	4-5
Memorandum of Law	6-8

Upon the foregoing papers it is ordered that the branches of the motion which are for summary judgment dismissing the first, second, third, and fourth causes of action are denied. Those branches of the motion which are for summary judgment dismissing the tenth and eleventh causes of action are granted.

I. Introduction

Plaintiff Felix Glaubach and defendant Robert Marx established a health care business known as Personal Touch in 1974. Personal Touch provides home health care services, including care by home health aides, social services workers, and physical therapists. Glaubach served as the President of the Company and Chief Executive Officer until 2011. Defendant David Slifkin, a 4.5% shareholder in the company, became the Chief Executive Officer in 2011.Marx serves as the Executive Vice-President, General Counsel, and Special Director of the company. Eventually, Personal Touch did business through over twenty-five S corporations having their own separate articles of incorporation and by-laws.

The complaint alleges that from 2008 to 2011, a period during which Glaubach was incapacitated, Slifkin caused Personal Touch to pay him undeclared and undisclosed income in excess of $500,000 and that he hid this unauthorized income by classifying it as the reimbursement of educational expenses which he never actually incurred. Slifkin also allegedly caused Personal Touch to pay unauthorized income to defendant Trudy Balk (the Vice-President of Operations), Marx, and others, which he allegedly disguised as reimbursement for educational expenses. Among the others allegedly receiving unauthorized income falsely classified as reimbursement for educational expenses were defendant Anthony Castiglione (Vice-President and Treasurer) who received at least $88,968, defendant Jack Bilancia (Chief Information Officer) who received at least $70,000, defendant Nancy Roa (Director of Human Resources) who received at least $17,500, and defendant Josephine DiMaggio (Executive Assistant) who received at least $10,000. The complaint further alleges that Marx, Slifkin, and Balk have conspired to freeze Glaubach out of company affairs.

II. The Plaintiff's Statement of Material Facts

In 1974, plaintiff Felix Glaubach and defendant Robert Marx established the business that grew into Personal Touch Holding Corp. (Personal Touch), a Delaware corporation having its principal place of business in New York. Glaubach, a shareholder and director of the company, brought this action on behalf of Personal Touch.

Defendant David Slifkin, who from 1991 to 2015 was an employee of Personal Touch and related entities, served as the Personal Touch Home Care Chief Financial Officer

and Chief Operating Officer from 1998 and 1999 respectively. In 2011, Slifkin became Personal Touch's Chief Executive Officer, and he remained in that position until December 7, 2015.Slifkin also served on Personal Touch's Board of Directors from December, 2010 until July, 2013. Personal Touch or related entities also employed defendant Trudy Balk, the wife of defendant Slifkin, from 1980 to January 1, 2015.

From 2008 to 2011, Personal Touch and related entities paid over $2,000,000 to numerous employees that the companies deliberately misclassified as continuing education expenses. In 2008, Slifkin instructed Denise Diaz, the accounting manager, to "misclassify [his] bonus payments as continuing education expense payments" because he "started receiving large bonuses" and wanted " a smaller tax liability." Slifkin told Diaz to do the same for Balk. Diaz, who reported directly to Slifkin, followed his directions.

Because the misclassified payments were recorded as expense reimbursements, they " were not reflected on [the] W-2 forms" for Slifkin and Balk, and "taxes were not withheld from those payments". The misclassified payments totaled almost $900,000 for Slifkin during the period 2008-2010 and totaled approximately $330,000 for Balk during the period 2008 to 2011. Slifkin knew that other employees were also receiving misclassified payments, but he did not object. Glaubach did not learn of the scheme until years after it ended, and he received no improper payments.

In 2010, Personal Touch established an employee stock ownership plan (ESOP), whereby Personal Touch employees received shares in the company, and, according to Slifkin's deposition testimony, at the end of 2011 he stopped all of the misclassification of payments for that reason.

After learning of the tax fraud scheme, plaintiff Glaubach informed the Board of Directors, which tasked an Audit Committee comprised of defendant John L. Miscione, defendant John D. Calabro, defendant Lawrence J. Waldman, and defendant Robert E. Goff to investigate the matter. The Audit Committee retained the accounting firm Friedman LLP to handle the investigation, which has cost the company at least $600,000 plus legal fees.

