SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 39

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IN THE MATTER OF THE APPLICATION OF ALAN ADES,,

Petitioner,

- v -

FOR THE DISSOLUTION OF A&E STORES, INC., A DOMESTIC CORPORATION, PURSUANT TO SECTION 1104 OF THE NEW YORK BUSINESS CORPORATION LAW,

Respondent.

INDEX NO. 650267/2017

MOTION DATE _____

MOTION SEQ. NO. 001

DECISION AND ORDER

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The following e-filed documents, listed by NYSCEF document number 12, 18, 19, 20, 22, 25, 29, 30, 31, 32, 33, 35, 36, 37, 38, 39, 40, 41, 42, 43, 44, 45, 46, 47

were read on this application to/for Dissolution.

HON. SALIANN SCARPULLA:

Petitioner Alan Ades ("Ades") commenced this special proceeding by Verified Petition and Order to Show Cause (motion seq. no. 001) seeking the dissolution of A&E Stores, Inc. ("A&E") pursuant to Business Corporation Law ("BCL") § 1104(a) (1), (2), and (3) and for the appointment of a permanent receiver to wind up A&E's affairs.

Background

A&E was incorporated in 1973. Ades is a 50% shareholder of A&E, Albert Erani ("Erani") is a 25% shareholder, and Erani's brother, Dennis Erani, is a 25% shareholder. A&E's Board of Directors has four members: Ades, Robert Ades (Ades's son), Erani, and Dennis Erani (collectively, "Directors"). A&E's by-laws provide that, if either Ades

or Robert Ades are no longer able or willing to serve on the Board of Directors, the vacancy would be filled by and Ades's nominee, and if either Erani or Dennis Erani are no longer able or willing to serve on the Board of Directors, that vacancy would be filled by and Erani nominee. A&E's bylaws do not provide any mechanism for avoiding deadlock or for dissolution.

Through the operation of A&E, the shareholders developed and operated three retail clothing chain stores, "Strawberry," Bolton's," and "Pay Half."[1] Currently, A&E's day-to-day operations are performed by three senior executives, and Ades and Erani no longer work at A&E fulltime.

In or around October 2014, Ades and Erani adopted a shareholders' resolution permitting either Ades or Erani to unilaterally close all non-Bolton's A&E stores by March 31, 2016. On or about November 10, 2015, Ades and Erani modified the October 2014 resolution ("Store-Closing Plan"), in part to extend deadline for the closing of non-Bolton's stores to August 31, 2016 and to extend the deadline for converting one of the stores to a Bolton's to April 16, 2016.

Ades contends that, in or around 2015, he decided that he no longer wished to continue operating A&E because it has become increasingly less profitable. Erani disputes Ades's contention regarding the profitability of A&E, and claims that A&E has continued to operate at a profit.

[1] "Each store in the chain has been represented by a separate entity that holds the lease to the store's premises. The store-level entities are owned 50/50 by the same shareholders as A&E stores, and have an identical Board composition." Pet. ¶ 6.

Ades acknowledges that the shareholders disagree with him and wish to continue operating A&E, but nevertheless concludes that A&E should be sold or liquidated so that he may get the best return on his investment. Ades asserts that various disputes have arisen between himself and Erani and Dennis Erani throughout 2016. The disputes specifically regarded whether to close A&E or whether to continue operating and investing in A&E by updating the computer systems, opening additional stores, extending stores' leases, hiring employees, and maintaining its trademark. Ades also asserts that Erani and Dennis Erani have countermanded Ades's instructions given to various executives and employees, which Erani denies.

On or around November 29, 2016, Ades sent a notice to Erani and Dennis Erani proposing a joint meeting of the Board of Directors and shareholders. The notice proposed a resolution to sell or liquidate A&E within 180 days. On or around December 15, 2016, the Directors met for the joint meeting of the Board of Directors and shareholders. This joint meeting ended early and Ades's resolution was not discussed because Erani and Dennis Erani refused to continue the meeting unless it was tape recorded, to which Ades refused to consent.[2]

Ades asserts that he withheld consent to tape record the meeting because he thought that Erani and Dennis Erani "would simply make self-serving statements and engage in posturing, rather than participate in a meaningful dialogue," Pet. ¶ 22, and no prior meeting had ever been tape recorded. Ades concludes that the tape recording

[2] Ades does not specify whether the December 15, 2016 meeting was the only meeting where the Directors were not able to achieve the votes required for A&E action.

demand demonstrates that the relationship between shareholders has completely broken down and that they are no longer able to work together. Erani, however, disputes Ades's assertions and claims that he insisted on tape recording the meeting because Ades was becoming increasingly forgetful and would often revoke consent for business decisions that he previously consented to or approved.

