

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

PRESENT: MARILYN B. DERSHWITZ, sp/rel

PART 80R

Index Number : 600926/2007
FICUS INVESTMENT
vs
PRIVATE CAPITAL MANAGEMENT
Sequence Number : 041
HEAR AND REPORT

INDEX NO. _____
MOTION DATE _____
MOTION SEQ. NO. _____
MOTION CAL. NO. _____

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

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

Answering Affidavits — Exhibits _____

Replying Affidavits _____

PAPERS NUMBERED

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered that this ~~motion~~ matter resolved in
accordance with attached report.

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

FILED
Aug 21 2009
NEW YORK
COUNTY CLERK'S OFFICE

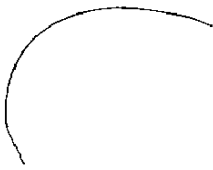
Dated: August 21, 2009

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Check if appropriate: DO NOT POST REFERENCE

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



-----X
FICUS INVESTMENTS, INC. and PRIVATE CAPITAL
GROUP, LLC,

Plaintiffs,

Index No.: 600926/07E
Referee Report

-against-

PRIVATE CAPITAL MANAGEMENT, LLC, THOMAS
B. DONOVAN, et al.,

Defendants.

-----X
MARILYN B. DERSHOWITZ, Spec Ref:

Pursuant to the Orders of Honorable Bernard J. Fried, JSC, dated November 13, 2007 and May 29, 2008, the issue of whether the defendants Thomas Donovan and Christopher Chalavoutis are in contempt of the provisions of Justice Fried's Orders, dated March 26, 2007, April 12, 2007, and May 1, 2007, was referred for hearing and report with recommendations by the undersigned. The hearing on the discrete issue of whether the actions of the defendants with regard to books and records constituted contempt proceeded on November 10, 12-14, 2008, January 5-6, 8-9, 2009, March 16-20, 2009, May 14-15, 27-28, 2009 and June 17, 2009 to completion. The witnesses included Gerard Bambrick, Michael Bode, Christopher Chalavoutis, Lawrence A. Cline, Vincent A. D'Amelio, Pamela Donovan, Thomas B. Donovan, Virginia Donovan, Stuart Donald Ebner, Petrina Gherardi, Alissa Gladstone, Peter Kamran, Craig Kuglar, Tyler Vans Piercy, Peter J. Schancupp, Lawrence Spirio, II and Jefferson R. Voss. The documents marked in evidence accompany this report.

Mr. Donovan is the former Chief Executive Officer of Private Capital Group, LLC

plaintiffs commenced this action against the defendants on claims of, *inter alia*, breach of fiduciary duties. On March 26 and April 12, 2007, Judge Fried granted plaintiffs' applications for two temporary restraining orders prohibiting the defendants from removing, concealing, etc. PCG books and records. Plaintiffs were to be afforded full access to the PCG premises; defendants were to cooperate fully with plaintiffs in the restoration of any previously removed PCG books and records and other information concerning PCG's operations. On May 1, 2007, Judge Fried converted the restraining orders into a preliminary injunction. Plaintiffs Ficus Investments, Inc. ("Ficus") and PCG here argue that the defendants Donovan and Chalavoutis are in contempt of these Orders by, *inter alia*, removing and failing to restore PCG books and records.

During the hearing, there was testimony that Donovan and Cline, PCG's former president and a former defendant in the main action (prior to his settlement with the plaintiffs in July 2007), took approximately \$9.872 million out of PCG's account, and thereafter a meeting was called by Ficus in Florida. Those funds were discussed; Donovan and Cline were informed of Ficus' plan to audit and take control of PCG. The plaintiffs subsequently commenced this action against the defendants. Various Ficus representatives and PCG officers and employees testified about the events of March 21, 2007, the date the plaintiffs commenced this action. Plainly, the defendants Donovan and Chalavoutis, with the assistance of several PCG officers and employees, removed books, records and assets from 2 Jericho Plaza and then concealed them from the plaintiffs.

