

Epmmy LLC v Nycanna LLC
2020 NY Slip Op 30316(U)
January 6, 2020
Supreme Court, New York County
Docket Number: 655480/2018
Judge: Andrea Masley
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART IAS MOTION 48EFM

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EPMMNY LLC,

Plaintiff,

- v -

NYCANNA LLC, TERRADIOL MANAGEMENT COMPANY
LLC, TERRADIOL OHIO LLC, NYCI HOLDINGS LLC,
NEW AMSTERDAM DISTRIBUTORS LLC, IMPIRE
STATE HOLDINGS LLC, JOHN VAVALO, DOMINIC
FALCONE, DENNIS DUVAL, DINO DIXIE, PATRICK
HARVEY, PHILLIP HAGUE, JEFFREY SCHEER, BOND,
SCHOENECK & KING PLLC ,ACREAGE NEW YORK,
LLC, NY MEDICINAL RESEARCH & CARING, LLC,

Defendants.

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INDEX NO.	<u>655480/2018</u>
MOTION DATE	<u>04/01/2019, 04/01/2019, 04/02/2019, 04/02/2019, 04/01/2019</u>
MOTION SEQ. NO.	<u>003 004 005 006 007</u>

**DECISION + ORDER ON
MOTION**

HON. ANDREA MASLEY:

The following e-filed documents, listed by NYSCEF document number (Motion 003) 73, 74, 75, 76, 77, 78, 79, 80, 81, 82, 83, 84, 121, 122, 131, 132, 133, 134, 135, 136, 137, 138, 139, 140, 141, 142, 143, 144, 145, 146, 147, 148, 149, 150, 151, 152, 153, 154, 155, 156, 157, 158, 159, 160, 161, 162, 163, 164, 165, 166, 167, 168, 169, 192, 193, 194, 195, 196, 197

were read on this motion to/for

DISMISSAL

The following e-filed documents, listed by NYSCEF document number (Motion 004) 91, 92, 93, 94, 95, 96, 97, 98, 99, 100, 101, 102, 103, 170, 171, 198, 199, 200, 201, 202, 203, 204, 238, 239, 240

were read on this motion to/for

DISMISSAL

The following e-filed documents, listed by NYSCEF document number (Motion 005) 85, 86, 87, 88, 89, 90, 172, 173, 207

were read on this motion to/for

DISMISS

The following e-filed documents, listed by NYSCEF document number (Motion 006) 104, 105, 106, 107, 108, 109, 110, 174, 175, 206

were read on this motion to/for

DISMISSAL

The following e-filed documents, listed by NYSCEF document number (Motion 007) 111, 112, 113, 114, 115, 116, 117, 118, 119, 120, 176, 177, 205

were read on this motion to/for

DISMISS

Masley, J.:

In motion sequence number 003, defendants Bond, Schoeneck & King, PLLC (Law Firm) and Jeffrey Scheer move, pursuant to CPLR 3211, to dismiss the amended complaint. In motion sequence number 004, defendants NYCI Holdings LLC (NYCI), New Amsterdam Distributors, LLC (New Amsterdam), John Vavalo, Dominic Falcone, Dennis T. Duval, Dino Dixie, and Patrick Harvey (collectively, NYCI Defendants) move, pursuant to CPLR 3211 (a) (1), (3), and (7), General Obligations Law (GOL) § 5-701 (a) (1), and Business Corporation Law (BCL) §§ 503 (b) and 626, to dismiss the amended complaint. In motion sequence number 005, defendants Terradiol Management Company, LLC (Terradiol Management) and Terradiol Ohio, LLC (Terradiol Ohio) (collectively, Terradiol Defendants) move, pursuant to CPLR 3211 (a) (7) and (8), to dismiss the amended complaint. In motion sequence number 006, defendant Phillip Hague moves, pursuant to CPLR 3211 (a) (1), (3), and (7), to dismiss the amended complaint. In motion sequence number 007, defendants NYCANNA, LLC (NYCANNA), New York Medicinal Research & Caring (NY Medicinal), Impire State Holdings, LLC (Impire), and Acreage New York LLC (Acreage LLC) (collectively, Acreage Defendants) move, pursuant to CPLR 3211, to dismiss the amended complaint.

Background

The following facts are alleged in the January 31, 2019 amended complaint (NYSCEF Doc. No. [NYSCEF] 48, amended complaint), and for the purposes of these motions to dismiss, are accepted as true.

