

Matter of Pappas

2014 NY Slip Op 30470(U)

February 28, 2014

Sur Ct, New York County

Docket Number: 2003-2184

Judge: Nora S. Anderson

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SURROGATE'S COURT : NEW YORK COUNTY

New York County Surrogate's Court
DATA ENTRY DEPT.

FEB 28 2014

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In the Matter of the Application of
Robert H. Groman and Helga Hensing, as
Co-Executors of the Estate of

CHRISTO BYRON PAPPAS,

File No. 2003-2184

Deceased,

for Leave to Compromise the Claims as
and Between Nicholas Cola and Byron
Chemical Company, Inc., and the Estate
of Christo Byron Pappas Pursuant to
SCPA § 1813.

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A N D E R S O N, S.

The executors of the estate of Christo Byron Pappas renew their request for permission to compromise various claims (SCPA § 1813). This court previously denied such application without prejudice to renew upon the submission of additional information that would permit the court to evaluate whether the proposed settlement was in the best interests of the estate (*Matter of Pappas*, 36 Misc 3d 1204[A], 2012 NY Slip Op 51189[U][Sur Ct, NY County 2012]). Such information has now been submitted. Of the more than 35 beneficiaries under decedent's will, only Laura Candela, a devisee of certain real property and a six percent residuary beneficiary, objects. The parties have stipulated that the court may decide the matter on the papers submitted.

The following is a brief discussion of the history of this estate and the claims at issue. Decedent died on June 6, 2003. Under his will, probated in this court, he left his estate, worth approximately \$31,700,000, to family, friends and various

employees of Byron Chemical Company, Inc. ("Byron Chemical"), the company of which he was the founder and majority shareholder. Letters testamentary issued on October 23, 2003, to Robert H. Groman, Helga Hensing, and Ms. Candela, the last of whom resigned with court permission a year later (*Matter of Pappas*, NYLJ, Nov. 18, 2004, at 31, col 4 [Sur Ct, NY County 2004]).

At the time of his death, decedent owned 164 shares (82 percent) of the outstanding shares of Byron Chemical. Nicholas Cola and Ms. Candela, Byron Chemical employees, each owned 18 shares (collectively, 18 percent), which they had received from decedent in 1993. Upon decedent's death, the disposition of his ownership interest in the company was governed by a Shareholder Agreement and Irrevocable Proxy executed on September 23, 1993, and amended on December 23, 2002 (the "Shareholder Agreement"), which provided for the sale of decedent's stock to the other two shareholders, Ms. Candela and Mr. Cola. Pursuant to the terms of the Shareholder Agreement, the estate sold half of its interest in Byron Chemical (82 shares) to Mr. Cola in December 2003 for \$1,721,081.81. For reasons not relevant here, Byron Chemical redeemed Ms. Candela's 18 shares, and she opted not to purchase the estate's remaining 82 shares under the Shareholder Agreement. Thus, Mr. Cola currently owns 100 shares of the company (55 percent) and the estate owns 82 shares (45 percent).

There is no dispute that the administration of this estate

was complicated and contentious from the outset, resulting in multiple litigations in different forums. The executors first contended with Mr. Cola, who they believed had taken money and documents from decedent's Manhattan apartment after his death. In December 2003, they obtained an Order to Attend in this court (SCPA § 2103), compelling Mr. Cola to appear for an inquiry concerning the property (the "Discovery Proceeding"). Mr. Cola turned over estate documents and cash and submitted to an examination. The executors took no further action.

Shortly after the Discovery Proceeding was commenced, Ms. Candela brought an action against the estate, Mr. Cola and Byron Chemical in Supreme Court, Nassau County (the "Candela Action"), alleging that Byron Chemical had breached her executive employment contract by failing to pay her annual bonuses equaling 10 percent of Byron Chemical's pre-tax profits. She also asserted causes of action against the estate for, among other things, fraud, unjust enrichment and breach of fiduciary duty based upon alleged misconduct by decedent related to Byron Chemical. Ultimately, she was successful only on her employment contract claims against Byron Chemical, but her damages were substantial. In October 2008, after Byron Chemical had exhausted its appeals, she received \$6,749,500 in satisfaction of her judgment.