Also on or around December 15, 2016, Ades unilaterally entered into an agreement with the landlord for the Strawberry store on 42nd Street ("42nd Street Strawberry"), whereby he arranged to close the store and surrender the lease by February 2017. Ades had been negotiating this lease since October 19, 2016, and claims that these actions were taken pursuant to the Store-Closing Plan. Erani – insisting that Ades did not have the authority to act unilaterally here because it was after August 31, 2016, the Store-Closing Plan's deadline – then sent a letter to the landlord in a failed attempt to impede the lease surrender and closing of the 42nd Street Strawberry.

Based on the foregoing, Ades commenced this proceeding by Verified Petition and Order to Show Cause seeking the dissolution of A&E pursuant to BCL § 1104(a)(1), (2), and (3) and for the appointment of a permanent receiver to wind up A&E's affairs.[3]

Erani opposes dissolution and asserts that a hearing is required. Erani contends that, once he refused to consent to Ades's suggestion that they cease A&E's operations,

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[3] On January 20, 2017, I signed Ades's proposed order to show cause and issued a TRO which, in part, limited monthly distributions to shareholders and enjoined shareholders from making any material changes to A&E's business or operations or entering into any transaction outside of the ordinary course of business without Ades's written approval.

Ades deliberately caused disputes in 2016 by acting and taking positions that were directly aimed at harming A&E financially and forcing it out of business. Erani posits that these manufactured disputes are what Ades cites to justify dissolution. Erani also alleges Ades created disputes by voting for resolutions but later revoking his consent once substantial time, effort, and/or money was expended to execute them.[4] Therefore, Erani concludes that any alleged deadlock or dissension was manufactured by Ades in bad faith to force dissolution of A&E.

Further, Erani disputes the existence of dissension or deadlock. He argues that the decision of whether to continue operating A&E or to sell or liquidate the business does not constitute deadlock; while Ades's practice of unilaterally revoking his consent for certain business decisions may have possibly resulted in deadlock, no deadlock occurred and A&E continued to function because Erani yielded to Ades regarding most disputed business decisions. Erani also argues that, regardless of any alleged deadlock or dissension, A&E continues to function because three senior executives manage A&E's day-to-day operations. Any disagreement between himself and Ades has not prevented A&E from functioning.

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[4] For example, while Ades contends that A&E is not able to function effectively because of outdated technology, Erani alleges that the parties voted and agreed to update its operating software. After A&E expended numerous resources and almost a year researching finding adequate software and signed the purchasing contract, Ades unilaterally changed his mind and reversed his decision. Another example that Erani cites is that the parties voted and agreed to convert two of their stores to Bolton's. Ades then changed his mind and rescinded consent for these conversions shortly before the stores were scheduled to open, after the merchandise was purchased and stored in a warehouse.

Discussion

A shareholder owning at least "one-half of the votes of all outstanding shares of a corporation entitled to vote in an election of directors" may petition the court for dissolution based on at least one of the following grounds:

> (1) That the directors are so divided respecting the management of the corporation's affairs that the votes required for action by the board cannot be obtained.
> (2) That the shareholders are so divided that the votes required for the election of directors cannot be obtained.
> (3) That there is internal dissension and two or more factions of shareholders are so divided that dissolution would be beneficial to the shareholders.

BCL § 1104(a).[5] The petition for dissolution may be granted summarily – "[a] hearing is only required where there is some contested issue determinative of the validity of the application." *Weiss v. Gordon*, 32 AD2d 279, 280 (1st Dept 1969) (internal citations omitted); *Matter of Klein Law Group, P.C.*, 134 AD3d 450 (1st Dept 2015).

