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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: O. PETER SHERWOOD, *Justice* PART 49

ALFRED THOMAS GIULIANO, *et al.*,

Plaintiffs,

-against-

STEPHEN GAWRYLEWSKI, *et al.*,

Defendants.

INDEX NO. 654215/2012

MOTION DATE June 18, 2013

MOTION SEQ. NO. 001

MOTION CAL. NO. ______

The following papers, numbered 1 to ______ were read on this motion to dismiss action.

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
Answering Affidavits — Exhibits	
Replying Affidavits	

Cross-Motion: □ Yes □ No

Upon the foregoing papers, it is ordered that this motion to dismiss action is decided in accordance with the accompanying decision and order.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE
FOR THE FOLLOWING REASON(S):

Dated: June 27, 2013

O. P. Sherwood

O. PETER SHERWOOD, *J.S.C.*

Check one: ☑ FINAL DISPOSITION □ NON-FINAL DISPOSITION

Check if appropriate: □ DO NOT POST □ REFERENCE

□ SUBMIT ORDER/ JUDG. □ SETTLE ORDER/ JUDG.

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY: COMMERCIAL DIVISION PART 49

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ALFRED THOMAS GIULIANO, CHAPTER 7
TRUSTEE, c/b/o NEC HOLDINGS CORP.,
and JOAN LEVY, directly,

Plaintiffs,

-against-

STEPHEN GAWRYLEWSKI, DENISE F. UNGAR
STERN, LESLIE F. STERN, RITA L. UNGAR
MOSER, NATHAN F. MOSER, and LOUGHLIN
MANAGEMENT PARTNERS + CO.,

Defendants.

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DECISION AND ORDER

Index No. 654215/2012
Mot. Seq. Nos.: 001-003

O. PETER SHERWOOD, J.:

Before the court are three motions to dismiss the complaint in this action arising from the Chapter 7 bankruptcy filing of NEC Holdings Corp. ("NEC" or the "Company"). As these are motions to dismiss, the allegations are taken from the complaint and are assumed to be true (*see Morone v Morone*, 50 NY2d 481, 484 [1980]).

Plaintiff Alfred Thomas Giuliano is the Chapter 7 Trustee ("Trustee") in the bankruptcy proceeding of NEC. Plaintiff Joan Levy ("Levy") was a member of NEC's board of directors and a beneficial owner of 25% of the Company's equity.

Defendant Stephen Gawrylewski ("Gawrylewski") was NEC's chief restructuring officer ("CRO") from March 18, 2009 until July 23, 2010, and an employee of defendant Loughlin Management Partners + Company, formerly known as Loughlin Meghji + Co ("LM"). He was placed at NEC pursuant to a services contract between NEC and LM. Defendants, Denise F. Ungar Stern ("D. Stern") and Rita L. Ungar Moser ("R. Moser") were during the time relevant to this action, members of the board of directors of NEC. Each was a beneficial owner of 25% of the Company. Defendant Leslie F. Stern ("L. Stern") is D. Stern's husband and is a former director, CEO, and COO of NEC (D. Stern and L. Stern are sometimes referred to collectively as the "Sterns"). Defendant Nathan F. Moser ("N. Moser") is R. Moser's husband and is a former director, President, and CEO of NEC (R. Moser and N. Moser are sometimes referred to collectively as the "Mosers").

The NEC board consisted of five members: non-party William Ungar, and his daughters, non-party Florette Shaashua, plaintiff Levy, defendant R. Moser, and defendant D. Stern. Plaintiffs allege that at the time the events described in the complaint occurred, William Ungar was 96 years old and "generally followed the advice of the Mosers and Sterns on matters related to NEC and, as a result, voted as a director according to their wishes." The complaint does not allege facts or assert that Ungar was mentally infirm.

Plaintiffs allege that the defendants took advantage of NEC's financial distress to pursue their personal interests in obtaining control of the Company, and reaping other personal benefits to the detriment of the Company, its creditors, non-defendant shareholders, and employees. Specifically, the defendants jeopardized, and ultimately sacrificed, the interests of these parties by refusing to consider all options that might have averted bankruptcy. This action is brought by the Trustee on behalf of the Company and its creditors, and by Levy directly in her personal capacity.