The testimony of Voss and Piercy, Ficus representatives, Bambrick, PCG's former general counsel, and Cline established that on March 20, 2007 a meeting called by the plaintiffs was held in Florida and was attended by Donovan, Bambrick, Cline, Voss, Piercy and Tom

was held in Florida and was attended by Donovan, Bambrick, Cline, Voss, Piercy and Tom Youth, another Ficus representative. (11/14/08 Tr at 682:4-16 [Voss]; 1/5/09 Tr at 1054:18-1055:7 [Piercy]; 1/5/09 Tr at 936:12-20 [Bambrick]; 1/6/09 Tr at 1304:21-1305:10 [Cline]). During the contentious meeting, Donovan and Cline refused to return the money, and they informed Ficus that they would not allow an audit to be conducted. (11/14/08 Tr at 683:21-684:4 [Voss]; 1/5/09 Tr 1057:11-15 [Piercy]; 1/6/09 Tr 1306:10-15, 1307:9-14 [Cline]). Despite agreeing to continue the meeting the following morning, Donovan, Cline and Bambrick chartered a plane that night back to New York and arrived at 2 Jericho Plaza at around 7:30 in the morning. (11/14/08 Tr at 684:9-685:3 [Voss]; 1/6/09 Tr 1306:12-20, 1309:25-1310:5, 1310:2-3, 1310:18-24 [Cline]; 1/5/09 Tr 937:11-12 [Bambrick]).

The testimony of Cline and Chalavoutis establishes unequivocally that Donovan and Cline held a meeting with the employees present at 2 Jericho Plaza that morning, informed them of Ficus' intention to enter the premises to conduct an audit and explained that they were not going to let that happen. (1/6/09 Tr at 1308:18-1309:2, 1312:6-11 [Cline]; 5/15/09 Tr at 3009:13-24 [Chalavoutis]). Donovan also gave the employees instructions designed to frustrate Ficus' ability to conduct an audit and to prevent it from learning about multiple entities connected to PCG and their respective books and records. (5/27/09 Tr at 3342:7-21 [Cline]).

Donovan then gave specific instructions to Gladstone, PCG's former bookkeeper, to initiate a series of transfers of approximately \$14 million out of PCG accounts and into a related company's account and to move financial records stored in her office along with bank records stored in white binders to 143/135 Main Street. (1/6/09 Tr at 1315:22-1316:10, 1314:15-16 [Cline]; 3/19/09 Tr at 2513:17-21 [Gladstone]; 11/13/08 Tr at 486:10-487:3 [Schancupp]).

Gladstone's testimony established that both Donovan and Chalavoutis were aware that she had moved the white binders to 143/135 Main Street and that Donovan was aware that she had concealed them there. (3/19/09 Tr at 2508:25-2509:5, 2509:16-18 [Gladstone]).

The testimony of Cline, Pamela Donovan, Gladstone, Chalavoutis, Bambrick, Ebner, a representative of ProActive, PCG's IT vendor, and Schancupp, PCG's former associate general counsel, established that Donovan then gave specific instructions to certain PCG employees about the removal of certain PCG property, such as computers, computer server back-up tapes, corporate kits, personnel and accounts payable files and electronic files from 2 Jericho Plaza. (1/6/09 Tr at 1314:12-15, 1315:7-12, 1341:20-1342:6, 1339:14-1340:2, 1318:12-20, 1342:20-23, 1327:8-1329:8, 1329:14-20, 1330:2-8, 1333:20-1334:13, 1330:2-24, 1334:26-1335:13, 1340:9-23, 1319:2-11, 1320:5-18, 1321:9-14, 1322:13-1324:25, 1324:16-24, 1324:16-1325:5, 1342:20-23 [Cline]; 5/28/09 Tr at 3431:10-22, 3441:22-25 [P. Donovan]; 3/18/09 Tr at 2330:5-20 [Gladstone]; 5/15/09 Tr at 3060:14-17 [Chalavoutis]; 1/5/09 Tr at 940:20-23 [Bambrick]; 1/9/09 Tr at 1814:3-1815:22, 1816:21-1817:11, 1817:20-25 [Ebner]; 11/13/08 Tr at 481:17-21, 483:15-484:6 [Schancupp]; Pl's Exh 28).

The testimony of Voss and Piercy established that when Piercy and other Ficus representatives arrived at 2 Jericho Plaza to conduct the audit on March 21, they found the front doors of the building locked, and when they entered the building through another open door, Donovan and Cline refused them access to PCG books and records. (11/14/08 Tr at 685:24-686:19 [Voss]; 1/5/09 Tr at 1057:16-1058:9, 1058:10-21, 1058:21-23, 1058:21-1059:12 [Piercy]).

