

Newman v National Distrib. Alliance, LLC

2023 NY Slip Op 31701(U)

May 19, 2023

Supreme Court, New York County

Docket Number: Index No. 654439/2021

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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DENNIS ROY NEWMAN, MITCHELL NEWMAN, WENDY GORDON, PAUL J. RIZZI, DENNIS ROY NEWMAN 2011 FAMILY SPRAY TRUST FBO ALAN NEWMAN, DENNIS ROY NEWMAN 2011 FAMILY SPRAY TRUST FBO LAUREN ALTER, DENNIS ROY NEWMAN 2011 FAMILY SPRAY TRUST FBO ERIC NEWMAN

Plaintiff,

- v -

NATIONAL DISTRIBUTION ALLIANCE, LLC, NORTHEAST DISTRIBUTION SERVICES LLC, MICHAEL PRESTO, MICHAEL S. POUCHIE,

Defendant.

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INDEX NO. 654439/2021
MOTION DATE 03/15/2023
MOTION SEQ. NO. 006

DECISION + ORDER ON MOTION

HON. ANDREW BORROK:

The following e-filed documents, listed by NYSCEF document number (Motion 006) 128, 129, 130, 131, 132, 133, 134, 135, 136, 137, 138, 139, 140, 141, 142, 143, 144, 145, 146, 147, 148, 149, 157, 158, 159, 160, 161, 162, 163, 164, 165, 166, 167, 168, 169, 170, 171, 172, 175, 176, 177

were read on this motion to/for DISMISSAL.

Upon the foregoing documents, the defendants’ motion to dismiss (Mtn. Seq. No. 006) the Amended Complaint (**AC**; NYSCEF Doc. No. 125) must be granted in part. The breach of fiduciary duty claim (third cause of action) and aiding and abetting a breach of fiduciary claim (fifth cause of action) claims must be dismissed because these claims were squarely in front of the Hon. Emily Pines (Ret.) (the **Arbitrator**) and were fully and fairly litigated in the Prior Arbitration (*Marinelli Assocs. v Helmsley-Noyes-Co.*, 265 AD2d 1, 5 [1st Dept 2000]).

The branch of the breach of implied covenant of good faith and fair dealing claim (eight cause of action) which alleges that the Newmans (hereinafter defined) were frozen out of NDA and the branch of the claim for accounting (ninth causes of action) which seeks an accounting of NDA

must also be dismissed. These claims arise out of the NDA Operating Agreement which has a mandatory arbitration provision requiring these claims to be arbitrated.

The claims that arise out of the NDS Operating Agreement however, cannot be dismissed because the NDS Operating Agreement does not contain a mandatory arbitration provision and were decidedly not in front of the Arbitrator in the Prior Arbitration (*see* NYSCEF Doc. No. 100 § 13.03). In fact, during the Prior Arbitration, the parties and the Arbitrator acknowledged that the NDS Operating Agreement did not include an arbitration provision and as such, any claims which arise under that agreement would be adjudicated in this Court:

MR. LESSER: And I don't think it would be part of the arbitration because it's an NDS issue and the NDS Operating Agreement does not have an arbitration clause. So I believe that would be an issue for Justice Borrok.

MS. STALLONE: Okay. So we can litigate this issue before Justice Borrok. Fine (NYSCEF Doc. No. 160 at 1663).

THE ARBITRATOR: -- with regard to whether if you asked me to do that, that I'd have to go back to the NDS agreement. I'm not ruling on that (*id.*, at 1667).

Thus, the defendants are not now entitled to dismissal based on transactional claim preclusion as to the claims they specifically agreed would be litigated in this Court (*Cine-Source, Inc. v Burrows*, 180 AD2d 592, 595 [1st Dept 1992]).