The complaint asserts five causes of action: (1) breach of fiduciary duties (against Gawrylewski and his employer, LM); (2) aiding and abetting breach of fiduciary duties (against D. Stern and R. Moser); (3) breach of fiduciary duties (against D. Stern and R. Moser); (4) aiding and abetting breach of fiduciary duties (against L. Stern and N. Moser); and (5) negligence (against Gawrylewski and LM). All claims arise from an alleged refusal of defendants to pursue Levy's proposal to raise funds required to avert bankruptcy through a high-yield bond transaction (the "high-yield alternative"). The other directors and Gawrylewski sought to raise cash through sale of equity interests in NEC.

In motion sequence number 001, the Sterns and Mosers seek dismissal of the complaint as against them, specifically the Second, Third and Fourth Causes of Action. In motion sequence number 002, LM seeks dismissal of the complaint against it, specifically the First and Fifth Causes of Action. In motion sequence number 003, Gawrylewski moves to dismiss the claims against him, specifically the First and Fifth Causes of Action.

DISCUSSION

Since NEC was incorporated in Delaware, substantive Delaware law applies to this case (*see Hart v General Motors Corp.*, 129 AD2d 179 [1st Dept 1987]). Claims for breach of fiduciary duty are subject to the heightened pleading standards of CPLR 3016.

A. Motion to Dismiss Standards

1. CPLR 3211 (a) (1) Standard

To succeed on a motion to dismiss, pursuant to CPLR 3211 (a) (1), the documentary evidence submitted that forms the basis of a defense must resolve all factual issues and definitively dispose of the plaintiff's claims (*see 511 W. 232nd Owners Corp. v Jennifer Realty Co.*, 98 NY2d 144, 152 [2002]; *Blonder & Co., Inc. v Citibank, N.A.*, 28 AD3d 180 [1st Dept 2006]). A motion to dismiss pursuant to CPLR 3211 (a) (1) "may be appropriately granted only where the documentary evidence utterly refutes plaintiff's factual allegations, conclusively establishing a defense as a matter of law" (*McCully v Jersey Partners, Inc.*, 60 AD3d 562, 562 [1st Dept 2009] [citation omitted]).

CPLR 3211 (a) (1) does not explicitly define "documentary evidence." As used in this statutory provision, "'documentary evidence' is a 'fuzzy term', and what is documentary evidence for one purpose, might not be documentary evidence for another" (*Fontanetta v John Doe 1*, 73 AD3d 78, 84 [2d Dept 2010]). "[T]o be considered 'documentary,' evidence must be unambiguous and of undisputed authenticity" (*id.* at 86, citing Siegel, Practice Commentaries, McKinney's Cons. Laws of N.Y., Book 7B, CPLR 3211:10, at 21-22). Typically, that means judicial records such as judgments and orders, as well as documents reflecting out-of-court transactions such as contracts, releases, deeds, wills, mortgages and any other papers, "the contents of which are 'essentially undeniable'" (*id.* at 84-85).

2. CPLR 3211 (a) (7) Standard

On a motion to dismiss a plaintiff's claim pursuant to CPLR 3211 (a) (7) for failure to state a cause of action, the court is not called upon to determine the truth of the allegations (*see Campaign for Fiscal Equity v State*, 86 NY2d 307, 317 [1995]; *219 Broadway Corp. v Alexander's, Inc.*, 46 NY2d 506, 509 [1979]). Rather, the court is required to "afford the pleadings a liberal construction, take the allegations of the complaint as true and provide plaintiff the benefit of every possible inference. Whether a plaintiff can ultimately establish its allegations is not part of the calculus in determining a motion to dismiss" (*EBC I v Goldman, Sachs & Co.*, 5 NY3d 11, 19 [2005] [citation omitted]). The court's role is limited to determining whether the pleading states a cause of action, not whether there is evidentiary support to establish a meritorious cause of action (*see Guggenheimer v Ginzburg*, 43 NY2d 268, 275 [1977]; *Sokol v Leader*, 74 AD3d 1180 [2d Dept 2010]).

