

Casey Capital, LLC v Levy
2016 NY Slip Op 31619(U)
August 19, 2016
Supreme Court, New York County
Docket Number: 652805/15
Judge: Saliann Scarpulla
Cases posted with a "30000" identifier, i.e., 2013 NY Slip Op <u>30001</u> (U), are republished from various state and local government websites. These include the New York State Unified Court System's E-Courts Service, and the Bronx County Clerk's office.
This opinion is uncorrected and not selected for official publication.

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 39

-----X
CASEY CAPITAL, LLC, GAMMA OPPORTUNITY
FUND, LP, and KEVIN M. CASEY,

Plaintiffs,

-against-

LAWRENCE LEVY and EDWARD LEVY,

Index No. 652805/15

Defendants,

and

ESSEX RENTAL CORP., a Delaware
Corporation,

Nominal Defendant.

-----X
SALIANN SCARPULLA, J.:

In this stockholders' derivative action alleging, among other things, breach of fiduciary duty, defendants Laurence Levy¹ ("L. Levy") and Edward Levy ("E. Levy")² (collectively, the "Director Defendants"), and nominal defendant, Essex Rental Corp. ("Essex Rental" or the "Company") move (in motion sequence number 001) to dismiss the complaint, pursuant to CPLR 3211 (a) (7), based upon lack of standing.

¹ Laurence Levy is incorrectly named in the caption as Lawrence Levy.

² Although they share the same surname, L. Levy and E. Levy are apparently unrelated.

Plaintiffs Casey Capital, LLC, Gamma Opportunity Fund and Kevin M. Casey (collectively, "Casey Capital" or "Plaintiffs") are stockholders in the Company and brought this action for the benefit of Essex Rental.

Essex Rental, a Delaware corporation, was formerly known as Hyde Park Acquisition Corporation. In October 2008 it acquired Essex Crane Rental Corp. and in November 2010 it acquired the assets of Coast Crane Company. Through those acquisitions, Essex Rental is one of North America's largest providers of lifting equipment.

The board of directors of Essex Rental is composed of two classes of directors, with one class of three directors elected every year.³ L. Levy is the chairman of the board of Essex Rental and served as its chief executive officer from the Company's inception until October 2008. E. Levy was a member of the board of directors from Essex Rental's inception through June 2015 and served as its president until 2008. According to the complaint, during the Director Defendants' time on the board, the Company's stock price plummeted from \$7.64/share in 2011 to less than \$.60/share in 2015.

In April 2015, plaintiff Casey Capital announced that it intended to wage a proxy battle in connection with the scheduled election of three members of the board of directors in June 2015. Once the proxy challenge was announced, the Company stated that it was undertaking a search to identify a management slate of candidates, but

³ Plaintiffs allege that by staggering the elections L. Levy maintains control of the board.

subsequently indicated that it intended to fill only two of the three open spots on the board. Plaintiffs allege that the board reduction decision was made in order to insure that L. Levy could continue to control the board in the face of the insurgents' challenge and constituted a violation of the Certificate of Incorporation of Essex Rental, which provides that each class of the board of directors "shall be nearly as equal as possible."

Plaintiffs further allege that the Company initially challenged the name of one of their two board nominees, contending that the nominees were defective, though it later withdrew its objection. The Casey Capital nominees were ultimately elected to the two seats being filled, resulting in a board consisting of L. Levy, Bill Fox ("Fox"), Nick Matthews ("Matthews"), who is the CEO of the company, and the two newly elected Casey Capital nominees, Lee D. Keddie and John Climaco. The nominating committee then elected Fox to chair two board committees, and L. Levy to chair the audit committee and sit on all of the other committees.

After the board elections, Plaintiffs brought this action on behalf of the corporation, pursuant to section 626 of the Business Corporation Law, "to redress injuries suffered and to be suffered by the Company as a result of the Director Defendants' violations of their fiduciary obligations." Specifically, Plaintiffs allege that L. Levy and E. Levy breached their fiduciary duty to Essex Rental in the following four areas: 1) Compensation – despite the Company's poor performance, L. Levy and E. Levy were compensated for serving as directors and sitting on board committees in amounts that Plaintiffs claim are more suitable to "large" companies (i.e. companies with annual revenues of \$2.5 to \$10 billion); 2) Rental of office space – L. Levy allegedly caused

Essex Rental to lease unnecessary and “pricey” office space in New York City from a firm with which he is affiliated, Hyde Park Real Estate LLC; 3) Errors in financial statements – errors were allegedly made in the 2013 and 2014 financial statements while the Director Defendants were “at the helm” of the Audit Committee, causing damage to the Company’s financial credibility; and 4) 2015 election – the board of directors election was allegedly manipulated by the Director Defendants, resulting in a board controlled by L. Levy.

