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| Deane v Starrett City, Inc. |
| 2018 NY Slip Op 30000(U) |
| January 2, 2018 |
| Supreme Court, New York County |
| Docket Number: 656087/2017 |
| Judge: Saliann Scarpulla |
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 39

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DISQUE DEANE, KATHRYN DEANE, MARJORIE DEANE
SWAIN, WALTER DEANE, DEANE FAMILY TRUST U/A DTD
7/31/66 F/B/O DISQUE D. DEANE, JR., DEANE FAMILY
TRUST U/A DTD 7/31/66 F/B/O KATHRYN M. DEANE, DEANE
FAMILY TRUST U/A DTD 7/31/66 F/B/O MARJORIE G. DEANE,
DEANE FAMILY TRUST U/A DTD 7/31/66 F/B/O WALTER L.
DEANE, STARRETT CITY AFFORDABLE LP LLC,

INDEX NO. 656087/2017

MOTION SEQ. NO. 001

DECISION AND ORDER

Plaintiff,

- v -

STARRETT CITY, INC., DD SPRING CREEK, LLC, SK SPRING
CREEK LLC, STARRETT CITY ASSOCIATES, LP, SPRING
CREEK PLAZA, LLC, SC LP SHOPPING CENTER LLC, DD
SHOPPING CENTER LLC, SK SHOPPING CENTER LLC,

Defendant.

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The following e-filed documents, listed by NYSCEF document number 2, 28, 51, 53, 54, 55, 56, 57, 58,
59, 60, 61, 62, 63, 64, 65, 66, 67, 68, 69, 70, 71, 72, 73, 74, 75, 76, 77, 79, 80, 81, 82, 83, 84, 85, 86,
87, 88, 89, 90, 91, 92, 93, 94, 95, 96, 97, 98, 99, 100, 101, 102, 103, 108, 109, 110, 111, 112, 113,
114, 115, 116, 117, 118, 119, 120, 125, 126

were read on this application to/for PREL INJUNCTION/TEMP REST ORDR

HON. SALIANN SCARPULLA:

In this action for breaches of fiduciary duty, plaintiffs Disque D. Deane, Jr., Kathryn M.
Deane, Marjorie G. Deane Swain, Walter L. Deane, Deane Family Trust U/A DTD
7/31/66 F/B/O Disque Deane, Jr., Deane Family Trust F/B/O Kathryn M. Deane, Deane
Family Trust F/B/O Marjorie G. Deane, Deane Family Trust F/B/O Walter L. Deane,
(collectively, the "Deane Family"), Patrick A. Gerschel, individually and as trustee of the
Gerschel Living Trust ("Gerschel"), and Starrett City Affordable LP LLC ("SCA") move

for a preliminary injunction enjoining any steps taken to consummate a sale of Spring Creek Towers a/k/a Starrett City (“Starrett City”).

Background

Starrett City is the largest federally subsidized housing project in the United States. Defendant Starrett City Associates, L.P. (“Partnership”) is a New York limited partnership that was organized in 1972 to develop and operate Starrett City, and the Partnership operates under a partnership agreement that has been amended several times since then (“Partnership Agreement”).

As part of a refinancing in 2009, Starrett City’s ownership and management structure was bifurcated into residential and commercial portions. The Partnership owns 100% of the equitable interest in the residential portion of Starrett City. Defendant Starrett City, Inc. (“Housing Company”) is a managing general partner of the Partnership with legal title to Starrett City, and defendants DD Spring Creek LLC and SK Spring Creek LLC are also managing general partners of the Partnership with ownership interests in it (collectively, “Managing General Partners”).

Defendant Spring Creek Plaza, LLC (“Commercial Owner”) owns 100% of the equitable interest in the commercial portion of Starrett City. Defendants DD Shopping Center LLC and SK Shopping Center LLC (collectively, “Controlling Members”) control and manage the Commercial Owner. Controlling Members are also members of Defendant SC LP Shopping Center LLC, which is a member of the Commercial Owner.

Carol Deane (“Deane”) is president of the Housing Company, the Partnership’s Managing General Partners, and the Commercial Owner’s Controlling Members (collectively, “MGPs”).

Deane Family, Gerschel, and SCA (collectively, “Dissenting Limited Partners”) own interests in the Partnership as limited partners and also own parallel interests in the Commercial Owner as beneficial owners through SC LP Shopping Center LLC.¹ However, unlike the Deane Family and Gerschel, who own interests with certain voting rights, SCA’s interest is solely economic. Belveron Real Estate Partners, through Belveron Partners Fund IV JV, LLC and LP Solutions Fund, LLC (collectively, “Belveron”), owns SCA.