III. Defendant Slifkin's Version of the Facts

In October, 2012, Slifkin told Glaubach that part of the salary and bonus that he and defendant Balk had received from Personal Touch from 2008 through 2010 had been recorded on the company's accounting records as a reimbursement of educational expenses and had not been shown on their W-2's. Slifkin had been instrumental in establishing the ESOP for the company in 2010, a transaction which resulted in a $27,000,000 payment to Glaubach, and Glaubach merely told him to "take care" of his tax problem, so that they could

"continue to grow the Company together." Glaubach admitted under oath that he knew about the misclassification by May, 2013. In May and June 2013, at meetings held with a tax attorney and an accountant hired in connection with an IRS audit, Glaubach was informed that part of the compensation paid to Slifkin and some other employees had been recorded in the company's accounting records as a reimbursement of educational expenses. Glaubach did not bring the matter to the Board's attention during the remainder of 2013 and during 2014.

In September, 2014, several female employees of the company accused Glaubach of sexual harassment, but Glaubach continued his misbehavior despite the advice of outside counsel not to retaliate against them. On November 25, 2014, Glaubach hung a painting of a hand grenade in the main lobby and threatened employees that the situation in the office was about to "blow up." Personal Touch immediately suspended Glaubach, who was informed of the suspension by Slifkin, then the company's CEO. Glaubach blamed Slifkin for his suspension, and Slifkin and his wife for the accusations of sexual harassment made by the three female employees. In June, 2015, Personal Touch terminated Glaubach's employment as President on the grounds that he had: (1) retaliated against the three female employees who had accused him of sexual harassment; (2) misappropriated company assets and opportunities; (3) created an atmosphere of fear and intimidation and (4) engaged "in a self-declared campaign to drive [Slifkin] from the company."

At a meeting of the Board of Directors on February 10, 2015, Glaubach accused Slifkin of stealing millions from the company. The Board reacted to these accusations by appointing an Audit Committee comprised of the four independent directors (defendants Miscione, Calabro, Waldman, and Goff) which hired the forensic accounting firm, Friedman LLP. The accounting firm concluded that no matter how certain sums received from the company by Slifkin had been recorded in the company's accounting records, Slifkin had received only the aggregate compensation to which he was entitled for the years 2008 through 2010 from the company pursuant to his employment agreement.

Slifkin and the other employee defendants have amended their personal tax returns for the purpose of paying the taxes, penalties, and interest on the misclassified sums paid to them.

The Board adopted the Audit Committee's recommendation that Personal Touch not bring any actions against Slifkin who had not received more compensation than he was contractually entitled to.

IV. The Relevant Causes of Action

Plaintiff Glaubach began the instant action by the filing of a summons and a complaint on March 30, 2015. He subsequently served an amended complaint dated January 13, 2016, and the first, second, third, fourth, tenth and eleventh causes of action are relevant here.

The first cause of action, after making reference to prior allegations in the complaint, alleges the following: From 2008 to 2010, Personal Touch paid Slifkin "undeclared and undisclosed income in the sum in excess of $500,000." Slifkin concealed the unauthorized income by having it recorded as the reimbursement of educational expenses which he never incurred. Slifkin not only directed that misclassified income be paid to himself, but also to other company employees. Slifkin's misconduct "exposed the company to risk by having the Company participate in his attempt to cover up taxable income received by him and others." The Company was damaged "in the sum of unauthorized compensation paid to the Company employees and hidden as reimbursement of education expenses." Slifkin's actions constituted a breach of fiduciary duty and a waste of corporate assets, permitting recovery under BCL§720.

The second cause of action charges that Slifkin committed a waste of corporate assets and gained an unjust enrichment by taking at least $500,000 from the company for educational expenses that he did not incur.

The third cause of action alleges that " Balk's taking of at least $85,000 as reimbursement for educational expenses that she did not incur constitutes unjust enrichment and waste of corporate assets of the Company for which recovery is called for under BCL§ 720".

The fourth cause of action alleges that Balk's taking of reimbursement for educational expenses that she did not incur amounted to a breach of fiduciary duty and intentional mismanagement " for which recovery is called for under BCL §720".

The tenth cause of action alleges the following: Slifkin and employees under his direct control planned a "severance package" for Balk that Glaubach objected to as extravagant, as a scheme to keep Balk on the company payroll as long as Slifkin desired. In order to prevent Glaubach from obtaining more information about the severance package and to stop him from presenting his objections to the Board, Slifkin and Balk schemed to isolate him from the company. In furtherance of their scheme, Slifkin and Balk solicited company employees to make unfounded accusations of sexual harassment against him. Slifkin and Balk also made false allegations that Glaubach was retaliating against those employees who had made the accusations of sexual harassment. "Slifkin made it known that if Gluabach

would stop objecting to the severance package proposed for Balk, the sexual harassment allegations would go away." Slifkin and Balk have committed a breach of fiduciary duty, waste of company assets, and intentional mismanagement.

