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SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: GEORGE J. SILVER Justice PART 10

Index Number : 102715/2009
FEDERAL INSURANCE COMPANY
vs
GRAUMAN, KEVIN D.
Sequence Number : 003
SUMMARY JUDGMENT

INDEX NO. _____
MOTION DATE _____
MOTION SEQ. NO. _____

The following papers, numbered 1 to _____, were read on this motion to/for _____

Notice of Motion/Order to Show Cause — Affidavits — Exhibits _____ | No(s). _____

Answering Affidavits — Exhibits _____ | No(s). _____

Replying Affidavits _____ | No(s). _____

Upon the foregoing papers, it is ordered that this motion is

RECEIVED
DEC 23 2014
GENERAL CLERK'S OFFICE
NYS SUPREME COURT - CIVIL

MOTION IS DECIDED IN ACCORDANCE WITH THE ACCOMPANYING MEMORANDUM DECISION

FILED
DEC 24 2014
NEW YORK
COUNTY CLERK'S OFFICE

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE
FOR THE FOLLOWING REASON(S):

Dated: DEC 23 2014

George J. Silver
_____, J.S.C.
GEORGE J. SILVER

1. CHECK ONE: ..... ☑ CASE DISPOSED ☐ NON-FINAL DISPOSITION
2. CHECK AS APPROPRIATE: .....MOTION IS: ☑ GRANTED ☐ DENIED ☐ GRANTED IN PART ☐ OTHER
3. CHECK IF APPROPRIATE: ..... ☐ SETTLE ORDER ☐ SUBMIT ORDER
☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

[* 2]

[* 3]

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 10

----------X

FEDERAL INSURANCE COMPANY,

Plaintiff,

Index No. 102715-2009

-against-

DECISION/ORDER

Motion Sequence 003

KEVIN D. GRAUMAN,

Defendant.

----------X

HON. GEORGE J. SILVER, J.S.C.

Recitation, as required by CPLR § 2219 [a], of the papers considered in the review of this motion:

Papers	Numbered
Notice of Motion/Order to Show Cause, Affirmation, Affidavit & Exhibits Annexed, Memorandum of Law	1, 2, 3, 4
Answering Affirmation, Affidavit(s) & Exhibits	5
Replying Memorandum of Law	6

Plaintiff Federal Insurance Company's (plaintiff) amended complaint alleges that plaintiff obtained a judgment on or about January 29, 2008 against The Outsource Group, LLC, a California limited liability company authorized to transact business in New York (Outsource), for certain unpaid Worker's Compensation deductibles in the amount of $435,564.79. The complaint further alleges that Outsource has not satisfied the judgment and that, following the April 17, 2008 turnover of $44,282.53 held in an Outsource bank account, there remains due and owing from Outsource $391,282.26. Plaintiff alleges that defendant Kevin D. Grauman (defendant), a California resident, is a principal and member of Outsource and the principal and sole shareholder of Payroll & Benefits Experts, Inc (Payroll) and that Payroll is a member of Outsource. Plaintiff's first cause of action alleges that defendant retained the proceeds from the July 1, 2006 sale of Outsource's assets and that such retention constitutes a violation of New York Limited Liability Company Laws §§ 508, 704 and 1005. The second cause of action alleges that defendant's retention of the distribution from Outsource constitutes a violation of California Corporations Code §§ 17254, 17255 and 17353.

Defendant now moves by notice of motion dated May 15, 2014 for an order granting him summary judgment dismissing plaintiff's complaint in its entirety. Defendant opposes the motion.

In support of the motion, defendant avers that he was not a member of Outsource in 2005,

2006 or any time thereafter. Plaintiff further avers that the Asset Purchase Agreement dated June 30, 2006 in which the assets of Outsource were sold to an entity called TriNet, lists defendant and an individual named Kevin Correa as manager of Outsource and Correa and Payroll as its members. Defendant claims that the only payments made to him by Outsource following the asset sale were for the reimbursement of business expenses accrued by defendant.

Defendant further avers that there were no transfers of money between Payroll and himself and that the monies received by Payroll from Outsource's asset sale were used by it for investment in an entity called Emportal, Inc. (Emportal), a California corporation owned by Payroll and Mark Robinson. According to defendant, he was CFO and Chairman of Emportal from 1006 through 2009. Defendant claims that Payroll is a functionally independent corporation engaged primarily in the holding of an investment in Emportal, that it has an independent corporate existence and maintains all required corporate formalities, including the filing of federal and California state taxes and the holding of all appropriate business licenses, authorizations and permits.

With respect to Outsource, defendant contends that as a manager only, he did not have authority under Outsource's operating agreement to effectuate transfers from Outsource's asset sale. Defendant further claims that when Outsource distributed the funds from its assets sale, he did not know or believe that such distributions did or would cause Outsource to be unable to pay its debts. Specifically, defendant claims that the liabilities of Outsource did not exceed its assets following the distributions. Defendant also claims that plaintiff's initial suit against Outsource was the only one defendant knew of at the time of Outsource's asset sale and subsequent distributions. That litigation, according to defendant, was deemed to be the subject of a substantial setoff and defendant believed that the exposure in that action was limited to $50,000, which was included in the schedules of the asset purchase agreement.

In opposition, plaintiff, through an affirmation of its attorney, argues that the distributions from Outsource to Payroll rendered Outsource insolvent and claims that the transfer of Payroll's distribution from Outsource's asset sale to Emportal was an obvious attempt by defendant to insulate himself from potential liabilities arising out of Outsource's insolvency. Plaintiff also argues that defendant, as sole shareholder of Payroll, the majority owner of Outsource, exercised control over Outsource for his own benefit and that, pursuant to the alter ego doctrine, defendant should be held personally liable for Outsource's outstanding judgment.

To obtain summary judgment, the movant must establish its cause of action or defense sufficiently to warrant the court as a matter of law in directing judgment in its favor (CPLR § 3212 [b]; *Bendik v Dybowski*, 227 AD2d 228 [1st Dept 1996]). This standard requires that the proponent of a motion for summary judgment make a *prima facie* showing of entitlement to judgment as a matter of law by advancing sufficient "evidentiary proof in admissible form" to demonstrate the absence of any material issues of fact (*Winegrad v New York Univ. Med. Ctr.*, 64 NY2d 851, 853, 476 NE2d 642, 487 NYS2d 316 [1985]; *Zuckerman v City of New York*, 49 NY2d 557, 562, 404 NE2d 718, 427 NYS2d 595 [1980]; *Silverman v Perlbinder*, 307 AD2d 230 [1st Dept 2003]; *Thomas v Holzberg*, 300 AD2d 10, 11 [1st Dept 2002]). Thus, the motion must be supported "by affidavit [from a person having knowledge of the facts], by a copy of the pleadings and by other available proof, such as depositions" (CPLR § 3212 [b]).

To defeat a motion for summary judgment, the opposing party must show facts sufficient

to require a trial of any issue of fact (CPLR § 3212 [b]). Thus, where the proponent of the motion makes a prima facie showing of entitlement to summary judgment, the burden shifts to the party opposing the motion to demonstrate by admissible evidence the existence of a factual issue requiring a trial of the action, or to tender an acceptable excuse for his or her failure to do so (*Vermette v Kenworth Truck Co.*, 68 NY2d 714, 717, 497 NE2d 680, 506 NYS2d 313 [1986]; *Zuckerman*, 49 NY2d at 560, 562; *Forrest v Jewish Guild for the Blind*, 309 AD2d 546 [1st Dept 2003]). Like the proponent of the motion, the party opposing the motion must set forth evidentiary proof in admissible form in support of his or her claim that material triable issues of fact exist (*Zuckerman*, 49 NY2d at 562). The opponent "must assemble and lay bare [its] affirmative proof to demonstrate that genuine issues of fact exist" and "the issue must be shown to be real, not feigned, since a sham or frivolous issue will not preclude summary relief" (*Kornfeld v NRX Technologies, Inc.*, 93 AD2d 772 [1st Dept 1983], *affd*, 62 NY2d 686, 465 NE2d 30, 476 N.Y.S.2d 523 [1984]). Mere conclusions, expressions of hope or unsubstantiated allegations or assertions are insufficient (*Alvord and Swift v Stewart M. Muller Constr. Co.*, 46 NY2d 276, 281-82, 385 NE2d 1238, 413 NYS2d 309 [1978]; *Fried v Bower & Gardner*, 46 NY2d 765, 767, 386 NE2d 258, 413 NYS2d 650 [1978]; *Plantamura v Penske Truck Leasing, Inc.*, 246 AD2d 347 [1st Dept 1998]). Summary judgment is a drastic remedy that should only be employed where no doubt exists as to the absence of triable issues (*Leighton v Leighton*, 46 AD3d 264 [1st Dept 2007]). The key to such procedure is issue-finding, rather than issue-determination (*id.*).

As an initial matter, plaintiff's first cause of action alleging a violation by defendant of Limited Liability Company Law §§ 508, 704 and 1005 is dismissed. Under New York law, the laws of the jurisdiction under which a foreign limited partnership and foreign limited liability company are organized govern, respectively, the liability of limited partners in a limited partnership, and the members and managers of a limited liability company (*see* Limited Liability Company Law § 801; *Treeline 1 OCR, LLC v Nassau County Indus. Dev. Agency*, 82 AD3d 748 [2d Dept 2011]). It does not appear from the parties' submissions that there is any dispute that California law applies to the claims asserted against defendant. In fact, plaintiff concedes paragraph 24 of its amended complaint that application of California law is proper under Limited Liability Company Law § 801. Accordingly, plaintiff's first cause of action is dismissed.