Defendants move to dismiss the complaint arguing that Plaintiffs’ failed to comply with the requirements of Business Corporation Law (BCL) § 626 in that they “have not alleged that a majority of the Board is disabled from considering their demand” and they therefore lack standing to bring a derivative action on behalf of the Company.

Discussion

On a motion to dismiss pursuant to CPLR 3211 (a), the court must “accept the facts alleged in the complaint as true, accord plaintiff[] the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory.” *Leon v. Martinez*, 84 N.Y.2d 83, 87-88 (1994); *Cabrera v. Collazo*, 115 A.D.3d 147, 150-151 (1st Dept. 2014).

As a threshold matter, the parties disagree on whether New York or Delaware law govern this derivative action.⁴ Issues of corporate governance are governed by the law of

⁴ Plaintiffs argue that DE law is applicable while Defendants posit that NY law applies.

the State in which the corporation is chartered. *Lerner v. Prince*, 119 A.D. 3d 122 (1st Dept. 2014); *Hart v. General Motors Corp.*, 129 A.D.2d 179, 182 (1st Dept. 1987); see *Venturetek, L.P. v. Rand Pub. Co., Inc.*, 39 A.D.3d 317 (1st Dept. 2007) (finding that “[i]t is well settled that the law of the state in which an entity was incorporated [] is controlling as to matters relating to its internal affairs”). Here, Delaware law applies because Essex Rental is a Delaware corporation.

Under Delaware law, “the right of a stockholder to prosecute a derivative suit is limited to situations where the stockholder has demanded that the directors pursue the corporate claim and they have wrongfully refused to do so or where demand is excused because the directors are incapable of making an impartial decision regarding such litigation.” *Rales v. Blasband*, 634 A.2d 927, 932 (Del. 1993). Further, a derivative suit complaint must “allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and the reasons for the plaintiff’s failure to obtain the action or for not making the effort.” Del. Ch. Ct. R. 23.1 (a). The Delaware rule rests on the foundation that “the business affairs of a corporation ... shall be managed by or under the direction of a board of directors.” *Aronson v Lewis*, 473 A.2d 805, 811-812 (Del. 1984) (citation omitted), *partially overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000) (“By its very nature the derivative action impinges on the managerial freedom of directors” and thus “the demand requirement is a recognition of the fundamental precept that directors manage the business and affairs of corporations.”).

Plaintiffs state that in this case a pre-suit demand on the board is not required because such demand would have been futile. Plaintiffs' contend that three of the five current members of the board "at all relevant times were interested, lacked independence or faced a threat of liability and therefore would not be able to impartially consider a demand by Plaintiffs." Plaintiffs further allege that the board's actions to manipulate the election process were taken with the knowledge and approval of all board members, had no justifiable business purpose, and raise a reasonable doubt regarding the interests and independence of three of the board members. Finally, Plaintiffs allege that the payment of what it describes as excessive directors' fees and rent could not have been a valid exercise of business judgment given the cash position of the company.

In order to demonstrate futility under Delaware law, "the burden is upon the plaintiff in a derivative action to overcome [the] presumption" that the company's directors were "faithful to their fiduciary duties." *Beam ex. rel. Martha Stewart Living Omnimedia, Inc. v. Stewart*, 845 A.2d 1040, 1048-1049 (Del. 2004). Moreover, "a director will be considered unable to act objectively with respect to presuit demand if he or she is interested in the outcome of the litigation or is otherwise not independent." *Id.* at 1049. A trial court must determine whether the factual allegations of the complaint "create a reasonable doubt" that the board could have exercised its independent and disinterested business judgment in responding to a demand. *Aronson*, 473 A.2d at 818.

The protections of the Delaware business judgment rule can be claimed only by disinterested directors. "[T]his means that directors can neither appear on both sides of a transaction nor expect to derive any personal financial benefit from it in the sense of

self-dealing, as opposed to a benefit which devolves upon the corporation or all stockholders generally.” *Id.* at 812. Next, “to invoke the rule’s protection directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them. Having become so informed, they must then act with requisite care in the discharge of their duties.” *Id.* Under the Delaware rule, a plaintiff need “only allege facts which, if true, show that there is a reasonable inference that the business judgment rule is not applicable for purposes of considering a pre-suit demand pursuant to Rule 23.1.” *Id.* at 809 (citation omitted).

Here, the Plaintiffs’ allegations as to demand futility are entirely conclusory. Plaintiffs’ first argument, that demand was futile because the contested fees and rent could not have been a valid exercise of business judgment by the board, is the type of circular reasoning that has been found insufficient to establish demand futility by Delaware courts. *See In re INFOUSA, Inc. Shareholders Litigation*, 953 A.2d 963, 972 (Del. Ch. 2007) (finding that plaintiffs’ argument that “demand would be futile with respect to the defendant directors simply because no board, in the exercise of its business judgment, could ever have doled out so much largess to [Defendant]” is the same kind of argument that “has been roundly rejected by this Court as circular reasoning that would eviscerate the business judgment rule of any purpose.”)

Plaintiffs’ second demand futility allegation, that three of the five directors of the current board “at all relevant times were interested, lacked independence or faced a threat of liability and therefore would not be able to impartially consider a demand by Plaintiffs,” is also deficient. Plaintiffs’ complaint fails to identify the three interested

directors. In any event, it is uncontested that two of the five current board members, Lee Keddie and John Climaco, were elected as a result of the proxy battle initiated by the Plaintiffs, so there is no basis to allege that they lacked impartiality. I therefore presume that Plaintiffs contend that the interested directors are L. Levy, Matthews, and Fox.

As Defendants point out, Matthews is not even mentioned by name in the complaint, and Fox is mentioned only as having been elected to chair two unspecified committees. Indeed, the complaint is devoid of any factual allegations showing how Fox and Matthews were interested in the alleged breaches of fiduciary duty by the Director Defendants, faced a threat of liability, lacked independence, or were controlled by L. Levy. In addition, the fact that Fox and Matthews may have approved decisions by the board which resulted in the challenged corporate actions is insufficient under Delaware law to demonstrate lack of impartiality. As stated by the Delaware Supreme Court, if “any board approval of a challenged transaction automatically connotes ‘hostile interest’ and ‘guilty participation’ by directors,” then the Delaware demand requirement would be rendered meaningless. *Aronson*, 473 A2d at 814.

The only substantive allegations in the complaint concerning current directors relate to L. Levy, against whom Plaintiffs’ assert a breach of fiduciary duty claim.⁵ Notably, “a derivative complaint must plead facts specific to each director, demonstrating that at least half of them could not have exercised disinterested business judgment in

⁵ The other individual defendant, E. Levy, withdrew as a candidate for director and was no longer on the board so is not relevant to an analysis of whether demand futility existed here.

responding to a demand.” *Desimone v. Barrows*, 924 A.2d 908, 943 (Del. Ch. 2007); see also *Teamsters Union 25 Health Services & Insurance Plan v. Baiera*, 119 A.3d 44, 57 (Del. Ch. 2015) (stating that “to establish demand futility... [p]laintiff must impugn the ability of at least half of the directors in office when it initiated this action (*i.e.*, the Demand Board) to have considered a demand impartially.”). Because Plaintiffs’ complaint falls far short of this specificity requirement, I find that demand is not excused in this case. As Plaintiffs have not established demand futility, their failure to make a demand on the board requires a dismissal of this complaint.

Having determined that Defendants demonstrated Plaintiffs’ lack of standing to bring a derivative suit, it is unnecessary for me to review the adequacy of Plaintiffs’ cause of action.

Accordingly, it is hereby

ORDERED that Defendants’ motion to dismiss is granted and Plaintiffs’ complaint is dismissed in its entirety, with costs and disbursements to Defendants as taxed by the Clerk of the Court, and the Clerk is directed to enter judgment accordingly in favor of Defendants.

This constitutes the decision and order of the Court.

DATE:

8/19/14


SALIANN SCARPULLA, JSC