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

In the Matter of the Application of	:	
LAWRENCE A. CLINE, as a Member of Private Capital Management, LLC, and PCM INTEREST HOLDING, LLC as a Beneficial Holder of Part of the Economic Interest in Private Capital Management, LLC,	:	
Petitioners,	:	Index No. 650117/2009
for an order and judgment dissolving the limited liability company, Private Capital Management, LLC, pursuant to New York Limited Liability Company Law Section 702,	:	Hon. Bernard J. Fried
-against-	:	
THOMAS B. DONOVAN,	:	
Respondent.	:	

MEMORANDUM IN OPPOSITION TO RESPONDENT'S MOTION TO DISMISS VERIFIED PETITION

ALSTON & BIRD LLP

John F. Cambria
Craig Carpenito
Jill C. Barnhart
90 Park Avenue
New York, New York 10016
(212) 210-9469

Attorneys for Petitioner PCMIH, LLC

GREENBERG FREEMAN LLP

Sanford H. Greenberg
110 East 59th Street
29th Floor
New York, New York 10022

Attorneys for Petitioner Lawrence A. Cline

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases **Page(s)**

Rules and Statutes

Rules and Statutes **Page(s)**

Petitioners Lawrence A. Cline ("Cline"), as a Member of Private Capital Management, LLC ("PCM"), and PCM Interest Holding, LLC ("PCMIH"), as a beneficial holder of Cline's economic interest in PCM (collectively, "Petitioners"), respectfully submit this Memorandum of Law in opposition to Respondent Thomas B. Donovan's ("Donovan") Motion to Dismiss Petitioners' Verified Petition (the "Petition") for the judicial dissolution of PCM.

PRELIMINARY STATEMENT

On March 9, 2009, Cline and PCMHI, together the 50% Member and economic interest-holder in PCM, filed a thirty-one paragraph Petition for the dissolution of PCM which detailed the formation of PCM and the hopeless decomposition of the entity and the relationship of its two equal members – Thomas Donovan and Lawrence Cline. As set forth in the factual allegations of the Petition, as a result of the hopelessly deadlocked relationship between Cline and Donovan, PCM can no longer carry out any viable function other than that of Donovan's pawn. Indeed, Donovan continues to use PCM to further his litigation tactics in ongoing actions, including through foisting unconscionable legal fees and expenses of "PCM" upon Private Capital Group, LLC (the "Company") and the taking of legal positions contrary to Cline's interests at every turn in those matters.

In the face of these undeniable facts, Donovan is forced to make the argument, without any valid legal support, that the Petition does not establish a legal basis for dissolution because PCM could possibly still serve some function. Yet Donovan can provide no actual legal support for this proposition -- instead, Donovan is trying to play judge and force his own interpretation of the dissolution laws upon this Court. It is clear

that Donovan has decided that because PCM serves his own purposes, it should continue its otherwise useless and irrational existence. Donovan is attempting to create the illusion of a legal insufficiency where there is plainly not one – all in service of Donovan's goal to force Cline and its economic interest-holder, PCMHI, to suffer through Donovan's tyrannical control of PCM. Respectfully, Donovan's motion falls well short of establishing his high burden in seeking to dismiss this Petition, and the Court should deny his motion.

FACTUAL ALLEGATIONS

As this Court is all too aware, Donovan and Cline formed PCM, a New York Limited Liability Company ("LLC") on November 16, 2005 for the sole purpose of holding their 20% minority interest in Private Capital Group, LLC (the "Company"). Petition at ¶¶ 7 and 8. Donovan and Cline are the sole, equal owners of PCM and its only managing members. Petition at ¶¶ 5 and 6. PCM did not observe any corporate formalities and was dominated by its members – Donovan and Cline. Petition at ¶ 12. Other than the foregoing, PCM never had any other purpose or business of its own. Petition at ¶ 10. As such, PCM is simply an alter ego of Donovan and Cline. Petition at ¶ 11. That was, until, the Plaintiffs commenced the main action, *Ficus Investments, Inc., et ano. v. Private Capital Management, LLC, et al.*, 600926/2007 (the "Main Action"), against PCM, Donovan, and Cline.