With that as a backdrop, this action was commenced on July 19, 2021, when The A.M. Newspaper Delivery Service, Inc., Roy Newman, Wendy Gordon, Paul J. Rizzi Jr., Mitchell

Newman, and the Roy Newman Family Spray Trusts FBO Alan Newman, Lauren Alter, and Eric Newman (hereinafter, collectively the **Newmans**) filed a Complaint (NYSCEF Doc. No. 2), in which they alleged, *inter alia*, that Michael Presto, a manager of National Distribution Alliance, LLC (**NDA**) and majority member and operating manager of Northeast Distributions Services, LLC (**NDS**), breached (i) the NDA Operating Agreement and (ii) his fiduciary duties to NDA. The defendants moved to compel arbitration (Mtn. Seq. No. 001). This Court granted the motion because Article 19 of the NDA Operating Agreement contains a broad arbitration provision providing for arbitration of “any dispute, controversy or claim arising out of or in connection with this Agreement or any breach or alleged breach” (NYSCEF Doc. No. 71; NYSCEF Doc. No. 12, Art. 19).

Subsequently, NDA filed a Statement of Claim with the American Arbitration Association (i) alleging breach of the NDA Agreement against the Newmans, (ii) alleging breach of fiduciary duty against Roy Newman, and (iii) seeking a declaratory judgment that Roy Newman “shall have deemed to have resigned his position as Manager” of NDA (NYSCEF Doc. No. 102). The Newmans responded by filing a Consolidated Counterclaim and Third-Party Statement of Claim in which they asserted five counterclaims against NDA, Mr. Presto and Mr. Pouchie (NYSCEF Doc. No. 103).

In the first counterclaim, the Newmans sought a declaratory judgment (**First Counterclaim**) that they did not breach §15.1 of the NDA Operating Agreement (*id.*, ¶ 87). In the second counterclaim, the Newmans sought a declaratory judgment (**Second Counterclaim**) that NDA, Mr. Presto, and Mr. Pouchie violated § 11.2 of the NDA Operating Agreement when they sought

to force a buyout of the Newmans' membership interest without obtaining the requisite consent from Roy Newman (*id.*, ¶ 89). In the third counterclaim, the Newmans sought a declaratory judgement (**Third Counterclaim**) that (i) Mr. Presto and Mr. Pouchie (x) attempted to force the buyout of the Newmans' membership interests in NDA, and (y) withheld the Newmans' portions of the NDA profits for the 2020 FY and (ii) these actions, pursuant to the §11.2.1 of the NDA Operating Agreement, are deemed to constitute a for cause reason for removing Mr. Presto and Mr. Pouchie as managers of NDA (*id.*, ¶¶ 93-94). In the fourth counterclaim, the Newmans alleged that Mr. Presto and Mr. Pouchie breached their fiduciary duties owed to NDA (**Fourth Counterclaim**) by (i) paying themselves excessive salaries, (ii) using NDA funds to make unauthorized and improper personal non-business expenditures, (iii) mischaracterizing many of the improper charges on NDA's financial statements in order to avoid paying Newmans their rightful distributions, and (iv) engaging in self-dealing by using NDA funds, employees and facilities for the benefit of two separate entities – Two Mikes Delight and NDA Logistics – that Mr. Presto and Mr. Pouchie own (NYSCEF Doc. No. 105 at 9-12). Finally, in the fifth counterclaim, the Newmans allege that Mr. Presto and Mr. Pouchie breached §11.12 of the NDA Agreement (**Fifth Counterclaim**) when they sought to force a buyout of the Newmans' membership interests in NDA without the requisite approval (NYSCEF Doc. No. 103 ¶ 102).

Upon the parties' motions for summary judgment, the Arbitrator (i) dismissed each of the Newmans' claims and (ii) granted the First Counterclaim:

1. Respondents' motion for Summary Judgment dismissing Claimant's, Presto's and Pouchie's First Claim for breach of the Covenant Not to Compete in the Operating Agreement is granted.

2. Respondents' motion for Summary Judgment dismissing Claimant's, Presto's and Pouchie's Second Claim for breach of fiduciary duty against Roy Newman is granted.

3. Respondents' motion for Summary Judgment dismissing Claimant's, Presto's and Pouchie's Third Claim for a Declaratory award approving the mandatory buyout and resignation is granted.