The eleventh cause of action is based on allegations that Slifkin and others conspired to freeze Glaubach out of the company, caused employees to make unfounded accusations of sexual harassment against him, and barred him from entering his office. The eleventh cause of action reads in relevant part: "Slifkin's and Marx's ultra vires acts of barring Glaubach from Personal Touch's office constitutes a breach of their fiduciary duty. *** As a result of such actions, the Company has incurred significant expenses which are a waste of corporate assets which Slifkin and Marx should reimburse the Company pursuant to BCL §720".

V. Discussion

In regard to the first, second, third, and fourth causes of action, defendant Slifkin and defendant Balk argue that they are entitled to summary judgment because: (1) there is no present loss or damage to the company; (2) although they received compensation that was misclassified as the reimbursement of educational expenses, they did not receive more compensation than they were entitled to; (3) neither the IRS nor the State of New York has sought to collect unpaid taxes from the company because of the tax schem and (4) derivative claims cannot be based on a "hypothetical" tax liability (*see, SC Note Acquisitions, LLC v. Wells Fargo Bank, N.A.,* 934 F. Supp. 2d 516). This Court has previously rejected these arguments because, *inter alia*, the company did indeed incur a loss from the expensive investigation required by Glaubach's accusations about the tax scheme made to the Board of Directors (see, the decision and order rendered on plaintiff Glaubach's motion for summary judgment against defendant Slifkin on the first and second causes of action in the amended complaint, Sequence Number "11"). The Court also rejects the argument made here which is to the effect that the company could have avoided the expenses of the investigation by simply accepting at face value the admissions made by Slifkin and the entries in the company's records about the nature and extent of the misconduct. Defendant Slifkin and defendant Balk are not entitled to summary judgment dismissing the first, second, third, and fourth causes of action (see, the decision and order rendered on plaintiff Glaubach's motion for summary judgment against defendant Slifkin on the first and second causes of action in the amended complaint, Sequence Number "11"). The Court notes that it does reject plaintiff Glaubach's theory that the company may recover the compensation paid to defendant Slifkin and defendant Balk under the "faithless servant" doctrine. The faithless servant doctrine provides that an employee who violates his or her duty of loyalty or fidelity in the performance of his or her work forfeits the right to compensation for that work (*see, In re Blumenthal,* 32 AD3d 767, 768; *Soam Corp. v. Trane Co.*, 202 AD2d 162;

complaint does not seek the forfeiture of the defendants' compensation, and, while an unpleaded matter can be raised on a motion for summary judgment "as long as it would not be likely to surprise the adverse party or raise issues of fact not previously apparent" (*Brodeur v. Hayes*, 305 AD2d 754, 755; *Warner v. Kain*, -AD3d-, - NYS3d-, 2018 WL 3057884), the Court finds that in regard to the forfeiture of compensation, plaintiff Glaubach has attempted to raise a matter in an opposition memorandum of law that was not previously apparent as a relevant issue in this case. Moreover, Delaware has not adopted the faithless servant doctrine (*see, Enzo Life Scis., Inc. v. Adipogen Corp.*, 82 F Supp. 3d 568[D. Del. 2015]), and under New York law, "the doctrine only applies where the employee's misconduct permeated the employee's service in its most material and substantial part" (*Sanders v. Madison Square Garden, L.P.*, 2007 WL 1933933, at 3 [S.D.N.Y. July 2, 2007]), which was not the case here.

In regard to the tenth cause of action, which concerns the severance package given to defendant Balk and allegedly false accusations of sexual harassment, "the proponent of a summary judgment motion 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 ***" (*Alvarez v. Prospect Hospital*, 68 NY2d 320, 324). The defendants successfully carried this burden.

The Court notes initially that the thrust of the tenth cause of action is not against the severance package itself. In any event, the defendants submitted evidence showing that a special committee comprised of the Independent Directors, established by the unanimous decision of the entire board, including Glaubach, determined Balk's severance package, not Slifkin and employees under his direct control. Glaubach expressed his objections to the severance package in a July 29, 2014 letter to one of the Independent Directors and again on August 4, 2014 when he met with the special committee. Despite Glaubach's objections, the special committee found that the terms were consistent with those received by departing company executives in the past and that terms beneficial to the company were included such as eighteen months compensation in consideration of which Balk consented to a broad non-competition and confidentially agreement. The defendants showed prima facie that the Board's approval of the severance package is protected by the business judgment rule, which under both New York and Delaware law essentially "prohibits judicial inquiry into actions of corporate directors taken in good faith and in the exercise of honest judgment in the lawful and legitimate furtherance of corporate purposes" (*Levandusky v. One Fifth Ave. Apartment Corp.*, 75 NY2d 530, 537– 538). In opposition, Glaubach failed to produce evidence sufficient to create a triable issue of fact in regard to the severance package itself.