While affidavits may be considered on a motion to dismiss for failure to state a cause of action, unless the motion is converted to a CPLR 3212 motion for summary judgment, the court will not consider them for the purpose of determining whether there is evidentiary support for properly pleaded claims, but, instead, will accept such submissions from a plaintiff for the limited purpose of remedying pleading defects in the complaint (*see Nonnon v City of New York,* 9 NY3d 825, 827 [2007]; *Rovello v Orofino Realty Co.,* 40 NY2d 633, 635-636 [1976]). Affidavits submitted by a defendant will almost never warrant dismissal under CPLR 3211 "*unless* they 'establish conclusively that [plaintiff] has no . . . cause of action" (*Lawrence v Graubard Miller,* 11 NY3d 588, 595 [2008], citing *Rovello,* 40 NY2d at 636). In this posture, the lack of an affidavit by someone with knowledge of the facts will not necessarily serve as a basis for denial of a motion to dismiss. Accordingly, the court will construe the complaint in the generous light to which it is entitled on a motion to dismiss.

B. The Sterns and Mosers Motion

The Sterns and the Mosers (collectively, the "Sterns/Mosers") move to dismiss the Second, Third and Fourth Causes of Action.

1. The Levy Claims

The Sterns/Mosers first argue that Levy's claims must be dismissed, because (1) Levy has no standing to bring an individual claim against the Sterns/Mosers for harm to NEC, and (2) Levy has no claim against the Sterns/Mosers for the $400,000 she allegedly spent on the high-yield alternative. Plaintiffs do not address the second point in their opposition papers, and thus apparently concede that Levy has no claim for the $400,000 she spent.

In order to bring a claim for a direct injury under Delaware law, the claimed direct harm "must be independent of any alleged injury to the corporation. The stockholder must demonstrate that the duty breached was owed to the stockholder and that he or she can prevail without showing an injury to the corporation" (*Tooley v Donaldson, Lufkin & Jenrette, Inc.*, 845 A2d 1031, 1039 [Del 2004]). "The mere fact that the alleged harm is ultimately suffered by, or the recovery would ultimately inure to the benefit of, the stockholders does not make a claim direct under *Tooley*" (*Feldman v Cutaia*, 951 A2d 727, 733 [Del 2008]). "A breach of fiduciary duty that works to preclude or undermine the likelihood of an alternative, value-maximizing transaction is treated as a derivative claim because the company suffers the harm, having been 'precluded from entering into a transaction that would have maximized the return on its assets'" (*In re NYMEX Shareholder Litig.*, 2009 WL 3206051, *9 [Del Ch Sept. 30, 2009], quoting *Agostino v Hicks*, 845 A2d 1110, 1123 [Del Ch 2004]).

The Sterns/Mosers argue that Levy is seeking to recover damages in her individual capacity as a former shareholder of NEC. Indeed, Levy asserts in the complaint that she brought "this action to recover her personal damages that resulted from the Defendants' breaches" (Complaint ¶ 9). The Sterns/Mosers argue that Levy cannot demonstrate, as she must, that she "suffered some individualized harm not suffered by all of the stockholders at large" (*Feldman*, 951 A2d at 733). For these reasons, Levy's complaint must be dismissed.

In opposition, plaintiffs contend that Levy has alleged that, in addition to harm to NEC, the defendants' actions caused Levy a personal injury, i.e., the loss of the entire value of her shares of NEC. This argument is without merit, because all of NEC's shareholders suffered the same injury (*see id.*). Accordingly, Levy's claims must be dismissed.[1]

2. Breach of Fiduciary Duty Claims

Defendants argue that plaintiffs' Third Cause of Action (breach of fiduciary duties against D. Stern and R. Moser) should be dismissed, because (1) the business judgment rule protects board decisions concerning the high-yield alternative, and (2) the complaint does not identify acts or omissions by either D. Stern or R. Moser that might constitute a breach of fiduciary duty.

In connection with the business judgment rule arguments, defendants assert that (1) D. Stern and R. Moser did not have an interest and did not lack independence, and (2) plaintiffs have not pleaded that a majority of the board was interested or lacked independence. The business judgment rule "is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interest of the company" (*Aronson v Lewis*, 473 A2d 805, 812 [Del 1984], *overruled on other grounds*, *Brehm v Eisner*, 746 A2d 244 [Del 2000]). Under that rule, "a court will not substitute its judgment for that of the board if the latter's decision can be attributed to any rational business purpose" (*Unocal Corp. v Mesa Petroleum Co.*, 493 A2d 946, 954 [Del 1985] [internal quotation marks omitted]). In order to overcome the presumption, plaintiffs must allege a "disabling" directorial interest, which arises

[1] These reasons also mandate that Levy's complaint against Gawrylewski and LM must be dismissed as well.