Plaintiff EPMMNY LLC (EPMMNY) brings this action on its own behalf and derivatively as a member and 25% vest equity owner of NYCANNA LLC (NYCANNA)

(*id.*, ¶ 2). EPMMNY was formed to engage in the business of owning and operating licensed medical cannabis businesses (*id.*, ¶ 26). In March 2015, the New York State Department of Health (DOH) issued a public notice that it was going to entertain license applications for medical cannabis business with a filing deadline of June 5, 2015 (*id.*, ¶ 27). David Feder, a New York attorney with experience in the legal cannabis industry, had been preparing to submit a license application and began assembling a team to operate in New York (*id.*, ¶ 28). Feder began working with Malcolm Morrison, an experienced legal cannabis businessperson, who had successfully obtained cannabis licenses in other states (*id.*, ¶ 29). Feder and Morrison recruited additional members of their team – defendant Philip Hague, Scott Bergin, and Ian DeQueroiroz - all major players in the medical cannabis field (*id.*, ¶ 32). With this team in place, Feder and Morrison created EPMMNY with barely more than a month remaining to prepare and submit the New York license application (*id.*, ¶ 34).

In late April 2015, Feder was introduced to James Esposito, who represented that he was part of defendant New Amsterdam, whose principal was defendant John Vavalo (*id.*, ¶ 36). New Amsterdam also wanted to apply for a medical cannabis license in New York (*id.*). On May 1, 2015, Feder and Morrison met with Esposito to discuss their respective team's abilities and plans (*id.*, ¶ 37). At this meeting, it became clear to Feder that New Amsterdam was not as experienced as EPMMNY and unprepared to develop a license application (*id.*, ¶ 38). On May 8, 2015, Feder, Morrison, Esposito and Vavalo met to discuss forming a business partnership between EPMMNY and New Amsterdam to jointly pursue a license application (*id.*, ¶ 40). The parties agreed that

New Amsterdam would hold 75% equity and EPMMNY would hold a non-dilutable 25% equity in the newly formed entity, New York Canna, Inc. (NY Canna) (*id.*, ¶ 41).

The parties agreed that EPMMNY would contribute the application preparation and filing, and if a license was awarded, would control and be compensated for the operational aspects of the business; in turn, New Amsterdam would provide the required financial support, local and political contacts, a union agreement, and targeted real estate (*id.*).

In May 2015, defendant Scheer and the Law Firm were retained to perform legal services for NY Canna, including drafting its shareholders' agreement (*id.*, ¶ 44). On June 3, 2015, Scheer sent the parties several NY Canna corporate documents, including bylaws, subscription agreements, corporate resolutions and meeting minutes, but not a shareholder agreement (*id.*, ¶ 49). Feder asked Scheer for the shareholder agreement before the license application deadline of June 5, 2015, and Scheer responded that he had not prepared that agreement and Feder should send any proposed changes to the Term Sheet (*id.*, ¶ 52). Scheer informed Feder that the shareholder agreement would be worked on after June 5th (*id.*). The parties continued to work on the final application for submission to the DOH despite not having a shareholder agreement in place (*id.*, ¶¶ 55-58). The license application was submitted, but EPMMNY never received a copy (*id.*, ¶ 60).

Again, Feder inquired about the shareholder agreement, but was ignored (*id.*, ¶ 62). On June 10, 2015, Esposito, in a group email, inquired why NY Canna was formed as a corporation and not a limited liability company to which Scheer responded that "NY Canna was formed as a corporation because, unlike the other applicants which had

hired outside consultants to write their application and other outside management teams to run their business, ‘we have active owners, helps with tax issues’” (*id.*, ¶ 64). On July 2, 2015, Scheer wrote to Feder, explaining that “NY Canna is a corporation – no Operating Agreement. There is a Certificate of Incorporation and Bylaws. The Bylaws are somewhat standard They may be revised based on the final version of the Term Sheet Coupled with the Bylaws will be Subscription Agreements from EPMMNY, LLC and from New Amsterdam Distributors, LLC to New York Canna which will provide additional evidence of the stock ownership. Again, these will be finalized at the same time as the Term Sheet” (*id.*, ¶ 68). On July 15, 2015, Feder wrote to Scheer demanding copies of all the parties’ agreements and the full license application (*id.*, ¶ 72). Scheer did not comply with this demand (*id.*, ¶ 77).

