Khandalavala v Artsindia.com, LLC
2014 NY Slip Op 30940(U)
April 8, 2014
Supreme Court, New York County
Docket Number: 652450/13
Judge: Melvin L. Schweitzer
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[* 1]

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK : PART 45

RUSTOM KHANDALAVALA, SUBHAS KHARA, ARVIND RAGHUNATHAN, and SOUMYO SARKAR, both individually and derivatively on behalf of ARTS INDIA FUND TWO, LLC,	
Plaintiffs,	Index No.: 652450/13:
-against-	DECISION AND ORDER
ARTSINDIA.COM, LLC, PRAJIT K. DUTTA, ANDREW SHEA, and ARTS INDIA FUND TWO, LLC, as Nominal Defendant,	Motion Sequence No. 008
Defendants.	

MELVIN L. SCHWEITZER, J.:

In this action, plaintiffs, members of nominal defendant Arts India Fund Two, LLC (the Fund), sue to recover damages arising out of alleged improper actions taken by defendants, the Managing Member of the Fund and its managing partner and administrator. The Amended Complaint alleges eight causes of action. The first is a direct claim for an accounting. The second through eighth causes of action, brought derivatively on behalf of the Fund, allege breach of contract (second), fraudulent misrepresentation (third), breach of fiduciary duty (fourth), aiding and abetting breach of fiduciary duty (fifth), misappropriation (sixth), conversion (seventh), and unjust enrichment (eighth). Defendants move (seq. # 008), pursuant to CPLR 3211 (a) (1) and (7), to dismiss the Amended Complaint based on documentary evidence and failure to state a cause of action.

Background

Arts India Fund Two, LLC, a Delaware limited liability company, was formed in or around March 2006 to invest in art from India and Pakistan, and now is in the process of

liquidating. Plaintiffs are members of the Fund, and each invested between $200,000 and $1 million in the Fund. Under the terms of the Fund's Limited Liability Company Agreement, defendant ArtsIndia.com, LLC (Arts India) was designated the Managing Member of the Fund, with responsibility for the day-to-day management of the business and affairs of the Fund, including operating the Fund and making buying and selling decisions. *See* Limited Liability Company Agreement (LLC Agreement), Ex. D (A) to Gorchkova Aff. in Support of Defendants' Motion to Dismiss (Gorchkova Aff.), § 11. Defendant Prajit K. Dutta (Dutta) is the Managing Partner of Arts India, and defendant Andrew Shea (Shea) is Arts India's Fund Administrator.

In early 2006, Dutta approached plaintiffs to invest in the Fund. Amended Complaint (Am. Complaint), NYSEF Doc. 69, ¶ 35. Dutta was the Managing Partner in Aicon Gallery, an independent art gallery specializing in Indian art, and he had previously managed a similar art investment fund, Arts India Fund One, LLC, which had been profitable. Am. Complaint, ¶ 22; Dutta Affidavit in Opposition to Order to Show Cause (Dutta Aff.), Ex. D to Gorchkova Aff., ¶¶ 5-6. Plaintiffs allege that, before they invested in the Fund, Dutta represented to them that, based on his relationships with artists and art galleries, he would be able to purchase art at "insider prices," which would protect their investments even with a downturn in the market. Am. Complaint, ¶ 36. Plaintiffs also allege that Dutta represented to them that an Investors' Committee would be created "to ensure the Fund was operating appropriately." *Id.*, ¶¶ 43-44.

In March 2006, plaintiffs, collectively, purchased 11 membership units (shares) in the Fund, at $200,000 per unit. Plaintiff Rustom Khandalavala (Khandalavala) purchased five membership units for $1 million; Arvind Raghunathan (Raghunathan) purchased three membership units for $600,000; Subhas Khara (Khara) purchased one membership unit for $200,000; and Soumyo Sarkar (Sarkar) purchased two membership units for $400,000. *Id.*,

¶¶ 37, 17, 19. Each plaintiff signed a Subscription Agreement (*Id.*, ¶ 37; Exs. D & E to Am. Complaint, NYSEF Doc. 70), and each executed, together with Arts India, the LLC Agreement. *Id.*, ¶ 39. There were 42 initial "high net worth" investors (the Members) in the Fund, including plaintiffs, in addition to Arts India and Dutta. Am. Complaint, ¶ 41; *see* Dutta Aff., ¶ 7.

The Subscription Agreement includes, under "Representations and Warranties," several non-reliance clauses. Section 2 (f) provides that "[t]he Investor is not relying upon any representation or warranty by the Company, or any agent of the Company, in determining to invest in the Shares . . . [and] has consulted . . . with the Investor's own advisors . . . and on that basis believes that an investment in the Shares is suitable and appropriate." The Subscription Agreement also provides that "[t]he Investor is aware and acknowledges . . . that the Shares involve a substantial degree of risk of loss of the entire investment and there is no assurance of any income from such investment." Section 2 (e).

Under the terms of the LLC Agreement, the Managing Member agreed to contribute $500,000 to the Fund, for 2.5 membership units. Am. Complaint., ¶ 50; *see* LLC Agreement, § 6 and Schedule A, Ex. G to Am. Complaint, NYSEF Doc. 70. Plaintiffs allege that Arts India "intentionally misused, converted, and misappropriated" the Fund's assets to pay for its initial capital contribution Am. Complaint, ¶¶ 51-53. Plaintiffs also allege that Dutta did not make an initial capital contribution of $200,000. *Id.*, ¶¶ 54-56. These allegations are based on plaintiffs' claims that a forensic accountant hired by them found evidence that approximately $167,000 was transferred from the Fund's Citibank account to Arts India's bank account on April 3 and 4, and May 4, 2006, and then, on May 5, 2006, $125,000 was transferred back to the Fund's Citibank account, and, upon information and belief, was used to make Arts India's capital contribution. *Id.*, ¶¶ 52-53. Plaintiffs' claim that Dutta did not make an initial capital contribution is based on

the forensic accountant's finding that an "Investment Receivable" account on the General Ledger indicates that $200,000 is still owed the Fund, and that Dutta "was likely" the investor who did not contribute $200,000. *Id.*, ¶¶ 54-56.

As set forth in section 3 of the LLC Agreement, the purposes of the Fund were

> "to buy, hold and sell art, incur indebtedness, secured and unsecured; to enter into and perform contracts and agreements of any kind necessary to, in connection with or incidental to the business of the Limited Liability Company; and to carry on any other activities necessary to, in connection with or incidental to the foregoing, as the Managing Member in his discretion may deem desirable."

The Fund planned to buy art between 2006 and 2008 and then sell it during a period ending on March 31, 2011), the original dissolution date of the Fund. Dutta Aff., ¶ 8; Dutta Aff. in Further Support of Defendants' Motion to Dismiss (Dutta Reply Aff.), ¶ 5. The LLC provided that the Fund could be "extended to March 31, 2013 by amendment of this Agreement by simple majority vote of members." LLC Agreement, § 5. The dissolution date of the Fund was extended twice, without a vote of the Members, until March 2013. According to the Fund's 2008 Annual Report, the Fund was fully invested by the end of that year. *See* Ex. Q to Am. Complaint, NYSEF Doc. 71, at 3. However, it is not disputed that the worldwide financial crisis in 2008 had a dramatic impact on the Indian and Pakistani art market, as parts of the market diminished by 80%, with no recovery until 2010. Dutta Aff., ¶ 8; Dutta Reply Aff., ¶ 5. As a result, the value of the Fund's holdings plummeted, and the Fund and its investors lost money. *Id.* Plaintiffs allege that, as of mid-2009, however, Dutta informed Khandalavala that the Fund had not suffered much impairment. Am. Complaint, ¶ 61.

Plaintiffs allege that, although defendants prepared annual reports, they only occasionally distributed semi-annual reports, and did not provide any quarterly reports as required by the LLC Agreement. *Id.*, ¶¶ 63-67. Plaintiffs also allege that defendants represented that market-wide issues had not materially affected the Fund (*id.*, ¶ 69), and reported only minimal losses. *Id.*, ¶¶ 69-72.

The 2008 Annual Report distributed to the Members informs the investors that the final two quarters of 2008 were "tough," that modern masters were selling for a third of their peak value and prices for contemporary artists were down 50%. Ex. Q to Am. Complaint, NYSEF Doc. 71, at 3. The report indicated that the Fund lost about $371,000 in 2008. *Id.* at 9. The report also noted that, in view of the market conditions, it did not seem in the best interest of the investors to sell the art, and it would be likely that the Fund's end date will be extended. *Id.* at 3. The 2009 Annual Report reported that the market was still down about 50% in the first two quarters of 2009, but had a modest rebound in the last two quarters of 2009, although the Fund lost about $335,000. Ex. R to Am. Complaint, NYSEF Doc. 71, at 3, 9.

The 2010 Annual Report reported that the market was starting to recover, especially for the "Modern Masters," which allowed Arts India to begin selling the Fund's holdings, "particularly on the Modern Masters side and especially in the latter half of 2010." Ex. S to Am. Complaint, NYSEF Doc. 71. at 3. The report stated that the Fund was "now mandated to exit by May, 2012" but a further extension may be necessary. *Id.* at 104-105. The Fund lost about $134,000 in 2010. *Id.* at 9.

According to the 2011 Annual Report (Ex. T to Am. Complaint, NYSEF Doc. 71), the market regressed in 2011, although sales of about a third of the Fund's holding yielded a profit,

and Arts India would "continue to manage the exit of the remaining portfolio" and "hope[d] to exit the Fund's holdings by year end 2013." *Id.* at 1, 3. The report stated that the Fund's assets were down, the Fund was losing money and would not be able to return investors' capital fully. *Id.* at 3. Arts India announced that it would, in order to maximize investors' returns, forego its share of annual profits. *Id.* The report concluded that it was anticipated that investors would receive between 76-86% of their initial capital investments. *Id.* at 4, 6.

The 2012 Annual Report, dated March 29, 2013 (Ex. U to Am. Complaint, NYSEF Doc. 71) noted that, although the original five-year term of the Fund ended in April 2011, Arts India had asked for "two extension years to try and exit the fund's holdings in an orderly fashion," largely because of difficulty selling contemporary works of art. *Id.* at 3. The report advised investors that the works of Modern Masters were expected to be sold in the next six months, but it was unclear what to do with the contemporary works, and Arts India was discussing with investors how to proceed and hoped to be able to return between 65-75% of the initial capital. *Id.* at 6. According to the report, some investors favored taking art against unreturned capital and some wanted the work to continue to be sold. *Id.* at 4. The report stated that the Fund had a net loss of about $727,000 in 2012. *Id.* at 9.

Plaintiffs allege that Arts India misrepresented initial capital committed in several annual reports (*id.*, ¶ 99), and received annual management fees and reimbursement for expenses in excess of fees allowed under the LLC Agreement. *Id.*, ¶¶ 100-102, 104-105. Plaintiffs further allege that Arts India took a percentage of net profits of the Fund when the Fund was operating at a loss, and, although the funds were returned, Arts India did not acknowledge that it was not

entitled to the funds. *Id.*, ¶¶ 73-74. Plaintiffs also allege that Arts India has not borne 20% of Fund's net losses "in contravention of the LLC Agreements." *Id.*, ¶ 107.

After advising members of the Fund that the Fund would be dissolved and the process of winding up would begin, Dutta requested that members offer suggestions for winding up. Dutta Aff., ¶ 10. In April 2013, Dutta sent a wind-up proposal to plaintiffs and other investors, which provided that investors could select art, up to the value of the member's shares, as a partial return on their investment, or wait for a return when the art works were sold at a future time. *Id.*; Am. Complaint, ¶ 79. A large majority of the Fund members approved the proposal, and Dutta then had the work appraised by Christies. Dutta Aff., ¶¶ 18-20. Plaintiffs objected to the proposal, and refused to vote on it. Am. Complaint, ¶¶ 80-82. They allege that there was no indication in the semi-annual and annual reports in 2012 that member investments would be returned in the form of an "in kind" distribution of art (*id.*, ¶ 76), and assert that the wind-up proposal is inequitable because members' selections would be limited to art that was not valued at a greater amount than the member's share. *Id.*, ¶ 152. Plaintiffs also claim that Arts India violated the LLC Agreement when it extended the dissolution date of the Fund without the necessary majority vote of the members (*id.*, ¶¶ 137-144), although there are no allegations that any of the plaintiffs objected to the extension, or otherwise objected to the management of the fund prior to the wind-up proposal, except when, in March 2012, Khandalavala objected to defendants' receipt of a fee at a time when the Fund was losing money.

In May 2013, plaintiffs demanded that defendants give them access to the Fund's records and books (*id.*, ¶ 84), and after negotiations for a date, and subsequent delays, records were made available. *Id.*, ¶¶ 85-89, 91-93. Plaintiffs claim the records show breaches of the LLC

Agreement, and plaintiffs allege that forensic accountants have found evidence of bank accounts and bank transactions related to the Fund which were not identified by defendants. *Id.*, ¶¶ 93-94. Plaintiffs claim that records show inconsistent labeling of art work, inconsistent pricing of similar work, errors in listing available inventory, and use of identical inventory numbers for different pieces of art (*id.*, ¶¶ 109-110), and that the forensic accountants found, among other things, errors in annual reports about the residual value of the Fund's portfolio and issues with the valuation and reporting of the Fund's assets. *Id.*, ¶¶ 111-115, 117.

Plaintiffs further allege that they found evidence that Arts India engaged in transactions when there was a conflict of interest between Arts India as Managing Member of the Fund and as Managing Partner of Aicon Gallery, by buying and selling art so that the gallery performed significantly better than the Fund, and by purchasing art from investors in the Fund. *Id.*, ¶¶ 119-121, 123-124, 126-127. In addition, plaintiffs claim that defendants reinvested the Fund's capital to purchase additional assets instead of returning it to the members as contemplated by the LLC Agreement (*id.*, ¶¶ 128, 130, 132), and obtained a commercial loan for Arts India of approximately $600,000, which resulted in additional interest payments and reduction of capital distribution to investors (*id.*, ¶ 133), and which transaction did not appear in the records produced by defendants. *Id.* ¶ 134.

Plaintiffs commenced the instant action in July 2013, alleging individual claims against defendants for breach of contract, fraud, fraudulent inducement, breach of fiduciary duty, aiding and abetting breach of fiduciary duty, and an accounting; and, at the same time, plaintiffs moved for a preliminary injunction to enjoin the disposition of the Fund's assets. Plaintiffs were granted a temporary restraining order, and after a hearing, the court vacated the temporary restraining

order and denied injunctive relief, with the understanding that Arts India would set aside $1.5 million of artwork during the pendency of this litigation. Plaintiffs' request for discovery of books and records of Arts India was granted, although limited, and, after plaintiffs' forensic accounting expert inspected the books and records produced, plaintiffs served the Amended Complaint, retaining the direct claim for an accounting, and replacing the other individual claims with derivative claims on behalf of the Fund.

Plaintiffs generally allege that, collectively, they invested $2.2 million dollars in the Fund, and have received in return only about $715,000, or 32.5% of their initial capital investment. Plaintiffs claim that they and the Fund have suffered substantial losses as a result of Arts India's breaches of the LLC Agreement and defendants' misrepresentations, breaches of fiduciary duty and self-dealing. Am. Complaint, ¶ 14. Defendants now move to dismiss the amended complaint in its entirety.

Discussion

It is well settled that on "a CPLR 3211 (a) (7) motion to dismiss, the court must afford the pleadings a liberal construction, accept the allegations of the complaint as true and provide plaintiff . . . 'the benefit of every possible favorable inference.'" *AG Capital Funding Partners, L.P. v State St. Bank & Trust Co.*, 5 NY3d 582, 591 (2005), quoting *Leon v Martinez*, 84 NY2d 83, 87 (1994); *see* CPLR 3026. "The motion must be denied if from the pleadings' four corners 'factual allegations are discerned which taken together manifest any cause of action cognizable at law.'" *511 W. 232nd Owners Corp. v Jennifer Realty Co.*, 98 NY2d 144, 152 (2002), quoting *Polonetsky v Better Homes Depot, Inc.*, 97 NY2d 46, 54 (2001). The court is not required, however, "'to accept at face value every conclusory, patently unsupportable assertion of fact

found in the complaint'" (*West 64th St., LLC v Axis U.S. Ins.*, 63 AD3d 471, 471 [1st Dept 2009] [citation omitted]; *see Erich Fuchs Enters. v American Civ. Liberties Union Found., Inc.*, 95 AD3d 558, 558 [1st Dept 2012]), and "'bare legal conclusions, as well as factual claims either inherently incredible or flatly contradicted by documentary evidence' are not presumed to be true and accorded every favorable inference." *Biondi v Beekman Hill House Apt. Corp.*, 257 AD2d 76, 81 (1st Dept 1999)(citation omitted), *affd* 94 NY2d 659 (2000); *see Zanett Lombardier, Ltd. v Maslow*, 29 AD3d 495, 495 (1st Dept 2006); *Robinson v Robinson*, 303 AD2d 234, 235 (1st Dept 2003).

"When evidentiary material is considered, the criterion is whether the proponent of the pleading has a cause of action, not whether he [or she] has stated one." *Guggenheimer v Ginzburg*, 43 NY2d 268, 275 (1977); *see Leon*, 84 NY2d at 88; *IIG Capital LLC v Archipelago, L.L.C.*, 36 AD3d 401, 402 (1st Dept 2007). Dismissal under CPLR 3211 (a) (1) "may be appropriately granted only where the documentary evidence utterly refutes plaintiff's factual allegations, conclusively establishing a defense as a matter of law." *Goshen v Mutual Life Ins. Co. of N.Y.*, 98 NY2d 314, 326 (2002), citing *Leon*, 84 NY2d at 88; *see 511 W. 232nd Owners Corp.*, 98 NY2d at 152; *Arnav Indus., Inc. Retirement Trust v Brown, Raysman, Millstein, Felder & Steiner*, 96 NY2d 300, 303 (2001).

Derivative Claims

At the outset, defendants move to dismiss the derivative claims on the grounds that plaintiffs failed to make a demand upon defendants prior to commencing this lawsuit and failed to adequately plead why demand would be futile.

It is undisputed here that, because the Fund is a Delaware company and operates under an agreement expressly governed by Delaware law,[1] Delaware substantive law applies to this case, and to the "threshold demand issue." *Hart v General Motors Corp.*, 129 AD2d 179, 182 (1st Dept 1987); *see Bodner v Grunstein*, 2011 NY Misc LEXIS 6904, *6 (Sup Ct, NY County 2011); *see also Portfolio Recovery Assocs., LLC v King*, 14 NY3d 410, 416 (2010) (procedural matters are, however, governed by the law of the forum); *Tanges v Heidelberg N. Am., Inc.*, 93 NY2d 48, 53 (1999) (same). "Delaware law requires, generally, that as a condition precedent to a plaintiff bringing a shareholder derivative lawsuit, said plaintiff must make a pre-suit demand upon the board of directors to prosecute the contemplated action." *Simon v Becherer*, 7 AD3d 66, 71 (1st Dept 2004), citing *Aronson v Lewis*, 473 A2d 805, 811-812 (Del 1984), *overruled in part on other grounds by Brehm v Eisner*, 746 A2d 244 (Del 2000).

Under Delaware Chancery Court Rule 23.1 (a),

> "[i]n a derivative action brought by one or more shareholders or members to enforce the right of a corporation or of an unincorporated association, . . . the complaint shall allege . . . with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and the reasons for the plaintiff's failure to obtain the action or for not making the effort."[2]

[1]Section 19 of the LLC Agreement contains a choice of law provision that states: "This Agreement and the rights and liabilities of the parties hereunder shall be governed by and determined in accordance with the laws of the State of Delaware."

[2]"For the purposes of this Rule, an 'unincorporated association' includes a . . . limited liability company." Del. Ch. Ct. R. 23.1 (d). *See also* 6 Del C § 18-1001 (permitting member of limited liability company to bring a derivative action "if managers or members with authority to do so have refused to bring the action or if an effort to cause those managers to bring the action is not likely to succeed").

See American Intl. Group v Greenberg, 965 A2d 763, 808 (Del Ch 2009); *Brehm*, 746 A2d at 254.

"[U]nder Delaware law, as elsewhere, the requirement of a demand upon directors of a corporation to pursue a derivative complaint is a recognition of the inherent powers of the board to manage the affairs of the corporation, which includes making decisions about whether or not to pursue such litigation." *Wilson v Tully*, 243 AD2d 229, 232 (1st Dept 1998) (applying Delaware law); *see Sagarra Inversiones, S.L. v Cementos Portland Valderrivas, S.A.*, 34 A3d 1074, 1082 (Del 2011); *Zapata Corp. v Maldonado*, 430 A2d 779, 782 (Del 1980)[3]. "The purpose of pre-suit demand is to assure that the stockholder affords the corporation the opportunity to address an alleged wrong without litigation, to decide whether to invest the resources of the corporation in litigation, and to control any litigation which does occur." *Spiegel v Buntrock*, 571 A2d 767, 773 (Del 1990); *see In Re Delta and Pine Land Co. Shareholders Litig.*, 2000 WL 875421, *5, 2000 Del Ch LEXIS 98, *14-15 (Del Ch 2000); *see Braddock v Zimmerman*, 906 A2d 776, 784 (Del 2006); *Aronson*, 473 A2d at 811-812. Thus, the demand requirement "exists at the threshold to prevent abuse and to promote intracorporate dispute resolution." *Pogostin v Rice*, 480 A2d 619, 624 (Del 1984), *overruled in part on other grounds by Brehm*, 746 A2d at 254. It also "attempt[s] to balance the Delaware prerogative that directors manage the affairs of a corporation with the realization that shareholder policing, via derivative actions, is a necessary check on the behavior of directors that serve in a fiduciary capacity to shareholders." *Agostino v Hicks*, 845 A2d 1110, 1116-1117 (Del Ch 2004).

[3] "[C]ase law governing corporate derivative suits is equally applicable to suits on behalf of an LLC." *VGS, Inc. v Castiel*, 2003 WL 723285, *11, 2003 Del Ch LEXIS 16, *43 (Del Ch 2003).

A plaintiff asserting demand futility must set forth in the complaint particularized factual allegations sufficient to create a reasonable doubt that "(1) the directors are disinterested and independent and (2) the challenged transaction was otherwise the product of a valid exercise of business judgment." *Aronson v Lewis*, 473 A2d at 814; *see King v Verifone Holdings, Inc.*, 12 A3d 1140, 1146 (Del 2010); *Brehm*, 746 A2d at 256; *Simon*, 7 AD3d at 71-72; *see generally Security Police & Fire Professionals of Am. Retirement Fund v Mack*, 30 Misc 3d 663 (Sup Ct, NY County 2010) (discussing Delaware law), *affd* 93 AD3d 562 (1st Dept 2012). "The prongs of the *Aronson* test are in the disjunctive; therefore, if plaintiff creates a reasonable doubt as to either prong of the test, demand is excused." *Kahn v Portnoy*, 2008 WL 5197164, *9, 2008 Del Ch LEXIS 184, *35 (2008); *see MCG Capital Corp. v Maginn*, 2010 WL 1782271, *162010 Del Ch LEXIS 87, *59 (Del Ch 2010).