Cline and Gladstone's testimony established that Gladstone and another employee had

maintained the accounts payable records at 2 Jericho Plaza, (1/6/09 Tr at 1319:2-8, 1320:8-18, 1356:24-1358:3, 1353:17-1354:16, 1356:24-1357:8, 1357:6-1358:7, 1353:6-24 [Cline]; 3/18/09 Tr at 2264:12-2269:10, 2272:26-2274:13 [Gladstone]). The testimony of Cline, D'Amelio, a representative of Navigant, PCG's litigation support services provider and Kuglar, a representative of plaintiffs' counsel, established that on March 21 the defendants removed accounts payable files from 2 Jericho Plaza. (1/6/09 Tr at 1354:17-1355:3 [Cline]; 11/10/08 Tr at 127:6-24, 184:6-186:10 [D'Amelio]; 6/17/09 Tr at 3799:6-3801:26 [Kuglar]).

The defendants also removed human resources and personnel files, including health insurance and tax forms, from 2 Jericho Plaza. (1/6/09 Tr at 1321:5-18, 1360:16-25, 1361:14-21 [Cline]; 11/10/08 Tr at 130:14-131:12, 11/12/08 Tr at 281:21-282:2 [D'Amelio]). There was also testimony that established that later requests made by Navigant for the various accounts payable and human resources files were unsatisfied by the defendants. (5/14/09 Tr at 2918:3-16, 2921:24-2923:22, 2925:26-2926:7, 2915:14-2916:11, 2917:8-12, 2918:3-2919:5 [Chalavoutis]; 11/10/08 Tr at 100:14-25, 104:12-24, 109:7-10, 110:10-13, 112:16-18, 118:19-21; 121:15-18, 122:14-20, 123:14-22, 127:18-24, 130:14-131:12, 11/12/08 Tr at 312:21-313:4 [D'Amelio]; Pl's Exhs 2A-2G, 4). Schancupp's testimony established that PCG encountered problems as a result of the removal of the human resources and personnel files. (11/13/08 Tr at 497:6-498:6 [Schancupp]).

Cline's testimony established that he and a paralegal had maintained records of mortgage files related to several PCG-related properties in binders at 2 Jericho Plaza, that Cline had given some of the binders to Nitkewicz, defendants' counsel, and Chalavoutis for safekeeping and that they had not been returned to the plaintiffs. (1/6/09 Tr at 1351:13-1352:12, 1352:26-1353:4 [Cline]). His testimony also established that on or about April 10, 2007 when Nitkewicz,

Donovan and Cline found mortgage files concerning PCG-related properties among boxes in the paralegal's office, Donovan gave the files to Nitkewicz and they were divided up in the 2 Jericho Plaza parking lot. (1/6/09 Tr at 1355:7-1356:17, 1365:25-1366:4 [Cline]; Pl's Exh 5).

Cline and Schancupp's testimony established that they saw binders containing insurance policies related to several PCG-related properties at 143 Main Street after March 21. (1/6/09 Tr at 1358:15-25, 1359:7-16 [Cline]; 11/13/09 Tr at 516:24-517:21 [Schancupp]). Kamran testified that the binders had been brought to 2 Jericho Plaza in early 2007 and that he had seen them there in March or April of 2007, although he could not be specific about the dates. (3/20/09 Tr at 2768:15-2771:6 [Kamran]).

The testimony of Gladstone, Chalavoutis, Piercy, Schancupp and Kamran, a former employee of PCG, established that on April 10, 2007, Donovan and Cline organized a mass resignation of PCG officers and employees along with a series of large payments that were made to certain of those employees to secure their cooperation in leaving PCG. (3/19/09 Tr at 2366:10-13, 2687:25-2688:2, 2696:6-11 [Gladstone]; 5/14/09 Tr at 2933:19-22, 2937:16-24, 2937:16-2938:13 [Chalavoutis]; 1/6/09 Tr at 1131:3-13, 1137:2-5 [Piercy]; 11/13/08 Tr at 460:25-461:26 [Schancupp]; 5/15/09 Tr at 3154:8-20 [Kamran]; Pl's Exhs 53A, 77, 94A). Pamela Donovan's testimony established that the payments, including a later one made to her, came from PCG funds. (5/28/09 Tr at 3466:14-3468:9, 3453:3-5 [P. Donovan]; Pl's Exhs 76, 77).

I find the testimony presented by the plaintiffs to be totally credible.

In response to the plaintiffs' claims pertaining to the removal of PCG's books and records, the defendants' testimony primarily centered on their position that any PCG books and records that they removed from 2 Jericho Plaza were removed prior to March 26, 2007, the date

of Judge Fried's first temporary restraining Order, and thus they were not within the scope of the Orders. (Def's Findings of Fact ¶¶ 58-65). However, even if true it is irrelevant, since Judge Fried's Orders not only prohibited the defendants from any removal of PCG books and records going forward, but also required the return of any items that had previously been removed. Therefore, by the defendants' own admissions, any PCG books and records that they removed from 2 Jericho Plaza would in fact fall squarely within the scope of Judge Fried's Orders.

