SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: **HON. FRANK NERVO** **PART** **04**

Justice

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ALVIN CLAYTON FERNANDES

Plaintiff,

- v -

MATRIX MODEL STAFFING, INC.,

Defendant.

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INDEX NO. 160294/2021

MOTION DATE 11/30/2021, 02/22/2022

MOTION SEQ. NO. 002 003

DECISION + ORDER ON MOTION

The following e-filed documents, listed by NYSCEF document number (Motion 002) 9, 10, 11, 12, 13, 15
were read on this motion to/for DISSOLUTION.

The following e-filed documents, listed by NYSCEF document number (Motion 003) 16, 17, 18, 19, 20, 21, 22, 23, 29, 30, 31, 32, 33
were read on this motion to/for DISMISS.

Petitioner, by order to show cause, seeks dissolution of the respondent corporation pursuant to Business Corporation Law § 1104 (motion sequence 002).[1] In lieu of filing an answer or opposition to the petition and order to show cause, respondent has filed a motion to dismiss the petition pursuant to CPLR §§ 3211(a)(1) and (7). The Court consolidates motion sequences 002 and 003 for the purposes of disposition.

[1] Motion sequence 001, a prior order to show cause, was declined due to counsel's non-compliance with Judiciary Law § 470, with leave to renew.

MOTION TO DISMISS

As with all motions to dismiss under CPLR § 3211, the complaint should be liberally construed, the facts presumed to be true, and the pleading accorded the benefit of every possible favorable inference (*see e.g. Leon v. Martinez*, 84 NY2d 83 [1994]). "Under CPLR § 3211(a)(1), a dismissal is warranted only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law" (*id.*; citing *Heaney v. Purdy*, 29 NY2d 157 [1971]).

To the extent that the motion seeks dismissal under § 3211(a)(7), it is likewise afforded the benefits of liberal construction, a presumption of truth, and any favorable inference (*id.*; *Anderson v. Edmiston & Co.*, 131 AD3d 416, 417 [1st Dept 2015]; *Askin v. Department of Educ. of City of N.Y.*, 110 AD3d 621, 622 [1st Dept 2013]). The motion must be denied if from the four corners of the pleadings "factual allegations are discerned which taken together manifest any cause of action cognizable at law" (*Polonetsky v. Better Homes Depot*, 97 NY2d 46, 54 [2001]). A complaint should not be dismissed so long as, "when the plaintiff's allegations are given the benefit of every possible inference, a cause of action exists," and a plaintiff may cure potential deficiencies in its pleading through affidavits and other evidence (*R.H. Sanbar Proj., Inc. v. Gruzen*

Partnership, 148 AD2d 316, 318 [1st Dept 1989]). However, bare legal conclusions and factual allegations which are inherently incredible or contradicted by documentary evidence are not presumed to be true (*Mark Hampton, Inc. v. Bergreen*, 173 AD2d 220 [1st Dept 1991]).

Here, respondent first contends that petitioner lacks standing to bring this action as petitioner has failed to establish his shares are voting shares under BCL § 1104-a. As relevant here, BCL § 1104-a provides holders of 20% or more of voting shares of a closely held corporation may seek judicial dissolution. Respondent's argument conflates the burden of proof; it is respondent who bears the burden on a CPLR § 3211 motion to establish, via documentary evidence, that petitioner's shares are non-voting. Respondent has failed to proffer any proof of this contention. Furthermore, and notably upon a cursory reading of respondent's papers, respondent does not argue that petitioner does not hold voting shares or is not otherwise entitled to vote in an election of directors – respondent only claims that petitioner has not proffered proof of those shares in the petition. Respondent cites no authority for the proposition that where a voting shareholder's status is not contested the failure to annex proof of the voting shares is fatal to a dissolution action. Accordingly, respondent's claim of lack of standing is palpably devoid of merit.

Next, respondent contends that petitioner has failed to plead the special circumstances and oppressive acts necessary for dissolution. BCL § 1104-a(a)(1) provides for dissolution on the grounds that "[t]he directors or those in control of the corporation have been guilty of illegal, fraudulent or oppressive actions toward the complaining shareholders". It is well established that oppressive conduct is measured by the complaining shareholder's 'reasonable expectations' and that oppression arises when objectively reasonable expectations central to a shareholder's decision to join the venture are substantially defeated (*Matter of Kemp & Beatley*, 64 NY2d 63, 73 [1984]).