On May 9, 2017, Deane, on behalf of the MGPs, entered into a Listing Agreement with Cushman & Wakefield for the sale of Starrett City. The agreement specifies that Douglas Harmon is the broker for the sale (“Broker”). In a June 30, 2017 letter, the MGPs notified the Partnership’s limited partners that it was “reviewing [] various restructuring alternatives, including . . . a sale of [Starrett City] or a refinancing.” As stated in the letter, exploring restructuring opportunities were time sensitive because a balloon payment would be due on Starrett City’s existing mortgage on January 1, 2020. In assessing refinancing as an option, Deane attests that the MGPs ultimately decided to sell Starrett City because a sale, unlike a refinancing, would resolve phantom tax issues that many of the Partnership’s limited partners faced.

¹ Deane Family’s, Gerschel’s, and SCA’s respective ownership interests are 3.395 percent, 1.9 percent, and 12.005 percent.

In evaluating a sale, Deane attests that the Broker advised a confidential sale process because the sale would require government approval, and the media and various constituencies would play into that outcome. Deane further attests to how Starrett City, as a complex and regulated real estate asset, complicated the sale process by way of prior transactions and other examples. Deane states that, with these considerations in mind, the Broker and MGPs proceeded with an unpublicized marketing process, whereby some of the identified qualified investors, including Belveron, were informally floated the idea to purchase.

On July 8, 2017, the MGPs received a letter of intent to purchase Starrett City from Brooksville Company LLC and Rockpoint Fund Acquisitions, L.L.C. (“Purchaser”) for \$905 million. Deane attests that, although the Purchaser’s offer hastened the sale process, she considered it attractive because the Purchaser intended to preserve Starrett City as an affordable housing complex, understood the challenges Starrett City presented, had experience with transactions that require government approval, presented a fair and satisfactory purchase price,² and eventually included additional negotiated concessions.

In a July 14, 2017 letter (“July 2017 Letter”), the MGPs again notified the Partnership’s limited partners that it was “reviewing [] options for a recapitalization” and further explained that it hired Broker to “explore a refinancing or sale of [Starrett City].” The July 2017 Letter did not include any information about the Purchaser’s offer but

² As stated by Deane, the purchase price of Starrett City presented a “just right” problem, in which the MGPs sought a purchase price that was low enough to receive government approval but also high enough to satisfy interest holders. This, in addition to other considerations, influenced Deane and the MGPs to forego a fairness opinion.

“[l]ooking ahead,” it reminded limited partners “that these actions will require a 51% approval of the limited partnership interests before finalization and execution[.]”³

Ultimately, on September 5, 2017, the Housing Company, the Partnership, and the Commercial Owner entered into a Purchase and Sale Agreement (“PSA”) with the Purchaser for the sale of Starrett City for an aggregate gross sale price of \$905 million. The next day, Belveron tendered an offer to purchase Starrett City for the same price. Despite the offer, on September 7, 2017, the Partnership sought the consent of its limited partners with a voting right to approve the PSA, and the Commercial Owner also sought the consent of its admitted beneficial owners (“Consent Solicitation”).⁴ The Consent Solicitation stated that the MGPs “received a competing offer to purchase” but “believes that the terms [with the Purchaser] are superior.” The Consent Solicitation provided a description of the transaction, including a summary of the terms and conditions, and other factors to consider.⁵

³ The Partnership Agreement, as amended, provides that the MGPs’ ability to “sell . . . the Partnership beneficial ownership” requires “the prior written consent of 51 percent in interest of the Limited Partners.” Similarly, the organizational documents of the Commercial Owner require the prior consent of 51 percent of each class of admitted beneficial owners.

⁴ MGPs provided interest holders without a right to vote a copy of the Consent Solicitation for informational purposes.

⁵ Specifically, the Consent Solicitation informed the limited partners and beneficial owners of a “a gross sale price of not less than \$850 million” for the residential portion and “a gross sale price of not less than \$30 million” for the commercial portion. Attached as an exhibit, the Consent Solicitation further provided the estimated net distributable proceeds. The Consent Solicitation provided the limited partners until September 25, 2017 to vote, which was subsequently amended to September 28, 2017.

On September 16, 2017, Belveron sent the MGPs a second offer to purchase Starrett City on identical terms as the Purchaser in addition to paying \$25 million more than the Purchaser or, in the alternative, to purchase the interests of MGPs and limited partners that wanted to sell. SCA alleges that it requested the MGPs to reevaluate their recommendation regarding Belveron's offer and revise the Consent Solicitation. Instead, the Partnership and Commercial Owner proceeded with the transaction and notified the Purchaser that, as of September 17 and September 18, 2017, the necessary consents from the Consent Solicitation were received.

The Dissenting Limited Partners allege that the Consent Solicitation contains material disclosure failures. Specifically, the Dissenting Limited Partners allege that the Consent Solicitation (1) failed to discuss MGPs' recapitalization efforts other than an asset sale, such as a refinancing; (2) mislead limited partners by characterizing the sale as a "result of a targeted and customized marketing process" when MGPs only negotiated with Purchaser; (3) failed to include or provide access to the PSA as part of the Consent Solicitation; and (4) lacked sufficient detail about the MGPs' conflict in the transaction, whereby the MGPs will earn additional compensation pursuant to the Partnership Agreement in the event of a successful sale.⁶

⁶ Pursuant to an amendment of the Partnership Agreement that was approved by 51% of the limited partners in 2003, the MGPs will receive a residual interest from the sale in the form of contingent management compensation of 19.9% of distributions. When distributions are made, the contingent compensation is paid to the MGPs, and then the distributions are paid to the limited partners and beneficial owners. Otherwise, Deane "unequivocally [attests] that there is no existing or future relationship between the MGPs and the Purchaser, and no monetary or other incentive" that creates a conflict.

Though the Consent Solicitation indicated that the PSA “is available for [the limited partner’s] review at the Partnership’s offices[,]” the Dissenting Limited Partners allege that an in-person review denied them meaningful review for informed consent. In response to complaints, on September 20, 2017, MGPs informed limited partners that access would soon be available via a confidential online database. Counsel for Gerschel claims that the nondisclosure agreement necessary to access the online database was unreasonable.

On September 28, 2017, the Deane Family and SCA filed a verified complaint.⁷ The complaint alleges that, in addition to the disclosure failures in the Consent Solicitation, the sale price in the PSA substantially undervalues Starrett City, and a more public bidding process would have garnered a higher sale price. Plaintiffs assert three causes of action: (1) breach of fiduciary duty of loyalty; (2) breach of fiduciary duty of candor and disclosure; and (3) breach of fiduciary duty of care. Plaintiffs seek to (a) permanently enjoin the certification of the Consent Solicitation and PSA consummation; (b) declare that MGPs breached their fiduciary duties and void consents pursuant to such breaches; or, in the alternative, (c) void any steps taken to consummate the PSA; or, in the alternative, (d) damages for the fair market value of the interests.

Deane attests that no limited partner who voted has asked to retract his/her/its consent despite the filing of the complaint in this action. As of September 29, 2017, the individual responsible for tallying the Consent Solicitation (“Vote Tracker”) attests that

⁷ Gerschel subsequently intervened in the action as a plaintiff, and Purchaser as a defendant.

more than 70% of the limited partners and beneficial owners in each class entitled to vote for the Partnership and Commercial Owner approved the PSA.⁸

This motion for a temporary restraining order and preliminary injunction to enjoin any steps taken to consummate the PSA was brought on by order to show cause dated September 28, 2017. I denied a temporary restraining order, and the parties returned on November 1, 2017 for a preliminary injunction hearing. This decision and order addresses plaintiffs' application for a preliminary injunction.

Discussion

Dissenting Limited Partners allege two wrongs: 1) disclosure failures in the Consent Solicitation as a breach of the duty of disclosure and 2) undervaluing Starrett City as a breach of the duty of care, for which Dissenting Limited Partners seek a preliminary injunction. On a motion for a preliminary injunction, “[t]he party seeking [it] must demonstrate a probability of success on the merits, danger of irreparable injury in the absence of an injunction and a balance of equities in its favor.” *Nobu Next Door, LLC v. Fine Arts Hous., Inc*, 4 N.Y.3d 839, 840 (2005).

Regarding undervaluing Starrett City, Dissenting Limited Partners have failed to demonstrate the inadequacy of monetary damages for this claim, and injunctive relief is inappropriate where other remedies are available. *Compare* Pls. Mem. in Reply 11 (stating that Belveron offered “to pay 25 million more than whatever [Purchaser] would

⁸ Vote Tracker further attests that even including limited partners who were not entitled to vote in the voting population, the PSA was still approved by more than 51% of the limited partners.

pay”, yet MGPs still proceeded with Purchaser), *with Madden Intern., Ltd. v Lew Footwear Holdings Pty Ltd.*, 50 Misc. 3d 1210(A) (N.Y. Sup. 2016), *affd*, 143 A.D.3d 418 (1st Dep’t 2016) (internal citations and quotation marks omitted) (stating that the movant must demonstrate that irreparable harm is “imminent, not remote or speculative, and the alleged injury must be one incapable of being fully remedied by monetary damages.”). Accordingly, I deny the request for a preliminary injunction based upon the alleged undervaluation of Starrett City.

