Albany Ave. Senior Hous. Corp. v DK Props. LLC
2023 NY Slip Op 32164(U)
June 27, 2023
Supreme Court, Kings County
Docket Number: Index No. 501392/2023
Judge: Leon Ruchelsman
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF KINGS : CIVIL TERM: COMMERCIAL 8
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ALBANY AVENUE SENIOR HOUSING CORP., on behalf of itself and derivatively on behalf of KCSR LLC,

Plaintiff, Decision and order

-against-

Index No. 501392/2023

DK PROPERTIES LLC d/b/a DKP GROUP,

Defendants,

and

June 27, 2023

KCSR LLC,

Nominal Defendant,
---x
PRESENT: HON. LEON RUCHELSMAN Motion Seq. #1

The defendant DK Properties LLC has moved seeking to change venue or alternatively to dismiss the lawsuit. The motions have been opposed. Papers have been submitted by the parties and arguments held. After reviewing all the arguments this court now makes the following determination.

Albany Avenue Senior Housing Corp., [hereinafter Albany] and DK Properties LLC [hereinafter DK] are each fifty percent owners in an entity called KCSR LLC. KCSR is the managing member of Kings County Senior Residence LLC [hereinafter the Company]. The Company was formed to acquire and operate an affordable housing property in compliance with the Federal Low Income Housing Tax Credit [hereinafter LIHTC] program pursuant to 26 USC §42 (see, Verified Direct and Derivative Complaint, ¶1 [NYSCEF Doc. No. 1]). The complaint further notes that various investor members contributed capital in exchange for tax benefits in the form of tax credits, namely MMA Kings County Senior, LLC and MMA Special Limited Partner, Inc., both managed by Boston Financial Investment Management [hereinafter BFIM]. Following the fifteen year compliance period outlined by the LIHTC program, KCSR had a one year option to either purchase the property or purchase the interests of the investor members. The complaint alleges that while Albany and DK were each half owners of KCSR, DK took control of KCSR and refused to allow KCSR to exercise its option to purchase the interests of the investor members unless Albany paid DK twenty million dollars. Essentially, the lawsuit asserts that DK frustrated KCSR from exercising the option and that Albany was harmed thereby. Albany instituted this direct and derivative action on behalf of KCSR alleging derivative and direct causes of action for breach of fiduciary duty and breach of implied covenant of good faith and fair dealing and a direct claim for a declaratory judgement. According to the complaint venue is based upon the fact Albany's principle place of business is in Kings County, the housing property is located in Kings County and "a substantial part of the events or omissions giving rise the claims here were committed in this County and directly impact the Property located in this County" (see, Verified Direct and Derivative Complaint, ¶18 [NYSCEF Doc. No. 1]).

The defendant DK has now moved seeking to change venue and transfer the case to New York County. Alternatively, DK has moved seeking to dismiss the lawsuit on the grounds it fails to include necessary parties and fails to state any cause of action. Concerning venue DK asserts that various forum selection clauses contained within agreements between the parties demand the case must be transferred to New York County.

Conclusions of Law

In 2017 CPLR §503(a) was amended to allow venue in "the county in which a substantial part of the events or omissions giving rise to the claim occurred" (id). This change now comports with the Federal venue standard and is therefore analyzed accordingly. As noted, venue is based upon that ground as well as the residence of the plaintiff. However, it is well settled that forum selection clauses are valid and govern the situs of a lawsuit unless the clause is unreasonable, against public policy or otherwise inappropriate (see, LSPA Enterprise, Inc., Jani-King of New York, Inc., 31 AD3d 394, 817 NYS2d 657 [2d Dept., 2006]).

The operating agreement of KCSR LLC states that "each Member irrevocably submits to the non-exclusive jurisdiction of the federal and state courts located in New York County, New York, over any suit, action or proceeding arising out of or relating to this Agreement" (see, Operating Agreement, ¶11.17 [NYSCEF Doc. No. 2]). The operating agreement further provides that "nothing contained herein shall affect the right of any Member to service of process in any manner permitted by law or to limit the right of any Member to bring any suit, action or proceeding against any other Member in the courts of any jurisdiction or jurisdictions" (id). Thus, on its face the KCSR operating agreement permits the filing of this action in Kings County.

DK argues that although the lawsuit concerns DK's conduct the lawsuit really arises out of the Company operating agreement. This is true because the plaintiff relies upon that operating agreement to support its claims against DK. Specifically, DK asserts that "Albany relies on numerous provisions of the Company OA...to justify its aggressive interpretation of the IMI Option, alleging that BFIM 'bargained for tax benefits, while KCSR undertook all of the risk and responsibility associated with the Company in exchange for the Company's . . . built-up equity in the Property'" (see, Memorandum in Support, page 11 [NYSCEF Doc. No. 27]).

However, any reference to the Company operating agreement does not mean the forum selection clause of that operating agreement controls the venue of this action. As noted, this lawsuit involves claims that DK breached duties to Albany (and KCSR) by frustrating KCSR's ability to exercise the option. Those claims are squarely based upon the KCSR operating agreement. To be sure, the alleged breaches may require an analysis of the Company operating agreement and the option agreement, however, that does not mean the parties are bound by the forum selection clauses of either of those operating agreements. Indeed, as with many cases, the nature of any breach requires an examination of certain documents, the conduct of the defendants, the applicable law and perhaps a trial. Surely discovery is relevant to support any claims, however, the actions which form the basis of this lawsuit arise out of duties contained only in the KCSR operating agreement. The mere fact the duties of the parties spelled out in the KCSR operating agreement may require consideration of other documents does not control venue at all.

The defendant insists that "each of Albany's claims against DK is premised on an alleged deprivation of KCSR's rights...or BFIM's rights...under the Company OA and the Option Agreement" (see, Memorandum in Support, page 11 [NYSCEF Doc. No. 27]). In truth, the deprivation of KCSR's rights is, as noted, based upon the KCSR operating agreement. Indeed, consider a hypothetical where two partners enter into contracts to purchase widgets in India. If one partner sues the other alleging some impropriety regarding the widgets contracts that would not require a lawsuit in India even if the basis for the improprieties involved Indian contracts. Of course, the Indian contracts would be necessary to determine whether in fact any impropriety occurred, however, it would be inaccurate to characterize the dispute as arising out of Indian contracts.

Thus, a fiduciary may breach a duty by engaging in actions that constitute misconduct (Kurtzman v Bergstol, 40 AD3d 588, 835 NYS2d 644, 646 [2d Dept., 2007]). While the misconduct by a fiduciary constituting a breach of duty can take one of two forms, either breach of loyalty or breach of care (Higgins v. New York Stock Exch., Inc., 10 Misc3d 257, 806 NYS2d 339 [Supreme Court New York County 2005]) the nature of any misconduct arises from the relevant agreements between the parties. Consequently, one partner can breach a duty to another partner. The precise manner in which the breach expresses itself may concern contracts in India or a Company's operating agreement or an option agreement entered into between the Company and KCSR. In either case the breach of duty only concerns Albany and DK. The manifestation of that breach does not mean the parties are bound by the forum selection clauses of those ancillary documents.

For these reasons BFIM is not a necessary party. While discovery may be required of BFIM in efforts of either party to secure their claims or defenses, they are not required to be added as parties to adjudicate whether DK breached any of its duties. In fact, a letter has been submitted by BFIM wherein they assert that "the Investor Members have no desire to become involved in Albany's and DK's dispute. The Investor Members wish to exit the Company as quickly as possible at a fair price and in a manner that maintains the Project as affordable housing. The Investor Members are happy to entertain any offers from Albany, DK, or KCSR to purchase the Investor Members' interests" (see, Letter dated April 14, 2023 [NYSCEF Doc. No. 47]). While the letter rejects Albany's interpretation of the option price provision, that does not mean the investor members are necessary parties to determine if any breach occurred. Whether Albany's exercise of the option was valid will require extensive discovery and undoubtedly judicial resolution. To the extent the investor members seek to protect their interests they may move to intervene at any time if they so choose. At this juncture they are clearly not necessary parties and the motion seeking to dismiss based on the failure to add them is denied.

Turning to the motion seeking to dismiss the complaint, it is well settled that upon a motion to dismiss the court must determine, accepting the allegations of the complaint as true, whether the party can succeed upon any reasonable view of those facts (Ripa v. Petrosyants, 203 AD3d 768, 160 NYS3d 658 [2d Dept., 2022]). Further, all the allegations in the complaint are deemed true and all reasonable inferences may be drawn in favor of the plaintiff (BT Holdings, LLC v. Village of Chester, 189 AD3d 754, 137 NYS2d 458 [2d Dept., 2020]). Whether the complaint will later survive a motion for summary judgment, or whether the plaintiff will ultimately be able to prove its claims, of course, plays no part in the determination of a pre-discovery CPLR §3211 motion to dismiss (see, Redwood Property Holdings, LLC v. Christopher, 211 AD3d 758, 177 NYS3d 895 [2d Dept., 2022]).

Section 4.01 the KCSR operating agreement appoints a management committee tasked with the "ordinary and usual decisions concerning the business affairs of the Company" (see, Section 4.01 of the Operating Agreement [NYSCEF Doc. No. 2]). Further, Section 4.27(a) states that "the Management Committee shall have the exclusive right and power to conduct the business and affairs of the Company and to do all things necessary to carry on the day-to-day business of the Company in accordance with the provisions of this Agreement and applicable law, and is hereby authorized to take any action of any kind and to do anything and everything it deems necessary or appropriate in accordance with the provisions of this Agreement and applicable law" (id). Indeed, the next section of the agreement lists eleven specific acts which the management committee may conduct. Notwithstanding the management committee's broad authority to act, Section 4.28(b) lists ten areas where the management committee maintains no authority. A careful examination of the activities wherein no authority is granted to the management committee reveals they all concern matters that are not day to day activities and all involve sweeping changes to the structure of the company and its assets. Whether exercising the option falls under activities that may be performed by the management committee is not dispositive of whether the lawsuit against DK is proper. The complaint asserts the management committee has maintained a vacancy since 2017 upon the resignation of Caple Spence and that DK has frustrated Albany's proposed replacement of that member on two occasions (see, Verified Direct and Derivative Complaint, ¶¶58-64 [NYSCEF Doc. No. 1]). Thus, the complaint alleges that DK has taken full control of KCSR notwithstanding the nominal existence of any management committee. Consequently, the complaint alleges that "DK is therefore the de facto controlling and managing member of KCSR" (id, at ¶68). If true, the complaint sufficiently alleges conduct that DK breached duties by failing to exercise the option agreement and that basis to dismiss the complaint is denied.

Next, Business Corporation Law §626(c) states that no derivative lawsuit may be commenced unless the complaint alleges "with particularity the efforts of the plaintiff to secure the initiation of such action by the board or the reasons for not making the effort" (id). As the Supreme Court noted, for a stockholder to sue derivatively "he must make an earnest, not a simulated effort, with the managing body of the corporation, to induce remedial action on their part, and this must be made apparent to the court" (see, Hawes v. City of Oakland, 104 US 450, 14 Otto 450 [1881]).

The defendant argues the plaintiff failed to comply with that provision and that consequently the plaintiff has no standing to pursue the claims. The plaintiff counters that specific evidence such notice would have been futile has been presented.

To succeed upon an assertion that notice would have been futile and hence not required, specific facts must be presented that the entity at issue was self-interested in the transactions (see, Bansbach v. Zinn, 1 NY3d 1, 769 NYS2d 175 [2003]. Thus, the plaintiff must establish that if a demand would have been filed with DK they could not have exercised independent and disinterested business judgement (id). Thus, DK will be considered incapable of being disinterested if facts support a personal benefit to it regarding the transaction being challenged (id). In that instance the business judgement rule is inapplicable and demand futility is established.

In this case, the complaint alleges that DK had material interests in the issues that comprise the causes of action, namely the demand of money from Albany as a prerequisite to exercise the option. Thus, demand upon DK or the management committee allegedly controlled by DK would obviously have been futile.