The judgment had a significant impact on the estate's

administration. Not only did it greatly reduce the value of the estate's interest in Byron Chemical, but it also triggered additional litigation with Mr. Cola and Byron Chemical. In August 2006, they jointly commenced an action against the estate in Supreme Court, Queens County, seeking in excess of \$10 million in damages for decedent's alleged breach of fiduciary duty, fraud and violations of New York's Business Corporation Law (the "Byron Action").¹

The basis for the claims were certain judicial findings in the Candela Action. The findings in question involved misconduct of decedent in his role as President and majority shareholder of Byron Chemical. The company and Mr. Cola contended that those findings, one of which was that decedent had caused Byron Chemical to underpay Ms. Candela her bonuses in violation of her employment contract, necessarily made decedent (and therefore the estate) liable to them. Since Mr. Cola's employment contract was the same as Ms. Candela, he asserted that he was entitled to a judgment for the same damages as she had obtained. Byron Chemical sought, among other things, to recover its liability to Ms. Candela and (potentially) to Mr. Cola under their respective employment contracts. In response, the estate, as a Byron Chemical shareholder, asserted several derivative counterclaims

¹ The Byron Action was subsequently transferred to Supreme Court, New York County.

against Mr. Cola arising out of his role as an officer of Byron Chemical.

Byron Chemical and Mr. Cola moved for summary judgment, asserting that the court's findings in the Candela Action regarding decedent's conduct conclusively established the estate's liability on their claims. No decision on the motion has been rendered because the Supreme Court is holding the motion in abeyance pending the outcome here.

At about the same time that the Byron Action was commenced, the executors brought an action against Byron Chemical in Supreme Court, New York County (the "Estate Action"), seeking approximately \$4.35 million for the unpaid compensation allegedly earned by decedent as President of Byron Chemical and Chairman of Byron Chemical's Board of Directors (\$1.4 million), as well as the unpaid balance of loans decedent allegedly had made to the Company (\$2.95 million). Byron Chemical interposed an answer asserting, among other things, that the estate was estopped from seeking recovery for the unpaid compensation and loans because of decedent's fraudulent conduct. The executors moved for summary judgment. However, that motion is also being held in abeyance pending a determination of this proceeding.

After commencing the Estate Action, the executors also filed a petition in this court seeking a declaration that Mr. Cola owed the estate additional funds for his December 2003 purchase of 82

shares of Byron Chemical stock. The executors alleged that the sale price was calculated incorrectly (the "Stock Purchase Proceeding"). In response, Mr. Cola counterclaimed, asserting that he was entitled to a refund of the entire amount that he had paid because the shares of the Company were essentially valueless. The parties have agreed to a stand-still of litigation pending the court's determination of the present application.

The Settlement and Release Agreement (the "Settlement Agreement") for which the executors seek authorization to execute (SCPA § 1813) would conclude the Discovery Proceeding, the Byron Action, the Estate Action and the Stock Purchase Proceeding through the exchange of mutual releases among Byron Chemical, Mr. Cola and the estate.² In addition, Mr. Cola, who is also a beneficiary under the will and has objected to the executors' second intermediate accounting, would withdraw his objections.³

The estate would recover from Byron Chemical \$1,999,297.84 of the total amount of outstanding loans allegedly owed to the

² Byron Chemical and Cola would also release the co-executors in their capacity as officers and directors of Byron Chemical and related entities.

³ Such a provision would normally raise concerns that the fiduciaries were motivated, at least in part, by a desire to resolve objections leveled against them. However, a review of Mr. Cola's objections indicates that the objections are not directed to specific conduct of the fiduciaries, but rather, to the way in which the account treats matters that are the subject of the pending litigations involving Mr. Cola and Byron Chemical.

estate (approximately \$2.95 million). In turn, the estate would refund to Mr. Cola \$1,536,581.80 of the total amount (\$1,721,081.81) that Cola had paid for his purchase of the 82 shares of the estate's Byron Chemical stock in December 2003. Additionally, the estate would sell to Mr. Cola its remaining 82 shares of Byron Chemical stock for \$202,725, making Mr. Cola Byron Chemical's sole shareholder. Further, because the estate would be refunding to Mr. Cola a substantial portion of the price that he had paid for its shares of Byron Chemical, the estate would have a basis to seek an estate tax refund from New York State and federal taxing authorities on the ground that the reported value of the estate's shares of Byron Chemical, as of the date of decedent's death, was overstated.⁴

According to petitioners, the Settlement Agreement is in the best interests of the estate for several reasons. First, it would resolve all pending litigation with Mr. Cola and Byron Chemical, thereby avoiding the possibility of substantial liability (or inability to recover on potential judgments obtained against Byron Chemical and Cola), as well as the very substantial legal fees that would no doubt be incurred to litigate the pending proceedings to conclusion. Second, it would

⁴ The executors represent that they have preserved the right to make a claim for a refund on this ground.

also result in the estate's receiving \$462,716.04⁵ plus \$202,725 for the estate's minority interest in Byron Chemical. Third, the settlement would support the Estate's effort to obtain a substantial refund for federal and New York State estate taxes. Finally, the settlement would permit the fiduciaries to move closer to a final accounting so that distributions can at long last be made to the more than 35 beneficiaries who have been awaiting the conclusion of more than ten years of litigation.

The power of a fiduciary to compromise claims brought in favor of or against the estate, provided such power is not limited by the court or the governing instrument, is well established (EPTL § 11-1.1[b][13]; see *Matter of Leopold*, 259 NY 274 [1932]). Interested parties may challenge any compromise in an accounting (see SCPA Article 22), and, if successful, obtain a surcharge against the fiduciary. A fiduciary need not wait until an accounting, however, to seek judicial approval of a compromise.

SCPA § 1813 permits fiduciaries to seek, "for good cause shown," court approval of a compromise in advance of an accounting. This enables a "fiduciary to obtain advance assurance that, so long as there is no fraud or like infirmity to taint his proposed compromise, he will be shielded from later

⁵ The estate would receive \$1,999,297.84 from Byron Chemical, but would be required to pay to Cola \$1,536,581.80.

second-guesses with respect to it" (*Matter of Lazarus*, NYLJ, Mar. 19, 1998, at 35, col 4 [Sur Ct, NY County], *affd* 257 AD2d 436 [1st Dept 1999]). When evaluating an application under SCPA § 1813, the central consideration for the court is "whether the proposed compromise is in the estate's best interests" (*id.*). Among the factors courts consider are the "relative merit of the parties' positions (as qualified by the knowledge that litigation is never risk-free) and the value of achieving peace for the combatants sooner rather than later" (*id.* [citations omitted]).

As noted above, the court initially denied the executor's application without prejudice. Specifically, the court concluded that it was not in a position to evaluate the Settlement Agreement because petitioners had not offered an appraisal for the shares of Byron Chemical that the executors propose to transfer to Mr. Cola for \$202,725 (*Matter of Pappas*, 36 Misc 3d 1204[A], 2012 NY Slip Op 51189[U], *supra*). In support of their renewed application, petitioners have offered a detailed appraisal, dated October 17, 2012, by Jennings Business Valuation, Inc., ("Jennings") for the estate's 45 percent interest in Byron Chemical as of the date of the Settlement Agreement, November 12, 2009. According to the appraisal, the value of Byron Chemical was then no more than \$200,000. Further, Jennings reviewed the company's audited financial statements for December 31, 2010 and 2011 "to ascertain if the financial

condition of [Byron] changed significantly." Such review resulted in Jennings' opinion, also dated October 17, 2012, that the company's financial condition had not changed since the date of the Settlement Agreement and that the value of the company "remain[ed] unchanged."

Ms. Candela does not offer her own appraisal or challenge in any way the executors' appraisal or its methodology. Nor does she suggest, much less identify, grounds for a higher valuation based upon the company's financial condition after the appraisal. Instead, she relies solely on her opposition to the executors' original application, which predates the appraisal. This is fatal to her efforts for two reasons. First, her primary challenge to the Settlement Agreement had been that the executors had failed to offer an appraisal for the estate's minority interest in Byron Chemical to support a sale to Mr. Cola for \$202,725, a price which she claimed was "absurdly low." Second, her claims regarding valuation (which were not supported by documentary evidence) were based upon purported company financial figures from 2004 (and earlier). Such outdated financial information is not relevant to the valuation of the shares reached by the executors years later.

The executors have now submitted the appraisal that Ms. Candela argued was required. It is undisputed that the appraisal was made by a reputable firm, and the court has no basis to

challenge the valuation methodology employed. Moreover, as correctly noted by petitioners, because Mr. Cola, who is already a majority shareholder, will receive the estate's interest in Byron Chemical, the estate's shares were valued on a control, rather than a non-control, basis. The appraisal states that if the shares were sold to a third party on the open market, they would be sold as a non-controlling (45 percent) interest and would likely garner a lower price. Ms. Candela does not challenge that assertion.

The fact that the executors have now submitted an appraisal does not end the court's analysis, however. The court noted in its earlier decision that "the sale [of the estate's Byron Chemical shares] should not be viewed in isolation" (*Matter of Pappas*, 36 Misc 3d 1204[A], 2012 NY Slip Op 51189[U], *10, *supra*). Rather, the sale is a part of a larger transaction which would result in the resolution of all pending litigation between the parties. The issue is whether the settlement as a whole is in the best interest of the estate (*see Matter of Lazarus*, NYLJ, Mar. 19, 1998, at 35, col 4, *supra*), taking into consideration that "while the Surrogate has the power to review [the fiduciary's discretion to compromise], [she] cannot substitute [her] own discretion for the discretion of those upon whom the duty has been cast in settling the affairs of the estate" (*Matter of Rappaport*, 102 Misc 2d 910, 911 [Sur Ct, Nassau County 1980],

citing *Matter of Leopold*, 259 NY 274, *supra*).

The record includes all the relevant pleadings and motion papers in the pending litigations. Of particular note is that positions taken by Mr. Cola and Byron Chemical against the estate in the Byron Action, the Estate Action and the Stock Purchase Proceeding rely upon decedent's adjudicated misconduct in the Candela Action, which ultimately led to a more than \$6.7 million judgment levied against Byron Chemical. In the Byron Action, for example, Mr. Cola and Byron Chemical have moved for partial summary judgment, arguing that collateral estoppel bars re-litigation of decedent's misconduct as President of Byron, which in turn entitles them to judgment as a matter of law on the issue of liability.

In support of their application, the executors note that, before Mr. Cola and Byron Chemical moved for summary judgment, the estate had moved to dismiss. The executors argued, among other things, that, because the court in the Candela Action had dismissed Ms. Candela's fraud claims for failure to state a cause of action, Byron Chemical and Mr. Cola's claims against the estate, all of which rested on fraudulent conduct by decedent, were precluded on *res judicata* and collateral estoppel grounds. The court not only rejected such argument, but noted that,

"if any party might be able to demonstrate entitlement to invoke these doctrines in its favor, it would be Cola [and Byron Chemical] based on [the] findings in the Candela Action pertaining to [decedent's] or the

Estate's breach of contract and other wrongful conduct. Under the circumstances, it would offend basic principles of fairness to allow the Estate to benefit from the wrongdoing of its decedent by invoking the doctrine of collateral estoppel or res judicata."

Byron Chemical v Estate of Christo Byron Pappas, at 5, Sup Ct, NY County, November 5, 2007, Moskowitz, J, Index No. 405073/2006.

Although the court's statement is not an indication that the pending summary judgment motion of Byron Chemical and Mr. Cola will be granted if the parties continued to litigate, it does support the executors' contention that the various risks to the estate in these litigations are real. This is particularly so when "allowance [is made] for the vagaries of litigation" (*Matter of Lazarus*, NYLJ, Mar. 19, 1998, at 35, col 4, supra). In the Byron Action alone, the estate's liability could exceed \$10 million. The cost of prosecuting the estate's claims and defending against the claims of Byron and Mr. Cola, who have already demonstrated a willingness to invest significant resources to the litigations, cannot be underestimated.

Ms. Candela attempts to minimize the strength of Byron Chemical and Mr. Cola's claims against the estate. However, none of her arguments establishes that the Settlement Agreement, when viewed as a whole, is not in the best interests of the estate. For example, Ms. Candela asserts that, in the Candela Action, Mr. Cola testified that Ms. Candela was not entitled to additional compensation under her employment contract with Byron Chemical,

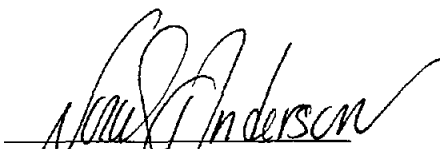
and thus he should be estopped from making any claim himself under the agreement in the Byron Action. She offers no legal support for this position and, in any event, she fails to provide a transcript of this purported testimony (which Mr. Cola challenges), even though she would have access to the transcript as a party to the action. Similarly, her argument that Mr. Cola's claim against the estate for unpaid compensation is "exceedingly far-fetched" ignores that Byron Chemical is seeking, in essence, the same damages from the estate for its liability to Ms. Candela and any potential liability to Mr. Cola under their respective employment contracts.

The settlement will provide a net recovery to the estate in excess of \$650,000, plus the potential for an estate tax refund. The risk of substantial liability as well as the additional costs of litigation will be avoided. After more than ten years of very expensive litigation on several fronts, the executors finally will be able to move toward winding up the estate and making distributions. The possibility that the executors might recover more through continued litigation than through settlement is outweighed by the estate's exposure to heavy liability for decedent's misconduct. With regard to the price at which the executors propose to sell the estate's minority interest in Byron Chemical, there is no dispute that the estate would need to liquidate its minority interest in Byron Chemical. The price for

the shares, which is just one aspect of the settlement, is supported by an appraisal, which Ms. Candela had an opportunity to challenge, but elected not to do so.

Based upon the foregoing, the court finds that the executors have demonstrated that the settlement is in the best interests of the estate. Accordingly, the petition is granted. The executors are authorized to settle the claims as between Mr. Cola and Byron Chemical and the estate as set forth in the Settlement Agreement pursuant to SCPA § 1813. This decision constitutes the order of the court.

Dated: February 28, 2014


S U R R O G A T E