Once a petitioner has established a prima facie showing of entitlement to dissolution, it is entirely within the court's discretion whether to issue an order granting dissolution, *see* BCL § 1111(a), and "[t]he ultimate remedy of dissolution and forced sale of corporate assets should only be applied as a last resort." *Matter of Klein Law Group,*

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[5] While Ades is seeking dissolution pursuant to BCL § 1104(a)(1), (2), and (3), he has not made any showing under BCL §1104(a)(2) that "the shareholders are so divided that the votes required for the election of directors cannot be obtained." The November 21, 2012 Unanimous Written Consent between the shareholders obviates any need for a shareholder election to replace a vacant seat on the Board of Directors. Thus, Ades is not entitled to dissolution of A&E pursuant BCL § 1104(a)(2) and the discussion and analysis below are only pursuant to BCL § 1104(a)(1) and (3).

P.C., 134 AD3d at 450 quoting *Application of Ng*, 174 AD2d 523, 526 (1st Dept 1991) (internal citations omitted).

Dissolution is generally appropriate where the complained of internal dissension and/or deadlock impedes the daily functioning of the corporation, *see generally Hayes v Festa*, 202 AD2d 277, 277 (1st Dept 1994), thereby "pos[ing] an irreconcilable barrier to the continued functioning and prosperity of the corporation," *Matter of T.J. Ronan Paint Corp.*, 98 AD2d 413, 421 (1st Dept 1984).

Where the undisputed facts show that genuine dissension and/or deadlock exists, it is irrelevant who is at fault for the underlying conflict, and a hearing is not required. *Id.* at 422. "Rather, the critical consideration is the fact that dissension exists and has resulted in a deadlock precluding the successful and profitable conduct of the corporation's affairs." *Id.* (finding that "deadlock [was] harmful to the continued success of the corporation, such clearly established by four years of 'corporate warfare', during which [petitioner] was accused of theft, allegedly beaten, denied his salary, and locked out of the corporate offices, which, as a result were exclusively presided over by [respondent]"). *See also Neville v. Martin*, 29 AD3d 444 (1st Dept 2006); *Application of Glamorise Foundations, Inc.*, 228 AD2d 187, 189 (1st Dept 1996); *Matter of Dream Weaver Realty*, 70 AD3d 941, 942 (2d Dept 2010); *Matter of Eklund Farm Machinery, Inc.*, 40 AD3d 1325, 1326-27 (3d Dept 2007).

However, even if dissension and/or deadlock do exist, allegations that a petitioner acted in bad faith by creating the underlying disputes to justify dissolution "constitute a defense to a dissolution proceeding," and a hearing is required. *Myers v Gold*, 77 AD2d

652, 653 (2d Dept 1980) (internal citations omitted); *see Application of Glamorise Foundations, Inc.*, 228 AD2d at 189; *Feinberg v Silverberg*, Index No. 3120-2011 (Sup Ct, Nassau County 2013) (citing *Kavanaugh v. Kavanaugh Knitting Co.*, 226 NY 185 [1919] and concluding that the "manufactured creation of the dissension . . . is the *sine qua non* of bad faith" and petitioner's "[intent] for creating dissension and deadlock is nevertheless relevant"); *Matter of Rappaport*, 110 AD2d 639, 641 (2d Dept 1985). *But see Matter of Eklund Farm Machinery*, 40 AD3d at 1326-27 (summarily granting dissolution despite allegations that petitioner acted in bad faith by "creat[ing] dissension to obtain dissolution" where the record clearly established that the petitioner was completely excluded from control and operation of the corporation by respondent).

Here, there is no dispute that Ades and Erani disagree as to whether A&E should be dissolved or whether it should continue to operate. However, A&E is not a service corporation,[6] and because neither Ades nor Erani are responsible for A&E's day-to-day operations, this disagreement "is not dispositive of the fundamental issue of whether the conditions of the statute have been satisfied such that the extraordinary step of judicial dissolution is warranted." *Application of Glamorise Foundations, Inc.*, 228 AD2d at 189; *Wagner v Dombrowsky*, 6 Misc 3d 1041(A) (Sup Ct, Nassau County 2004) ("the internal dissension does not arise from the day-to-day operation of the properties but rather,

[6] In service-oriented close corporations, courts have found that a petitioner seeking dissolution based on the desire not to continue the business does not constitute bad faith and may be sufficient to justify dissolution. *See, e.g.*, *Weiss*, 32 AD2d at 280-81; *Petition of Petters*, 117 Misc. 2d 21, 24 (Sup Ct, NY Count 1982) ("In a service corporation, where the services to the clients are performed by the parties to the proceedings who are not working together, where there is a deadlock and consequent loss of profits, the act of one party in seeking to discontinue the business is not in bad faith.").

principally derives from a philosophical business disagreement with respect to whether the parties should continue to operate the business in light of the alleged financial difficulties"). *Cf. Weiss*, 32 AD2d at 281.

Further, Ades contends that he wants to either sell or liquidate A&E while it is still profitable so that he may recoup his investments and avoid any personal financial loss. This alone, however, is not a basis for dissolution under BCL § 1104.[7] *See Application of Dubonnet Scarfs, Inc.*, 105 AD2d 339, 343 (1st Dept 1985) (denying dissolution because the petitioner failed to allege "a single instance of internal dissension, which resulted in a deadlock over a management decision," thereby deducing that the petitioners sought dissolution solely as a pretext for obtaining funds to satisfy personal debts); *Wagner*, 6 Misc 3d 1041(A).

Despite Ades's contention that no hearing is required and that this application should be summarily granted because there is no dispute that Ades and Erani cannot work together, I cannot determined whether dissolution is appropriate on the papers alone because of the parties' s conflicting submissions and allegations. Material issues of fact exist as to whether the dissension and deadlock alleged by Ades exists and whether Ades acted in bad faith by manufacturing the complained-of disputes and dissension to financially harm A&E and justify dissolution.

[7] *Cf.* BCL § 1104-a(b)(1) (In actions under BCL § 1104-a, one of the factors that the court considers in deciding whether dissolution is appropriate is "[w]hether liquidation of the corporation is the only feasible means whereby petitioners may reasonably expect to obtain a fair return on their investment.").

If dissension and/or deadlock do exist – and dissolution is not barred by Ades's alleged bad faith – material issues of fact also exist as to the profitability and financial viability of A&E and whether the proposed dissolution would benefit the shareholders. *See* BCL § 1111(b)(2). *See also Wagner*, 6 Misc 3d 1041(A) ("conflicting allegations with respect to the corporation's financial prospects and the significance of the [current] market and financial conditions . . . require that a hearing be held to determine if dissolution would, in fact, be beneficial to the stockholders within the meaning of BCL § 1104(a)(3)"). Accordingly, I order an evidentiary hearing to resolve these material issues of fact. BCL § 1109.

In accordance with the foregoing, it is

ORDERED that an evidentiary hearing be held before a Special Referee to determine:

(1) Whether the alleged dissension and deadlock exists;

(2) Whether Ades acted in bad faith to manufacture dissension to obtain dissolution; and

(3) The financial benefit to shareholders if dissolution is ordered.

The Special Referee is to report to this Court with all convenient and deliberate speed, except that, in the event of and upon the filing of a stipulation of the parties, as permitted by CPLR § 4317, the Special Referee, or another person designated by the parties to serve as referee, shall determine these issues; and it is further

ORDERED that Ades's petition for judicial dissolution and for the appointment of a permanent receiver to wind up A&E's affairs (motion seq. no. 001) is held in abeyance

pending receipt of the report and recommendations of the Special Referee and a motion pursuant to CPLR § 4403 or receipt of the determination of the Special Referee or the designated referee; and it is further

ORDERED that counsel for the Petitioner shall, within 30 days from the date of this order, serve a copy of the order with notice of entry, together with a completed Information Sheet, upon the Special Referee Clerk in the Motion Support Office in Room 119 at 60 Centre Street, who is directed to place this matter on the calendar of the Special Referee's Part (Part 50R) for the earliest convenient date; and it is further

ORDERED that upon receipt of the Special Referee's report, Petitioner's petition for judicial dissolution and for the appointment of a permanent receiver to wind up A&E's affairs shall be disposed of in accordance with the results of the Special Referee's report as to service and this decision.

This constitutes the decision and order of the Court.

1/22/18
DATE

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SALIANN SCARPULLA, J.S.C.

CHECK ONE:		CASE DISPOSED			X	NON-FINAL DISPOSITION	
		GRANTED		DENIED		GRANTED IN PART	X OTHER
APPLICATION:		SETTLE ORDER				SUBMIT ORDER	
CHECK IF APPROPRIATE:		DO NOT POST				FIDUCIARY APPOINTMENT	REFERENCE