On August 1, 2015, the DOH released a list of ranked applicants; NY Canna was sixth out of forty-three applications submitted, placing it in line for a license in the near future (*id.*, ¶¶ 78-79). This made NY Canna a valuable business (*id.*, ¶ 80). It is alleged that New Amsterdam isolated and sought to disenfranchise EPMMNY (*id.*, ¶ 81). In 2016, New Amsterdam undertook to unilaterally change the NY Canna’s corporate structure by transforming it into a limited liability company (*id.*, ¶ 84). On November 20, 2016, EPMMNY received notice that NY Canna was merging with defendant NY Medicinal without its consent and that EPMMNY’s equity interest was being diluted by 50% to 12.5% (*id.*, ¶ 91). NY Medicinal was owned in whole or in part by Acreage Holding LLC’s predecessor, High Street Capital Partners (*id.*, ¶ 92). On December 1, 2016, Feder responded to the merger notice by rejecting it outright and demanding NY Canna’s books and records (*id.*, ¶ 96).

At a meeting on January 11, 2017, Vavalo advised EPMMNY's members that EPMMNY's equity share was being reduced to 12.5% and EPMMNY would not receive management fees (*id.*, ¶ 103). At this meeting, Vavalo encouraged Hague and DeQueiroz to forego their fiduciary duties to EPMMNY and convince their EPMMNY partners to accept these new terms (*id.*, ¶ 104).

In February 2017, with EPMMNY's knowledge, NY Canna submitted a revised license application to the DOH (*id.*, ¶ 105). The revised application stated that

"[t]he initial shareholders of [NY Canna], as stated in the original Application, were intended to be [New Amsterdam] and [EPMMNY]. However, [New Amsterdam] and EPMMNY were unable to reach an agreement as to EPMMNY's contributions to the operating entity and the terms of investment. Accordingly, the terms of EPMMNY's equity were never finalized and the entity is not included as a stakeholder of the applicant going forward. Therefore, the sole shareholder of New York Canna, Inc. prior to any of the events described below was [New Amsterdam]"

(*id.*, ¶ 106). Around the same time, EPMMNY learned of Hague's defection to NY Canna (*id.*, ¶ 108).

Discussion

Before the court can address the merits, it must first address the threshold issue of EPMMNY's capacity to sue both individually and derivatively on behalf of NY Canna (*see Town of Riverhead v New York State Bd. Of Real Prop. Servs.*, 5 NY3d 36 [2005]).

Here, defendants argue that EPMMNY's Articles of Organization do not provide for management by a manager; rather, pursuant to New York Limited Liability Company Law (NY LLCL) § 401 (a), it is managed by all of its members and NY LLCL §§ 403, 405, and 407 require EPMMNY's actions to be approved by its members at a meeting held on notice or by written consent in lieu of such meeting. Defendants assert that these requirements were not met, and thus, Feder cannot act alone in filing this action

on EPMMNY's behalf. In support of their argument, defendants rely on Hague's affidavit, wherein he attests that, in early 2017, EPMMNY's members took a vote on whether to commence a lawsuit against NY Canna and the members could not agree (NYSCEF 105, Hague Aff, ¶ 31). Hague also attests that he never received notice that a meeting was called regarding whether EPMMNY should file this action (*id.*, ¶ 33). Hague also attests that he was never informed of his alleged removal as Chairman and President of EPMMNY, as Feder claims (*id.*, ¶ 30).

EPMMNY does not dispute that NY LLCL's requirements; rather, it argues that EPMMNY's members have authorized the commencement of this action. In support, EPMMNY submit an affidavit from Feder, in which he attests that during an October 2016 meeting of EPMMNY's members, it was decided that EPMMNY's officers are authorized to "take all actions and to sign all documents reasonably needed to operate the Company in the interests of its Members, including speaking for, and/or negotiating on behalf of the Company, and other activities as may be needed" (NYSCEF 171, Feder Aff., ¶ 4; *see also* NYSCEF 135, Meeting Minutes). Feder concludes that "actions" include the filing of this action (*id.*). Feder also attests that Hague was removed as Chairman and President of EPMMNY at an August 13, 2018 meeting and was replaced by Feder (*id.*, ¶ 9).

Where "standing is put into issue by a defendant, a plaintiff must prove its standing in order to be entitled to relief" (*Deer Park Assocs. v Town of Babylon*, 121 AD3d 738, 740-41 [2d Dept 2014]). Feder's affidavit and the minutes from the October 13, 2016 meeting of EPMMNY's members do not conclusively prove that Feder has the authority to bring this action on behalf of EPMMNY especially in light of Hague's sworn

statements. Although Feder states that Hague was removed as EPMMNY's Chairman and President, he does not state that Hague is no longer a member of EPMMNY, who under the NY LLCL would have to consent to this lawsuit. Hague attests that he never approved this filing (NYSCEF 105, ¶ 32-33) Thus, a hearing on capacity is necessary. The defendants' motions to dismiss are held in abeyance until a determination on this issue.