Deane Family and Gerschel next argue that the disclosure failures in the Consent Solicitation are direct claims that may be individually asserted to vindicate their right to informed consent.⁹ I have not found a New York case definitively holding that disclosure claims are direct and/or that the corresponding harm is irreparable under New York law, nor have the parties presented such a case to me. However, there is precedent concerning shareholder voting in general. For example, in *Akasa Holdings, LLC v Sweet*, 115 A.D.3d 556 (1st Dep’t 2014), the Appellate Division, First Department held that because “[p]laintiff is seeking to vindicate its right as a shareholder to elect directors . . . its claims [for equitable relief] are individual, not derivative[.]” *Akasa*, 155 A.D.3d at 556 (citing *Eisenberg v. Flying Tiger Line, Inc.*, 451 F.2d 267 (2d Cir. 1971), in which the Second Circuit emphasized in dicta that plaintiff’s cause of action to enjoin a reorganization was personal because the stockholder complained that the reorganization

⁹ I note that SCA is a limited partner with only an economic interest and therefore, has no standing to seek a preliminary injunction based on the alleged disclosure failures in the Consent Solicitation.

would deprive him of a voice in the affairs of the previously existing operating company). Although Deane Family and Gerschel attempt to frame the alleged disclosure failures as an individual voting rights violation entitling them to directly seek a preliminary injunction, the damages they claim do not show irreparable harm.

Here, the only potential loss to the Deane Family and Gerschel is the right to a higher purchase price for Starrett City (or a different method of restructuring). This potential loss is not irreparable because the value may be calculated and be compensable by monetary damages. *See Broadway 500 W. Monroe Mezz II LLC v Transwestern Mezzanine Realty Partners II, LLC*, 80 A.D.3d 483 (1st Dep't 2011) (“Since ‘[plaintiffs]’ interest in the real estate is commercial, and the harm [they] fear[] is the loss of [their] investment . . .’ they can be compensated by damages and therefore cannot demonstrate irreparable harm . . . even [when] lost profits [] are difficult to ascertain”) (citation omitted) (quotation marks and changes in original); *see also Hemmings v Ivy League Apt. Corp.*, 42 Misc. 3d 1215(A) (Sup. Ct. 2013) (same).

The MGPs’ alleged conduct has not barred the Deane Family and Gerschel from acting on a right or privilege that is theirs, *e.g.*, the loss of the ongoing management and control of their business interests. Thus, the rights at issue here are not at all comparable with those at issue in *Akasa*. *See Wenz v Globecom Sys., Inc.*, 37 Misc. 3d 1222(A) (Sup. Ct. 2012) (“This Court sees no need to carve out an exception to the above-mentioned rules of what constitutes irreparable harm in order to accommodate claimed disclosure deficiencies by class action shareholder plaintiffs, unless confronted with extreme circumstances where a clear legal right is shown.”).

Moreover, a review of the record before me, including the affidavit and deposition transcript of Deane, shows that there is a sharp dispute as to whether the alleged disclosure failures amount to a breach of fiduciary duty or deception, or whether any of the allegedly omitted or misleading information complained of would have altered the information available to the limited partners in deciding whether to vote on the Consent Solicitation. *Compare* Pls.' Compl. (complaining that the Consent Solicitation failed to discuss MGPs' refinancing efforts; failed to clarify that the sale process only included negotiations with Purchaser; failed to include the PSA and sale price; failed to sufficiently describe MGPs' conflict, including waterfall distributions) *with* Deane Aff. In Opp'n (explaining that refinancing would not address the phantom tax issues limited partners faced, a topic mentioned in the Consent Solicitation; explaining that by pursuing a "targeted" approach, MGPs considered extrinsic and intrinsic factors such as public opinion and governmental approval to reach an achievable opportunity with Purchaser; explaining that the Consent Solicitation disclosed that the MGPs would receive additional compensation pursuant to the Partnership Agreement; explaining that the Consent Solicitation provided total estimated net distributable proceeds and the limited partner's corresponding "Schedule K-1 Economic Interest"; adding that no limited partners who affirmatively voted have asked to retract their consent). In light of the strength of defendants' arguments, plaintiffs' have failed to show a clear likelihood of success on the merits.

Lastly, balance of the equities does not favor judicial interference with the PSA, a potentially achievable deal that faces more scrutiny beyond that of the Dissenting Limited

Partners. I have considered the Dissenting Limited Partners remaining arguments and find them unavailing.

In accordance with the foregoing, it is

ORDERED that the motion for a preliminary injunction is denied.

This constitutes the decision and order of the Court.

1/2/18
DATE

Saliann Scarpulla
SALIANN SCARPULLA, J.S.C.

CHECK ONE:

- CASE DISPOSED
- GRANTED
- SETTLE ORDER
- DO NOT POST

DENIED

- NON-FINAL DISPOSITION
- GRANTED IN PART
- SUBMIT ORDER
- FIDUCIARY APPOINTMENT

OTHER

REFERENCE

APPLICATION:

CHECK IF APPROPRIATE: