21st Century Diamond, LLC v Allfield Trading, LLC
2010 NY Slip Op 33880(U)
January 13, 2010
Supreme Court, New York County
Docket Number: 650331-2009
Judge: James A. Yates

SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: James A. Yates PART 49

Index Number : 650331/2009

21ST CENTURY DIAMOND, LLC

vs

ALLFIELD TRADING,

Sequence Number : 003

DISMISS

INDEX NO. _____

MOTION DATE _____

MOTION SEQ. NO. _____

MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to/for _____

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
Answering Affidavits — Exhibits	
Replying Affidavits	

Cross-Motion: ☐ Yes ☑ No

Upon the foregoing papers, it is ordered that this motion

is decided in accordance with the attached Decision and Order, dated January 13, 2010.

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Dated: JAN 13 2010

James A. Yates
J.S.C.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Check one: ☐ FINAL DISPOSITION ☑ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 49

21ST CENTURY DIAMOND, LLC, Plaintiff, -against- ALLFIELD TRADING, LLC, JOSHUA ALLEN, AND ROBERT CORNFIELD, Defendants, -and- ALLFIELD TRADING, LLC, Third Party Plaintiff, -against- EXELCO GROUP d/b/a EXELCO NORTH AMERICA, INC., JEAN PAUL TOLKOWSKY, FAZAL CHAUDHRI, ISIDOR, INC., AND ORI LEVY, Third Party Defendants.	Decision and Order Index No. 650331-2009

Hon. James A. Yates, J.

Plaintiff brought this action seeking injunctive, declaratory and other relief due to defendants' alleged misconduct in their former roles as day-to-day managers of plaintiff. Plaintiff moves to dismiss defendants' counterclaims (motion sequence 003), and third party defendants move to dismiss third party plaintiff's complaint (motion sequence 004). Both motions are consolidated for disposition.

Background

Plaintiff 21st Century Diamond, LLC ("21st Century") is a limited liability company organized in Delaware engaged in diamond and jewelry wholesale. The majority member of 21st Century is Exelco North America, Inc. ("Exelco"), with an 82% interest. Defendant Allfield Trading, LLC ("Allfield") owns the remaining 18%. Defendants Joshua Allen and Robert Cornfield are

former managers of 21st Century, and are principals of Allfield (collectively, "defendants"). The heart of this case involves four resolutions that 21st Century is alleged to have passed on May 18, 2009, May 21, 2009, June 2, 2009, and June 4, 2009.

On May 18, 2009, 21st Century held a members' meeting in which Cornfield, Allen, and their counsel, Thomas Mullaney, participated, to address 21st Century's substantial decline in sales. Both members of 21st Century, including the two principals of Allfield, Cornfield and Allen, received proper notice on May 11, 2009. The members passed a number of resolutions, including: (1) paying 21st Century's credit lines to the maximum extent possible, (2) adding Jean Paul Tolkowsky and Fazal Chaudhri as signatories, (3) requiring all activity taken in connection with 21st Century's bank account to be approved by Tolkowsky and Chaudhri, and (4) requiring Cornfield and Allen to deliver weekly financial reports to the members.

On May 21, 2009, 21st Century alleges that Mullaney announced that Cornfield and Allen did not intend to comply with the May 18, 2009 resolutions. Using 21st Century's funds, Cornfield and Allen paid over $300,000.00 to a company owned by their principals without Tolkowsky or Chaudhri's consent.

Accordingly, 21st Century passed further resolutions on May 28, 2009. The May 28, 2009 resolutions: (1) terminated the consulting arrangement with Cornfield and Allen and removed them as 21st Century's managers, (2) appointed Chaudhri as 21st Century's unpaid manager, and (3) granted Chaudhri sole signatory rights.

To facilitate the management transition, on May 30, 2009, Chaudhri wrote to Cornfield and Allen to ask them to meet him at 21st Century's office on June 2, 2009, at 9:00 A.M., to hand over the keys and safe codes. Unbeknownst to Chaudhri, on June 1, 2009, and very early in the morning on June 2, 2009, Cornfield, Allen, and an unidentified woman had visited 21st Century's office to remove a number of items. Additionally, on June 3, 2009, Allfield filed *21st Century Diamonds, LLC v Exelco North America, Inc.* and *Metropolitan National Bank*, Index Number 601710-2009, and sought a preliminary injunction and a temporary restraining order to prevent enforcement of the May 21, 2009, and May 28, 2009 resolutions.

In response, on June 4, 2009, 21st Century passed a resolution stating that Allfield's counsel did not have authority to act on its behalf and requiring him to withdraw the suit. The Court denied the preliminary injunction and temporary restraining

order, and Allfield discontinued its action.

