Small v DMRJ Group LLC
2022 NY Slip Op 31956(U)
June 22, 2022
Supreme Court, New York County
Docket Number: Index No. 654522/2018
Judge: Joel M. Cohen
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 03M

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DANIEL SMALL, Plaintiff,	INDEX NO. 654522/2018
- v -	MOTION DATE N/A, N/A, N/A
DMRJ GROUP LLC, Defendant.	MOTION SEQ. NO. 006 007 009
	DECISION + ORDER ON MOTION

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HON. JOEL M. COHEN:

The following e-filed documents, listed by NYSCEF document number (Motion 006) 162, 163, 164, 165, 166, 167, 168, 169, 170, 171, 172, 173, 174, 175, 176, 177, 178, 179, 180, 181, 182, 183, 184, 185, 186, 187, 188, 189, 190, 191, 192, 193, 194, 195, 196, 197, 198, 199, 209, 249, 284, 285, 286, 287, 288, 289, 290, 291, 292, 293, 294, 295, 296, 297, 298, 299, 300, 301, 302, 303, 304, 305, 306, 316

were read on this motion for SUMMARY JUDGMENT.

The following e-filed documents, listed by NYSCEF document number (Motion 007) 200, 201, 202, 203, 204, 205, 206, 207, 208, 250, 251, 252, 253, 254, 255, 256, 257, 258, 259, 260, 261, 262, 263, 264, 265, 266, 267, 268, 269, 270, 271, 272, 273, 274, 275, 276, 277, 278, 279, 280, 281, 282, 283, 314, 315, 365, 366, 367, 368

were read on this motion for SUMMARY JUDGMENT.

The following e-filed documents, listed by NYSCEF document number (Motion 009) 307, 308, 309, 310, 311, 312, 313, 317, 318, 319, 320, 321

were read on this motion to PRECLUDE.

This is a breach of contract case. Plaintiff Daniel Small seeks to recover compensation from Defendant DMRJ Group LLC ("DMRJ") for the years 2012-2017 under the terms of DMRJ's Operating Agreement. DMRJ is an LLC created to make and hold investments for a hedge fund; Small managed the hedge fund and received a profits interest in DMRJ. At issue here, among other things, is Small's entitlement to compensation from DMRJ in light of the hedge fund's collapse—a collapse allegedly precipitated by Small's own fraud, as well as others

in his orbit. The hedge fund, and its investment positions, are the subject of ongoing criminal and civil proceedings in which Small himself is a defendant.

Now before the Court are three motions: (1) Small's motion for summary judgment on his causes of action (MS 006); (2) DMRJ's motion for summary judgment seeking to dismiss the action or, alternatively, obtain a ruling about the interpretation of the relevant agreements (MS 007); and (3) Small's motion to strike DMRJ's expert, Ronald G. Quintero (MS 009).

For the reasons set forth below, (1) Small's motion for summary judgment is denied; (2) DMRJ's motion for summary judgment is granted; and (3) Small's motion to strike (MS 009) is denied as moot.

BACKGROUND

A. Small's Compensation under the Operating Agreement and IMA.

Beginning in 2007, Small was a portfolio manager for Platinum Management (NY) LLC ("PMNY") (Pl.'s Rule 19-a stmt. ["SMF"] ¶ 1) under the terms of an Investment Management Agreement ("IMA") (*id.* ¶ 4). PMNY was the general partner and investment manager for Platinum Partners Value Arbitrage Fund L.P. ("PPVA") (*id.* ¶ 5), a hedge fund. And PPVA, in turn, used special purpose LLCs to make and hold investments (*id.* ¶ 6). Defendant DMRJ was one such LLC. And Small was a "First Profits Interest Member" in DMRJ (*id.* ¶ 7; NYSCEF 167 § 6.1 [DMRJ Operating Agreement]).

Under section 8.2 [A] of the DMRJ Operating Agreement, Small is entitled to receive, as compensation, the *lesser* of (i) 6.5% of DMRJ's annual "Net Profits" and (ii) his "Adjusted Profits Amount" based on the IMA (SMF ¶ 12; DMRJ Operating Agreement § 8.2 [A]). "Net Profits" denotes DMRJ's "net profits . . . as determined for Federal income tax purposes" (*id.* § 8.1). The formula for calculating "Adjusted Profits Amount," meanwhile, takes into account the

"Bonus" under Small's IMA (*id.* § 8.2; *see* NYSCEF 168 § 3 [b] [IMA]). And the "Bonus" includes, among other things, the Net Profit attributable to the "account assets" which Small managed for PMNY (*id.*; *see id.* §§ 1 [a], 1 [j]). If those assets suffered a "Net Loss" in a calendar year, the amount of the loss would offset "Net Profits" in that year, and any unused loss would carry forward to future years until fully spent against Net Profits. Essentially, Small's compensation, like that of many investment managers, was tied to the value of the assets he managed.

B. PPVA's Collapse and Subsequent Actions.

The value of those assets came under scrutiny when PPVA collapsed in 2016 (*see* Quintero Aff. ¶ 55 [NYSCEF 188]), "one of the largest investment fund collapses" since the Madoff Ponzi scheme (Trott Aff. ¶ 6 [NYSCEF 292]; Quintero Aff. ¶ 20 ["Platinum has been characterized in the press as a 'mini Madoff.'"]). As later alleged by federal prosecutors, the SEC, and aggrieved investors, PPVA's collapse was precipitated, in large part, by the unraveling of "Black Elk," an oil and gas company in which PPVA held a large investment position (Def.'s counterstatement of material facts ["CSMF"] ¶ 52 [NYSCEF 294]). Small managed the Black Elk position for PMNY. He and other Platinum personnel allegedly overstated Black Elk's value despite severe financial distress at the company, and then orchestrated a transaction to defraud Black Elk's bondholders while enriching "Platinum insiders, including [Small] himself" (*id.* ¶ 57; Quintero Aff. ¶ 26). PPVA's demise – and the Black Elk scheme – has spawned criminal, civil, and regulatory actions in which Small himself is a defendant (CSMF ¶¶ 54-55 [listing actions]).

On July 9, 2019, following a nine-week jury trial in the federal district court for the Eastern District of New York, Platinum CIO Mark Nordlicht and portfolio manager David Levy

were convicted of securities fraud, conspiracy to commit securities fraud, and conspiracy to commit wire fraud in connection with the Black Elk scheme (*United States v Landesman*, 17 F4th 298, 303 [2d Cir 2021]). Post-trial, the district court granted Nordlicht's motion for a new trial and granted Levy's motion for a judgment of acquittal (*id.* at 317-318). But in November 2021, the Second Circuit Court of Appeals vacated those orders. In a 104-page opinion, the Second Circuit laid out in detail the facts established at trial justifying the jury's convictions (*see* NYSCEF 366 [copy of Court of Appeals' opinion]).

In doing so, the Court of Appeals highlighted the interplay between PPVA and the Black Elk fraud. Among other things, the opinion noted that Platinum, which "consisted of multiple investment funds, including . . . PPVA," was "[c]entral to the alleged Black Elk Scheme" (*Landesman*, 17 F4th at 303). And because of PPVA's large position in Black Elk, "Black Elk's dire financial straits" and possible bankruptcy "would have negative ramifications for PPVA" (*id.* at 322-323). In a March 2014 email from Nordlicht to Small, introduced as evidence at trial, Nordlicht stated:

> I need to figure out how to restructure and raise money to pay back 110 million of preferred [equity in Black Elk] which ***if unsuccessful, w[oul]d be the end of the fund [(PPVA)]***. This "liquidity" crunch [at PPVA] was ***caused by our mismanagement – yours[,] David [Levy] and I – of the black elk position*** . . .

(*id.* at 308 [emphasis added]); *id.* at 309 ["I think we need to revamp the strategy on PPVA and figure out what to do. It can't go on like this or practically, we [(PPVA)] will need to wind down. . . . I think we can overcome this but this is code red"] [June 2014 email from Nordlicht to Uri Landesman]). Further, the evidence established at trial that shielding PPVA from the "negative ramifications" of "Black Elk's impending bankruptcy" provided Platinum with "a motive" to orchestrate the fraudulent transaction (*id.* at 323).

Meanwhile, PPVA's assets underwent further examination when the fund was placed into liquidation by the Grand Court of the Cayman Islands (Trott Aff. ¶ 4; Quintero Aff. ¶ 21), where it was organized (IMA at 1). There, two Joint Official Liquidators ("JOLs") were appointed to act as "independent fiduciar[ies] for all stakeholders" (Trott Aff. ¶ 7). The JOLs have "broad authority to act in connection with the assets and management of PPVA and its subsidiaries, which includes DMRJ," under Cayman Islands law (*id.*). The JOLs replaced PMNY as general partner of PPVA, and PPVA was appointed sole operating manager for DMRJ (*id.* ¶ 11). According to one of the JOLs, Martin Trott, that means "all acts [that] were previously within the power of Platinum Management vis-à-vis PPVA are now powers of the JOLs," including "the right and duty to reset and take positions regarding PPVA's assets values from 2012 through the present" (*id.* ¶ 10). Despite representations that PPVA's assets were worth around $1 billion, the JOLs report that PPVA "was insolvent upon commencement of the Cayman Liquidation and its equity had zero value based upon the true value of the assets under management" (*id.* ¶ 6). The upshot is that, in the JOLs' view, "[i]f Small had been paid any fees based on the purported value of the assets, they would be subject to clawback" (*id.*).

C. The Instant Action.

Small's employment with PMNY was terminated in July 2015 (SMF ¶ 31). In 2018, Small initiated this action to recover compensation DMRJ was allegedly required to pay him between 2012 and 2017 (NYSCEF 165). Specifically, in his First Cause of Action for breach of contract, Small asserts that DMRJ must pay his allocated portion of DMRJ's Net Profits, a share amounting to $6,962,550 (plus interest), under the terms of DMRJ's Operating Agreement (*see* NYSCEF 199 at 1 [Pl.'s mot. for S.J.]; Compl. ¶¶ 56-61). And in his Second Cause of Action,

Small seeks access to DMRJ's books and records (*id.* ¶¶ 62-67). These motions followed Small's filing a Note of Issue on February 11, 2021 (NYSCEF 159).

DISCUSSION

To prevail on a motion for summary judgment, the movant "must make a prima facie showing of entitlement to judgment as a matter of law, tendering sufficient evidence to demonstrate the absence of any material issues of fact'" (*Ayotte v Gervasio*, 81 NY2d 1062, 1063 [1993] [citation omitted]). "Failure to make such showing requires denial of the motion, regardless of the sufficiency of the opposing papers" (*Winegrad v New York Univ. Med. Ctr.*, 64 NY2d 851, 853 [1985]). If a prima facie showing is made, the burden then shifts to the party opposing summary judgment to present evidentiary facts sufficient to raise triable issues of fact (*Zuckerman v City of New York*, 49 NY2d 557, 562 [1980]). The court is required to examine the evidence in a light most favorable to the party opposing the motion (*Martin v Briggs*, 235 AD2d 192, 196 [1st Dept 1997]).

A. Small's Motion for Summary Judgment (MS 006) is Denied.

Small's motion for summary judgment is denied. Among other things, DMRJ has raised triable issues of fact about whether Small is allowed to enforce section 8.2 [A] under the circumstances alleged here. It is a "familiar rule that illegal contracts, or those contrary to public policy, are unenforceable and that the courts will not recognize rights arising from them" (*Szerdahelyi v Harris*, 67 NY2d 42, 48 [1986]). "No one shall be permitted to profit by his own fraud, or to take advantage of his own wrong, or to found any claim upon his own iniquity, or to acquire property by his own crime" (*McConnell v Commonwealth Pictures Corp.*, 7 NY2d 465, 469 [1960], citing *Carr v Hoy*, 2 NY2d 185 [1957]). And "[e]ven where a contract is not itself unlawful, the bargain may still be illegal [and unenforceable] under New York law if it is closely

connected with an unlawful act" (*CMF Investments, Inc. v Palmer*, 13-CV-475 VEC, 2014 WL 6604499, at *2 [SD NY Nov. 21, 2014], quoting *United States v Bonanno Organized Crime Family of La Cosa Nostra*, 879 F2d 20, 28 [2d Cir 1989]).

Here, viewing the evidence in the light most favorable to DMRJ, there is a fact dispute about whether compensating Small under the Operating Agreement would permit him to exploit the alleged fraud at PPVA for his own gain. Small's compensation depends, in part, on stated asset values in the PPVA portfolio; individuals who managed PPVA have been criminally convicted for defrauding investors, and others, including Small himself, still face criminal and civil liability stemming from PPVA. Indeed, the Second Circuit Court of Appeals has ruled that PPVA, and other Platinum funds, were "[c]entral to the alleged Black Elk Scheme" to defraud bondholders (*Landesman*, 17 F4th at 303). Small, specifically, was chastised by Nordlicht for causing a "'liquidity' crunch [at PPVA]" through his "mismanagement . . . of the black elk position" (*id.* at 308). And in another action pending in the Southern District of New York, the JOLs and PPVA alleged that "the Platinum Defendants" – including Small – overstated "their reported valuation of PPVA's investment in Black Elk" despite "serious financial problems" afflicting the investment (*In re Platinum-Beechwood Litig.*, 18-CV-10936 (JSR), 2019 WL 1570808, at *2 [SD NY Apr. 11, 2019] [denying in part motions to dismiss]).

Against that backdrop, DMRJ also raises fact questions about whether the "Managers'" calculation of Net Profits under the IMA is enforceable if (1) the Managers in question were defrauding PPVA's investors during the relevant time period; and (2) the investments became "worthless" under the Internal Revenue Code, GAAP, and accepted methods to calculate fair market value (*see, e.g.*, Quintero Report ¶ 13). In addition, DMRJ raises a fact question about whether the JOLs' asserted power to "take positions regarding PPVA's assets values from 2012

through the present" means that the compensation sought by Small is subject to claw-back in the Cayman Islands liquidation (Trott Aff. ¶¶ 10, 13).

Therefore, Small's motion for summary judgment is denied.

B. DMRJ's Motion for Summary Judgment (MS 007) is Denied.

In its own motion for summary judgment, DMRJ argues that the action must be dismissed as a consequence of Small's invocation of his Fifth Amendment privilege during discovery in this action. Under New York law, "[t]he privilege against self incrimination was intended to be used solely as a shield, and thus a plaintiff cannot use it as a sword to harass a defendant and to effectively thwart any attempt by defendant at a pretrial discovery proceeding to obtain information relevant to the cause of action alleged and possible defenses thereto" (*Laverne v Inc. Vil. of Laurel Hollow*, 18 NY2d 635, 638 [1966]; *Batista v City of New York*, 15 AD3d 304, 306 [1st Dept 2005] ["Plaintiffs may not maintain the instant action while denying defendants information material and necessary to their defense by invoking the Fifth Amendment privilege against self-incrimination"]; *Nasca v Town of Brookhaven*, 10 AD3d 415, 416 [2d Dept 2004] ["Although the plaintiffs have the right to invoke the Fifth Amendment privilege against self-incrimination . . . that they are not entitled to continue to maintain this action if the assertion of the privilege prevent[s] the defendant from properly defending the lawsuit"]).

DMRJ's motion is granted. By repeatedly invoking his Fifth Amendment right at his deposition (*see* NYSCEF 201 ¶¶ 20, 26, 28, 36, 39, 48, 64, 68, 73 [DMRJ's SMF]), Small is "prevent[ing] the defendant from properly defending the lawsuit" (*Nasca*, 10 AD3d at 416).[1] Even if Small prevails on his interpretation of the Operating Agreement and IMA, DMRJ still

[1] Small also invoked his Fifth Amendment right in his response to DMRJ's Rule 19-a statement (*see* NYSCEF 251 ¶¶ 50, 51, 56, 57, 58, 59, 66).

may defend on the basis that Small's claim effectively rewards him for fraudulent conduct. As noted above, a contract is unenforceable under New York law "if it is closely connected with an unlawful act" (*CMF Investments*, 13-CV-475 VEC, 2014 WL 6604499, at *2). Accepting Small's contention that losses on certain investments, designated as "Realized Only" assets in the IMA, do not matter for purposes of calculating IMA Net Profits, DMRJ still may argue that ignoring those losses "permit[ ] [Small] to profit by his own fraud" (*McConnell*, 7 NY2d at 469). And in that regard, Small refused to answer basic questions about his role with Black Elk:

- When asked "when was the first time that you heard the name Black Elk," Small invoked the Fifth Amendment (SMF ¶ 26, citing Small Dep. Tr. 295:18-22).

- When asked "were you the portfolio manager for Black Elk from 2010 to 2015," Small invoked the Fifth Amendment (SMF ¶ 26, citing Small Dep. Tr. 296:4-9).

- When asked "and you were obligated to act in PPVA's best interests in 2014; isn't that right," Small invoked the Fifth Amendment (SMF ¶ 26, citing Small Dep. Tr. 327:19-21).

- When asked "you were in charge of managing Black Elk's response to the civil and criminal litigation on behalf of Platinum; isn't that right," Small invoked the Fifth Amendment (SMF ¶ 28, citing Small Dep. Tr. 310:16-25).

- When asked if "the Black Elk Opportunities Funds were set up to strip value from PPVA," Small invoked the Fifth Amendment (SMF ¶ 36, citing Small Dep. Tr. 325:11-17).

- When asked if "subordinating PPVA's interests" resulted in "you, personally, Dan Small," being "paid out on your $100,000 investment in Platinum Partners Black Elk Opportunities Fund; isn't that right," Small invoked the Fifth Amendment (SMF ¶ 68, citing Small Dep. Tr. 331:7-15).

And so on. Small's unwillingness to testify about his role in causing the losses that allegedly negate his entitlement to compensation prejudices DMRJ's ability to defend this case.

Notably, the consequences attendant on Small's repeated invocation of his Fifth Amendment rights was a risk previewed over three years ago, when DMRJ moved to stay this action "pending the resolution of certain civil, criminal and regulatory actions currently pending against" Small (NYSCEF 36). Among other things, DMRJ forewarned that "the effect of the pending criminal action against Plaintiff is likely to result in Plaintiff pleading a Fifth Amendment privilege in response to defenses raised by Defendant, thus substantially prejudicing DMRJ from defending this action" (*id.* at 4). Small opposed a stay, however, criticizing "DMRJ's flawed reasoning" that "Small is likely to invoke the Fifth Amendment privilege in this matter" (NYSCEF 60 at 2). From the outset, therefore, Small assumed the risk that the criminal and civil cases swirling around the Platinum funds and Black Elk could impinge on his ability to prosecute this action.

Small's arguments to the contrary are unavailing. That Small "submitted to 7 hours of examination in which he answered all non-privileged questions not involving the Indictment" (NYSCEF 252 at 2), for example, does not address the prejudice resulting from Small's repeated assertion of privilege. In *Batista*, the First Department permitted defendants to ask questions at depositions relating to issues relevant to their defenses, and cautioned that "[s]hould plaintiff continue to invoke his Fifth Amendment right against self-incrimination, he does so at the risk of having his complaint dismissed" (*Batista*, 15 AD3d at 306). Similarly, here, it is Small's refusal to answer relevant questions that prejudices DMRJ, regardless of his willingness to answer questions he deems "non-privileged." Also, Small's argument that DMRJ is not entitled to summary judgment on the merits of its affirmative defenses misses the mark. DMRJ is not moving for summary judgment on its affirmative defenses, but rather based on a showing that

Small's involvement with the Black Elk scheme is *relevant* to its defenses and that he cannot prosecute this action while at the same time blocking DMRJ's access to relevant information.

Therefore, DMRJ's motion for summary judgment is granted, and the Complaint is dismissed.

C. Small's Motion to Strike (MS 009) is Denied.

In light of the foregoing, Small's motion to strike the entirety of the expert reports prepared by Ronald G. Quintero is denied as moot.

* * * *

Accordingly, it is

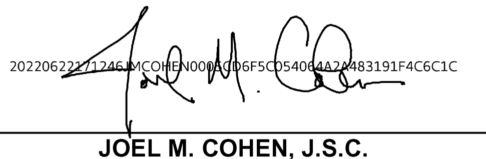
ORDERED that Small's motion for summary judgment (MS 006) is **denied**; it is further

ORDERED that DMRJ's motion for summary judgment (MS 007) is **granted** and the complaint is dismissed with costs and disbursements to defendant as taxed by the Clerk upon the submission of an appropriate bill of costs; it is further

ORDERED that Small's motion to strike (MS 009) is **denied as moot**; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

This constitutes the Decision and Order of the Court.



6/22/2022			JOEL M. COHEN, J.S.C.		
DATE					
CHECK ONE:	[ ] CASE DISPOSED		[X] NON-FINAL DISPOSITION		
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APPLICATION:	[ ] SETTLE ORDER		[ ] SUBMIT ORDER		
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