

Shetty v Nastel Tech., Inc.

2007 NY Slip Op 34018(U)

December 12, 2007

Supreme Court, Suffolk County

Docket Number: 0026557/2006

Judge: Elizabeth H. Emerson

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SUPREME COURT - STATE OF NEW YORK
COMMERCIAL DIVISION
TRIAL TERM, PART 44 SUFFOLK COUNTY

PRESENT: Hon. Elizabeth Hazlitt Emerson

KRISH SHETTY, x

Petitioner/Plaintiff,

-against-

NASTEL TECHNOLOGIES, INC., DAVID MAVASHEV,
ALBERT MAVASHEV, DAVID ZATUCHNI,
ZATUCHNI & ASSOCIATES, LLC, ILJETO, LLC,
JITEX, INC., MATRIX CONCEPTS, INC., LUMLA
SOFTWARE, INC., CONTRADO, INC., and STEVEN
DMISZEWICKI,

Respondents/Defendants,

x

MOTION DATE: 11-29-06, 9-14-07
SUBMITTED: 5-23-07, 9-19-07
MOTION NO.: 002 Mot D
003 Mot D

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Upon the following papers numbered 1 to 9 read on this Motion to Dismiss the Complaint; Notice of Motion and supporting papers 1-6; Notice of Cross Motion and supporting papers; Answering Affidavits and supporting papers 7-8; Replying Affidavits and supporting papers 9; and Upon the papers numbered 1 to 27 read on Zatuchni's Motion to Dismiss the Complaint; Notice of Motion and supporting papers 1-15; Notice of Cross Motion and supporting papers; Answering Affidavits and supporting papers 16; Replying Affidavits and supporting papers 17-27 it is,

ORDERED that the motion dated November 16, 2006, by defendants Nastel Technologies Inc., David Mavashev, Albert Mavashev, Steven Dmiszewicki, Iljeto, llc., Matrix Concepts, Inc., Lumla Software, Inc., and Contrado Partners, LLC ("Nastel Defendants") seeking dismissal of the Complaint and the motion to dismiss dated September 14, 2007 by defendants and/or respondents David Zatuchni and Zatuchni and Associates ("Zatuchni Defendants") are decided as follows:

Krish Shetty ("Shetty") brought this proceeding for corporate dissolution of Nastel Technologies, Inc. ("the Company" or "Nastel") pursuant to Section 1104-a of the NYBCL and the

dissolution of a related partnership between Shetty and defendant/respondent David Mavashev (“D. Mavashev”). In addition to the dissolution causes of action, Shetty purports to assert in his complaint derivative claims against defendants D. Mavashev, Albert Mavashev and Steven Dmiszewicki, as well as, both direct and derivative claims for breach of fiduciary duty against these three defendants and a claim for usurpation of a corporate opportunity against D. Mavashev and Albert Mavashev. In addition, Shetty alleges direct and derivative claims of aiding and abetting a breach of fiduciary duty against defendants Zatuchini, Zatuchni & Associates, Iljeto, Jitex, Matrix and Contrado. Shetty also alleges in the complaint breach of contract and breach of the implied duty of good faith and fair dealing by D. Mavashev. Finally, Shetty seeks the appointment of a receiver for Nastel’s assets pursuant to section 1113 of the BCL.

Shetty is a 36.5% shareholder in Nastel, which was incorporated on or about November 9, 1994, under the laws of the State of Delaware. Nastel’s offices are in New York and Nastel conducts all of its business in the State of New York. At the time of incorporation, Shetty owned 40% of the shares and D. Mavashev, the remaining 60%. On or about December 6, 1994, Shetty and D. Mavashev decided to grant Albert Mavashev 5% of the stock by reducing each of their shares by 2.5%. Shortly after incorporation, D. Mavashev and Shetty entered into a contract which purports to set forth certain terms of operating Nastel, including designating New York State as the state having jurisdiction over the agreement. The contract states that it is a partnership agreement made between David Mavashev and Shetty. However, the terms of this contract relate to the ownership and operation of the Company and is in essence a shareholder agreement. The contract further states that prior to the execution of the partnership agreement, Shetty had been developing, under the trade name of Nastel Technologies, prospective clients and agreed to contribute to the Company these existing prospects and contacts. This contract further outlines the contributions each party made to the Company and stated that D. Mavashev was entitled to 60% of equity in the Company and Shetty was entitled to 40% equity in the Company. This contract was signed by both parties on or about December 6, 1994.

The allegations in the Verified Petition and Complaint claim that Shetty was wrongfully removed from his position as CEO. Shetty further alleges that he was forced in 1994, to sell shares at arbitrary and undervalued prices and that D. Mavashev caused substantial sums of money to be distributed to defendants Iljeto, Jitex, Matrix and Albert Mavashev from Nastel without any business purpose. Shetty alleges that Iljeto, Jitex, Matrix are owned and controlled by D. Mavashev. Shetty also alleges that Mavashev caused unreasonable and excessive fees to be paid to defendants Zatuchni and Zatuchni and Associates. Shetty claims that a combination of these allegations constitute conversion and waste of a substantial portion of Nastel’s assets in violation of his rights, and serve to wrongfully oppress him.

Prior to filing this action, Shetty sent a demand letter on or about August 11, 2006, requesting that the board of directors of Nastel investigate his allegations. In response, the board appointed a one-person Special Committee to conduct the investigation. The sole member of this committee was Steven Dmiszewicki, a defendant in this action. Shetty alleges that his demand for board intervention was futile as the majority of the Board of Directors has a hostile interest and/or participated in the alleged wrongdoing.

The Nastel Respondents/Defendants made the within motion to dismiss each of the allegations against them alleging that the complaint fails to state claims upon which relief may be granted, that certain causes of action are barred by the statute of limitations, that Shetty is an improper party to bring a derivative claim on behalf of the other shareholders of Nastel and that the Court lacks subject matter jurisdiction to dissolve Nastel.

The Zatuchni Defendants also allege that Shetty is an improper derivative plaintiff incapable of representing the other shareholders of Nastel, that the complaint fails to state a claim upon which relief may be granted and that the documentary evidence provides the Zatuchni Defendants with a complete defense to Shetty's allegations. The claim against the Zatuchni Defendants consists of one cause of action alleging aiding and abetting a breach of fiduciary duty.

It is well settled under New York law that on a motion to dismiss pursuant to CPLR 3211(a)(7), the Court is to liberally construe the complaint, accept the alleged facts as true, give the plaintiff the benefit of every possible favorable inference, and determine only whether the alleged facts fit within any cognizable legal theory (*see, Leon v Martinez*, 84 NY2d 83; *Guggenheimer v Ginzburg*, 43 NY2d 268; *Rovello v Orofino Realty Co.*, 40 NY2d 633). Under CPLR 3211(a)(1), dismissal is warranted if the documentary evidence submitted utterly refutes the plaintiff's factual allegations, conclusively establishing a defense to the asserted claims as a matter of law (*see, Goshen v Mut. Life Ins. Co.*, 98 NY2d 314, 326; *Leon v Martinez*, *supra* at 88). Furthermore, an action is subject to dismissal if said action is barred by the applicable statute of limitations. (*see, A. Morrison Trucking v. Bonfiglio*, 13 Misc 3d 1211A). Similarly, Delaware law requires a court to accept all of the plaintiff's factual allegations as true and give the plaintiff the benefit of all inferences that may be drawn from those facts (*see, E.I. Dupont De Nemours and Company Inc., v Huttig Building Products*, 2002 Del. Super. Lexis 315).

