To be Argued by:
MICHAEL J. MALONEY
(Time Requested: 15 Minutes)

New York Supreme Court

Appellate Division—Second Department

Docket No.: 2020-06947

NANCY SHUNKUEN NG, individually and derivatively on behalf of ASquared Group, Inc. as Successor in Interest to Kyoto Restaurant Inc. and Kyoto Dining Group Inc.,

Plaintiff-Respondent,

– against –

ASQUARED GROUP, INC. as Successor in Interest to Kyoto Restaurant Inc. and Kyoto Dining Group Inc., XYZ CORP. a fictitious corporation name intending same to be a successor in interest to ASquared Group, Inc. d/b/a Mira Sushi a/k/a Mira Sushi & Izakaya and ANDY LEE,

Defendants-Appellants.

REPLY BRIEF FOR DEFENDANTS-APPELLANTS

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SUMMARY OF REPLY

Punitive damages are only proper upon a finding of "exceptional" misconduct, such as the utter disregard of a plaintiff's ownership interest. Here, however, Plaintiff does not dispute that, following the corporate reorganization that is the subject of Plaintiff's complaint, she continued to receive payment of her 25% interest in profits during the time when the business was profitable. Thus, Plaintiff concedes that Defendant did not disregard Plaintiff's ownership interest. There is no "exceptional" misconduct here sufficient to support an award of punitive damages.

Plaintiff contends she is aggrieved because she did not receive certain financial statements. But, even if true, failure to provide timely financial statements does not support a finding of exceptional misconduct.

Moreover, the facts show that Mr. Lee did not act nefariously in reorganizing the business. Mr. Choi, who made decisions on behalf of Plaintiff, his mother, admitted that Mr. Lee informed him of the intent to reorganize as early as 2013. Mr. Choi also admitted that after the reorganization, Defendants continued to pay Plaintiff 25% of the profits and treated her as a continuing owner. This is plainly not a case of corporate theft; it is merely one of shareholders' deadlock once a business ceased being profitable and one partner – Plaintiff and Mr. Choi – refused to invest further capital. The deadlock was a result of Plaintiff's refusal to take action without Mr. Choi's consent, and Mr. Choi – living abroad in China – remained unavailable

during the time when important decisions needed to be made for the company. While the facts may have warranted dissolution per Bus. Corp. Law § 1104(a)(3), they certainly did not warrant punitive damages.

Further, the compensatory damages award was calculated improperly. It was improper for the Court to accept Plaintiff's invitation to calculate compensatory damages based on a formula in the shareholder agreement that provides for a purchase price based on average monthly "gross sales." Defendants produced the books and records of the company during discovery before the lower court, but Plaintiff failed to submit expert analysis of those records. Thus, Plaintiff's reliance on (i) credit card receipts from October 2015 through September 2016 and (ii) Mr. Choi's testimony is entirely speculative as to "gross sales." The credit card sales failed to reflect processing fees and other transaction costs, and Mr. Choi lacked any personal knowledge of any purported cash sales.

Finally, the lower court erred by granting Plaintiff's motion for judgment on default because Defendants demonstrated a reasonable excuse for their delay and a meritorious defense.

Accordingly, the lower court's decision should be reversed in its entirety. It should be remanded solely for a new trial on compensatory damages.

ARGUMENT

I. THE PUNITIVE DAMAGES AWARD SHOULD BE VACATED AND REVERSED

In her opposition, Plaintiff-Respondent fails to dispute, and does not even address the fact that Defendant-Appellant continued to pay to Plaintiff-Respondent her 25% share of profits generated by the Kyoto Entities. Plaintiff's tacit acknowledgement that Defendant-Appellant continued to treat Plaintiff-Respondent as a 25% owner of the business after the reorganization of the business undercuts the entire basis for the punitive damages award.

New York precedent makes clear that punitive damages are only warranted when misconduct is "exceptional." *Sharapata v. Islip*, 56 N.Y.2d 332, 335, 452 N.Y.S.2d 347, 349, 437 N.E.2d 1104, 1106 (1982). "Exceptional" misconduct justifying punitive damages is often described as "manifest[ing] a conscious disregard of the rights of others," *Chauca v. Abraham*, 30 N.Y.3d 325, 331 (2017), or "malice or evil motive," *Ross v. Louise Wise Servs.*, 8 N.Y.3d 478, 489 (2007).

Mr. Lee's continued payment to Plaintiff-Respondent of her 25% share of profits after the allegedly fraudulent reorganization is the exact opposite of the type of "disregard for the rights of others" or "malice or evil motive" that is necessary to support an award of punitive damages. *Id.*

Plaintiff-Respondent also reiterates, in conclusory fashion, her contention that the reorganization occurred without notice to her son, Mr. Choi. Plaintiff-

Respondent fails to dispute the evidence showing that Defendant-Appellant provided notice to Mr. Choi by email and telephone in 2013 regarding a second reorganization (*i.e.*, the transfer of the business to Asquared). Mr. Choi acknowledged receiving these emails and declining to request records at that time. Mr. Lee's emails, although arguably unartfully drafted, show that Mr. Lee made a good faith attempt to provide email notice to Mr. Choi, who in all respects acted on behalf of Plaintiff-Respondent, and undercut Plaintiff-Respondent's contention that the reorganization was without notice.

The cases relied upon by Plaintiff-Respondent are entirely inapposite. *Giblin v. Murphy*, 73 N.Y.2d 769 (1988), involved the transfer by insiders of a company's assets without notice and with intent to deceptively deprive other shareholders of the value of their holdings. These facts are entirely distinguishable because in this action, Defendant-Appellant provided notice to Mr. Choi and continued to treat Mr. Choi and Plaintiff-Respondent as 25% owners after the reorganization.

In *Stein v. McDowell*, 74 A.d.3d 1323 (2d Dep't 2010), the defendant, despite incontrovertible evidence to the contrary, had actively sought to "usurp[] the[] ownership interest" of a co-shareholder and his successors-in-interest. *Stein*, 74 A.D.3d at 1326. That is not the case here, where Defendant-Appellant actively sought Mr. Choi's (and, therefore, Plaintiff-Respondent's) involvement in the

reorganization and continued to recognize and pay Plaintiff-Respondent's 25% share of profits following the reorganization.

In addition, Plaintiff-Respondent fails to dispute that the restaurant became unprofitable in 2015 or that she (and Mr. Choi) declined Mr. Lee's request to contribute additional funds in 2015, when the business faced substantial costs. In short, the business had little or no value in 2015 and, therefore, the 2016 sale of the business is not sufficient grounds to support an award of punitive damages.

Plaintiff-Respondent's reliance on *Fordham-Coleman v. Nat'l Fuel Gas Distribution Corp.*, 42 A.D.3d 106 (4th Dep't 2007) and *Nardelli v. Stamberg*, 44 N.Y.2d 500 (1978), is misplaced. Both of those cases involved jury trials. In a nonjury determination, such as this action, "as to a weight of the evidence review . . ., the Appellate Division has the power to make new findings of fact. . . ." *Green v. William Penn Life Ins. Co. of N.Y.*, 902 N.Y.S.2d 542, 543-44 (1st Dep't 2010) ("In reviewing a judgment of Supreme Court, the Appellate Division has the power to determine whether a particular factual question was correctly resolved by the trier of facts.") (quoting *Cohen v. Hallmark Cards*, 45 N.Y.2d 493, 498 (1978)). The punitive damages award is, therefore, without basis and should be vacated.

II. THE PUNITIVE DAMAGES AWARD IS EXCESSIVE

The quantum of the punitive damages award is also grossly excessive. "It is the duty of the court to keep a verdict for punitive damages within reasonable bounds

considering the purpose to be achieved as well as the *mala fides* of the defendant in the particular case." *Faulk v. Aware, Inc.*, 244 N.Y.S.2d 259, 266 (1st Dep't 1963), *aff'd without op.*, 14 N.Y.2d 899; *Manolas v. 303 W. 42nd St. Enters.*, 569 N.Y.S.2d 701, 702 (1st Dep't 1991).

In her opposition Brief, Plaintiff-Respondent cites to the policies underlying the Court's power to award punitive damages, such as the intention to "punish tortfeasors" and "deter future reprehensible conduct," but Plaintiff-Respondent fails to explain why the quantum of the award in this case bears any rational relationship to the *mala fides* of Mr. Lee. The relevant facts are not subject to any material dispute: Mr. Lee attempted to provide Mr. Choi with notice of the reorganization and the reasons why it was necessary, and, following the reorganization, Mr. Lee continued to regard Plaintiff-Respondent as a 25% owner of the business and to pay her 25% share of the profits. When the business suffered catastrophic losses, Mr. Lee sought additional capital from Plaintiff-Respondent, who declined to invest further funds. These are not the actions that justify a punitive damages award of $700,000. *See* *Nardelli v. Stamberg*, 44 N.Y.2d 500, 503, 406 N.Y.S.2d 443, 445 (1978); *Coscia v. Jamal*, 2017 NY Slip Op 09114, ¶ 3, 69 N.Y.S.3d 320, 325 (2d Dep't 2017).

The lower court failed to properly consider the motives and lack of *mala fides* on Defendants' part. Plaintiff-Respondent and her son admitted that Defendants continued to pay to them profits until 2015, well after the business transferred to

Asquared. Mr. Lee made attempts to confirm Plaintiff's continued 25% ownership interest in Asquared. As discussed above, continued operation of the business was impossible given (i) Plaintiff's unwillingness to consent to any corporate transactions without consulting with her son; (ii) Mr. Choi's continued unavailability; and (iii) Mr. Choi's refusal to contribute to expenses in accordance with the parties' long-standing agreement.

"In determining the amount of punitive damages, the trier of fact can properly consider all circumstances immediately connected with the transaction tending to exhibit or explain the motive of the defendant, the harm done to the plaintiff, the wealth of the defendant, and the degree of deterrence resulting from the award. . . ." *Laurie Marie M. v. Jeffrey T. M.*, 559 N.Y.S.2d 336, 342 (2d Dep't 1990). Here, the $700,000 award is plainly excessive.

III. THE COMPENSATORY DAMAGES AWARD SHOULD BE VACATED AND REMANDED FOR FURTHER PROCEEDINGS

In her opposition Brief, Plaintiff-Respondent makes several false statements. First, Mr. Lee did not "refuse[] to comply with requests to examine the corporate bank accounts and expense records." (Opp'n Br. 11.) Mr. Lee offered to permit inspection of those records at the company's offices, which is entirely consistent with Bus. Corp. Law § 624(b). (R. at 522) ("I can only show you numbers face to face".)

Second, the lower court's holding that the sale of Asquared was made at "a devalued price" is entirely speculation on the part of the lower court. Plaintiff-Respondent failed to offer any expert opinion as to the fair value of the business at the time of the sale, a matter that is ordinarily only provable through expert testimony. *See* *DeAngelis v. AVC Servs., Inc.*, 2008 NY Slip Op 10621, ¶ 2, 57 A.D.3d 989, 991, 871 N.Y.S.2d 290, 292-93 (2d Dep't 2008). It was not the place of the lower court to play the role of a business valuation expert and, upon making its own, subjective determination of fair value, hold that fact against Mr. Lee. *Wathne Imports, Ltd. v. PRL USA, Inc.*, 101 A.D.3d 83, 87 (1st Dep't 2012) (internal citation omitted) ("New York law does not countenance damage awards based on [s]peculation or conjecture"); *City of N.Y. v. State*, 27 A.D.3d 1, 4 (1st Dep't 2005); *76-82 St. Marks, LLC v. Gluck*, 147 A.D.3d 1011, 1013 (1st Dep't 2017) (a plaintiff bears the burden of proving any damages "with a reasonable certainty").

The business was transferred to Asquared in 2014, and then to Stellar 153 in 2016. Plaintiff alleges in the Complaint that Defendants breached their fiduciary duty by transferring the business from the Kyoto Entities to Asquared in 2014. Yet, at the inquest, Plaintiff failed to present any evidence of the value of her 25% interest as of the date of the transfers to Asquared. Instead, Plaintiff presented limited evidence of restaurant sales as of the Fall 2016 sale from Asquared to Stellar 153.

The lower court made no findings of fact as to which transaction gave rise to the alleged breach of fiduciary duty. The lack of findings warrants vacatur and remand for a new trial. Given the testimony and evidence of Defendants' continued receipt of profit distributions in accordance with the original terms of the parties' Shareholder Agreements, and acknowledgement of Plaintiff's continued 25% interest in the business, Plaintiff's decision to seek damages based on the 2016 transfer suggests a waiver on her part of any breach of fiduciary duty based on the 2014 transfer. Such a finding would affect the legal basis for punitive damages. If, however, it is found that the transaction giving rise to the breach of fiduciary duty was the 2014 transfer, then Plaintiff failed to meet her burden of proof with respect to gross sales at the time of that transfer.

Finally, Plaintiff-Respondent fails to address in her Opposition Brief the fact that her compensatory damages award was based, in part, on speculation by Mr. Choi – who during the relevant time was in China – as to the amount of purported cash sales at the business. (R. at 263:22-266:14.) Plaintiff-Respondent fails to address Mr. Choi's testimony that the raw credit card data on which her compensatory award was based necessarily included amounts not actually realized by the business as sales, such as tips, sales tax and credit card processing fees. (R. at 280:17-282:1; R. at 283:4-5; R. at 146.3-146.4; R. at 146.4.) Plaintiff-Respondent failed to present evidence contesting these issues.

Defendant-Appellant produced all financial records relevant to the deduction of these items from gross-sales, (R. at 29; R. at 119.1), and, as discussed above, Mr. Lee continued to treat Plaintiff-Respondent as a 25% owner after the reorganization and continued to pay her share of profits for so long as the business was profitable. The Court, therefore, should not have drawn any inference in favor of Plaintiff-Respondent in connection with the determination of the compensatory award. *See* *Wolf v. Rand*, 258 A.D.2d 401, 402-03 (1st Dep't 1999). Indeed, the lower court itself conceded that "the evidence utilized by the plaintiff to support both credit card sales and cash receipts was less than ideal. . . ." (R. at 29.)

Accordingly, the compensatory damages award should be vacated and remanded for further proceedings.

IV. THE MOTION FOR JUDGMENT ON DEFAULT SHOULD BE VACATED

Plaintiff-Respondent's reliance on CPLR § 5511 is entirely misplaced. "[A]n appeal from . . . a [default] judgment does bring up for review those matters which were the subject of contest before the Supreme Court." *Alam v. Alam*, 2014 NY Slip Op 09088, ¶ 1, 123 A.D.3d 1066, 1067, 1 N.Y.S.3d 227, 228 (2d Dep't 2014). In this case, Mr. Lee appeared by counsel to oppose Plaintiff's motion for judgment on default, (R. at 81-86), and, therefore, the entry of judgment on default is properly before the Appellate Division. *See id*.

As discussed above, Mr. Lee had a meritorious defense that the demand by Plaintiff-Respondent for punitive damages should have been dismissed as a matter of law. *See* *Reinah Dev. Corp. v. Kaaterskill Hotel Corp.*, 59 N.Y.2d 482, 487-88 (1983) (finding plaintiff not entitled to punitive damages as a matter of law); *164 Mulberry St. Corp. v. Columbia Univ.*, 4 A.D.3d 49 (1st Dep't 2004) (reversing denial of motion to dismiss claim for punitive damages as a matter of law).

There is no basis to conclude that Mr. Lee's default was willful. In fact, the record of this case shows that Mr. Lee had in sum or substance conceded that he owed certain monies to Plaintiff-Respondent based on the agreed upon formula contained in the parties' shareholder agreements. Mr. Lee only disputed the Plaintiff-Respondent's calculation of that amount and relied on statements by counsel for Plaintiff-Respondent in seeking to negotiate an out-of-court resolution. *See* *DiIorio v. Antonelli*, 240 A.D.2d 537, 537, 658 N.Y.S.2d 453, 454 (2d Dep't 1997) (oral agreement between counsel may form the basis for reasonable excuse). When Plaintiff-Respondent moved for entry on default, Mr. Lee opposed the motion on the grounds that he had a meritorious defense against the demand for punitive damages. (*See* R. at 82 ¶ 5).

Accordingly, the entry of judgment on default should be vacated. *See* *Liberty Cty. Mut. v. Ave. I Med., P.C.*, 2015 NY Slip Op 04815, ¶ 2, 129 A.D.3d 783, 785, 11 N.Y.S.3d 623, 625 (2d Dep't 2015).

CONCLUSION

For the foregoing reasons, the Court should reverse the lower court's Decision and Order; vacate the punitive damages award; dismiss Plaintiff's claims for punitive damages; remand this action for a new trial solely on compensatory damages; and grant such other and further relief as it deems just and proper.

Dated: July 7, 2021

Respectfully submitted,

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APPELLATE DIVISION – SECOND DEPARTMENT
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