"whenever divided loyalties are present, or a director either has received, or is entitled to receive, a personal financial benefit from the challenged transaction which is not equally shared by the stockholders" (*Pogostin v Rice*, 480 A2d 619, 624 [Del 1984], *overruled on other grounds, Brehm*, 746 A2d at 244; *see also Orman v Cullman*, 794 A2d 5, 25 n 50 [Del Ch 2002]). To be "disabling," an interest must be "of such subjective material significance to that particular director that it is reasonable to question whether that director objectively considered the advisability of the challenged transaction to the corporation and its shareholders" (*Orman*, 794 A2d at 5 n 50).

Defendants argue that D. Stern and R. Moser did not have a disabling interest and did not lack independence. Accordingly, defendants aver that plaintiffs cannot overcome the presumption. In this regard, defendants contend that due to the "conclusory and self-contradictory allegations" in the complaint, it is nearly impossible to determine what interests were so seductive to R. Moser and D. Stern that the performance of their duties as directors was compromised. Defendants argue that D. Stern, R. Moser and Levy each had precisely the same equity interest in the company, and that the purpose of the high-yield alternative was to "avert a change in control and benefit all shareholders equally." Further, defendants argue that the complaint does not allege that the Sterns/Mosers were interested in any way in the actual sale of NEC or its assets in the bankruptcy proceeding. In fact, all of the shareholders lost their equity in NEC as a result of the bankruptcy. Additionally, NEC never consummated a sale or other transaction in which the Sterns/Mosers are alleged to have an interest.

Defendants also contend that the complaint does not adequately allege the interests of L. Stern or N. Moser. Defendants note that the complaint alleges that L. Stern became "affiliated" with the Alpine Group ("Alpine") for the purpose of proposing a capital contribution to NEC, as required by G.E. Capital Corp. ("GECC"), NEC's principal lender, and further that N. Moser was similarly "affiliated" with KPS Capital Partners, LP ("KPS"), another potential investor or bidder for NEC. Defendants argue that nowhere does the complaint quantify or describe any financial interest or benefit that might accrue to L. Stern or N. Moser through those purported relationships, nor does it state the "economic circumstances" required to support a finding of a disabling interest (*see In re General Motors Class H Shareholders Litig.*, 734 A2d 611, 617 [Del Ch 1999] [dismissing breach of fiduciary duty claim where challenge to independence of board members was "too weak to state a claim that the business judgment rule does not apply . . . . To show that a . . . director's independence was compromised by her ownership of greater amounts of . . . stock, the plaintiffs must plead that the amount of such holdings and the predominance of such holdings over GMH holdings was of a sufficiently material importance, in the context of the director's economic circumstances, as to have made it improbable that the director could perform her fiduciary duties to the . . . shareholders without being influenced by her overriding personal interest in the performance of the . . . shares"]).

Defendants further argue that plaintiffs fail to plead how the "self interest" L. Stern and N. Moser had in blocking the high-yield alternative is imputed to D. Stern and R. Moser, who undoubtedly had as much of an interest in preserving their equity interests in NEC as Levy.

In opposition, plaintiffs contend that D. Stern and R. Moser were not disinterested directors, and further that they have properly pleaded that D. Stern and R. Moser breached their duties of loyalty. In this regard, plaintiffs rely heavily on paragraph 20 of the complaint. Plaintiffs argue that they pleaded that the sisters' husbands were actively pursuing opportunities to acquire NEC to the exclusion of the other shareholders. By way of example, plaintiffs contend that the complaint asserts that Gawrylewski and the Sterns/Mosers aligned their interests to facilitate a transaction that would result in them, individually or jointly, obtaining control of NEC's assets through a sale transaction (Complaint ¶ 20). Plaintiffs assert that D. Stern and R. Moser used their directors' votes to support their husbands' interests by attempting to control the selection of an investment banker that would tolerate the creation of an "inside" shareholder track for introduction of purchasers. Further, the Sterns/Mosers acted in their own self-interest to attempt to force a sale of a controlling interest in NEC that would provide significant benefits solely to themselves in their individual capacities, rather than to the Company and NEC equally. In addition, the Sterns/Mosers blocked the steps necessary for the high-yield alternative's continued viability by refusing to approve a budget that would enable completion of an offering circular.

