

Goren v Barnett

2023 NY Slip Op 31610(U)

May 11, 2023

Supreme Court, New York County

Docket Number: Index No. 653221/2019

Judge: Andrew Borrok

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This opinion is uncorrected and not selected for official publication.

SUPREME COURT OF THE STATE OF NEW YORK
 COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 53

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LELA GOREN,

Plaintiff,

- v -

GARY BARNETT INDIVIDUALLY, OMS MANAGER, LLC, 555 TENTH AVENUE MANAGER, LLC, CPT EB5 MANAGER, LLC, WNCE MANAGER, LLC, HRH NCE MANAGER, LLC, EXTELL 4110 LLC, EX HOLDINGS LLC, A NEW YORK LIMITED LIABILITY COMPANY, EXTELL DEVELOPMENT COMPANY, EXTELL NEW YORK REGIONAL CENTER, LLC

Defendant.

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INDEX NO. 653221/2019

MOTION DATE 07/22/2022

MOTION SEQ. NO. 005

DECISION + ORDER ON MOTION

HON. ANDREW BORROK:

The following e-filed documents, listed by NYSCEF document number (Motion 005) 114, 115, 116, 117, 118, 119, 120, 121, 122, 123, 124, 125, 126, 127, 128, 129, 130, 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

were read on this motion to/for DISMISS.

Upon the foregoing documents, the defendants’ motion to dismiss (Mot. Seq. No. 005) the Second Amended Complaint (**SAC**; NYSCEF Doc. No. 109) must be denied in its entirety.

The SAC asserts the following six causes of action: (i) a declaratory judgment that Gary Barnett owes fiduciary duties to the plaintiff (first cause of action), (ii) breach of fiduciary duty by Mr. Barnett (second cause of action), (iii) breach of contract by Mr. Barnett (third cause of action), (iv) an accounting (fourth cause of action), (v) aiding and abetting breach of fiduciary duties against all of the other defendants (fifth cause of action), and (vi) a declaratory judgment that 555 Tenth Avenue Manager, LLC, OMS Manager, LLC, CPT EB5 Manager, LLC, WNCE Manager, LLC, and HRH NCE Manager, LLC (collectively, hereinafter the **Barnett LLCs**) are

part of a common or single business enterprise with the Extell New York Regional Center, LLC (the **RC**) (sixth cause of action).

The first cause of action can not be dismissed because Ms. Goren is entitled to a declaration that as the managing member of the RC, Mr. Barnett owed the RC and its other members fiduciary duties (*Kelly v Blum*, 2010 WL 629850 at *12 [Del Ch 2010]) subject to the limitation on liability set forth in Section 7.1 of the RC's Operating Agreement which provides:

7.1 Limitation of Liability. To the extent permitted by law, the Manager or a Member and its officers, directors, partners, trustees, managers, members, employees and agents shall not be liable for damages or otherwise to the Company or any Member for any act, omission or error in judgment performed, omitted or made by it or them in good faith and in a manner reasonably believed by it or them to be within the scope of authority granted to it or them by this Agreement and in the best interests of the Company, provided that such act, omission or error in judgment does not constitute bad faith, fraud, gross negligence or willful misconduct.

(NYSCEF Doc. No. 110 §7.1).

The second cause of action for breach of fiduciary duty also is not ripe for dismissal because it is predicated on the allegation that Mr. Barnett entered into a series of transactions in bad faith where he diverted approximately \$765 million of administrative and management fees from the RC to entities owned and controlled by him to pay expenses otherwise not chargeable to the RC:

17. There is no set of market forces that can justify the virtual elimination of fee income being paid to the RC with respect to Post-IGT Projects. In fact, the dramatic shift in fees is a direct by-product of Barnett's self-dealing and overreaching by entering into a new set of one-sided agreements with affiliates which harmed the RC by, inter alia, stipulating to the following:

- a. The management and administrative fees would be paid to the New Barnett Management Affiliates rather than the RC.
- b. The Regional Center would receive an “RC Fee”, which was to be the management fee less “the cumulative compensation paid... to finders, broker-dealers, emigration agents or other introducers of capital.”
- c. RC Fee would be payable to the Regional Center “one hundred and twenty (120) days following the date upon which the Company has received the final Management Fee payment.”
- d. Each Regional Center Service Agreement also included that “The Regional Center will be responsible for all expenses incurred in performing the Services or any other obligation of the Regional Center under this Agreement.”

(*id.*, ¶ 17).

46. After 2014, Barnett diverted most of the fee income and profit making opportunities away from the RC by engaging in rampant self-dealing in connection with the Post-IGT Projects, including:

- (a) Modifying the Regional Center’s 4% management fee structure as set forth herein to divert this income to wholly owned shell entities (the New Barnett Management Affiliates (or other project related affiliates)), in connection with the Post-IGT Projects;
- (b) By executing an inferior set of management and service agreements to drastically reduce the RC’s share of income;
- (c) By burdening the Regional Center with expenses relative to extensive marketing, sponsoring, and compliance with EB-5 regulations even though the RC was no longer receiving its rightful share of the management fees;
- (d) Redeploying capital from Extell 4110 LLC based on loans to EX Holding LLC, while bypassing the Regional Center’s entitlement to additional fees;
- (e) Charging the RC and not the projects for any increased costs associated with finder’s commissions; and
- (f) Charging interest to the RC when the projects themselves are responsible to pay EB-5 investors.

(*id.*, ¶ 46).

Taking these allegations as true, this is sufficient. For the avoidance of doubt, Mr. Barnett's argument that he is entitled to dismissal because his decision to hoard cash in his wholly owned Barnett LLCs until all of the costs of the project are known and paid is (i) made in good faith, (ii) sound particularly given that placement fees associated with obtaining EB-5 candidates went up and now exceed the administrative fees and require supplementation of the management fees, and (iii) subject to the business judgment rule raises factual issues not properly resolved at this stage of the litigation for many reasons. By way of example, inasmuch as the fees are known and can be projected, to the extent that the amount to pay third parties has gone up as he claims, this additional known amount only can be held back from distribution. What Mr. Barnett has done as alleged is hold back everything and charge expenses not properly attributable to the RC.

The breach of contract claim (third cause of action) is also not properly dismissed at this stage of the litigation. The SAC alleges that Mr. Barnett failed to (i) collect and maximize available cash for distribution by allowing the RC to enter into inequitable and commercially unreasonable agreements with the Barnett LLCs, (ii) operate the RC in accordance with its charter, (iii) obtain reimbursement of expenses incurred by the RC that should have been incurred by the Barnett LLCs, and (iv) maintain full and complete books and records for the RC (*id.*, ¶ 106). This is sufficient at this stage of the litigation.

The fourth cause of action seeking an accounting also cannot be dismissed. As discussed below, the SAC properly alleges that the Barnett LLCs and the RC are part of a single business enterprise and that Mr. Barnett has abused the corporate form such that they must be disregarded as separate entities. As such, the cause of action seeking an accounting claim can not be dismissed on this basis.

The aiding and abetting a breach of fiduciary duty claim (fifth cause of action) also presents factual issues making dismissal at this stage of the litigation inappropriate (*Stone & Paper Invs., LLC v. Blanch*, 2019 WL 2374005, at *7 [Del. Ch. May 31, 2019]).

Finally, the cause of action seeking a declaratory judgment that the Barnett LLCs are part of a single business enterprise with the RC (sixth cause of action) cannot be dismissed. As alleged in the SAC,

130. The Regional Center and New Barnett Management Affiliates operate as a single consolidated business, without limitation, in the following ways:
- a. Barnett has improperly diverted the Regional Center's fee income stream to the New Barnett Management Affiliates;
 - b. Barnett has improperly attributed significant expenses (including expenses for EB-5 oversight and compliance, payroll, marketing, etc.) of the New Barnett Management Affiliates to the Regional Center without reimbursement; and
 - c. Barnett has consolidated the revenue (for tax purposes and internal financial reporting) of each of his separate, solely owned and controlled New Barnett Management Affiliates with the revenue of Regional Center.
 - i. For example, the Regional Center and Affiliates Management Report from August 2018 notes a year-end

cash balance for FY 2017 of \$11,131,014 combined for the Regional Center and New Barnett Management Affiliates. This is the exact number reported on the consolidated 2017 Regional Center and New Barnett Management Affiliates tax return.

- ii. Similarly, the Regional Center's 2017 tax return reports revenue of \$41,325,196 because Barnett consolidated the revenue of the New Barnett Management Affiliates with the Regional Center

(NYSCEF Doc. No. 109, ¶ 130).

The Barnett LLCs were allegedly formed for the improper purpose of diverting fees away from the RC (*id.*, ¶ 129), they file consolidated tax returns with the RC, and they are controlled and dominated by Mr. Barnett for the purpose of improperly withholding cash from distribution and paying expenses for which the RC is not responsible (*id.*, ¶ 131). This is sufficient (*In re Broadstripe, LLC*, 444 BR 51, 102 [Bankr D Del 2010]).

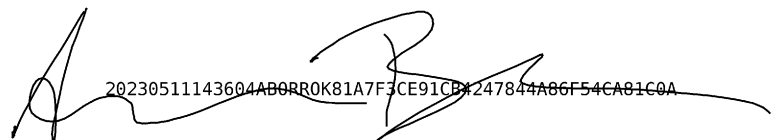
It is hereby ORDERED that the motion to dismiss is denied in its entirety; and it is further

ORDERED that the Defendants shall file an answer within 20 days of the date of this order; and it is further

ORDERED that the parties shall appear for a preliminary conference on **June 9, 2023, at 11:30am.**

5/11/2023

DATE



ANDREW BORROK, J.S.C.