"Directorial interest exists whenever divided loyalties are present, or a director either has received, or is entitled to receive, a personal financial benefit from the challenged transaction which is not equally shared by the stockholders." *Pogostin*, 480 AD2d at 624 (internal citation omitted); *see Aronson*, 473 A2d at 812. "Directorial interest also exists where a corporate decision will have a materially detrimental impact on a director, but not on the corporation and the stockholders." *Rales v Blasband*, 634 A2d 927, 936 (Del 1993); *see Simon*, 7 AD3d at 72.

Further, "[a] director will be considered unable to act objectively with respect to a presuit demand if he or she is interested in the outcome of the litigation or is otherwise not independent." *Beam v Stewart*, 845 A2d 1040, 1049 (Del 2004). Delaware courts have long held "that if by reason of hostile interest or guilty participation in the wrongs complained of, the directors cannot be expected to institute suit, or if a suit is instituted it is apparent that the directors would not be

the proper persons to conduct it, no demand upon them to institute suit is requisite to enable a stockholder to sue in behalf of the corporation." *Miller v Loft, Inc.*, 153 A 861, 862 (Del Ch 1931); *see Fleer v Frank H. Fleer Corp.*, 125 A 411, 415 (Del Ch 1924); *cf Aronson*, 473 A2d at 814. "In such circumstances, a director cannot be expected to exercise his or her independent business judgment without being influenced by the adverse personal consequences resulting from the decision." *Rales*, 634 A2d at 936; *see Beam v Stewart*, 85 A2d at 1049.

In this case, plaintiffs did not make a pre-suit demand upon defendants. Instead, they allege that demand would have been futile and should be excused because defendants are the accused wrongdoers, are personally interested in the transactions at issue and the outcome of the litigation, and face a substantial likelihood of liability for the alleged wrongful conduct, which makes them personally interested in the outcome of the decision on whether to pursue litigation. Am. Complaint, ¶¶ 158-161. Plaintiffs also allege that defendants have openly opposed bringing a derivative action. *Id.*

Accepting the allegations of the amended complaint as true and giving plaintiffs the benefit of all favorable inferences, as the court is required to on a 3211 (a) (7) motion, the amended complaint alleges sufficiently particularized facts to create a reasonable doubt that defendants were disinterested or could have made an impartial decision about whether to institute litigation against themselves.

Nor does defendants' appointment of a special committee subsequent to the commencement of this litigation definitively demonstrate that demand would not have been futile. In *Zapata v Corp. v Maldonado*, the Delaware Supreme Court addressed the question of "[w]hen, if at all, should an authorized board committee be permitted to cause litigation, properly

initiated by a derivative stockholder in his own right, to be dismissed?" 430 A2d at 785. The Court did not hold that creation of a special committee demonstrated that demand was not excused. Rather, "[i]t held that even in a case where demand was excused and the initial decision of whether to litigate was not placed before it, the board of directors still retained all of its corporate powers concerning litigation decisions. . . . The underlying power to terminate the suit remained." *Abbey v Computer & Communications Tech. Corp.*, 457 A2d 368, 372 (Del Ch 1983). That is, as the Delaware Supreme Court explained in *Abbey*, "even where a board of directors was tainted with obvious self-interest, it nonetheless had the power . . . to delegate its authority to a committee of disinterested directors . . . to determine whether the pending suit brought on behalf of the corporation should be maintained or whether it was in the best interests of the corporation to have it discontinued." *Id.*

As courts also have found, "the act of establishing a special litigation committee constitutes an implicit concession by a board that its members are interested in the transaction." *Levine v Smith*, 591 A2d 194, 209 (Del 1991); *see Abbey*, 457 A2d at 374; *see also Sutherland v Sutherland*, 2008 WL 3021024, *1 n 1, 2008 Del Ch LEXIS 100, *2 n 1 (Del Ch 2008) (by appointing a special committee, defendants conceded self-dealing was adequately alleged, but did not concede self-dealing as a substantive matter).

Defendants also argue that the derivative claims should be dismissed because plaintiffs do not adequately represent the Fund and its other members. Defendants contend that the vast majority of the Fund's other members supported Arts India's proposed liquidation plan for the Fund and do not support this lawsuit, and that plaintiffs are seeking to extract a greater return

than what the other investors will get, and their interests, therefore, are antagonistic to the other members.

"Under Delaware law, a derivative action may be dismissed if the Court determines that the plaintiff is an inadequate representative of the company's other shareholders." *MCG Capital Corp.*, 2010 WL 1782271, at *22, 2010 Del Ch LEXIS 87, at *82-83 (citation omitted).

> "[T]he traditional factors that the Court considers to determine plaintiff's representative adequacy . . .. [include] (1) the existence of economic antagonisms between the plaintiff and the company's other shareholders, (2) the nature of the remedy sought, (3) indications that the plaintiff was not the driving force behind the litigation, (4) whether the plaintiff is familiar with the litigation, (5) the existence of other litigation pending between the plaintiff and defendants, (6) the relative magnitude of the plaintiff's personal interests as compared with its interest in the derivative action, (7) plaintiff's vindictiveness towards the defendants, and (8) the degree of support plaintiff receives from the other shareholders."

Id.; *see Youngman v Tahmoush*, 457 A2d 376, 379-380 (Del Ch 1983).

"Although these elements have been frequently combined to provide the basis for a court's decision to dismiss, often a strong showing of one factor which is actually inimical to the class, will permit the same conclusion." *Youngman*, 457 A2d at 380. The burden is on the defendant, however, to prove a plaintiff should be disqualified and defendant must "show a substantial likelihood that the derivative action is not being maintained for the benefit of the shareholders." *Emerald Partners v Berlin*, 564 A2d 670, 674 (Del Ch 1989) (citations omitted); *accord South v Baker*, 62 A3d 1, 22 (Del Ch 2012); *Bakerman v Sidney Frank Importing Co.*, 2006 WL 3927242, *10, 2006 Del Ch LEXIS 180, *34 (Del Ch 2006); *Khanna v McMinn*, 2006 WL 1388744, 2006 Del Ch LEXIS 86, *178-179 (Del Ch 2006). "Hypothetical or potential

conflicts of interest do not bar a plaintiff from acting as representative. Nor will a plaintiff with interests that go beyond the interests of the class be barred from acting as representative so long as the plaintiff's personal interests are coextensive with the class." *MCG Capital Corp.*, 2010 WL 1782271, at *22, 2010 Del Ch LEXIS 87, at *82-83.

In support of their contention that plaintiffs are the only members, out of 42, that have not agreed with the liquidation plan proposed for the Fund, defendants submit statements from approximately 35 members stating, generally, that they oppose the action brought by plaintiffs. *See* Statements, Ex. C to Gorchkova Aff. None of those statements, however, is verified and their veracity is challenged by plaintiffs. Even if the statements weigh in favor of finding that the majority of the Fund's other members do not support plaintiffs' action, they are insufficient at this stage to warrant dismissal. Defendants' contention that plaintiffs' economic interests are antagonistic to the other investors, because plaintiffs have individually sought settlements, also is not enough to disqualify plaintiffs.

The court thus turns to whether plaintiffs' claims otherwise can survive the instant motion to dismiss.