4. Respondents' motion for Summary Judgment dismissing Claimant's, Presto's and Pouchie's Fourth Claim for a Declaratory award requiring return of escrowed funds is granted.

5. Respondents' motion for Summary Judgment granting their Second, Third, Fourth and Fifth Counterclaims as well as Claimant's, Presto's and Pouchie's motion to dismiss the same are all denied

(NYSCEF Doc. No. 104 at 25).

Beginning on June 1, 2022, the parties' engaged in a six-day arbitration (the **Prior Arbitration**; NYSCEF Doc. Nos 140-145). On November 16, 2022, following the hearing and a full briefing, the Arbitrator issued the final arbitration award (the **Final Award**; NYSCEF Doc. No. 105).

With respect to the Second and Fifth Counterclaims, the Arbitrator denied the claims based on the findings that the express terms of the NDA Agreement allowed Mr. Presto and Mr. Pouchie to seek a forced buyout of the Newmans' membership interests in NDA:

With regard to Counterclaimants' Second and Fifth Counterclaims, based upon the assertion that the Claimant and Third-Party Respondents violated the NDA Operating Agreement by forcing the buyout of the Newmans' interest in NDA without a unanimous vote of all Members, these claims must also fail since the clear language of Section 11.9 of the parties' Operating Agreement specifically allocates to the A Managers (Presto and Pouchie) all rights and powers necessary for management of business affairs, including "[e]nforcement, compromise, and settlement of any rights or claims in favor or against the company"

(*id.*, at 20).

With respect to the Third Counterclaim, the Arbitrator denied the claim based on a finding that the allegations that Mr. Presto and Mr. Pouchie's conduct constituted cause for resignation as managers of NDA ignored the express terms of the NDA Operating Agreement:

The Third Counterclaim that seeks the removal of Presto and Pouchie for improperly pursuing NDA's rights against them in connection with the Covenant Not to Compete is not sustainable since it ignores the language of Section 7.13 of the Operating Agreement, which states that: "[t]he receipt of advice of counsel that certain acts and omissions are within the scope of authority conferred by this Agreement, shall be conclusive evidence of good faith. . ." The credible testimony of Sylvor, Presto and Pouchie make clear that the actions taken in connection with the alleged Covent Not to Compete were in accordance with advice provided to the Claimant and Third-Party Respondents by corporate counsel

(*id.*, at 21).

With respect to the Fourth Counterclaim, the Arbitrator denied the claim based on the findings that Mr. Presto and Mr. Pouchi did not (i) improperly increase their own salaries, (ii) fail to pay the Newmans their rightful distributions, (iii) make unauthorized non-business expenditures, and (iv) engage in self-dealing:

SALARY

The increase of salaries for Presto and Pouchie occurred in 2012 and has remained at that level and not increased thereafter. Roy Newman was aware of this and specifically instructed his daughter, who ran NDA's prior payroll firm, to raise the salaries, (Lazzara May 5, 2022 Aff. at 3). The payroll increase was due to successful management by Presto and Pouchie raising the NDA net income from \$5 million to \$7.66 million. (*id.* at 3,4).

DISTRIBUTIONS

Counterclaimants' argument that Presto's compensation for 2018-2020 was passed through by the payroll firm as a "special bonus" in addition to his distributions is inaccurate. A review of Presto's Earning Statements reflects that he received his \$600,000.00 salary and that his receipt of \$577,875.00 was his share of the \$2.3 million distribution to all owners in 2018 representing his 50.25% ownership of NDS and corresponding ownership of NDA. For 2019, he also received his \$600,000.00 salary and the additional \$804,000.00 he received was, again, his share of the 2019 distributions of \$3.23 million. In 2020, he received his \$600,000.00 salary and in addition, \$1.1 million which also constitutes his share of the distribution of \$4.5 million representing his 50.25% interest in NDS and corresponding interest in NDA. (Lazzara Aff. May 5, 2022 and August 11, 2022 Aff. at 14). As explained by Viola in his role as NDA's tax preparer, the numbers Counterclaimants define as compensation to Presto for the same three years fail to take into consideration the fact that these sums are but a percentage of gross receipts of NDS. As Viola set forth, Counterclaimants' expert has overstated Presto's NDS compensation by \$1,722,125 in 2018; by \$1,803,693 in 2019, and \$1,534,001 in 2020. (Viola May 8, 2022 Aff. at 2,3).

EXPENSE REIMBURSEMENTS

The expense reimbursements were reported on monthly expense reimbursement reports, which included supporting receipts and documentation. For Presto, the great majority of such receipts were countersigned by Roy Newman. In addition, each reimbursement submission was received by the NDA CFO, Eric Newman, for review and processing. (Viola August 11, 2022 Aff. at 5). Pouchie followed the same procedure and Presto reviewed and approved all of his monthly expense and reimbursement reports. (id.). This process applied to all the expense items discussed as having appeared on social media – those relating to Presto were approved by Roy Newman. Frank Lazzara refers to and repeats the fact that all reimbursements are recorded in NDA's tax returns, as well as the total of such reimbursements equating to \$222,405.88 and an even lower figure. When these amounts take into account a deductible portion of the reimbursements, they amount to a total of \$183,484.00 from 2015-2020 translating to \$30,000.00 per year. (Lazzara Aff. August 17, 2022 at 15; Viola August 11, 2022 Aff. at 6).

CHARITABLE CONTRIBUTIONS AND DONATIONS

Counterclaimants, according to Viola, in criticizing charitable contributions to Presto's daughter's college (\$12,500.00 for each of 2 years), ignore the greater contributions to Eric Newman's MBA university (\$40,000.00). They also fail to consider charitable contributions made to medical institutions, and as scholarships

for low-income students at the college attended by Presto's daughter, all of which were proper expenses in the normal course of corporate operations. (Viola August 11, 2022 Aff. at 7,8).

MEDICAL EXPENSE REIMBURSEMENTS TO PRESTO

Counterclaimants' assertion that between 2015 and 2020, Presto and Pouchie obtained \$426,591.00 in medical expense reimbursements from NDA is incorrect. The amount represents the total healthcare cost for NDA employees including Presto and Pouchie and Eric Newman among others. (Lazzara May 5, 2022 Aff. at 22). In addition, even if this amount was solely for Presto and Pouchie family coverage, it equates to \$2,960.00 per month per officer, and the monthly premium cost for family coverage is currently between \$2,681.00 and \$3,059.00 as set forth on the N.Y. State of Health website. (id.). Further, Presto did not participate in NDA's insurance program, and, therefore, NDA reimburses Presto for premiums he would have been paid if he had participated in the plan, amounting to \$32,000.00 annually. (Lazzara May 5, 2022 Aff. at 8). These monthly medical plan reimbursements to Presto were approved by Roy Newman. (id). According to Lazzara, some of the medical bills to which Counterclaimants and their expert witness refer overstate Presto's reimbursement by 90%. These include out of pocket medical expenses by Presto totaling \$35,352.34 in September 2020 for which he only received reimbursement of \$3,200.00 and \$35,489.80 in October and November, 2020 expended by Presto for which he received reimbursement of \$3,430.00. (Lazzara May 5, 2022 Aff. at 9). In any case, every medical expense statement referred to was reported in the monthly expense report and approved by Roy Newman. (id.). Based on all the above information, the annual cash outlay by the Newmans is less than \$5,400.00. (id.). These were a minimal fraction of NDA's revenue and a small fraction of NDA's net profits to the NDA owners. (id. at 9,10).

ALLEGED SELF-DEALING REGARDING TWO-MIKES DELIGHT AND NDA LOGISTICS

NDA was a 50% owner of Two Mikes and a 90% owner of NDA Logistics. (Lazzara 5/522 Aff. at 11). NDA funded its portion of Two Mikes capital contribution at its inception and the remaining members, including Eric Newman, Mike Presto and Mike Pouchie, funded their portions of the initial capital contribution. (id.). NDA Logistics was self-funded from its inception. Lazzara sets forth the convincing argument that the figures Counterclaimants and their expert refer to as investments and loans by NDA to these two companies are balance sheets, not Profit and Loss statements, and they are not year-over-year expenses; but, rather, are a running total of the NDA investment. (id). In addition,

amounts allegedly described as payroll expenses for Two Mikes paid for by NDA represent a liability of NDA for commissions advanced by Two Mikes to NDA. (id.)

(*id.*, at 14-19).

Based on these findings, the Arbitrator denied all of the Newmans' counterclaims against NDA, Mr. Presto and Mr. Pouchie:

FINAL AWARD

Based upon the post-hearing rulings set forth herein, the Arbitrator rules as follows:

1. Counterclaimants'/Third-Party Respondents' Second Counterclaim is denied.
2. Counterclaimants'/Respondents' Third Counterclaim is denied.
3. Counterclaimants'/Respondents' Fourth Counterclaim is denied.
4. Counterclaimants'/Respondents' Fifth Counterclaim is denied.

(*id.*, at 23).

On February 23, 2023, the Newmans filed the AC in which they assert nine causes of action against NDA, NDS, Mr. Presto and Mr. Pouchie which they allege all arise under the NDS Operating Agreement and were not previously litigated in the Prior Arbitration (NYSCEF Doc. 125).

DISCUSSION

As to the minority shareholder oppression claim (first cause of action), the Newmans allege that Mr. Presto abused his authority as an officer and director of NDS and NDA by effectively shutting out the Newmans from the decision-making process in NDS in violation of Article VII

of the NDS Operating Agreement (NYSCEF Doc. No. 125, ¶¶ 126, 128). The Newmans also allege that Mr. Presto siphoned assets of NDA and NDS to related entities in order to deprive the Newmans of their rightful distributions as 49.75% interest holders of NDS (*id.*, ¶ 132). This claim cannot be dismissed based on the Prior Arbitration, because, although the Final Award found that the Newmans had not been deprived of their rightful distributions, the allegation that the Newmans had been shut out of the decision-making process in NDS and whether that constitutes minority shareholder oppression was simply not litigated in the Prior Arbitration.

As to the breach of contract claim (second cause of action), the Newmans allege that Mr. Presto breached Article VII of the NDS Operating Agreement by making expenditures in excess of \$10,000, without first obtaining the requisite written consent of Roy Newman (*id.*, ¶ 136). The Newmans allege that in 2020, NDA, at Mr. Presto and Mr. Pouchie's instruction, and without Roy Newman's consent, purchased Mr. Presto's and Mr. Pouchie's interest of Two Mikes Delights for the aggregate price of \$26,000 (*id.*, ¶ 90). Mr. Presto also authorized NDA to make numerous payments over \$10,000 to Two Mikes Delights and NDS Logistics without first obtaining Roy Newman's authorization (*id.*, ¶ 91). This claim cannot be dismissed based on the Prior Arbitration because it arises from an alleged breach of the NDS Agreement and was not litigated in the Prior Arbitration.

As to the breach of fiduciary duty claim (third cause of action), the Newmans allege that Mr. Presto, as a majority interest holder and operating manager of NDS, owed the other member fiduciary duties (*id.*, ¶ 149) which he breached by engaging in numerous self-dealing activities, including (i) directing significant labor and finances from NDA into Two Mikes Delights and

NDA Logistics without any compensation to NDA and (ii) charging personal non-business related expenses of over \$2 million to NDA without Roy Newman's approval (*id.*, at ¶¶ 150-151). This claim must be dismissed. The Final Award found that (i) Mr. Presto's activities with regards to Two Mikes Delights and NDA Logistics did not constitute a breach of his fiduciary duties and (ii) the allegation that he charged non-business related expenses to NDA was found to be without merit.

