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Matter of Natanel v Cohen
2014 NY Slip Op 50677(U)
Decided on April 18, 2014
Supreme Court, Kings County
Demarest, J.
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In the Matter of the Application of Yariv Natanel, Holder of a 50% Membership Interest, Petitioner, For the Dissolution of, and Appointment of a Receiver or Liquidating Trustee for, Y and Y Ditmas LLC, Pursuant to §§702 and 703 of the Limited Liability Company Law,

against

Yosef Cohen, Respondent.

502760/13

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Carolyn E. Demarest, J.

The instant petition seeks dissolution of Y and Y Ditmas LLC (Y and Y or the LLC) which owns 9502 Ditmas Avenue in Brooklyn (the Building). During a hearing commenced on December 16, 2013, at the close of petitioner's direct case, respondent moved for dismissal claiming that petitioner had failed to establish grounds for dissolution under Limited Liability Company Law (LLCL) §702 and controlling case law, specifically *Matter of 1545 Ocean Avenue, LLC v Ocean Suffolk Properties, LLC* (72 AD3d 121 [2d Dept 2010]).The Court reserved decision following argument. By Decision and Order dated January 2, 2014,the Court denied the motion to dismiss finding that, although the evidence did not establish that continuation of the LLC is financially unfeasible, other issues remained as to the feasibility of its [*2]continuation and whether the purpose of the LLC was being frustrated by the estranged relationship of the two 50/50 members. The trial was resumed on January 9, 2014.

Findings of Fact

Petitioner Natanel and respondent Cohen purchased A-One Moving & Storage, Inc (A-One) in 1997. A-One rented approximately 60% of the space in the Building, from which its business was operated. In 2004, the Building was placed on the market for sale and, in order to avoid losing their business premises upon purchase by another, Natanel and Cohen formed Y and Y and purchased the Building upon very favorable terms from their prior landlord who took back a mortgage, which will be fully satisfied this year. The Articles of Organization of Y and Y, filed with the Department

of State on October 20, 2004, contain no mention of the purpose of the LLC, but merely specify that it "is to be managed by 1 or more members". No Operating Agreement has been created, nor is there any other written documentation evidencing the terms of the contract between the members or their purpose in creating Y and Y. Accordingly, Y and Y is exclusively governed by statute (see *Matter of Eight of Swords, LLC*, 96 AD3d 839 [2d Dept 2012]; *1545 Ocean* at 129; *Matter of Spires v Lighthouse Solutions, LLC*, 4 Misc 3d428, 433 [Sup Ct, Monroe County 2004]).

It is undisputed that beginning in 2007 or 2008, the relationship between petitioner and respondent began to deteriorate and the day-to-day management of A-One and Y and Y was thereafter rotated monthly between the two partners.[FN1] Contact between the members was minimal, although both A-One and Y and Y were apparently successfully and profitably operated for some years. Petitioner testified, in support of his petition for dissolution, however, that he was unable to make decisions because of respondent's lack of co-operation and that fights were frequent. On one occasion the police were called. An attempt was made in 2012 to settle their differences through a negotiated buyout, but it was unsuccessful and it has been over a year since petitioner has spoken to respondent.

It is undisputed that A-One was closed in mid 2012 and petitioner moved out to open his own trucking and storage business at a new location, while respondent also established his own competing trucking and storage business, but continued to occupy a portion of the space previously occupied by A-One. Although A-One has not been formally dissolved, there is no dispute that, as a practical matter, it no longer exists as a business. While property of some of A-One's customers continues to be stored in the Building, the evidence is that the parties agreed to divide the customers of A-One equally, transferring their business to the separate businesses of the parties; however, e-mails exchanged between the members' wives evidence considerable bickering concerning the disposition of A-One's assets and the time each of the members was [*3]expected to contribute to the continuing operation of A-One and Y and Y. The Court rejects the argument that, because three of A-One's customers still store property in Y and Y's Building, dissolution should be denied. Storage is not the business of Y and Y, for which it has no license, but was the business of A-One, which both parties admit is no longer functioning.

The Court notes the receipt of an exchange of letters from counsel for the respective parties between December 24 and December 31, 2013, while the *prima facie* motion for dismissal was *sub judice*, in which petitioner accused respondent of changing the locks and disabling the garage door on the Building so as to deny him access, to which respondent's counsel responded, acknowledging

that the locks had been changed, purportedly in order to prevent petitioner's theft of anything left in the Building that was "not nailed down". In an affidavit, petitioner vigorously denied having removed any property from the premises. Respondent's counsel further initially asserted that a police report had been filed, although this assertion was subsequently withdrawn by counsel, who also explained that the locks had not been changed but that a "misunderstanding" had occurred. Respondent's sole witness, Suzanne, testified that the locks had not been changed, but that repairs had been made to the "gate", and that she knew nothing of the allegations of theft against petitioner.

Since mid 2012, the day-to-day operation of Y and Y has been managed by petitioner's wife, Naomi Natanel, and respondent's wife, Suzanne Mane. A-One had paid rent for its space, but, until this Court directed the payment of use and occupancy during the pendency of this proceeding, respondent paid no rent to Y and Y, thus causing a financial crisis for Y and Y, which was unable to pay the taxes on the Building. Though efforts have been made to find a new tenant for a portion of the space previously occupied by A-One, the parties could not agree on prospective tenants or the use of a particular broker. Obviously, respondent would have an interest in thwarting the creation of a new tenancy for the space he was occupying, rent-free, in Y and Y's Building. There was evidence, moreover, that respondent's new business, which bears the name A-One Van Lines, Inc., sent out letters to all of A-One's customers giving notice of the closing of A-One Moving and Storage and offering favorable terms to relocate the belongings of A-One's customers to its new location. This attempt to acquire more than half of the business of the parties' prior company may well have exacerbated petitioner's determination to terminate Y and Y, liquidate his investment by selling the Building and disassociate from the respondent. As noted, the parties have been able to agree to terminate the business operation of their shared corporation, A-One, and substantially wind up its affairs. The present litigation concerns their dispute over the fate of Y and Y: petitioner wishes to sell the Building and distribute the sale price, while respondent wants to retain the property as an "investment".

Respondent Cohen did not testify on his own behalf, but called his wife Suzanne, who had been employed by A-One prior to its demise. Suzanne testified that Y and Y had been very effectively managed by herself and Naomi, with whom she was in frequent communication. On rebuttal, however, Naomi vigorously refuted this testimony and adamantly declared her refusal to continue functioning as a surrogate for her husband in managing Y and Y. Naomi testified that she had observed first-hand the hostility between petitioner and respondent and heard threats exchanged between them, although she did acknowledge that she and Suzanne had managed the Building successfully, with the exception of the on-going disagreements regarding new tenancies and the

need to market the vacant space. This Court does not find the testimony of either wife to [*4]be convincing as each was obviously primarily concerned with supporting her husband's position in the litigation. The evidence is unequivocal, however, that Suzanne and Naomi have together effectively operated the business of Y and Y and that Y and Y would be quite profitable if the Building were fully occupied by rent-paying tenants. Petitioner himself admitted that the instant litigation and the on-going hostility between himself and respondent was not affecting the existing tenants. As to respondent's refusal to accept two prospective tenants, the evidence suggests the lack of consent was well-founded, either because of the terms demanded or because of the questionable financial viability of the tenant. Notwithstanding that LLCL §408(b) requires that management be by a majority vote, the disagreement as to whether one space or another should be rented out first does not present so insurmountable an obstacle to the reasonable practicability of continued operation of Y and Y as to alone warrant dissolution, especially now that respondent is paying for the use of his space. This Court has already rejected, in its decision of January 2, petitioner's contention that dissolution is warranted because Y and Y is not financially viable. As suggested by Suzanne, a professional manager could be hired to operate the Building, which would obviate the need for day-to-day interaction between the members or their spouses, a practice common in real estate investment. Given the length of time that Y and Y has been effectively operated through the ingenuity of the parties in circumventing their mutual hostility, this Court is unable to perceive a deadlock that would preclude the carrying on of the business of Y and Y as a real estate investment.

As "the dissolution of a limited liability company under [LLCL] §702 is initially a contract-based analysis" (*1545 Ocean* at 128), a necessary and critical issue of fact is, however, the purpose for the formation of Y and Y and the purchase of the Building. In the absence of any documentary evidence, the testimony of the parties must be dispositive (*cf. Mizrahi v Cohen*, 104 AD3d 917, 919 [2d Dept 2013]; *Sieni v JAMSFAB* ,2013 WL 3713604 *5 [Sup Ct, Suffolk County 2013]). While petitioner testified that the purchase of the Building was exclusively motivated by the need to retain the business premises of A-One and ensure that it would not be evicted upon a sale, Suzanne testified that petitioner had lauded the investment opportunity it presented and that she had been present with petitioner and respondent during a conversation in which the two men had discussed taking money out of Y and Y after the mortgage was paid off and that such income from the Building would permit them to retire. Upon rebuttal, petitioner denied having the conversation described, insisting he would not have purchased the Building as an investment but was forced to purchase because of the risk of loss of A-One's premises. Naomi also denied that investment was a purpose for the purchase of the Building, testifying that, at the time of the break-up of A-One, the disposition of Y and Y and the sale of the Building was discussed, but that respondent would not

agree, insisting that the property be retained as an investment. Suzanne herself acknowledged that no other properties had been purchased or even considered by Y and Y. Since respondent did not testify regarding his own purpose or his discussions with petitioner, the Court credits petitioner's testimony and finds that the sole purpose of Y and Y was to be a holding company for the real property which housed A-One and that, with the closure of A-One, that purpose is extinguished. Petitioner's position is that, with the closing of A-One, Y and Y's purpose no longer exists and dissolution is mandated.

Conclusions of Law

LLCL §702 provides for judicial dissolution of a limited liability company "whenever it [*5]is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement". In *Matter of 1545 Ocean Avenue, LLC* (72 AD3d 121), the Court examined the proper interpretation to be accorded the statutory standard "not reasonably practicable". While cautioning that a limited liability company is to be distinguished from both a corporation and a partnership, the Court noted that the language is derived from Revised Partnership Law § 121-802 and Partnership Law §63(1)(d). As no New York cases had interpreted the statutory standard (*but see Seligson v Russo*, 16 AD3d 253 [1st Dept 2005] interpreting the same language in Partnership Law §63(1)(d)), relying on the decision of the Delaware Chancery Court in *Red Sail Easter Ltd. Partners, LP v Radio City Music Hall Products, Inc* (1992 WL 251380, * 5-6[1992]), the Court noted that mere disagreements between partners regarding accounting are insufficient to warrant dissolution (*1545 Ocean at 128).* Rejecting the applicability of the more flexible statutory standards for judicial dissolution of both corporations and partnerships, the Court cited *Matter of Horning v Horning Construction, LLC* (12 Misc 3d 402, 413 [Sup Ct, Monroe County 2006]), in which, in the absence of an operating agreement, the court dismissed the petition for dissolution brought primarily to provide an exit-strategy for the disenchanted member, holding that LLCL §702 establishes a "more stringent" standard (72 AD3d at 127).[FN2] Rejecting petitioner's claim that dissolution was warranted by the parties' deadlock, in *1545 Ocean*, the Appellate Division, Second Department expressly held:"for dissolution of a limited liability company pursuant to *Limited Liability Company Law § 702*, the petitioning member must establish, in the terms of the operating agreement or articles of incorporation, that (1) the management of the entity is unable or unwilling to reasonably permit or promote the stated purpose of the entity to be realized or achieved, or (2) continuing the entity is financially unfeasible" (72 AD3d at 131). Thus, a petitioner seeking dissolution must demonstrate that the limited liability company is "unable to function as intended or that it is failing financially" (*id at 129).* It has already been determined that Y and Yis not failing financially and its continued operation is not unfeasible. The issue before the Court is, therefore, whether petitioner has established that Y and Y is unable to function so as to achieve its intended purpose.

Insisting that, in *1545 Ocean,* the Courtrecognized "deadlock as an underlying basis for dissolution under § 702", petitioner relies upon the Court's"borrowing" of the analysis of Delaware's Court of Chancery in applying its own substantially identical statute providing for the dissolution of a limited liability company (6 Del. C. § 18-802) (Petitioner's Letter Brief of [*6]January 24, 2014).[FN3] However, this Court perceives the Appellate Court's *1545 Ocean* decision as instructing the application of greater restraint in exercising the court's discretion to grant dissolution of a New York limited liability company.

Petitioner also cites five New York Supreme Court decisions in support of his petition to dissolve Y and Y based upon the animosity and resultant deadlock in managing the LLC. Three of those cases were decided before the Second Department defined "not reasonably practicable" in its January 2010 *1545 Ocean* decision *(Matter of Youngwall (Youngwall Realty, LLC)* 2008 WL 827916 [Sup Ct, Nassau County 2008]; *Dahlberg v Clipper Holding Assoc. LLC,* Index No. 115592/04 [Sup Ct , NY County 2005]; *Matter of Hauke(VB & H Financial Services, LLC)* Index No. 116251/04 [Sup Ct, NY County 2005]). In light of the *1545 Ocean* decision, which supercedes those cases and this Court is bound to follow, those cases will not be considered as reflecting controlling law. Petitioner also cites *Matter of Fass,* in which the court determined that dissolution had already been effected by the member's 60 day notice of termination as provided in the operating agreement and was only left to direct the winding up of the LLC's affairs. The finding that the parties' disagreement or conflict would alternatively justify dissolution, citing the concurring opinion in *1545 Ocean* of Fisher, J., concluding that a "disagreement or conflict among the members regarding the means, methods, or finances . . . so fundamental and intractable as to make it unfeasible for the company to carry on its business as originally intended" may meet the standard of not reasonably practicable' (72 AD3d at 133), is explained by the fact that no effort had been made to effectuate the purpose of the LLC. *Fass* is, therefore, actually consistent with the court's reasoning herein that the extinguishment of the purpose of the [*7]LLC warrants dissolution. Petitioner also relies upon *Matter of Selcuk (Salata LLC*)(2010WL 1954125[Sup Ct, NY County 2010]), in which the court determined that a management deadlock had resulted from the "dissension" between the members such that it was not reasonably practicable to carry on the business of the LLC, which was seriously in debt. Since this decision was rendered, the Appellate Division, First Department has adopted the ruling in *1545 Ocean,* suggesting that *Selcuk* might no longer be reliable authority (see *Doyle v Icon, LLC,* 103 AD3d 440 [1st Dept 2013]).

In contrast, in support of dismissal of the instant petition, respondent cites, in addition to *1545 Ocean* and *Eight of Swords, Sieni v JAMSFAB, LLC (*2013 WL at *5), in which the court observed:

"[d]isputes between members are alone not sufficient to warrant the exercise of judicial discretion to dissolve an LLC that is operates [sic] in a manner within the contemplation of its purposes and objectives" (accord *Matter of Eight of Swords*, 96 AD3d 839,840 [2d Dept 2012]; *Doyle v Icon, LLC*, 103 AD3d 440 [1st Dept 2013] (citing *1545 Ocean)).* This Court agrees with the above statement of the law as consistent with *1545 Ocean*. Upon the evidence that Y and Y is both financially viable and capable of operating efficiently even in the face of its members' acrimony, dissolution would be unwarranted. Notwithstanding the animosity between the members, the LLC continues to muddle along; whether it was meant to do so once A-One was no longer in business is the controlling issue in this case. The determinative question, in deciding this case, is: where the intended purpose of the LLC no longer exists, must the petition be granted? This Court finds that the clear language of LLCL § 702 mandates that it must.

Respondent relies upon his contention that the purpose of Y and Y was to provide a vehicle for real estate investment. The statute mandates an examination of the operating agreement or the articles of organization defining the purposes of the LLCto determine whether it is reasonably practicable to continue the business. As noted, however, no operating agreement was ever signed here and the articles of organization fail to recite the purpose of the LLC. While generally, under such circumstances, the LLCL will prescribe the default rules, the statute cannot define the purely contractual basis for forming the LLC so as to permit a determination of whether its purpose is being thwarted by the conflict between the members.

In *Horning* (12 Misc 3d at 408-413), analyzing the effects of the 1999 amendments to the LLCL (L1999, ch 420), the court noted that a member desirous of withdrawing from the LLC, which appears to be petitioner's purpose here, may not do so "just for the asking, especially if there is no operating agreement". Rather, the default provisions of LLCL § 701 require the continuation of the LLC upon the termination of any membership interest, leaving such member at the mercy of other members if the statutory standard of § 702 is not met. As noted in *Horning*, this is especially true because there is no buy-out provision in the LLCL **[FN4]**. However, the controlling statute provides for dissolution of the LLC, in the discretion of the court, where the purpose of the LLC can no longer be achieved. The credible, competent evidence is that petitioner and respondent formed Y and Y exclusively in order to continue to house A-One. [*8]There is no dispute that A-One no longer functions as a business and, indeed, both partners have formed separate businesses in competition with A-One and each other. In such circumstances, Y and Y's purpose no longer exists and dissolution is appropriate.

Petitioner seeks the appointment of a liquidating trustee, pursuant to LLCL §703 to wind up the affairs of the LLC and distribute its assets. The Court will make such appointment if the parties cannot agree upon a more appropriate course of action, such as an agreed buyout or a mutually-agreeable broker to market the property. If no agreement can be reached, each party shall submit the names of at least two candidates to act as liquidating trustee no later than May 5, 2013.

CONCLUSIONThe petition for dissolution is granted. Petitioner is directed to file a certificate of dissolution with the Secretary of State within 30 days. The parties shall submit the names of prospective liquidating trustees to this Court on or before May 5, 2013.

This constitutes the decision and order of the Court.

April 18, 2014_____

CAROLYN E. DEMAREST

JUSTICE OF THE SUPREME COURT

Footnotes

Footnote 1: Petitioner testified that the origin of the animosity between the parties was related to respondent's relationship to the secretaries employed by the business. The circumstances were not further developed at trial, except that petitioner admitted on cross examination that, before work began, he would visit sites on his computer containing sexual materials, of which the staff, according to petitioner, had no complaints. In her testimony, petitioner's wife stated that respondent had accused her of "seducing him". There was also testimony that the amount of time devoted to A-One's business was becoming a point of contention as respondent accused petitioner of maintaining a separate business selling used cars.

Footnote 2: The *Horning* decision seems to suggest that the failure to create an operating agreement, or to express the purpose of the LLC in the Articles of Organization, may preclude the granting of a petition for dissolution based exclusively on the frustration of the purpose of the LLC (12 Misc 3d at 411; see also, *Matter of Fass Corp. (Emily Kodiak Developers of Woodbury, LLC),* 31 Misc 3d 782, 785 [Sup Ct, Nassau County 2011] (finding that because "an operating agreement is essential to determining whether judicial dissolution should be granted", "if the operating agreement is terminated, there is no basis for the court to determine whether in the context of the . . . operating agreement' the stated purpose of the company may be realized")). This Court does not find such result to be the statutory intent.

Footnote 3: Petitioner cites numerous decisions from the Delaware Court adopting deadlock as a basis to grant dissolution; however, most of the cases are distinguishable on both the facts and the legal analysis. In *Haley v Talcott* (864 A. 2d 86 [Del. Ch. 2004]), the contractual buy-out provision was rejected as inequitable and dissolution was granted to break a deadlock that was precluding the LLC from functioning based upon the application of the language of Delaware's General Corporate Law §273 providing for judicial dissolution of joint venture corporations with only two shareholders. Similarly, in *In re: Silver Leaf, LLC* (2005 WL 2045641), applying Delaware's dissolution statute for limited partnerships (6 Del. C. §17-802), the court granted dissolution on a finding that, not only was there deadlock between the members, but the LLC's business purpose was both moot and fraudulent. See also *Phillips v Hove* (2011 WL 4404034 [Del Ch 2011]), in which a complex of legal and factual issues, including both parties' breach of fiduciary duty to the LLC, led the Court to grant dissolution based on deadlock. In *Vila v BVWEBTIES* LLC (2010 WL 3866098) and *Fisk Ventures, LLC v Segal* (2009 WL 73957 [Del. Ch. 2009]), dissolution was granted upon findings of "deadlock" where the company was already non-existent ("no office, no employees, no operating revenue, no prospects of equity" (*Fisk*);no license to operate (*Vila*), applying the logic of DGCL §273 (in *Vila*) and 6 Del. C. §17-802, applicable to limited partnerships (in *Fisk).* Most of the subject LLCs did have an operating agreement or other controlling documentation, unlike Y and Y. Given the Court's admonition in *1545 Ocean,* that LLCs are not to be treated like corporations or parnerships for purposes of judicial dissolution, but are subject to a much higher standard, it does not appear that Delaware law applies in New York.

Footnote 4: However, in *Mizrahi v Cohen,* the Appellate Division, Second Department recognized that, although the LLCL "does not expressly authorize a buyout in a dissolution proceeding, . . . in certain circumstances, a buyout may be an appropriate equitable remedy" (104 AD3d at 920).

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