Breach of Contract (against Arts India)

Defendants assert that plaintiffs' breach of contract claim (as well as their fraudulent misrepresentation, misappropriation, conversion and unjust enrichment claims) is barred by the applicable six-year statute of limitations. The instant action was commenced in July 2013 and, therefore, defendants argue, any claims arising prior to July 2007 cannot be maintained.

A breach of contract cause of action "generally accrues at the time of the breach." *Hahn Automotive Warehouse, Inc. v American Zurich Ins. Co.*, 18 NY3d 765, 770 (2012); *accord*

Ely-Cruikshank Co. v Bank of Montreal, 81 NY2d 399, 402 (1993). "'[T]he Statute runs from the time of the breach though no damage occurs until later.'" *Id.* (citations omitted); *see Eli Intl., Inc. v Macy's W. Inc.*, 106 AD3d 442, 443 (1st Dept 2013); *Chelsea Piers L.P. v Hudson Riv. Park Trust*, 106 AD3d 410, (1st Dept 2013). However, "installment obligations . . . warrant different considerations and results under the Statute of Limitations' microscope." *Phoenix Aquisition Corp. v Campcore, Inc.*, 81 NY2d 138, 143 (1993). "'[W]here a contract provides for continuing performance over a period of time, each breach may begin the running of the statute anew such that accrual occurs continuously.'" *Beller v William Penn Life Ins. Co.*, 8 AD3d 310, 314 (2d Dept 2004) (citations omitted); *see Bulova Watch Co. v Celotex Corp.*, 46 NY2d 606, 611 (1979); *Meadowbrook Farms Homeowners Assn., Inc. v JZG Resources, Inc.*, 105 AD3d 820, 822 (2d Dept 2013); *New York Central Mut. Fire Ins. Co. v Glider Oil Co.*, 90 AD3d 1638, 1642 (4th Dept 2011); *Kerr v Brown*, 283 AD2d 343, 345 (1st Dept 2001). Plaintiffs may only recover damages, however, for those alleged breaches occurring up to six years prior to commencement of the action. *See Beller*, 8 AD3d at 314; *Bulova Watch Co.*, 46 NY2d at 612.

Plaintiffs entered into the LLC Agreement in March 2006. Their breach of contract claim against Arts India is based on allegations that, among other things, Arts India failed to make the required initial capital contribution, failed to issue quarterly reports, extended the Fund's dissolution date without authorization of a majority of the members, refused to provide access to complete set of books and records, charged excess management fees and received excess reimbursement of expenses, and failed to bear 20% of the Fund's losses. Am. Complaint, ¶ 170.

Defendants argue that the claim that defendants failed to make capital contributions accrued at the latest in March 2007, when three-quarters of the contribution should have been

paid. See LLC Agreement, § 6. As plaintiffs note, however, the final quarter of the contribution was due "during the eighteenth month after the execution of this Agreement," that is, in September 2007. Moreover, the agreement provides that the due dates for the second, third and fourth payments could be postponed by the Managing Member. *Id.* Defendants also argue that plaintiffs' claim that Arts India failed to distribute quarterly reports accrued at the start of the contract in March 2006. As plaintiffs contend, however, the obligation to provide quarterly reports continued throughout the life of the Fund. *See Bld Prods., LLC v Viacom, Inc.*, 2011 WL 1327340, *13, 2011 US Dist LEXIS 36486, *38-39 (SD NY 2011), *affd in part and vacated in part* 509 Fed Appx 81 (2d Cir 2013) (continuing obligation to issue accounting statement on semi-annual basis). Thus, as there are at least some timely allegations, the breach of contract cause of action survives the instant motion to dismiss.[4]

Fraudulent Misrepresentation (against all defendants)

Defendants seek dismissal of plaintiffs' fraud claims on the grounds that they are time-barred under CPLR 213 (7), fail to meet the pleading requirements of CPLR 3016 (b), cannot establish reliance, and are precluded by the out-of-pocket rule of damages.

Generally, under New York and Delaware law, "in a claim for fraudulent misrepresentation, a plaintiff must allege 'a misrepresentation or a material omission of fact which was false and known to be false by defendant, made for the purpose of inducing the other party to rely upon it, justifiable reliance of the other party on the misrepresentation or material omission, and injury.'" *Mandarin Trading Ltd. v Wildenstein*, 16 NY3d 173, 178 (2011),

[4]To the extent that defendants argued in their initial moving papers that the breach of contract claim is barred by the exculpatory provision of the LLC Agreement, defendants, in reply, appear to have abandoned that argument. *See* Defendants' Reply Memorandum of Law, at 5.

quoting *Lama Holding Co. v Smith Barney Inc.*, 88 NY2d 413, 421 (1996) (other citation omitted); *see Lord v Souder*, 748 A2d 393, 402 (Del 2000); *Sammons v Anderson*, 968 A2d 492, 492 n 11 (Del 2009); *Cohen PDC, LLC v Cheslock-Bakker Opportunity Fund, LP*, 2012 WL 4530242, 2010 NY Misc LEXIS 5382, *29, 2010 NY Slip Op 33108(U) (Sup Ct, NY County 2010) (applying Delaware and New York law), *affd* 94 AD3d 539 (1st Dept 2012). Further, fraud claims are subject to the heightened pleading requirements of CPLR 3016 (b), which provides that "the circumstances constituting the wrong shall be stated in detail." *See Mandarin Trading Ltd.*, 16 NY3d at 178; *Eurycleia Partners, LP v Seward & Kissel, LLP*, 12 NY3d 553, 559 (2009).

"In a fraudulent inducement claim, the alleged misrepresentation should be one of then-present fact, which would be extraneous to the contract and involve a duty separate from or in addition to that imposed by the contract, and not merely a misrepresented intent to perform." *Hawthorne Group, LLC v RRE Ventures*, 7 AD3d 320, 323-324 (1st Dept 2004) (internal citations omitted); *see Perrotti v Becker Glynn, Melamed & Muffly LLP*, 82 AD3d 495, 498 (1st Dept 2011); *Town House Stock LLC v Coby Hous. Corp.*, 36 AD3d 509, 509 (1st Dept 2007). A fraud claim that only alleges "fraudulent misrepresentations related to defendants' obligation under their agreements" may not be maintained. *RGH Liquidating Trust v Deloitte & Touche LLP*, 47 AD3d 516, 517 (1st Dept 2008); *see New York Univ. v Continental Ins. Co.*, 87 NY2d 308, 318 (1995); *Sound Communications, Inc. v Rack & Roll, Inc.*, 88 AD3d 523, 523-524 (1st Dept 2011); *Coppola v Applied Elec. Corp.*, 288 AD2d 41, (1st Dept 2001); *Orix Credit Alliance, Inc. v R.E. Hable Co.*, 256 AD2d 114, 115 (1st Dept 1998).

The statute of limitations for a fraud claim is "the greater of six years from the date the cause of action accrued or two years from the time the plaintiff . . . discovered the fraud, or could with reasonable diligence have discovered it." CPLR 213 (8); *see Kaufman v Cohen*, 307 AD2d 113, 122-123 (1st Dept 2003); *Ghandour v Shearson Lehman Bros.*, 213 AD2d 304, 305 (1st Dept 1995). Under CPLR 213 (7), a derivative action brought on behalf of a corporation on the ground of fraud, among other things, must be commenced within six years. Defendants argue that the discovery accrual rule in CPLR 213 (8) does not apply to fraud claims under CPLR 213 (7) because it is not included in the statutory provision. Defendants submit no legal authority to support their argument, and, to the contrary, there is some authority for finding that the discovery accrual rule does apply to fraud claims under CPLR 213 (7). *See Whitney Holdings v Givotovsky*, 988 F Supp 732, 744-745 (SDNY 1997) ("Despite the general rule that claims under . . . Section 213 (7) accrue upon breach rather than discovery, New York traditionally has excepted claims of fraud, which instead accrue only upon the plaintiff's actual or constructive discovery of the facts constituting the fraud."); *cf Kaufman*, 307 AD2d at 123 n 5.