Here, petitioner alleges that, inter alia, respondent, through its director Willard and without petitioner's consent, designated petitioner as the person responsible for collecting and paying employment taxes for respondent corporation. Petitioner further alleges that respondent, again acting through its director Willard, failed to pay appropriate employment taxes, resulting in over $200,000.00 in penalties being assessed against petitioner, personally, by the Internal Revenue Service (IRS). Finally, petitioner avers, and respondent does not deny, that petitioner was never responsible for collecting, accounting, or paying employment taxes for respondent's employees. Notably, no affidavit from Willard or respondent is submitted on this motion.

Failing to pay tax liabilities is corporate mismanagement which defeats a petitioner's reasonable expectations sufficient to constitute oppression (*In re Miescher*, 288 AD2d 129 [1st Dept 2001]). It is beyond argument that a shareholder, who is not responsible for payroll and accounting, has an objectively reasonable expectation that the corporation will not designate the shareholder as the responsible party for payroll withholdings in IRS filings. The designation of the shareholder, without their consent, in IRS filings as the responsible party for payroll taxes and the corporation's subsequent failure to properly withhold payroll taxes – resulting in several hundred-thousand dollars of tax penalties being levied against the shareholder – is oppressive, if not fraudulent or criminal behavior. To the extent that respondent argues petitioner rejected an involved role at respondent corporation as militating against dissolution, such argument further supports a finding that respondent's designation of petitioner, a non-involved shareholder, as the responsible party for its IRS payroll withholdings defeats the shareholder's objectively reasonable expectations. Consequently, respondent's argument that the petition fails to plead requisite oppression for dissolution is entirely without merit.

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DISSOLUTION BY ORDER TO SHOW CAUSE

Turning to the petition for dissolution, and as discussed supra, BCL § 1104-a provides for a right of judicial dissolution where holders of 20% or more of the outstanding shares of a closely held corporation seek to dissolve the corporation under certain special circumstances. "The specified circumstances are (1) where the directors or those in control of the corporation have been guilty of illegal, fraudulent or oppressive actions toward the complaining shareholders; or (2) where the property or assets of the corporation are being looted, wasted or diverted for noncorporate purposes by the controlling faction" (*Fedele v. Seybert*, 250 AD2d 519 [1st Dept 1998]; *see also* BCL § 1104-a). In determining whether involuntary dissolution is appropriate, the Court must consider whether dissolution is the only feasible means that petitioner will reasonably expect a fair return on investment and whether dissolution is reasonably necessary to protect the rights and interests of shareholders or petitioner (BCL §§ 1104-a[b][1] and [2]). Notwithstanding a petition to dissolve a corporation, BCL § 1118 provides the non-petitioning shareholders "an absolute right to avoid the dissolution proceedings and any possibility of the company's liquidation by electing to purchase petitioner's shares at their fair value and upon terms and conditions approved by the Court" (*Matter of Pace Photographers [Rosen]*,71 NY2d 737, 744-745 [1988]; *see also Fedele v. Seybert*, 250

AD2d 519 [1st Dept 1998]). However, the election of a shareholder's absolute right to avoid dissolution under BCL § 1118(a) via purchase of petitioner's shares must be effectuated within 90 days of filing the petition. An election after the 90 days is subject to the Court's discretion (*see* BCL § 1118[a]).

Here, as an initial matter, the only shareholder of respondent, other than petitioner, is the current director of respondent and owner of 80% of the respondent's shares, Willard, who has not elected to purchase petitioner's 20% stake. Furthermore, respondent's opposition to dissolution and in support of the motion to dismiss this action is wholly silent on the issue of any buy-back. Consequently, respondent Matrix cannot avoid dissolution via BCL § 1118 at this time; Willard having not elected to exercise her rights under § 1118.

Turning to the merits of the petition for dissolution, as discussed *supra*, the failure to pay a corporation's tax liabilities is corporate mismanagement and defeats a petitioning shareholder's reasonable expectations regarding their investment sufficient to constitute oppression under BCL § 1104-a (*In re Miescher*, 288 AD2d 129). Here, petitioner alleges the respondent corporation's failure to properly withhold its employees' taxes, and respondent improperly informing the IRS that petitioner was responsible for payroll/accounting and

employee tax withholding, has resulted in the IRS levying more than $200,000.00 in tax penalties against petitioner, in his individual capacity. Respondent has not answered the petition nor has respondent disputed that it, through Willard and without petitioner's consent: filed documents with the IRS naming petitioner as the responsible designee for payroll tax withholdings; and failed to withhold taxes from its employees' pay. As discussed supra, an objectively reasonable shareholder would not expect the corporation to name the shareholder as responsible for tax liabilities of the corporation's employees without the shareholder's consent. Such improper designation, resulting in hundreds of thousands of dollars of tax liabilities against the individual shareholder, likely frustrates the shareholder's reasonable expectations central to a shareholder's decision to join the venture (*Matter of Kemp & Beatley*, 64 NY2d at 73).