As to the declaratory judgment that Mr. Presto has been removed as operating manager of NDS for cause (fourth cause of action), the Newmans allege that Mr. Presto's breaches of the NDS Operating Agreement justify his removal for cause and that Sections 7.08 and 4.13 of the NDS Operating Agreement entitles them to affirmatively remove him as operating manager (*id.*, ¶¶ 157-159). This claim cannot be dismissed because whether Mr. Presto breached the NDS Operating Agreement and whether that breach justified a "for cause" removal was not litigated in the Prior Arbitration.

As to the aiding and abetting breach of fiduciary duty claim (fifth cause of action) against Mr. Pouchie, the Newmans allege that Mr. Pouchie was aware of Mr. Presto's fiduciary obligations to NDS and the Newmans and knowingly induced and participated in Mr. Presto's breach of those duties including helping him direct NDA resources to Two Mikes Delights and NDA Logistics (*id.*, ¶170). This claim must be dismissed because the Final Award found that Mr. Presto did not breach his fiduciary obligations.

As to the tortious interference of contract claim (sixth cause of action) against Mr. Pouchie, the Newmans allege that Mr. Pouchie improperly induced Mr. Presto to breach the NDS Operating Agreement with full knowledge of the damage to the plaintiffs that would result (*id.*, ¶¶ 175-176). This claim is not ripe for dismissal based on the Prior Arbitration because, as discussed above, whether Mr. Presto breached the NDS Operating Agreement was not litigated in the Prior Arbitration. Nor was any potential participation by Mr. Pouchie of any such breach.

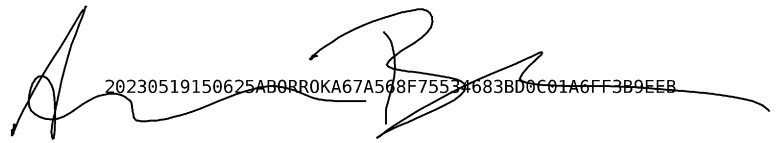
For completeness, this action is a proper derivative action and can not be dismissed because it is brought as such (*id.*, ¶ 179).

As to the breach of implied covenant of good faith and fair dealing (eighth cause of action), the Newmans allege that Mr. Presto's acts of looting, self-dealing and freezing Roy Newman out of NDA and NDS were done with the intent to deprive the Newmans of their rights as a member of NDS (*id.*, ¶ 189). This claim is not subject to dismissal based on the Prior Arbitration because although the Final Award found that Mr. Presto did not commit acts of looting or self-dealing, whether he froze the Newmans out of the decision-making process of NDS with the intent to deprive them of their rights as a member of NDS was not litigated in the Prior Arbitration. However, to the extent that the Newmans seek relief for being frozen out of the decision-making process of NDA, the claim must be dismissed because, pursuant to Article 19 of the NDA Operating Agreement, the parties agreed that all claims arising out of that agreement must be arbitrated.

Finally, the claim for an accounting of NDS (ninth cause of action) (*id.*, ¶195) can not be dismissed based on the Prior Arbitration because whether the Newmans have accounting rights was not litigated during the Prior Arbitration. However, the branch of the claim which seeks an accounting of NDA must be dismissed because Article 19 of the NDA Operating Agreement requires that claim to be arbitrated.

It is hereby ORDERED that the motion to dismiss is granted solely to the extent to the third cause of action, fifth cause of action, the branch of the eighth cause of action which seeks relief for the Newmans being frozen out of NDA, and the branch of the ninth cause of action which seeks an accounting of NDS.

The Court has considered the parties remaining arguments and finds them unavailing.



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5/19/2023
DATE

ANDREW BORROK, J.S.C.

CHECK ONE:

CASE DISPOSED

NON-FINAL DISPOSITION

GRANTED

DENIED

GRANTED IN PART

OTHER

APPLICATION:

SETTLE ORDER

SUBMIT ORDER

CHECK IF APPROPRIATE:

INCLUDES TRANSFER/REASSIGN

FIDUCIARY APPOINTMENT

REFERENCE