Even assuming that the discovery accrual rule applies here, however, plaintiffs' claims that they were fraudulently induced into entering the LLC Agreement in March 2006 are untimely. Plaintiffs allege that, prior to investing in the Fund, Dutta represented to them that he would be able to purchase art at insider prices, which would provide greater protection for their investments, and he would form an Investors' Committee with oversight responsibilities. Am. Complaint, ¶ 173. These alleged statements occurred more than six years prior to commencement of this action, and there are no allegations that the truth of these statements could not have been discovered with reasonable diligence more than two years before the action was

commenced. It also appears that plaintiffs do not seriously dispute that these claims are untimely. *See* Plaintiffs' Memorandum of Law in Opposition to Defendants' Motion to Dismiss, at 12.

In any event, the alleged misrepresentations, in essence, amount to no more than predictions or promises in connection with the LLC Agreement. "They are simply statements of expectation or opinion about the future of the company and the hoped for results of business strategies. Such opinions and predictions are generally not actionable under Delaware [or New York] law." *Trenwick Am. Litig. Trust v Ernst & Young, L.L.P.*, 906 A2d 168, 209 (Del Ch 2006), *affd* 931 A2d 438 (Del 2007); *see Mandarin Trading Ltd.*, 16 NY3d at 179. Plaintiffs allege no misrepresentations of then-present facts and allege no facts to show that defendants entered into the contract with the intention not to perform it. The LLC Agreement also flatly contradicts plaintiffs' claim that defendants were required to create an Investors' Committee. By the terms of the LLC Agreement, the Managing Member was authorized to establish an Investors Committee, "at his discretion." LLC Agreement, § 11. Courts have "repeatedly held that a party claiming fraudulent inducement cannot be said to have justifiably relied on a representation when that very representation is negated by the terms of a contract executed by the allegedly defrauded party." *Perrotti v Becker Glynn, Melamed & Muffly LLP*, 82 AD3d 495, 498-499 (1st Dept 2011) (citations omitted).

Plaintiffs' allegations of fraudulent misrepresentations made after plaintiffs invested in the Fund cannot form the basis for claiming they were fraudulently induced into investing. *See High Tides, L.L.C. v DeMichele*, 88 AD3d 954, 958 (2d Dept 2011). As to plaintiffs' allegations that they were fraudulently induced into "continuing their investment in the Fund," these

allegations are largely duplicative of the breach of contract claims and otherwise are grounded "on the softest of turf." *Trenwick Am. Litig. Trust*, 906 A2d at 209.

As to whether plaintiffs have sufficiently alleged "out-of-pocket" damages, plaintiffs contend that they simply are seeking "the sum necessary for restoration to the position occupied before the commission of the fraud," consistent with recoverable fraud damages. Plaintiffs' Memo. of Law in Opp., at 21. Damages for fraudulent misrepresentation are limited to "the actual pecuniary loss sustained as the direct result of the wrong . . . or what is known as the out-of-pocket rule." *Lama Holding Co.*, 88 NY2d at 421 (quotation marks and citations omitted).

> "Under this rule, the loss is computed by ascertaining the difference between the value of the bargain which a plaintiff was induced by fraud to make and the amount or value of the consideration exacted as the price of the bargain. Damages are to be calculated to compensate plaintiffs for what they lost because of the fraud, not to compensate them for what they might have gained. Under the out-of-pocket rule, there can be no recovery of profits which would have been realized in the absence of fraud."

Id. (quotations marks and citations omitted); *see Starr Found. v American Intl. Group, Inc.*, 76 AD3d 25, 27 (1st Dept 2010).

That is, "the recovery of consequential damages naturally flowing from a fraud is limited to that which is necessary to restore a party to the position occupied before commission of the fraud." *Id.* at 423 (quotation marks and citation omitted); *see ESBE Holdings, Inc. v Vanquish Acquisitions Partners, LLC*, 50 AD3d 397, 398 (1st Dept 2008); *Orbit Holding Corp. v Anthony Hotel Corp.*, 121 AD2d 311, 315 (1st Dept 1986). "Plaintiffs' claims for damages stemming from other speculative uses of their monies, such as lost opportunities for investment, stock

appreciation and dividends, are also unavailable." *Johnson v Proskauer Rose, LLP*, 2014 WL 317839, *12, 2014 NY Misc LEXIS 405, 2014 NY Slip Op 30262(U) (Sup Ct, NY County 2014); *see Starr Found.*, 76 AD3d at 28. Similarly, "[c]laims based upon defendants' projections of returns on investment . . . are not actionable because such projections are merely statements of prediction or expectation." *ESBE Holdings, Inc.*, 50 AD3d at 398; *see Naturopathic Labs Intl., Inc. v SSL Ams., Inc.*, 18 AD3d 404, 404 (1st Dept 2005).

Plaintiffs assert that they are seeking out-of-pocket expenses, and with respect to those damages, they allege that they, and other members, have received only 32.5% of their initial capital investment and "stand to suffer significant additional losses." Am. Complaint, ¶ 155. In opposition to defendants' motion, plaintiffs do not otherwise identify what out-of-pocket expenses or actual pecuniary loss they are claiming, but assert that they are not seeking lost profits. The allegations, therefore, are not only lacking in specificity but appear to seek "to recover the value [they] hypothetically would have realized" for their investment in the absence of any alleged fraud. *Starr Found.*, 76 AD3d at 27. Further, as in *Starr*, plaintiffs, by continuing their investment, "did not lose or give up any value; rather, [they] remained in possession of the true value of the [membership units], whatever that value may have been at any given time." *Id.*, 76 AD3d at 28.

To the extent that plaintiffs contend that they seek as consequential damages the difference between the amount that they invested and the amount that they received back (*see Maisano v Beckoff*, 2 AD3d 412, 414 [2d Dept 2003] [awarding in a fraud claim, as out-of-pocket loss, "the difference between the amount which he invested and the amount which he received back"]), where, as here, those same damages are recoverable under a breach of contract

claim, the fraudulent misrepresentation claim is duplicative. *See Rockefeller Univ. v Tishman Constr. Corp.*, 240 AD2d 341, 342 (1st Dept 1997); *see Tag 380, LLC v ComMet 380, Inc.*, 40 AD3d 1, 8 (1st Dept 2007), *affd as modified* 10 NY3d 507 (2008) (fraudulent misrepresentation claim is duplicative of breach of contract cause of action where identical damages sought).

Breach of Fiduciary Duty (against Arts India)

Generally, Delaware courts recognize that managing members of a limited liability company owe a fiduciary duty to the company and its members. *See Feeley v NHAOCG, LLC*, 62 A3d 649, 660 (Del Ch 2012) (and cases cited therein). Under Delaware law, however, the parties to a limited liability company agreement are expressly permitted to modify the scope of those fiduciary duties. *See* Delaware Limited Liability Company Act (6 Del C § 18-101 et seq) (LLC Act) § 18-1101 (c) and (e). Section 18-1101 (c) of the LLC Act provides that a managing member's duties, including fiduciary duties, "may be expanded or restricted or eliminated by provisions in the limited liability company agreement." "In Delaware, as elsewhere, a court will give full force to the terms of a contract that diminishes the fiduciary duty of care a general partner owes the limited partners." *Aris Multi-Strategy Fund, L.P. v Accipiter Life Sciences Fund II (QP), L.P.*, 89 AD3d 454, 454-455 (1st Dept 2011) (citations omitted) (applying Delaware law);[5] *see Continental Ins. Co. v Rutledge & Co., Inc.*, 750 A2d 1219, 1235 (Del Ch 2000). "Accordingly, to decide fiduciary duty claims in the LLC context, the Court must closely examine and interpret the LLC's governing instrument to determine the parameters of the fiduciary relationship." *Zimmerman v Crothall*, 62 A3d 676, 701-702 (Del Ch 2013).