The defendants urge further that the removal of any books and records from 2 Jericho Plaza was not within the scope of Judge Fried's Orders because the books and records they removed belonged to companies separate and independent of PCG. (5/28/09 Tr at 3525:23-25 [T. Donovan]; 5/14/09 Tr at 2874:4-17, 2876:3-4, 2879:6-9, 2886:11-16 [Chalavoutis]). However, the plaintiffs presented significant testimony by Cline, Voss, Piercy, Bambrick and Schancupp and documentary evidence to the contrary. (Pl's Findings of Fact ¶¶ 43-158). In any event, the companies whose books and records were removed were listed as joint ventures by defendants on the books of PCG. (Pl's Exh 5).

The defendants' remaining testimony in response to the plaintiffs' specific claims of the removal of PCG books, records and assets from 2 Jericho Plaza was, at best, wanting given that their defenses were clearly contradicted by the testimony elicited by the witnesses. For instance, regarding the plaintiffs' allegations of the removal of accounts payable and human resources/personnel records, Mr. Chalavoutis, in an earlier court document in this action, represented that it was not PCG's practice to maintain these types of files, and thus they were never located at 2 Jericho Plaza. (5/14/09 Tr at 2911:26-2916:16, 2913:7-10, 2920:9-15 [Chalavoutis]). However, during the hearing, Cline, Gladstone and even Chalavoutis' own

testimony established that PCG maintained these types of records. (1/6/09 Tr at 1354:17-1355:3, 1360:16-17, 1360:23-24, 1360:26-1361:4, 1361:14-21 [Cline]; 3/18/09 Tr at 2264:12-2269:10, 2272:26-2274:13 [Gladstone]; 5/14/09 Tr at 2848:9-12, 2919:10-13, 2922:6-20, 2925:18-2926:3 [Chalavoutis]; Pl's Exh 20).

A finding of civil contempt requires that "a lawful judicial order expressing an unequivocal mandate must have been in effect and disobeyed," the defendants "must have had actual knowledge of the order" and "prejudice to the rights of a party to the litigation must be demonstrated." (*McCain v Dinkins*, 84 NY2d 216, 226 [1994]; *see also* Judiciary Law § 753[A]). The moving party bears the burden of establishing the contempt by "clear and convincing evidence." (*Yalkowsky v Yalkowsky*, 93 AD2d 834, 835 [2d Dep't 1983]).

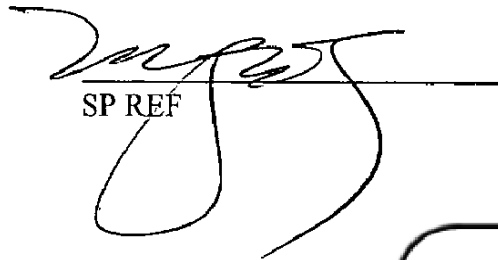
On January 20, 2009, the First Department dismissed the defendants' appeal of the May 1, 2007 preliminary injunction and stated that were it to review the appeal on the merits, it "would find the order clear and unambiguous." (*Ficus Inv., Inc. v Private Capital Mgmt. LLC*, 61 AD3d 1, 12 [1st Dep't 2009]). Plainly, an unequivocal judicial mandate was clearly in effect; defendants do not deny knowledge of the mandate. By the testimony and documentary proof presented, the plaintiffs have established by clear and convincing evidence that those Orders were violated by the defendants. The plaintiffs have further established that their rights have been prejudiced by Chalavoutis' and Donovan's failure to comply with the Orders, at a minimum, by the hindering of the prosecution of the main action and by necessitating this motion for contempt.

Accordingly, I report that the plaintiffs have established that the defendants deliberately violated Judge Fried's Orders, and that they be held in contempt with appropriate sanctions including costs engendered by their actions. Civil contempt lies where the rights of a party have

been harmed by a contemnor's failure to obey a court order as was demonstrated by the hearing herein. The "penalty imposed is designed not to punish but, rather, to compensate the injured party or to coerce compliance with the court's mandate or both." *Matter of Dep't of Env'tl. Prot. of City of N.Y. v Dep't of Env'tl. Conservation of State of N.Y.*, 70 NY2d 233, 239 (1987).

I recommend that upon a motion pursuant to CPLR § 4403 that this report be confirmed and that the defendants Chalavoutis and Donovan be held in contempt and required to pay all plaintiffs' attorney's fees associated with the motion for contempt and this prolonged hearing.

Dated: August 20, 2009


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