SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK – PART 60

PRESENT: Hon. Marcy Friedman, J.S.C.

ONEIRIC HOLDINGS LLC and CENK FIKRI,

Plaintiffs,

Index No.: 655833/16

– against –

DECISION/ORDER

JEAN BAPTISTE LEONELLI,

Defendant.

This breach of contract action involves a dispute between the two members of plaintiff Oneiric Holdings LLC (Oneiric), plaintiff Cenk Fikri and defendant Jean Baptiste Leonelli, as a result of Leonelli's failure to respond to two Capital Calls. Defendant moves, pursuant to CPLR 3211 (a) (1) and (7), to dismiss the complaint.

The following facts are undisputed. The parties formed Oneiric, a Delaware limited liability company, to own and operate hotels, restaurants, night clubs, and bars. (Operating Agreement, § 2.3 [executed copy annexed to letter of Mark Warren Moody (Ps.' Atty), dated January 30, 2017]; Compl., ¶ 7.) The Operating Agreement between the parties was effective as of June 5, 2015, and names Fikri as the Managing Member.[1] (Operating Agreement, Opening Paragraph, § 1.1 [Defined Terms].) The Operating Agreement states that, as of Oneiric's inception, Fikri and Leonelli each hold a fifty percent Percentage Interest in Oneiric. (Id., Schedule A.) In a provision entitled "Initial Contributions," the Operating Agreement recites

[1] Leonelli initially argued that he did not enter into the Operating Agreement with Fikri. (Aff. of Diana Fabi [Def.'s Atty], ¶ 6.) By letter dated January 30, 2017, plaintiffs' counsel submitted a copy of the executed Operating Agreement. At the oral argument of the motion, Leonelli's counsel acknowledged the execution of the Operating Agreement. (Oral Argument Transcript [Tr.], at 3-4.)

that "[o]n or prior to the date of this Agreement, Mr. Leonelli has made Capital Contributions to the Company in the amount of One Hundred Thousand Dollars ($100,000)." (Id., § 5.3.) The Operating Agreement provides for subsequent Capital Contributions by Leonelli. Section 5.4 states in pertinent part:

> "Subsequent Contributions. Following the date of this Agreement, Mr. Leonelli shall make one or more additional cash Capital Contributions to the Company in the aggregate amount of up to Twenty-Three Million Dollars ($23,000,000) (the 'Subsequent Contributions'). . . . At such times as the Managing Member may elect, the Managing Member may deliver written notice to Mr. Leonelli requiring Subsequent Contributions by Mr. Leonelli to the Company (each such notice, a 'Capital Call'). . . . If at any time Mr. Leonelli fails to make any Subsequent Contribution as required hereby, the Percentage Interests of Mr. Leonelli shall be decreased by One Percentage Interest (1%) for each Four Hundred Sixty Thousand Dollars ($460,000) of Subsequent Contributions not yet made by Mr. Leonelli at such time. The Percentage Interests of Mr. Fikri shall be increased by the amount by which Mr. Leonelli's Percentage Interests decreases pursuant to the preceding sentence."

(Italics omitted.)

On July 17, 2015 and September 23, 2016, respectively, Fikri made two Capital Calls to Leonelli in the amounts of $300,000 and $23,000,000. (Compl., ¶¶ 13, 16; Def.'s Memo. In Supp., at 8.) Leonelli failed to respond to both Capital Calls. (Compl., ¶¶ 19, 22; Def.'s Memo. In Supp., at 8.) Fikri and Oneiric commenced this action to recover the amounts of the Capital Calls. The complaint pleads two causes of action for breach of contract. The first seeks to recover the "first Subsequent Contribution" in the amount of $300,000. (Compl., ¶¶ 18-20.) The second seeks to recover the "second Subsequent Contribution" in the amount of $23,000,000. (Id., ¶¶ 21-23.)

Discussion

It is well settled that on a motion to dismiss pursuant to CPLR 3211 (a) (7), "the pleading is to be afforded a liberal construction (see, CPLR 3026). [The court must] 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." (Leon v Martinez, 84 NY2d 83, 87-88 [1994]. See 511 W. 232nd Owners Corp. v Jennifer Realty Co., 98 NY2d 144 [2002].) However, "the court is not required to accept factual allegations that are plainly contradicted by the documentary evidence or legal conclusions that are unsupportable based upon the undisputed facts." (Robinson v Robinson, 303 AD2d 234, 235 [1st Dept 2003]; see also Water St. Leasehold LLC v Deloitte & Touche LLP, 19 AD3d 183 [1st Dept 2005], lv denied 6 NY3d 706 [2006].) When documentary evidence under CPLR 3211 (a) (1) is considered, "a dismissal is warranted only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law." (Leon, 84 NY2d at 88.)

The parties dispute whether plaintiffs are entitled to monetary damages under the Operating Agreement. Leonelli claims that under Delaware law, parties may choose "dilution as the consequence for failing to respond to a capital call. And it is only when such language is absent from the agreement that courts have held that a non-contributing member will retain his interest and an action for breach of contract could then be brought against the member to satisfy the required contribution." (Def.'s Memo. In Supp., at 5 [internal citations omitted].) As the Operating Agreement "addresses the possibility that Defendant might choose not to invest in the company and provides for the consequence if he chooses not to do so, Plaintiffs have no valid

claims for any further remedy, such as damages or specific performance arising out of defendant's decisions not to invest $300,000 and $23,000,000." (Id., at 8.)

Plaintiffs argue that their remedy is not limited to the decrease in Leonelli's Percentage Interest and proportional increase in Fikri's Percentage Interest. (Pls.' Memo. In Opp., at 2, 4.) Rather, according to plaintiffs, "all of Plaintiffs[']' common law rights of recovery are open to them under well-settled principles of Delaware law as the Operating Agreement does not assert (either implicitly or explicitly) that the remedy of dilution is exclusive." (Id., at 2 [emphasis in original].) Further, plaintiffs argue that Leonelli's interpretation of the Agreement would render the Agreement illusory. (Id., at 5.)

The Operating Agreement provides that it "shall be construed and enforced in accordance with and governed by the laws of the State of Delaware. . . ." (Operating Agreement, §§ 15.5, 15.6.) More specifically, the Operating Agreement is subject to the Delaware Limited Liability Company Act (6 Del C, ch 18) (Delaware LLC Act). Section 18-502 of this statute, entitled "Liability for contribution," provides:

> "(a) Except as provided in a limited liability company agreement, a member is obligated to a limited liability company to perform any promise to contribute cash or property or to perform services, even if the member is unable to perform because of death, disability or any other reason. If a member does not make the required contribution of property or services, the member is obligated at the option of the limited liability company to contribute cash equal to that portion of the agreed value (as stated in the records of the limited liability company) of the contribution that has not been made. The foregoing option shall be in addition to, and not in lieu of, any other rights, including the right to specific performance, that the limited liability company may have against such member under the limited liability company agreement or applicable law.
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> . . .
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> (c) A limited liability company agreement may provide that the interest of any member who fails to make any contribution that the member is obligated to make shall be subject to specified penalties for, or specified consequences of, such failure. Such penalty or

> consequence may take the form of reducing or eliminating the defaulting member's proportionate interest in a limited liability company, subordinating the member's limited liability company interest to that of nondefaulting members, a forced sale of that limited liability company interest, forfeiture of the defaulting member's limited liability company interest, the lending by other members of the amount necessary to meet the defaulting member's commitment, a fixing of the value of the defaulting member's limited liability company interest by appraisal or by formula and redemption or sale of the limited liability company interest at such value, or other penalty or consequence."

There is authority that the failure of a member of a limited liability company to satisfy a capital call will not result in the diminution of the member's ownership interest unless the limited liability company operating agreement explicitly provides for the penalty of diminution in the event of such failure. (See Grove v Brown, 2013 WL 4041495, * 6-7 [Del Ch, CA No. 6793 (VCG), Aug. 8, 2013].) The parties do not cite, and the court's own research has not located, Delaware authority which has determined whether, if the parties' operating agreement does provide for the penalty of diminution in the event a member fails to meet a capital call, the non-defaulting member will be limited to diminution as its exclusive remedy or may still seek damages in the amount of the capital call.

The court must accordingly construe the parties' Operating Agreement under general principles of contract interpretation. It is well settled that "Delaware law adheres to the objective theory of contracts, i.e., a contract's construction should be that which would be understood by an objective, reasonable third party." (Salamone v Gorman, 106 A3d 354, 367-368 [Del 2014] [internal quotation marks and citation omitted]; accord Exelon Generation Acquisitions, LLC v Deere & Co., 176 A3d 1262, 1267 [Del 2017].) When interpreting a contract, the court "will give priority to the parties' intentions as reflected in the four corners of the agreement" and must "construe the agreement as a whole, giving effect to all provisions therein." (GMG Capital Inv.,

LLC v Athenian Venture Partners I, L.P., 36 A3d 776, 779 [Del 2012] [internal quotation marks and citation omitted]; accord Salamone, 106 A3d at 368.) "If a contract is unambiguous, extrinsic evidence may not be used to interpret the intent of the parties, to vary the terms of the contract, or to create an ambiguity." (Exelon, 176 A3d at 1267, 1273 [internal quotation marks and citation omitted].) Ambiguity in a contract arises "when the provisions in controversy are fairly susceptible of different interpretations or may have two or more different meanings." (GMG Capital, 36 A3d at 780 [internal quotation marks, brackets, and citation omitted]; accord Salamone, 106 A3d at 369.)

Applying these standards, the court holds that the Operating Agreement unambiguously limits the remedy for Leonelli's failure to meet a Capital Call to diminution of Leonelli's Percentage Interest. As quoted above (supra at 4-5), Delaware LLC Act § 18-502 (c) expressly allows the contracting parties to the operating agreement to specify a penalty for a member's failure to make a capital contribution, including a penalty in the form of diminution of the defaulting member's proportionate interest in the company. Section 18-502 (a) of the statute, quoted above (supra at 4), also provides that except as provided in the operating agreement, other remedies, including a right to compel the required contribution, will be available. Here, the Operating Agreement specifies the remedy of diminution. Other common law remedies are accordingly unavailable.

This interpretation of the Operating Agreement is consistent with the policy reflected in the Delaware LLC Act. Section 18-1101 (b) of the Act provides: "It is the policy of this chapter to give the maximum effect to the principle of freedom of contract and to the enforceability of limited liability company agreements." As the Delaware Supreme Court has observed, "[t]he basic approach of the Delaware Act is to provide members with broad discretion in drafting the

[Operating] Agreement and to furnish default provisions when the members' agreement is silent. The Act is replete with fundamental provisions made subject to modification in the Agreement (e.g. 'unless otherwise provided in a limited liability company agreement. . . .')." (Elf Atochem N. Am., Inc. v Jaffari, 727 A2d 286, 291 [Del 1999]; see Grove, 2013 WL 4041495, * 5.) "Once members exercise their contractual freedom in their limited liability company agreement, they can be virtually certain that the agreement will be enforced in accordance with its terms." (Walker v Resource Dev. Co. Ltd., L.L.C. (DE), 791 A2d 799, 813 [Del Ch 2000].) An interpretation that would permit a non-defaulting member to obtain a remedy that is not the penalty to which the members specifically agreed would ignore the terms of the Operating Agreement.

In so holding, the court rejects plaintiffs' claim that, because the Operating Agreement does not explicitly state that diminution is their exclusive remedy, "all of the common-law remedies are available. . . ." (Tr., at 10.) As explained by the Delaware Supreme Court in a leading case, Gotham Partners, L.P. v Hallwood Realty Partners, L.P. (817 A2d 160, 176 [Del 2002]), Delaware courts "will not construe a contract as taking away a common law remedy unless that result is imperatively required. . . . [E]ven if a contract specifies a remedy for breach of that contract, a contractual remedy cannot be read as exclusive of all other remedies if it lacks the requisite expression of exclusivity." (Id. [internal quotation marks, citations, and brackets omitted]; accord Brevan Howard Credit Catalyst Master Fund Ltd. v Spanish Broadcasting Sys., Inc., 2014 WL 2943570, * 7, n 44 [Del Ch, CA No. 9209 (VCG), June 27, 2014] [internal quotation marks omitted]; Reid v Thompson Homes at Centreville, Inc., 2007 WL 4248478, * 5 [Del Super, CA No. 06C-10-075 (RBY), Nov. 21, 2007].) The Supreme Court also stated in Gotham Partners that "courts will not construe a contract as taking away other forms of

appropriate relief, including equitable relief, unless the contract explicitly provides for an exclusive remedy." (817 A2d at 175.) The Gotham Partners Court held, under the substantially similar Delaware partnership law (6 Del C, ch 17), that the Court of Chancery properly awarded equitable damages as a remedy for defendant's breach of a "contractually created fiduciary duty," where the partnership agreement was "silent regarding damages." (817 AD2d at 175.) Gotham Partners was followed by the Delaware Supreme Court in Gatz Properties, LLC v Auriga Capital Corp. (59 A3d 1206, 1220 n 74 [Del 2012]), which held, under the Delaware LLC Act, that the Court of Chancery properly awarded equitable damages as a remedy where defendants "breached a contracted-for fiduciary duty . . . , and . . . the LLC Agreement did not dictate otherwise."

Neither Gotham Partners nor Gatz involved a failure of a member or partner to make a capital contribution. More important, neither case involved an agreement in which the parties availed themselves of a statutory option to limit their remedies for breach of contract. Here, in contrast, the parties' Operating Agreement is not silent as to the availability of remedies other than the penalty of diminution for a member's failure to meet a capital call. On the contrary, the Agreement reflects the parties' election of their option, under section 18-502 (a) of the Delaware LLC Act, to eliminate other remedies by providing expressly for the diminution penalty.

As stated above, the Delaware courts have not considered the effect of contracting parties' exercise of their statutory right to impose a penalty of diminution for a member's or partner's failure to make a required capital contribution. Nor have the New York courts considered this issue, although New York has a substantially similar limited liability company act. (Limited Liability Company Law § 502.) However, other courts which have considered the issue, under limited liability company or partnership acts that are substantially similar to those of

Delaware, have reached the same conclusion as this court. Thus, in Canyon Creek Development, LLC v Fox (46 Kan App 2d 370 [Kan Ct App 2011]), the Court addressed the remedy against a member who failed to make a capital contribution, construing the operating agreement in light of the Kansas statutory equivalent of Delaware LLC Act § 18-502. The operating agreement provided for dilution of the interest of the defaulting member to the extent that other members covered by making additional contributions. (Id., at 382.) Noting that dilution was "the only consequence specified in the provisions of the operating agreement relating to the infusion of additional capital" (id.), the Court held that the remedy of damages was unavailable against the defaulting member. (Id.) The Court "conclude[d] that failing to specify in the operating agreements so fundamental a remedy as damages when a member fails to contribute additional capital to the venture is not an oversight but rather the expression of a clear intent that damages cannot be assessed against a member who fails to contribute additional capital to the venture after it is up and running." (Id., at 383; see also Matter of Villa W. Assocs. [v Kay], 146 F3d 798, 805 [10th Cir 1998] [holding a damages remedy unavailable under a Kansas partnership agreement which provided for the penalty of dilution for a partner's failure to make capital contributions].)

Conversely, courts have held that where an operating agreement or partnership agreement provides a dilution penalty for a member's or partner's failure to meet a capital call, that penalty does not bar a damages claim if the agreement specifically preserves other rights and remedies. (See e.g. Skyscapes of Castle Pines, LLC v Fischer, 2014 WL 5801042, * 4 [Kan Ct App, No. 100,444, Oct. 31 2014] [recognizing a Kansas LLC's right to sue a member for delinquent capital contributions, where the operating agreement not only provided for a penalty of dilution but also specifically preserved other legal and equitable remedies, the court distinguishing

Canyon Creek on the ground that the Canyon Creek operating agreement did not contain a similar provision which preserved other remedies]; Devon Park Bioventures, L.P. v Sebastian Holdings, Inc., 2012 WL 440660, * 3-4 [ED Pa, No. 11-3044, Feb. 10, 2012] [applying Delaware law and holding that, although the partnership agreement permitted the general partner to reduce a partner's capital account where the partner failed to meet a capital call, the general partner could also pursue equitable relief, as the partnership agreement permitted the general partner to "elect in its sole and absolute discretion to . . . impose any one or more remedies at law or in equity available to it, in addition or in the alternative, to" the dilution remedy] [brackets omitted, ellipses in original].)

Finally, the court finds unpersuasive plaintiffs' apparent contention that if Leonelli is permitted not to meet the Capital Calls at issue – i.e. if he is not subject to a damages award for the amount of his missed subsequent Capital Contributions – the Operating Agreement would be "illusory." (Pls.' Memo. In Opp., at 5.) Contractual provisions that specify dilution of a member's interest as the penalty for the failure to make capital calls have been enforced under both Delaware and New York law. (See Fried v Lehman Bros. Real Estate Assocs. III, L.P., 156 AD3d 464, 465 [1st Dept 2017], affg 2016 NY Slip Op 31490 [U], 2016 WL 4181014, * 9-10 [Sup Ct, NY County 2016] [applying New York and Delaware law]; Shapiro v Ettenson, 146 AD3d 650, 650 [1st Dept 2017], lv denied 29 NY3d 915 [applying New York Law]; Abuy Dev., L.L.C. v Yuba Motorsports, Inc., 2008 WL 1777412, * 11 [ED Mo, No. 4:06-CV-799 (SNL), Apr. 16, 2008] [applying Delaware Law].)

Further, as stated above (supra at 2), the Operating Agreement specifically provides that, as of Oneiric's inception, Fikri and Leonelli are each fifty percent owners, and that "Leonelli has made Capital Contributions . . . of One Hundred Thousand Dollars ($100,000)." The court notes

that it is undisputed that Leonelli did not in fact make an initial Capital Contribution in any amount. (Def's Memo. In Supp., at 8; Pls.' Memo., In Opp. at 3.) The Operating Agreement, however, provides for a penalty of dilution only for Leonelli's failure to make subsequent Capital Contributions and not for Leonelli's failure to make the Initial Contribution. (Compare Operating Agreement, § 5.4 with § 5.3.) Leonelli thus had an interest in Oneiric which was "not contingent on providing the appropriate capital contribution." (See Grove, 2013 WL 4041495, * 6-7.)[2]

The court accordingly holds that the diminution penalty in section 5.4 of the Operating Agreement is enforceable and bars plaintiffs' claims for monetary damages for Leonelli's breach of contract in failing to make the subsequent Capital Contributions.[3]

It is accordingly hereby ORDERED that the motion to dismiss of defendant Jean Baptiste Leonelli is granted to the extent of dismissing the complaint.

This constitutes the decision of the court.

Dated: New York, New York
April 6, 2018

MARCY FRIEDMAN, J.S.C.

[2] It is noted that the complaint does not plead a cause of action for recovery of the $100,000 initial contribution.

[3] Although the first subsequent Capital Call was for $300,000, the second subsequent Capital Call was for the entire $23,000,000. There is no claim on this motion that Fikri was not entitled to make the second Capital Call for the entire amount. Applying the penalty in section 5.4 of the Operating Agreement, Leonelli's Percentage Interest has been decreased to zero. Section 5.4 provides that Leonelli's Percentage Interest is "decreased by One Percentage Interest (1%) for each Four Hundred Sixty Thousand Dollars ($460,000) of Subsequent Contributions not yet made. . . ." (Id.) $23 million divided by $460,000 is 50, which eliminates Leonelli's entire fifty percent Percentage Interest.