[5]"[T]he law in New York and Delaware law is the same with regard to the breach of fiduciary duty claim and the aiding and abetting a breach of fiduciary duty claim." *JFK Family Ltd. Partnership v Millbrae Natural Gas Dev. Fund 2005 L.P.*, 21 Misc 3d 1102 (A), *18 n 18 (Sup Ct, Westchester County 2008).

In this case, the LLC Agreement provides that the "Managing Member's duty of care in the discharge of the Managing Member's duties to the Limited Liability Company and the Members is limited to refraining from engaging in grossly negligent conduct, intentional misconduct, or a knowing violation of law." LLC Agreement, § 11. As the contract limits defendants' liability to losses caused by "gross negligence, intentional misconduct, or a knowing violation of laws," it serves "to exculpate defendants from breach of fiduciary duty claims that do not involve allegations of this misconduct." *Aris Multi-Strategy Fund, L.P.*, 89 AD3d at 455 (citations omitted).

"Gross negligence" has been defined by the Delaware Supreme Court as "a higher level of negligence representing 'an extreme departure from the ordinary standard of care.'" *Browne v Robb*, 583 A2d 949, 953 (Del 1990), *cert denied* 499 US 95 (1991) (citation omitted); *see Metropolitan Life Ins. Co. v Tremont Group Holdings., Inc.*, 2012 WL 6632681, *7, 2012 Del Ch LEXIS 287, *25 (Del Ch 2012). "Gross negligence has a stringent meaning under Delaware corporate (and partnership) law, one 'which involves a devil-may-care attitude or indifference to duty amounting to recklessness.'" *Albert v Alex. Brown Mgt. Servs., Inc.*, 2005 WL 2130607, *4, 2005 Del Ch LEXIS 133, *14 (Del Ch 2005) (citation omitted); *see Gelfman v Weeden Investors, L.P.*, 859 A2d 89, 114 (Del Ch 2004); *Solash v Telex Corp.*, 1988 WL 3587, *9, 1988 Del. Ch. LEXIS 7, *24 (Del Ch 1988).

"In the duty of care context with respect to corporate fiduciaries, gross negligence has been defined as a reckless indifference to or a deliberate disregard of the whole body of stockholders or actions which are without the bounds of reason." *Albert*, 2005 WL 2130607, at *4, 2005 Del Ch LEXIS 133, at *14 (internal quotation marks and citation omitted); *accord*

Tomczak v Morton Thiokol, Inc., 1990 WL 42607, *12, 1990 Del Ch LEXIS 47, *35 (Del Ch 1990); *see Cincinnati Bell Cellular Sys. Co. v Ameritech Mobile Phone Service of Cincinnati, Inc.*, 1996 WL 506906 at *14, 1996 Del Ch LEXIS 116, *42-43 (Del Ch 1996), *affd* 692 A2d 411 (Del 1997); *see also Stewart v BF Bolthouse Holdco, LLC*, 2013 WL 5210220, *10, 2013 Del Ch LEXIS 215, *32 (Del Ch 2013); *McPadden v Sidhu*,, 964 A2d 1262, 1274 (Del Ch 2008). Pleading gross negligence, in contrast to ordinary negligence, "requires the articulation of facts that suggest a *wide* disparity between the process the directors used . . . and that which would have been rational." *Guttman v Jen-Hsun Huang*, 823 A2d 492, 507 n 39 (Del Ch 2003) (emphasis in original). "'[T]o prevail on a claim of gross negligence, a plaintiff must plead and prove that the defendant was recklessly uninformed or acted outside the bounds of reason.'" *DiRienzo v Lichtenstein*, 2013 WL 5503034, *29, 2013 Del Ch LEXIS 242, *100 (Del Ch 2013) (citation omitted); *see Alex. Brown Mgt. Servs., Inc.*, 2005 WL 2130607, at *4, 2005 Del Ch LEXIS 133, at *14. Further, "[u]nder Delaware Law, when a duty sought to be enforced arises out of the parties' contractual relationship, and the same facts that underlie the contract claim also form the basis of plaintiff's fiduciary claim, the fiduciary claim is precluded." *Kagan v HMC-New York, Inc.*, 2010 WL 8470638, 2010 NY Misc LEXIS 6728, *16-17, 2010 NY Slip Op 33769 (Sup Ct, NY County 2010), citing *Gale v Bershad*, 1998 WL 118022, *5, 1998 Del Ch LEXIS 37, *20 (Del Ch 1998) (other citations omitted), *modified in part and affd in part* 94 AD3d 67 (1st Dept 2012).

The allegations underlying plaintiffs' breach of fiduciary claims are that Arts India transferred money from the Fund's banking account to pay part of its initial capital contribution (Am. Complaint, ¶¶ 51-53, 183); Arts India purchased art from artists represented by Dutta's

independent gallery and invested the Fund's money in art "that had a higher degree of appreciation when co-owned by Defendant Arts India acting independently and the Fund than when solely owned by the Fund" (*id.*, ¶¶ 119-124, 183); and Arts India and Dutta managed the distribution of art works during the wind-up process, while maintaining an interest as members in selecting works or art. *Id.*, ¶¶ 153, 183.

These allegations, even assuming them to be true, do not rise to the level of gross negligence or willful misconduct. The LLC Agreement both authorizes the Managing Member to manage the business and affairs of the Fund, and to be compensated, and permits the Managing Member to conduct other business activities independent of the Fund's activities. *See* LLC Agreement, § 11. Nor do the allegations that Arts India conducted other business that affected the Fund, and had a financial interest in the wind-up of the Fund demonstrate "a disabling conflict of interest." *In re Synthes, Inc. Shareholder Litig.*, 50 A3d 1022, 1035 (Del Ch 2012). As to the claim that Arts India improperly used the Fund's assets to pay its capital contribution, that allegation is based on plaintiffs' expert's belief that evidence that there was a transfer of funds from the Fund's account to Arts India's account and back to the Fund indicated that Arts India was wrongfully paying itself through the Fund's bank account. Am. Complaint, ¶ 53. This allegation, however, rests on speculation about the purpose of the transfers.

While, "[g]enerally, factual questions regarding whether or not a standard of care has been met are resolved later in the proceedings, not at the motion to dismiss stage . . . the Court may grant a motion to dismiss a claim where the plaintiffs have not adequately pled that the defendants' conduct constitutes a non-exculpated claim." *Metropolitan Life Ins. Co.*, 2012 WL 6632681, at *7, 2012 Del Ch LEXIS 287, at *24; *see Brinckerhoff v Enbridge Energy Co.*, 2012

WL 1931242, *2 n 11, 2012 Del Ch LEXIS 291, *6 n 11 (Del Ch 2012) (the court "may consider an exculpatory provision on a motion to dismiss"); *see also Wood v Baum*, 953 A2d 136, 141 (Del 2008) (a serious threat of liability may only be found if the plaintiff pleads a non-exculpated claim based on particularized facts). To the extent that plaintiffs allege that Arts India breached its fiduciary duty by failing to maintain the Fund's books and records, failing to create an Investors' Committee, obtaining a bank loan for the Fund to pay management fees, and receiving excess fees (Am Complaint, ¶ 183), those claims clearly arise out of the LLC agreement. "[B]ecause the contract claim addresses the alleged wrongdoing . . ., any fiduciary duty claim arising out of the same conduct is superfluous." *Gale*, 1998 WL 118022, at *5, 1998 Del Ch LEXIS 37, at *22; *see Nemec v Shrader*, 991 A2d 1120, 1129 (Del 2010).

