

ESP Intl. Inc. v Cooke
2019 NY Slip Op 32391(U)
August 1, 2019
Supreme Court, New York County
Docket Number: 650259/2017
Judge: Andrew Borrok
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prepared ESP's Shareholder Agreement and By-Laws that are at issue in this lawsuit. The Lazer Firm also represents ESP in this action.

ESP commenced this action on January 17, 2017. Pursuant to a Commitment Letter, dated May 24, 2015, ESP alleged that Mr. Cooke agreed to raise \$570,000 in exchange for ownership of 30% of ESP stock (NYSCEF Doc. No. 1, ¶ 10). However, Mr. Cooke's alleged misrepresentations regarding the adequacy of ESP's capitalization and distribution of ESP products resulted in the Meeting. The Complaint asserts (1) a declaratory judgment that Mr. Cooke was properly removed as a director and officer of ESP (first cause of action), (2) a declaratory judgment that Stabilis's shares of capital stock were void for failure of consideration and by virtue of Stabilis's fraudulent representations and breach of agreement (second cause of action), and (3) breach of fiduciary duty by Mr. Cooke (third cause of action).

In their Answer and Counterclaims, the Defendants allege that the Meeting was part of a fraudulent scheme by ESP to misappropriate Stabilis' stock and secure new investor funds without diluting the stock interests of any ESP shareholder other than Mr. Cooke (NYSCEF Doc. No. 4, ¶¶ 9-11). The Defendants claim that the notice of the Meeting did not mention its purpose, and that neither Stabilis or Mr. Cooke received a proxy; however, Mr. Cooke believes that executed proxies provided by ESP shareholders at the Meeting authorized his removal and the cancellation of Stabilis' shares of ESP stock (*id.*). The counterclaims assert (1) fraudulent conduct and breach of the shareholders agreement in the cancelation of Stabilis' stock (first counterclaim), and (2) fraudulent conduct in the purported termination of Mr. Cooke as a director of ESP (second counterclaim).

In the Defendants' First Notice for Discovery and Inspection to Plaintiff, dated August 4, 2017, the Defendants sought all "communications between [plaintiff] or any person acting on [plaintiff's] behalf (including without limitation either Testa or Desideri) and any other person (including without limitation any of your shareholders) concerning the January 10, 2017 shareholders or board of directors meeting" (NYSCEF Doc. No. 83, at 11-12, the **First Notice**).

The Defendants later requested ESP's legal bills concerning any services rendered in connection with the Meeting. Although ESP initially refused to provide the legal bills on the basis of attorney-client privilege, ESP ultimately provided the Defendants with legal bills from the Lazer Firm on April 10 and April 30, 2019 (NYSCEF Doc. No. 79, at 4-5). The bill statement as of December 31, 2016 indicates that the Lazer Firm billed ESP in the amount of 46.60 hours for tasks including:

review Shareholders Agreement; call on need for capital and equity rights; research re: substantive Delaware requirements for voting proxies; review Delaware law on shareholder consent without meeting and proxies; review meeting requirements and notice, work on proxy; review bylaws and discuss with client; delaware law research on private companies issuing shares to retain share ownership at the expense of a minority shareholder; researched argument related to "lack of consideration" for stock issuance; review emails on correspondence with Cooke on raising funds, call with Ezio on same, research; researched cause of action related to failure to obtain capital investments; researched argument related to "lack of consideration" for stock issuance; research on Delaware case law pertaining to share dilution by controlling shareholders and non-controlling factions; researched cause of action related to failure to obtain capital investments; researched argument related to "lack of consideration" for stock issuance; researched enforcement of commitment letters; researched causes of action related to breach of contract for failure to raise capital, breach of fiduciary duty, and membership interest consideration; researched corporate remedies and causes of action for failure to provide agreed-upon consideration for shares; drafted memorandum to client regarding research findings; *conference call with client regarding strategy; notice of Board meeting; drafted resolution regarding cancellation of shares; call with client (12/28)* [emphasis added] (NYSCEF Doc. No. 82, hereinafter the **Bills**).

The bill statement as of January 31, 2017 is partially redacted, but unredacted portions reveal that the Lazer Firm billed ESP for tasks including “resolutions; researched and drafted corporate resolutions; researched and revised resolutions; *drafted script for shareholder/board of director meeting*” (*id.*) [emphasis added], all of which occurred prior to the Meeting where Mr. Cooke was removed and concerned documents that were unquestionably responsive to both the First Notice, and relevant to the claims asserted by ESP and the counterclaims asserted by the Defendants, and none of which had either been provided to the Defendants or otherwise identified or disclosed in an appropriate privilege log.

Notwithstanding the foregoing, the Plaintiff filed NOI on May 16, 2019. The Defendants now move by order to show cause to obtain these hidden documents and to vacate NOI so that discovery can proceed based on this withheld information.

Discussion

A. Production of Documents Related to the Bills

The Defendants argue that ESP and the Lazer Firm should be ordered to produce documents related to the Bills. Under CPLR § 3101, parties must disclose all matters material and necessary to an action. Under CPLR § 3126, if any party willfully fails to disclose information which the court finds ought to have been disclosed, the court may make such orders with regard to the failure or refusal as are just.