Applying this law to the facts of the case the Court finds that dismissal is warranted as to the First cause of action seeking dissolution of Nastel Technologies, Inc. The parties do not disagree that Nastel is an entity incorporated under Delaware Law. Notwithstanding that fact, Shetty argues that New York courts have the authority to rule on the internal affairs of a foreign corporation relying on the case of *Brioda v Bancroft*, (103 A.D.2d 88). However, it is well settled that a foreign corporation is controlled, as to its dissolution, by the laws of its domicile (*see, In the Matter of Candis I. Warde-McCann v Commex, Ltd.* 135 A.D.2d 541). Furthermore, jurisdiction will be declined where the determination of the internal affairs of the corporation are dependant on the laws of the foreign state, where the relief sought is more appropriately adjudicated in the courts of the State in which the corporation is formed, (*see Langfelder v Universal Laboratories, Inc.*, 293 NY 200). Thus, the Court finds that it does not have subject matter jurisdiction to dissolve Nastel Technologies Inc. under BCL 1104-a, and the First cause of action is dismissed.

Turning to the Second cause of action, as previously set forth herein, Shetty and D. Mavashev entered into a contract on or about December 6, 1994. This contract sets forth the terms under which Nastel Technologies, Inc. was formed. Shetty argues that this agreement forms a partnership between himself and D. Mavashev, governed by the laws of the State of New York and is separate and apart from the corporation. In his petition, Shetty seeks dissolution of this

partnership under New York law. In their motion to dismiss, the Nastel Respondents argue that there is no current and ongoing partnership between Shetty and D. Mavashev.

A partnership and a corporation are mutually exclusive, each governed by a separate body of law, (*see Savino Notar-Francesco v Furci* 149 AD2d 490). “When parties adopt the corporate form, with the corporate shield extended over them to protect them against personal liability, they cease to be partners and have only the rights, duties and obligations of stockholders. They cannot be partners *inter sese* and a corporation as to the rest of the world”, (*see Weisman v Awnair Corporation of America* 3 NY2d 444). Moreover, to the extent that a partnership might have been formed, the partnership ceased to exist when Shetty and D. Mavashev formed a corporation (*see, Weiner v Hoffinger*, 298 AD2d 453). Accordingly, the court dismisses the Second cause of action.

Shetty also petitions for the appointment of a receiver under BCL 1113. Pursuant to BCL 1202, courts can appoint a receiver only under certain circumstances including, without limitation, in a proceeding for Judicial Dissolution (*see, BCL 1202(a)(1)*). Since the court has dismissed Shetty’s causes of action for dissolution, the request for the appointment of a receiver must also be dismissed.

Turning to Shetty’s claims which purport to be derivative claims against D. Mavashev, Albert Mavashev and Steven Dmiszewicki which allege fraud, misconduct, and breach of fiduciary duty, as well as the derivative claim of aiding and abetting a breach of fiduciary duty against the remaining defendants, the movants claim that Shetty is not a valid plaintiff to bring a derivative claim, as he does not represent the interests of the other shareholders of Nastel. They claim that since Shetty has named the remaining shareholders in Nastel as defendants he cannot represent their interest. Furthermore, they argue that Shetty has not sufficiently plead these causes of action.

One of the abiding principles of the law of corporations is that issues of corporate governance are regulated by the law of the state in which the corporation is chartered, in this case, Delaware (*see, Hart v General Motors*, 129 AD2d 179). Therefore, in evaluating the derivative claims asserted in the complaint, the Court will apply applicable Delaware law. There are several factors which may be considered in determining whether a derivative plaintiff may maintain a lawsuit, including the economic antagonisms between representative and the class, the relative magnitude of plaintiff’s personal interests and the vindictiveness toward defendants (*see, In re Dairy Mart Convenience Stores, Inc.* 1999 Del. Ch. Lexis 94). Furthermore, where a shareholder is the driving force behind the litigation and acted for the benefit of all, he is an adequate class representative (*Id.*). In the case at bar, Shetty is a proper representative of the shareholders since the remaining shareholders are accused of the alleged wrongdoing. If Shetty is disqualified as a representative, there is no other shareholder to bring this action on behalf of all shareholders of Nastel. If Shetty prevails on his derivative claims, all of the shareholders will benefit through the Company.

The Nastel defendants also argue that the complaint should be dismissed because the board of directors properly responded to Shetty’s August 11, 2006 demand and took appropriate

action. The complaint asserts that Shetty sent a letter to the board describing the acts which he believes gives rise to this litigation. The complaint sets forth specific instances where Shetty believes corporate conversion has occurred. It is not disputed that in response to Shetty's letter, the board appointed a one-member committee consisting of Dmiszewicki, a defendant in this action and one of the individuals who Shetty alleges participated in the complained of actions. Pursuant to Delaware General Corporation Law, the complaint must allege with particularity the efforts, if any, made by the plaintiff showing he has demanded that the directors pursue a corporate claim and the directors have wrongfully refused to do so, or that the directors are incapable of making an impartial decision. **Del. Ch. Ct. R. 23.1**. Furthermore, the pleading must set forth particularized factual statements that are essential to the claim (*see, Brehm v Eisner*, 746 A2d 244).

The court concludes that Shetty has sufficiently plead both the allegations and the futility of his efforts in bringing these matters to the board. Therefore the court denies the Nastel Defendants motion to dismiss as to the Third and Fourth causes of action and to the derivative portions of causes of action Six, Seven and Ten¹. However, since Shetty has failed to properly plead the derivative causes of action by naming Nastel as a plaintiff, the court directs Shetty to serve an amended complaint which sets forth in the caption his intention to bring these claims on behalf of all Nastel shareholders.

Shetty also alleges direct claims in cause of action Six for breach of fiduciary duty by defendants D. Mavashev, Albert Mavashev and Steven Dmiszewicki. Shetty claims that these three defendants make up the current board of directors of Nastel. Shetty further alleges that on August 11, 2006 he demanded that the Board of Directors cause Nastel to take corrective action against the "offending defendants." He alleges that his demand for action was futile since these three directors constitute a majority of the Board and their hostile interest caused damage to Nastel and Shetty as a shareholder. In cause of action Seven, Shetty pleads a direct claim for aiding and abetting a breach of fiduciary duty by defendants Zatuchni, Zatuchni & Associates, Iljeto, Jitex, Matrix, Lumla and Contrado. Shetty also directly alleges Breach of Contract in his Eighth cause of action against D. Mavashev and Breach of Duty of Good Faith and Fair Dealing against D. Mavashev in his Ninth cause of action. Finally, in cause of action Ten, Shetty alleges usurpation of corporate opportunity by D. Mavashev and Albert Mavashev. Since the actions which give rise to these claims purport to have been performed in New York and are not claims of the corporation, they will be decided under New York Law.

It is axiomatic that a shareholder has no individual cause of action to recover damages for a wrong against a corporation, even if that shareholder loses the value of his investment or incurs personal liability in an effort to maintain the solvency of the corporation. Allegations of mismanagement or diversion of assets by officers or directors for their own enrichment, without more, plead a wrong to the corporation only, for which a shareholder may sue derivatively, but not individually. (*see, Abrams v Donati*, 66 NY2d 951, 953; *Elenson v Wax*, 215 AD2d 429). The pertinent inquiry is whether the thrust of the plaintiff's action is to vindicate

1. Although cause of action ten does not state that it is a derivative claim, the language used and the relief sought indicate that it is brought as both a derivative and direct cause of action.

his personal rights as an individual and not as a stockholder on behalf of the corporation (*see*, **Albany-Plattsburgh United Corp. v Bell**, 307 AD2d 416, 419).

This case presents no established exception to the general rule (*see*, **Glenn v Hoteltron Sys.**, 74 NY2d 386, 393; **Abrams v Donati**, *supra* at 953-954). Shetty purports to seek damages directly and as a shareholder, but has failed to plead on behalf of the other shareholders of Nastel. Shetty's standing is that of a shareholder suing another shareholder who mismanaged a corporate asset, entitling him to sue only derivatively (*see*, **Wolf v Rand**, 258 AD2d 401, 403; *see also*, **Elenson v Wax**, *supra* at 429). Therefore, the court dismisses the direct portions of causes of action Six and Seven, Nine and Ten.

However, the Court denies dismissal of the Eighth and Ninth causes of action asserted directly against D. Mavashev. These causes of action are based on the agreement signed by Shetty and D. Mavashev on or about December 6, 1994. In reading this agreement, the Court finds that even though it is not a partnership agreement, as previously discussed herein, it is a valid binding contract between the individual parties with specific propositions that must be evaluated in light of the allegations raised (*see*, General Obligations Law §5-701). Every contract contains an implied covenant of good faith and fair dealing, (*see*, **Abiele Contracting, Inc. v New York City School Construction Authority**, 91 NY2d 1).

The Eighth cause of action alleges that D. Mavashev "forced" Shetty to give up certain of his shares in Nastel. According to the record now before the Court, the latest transfer of stock occurred in 1996. This action was not commenced until September 2006. Thus, this portion of the claim is clearly barred by the applicable six-year statute of limitations which applies to breach of contract actions, *see* CPLR 213. However, Shetty also alleges improper transfers of funds by D. Mavashev as late as December 2005, in violation of paragraph six of the agreement. Shetty contends that these alleged improper transfers constitute a breach of contract and breach of good faith and fair dealing by D. Mavashev in his individual capacity. The Court finds that Shetty has sufficiently pled both breach of contract and breach of the duty of good faith and fair dealing by D. Mavashev to survive this motion to dismiss and denies defendants motion as to these causes of action.

The Zatuchni Defendants move to dismiss the Seventh cause of action against them for aiding and abetting a breach of fiduciary duty. Since, the direct cause of action by Shetty has been dismissed above, the Court turns now to the derivative claim. Under Delaware law, a third party may be liable for aiding and abetting a breach of a corporate fiduciary's duty to the stockholders if the third party knowingly participates in the breach (*see*, **Khanna v McMinn**, 2006 Del. Ch. LEXIS 86). To survive a motion to dismiss, the complaint must allege facts that satisfy the four elements of an aiding and abetting claim: 1) the existence of a fiduciary relationship, 2) a breach of the fiduciary's duty, 3) knowing participation in that breach by the defendants, and 4) damages proximately caused by the breach (*Id.* at 112). The Zatuchni Defendants argue that Shetty has failed to plead the required elements and that the documentary evidence submitted in support of their motion supports dismissal of this action against them. Shetty alleges that the Zatuchni Defendants, as attorneys for Nastel, knew of the fiduciary relationship between the Nastel Defendants and the shareholders of Nastel and has pled breach of fiduciary duty against the Nastel

Defendants. Shetty further alleges that Zatuchni participated in the breach by accepting a contingency fee in December 2005, which he contends was excessive and unwarranted. Shetty also alleges that Zatuchni accepted a fee for services provided, which was not due to them for at least six months. Shetty alleges that Nastel was damaged by the Zatuchni Defendants in an amount to be determined at trial. The Zatuchni Defendants claim that the documents submitted in support of their motion prove that Shetty was aware of this fee and that this fee was neither excessive nor unwarranted. In review of the record and accepting each of these allegations as true, the Court finds that Shetty has adequately pled a cause of action for aiding and abetting a breach of fiduciary duty against the Zatuchni Defendants and, therefore, denies the motion to dismiss the derivative claim against the Zatuchni Defendants.

As previously stated, Shetty has remaining derivative causes of action. The Court directs Shetty to serve an Amended Complaint which properly names Nastel as a plaintiff and that Shetty is bringing this action on behalf of all of the shareholders of Nastel along with his direct claims for Breach of Contract and Breach of Fiduciary Duty against D. Mavashev.

HON. ELIZABETH HAZLITT EMERSON

DATED: December 12, 2007

J. S.C.