Consequently, the petition alleges a demonstrated risk to petitioner's rights – chiefly continued future tax and other financial liabilities arising from respondent's oppressive conduct. It is, therefore, "incumbent upon the parties seeking to forestall dissolution to demonstrate to the court the existence of an adequate, alternative remedy" (*id*. at 74). Respondent has failed to offer alternative remedies. Respondent's concern that dissolution will result in its 170

employees being terminated is largely contradicted by respondent Matrix's failure to offer any alternatives to dissolution. "A court has broad latitude in fashioning alternative relief, but when ... there has been a complete deterioration of relations between the parties, a court should not hesitate to order dissolution" (*id.*).

However, the Court is mindful of BCL § 1109, generally which requires a hearing establishing the underlying facts prior to a finding of dissolution. As discussed, *supra*, respondent has not denied the allegations of the petition, nor has respondent offered any alternative remedy to dissolution. While neither respondent corporation nor its director, Willard, has submitted an affidavit raising a question of fact, respondent has, nevertheless, questioned the need for dissolution (*see e.g. Matter of Steinberg*, 249 AD2d 551 [2d Dept 1998] reversing trial court's granting of dissolution petition, finding hearing required where questions of fact regarding merits of petition and appropriate remedy raised in competing affidavits). Accordingly, the matter is referred to a referee to hear and report on the issue of dissolution.

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Accordingly, it is

ORDERED that respondent's motion to dismiss (motion sequence 003) is denied in its entirety; and it is further

ORDERED that the petition (motion sequence 002), is referred to a referee to hear and report, as below; and it is further

ORDERED that a Judicial Hearing Officer ("JHO") or Special Referee shall be designated to hear and report to this court on the following individual issues of fact, which are hereby submitted to the JHO/Special Referee for such purpose:

1. Establishing the underlying facts of the petition for dissolution, the merits of the petition, and the appropriate remedy (*see e.g. Matter of Steinberg*, 249 AD2d 551 [2d Dept 1998]; *Matter of Kournianos*, 175 AD2d 129 [2d Dept 1991]; BCL § 1109)

and it is further

ORDERED that the powers of the JHO/Special Referee shall not be limited beyond the limitations set forth in the CPLR: and it is further

ORDERED that this matter is hereby referred to the Special Referee Clerk (Room 119, 646-386-3028 or spref@nycourts.gov) for placement at the earliest possible date upon the calendar of the Special Referees Part (Part SRP), which, in accordance with the Rules of that Part (which are posted on the website of this court at www.nycourts.gov/supctmanh at the "References" link), shall assign this matter at the initial appearance to an available JHO/Special Referee to hear and report as specified above; and it is further

ORDERED that counsel shall immediately consult one another and counsel for plaintiff/petitioner shall, within 15 days from the date of this Order, submit to the Special Referee Clerk by fax (212-401-9186) or e-mail an Information Sheet (accessible at the "References" link on the court's website) containing all the information called for therein and that, as soon as practical thereafter, the Special Referee Clerk shall advise counsel for the parties of the date fixed for the appearance of the matter upon the calendar of the Special Referees Part; and it is further

ORDERED that on the initial appearance in the Special Referees Part the parties shall appear for a pre-hearing conference before the assigned JHO/Special Referee and the date for the hearing shall be fixed at that

conference; the parties need not appear at the conference with all witnesses and evidence; and it is further

ORDERED that, except as otherwise directed by the assigned JHO/Special Referee for good cause shown, the trial of the issue(s) specified above shall proceed from day to day until completion and counsel must arrange their schedules and those of their witnesses accordingly; and it is further

ORDERED that counsel shall file memoranda or other documents directed to the assigned JHO/Special Referee in accordance with the Uniform Rules of the Judicial Hearing Officers and the Special Referees (available at the "References" link on the court's website) by filing same with the New York State Courts Electronic Filing System (see Rule 2 of the Uniform Rules); and it is further

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ORDERED that any motion to confirm or disaffirm the Report of the JHO/Special Referee shall be made within the time and in the manner specified in CPLR 4403 and Section 202.44 of the Uniform Rules for the Trial Courts.

THIS CONSTITUTES THE DECISION AND ORDER, AND ORDER OF REFERENCE OF THE COURT.

4/20/2022
DATE

FRANK NERVO, J.S.C.

CHECK ONE:		CASE DISPOSED			X	NON-FINAL DISPOSITION	
		GRANTED		DENIED		GRANTED IN PART	X OTHER
APPLICATION:		SETTLE ORDER				SUBMIT ORDER	
CHECK IF APPROPRIATE:		INCLUDES TRANSFER/REASSIGN				FIDUCIARY APPOINTMENT	X REFERENCE