In view of the finding that there is no viable claim for breach of fiduciary duty against Arts India, the cause of action for aiding and abetting such a breach as against Dutta and Shea also cannot be sustained. *See Kagan*, 94 AD3d at 73; *see Madison Realty Partners 7, LLC v AG ISA, LLC*, 2001 WL 406268, *6 n 19, 2001 Del Ch LEXIS 37, *21 n 19 (Del Ch 2001).

Misappropriation, Conversion, Unjust Enrichment(against Arts India)

Plaintiffs' causes of action for misappropriation and conversion are based on allegations that, in April and May 2006, Arts India transferred money from the Fund's bank account into its own account for its own use, including transfers of $45,000 and $5,600 in April 2006, and a $116,540 transfer in May 2006; and then transferred $125,000 back to the Fund's account to pay for Arts India's capital contribution to the Fund. Am. Complaint, ¶¶ 195-196, 202-203.

Conversion and misappropriation claims, when alleged in an action brought on behalf of a corporation, are subject to the six-year statute of limitations under CPLR 213(7). *See Matter of*

Skorr v Skorr Steel Co., Inc., 29 AD3d 594, 595 (2d Dept 2006) (misappropriation claim in shareholder derivative suit subject to six-year statute of limitations pursuant to 213[7]); *Toscano v Toscano*, 285 AD2d 590, 591 (2d Dept 2001) (claims of diversion of corporate assets and misappropriation of corporate assets in action against corporation subject to six-year statute of limitations). For statute of limitations purposes, accrual of a cause of action for conversion "runs from the date the conversion takes place and not from discovery or the exercise of diligence to discover the conversion." *Vigilant Ins. Co. of Am. v Housing Auth. of the City of El Paso, Texas*, 87 NY2d 36, 44-45 (1995), citing *Sporn v MCA Records, Inc.*, 58 NY2d 482, 488 (1983); *Varga v Credit-Suisse*, 5 AD2d 289 1st Dept 1958), *affd* 5 NY2d 865.

Further, when such claims seek money damages, including the return of misappropriated funds, and a fraud allegation is not essential to the claim, they are governed by the limitations period applicable to claims for injury to property. *See Powers Mercantile Corp. v Feinberg*, 109 AD2d 117, 119-120 (1st Dept 1985), *affd* 67 NY2d 981 (1986) (courts will not apply fraud statute of limitations to misappropriation claim where essence of claim is diversion of assets); *Pursnani v Stylish Move Sportswear, Inc.*, 92 AD3d 663, 664 (2d Dept 2012) (claims for waste of business assets and conversion, seeking money damages and not grounded in allegations of fraud are governed by [the three-year] limitations period applicable to injury to property); *see also Monaghan v Ford Motor Co.*, 71 AD3d 848, 850 (2d Dept 2010) (when fraud allegation is only incidental to the allegation of breach of fiduciary duty, and not essential to it, then the three-year statute of limitations will apply).

Moreover, neither misappropriation nor conversion can "be predicated on a mere breach of contract." *Kopel v Bandwidth Tech. Corp.*, 56 AD3d 320, 320 (1st Dept 2008). Plaintiffs'

misappropriation and conversion claims are largely duplicative of their breach of contract claim. Plaintiffs claim that defendants used the Fund's money, but returned most of it to the Fund, and the gist of the claim is that defendants failed to make their capital contribution as required under the LLC Agreement.

Similarly, in Delaware and New York, "[c]ourts developed unjust enrichment, or quasi-contract, as a theory of recovery to remedy the absence of a formal contract." *ID Biomedical Corp. v TM Technologies, Inc.*, 1995 WL 130743, *15, 1995 Del Ch LEXIS 34, *39 (Del Ch 1995); see *Goldman v Metropolitan Life Ins. Co.*, 5 NY3d 561, 572 (2005); *Bakerman v Sidney Frank Importing Co., Inc.*, 2006 WL 3927242, *18, 2006 Del Ch LEXIS 180, *66 (Del Ch 2006). "A claim for unjust enrichment is not available if there is a contract that governs the relationship between parties that gives rise to the unjust enrichment claim." *Kuroda v SPJS Holdings, L.L.C.*, 971 A2d 872, 891 (Del Ch 2009); *see Bakerman*, 2006 WL 3927242, at *18, 2006 Del Ch LEXIS 180, at *66; *ID Biomedical Corp.*, 1995 Del Ch LEXIS 34, at *39, 1995 WL 130743, at *15; *Pappas v Tzolis*, 20 NY3d 228, 234 (2012); *IDT Corp. v Morgan Stanley Dean Witter & Co.*, 12 NY3d 132, 142 (2009); *see also Collins & Aikman Corp. v Stockman*, 2009 WL 1530120, *27, 2009 US Dist LEXIS 43472, *88-89 (D Del 2009) ("Neither Delaware nor New York law permit an unjust enrichment claim where a legally enforceable contract governs the relationship between the parties."). "This is the case even when the enforceable contract gives rise to a fiduciary relationship between the parties." *Bakerman*, 2006 WL 3927242, at *18, 2006 Del Ch LEXIS 180, at *66.

Plaintiffs allege against Arts India that it was unjustly enriched because it claimed the benefits of membership in the Fund without paying for them, used the Fund's money to fund its

capital contribution, and failed to contribute additional required capital. Am. Complaint, ¶¶ 210-212, 214. As these claims arise out of the contract governing the parties' relationship, the unjust enrichment cause of action is precluded.

Accounting (against Arts India)

Plaintiffs, as individual members of the Fund, seek an "immediate accounting of the Fund, including the financial state and affairs, assets, sales and purchases, net profits, net losses, and distributions of the Fund." Am. Complaint, ¶ 166.

Under Delaware law, "[a]n accounting is an equitable remedy that consists of the adjustment of accounts between parties and a rendering of a judgment for the amount ascertained to be due to either as a result." *Jacobson v Dryson Acceptance Corp.*, 2002 WL 3151109, 2002 Del Ch LEXIS 4, *12-13 (Del Ch 2002), *affd* 826 A2d 298 (Del 2003); *see Alex. Brown Mgt., Servs., Inc.*, 2005 WL 2130607, at *11, 2005 Del Ch LEXIS 133, at *40-41. Also, under Delaware law, it "is not so much a cause of action as it is a form of relief." *Rhodes v Silkroad Equity, LLC*, 2007 WL 2058736, *11, 2007 Del Ch LEXIS 96, *43 (Del Ch 2007); *see MCG Capital Corp.*, 2010 WL 1782271, at *25, 2010 Del Ch LEXIS 87, at *93 (claim for an accounting was "really a remedy pled as a cause of action"). Where one or more causes of action survive a motion to dismiss, plaintiffs "may proceed with their secondary claims," such as a claim for an accounting. *AQSR India Private, Ltd. v Bureau Veritas Holdings, Inc.*, 2009 WL 1707910, *14, 2009 Del Ch LEXIS 105, *46-47 (Del Ch 2009). "As it is a remedy, should the plaintiffs ultimately be successful on one or more of their claims, the court will address their arguments for granting an accounting." *Alex. Brown Mgt. Servs.*, 2005 WL 2130607, at *11, 2005 Del Ch LEXIS 133, at *41; *see MCG Capital Corp.*, 2010 WL 1782271, at *25, 2010 Del

Ch LEXIS 87, at *93-94. The court, therefore, does not reach the question of whether, under Delaware law, an accounting can ever be maintained as an independent cause of action.

Accordingly it is

ORDERED that defendants' motion to dismiss the complaint is granted in part and denied in part and the third, fourth, fifth, sixth, seventh and eighth causes of action are dismissed; and it is further

ORDERED that the remaining claims are severed and shall continue.

Dated: April 8, 2014

ENTER:

J.S.C.

MELVIN L. SCHWEITZER