In July 2007, Cline reached a comprehensive settlement with the Plaintiffs in the Main Action. Petition at ¶ 14. As clearly alleged in the Petition, since that time Donovan and Cline have been locked in "an ever-expanding array of litigations." Petition at ¶ 15. Most of these lawsuits – which include the Main Action and at least 7 additional actions –

are currently pending before Your Honor. It is clear that, given the fact that over a year has passed and the hostility between Donovan and Cline has gotten progressively worse, the parties do not speak and there is no possibility of reconciliation. Petition at ¶ 19. As a result of the aforementioned lawsuits and the resulting adverse interests of PCM's two equal "partners," PCM is hopelessly deadlocked and unable to function in its sole purpose – holding the joint interest of Donovan and Cline. Petition at ¶¶ 18 and 20. The dispute between Donovan and Cline, coupled with Your Honor's May 30, 2007 Preliminary Injunction granting Ficus Investments, Inc. control over the day-to-day operations of the Company, have rendered any "managerial" or "business function" allegedly carried out by PCM as moot. Petition at ¶ 27. Indeed, as Donovan has unilaterally taken control of PCM to the exclusion of Cline, PCM has become nothing more than a vehicle for Donovan to further his interest in this litigation to the detriment of his "partner," Cline. Petition at ¶ 21.

ARGUMENT

I. RESPONDENT'S MOTION MUST BE DENIED IF THE ALLEGATIONS OF THE PETITION ESTABLISH A PRIMA FACIE RIGHT TO JUDICIAL DISSOLUTION

Donovan makes his motion to dismiss pursuant to CPLR 404, based on Petitioners' alleged failure to state a cause of action upon which relief may be granted. Upon such a motion attacking the legal sufficiency of the Petition, it is well established that all allegations in the Petition must be taken as true and that the motion to dismiss must be denied if those allegations, given all favorable inferences, establish a prima facie right to relief. *See, e.g., Matter of Nistal v. Hausauer*, 308 N.Y. 146, 149 (1954); *Ahl v. City of Albany*, 118 A.D. 2d 1009, 1011, 500 N.Y.S.2d 376, 377 (3rd Dep't 1986) (stating

that petitioners were "[given]...the benefit of all favorable inferences available from the facts alleged in the petition") (citing *Lack v. Kreiner*, 91 A.D.2d 813, 458 N.Y.S.2d 40 (4th Dep't 1982)) ("On a motion to dismiss pursuant to CPLR 404, the petition is entitled to all favorable inferences and the motion to dismiss must be denied if the petitioner states any facts upon which he is prima facie entitled to relief.").

Donovan challenges the Petition on the basis that the facts alleged state no legal basis for dissolution of PCM and furthermore on the basis that PCMIH, as the holder of Cline's economic interest in PCM, has no standing to join Cline in making the Petition. As to the first claim, as will be shown below, under New York law, judicial dissolution of a limited liability company (an "LLC") is entirely proper when the members of the LLC are at an utter stalemate which makes the continuing function of the LLC impracticable, as the facts in the Petition clearly allege. The allegations contained in the Petition clearly set out that the deadlock between Cline and Donovan, two equal members of PCM engaged in a bitterly hostile, intractable, and litigious battle with one another, has significant impact on any valid management or function of PCM in the future. And as to Donovan's second claim, as will also be discussed below, under New York law Cline had full authority to assign his economic interest in PCM to PCMHI. PCMHI's joining with Cline on the Petition simply serves the purpose of uniting the associated membership and economic interests so that the Petition may be backed by the entirety of the 50% interest in PCM. Donovan has provided no basis for his claim that New York law bars Petitioners from proceeding in this manner. Finally, this standing argument is highly ironic since it was Donovan's confidante and shadow counsel Mr. Nitkewitz who initially opposed addressing this application by a cross-motion and insisted upon a plenary action.

II. NEW YORK LAW RECOGNIZES DEADLOCK BETWEEN MEMBERS AS A BASIS FOR DISSOLUTION OF AN LLC

New York law establishes that the stalemate or deadlock of the members of an LLC may serve as the basis for judicial dissolution of the LLC. Section 702 of New York's Limited Liability Law provides simply that judicial dissolution is proper "whenever it is not reasonably practicable to carry [on] the LLC's business in conformity with the articles of organization or operating agreement[1]." Owing to the fairly recent creation of New York's Limited Liability Law, case law on Section 702 is not extensive. However, as Donovan notes, in *Schindler v. Niche Holdings*, the New York County Supreme Court stated that it construed Section 702 to allow for judicial dissolution "only where the complaining member can show that the business sought to be dissolved is unable to function as intended, or else that it is failing financially." 1 Misc. 3d 713, 716, 772 N.Y.S.2d 781, 785 (Sup. Ct, N.Y. County 2003), *abrogated on other grounds in Tzolis v. Wolf,* 10 N.Y.3d 100, 855 N.Y.S.2d 6 (2008). However, Donovan conveniently ignored the very next sentence in the *Schindler* opinion, in which the court stated that it could not order judicial dissolution where the petitioning member had "failed to allege that [the LLC] [was] unable to carry on its business in accordance with its articles of organization or operating agreement, or that there is any internal "deadlock" impeding [the LLC's] smooth operation." *Id.* Plainly, the *Schindler* court recognized that such

[1] Although it is not clear from the statute, a New York court has held that on an application for judicial dissolution of an LLC for which there is no formal operating agreement of the entity – as is the case here – the court must consider whether it is not reasonably practicable to carry on the business in conformity with the terms of statutorily default provisions of New York Limited Liability Company Act. *See Spires v. Casterline*, 4 Misc. 3d 428, 436, 778 N.Y.S.2d 259, 265 (Sup. Ct. Monroe County 2004). The default provisions make clear that in the absence of an operating agreement, each member may be considered a manager. NY LLCL §§ 401 (a)-(b).

"internal deadlock" and an associated disruption to the "smooth operation" of an LLC could serve as the basis for judicial dissolution.

Donovan is well-aware that he cannot argue that the Petition does not set out ample basis for a finding of deadlock between the members of PCM. Indeed, Donovan knows that any attempt to deny the existence of such deadlock would be laughable, given the fact that he has actually sued Cline, directly or indirectly, in a total of eight separate actions. Donovan's only basis for argument is the assertion that the Petition does not state a cause of action because PCM was formed for the purpose of holding Donovan and Cline's joint interest in the Company and that "nothing alleged in the Verified Petition indicates that the deadlock or enmity between Donovan and Cline prevents PCM from continuing to serve as a passive investor in PCG(FL)." (March 27, 2009 Affirmation of David Katz ("Katz Aff.") at ¶ 12). Donovan is misreading Section 702 of New York's Limited Liability Law to allow for judicial dissolution only if it is completely impossible for an LLC to continue to function – even if such "functioning" is wholly inefficient and irrational – rather than "not reasonably practicable" for the LLC to operate, as is explicitly stated by the statute. Donovan cites no law in support of his interpretation of Section 702. Furthermore, he ignores the fact that the Petition does not simply state that Cline and Donovan are deadlocked, but rather provides ample allegations setting out how and why such deadlock makes the continued existence of PCM impracticable.

The Petition sets forth that Donovan and Cline formed PCM for the purpose of holding their joint 20% interest in the Company[2], but that such a joint arrangement and mingling of interests is no longer useful, practical, or in fact viable specifically because

[2] Of course, because its two sole members were the CEO and President of the Company, PCM also indirectly served the active purpose of carrying out the management of the Company; indeed, Donovan and Cline's executive positions make clear that PCM was/is the antithesis of a "passive" investor.

Donovan's and Cline's interests are irreversibly adverse. Petition at ¶ 11. The Petition furthermore makes clear that because of this enmity between Donovan and Cline, the two members of PCM will never again function together as a unit vis-à-vis the Company – the very purpose of PCM. Petition at ¶ 20. As also set forth in the Petition, PCM was created for the purpose of forming a business relationship and operation with Ficus and Ficus alone – the same Ficus in which Donovan in now involved in a litigation battle of seemingly endless bounds. Petition at ¶¶ 9-10. This Court is well aware, and the Petition furthermore makes clear, that there will never be a reconciliation of the Ficus-PCM relationship. PCM's continued operation is thus not only impracticable, it is irrational – the enmity between Cline and Donovan, and between Donovan/PCM and Ficus makes the continued bundling of Donovan's and Cline's interests in PCM entirely purposeless. It is plain that the only "viable" use of PCM is instead as Donovan's vehicle for litigation gamesmanship and to try to get Mr. Nitkewicz, "PCM's" counsel, paid with Company funds. The reality is that PCM is now being used for an entirely different purpose than intended.

Indeed, the impact of the deadlock on the continued operation of PCM is made abundantly clear in the Petition through the allegations that Donovan has now seized control of PCM and is directing its actions and strategy in this litigation – and perhaps elsewhere - specifically against the wishes of its 50% member Cline. Petition at ¶ 17. Under New York Limited Liability Company Law, which states that "Except as provided in the operating agreement...the managers shall manage the limited liability company by the affirmative vote of a majority of the managers," Donovan simply cannot unilaterally

direct the actions of PCM. (NY LLCL § 408(b) (McKinney 2007)).[3] It could not be any clearer. Donovan's sole direction of PCM, and the resulting negative impact on Cline's interests, is a dramatic example set out by the Petition of the impact of deadlock upon the "smooth operations" of PCM. The fact that Donovan has decided to simply ignore the stalemate and arrogate to himself the management of PCM cannot change the fact that valid management of PCM is impossible now and forever.[4] The Petition demonstrates that management of PCM is undeniably at an impasse, and the default provisions of the governing New York LLC law are such that this impasse cannot be resolved absent dissolution. Moreover, not only is Donovan's current use of PCM causing the entity to function with an entirely unlawful purpose, the consequences of "PCM"s" actions are to the detriment and potential liability of its 50% owner Cline; plainly, such consequences cannot be in line with the intended function of PCM.

Finally, the Petition sets out that in connection with Cline's settlement with the Company – the very reason for the hostile relationship between Donovan and Cline – Cline conveyed his economic interest in PCM to PCMIH, an entity wholly owned by Ficus. Petition at ¶ 14. While PCM was formed for the purpose of holding two co-executive officers' interest in the Company, this joint interest is in fact now beneficially held by Ficus and Donovan, two parties engaged in a heated litigation. The

[3] Donovan and Cline are each designated managing members because under New York Limited Liability Company Law, "[u]nless the articles of organization provides for management of the limited liability company by a manager or managers or a class or classes of managers, management of the limited liability company shall be vested in its members who shall manage the limited liability company…". (NY LLCL § 401(a) (McKinney 2007)). Furthermore, "any such member exercising such management powers or responsibilities shall be deemed to be a manager for purposes of applying the provisions of this chapter." (NYLLCL § 401(b) (McKinney 2007)).

[4] The Court should recall that on the earlier cross-motion, Donovan had the chutzpah to contend that PCM's only office was at his offices in Suffolk County where he runs his latest alphabet soup group of entities which, as has been vividly demonstrated in both pending contempt and partial summary judgments motions in the Main Action, were financed with stolen funds from the Company and proceeds of the now infamous "North Fork Mortgages."

impracticability of such an arrangement is made all the more obvious because this joint economic interest in the Company – the reason for the existence of PCM - can easily be severed and conveyed to the individual interest holders with no actual impact on the members' interests. Based on all of the foregoing, the Petition amply sets out how the existence of the hostile odds between Donovan and Cline create an environment in which PCM cannot function as was intended; that is, as an arrangement between Cline and Donovan to hold their interests in a Company in which they were jointly and actively involved.

III. DONOVAN HAS NOT AND CANNOT ESTABLISH THAT "AS A MATTER OF LAW," THE DEADLOCK BETWEEN ITS MEMBERS DOES NOT RENDER PCM'S CONTINUED OPERATION IMPRACTICABLE

Faced with multiple allegations setting out the effects of deadlock on PCM's operations, Donovan is forced to argue that Petitioners cannot make a case for dissolution because "as a matter of law" the deadlock between Cline and Donovan cannot possibly establish that it is "not reasonably practicable" to continue the operations of PCM. Donovan, not surprisingly, fails to cite even a single New York case in favor of this proposition. Instead, Donovan stretches to cite a single Delaware case which in no way supports this proposition and which has no precedential value nor binding effect on this Court. Donovan argues that *Seneca Investments, LLC v. Tierney*, No. Civ. A. 3624-CC, 2008 WL 5704773 (Del. Ch. Sept. 23, 2008) is "on all fours" with the facts of the Petition. This is categorically false. The Chancery Court explicitly states that the petition for dissolution was made on the sole basis that the LLC had "abandoned its business and should therefore be dissolved" rather than deadlock. *Id.* at *2. However, the Chancery Court did in fact note that dissolution had been ordered in previous cases

"where there was 'deadlock' that prevented the corporation from operating," citing one series of cases, "and where the defined purpose of the entity was fulfilled or impossible to carry out," citing a second line of cases. The court then held that "**since there is no allegation in the petition that [the LLC] is mired in a voting deadlock**, the inquiry must focus on whether it is now impracticable for [the LLC] to fulfill its business purpose." *Id.* at *2-3 (emphasis added). The Chancery Court found that since the only alleged purpose of the LLC was to "engage in any lawful act or activity for which corporations may be organized under the Delaware General Corporations Law," and the LLC's present function was "as a passive instrumentality that is holding title to assets, a corporate function that is lawful and common," the LLC should not be dissolved. In other words, the Chancery Court found that the only argument made in support of dissolution was that the LLC was functioning as a passive instrumentality, and this argument alone was not enough to result in judicial dissolution. The *Seneca* Court's inquiry involved no consideration whatsoever of the impact of stalemate or deadlock between LLC members upon the LLC's operations, because none was alleged. Plainly this case in no way supports Donovan's contention that "as a matter of law" Petitioners cannot argue that deadlock between Cline and Donovan makes the operation of PCM impracticable. Donovan's reading of this case is about as far-fetched as his absurd interpretations of this Court's orders in the Main Action – which have resulted in two of his cronies already being held in contempt; an ongoing hearing before Referee Dershowitz in which it has been admitted that Donovan orchestrated the removal of books and records pertaining to the Company's business; and the now-scheduled hearing on a third motion for contempt for outright violation of the Escrow Order.

Donovan also cites a portion of *Seneca* in which the Chancery Court states that the LLC's holding of counterclaims and third-party claims was an "acceptable, and common, corporate function," apparently in the service of a half-hearted argument that PCM cannot be dissolved in the face of its counterclaims.[5] *Id.* at *5. It is obvious why Donovan does not dwell long on this argument, as the Chancery Court goes on to state that "the rule [is] that the pursuit of claims by a **non-deadlocked** LLC is sufficient business activity to prevent a court from decreeing dissolution." *Id.* And, moreover, the Chancery Court in fact specifically cites to another case in which the judicial dissolution of a deadlocked LLC owned by two 50-50 members was properly ordered notwithstanding the fact that the LLC was pursuing claims. *Id.*, (citing *In re Silver Leaf, LLC*, No. Civ. A. 20611, 2005 WL 2045641 at *11 (Del. Ch. Aug. 18, 2005)). Furthermore, it should be noted that dissolution will not affect Donovan's right to make claims as a 50% owner of PCM.

Therefore, Donovan has in fact cites no authority for his argument that Petitioners cannot possibly establish through the deadlock between Cline and Donovan, and its consequences, that it is "not reasonably practicable" for PCM to continue in existence.[6]

---

[5] Indeed, Donovan cannot act on any such counterclaim without the express consent of PCM's other 50% member, Cline.

[6] Even Delaware case law goes directly against Donovan's proposition that deadlock in a "functioning" entity cannot lead to dissolution. In interpreting the state's LLC dissolution statute, which echoes New York's, Delaware courts have held that it does the continued operation of the LLC does not have to be impossible or "completely frustrated." *See Fisk Ventures LLC v. Segal*, No. Civ. A. 3017-CC, 2009 WL 73957 at * 3-4 (Del. Ch. Jan. 13, 2009) (holding that "[T]here is no need to show that the purpose of the limited liability company has been 'completely frustrated.' The standard is whether it is reasonably practicable for [an LLC] to continue to operate its business in conformity with its LLC Agreement.") (citing *In re Silver Leaf LLC*, 2005 WL 2045651 at *10). And in *Haley v. Talcott,* the Delaware Chancery Court ordered dissolution of an LLC, owned by two 50% managing members and established for the purpose of holding and managing real estate, based on the deadlock of the members despite the fact that the LLC was still "technically functioning." 864 A.2d 86, 96 (Del. Ch. 2004). The LLC member opposing dissolution insisted that despite any deadlock between the two equal owners, "the LLC [could] and [did] continue to function for its intended purpose and in conformity with the [LLC] agreement," as it was receiving payments from the renter of the real estate property and was writing checks to meet its

Rather, he is simply asserting his own interpretation of the purpose of New York's LLC dissolution law and asking the Court to apply it at this preliminary stage.

IV. DONOVAN HAS NOT ESTABLISHED THAT PCMIH CANNOT JOIN WITH MEMBER CLINE IN BRINGING THE PETITION FOR DISSOLUTION

Donovan also brings his motion to dismiss based on a claim that PCMIH, the assignee of Cline's 50% economic interest in PCM, cannot be a party to this special proceeding. Donovan ignores the fact that, as is clear from the face of the Petition, that PCMIH is not bringing this motion alone. Rather, this motion is obviously brought together with Cline, the holder of the corresponding 50% membership interest in PCM. In the abundance of caution, PCMIH joined with Cline in order that the entirety of the 50% membership interest would be in support of this dissolution petition. Cline has every right under the NY LLCL to transfer his economic interest to PCMIH, or any other assignee. The LLCL provisions which Donovan cites state actually specifically allow for the assignment of a member's interest. NY LLCL § 603(a) (McKinney 2007) ("Except as provided in the operating agreement, a membership interest is assignable in whole or in part"). The NY LLCL simply states that the assignee of that interest does not become a member – and indeed, PCMIH does not claim to be a member of PCM. *See* NYLLCL § 603(a)-(c) (McKinney 2007). Donovan, once again, has cited no law which shows that a dissolution petition brought by a member cannot be joined by the holder of

---

obligations under the mortgage. *Id.* The Chancery Court acknowledged this ability of the LLC to function, but still ordered dissolution of the LLC due to strident disagreements between the two members and the resulting inability of one member to validly operate the LLC without approval from the other member. The Chancery Court held that the argument that the LLC could function in line with its intended purpose under the sole control of the member opposed to dissolution could not overcome the need for dissolution in part because allowing sole control would leave the complaining member liable for mortgage debt of an entity over which he had no control. *Id.* at 89. Similarly, allowing PCM to continue in existence under the sole control of Donovan plainly exposes Cline to potential liability for actions taken without his consent or even his knowledge.

that member's economic interest. The single case cited by Donovan – not surprisingly, again a Delaware case – is yet another example of Donovan's tendency to analogize two factual situations which are plainly poles apart. In that case, *R&R Capital, LLC v. Buck & Doe Run Valley Farms, LLC,* the court held that certain LLCs (the "Pandora Entities"), whose members comprised multiple others LLCs, could not be dissolved through the petition of a LLC which was itself a member of one of the LLCs with membership interests in Pandora Entities. No. Civ. A. 3803-CC, 2008 WL 3846318 (Del. Ch. Aug. 19, 2008). It was plainly not the case that, as here, an economic interest holder joined together with the actual member of the LLC to petition for dissolution of that LLC. Despite Donovan's best efforts to distract this Court from the facts actually before it with this inapplicable and non-governing case law, Donovan has entirely failed to provide any basis on which PCMIH must be dismissed from the Petition.

CONCLUSION

For all the foregoing reasons, the Court should deny Donovan's Motion to Dismiss the Verified Petition.

Dated: New York, New York
April 6, 2009

ALSTON & BIRD LLP

By: _____
John F. Cambria
Craig Carpenito
Jill C. Barnhart
90 Park Avenue
New York, New York 10016
(212) 210-9469

Attorneys for Petitioner PCMIH, LLC

GREENBERG FREEMAN LLP

By: _____
Sanford H. Greenberg
110 East 59th Street
29th Floor
New York, New York 10022

Attorneys for Petitioner Lawrence A. Cline