The defendant argues the standard for demand futility has not been met since the futility has not been presented with sufficient particularity. However, particularity governs the totality of the futility and as long as such futility can be discerned by the court then the particularity will naturally suffice. Thus, where the directors are accused of self-dealing then obviously futility has been presented (see, Soho Snacks Inc., v. Frangioudakis, 129 AD3d 636, 13 NYS3d 31 [1st Dept., 2015]). The nature of the claims against DK reveal that such demand would have been futile. Indeed, it cannot seriously be argued that any alleged extortion by DK can be subject to protection under the business judgement rule. Thus, demand futility has been established.

Albany's direct claims (counts three, four and five) are all adequately pled. For example, the third count alleging a direct claim of a breach of a fiduciary duty against Albany states that "DK violated these fiduciary duties, specifically the duty of care and duty of loyalty, by failing to act in Albany's best interest, instead usurping KCSR's Option to be used as a tool in furtherance of its own self-interest in extracting a commitment from Albany to make a substantial payment to exit DK from KCSR after the Option was exercised" (see, Verified Direct and Derivative Complaint, ¶190 [NYSCEF Doc. No. 1]). The remaining paragraphs of this cause of action repeatedly assert that DK breached duties to Albany by failing to exercise the option on behalf of KCSR. That is sufficient to allege a direct claim. Likewise, the fourth cause of action alleges a direct claim that DK breached its covenant of good faith and fair dealing to Albany by failing to exercise the option. Paragraph 206 alleges that "DK has interfered with Albany's economic expectations under the KCSR Operating Agreement to continue owning and operating the Property following the end of the Compliance Period, and to acquire 50% of the total equity built-up in the Property during the Compliance Period, by arbitrarily and irrationally refusing to consent to KCSR exercising its Investor Member Interest Option unless Albany first commits to paying DK $20 million to exit KCSR" (id). That adequately alleges a direct claim against Albany.

Lastly, the fifth cause of action seeks a declaratory judgement that Albany's exercise of the option, upon the fear that DK would never exercise the option, was valid. Again, that is a direct claim sought by Albany. Therefore, the motion seeking to dismiss these causes of action is denied.

Turning to the specific claims, the second and fourth causes of action allege breaches of the KCSR operating agreement. As noted, the basis of these claims is DK's failure to exercise the option unless Albany paid a sum for the option. While Section 4.34 of the Operating Agreement limits the liability of the management committee for any breaches of any duties, the allegations in this case are not directed toward the management committee but toward DK. The complaint, as noted, asserts that DK took control of the management committee and acted on behalf of the committee without any participation from any representatives of Albany. Thus, at this juncture, the complaint adequately alleges causes of action relating to the breaches of such duties and the breach of the KCSR operating agreement. It is true that Albany cannot assert claims for the breach of the option agreement to which DK was not a party, however, claims DK breached the KCSR operating agreement survive a motion to dismiss. Lastly, the complaint adequately enumerates the damages that may be suffered by the plaintiff and damages already suffered as a result of the allegations contained in the complaint. Thus, the motion seeking to dismiss the second and fourth causes of action is denied.

Concerning the first and third causes of action alleging breaches of fiduciary duty, it is well settled that when a claim for breach of a fiduciary duty is merely duplicative of a breach of contract claim where they are based on the same facts and seek the same damage then the breach of fiduciary claim cannot stand (Pacella v. Town of Newburgh Volunteer Ambulance Corps. Inc., 164 AD3d 809, 83 NYS3d 246 [2d Dept., 2018]). In this case the cause of action alleging any breaches of a fiduciary duty is identical to the breach of contract claims, namely that the defendants failed to honor the terms of the operating agreement entered into between the parties. The plaintiff argues that "the contract claims arise from provisions of the KCSR OA, while the fiduciary duty claims arise from DK's duties and obligations as KCSR's de facto managing member" (see, Memorandum in Opposition, page 20 [NYSCEF Doc. No. 35]). However, DK's 'duties and obligations' are the very same responsibilities that are outlined in the operating agreement. Thus, the claims are duplicative. Consequently, the motion seeking to dismiss the first and third causes of action is granted. The motion seeking to dismiss any other causes of action is denied.

So ordered.

ENTER:

DATED: June 27, 2023
Brooklyn N.Y.

Hon. Leon Ruchelsman
JSC