The thrust of the tenth cause of action is against an alleged conspiracy by Slifkin and Balk to induce company employees to make false accusations of sexual harassment against

Glaubach for the purpose of forcing him to drop his objections to the severance package. Here, again, the defendants submitted evidence sufficient to show that they are prima facie entitled to judgment as a matter of law (*see, Alvarez v. Prospect Hospital, supra*). The investigation into Glaubach's misconduct did not begin until after he had already voiced his objections to the severance package. The Special Committee rendered its decision on the severance package on September 5, 2014, but Rachel Hold-Weiss , Esq. , then the company's Associate Counsel and one of the complainants against Glaubach, did not inform the company's outside counsel about the sexual harassment complaints against Glaubach until September 16, 2014. According to Hold-Weiss, she decided to investigate Glaubach's conduct after he slammed a door on Dr. Balk on September 8, 2014. On November 21, 2014, after an investigation, the outside law firm rendered its report about the allegations made against Glaubach by three female employees: Rachel Hold-Weiss, Esq., Pauline Martell, the Company's Director of Purchasing and Web Development, and Josephine DiMaggio, an administrative assistant. The report stated that Glaubach had made "comments of a sexual nature that made Complainants uncomfortable *** Glaubach admitted to making several such statements to Complainants *** Finally, the evidence supports that once Glaubach was told of the investigation, his behavior toward Complainants changed and he displayed adverse behavior toward them." None of the employees who accused plaintiff Glaubach of sexually harassing them testified that they did so to force Glaubach into dropping his objections to the severance package. The defendants showed prima facie that the investigation into the complaints against Glaubach was begun for a legitimate company purpose and that it was begun by Hold-Weiss, herself one of the complainants, not Slifkin and Balk. Moreover, the company's assets were not wasted by the investigation "[A]llegations of sexual harassment trigger federal law and an attendant duty imposed upon employers to take reasonable steps to correct harassing behavior, including, where appropriate, conducting an investigation" (*Malik v. Carrier Corp.*, 202 F3d 97,104; *see, Torres v. Pisano*, 116 F3d 625). In opposition, Glaubach failed to produce evidence sufficient to create a triable issue of fact.

The defendants are also entitled to summary judgment dismissing the eleventh cause of action. On or about September 16, 2014, the company's Associate General Counsel, told the company's outside counsel that three female employees had accused plaintiff Glaubach of, among other things, making lewd comments to them. Personal Touch subsequently hired a law firm (Klein Zelman) to investigate the charges. After interviewing Glaubach, the complainants, and witnesses, Klein Zelman wrote a report that found that Glaubach had made "comments of a sexual nature that made complainants uncomfortable." On November 25, 2014, just a few days after the report, Glaubach directed a painting of a grenade to be hung outside of defendant Marx's office. Glaubach warned employees that there is "an explosive situation" at the company and that "he does not know when it is going to blow up." Because of the plaintiff's conduct, the Independent Directors conferred among themselves and with

the company's outside counsel, and, acting upon the advice received from the attorneys, the Independent Directors decided that Glaubach would be suspended as the company's President and that he would be barred from his office because his "continued presence at the company poses an immediate and continuing threat to the interests of the company and its employees." Defendant Slifkin and defendant Marx were told to inform Glaubach of the Board's decision to suspend him. The company's outside counsel sent Slifkin an e-mail on November 25, 2014 stating that "the Independent Directors are fine with [the] e-mail [communicating the suspension to Glaubach]." The Board's attorney informed the plaintiff's attorney of the suspension by e-mail sent November 28, 2014. The eleventh cause of action alleges that "Slifkin's and Marx's ultra vires acts of barring Glaubach from Personal Touch's office constitutes a breach of their fiduciary duty." The evidence produced by the defendants concerning the authorization of Glaubach's suspension and restriction by the Independent Directors and the Board's confirmation of those measures on February 10, 2015, showed prima facie that Marx and Slifkin did not act "ultra vires" as alleged in the eleventh cause of action. In opposition, the plaintiff did not produce evidence showing that there is a triable issue of fact (*see, Alvarez v. Prospect Hospital, supra.*)

Dated:

AUG 14 2018

J.S.C.

FILED

AUG 22 2018

COUNTY CLERK
QUEENS COUNTY