Accordingly, it is

ORDERED that a Judicial Hearing Officer (JHO) or Special Referee shall be designated to hear and report, unless the parties stipulate to have the JHO or Special Referee hear and determine, to this court on the following individual issues of fact, which are hereby submitted to the JHO/Special Referee for such purpose:

- (1) the issue of whether Feder, on behalf of EPMMNY, has standing to bring this action. Specifically, whether, at the October 13, 2016 meeting, EPMMNY's members authorized EPMMNY Officers to unilaterally file lawsuits on EPMMNY's behalf without prior approval from all members, and if not, whether EPMMNY members approved the filing of this lawsuit in accordance with NY LLC Law; and it is further

ORDERED that this matter is hereby referred to the Special Referee Clerk (Room 119, 646-386-3028 or spref@nycourts.gov) for placement at the earliest possible date upon the calendar of the Special Referees Part (Part SRP), which, in accordance with the Rules of that Part (which are posted on the website of this court at www.nycourts.gov/supctmanh at the "References" link), shall assign this matter at the

initial appearance to an available JHO/Special Referee to hear and report as specified above; and it is further

ORDERED that counsel shall immediately consult one another and counsel for plaintiff/petitioner shall, within 15 days from the date of this Order, submit to the Special Referee Clerk by fax (212-401-9186) or e-mail an Information Sheet (accessible at the "References" link on the court's website) containing all the information called for therein and that, as soon as practical thereafter, the Special Referee Clerk shall advise counsel for the parties of the date fixed for the appearance of the matter upon the calendar of the Special Referees Part; and it is further

ORDERED that counsel shall file memoranda or other documents directed to the assigned JHO/Special Referee in accordance with the Uniform Rules of the Judicial Hearing Officers and the Special Referees (available at the "References" link on the court's website) by filing same with the New York State Courts Electronic Filing System (see Rule 2 of the Uniform Rules); and it is further

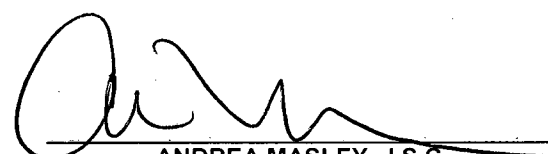
ORDERED that any motion to confirm or disaffirm the Report of the JHO/Special Referee shall be made within the time and in the manner specified in CPLR 4403 and Section 202.44 of the Uniform Rules for the Trial Courts; and it further

ORDERED that motion sequence numbers 003, 004, 005, 006, and 007 are held in abeyance pending this hearing and report and such shall be put on this court's calendar for a control date of March 4, 2020 (no appearance). If the court receives the Referee's Report prior to that date, it will decide these motions immediately, if necessary.

Motion Seq. No.003

1/6/2020
DATE

CHECK ONE: CASE DISPOSED GRANTED DENIED
APPLICATION: SETTLE ORDER
CHECK IF APPROPRIATE: INCLUDES TRANSFER/REASSIGN

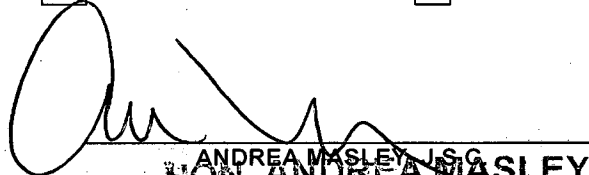

ANDREA MASLEY, J.S.C.
HON. ANDREA MASLEY

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

Motion Seq. No. 004

1/6/2020
DATE

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APPLICATION: SETTLE ORDER
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ANDREA MASLEY, J.S.C.
HON. ANDREA MASLEY

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

Motion Seq. No. 005

1/6/2020
DATE

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ANDREA MASLEY, J.S.C.
HON. ANDREA MASLEY

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

Motion Seq. No. 006

1/6/2020
DATE

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APPLICATION:

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ANDREA MASLEY, J.S.C.

HON. ANDREA MASLEY

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

Motion Seq. No. 007

1/6/2020
DATE

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APPLICATION:

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ANDREA MASLEY, J.S.C.

HON. ANDREA MASLEY

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