On June 10, 2009, 21st Century passed an additional resolution, allowing 21st Century to file suit against defendants. Thereby, 21st Century commenced this action against defendants for: (1) injunctive relief to return all items removed from 21st Century's offices, (2) declaratory relief that the resolutions are valid, (3) injunctive relief ordering defendants to comply with the resolutions, (4) injunctive relief prohibiting defendants from taking any action on behalf of 21st Century that is not approved in advance by the members, (5) breach of contract, (6) breach of implied covenant of good faith and fair dealing, (7) breach of fiduciary duty, (8) conversion, (9) intentional interference with prospective economic advantage, and (10) fraud.

On July 17, 2009, defendants filed an amended answer with counterclaims for: (1) breach of contract (operating agreement), (2) declaration that the May 18, 2009, May 28, 2009, June 2, 2009, and June 4, 2009 resolutions are invalid, (3) declaration reinstating Cornfield and Allen as managers, (4) indemnification, and (5) constructive trust. Then, on July 24, 2009, Allfield filed a third party complaint against Exelco, Jean-Paul Tolkowsky, Fazal Chaudhri, Isidor, Inc., and Ori Levy (collectively "third party defendants"), alleging: (1) breach of contract (operating agreement), where the resolutions were allegedly improperly passed, (2) breach of implied covenant of good faith and fair dealing, (3) breach of fiduciary duty, (4) aiding and abetting breach of fiduciary duty (against Tolkowsky, Chaudhri, Isidor and Levy), (5) fraudulent inducement / misrepresentation (against Tolkowsky, Chaudhri, Isidor and Levy), (6) intentional interference with business relations and economic advantage, and (7) misappropriation of confidential information. On August 6, 2009, 21st Century filed a motion to dismiss defendants' counterclaims, and on September 24, 2009, third party defendants filed a motion to dismiss Allfield's third party complaint.

For the following reasons, 21st Century's motion to dismiss defendants' first, second, and third counterclaims for breach of contract, declaration that the resolutions are invalid, and declaration reinstating Cornfield and Allen as managers, respectively, is granted; 21st Century's motion to dismiss defendants' fourth counterclaim for indemnification is denied; and 21st Century's motion to dismiss defendants' fifth counterclaim for constructive trust is denied. Finally, third party defendants' motion to dismiss Allfield's third party complaint is granted.

Discussion

"On a CPLR 3211 motion to dismiss, the court will accept the facts as alleged in the complaint as true, accord plaintiffs the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory" (*Nonnon v City of New York*, 9 NY3d 825, 827 [2007] [internal quotation marks omitted]). Applying this standard, the Court addresses each cause of action in turn.

I. 21st Century's Motion to Dismiss Defendants' Counterclaims

A. Counterclaim 1: Breach of Contract
Counterclaim 2: Declaration that the May 18, 2009, May 28, 2009, June 2, 2009, and June 4, 2009 Resolutions are Invalid
Counterclaim 3: Declaration Reinstating Cornfield and Allen as Managers

Under the Operating Agreement, section 5.3 (a) states:

> "The Members may from time to time designate such managers as they may deem necessary to carry out the day-to-day operations of the Company. Such managers need not be Members, and shall have such duties, powers, responsibilities and authority as may from time to time be prescribed by the Members, and may be removed at any time, with or without cause, by the Members."

(*See* affidavit of Stephen J. Pearson, Aug. 6, 2009, exhibit B [Operating Agreement], § 5.3 [a].)

Additionally, section 5.8 states:

> "*Action without Meeting. Any action required or permitted to be taken at any meeting of the Members may be taken without a meeting of the Members*, without prior notice and without a vote, *if Members holding voting interests sufficient to authorize such action at a meeting* at which all of the Members entitled to vote thereon were present and voted *consent thereto in writing*. Such consents shall be delivered to the Company and the Members by hand or by certified or registered

> mail, return receipt requested, for filing with the Company records. Action taken under this *Section 5.8* shall be effective when all necessary Members have signed a consent unless the consent specifies a different effective date."

(*See id.*, exhibit B [Operating Agreement], § 5.8 [emphasis added].)

Title 6, Section 18-302 (d) of the Delaware Code Annotated is consistent with section 5.8 of the Operating Agreement. It states, in relevant part:

> "Unless otherwise provided in a limited liability company agreement, on any matter that is to be voted on, consented to or approved by members, the members may take such action without a meeting, without prior notice and without a vote if a consent or consents in writing, setting forth the action so taken, shall be signed by the members having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting at which all members entitled to vote thereon were present and voted."

(*See* 6 Del C § 18-302 [d].)

Defendants interpret section 5.8 of the Operating Agreement to mean that there must be a meeting to decide that there does not need to be a meeting. Defendants cite *VGS, Inc. v Castiel & Virtual Geosatellite LLC*, 27 Del J Corp L 454, 458 (Del Ch 2000), arguing that it invalidates an action by written consent where voting rights are rendered "superfluous."

However, in *VGS*, the Court found that the majority vote of the LLC's Board of Managers could properly effect a merger. The court confirmed that the provision, "read literally, does not require notice to [the minority] before [the majority] could act by written consent." (*See id.* at 459.) But, the Court also found that two managers failed to discharge their duty of loyalty to the third manager in good faith by failing to give him advance notice of their merger plans under the unique circumstances of this case and the structure of this LLC Agreement. Accordingly, the Court declared the acts taken to merge as invalid, and the merger was ordered rescinded. This is not an issue here.

Rather, 21st Century correctly interprets section 5.8 of the Operating Agreement under its plain meaning. That is, Exelco, which holds an 82% interest, may take action without a meeting with written consent. (*See also Stellini v Oratorio*, 1979 WL 2703, *3, 1979 Del Ch LEXIS 472, *9 [denying motion for summary judgment for former director, and granting cross-motion for summary judgment for majority members, on action by written consent of majority members pursuant to Del Code Ann, tit 8, § 228 [a], which mirrors 6 Del C § 18-302 [d] for corporations].)

Thus, the first, second, and third counterclaims for breach of contract, declaration that May 18, 2009, May 28, 2009, June 2, 2009, and June 4, 2009 resolutions are invalid, and declaration reinstating Cornfield and Allen as managers, respectively, are dismissed.

B. Counterclaim 4: Indemnification
Counterclaim 5: Constructive Trust

Article 9.1 (a), (b) of the Operating Agreement states:

> "(a) *[T]he Company shall indemnify and hold harmless the Members*, officers, agents and employees of the Company and their respective shareholders, officers, directors, employees, agents, and other Affiliates (each, an "Indemnitee") *against all costs*, liabilities, claims, damages, fines, fees, penalties, deficiencies, losses and expenses (including, without limitation interest, court costs, fees of attorneys, accountants and other experts or other expenses of litigation or other proceedings or of any claim, default or assessment) (collectively, "Losses") *paid or incurred by any such Person in connection with the conduct of the Company's business*, except to the extent such Losses arise out of the fraud, gross negligence or willful misconduct of such Person; and
>
> (b) *[E]ach Indemnitee who at any time is, or has been, a Member*, officer, agent or employee of the Company (an "*Affiliate Indemnitee*"), *and is threatened to be,*

> *or is, made a party to any action*, suit or proceeding, whether civil, criminal, administrative or investigative, *by reason of the fact that he or it is, or was, a Member*, officer, agent or employee of the Company, or is serving, or has served, at the request of the Company as an officer, member, employee or agent of another Person, *shall be indemnified against all Losses actually and reasonably incurred in connection with any such pending, threatened or completed action*, suit or proceeding, except to the extent such Losses arise out of the fraud, gross negligence or willful misconduct of such Person."

(*See* affidavit of Stephen J. Pearson, Aug. 6, 2009, exhibit B [Operating Agreement], § 9.1 [a], [b].)

Defendants argue that the Operating Agreement and Delaware Law permit indemnification (*see Schoon v Troy Corp.*, 948 A2d 1157 [Del Ch 2008] [advancing indemnification fees for director for his defense of litigation brought by corporation against him alleging breach of fiduciary duty]; *Hibbert v Hollywood Park, Inc.*, 457 A2d 339 [Del Ch 1982] [indemnifying former director in litigation commenced by him against company challenging election process]). On the other hand, 21st Century argues that logically, these provisions cannot cover claims brought by 21st Century against its own members, because that would mean that it would pay for both the prosecution and defense of such claims as well as any damage awards, mooting the whole litigation.

21st Century cites no case law. Since the contract appears clear on its face, there is no basis for dismissal at this time.[1] Thus, 21st Century's motion to dismiss the fourth counterclaim for indemnification is denied.

As well, 21st Century's motion to dismiss the fifth counterclaim for constructive trust is denied (*compare* Answer with Counterclaims, July 15, 2009, ¶¶ 19, 44 ["In 2007, in order to assist the newly formed company to get started, Cornfield and

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[1] The Court notes that the indemnification provisions do not apply to losses arising out of fraud, gross negligence or willful misconduct (*see* affidavit of Stephen J. Pearson, Aug. 6, 2009, exhibit B [Operating Agreement], § 9.1 [a], [b]).

Allen agreed to defer receipt of salary . . . The May 28, 2009 purported resolutions, *inter alia*, [] improperly terminated Allen and Cornfield as managers, rescinded all current and past salary and fees they were due."], *with Pinkava v Yurkiw*, 64 AD3d 690, 693 [2d Dept 2009] [denying motion to dismiss unjust enrichment claim because "allegations of payment . . . and their contribution of time managing the property was sufficient to establish the transfer in reliance and unjust enrichment elements of a cause of action for a constructive trust"]).

