

Forbush v Goodale

2013 NY Slip Op 30351(U)

February 4, 2013

Sup Ct, Suffolk County

Docket Number: 33538/2011

Judge: William B. Rebolini

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Short Form Order

SUPREME COURT - STATE OF NEW YORK

I.A.S. PART 7 - SUFFOLK COUNTY

PRESENT:

WILLIAM B. REBOLINI
Justice

Susan Forbush, deriv atively on behalf of
herself and all others similarly situated,

Plaintiff,

-against-

Edgar F. Goodale, Joseph A. Gaviola, James E.
Danowski, J. Gordon Huszagh, David A. Kandell,
Thomas S. Kohlmann, Terence X. Meyer, Stacey L.
Moran, Susan V.B. C'Shea and John D. Stark, Jr.,

Defendants.

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Motion Sequence No.: 002; MD

Motion Date: 5/2/12

Submitted: 11/7/12

Motion Sequence No.: 003; MD

Motion Date: 5/2/12

Submitted: 11/7/12

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Clerk of the Court

Attorney for Defendants

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James E. Danowski, J. Gordon
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Kohlmann, Terence X. Meyer, Susan
V.B. O'Shea and John D. Stark, Jr.:

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Upon the following papers numbered A1 to A3 and 1 to 43 read upon these motions to dismiss: Notice of Motion and supporting papers, A1 - A3; Notice of Motion and supporting papers (003), 1 -16; Answering Affidavits and supporting papers, 17 - 30; Replying Affidavits and supporting papers, 31 - 39; Other, Supplemental Affirmation and supporting papers, 40 - 43; it is

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ORDERED that the motion (002) by defendant Stacey L. Moran for an order dismissing the complaint and the motion (003) by the remaining defendants and the nominal defendant for an order dismissing the complaint, are consolidated for the purposes of this determination; and it is further

ORDERED that the motions for orders dismissing the complaint pursuant to CPLR 3211 (a) (3) and (a) (7), 3013, 3016 (b), and BCL § 626 (c) are denied.

This is a shareholder derivative action brought to recover damages allegedly sustained by nominal defendant, Suffolk Bancorp, as a result of defendants' breach of fiduciary duties, abuse of control, gross mismanagement, waste of corporate assets, unjust enrichment, and aiding and abetting thereof by the individual defendants. Defendants Edgar F. Goodale, Joseph A. Gaviola, James E. Danowski, J. Gordon Huszagh, David A. Kandell, Thomas S. Kohlmann, Terence X. Meyer, Susan V. B. O'Shea, and John D. Stark, Jr., ("defendants") as well as nominal defendant Suffolk Bancorp now move for an order dismissing the complaint in its entirety for failure to state with particularity any effort by plaintiff to secure the initiation of an action by the board of directors of Suffolk Bancorp or the reasons she failed to make such an effort, for plaintiff's lack of capacity to sue, and for failing to state a cause of action. In support of the motion, defendants and Suffolk Bancorp submit copies of the complaint, Suffolk Bancorp's 2009 and 2010 annual reports and forms 10-K, and certain SEC filings on behalf of Suffolk Bancorp. Defendant Stacey L. Moran ("defendant Moran") moves for the same relief and joins in and incorporates by reference all of the factual and legal arguments set forth in defendants' moving papers.

Plaintiff's complaint of forty-four pages contains seventy-four separately enumerated paragraphs, some with up to as many as fifteen sub-parts, as well as lengthy quotations from various SEC filings. It alleges that plaintiff is and was a shareholder of Suffolk Bancorp during the relevant period (*i.e.* March 12, 2010 through August 12, 2011), for which she brings this action. The complaint maintains that Suffolk Bancorp is incorporated under the laws of the State of New York, with its principal offices in Riverhead, New York and that defendants Danowski, Gaviola, Goodale, Huszagh, Kandell, Kohlmann, Meyer, O'Shea, and Stark all served as directors of Suffolk Bancorp and that defendant Moran was the CFO of Suffolk Bancorp during the relevant period. Additionally, the complaint states that defendants Danowski, Gaviola, and Kandell were members of Suffolk Bancorp's audit committee (defendant Kandell having acted as the chairman), defendant Goodale was Chairman of the Board, and defendant Huszagh was president and CEO (and interim CFO since June 25, 2011) during the relevant period. Finally, plaintiff contends that defendant Kohlmann was chairman of the board, CEO and President of Suffolk Bancorp and the chief lending officer in years prior to the relevant period.

Business Corporation Law § 626 (a) states that "[a]n action may be brought in the right of a domestic or foreign corporation to procure a judgment in its favor, by a holder of shares ... of the corporation ..." As plaintiff has alleged that she was a shareholder of the nominal defendant corporation she is authorized to bring this action. Thus, those portions of the motions which seek to dismiss her claim pursuant to CPLR 3211 (a) (3) (*i.e.* that plaintiff has no legal capacity to sue) are denied.

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Because shareholder derivative actions infringe upon the corporate boards' managerial discretion, courts are reluctant to permit such actions, and the court's power to direct the management of a corporation's affairs should be exercised with restraint (*Marx v Akers*, 88 NY2d 189, 194, 644 NYS2d 121 [1996]), and, generally, a demand first must be made on the board of directors to pursue a claim before such an action is instituted (*Bansbach v Zinn*, 1 NY3d 1, 769 NYS2d 175 [2003]). Business Corporation Law § 626 (c) states that in a shareholders' derivative action, "the complaint shall set forth with particularity the efforts of the plaintiff to secure the initiation of such action by the board or the reasons for not making such an effort." A demand for the board to take action "would be futile if a complaint alleges with particularity that (1) a majority of directors are interested in the transaction, or (2) the directors failed to inform themselves to a degree reasonably necessary about the transaction, or (3) the directors failed to exercise their business judgment in approving the transaction" (*Marx v Akers, supra* at 198, 200, 201). Demand has been excused because of self-dealing by the controlling directors, self-interest of the directors in the challenged transaction (or specifically where the controlling directors breached a fiduciary obligation in return for personal benefits), breach of duty of due care and diligence to the corporation by disinterested outside directors (where the outside directors failed to do more than "rubber-stamp" the decisions of the outside managers) (*id*), and where a director with no direct interest in a transaction is "controlled" by a self-interested director (*Bansbach v Zinn, supra* at 9). A director is self-interested where he "will receive a direct financial benefit from the transaction which is different from the benefit to shareholders generally" (*Marx v Akers, supra* at 202). A plaintiff must state the claim of interest with particularity, simply stating conclusory allegations of wrongdoing or control is not sufficient to circumvent the statutory requirement that plaintiff demand the board to take action (*Bansbach v Zinn, supra*).

The complaint states, in pertinent part, that a demand upon the board to institute the action against the individual defendants would be futile because they are interested in its outcome. It alleges that defendants Huszagh and Meyer used their insider information to sell their company stock at greatly inflated values during the relevant period, that defendant Kohlmann's substantial retirement benefits and his vested interest in the value of Suffolk Bancorp's shares render him incapable of rationally assessing a demand on the board and that defendant Meyer receives substantial compensation for work done by a law firm, of which he is a member, on behalf of Suffolk Bancorp (and that Suffolk Bancorp plans to continue to retain his law firm). The complaint also claims that defendant Huszagh is unable to impartially consider a demand since three of the defendants comprise the compensation committee which sets his salary and that since defendants Danowski, Gaviola, Kandell and Stark were derelict in their duties, *viz a viz* their obligation to address risk management issues and concerns as part of the audit committee, they would be unable to properly assess a demand on the board that is based upon this previous dereliction of duties. As the complaint contends, non-employee directors, Danowski, Gaviola, Goodale, Kandell, Kohlmann, Meyer, O'Shea, and Stark have and continue to receive compensation in the form of cash and stock option awards making them interested in maintaining their positions on the board and safeguarding their compensation, thus rendering them interested and a request upon them to bring an action, futile. Additionally, the allegations of the complaint maintain that the directors would be forced to sue themselves and those other directors with whom they have extensive business and personal dealings,

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that other lawsuits could result from an action to remedy the wrongs alleged, hopelessly conflicting the directors in making an independent determination to sue themselves.

Here, where the complaint asserts particularized facts that allege that a majority of the board of directors either had a self-interest in the challenged transactions and that they would be incapable of making an impartial decision as to whether to bring suit, demand upon the board to bring suit would be futile and is excused (*see Bansbach v Zinn, supra; Marx v Akers, supra; Tsutsui v Barasch*, 67 AD3d 896, 892 NYS2d 400 [2d Dept 2009]; *Malkinson v Kordonsky*, 56 AD3d 734, 868 NYS2d 123 [2d Dept 2008]).

In making a determination to dismiss pursuant to CPLR 3211 (a) (7) the court must assume to be true the facts plead, give every favorable inference to the allegations, and determine only whether the alleged facts fit any cognizable legal theory (*Dickinson v Igoni*, 76 AD3d 943, 908 NYS2d 85 [2d Dept 2010]; *Tsutsui v Barasch, supra*). The Court denies the portions of defendants' motions to dismiss pursuant to CPLR 3211 (a) (7), it having determined that plaintiff has adequately plead her causes of action for gross mismanagement, contribution and indemnification, abuse of control, and waste of corporate assets within the four corners of the complaint. Additionally, the complaint is subject to the more strict pleading requirements of CPLR 3016 (b) since it alleges a breach of a fiduciary duty (*see Tsutsui v Barasch, supra*). The plaintiff is required to allege "facts [which] are sufficient to permit a reasonable inference of the alleged conduct" constituting the breach of fiduciary duty (*Pludeman v Norther Leasing Sys., Inc.*, 10 NY3d 486, 491, 860 NYS2d 422 [2008]). Here, where the complaint sets forth relevant portions of an October 25, 2010 agreement signed by a majority of directors which details the various obligations of competent management, internal audits, loan and lease loss programs and, relevant portions of annual reports and forms 10-K filed with the SEC and various press releases which state summary of loan losses and quarterly earnings, the allegations satisfy the requirements of CPLR 3016 (b). Thus, the portions of defendants' motions which request that the complaint be dismissed pursuant to CPLR 3016 (b) are denied.

Finally, those portions of defendants' motions which request the court to dismiss the complaint for failure to comply with CPLR 3013 are denied, the complaint complying with the requirement that it be sufficiently particular to give the court and parties notice of the transactions, occurrences, or series of them intended to be proved and the elements of each cause of action.

Accordingly, defendants' motions are denied in their entirety.

Dated: February 4, 2013


 HON. WILLIAM B. REBOLINI, J.S.C.

_____ FINAL DISPOSITION _____ X _____ NON-FINAL DISPOSITION