The Bills reveal that the ESP was in contact with the Lazer Firm before the Meeting that is the subject of this action. Significantly, the Bills also indicate that the Lazer Firm performed

services in connection with the Meeting, including but not limited to preparing a script for the Meeting. It is axiomatic that the documents sought are relevant to both the claims and counterclaims. The record indicates that ESP failed to comply with the Defendant's First Notice by not only withholding relevant documents, but by failing to identify the same in their privilege log (*see* NYSCEF Doc. No. 80). Although ESP asserts that certain emails in its privilege log should have alerted the Defendants to discussions between ESP and the Lazer Firm before the Meeting, it was only after the Bills were produced, that the Defendants could possibly become aware of the existence of any relevant documents that pre-dated the Meeting. ESP cannot participate in the creation of documents for the Meeting, withhold such documents from disclosure, and now allege that the Defendants should have known that that said documents existed. Simply put, the Defendants are entitled to test their theory that Mr. Cooke was removed pursuant to a pre-orchestrated unnoticed plan designed to divest him of his position so as not to dilute other shareholders' stock interests.

To the extent that ESP asserts attorney-client privilege as a defense to producing documents related to the Bills, this defense is inapplicable to undisclosed documents that were not identified in a privilege log. If the documents are subject to privilege, they should have been identified on a privilege log that the Defendant could review and then, if appropriate, challenge. As discussed at oral argument, Mr. Cooke may very well be entitled to view the documents because his conduct as a former director of ESP has been called into question and inspection of these documents is required to prepare his defenses (*People v Greenberg*, 50 AD3d 195, 202-203 [1st Dept 2008] [explaining that the movants had an "unequivocal right" to review relevant materials generated by the company's counsel during the period that the movants previously served as the

company's directors and officers]). For completeness, at oral argument, the Defendants confirmed that they were not seeking ESP's litigation files related to this action, but only those documents identified and related to the Bills, which concern the Meeting. Moreover, ESP may not invoke attorney-client privilege "where it involves client communications that may have been in furtherance of a fraudulent scheme, an alleged breach of fiduciary duty or an accusation of some other wrongful conduct" (*Ulico Cas. Co. v Wilson, Elser, Moskowitz, Edelman & Dicker*, 767 NYS2d 228, 228 [2003]). Here, the pleadings adequately allege breach of fiduciary duty by Mr. Cooke and fraudulent conduct by ESP (NYSCEF Doc. No. 1, ¶¶ 52-55; NYSCEF Doc. No. 4, ¶¶ 12-21). These circumstances favor disclosure (*id.*).

Accordingly, the Defendants motion for the production of documents set forth in the Bill is granted and said documents shall be produced by ESP, or set forth in an appropriate privilege log within 45 days of this order. For the avoidance of doubt, the branch of the Defendants' motion for sanctions is denied.

B. Vacating the Note of Issue

For the reasons set forth above, the NOI is stricken because it contained misstatements of material fact regarding the completion of discovery (*see Savino v Lewittes*, 160 AD2d 176, 177 [1st Dept 1990]). As a result, the time for the parties to file motions for summary judgment is also extended.

Accordingly, it is

ORDERED that the defendants' motion is granted to the extent that (1) the plaintiff shall produce documents set forth in the legal bills at NYSCEF Doc. No. 82 or produce an appropriate privilege log within 45 days of this order, and (2) the note of issue and certificate of readiness are hereby vacated and the case is stricken from the trial calendar; and it is further

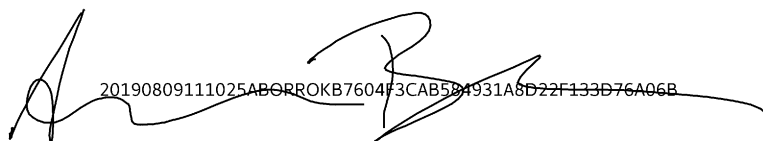
ORDERED that within 15 days from the date of this order, the defendants shall serve a copy of this order with notice of entry on all parties and upon the Clerk of the General Clerk's Office (60 Centre Street, Room 119), who is hereby directed to strike the case from the trial calendar and make all required notations thereof in the records of the court; and it is further

ORDERED that the time in which the parties may move for summary judgment is hereby extended until 60 days after a proper note of issue is filed; and it is further

ORDERED that the parties shall appear for a status conference on September 23, 2019 at 60 Centre Street, Room 238 at 11:30 am; and it is further

ORDERED that, on or before October 31, 2019, the plaintiff shall cause the action to be placed upon the trial calendar by the filing of a new note of issue and certificate of readiness (for which no fee shall be imposed), to which shall be attached a copy of this order; and it is further

ORDERED that such upon the Clerk of the General Clerk's Office shall be made in accordance with the procedures set forth in the *Protocol on Courthouse and County Clerk Procedures for Electronically Filed Cases* (accessible at the "E-Filing" page on the court's website at the address www.nycourts.gov/supctmanh).


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8/1/2019
DATE

ANDREW BORROK, J.S.C.

CHECK ONE:

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CASE DISPOSED

GRANTED

SETTLE ORDER

INCLUDES TRANSFER/REASSIGN

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DENIED

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NON-FINAL DISPOSITION

GRANTED IN PART

SUBMIT ORDER

FIDUCIARY APPOINTMENT

☐

OTHER

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REFERENCE

APPLICATION:

CHECK IF APPROPRIATE: