

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

PRESENT: BERNARD J. FRIED Justice

PART 60

FICUS INVESTMENTS, INC. and PRIVATE CAPITAL GROUP, LLC, Plaintiffs,

INDEX NO. 600926/2007

MOTION DATE

- v -

MOTION SEQ. NO. 074

PRIVATE CAPITAL MANAGEMENT, LLC, et al., Defendants.

MOTION CAL. NO.

The following papers, numbered 1 to were read on this motion to/for

PAPERS NUMBERED

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...

Answering Affidavits — Exhibits

Replying Affidavits

Cross-Motion: Yes No

Defendant, Thomas B. Donovan ("Donovan"), brings this motion to reject and modify the Amended Report of Special Referee Marilyn Dershowitz, dated July 7, 2009 (the "Report"); and Plaintiffs, Ficus Investments, Inc. ("Ficus") and Private Capital Group, LLC ("PCG" or the "Company"), cross-move for an order confirming the Report in its entirety. For the reasons set forth below, Defendant's motion is denied and Plaintiffs' motion is granted.

The history of this litigation is, by now, well-known, and requires no recitation here. The present dispute arises out of my Decision and Order dated April 24, 2008, (the "Advances Order") which concluded that Donovan, in accordance with the Operating Agreement, was entitled to advance of litigation expenses by PCG. The Advances Order referred to Special Referee Dershowitz "the factual inquiry as to (a) which of the Expenses apply to Donovan, (b) which Expenses were incurred as a result of Donovan's being 'a Party to a Proceeding because he . . . is a[n] . . . Officer' (Operating Agreement § 3.4. 3), and (c) the reasonableness of such Expenses." (Advances Order at 23.) The Advances Order also established a protocol governing the way in which demands for advances, and objections thereto, were to be made, and referring "each subsequent question of reasonableness" to Special Referee Dershowitz. Id. at 24-25.

1

The "Private Capital Group LLC Limited Liability Company Operating Agreement," a copy of which is annexed to the August 14, 2009 Affirmation of Craig Carpenito, as Exhibit A.

2

The Advances Order was affirmed by the Appellate Division, First Department in January 2009. See Ficus Investments, Inc. v. Private Capital Management, LLC, 61 A.D.3d 1, 10 (1st Dep't 2009).

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

In order to report on whether the expenses Donovan sought to have advanced were, indeed, subject to advancement, the Special Referee conducted an evidentiary hearing over 3 days, in March and April 2009. At the conclusion of the hearing, she reported that Donovan was entitled to recover, as "reasonable" and warranted, only \$1,852,594.62 out of the \$4,241,373.99 in expenses he sought. (Report at 8.) Her conclusion that over \$2 million of expenses were not reasonable or warranted was based, in part, on what she determined to be the credible testimony of John Silas Hopkins III, whom she qualified as an expert, and who recommended that about \$2 million in fees be deducted because they were generated in connection with work that was outside the scope of the Operating Agreement. Specifically, Special Referee Dershowitz concluded that Donovan was not entitled to recover fees for work that was necessitated by actions he took on his own behalf, rather than in his capacity as an Officer of the Company. Such actions include the conduct that gave rise to the hearings, also before Special Referee Dershowitz, relating to Donovan's access of former co-defendant Lawrence Cline's email account, and to Donovan's removal of certain books and records from the Company premises (respectively, the "Email Hacking Hearing" and the "Books and Records Hearing").

Donovan asserts that the Operating Agreement provides for advance of any and all expenses incurred because he is "a Party to a Proceeding because he . . . is a[n] . . . Officer." He contends that he is a defendant (a Party) in this action (a Proceeding) by virtue of his status as a (now former) Officer of PCG, and thus, any reasonable expenses incurred in furtherance of his defense are subject to advancement under the Operating Agreement. He argues that his right to advancement is not subject to a determination that the conduct giving rise to the expenses was conduct performed as an Officer of, or on behalf of, PCG. He therefore argues that Special Referee Dershowitz's conclusion that he is not entitled to certain expenses, including those incurred in connection with the Email Hacking Hearing and the Books and Records Hearing, is erroneous as a matter of law and unsupported by the record.

I disagree.

Donovan was brought into this lawsuit by virtue of his conduct as an Officer of PCG, and the Operating Agreement therefore requires PCG to "advance funds to pay for or reimburse the reasonable Expenses incurred" herein. (Operating Agreement § 3.4.3.) There is no dispute that if Donovan were made a party to this action on the basis of conduct other than that which he engaged in as an Officer of PCG, he would not be entitled to advancement or indemnification under the Operating Agreement. Likewise, Donovan cannot expect to be advanced funds to cover the expenses incurred in connection with defending against allegations of misconduct that commenced after he left PCG. That the misconduct complained of was undertaken in connection with the suit against Donovan the Officer is of no moment: it was Donovan the individual who took the actions, for the benefit of and on behalf of, Donovan the individual. There is no requirement within the Operating

Agreement that PCG advance the litigation expenses of Donovan the individual. The Special Referee's conclusion that the mere fact that certain expenses arose out of the action in which Donovan the Officer was sued "is not necessarily sufficient to mandate that the fees" are advanceable, and her conclusion that fees for hearings on activities undertaken - admittedly - on Donovan's own behalf and not on behalf of the Company are outside the scope of advanceable fees, are thus not erroneous.

Special Referee Dershowitz was tasked with making factual findings as to which of the expenses incurred by Donovan were incurred as a result of his having been made a Party to a Proceeding because he was an Officer of PCG, and as to which of those expenses were reasonable. The "Expenses" contemplated by the Operating Agreement include "all reasonable counsel fees, retainers, court costs, transcript costs, . . . and all other disbursements or expenses of the types customarily incurred in connection with prosecuting, defending, preparing to prosecute or defend, investigating, being or preparing to be a witness in, or otherwise participating in, a Proceeding, including any appeals." (*Id.* § 3.4.1(d).) Special Referee Dershowitz conducted a hearing, heard the testimony of witnesses, reviewed the records, and reached the conclusion that Donovan was entitled to only \$1,852,594.62 of the \$4,241,373.99 he sought. This conclusion appears to me to be amply supported by the record, and her Amended Report dated July 7, 2009 is therefore confirmed. *Baker v. Kohler*, 28 A.D.3d 375, 375-76 (1st Dep't 2006).

Accordingly, it is

ORDERED that the motion of Defendant, Thomas B. Donovan, pursuant to CPLR § 4403, to reject and modify the Amended Report of Special Referee Marilyn Dershowitz dated July 7, 2009, is DENIED; and it is further

ORDERED that Plaintiffs' cross-motion, pursuant to CPLR § 4403, to confirm the July 7, 2009 Report in its entirety is GRANTED; and it is further

ORDERED that, in accordance with the recommendations of Special Referee Dershowitz, the amount of \$2,388,779.37 is to be deducted from the \$4,241,373.99 demanded as advancements by Schlam Stone & Dolan LLP, counsel to Defendant, and it is further

ORDERED that Schlam Stone & Dolan LLP is entitled to recover as reasonable and warranted expenses the sum of \$1,852,594.62; and it is further

ORDERED that Plaintiffs are hereby directed to advance such sum to Schlam Stone & Dolan LLP by the close of business January 8, 2010.

Dated: \_\_\_\_\_

12/22/09

  
RON. BERNARD J. FRIED  
J.S.C.

Check one:  FINAL DISPOSITION  NON-FINAL DISPOSITION

Check if appropriate:  DO NOT POST  REFERENCE