II. Third Party Defendants' Motion to Dismiss Allfield's Third Party Complaint

First, third party defendants' motion to dismiss Allfield's first, second, third, and fourth third party causes of action for breach of contract, breach of implied covenant of good faith and fair dealing, breach of fiduciary duty, and aiding and abetting breach of fiduciary duty (against Tolkowsky, Chaudhri, Isidor and Levy), respectively, is granted for the reasons previously stated (*see infra* I.A).

Second, Allfield fails to state a claim for fraudulent inducement. Allfield alleges that Cornfield and Allen had nurtured Tolkowsky's contacts at Sterling Jewelers. Sterling had invited Tolkowsky to make a proposal to carry "Tolkowsky" jewelry in stores. (Third Party Complaint ¶ 36.) Allfield states that it was discussing pricing with Sterling (*id.* ¶ 39).

Allfield alleges that Tolkowsky requested Levy to participate in the Sterling transaction (*id.* ¶ 44). Allfield further claims that it reminded Tolkowsky that Sterling "would remain a 21st Century program," with which Tolkowsky and Levy "superficially agreed" (*id.* ¶ 45). Based on these representations, Cornfield discussed confidential pricing information and proposals for Sterling with Levy, when Levy was in fact a competitor (*id.* ¶ 48). Allfield then alleges that Tolkowsky "wrested control of the Sterling program for himself" (*id.* ¶ 53).

To state a claim for fraudulent misrepresentation, a plaintiff must prove (1) the defendant made a material false representation, (2) the defendant intended to defraud the plaintiff, (3) the plaintiff reasonably relied on the representation, and (4) the plaintiff suffered damage as a result of its reliance (*J.A.O. Acquisition Corp. v Stavitsky*, 18 AD3d 389, 391 [1st Dept 2005]).

However, Allfield has failed to allege any material false

representations. The only identified statement is that Levy and Tolkowsky represented that "the Sterling transaction would stay a 21st Century opportunity" (Third Party Complaint ¶ 47). This alleged statement is nothing more than a mere expression of future expectation, which is insufficient to form the basis of a fraudulent inducement claim (*see Hewlett v Staff*, 235 AD2d 696, 697 [3d Dept 1997]). Additionally, Allfield has failed to allege that third party defendants intended to defraud *Allfield*. This was a 21st Century opportunity, not an Allfield opportunity. Thus, third party defendants' motion to dismiss Allfield's fifth third party cause of action for fraudulent inducement / misrepresentation is granted.

Third, Allfield fails to state a claim for intentional interference with business relations. "The required elements of a cause of action for tortious interference with prospective business relations are as follows: (a) business relations with a third party; (b) the defendant's interference with those business relations; (c) the defendant acting with the sole purpose of harming the plaintiff or using wrongful means; and (d) injury to the business relationship" (*Advanced Global Tech. LLC v Sirius Satellite Radio, Inc.*, 15 Misc 3d 776, 779 [Sup Ct, NY County 2007], citing *Guard-Life Corp. v Parker Hardware Mfg. Corp.*, 50 NY2d 183 [1980]). But, as stated earlier, Allfield has failed to allege that the third party defendants intended to defraud *Allfield*, as opposed to 21st Century. Again, this was a 21st Century opportunity, not an Allfield opportunity. Thereby, third party defendants' motion to dismiss Allfield's sixth third party cause of action for intentional interference with business relations is granted.

Finally, Allfield's claim for misappropriation of confidential information is also dismissed. "[U]nfair competition and the misappropriation and exploitation of confidential information is the loss of profits sustained by reason of the improper conduct . . . limited to lost profits resulting from the defendant's actual diverting of customers" (*Suburban Graphics Supply Corp. v. Nagle*, 5 AD3d 663, 666 [2d Dept 2004] [internal quotation marks omitted]). However, as stated earlier, Allfield has no standing as an injured party on behalf of 21st Century. Accordingly, third party defendants' motion to dismiss Allfield's seventh third party cause of action for misappropriation of confidential information is granted.

Conclusion

For the reasons stated, it is hereby:

[* 11]

ORDERED, that 21st Century's motion to dismiss defendants' counterclaims is granted and the first, second, and third counterclaims for breach of contract (operating agreement), declaration that the May 18, 2009, May 28, 2009, June 2, 2009, and June 4, 2009 resolutions are invalid, and declaration reinstating Cornfield and Allen as managers, respectively, of the answer are severed and dismissed; and it is further

ORDERED, that the remainder of the action shall continue; and it is further

ORDERED, that third party defendants' motion to dismiss Allfield's third party complaint is granted and the third party complaint is dismissed with costs and disbursements to the third party defendants as taxed by the Clerk of the Court; and it is further

ORDERED, that the Clerk is directed to enter judgment accordingly.

Dated: January 13, 2010

JAN 13 2010

ENTER:

James A. Yates

James A. Yates, J.S.C.