Prior to its repeal in 2014, California Corporations Code § 17254 [a] stated "No distribution shall be made if, after giving effect to the distribution, either of the following occurs: (1) The limited liability company would not be able to pay its debts as they become due in the usual course of business. (2) The limited liability company's total assets would be less than the sum of its total liabilities plus, unless the operating agreement provides otherwise, the amount that would be needed, if the limited liability company were to be dissolved at the time of the distribution, to satisfy the preferential rights of other members upon dissolution that are superior to the rights of the member receiving the distribution." A member of a limited liability company was obligated by subsection Corporations Code § 17354 [e] "to return a distribution from limited liability company to the extent that (1) the member or assignee had actual knowledge of facts indicating the impropriety of the distribution . . . ." Even accepting as true plaintiff's claim that the distribution bu Outsource to Payroll left Outsource unable to pay its debts, defendant's affidavit establishes prima facie that defendant was not a "member or an assignee of a member"

as used in the statute and, more importantly, that he did not receive a distribution in his personal capacity from the proceeds of the sale of Outsource's assets. Moreover, the statute provides that a member who has actual knowledge of the impropriety of a distribution must return the distribution. While defendant denies knowing that the distribution from Outsource to Payroll would leave Outsource insolvent, even if defendant did receive a such distribution with knowledge of its impropriety, the remedy is not to hold defendant personally liable for Outsource's judgment but to require defendant to return the distribution. Thus, there is no basis for holding defendant personally liable under Corporations Code § 17254.

California Corporations Code § 17255, which was also repealed in 2014, provides that "a member or manager who votes for a distribution in violation of the operating agreement or Section 17254 or 17353 is personally liable to the limited liability company for the amount of the distribution that exceeds what could have been distributed without violating Section 17254 or 17353 or the operating agreement if it is established that the member or manger did not act in compliance with Section 17254 or 17353. This statute also does not provide a basis for holding defendant personally liable for Outsource's judgment's debt. Again, accepting as true plaintiff's allegation that the distribution in question left Outsource insolvent, plaintiff has not rebutted defendant's prima facie showing that defendant, as manager of Outsource, did not have authority under Outsource's operating agreement to vote for the distribution. Further, as with Corporations Code § 17354, section 17255 does not provide for the personal liability of a member or manager to a third-party judgment creditor when the member of manager votes for an improper distribution. Rather, section 17255 holds such a member or manager personally liable to the limited liability company.

Finally, California Corporations Code § 17353, by its plain terms, applies to limited liability companies "in the process of winding up." Plaintiff has not rebutted defendant's prima facie showing that Outsource continues to exist.

As to plaintiff's claim that defendant can be held personally liable under the alter ego doctrine, California law provides that under this doctrine a court may disregard the corporate entity and treat the corporation's acts as if they were done by the persons actually controlling the corporation where the corporation is used by an individual or individuals to perpetrate fraud, circumvent a statute, or accomplish some other wrongful or inequitable purpose (*Toho-Tawa Co., Ltd. v Morgan Creek Productions, Inc.*, 217 Cal.App.4th 1096 [CA Court of Appeal, Second Appellate District, Division Five 2013]). Disregard of the corporate entity is usually sought in order to fasten liability upon individual stockholders and because society recognizes the benefits of allowing persons and organizations to limit their business risks through incorporation, California public policy dictates that imposition of alter ego liability be approached with caution (*id.* [internal citations omitted]).

Other than alleging that defendant is a principal and member of Outsource, the principal and sole shareholder of Payroll and that Payroll is a member of Outsource, plaintiff's complaint does not allege any facts that would support an alter ego theory. There are no allegations in the complaint that defendant exercised complete domination of the corporation in respect to the transaction attacked or that such domination was used to commit a fraud or wrong against the plaintiff which resulted in plaintiff's injury. Moreover, the conclusory assertions by plaintiff that defendant benefitted from the distribution from Outsource to Payroll and that defendant

exercised control over Outsource for his own benefit because he was both the majority member of Outsource and the sole shareholder of Payroll do not raise a triable issues of fact. "Alter ego will not be applied absent evidence that an injustice would result from the recognition of separate corporate entities and [d]ifficulty in enforcing a judgment or collecting a debt does not satisfy this standard" (*Virtualmagic Asia, Inc. v Fil-Cartoons, Inc.*, 99 Cal.App.4th 228, 245 [Ca Court of Appeal, Fourth Appellate District, Division One 2002]). Accordingly, it is hereby

ORDERED that defendant's motion for summary judgment is granted and the complaint against him is dismissed in its entirety; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly; and it is further

ORDERED that defendant is to serve a copy of this order, with notice of entry, upon plaintiff within 20 days of entry.

Dated: DEC 23 2014
New York County

George J. Silver J.S.C.

GEORGE J. SILVER

FILED

DEC 24 2014

NEW YORK
COUNTY CLERK'S OFFICE