Plaintiffs further argue that the sisters' familial interests render them "interested." Under Delaware law, "disinterested directors" have been defined "as those directors that '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.' Likewise, 'independent' means that a 'director's decision is based on the corporate merits of the subject before the board rather than extraneous considerations or influences' " (*Williams v Geier*, 671 A2d 1368, 1379 n 19 [Del 1996], quoting *Aronson*, 473 A2d 805, 812 [other citations omitted]). Plaintiffs contend that under this test, D. Stern and R. Moser were not disinterested. Plaintiffs argue that the complaint alleges that at the behest of their husbands, the sisters were, in effect, on both sides of NEC's efforts to obtain financing necessary to cure NEC's default (Complaint ¶ 20). Furthermore, the complaint alleges that D. Stern and R. Moser had a significant personal financial interest in the outcome of the funding, and stood to benefit personally in a manner different that the other shareholders from their efforts to block the high-yield alternative (Complaint ¶ 20-21). Additionally, D. Stern and R. Moser conspired with Gawrylewski and LM to block the high-yield alternative and limit Levy's input into the financing process, thereby dominating the financing discussions.

The complaint does not reveal what sort of "alignment" or "interests" the husbands, and consequently the sisters, had with the potential investors. The complaint uses only the most conclusory terms to describe these connections. Indeed, the complaint provides no factual detail whatsoever concerning these purported "alignments." Further, apart from the undisputed allegation that they share the same parents, the complaint does not state how D. Stern and R. Moser were rendered interested, and thus unable to act in an independent manner with respect to the transaction Levy favored, i.e., the high-yield alternative. Defendants assert, correctly, that the complaint does not illuminate how L. Stern or N. Moser's purported "alignment" with any potential investor or bidder was different in any respect from Levy's "alignment" with Global Hunter, the investment banking firm Levy sought to introduce to NEC in connection with her proposal to explore the high-yield alternative. These allegations are insufficient to satisfy the heightened pleading requirements of CPLR 3016.

Plaintiffs' failure to plead with particularity aside, plaintiffs have failed to adequately plead that a majority of the board was interested or lacked independence and therefor cannot rebut the business judgment rule presumption. As former Chancellor Chandler has explained:

> "As a general matter, the business judgment rule presumption that a board acted loyally can be rebutted by alleging facts which, if accepted as true, establish that the *board* was either interested in the outcome of the transaction or lacked the independence to consider objectively whether the transaction was in the best interest

> of its company and all of its shareholders. To establish that a *board* was interested or lacked independence, a plaintiff must allege facts as to the interest and lack of independence of the *individual members* of that board. To rebut successfully business judgment presumptions in this manner, thereby leading to the application of the entire fairness standard, a plaintiff must normally plead facts demonstrating 'that a *majority* of the director defendants have a financial interest in the transaction or were dominated or controlled by a materially interested director'"

(*Orman*, 794 A2d at 22 [citations omitted]; *see also Carsanaro v Bloodhound Tech. Inc.*, 65 A3d 618, 637 [Del Ch 2013] ["[t]o overcome the presumption of loyalty, a stockholder plaintiff must allege facts supporting a reasonable inference that there were not enough independent and disinterested individuals among the directors making the decision to comprise a board majority"]). Indeed, in *Orman*, the Chancellor noted that "[the company] had an eleven-member board. In order to rebut the presumptions of the business judgment rule, [plaintiff] must allege facts that would support a finding of interest or lack of independence for a majority, or at least six, of the Board members" (*id.* at 24-25). NEC had a five-member board: defendant D. Stern, defendant R. Moser, plaintiff Levy, non-party William Ungar, and non-party Florette Shaashua. In order to rebut the business judgment rule presumption, plaintiffs must allege that three members of the board members had a financial interest in blocking the high-yield alternative or were dominated or controlled by a materially interested director (*id.* at 22). No such claim has been asserted here. Plaintiffs have not alleged that William Ungar or Florette Shaashua (and certainly not Levy) had a financial interest, or were dominated or controlled by either D. Stern or R. Moser.

In footnote 2 of the complaint, plaintiffs assert that William Ungar "was 96 years old when the events described in the Complaint occurred. He generally followed the advice of the Mosers and Sterns on matters related to NEC and, as a result, voted as a director according to their wishes" (Complaint ¶ 20 n 2). Plaintiffs assert that these allegations are enough to establish that William Ungar was controlled by the Sterns/Mosers and therefore lacked independence. "Control over individual directors is established by facts demonstrating that 'through personal or other relationships the directors are beholden to the controlling person' or so under 'their influence that their discretion would be sterilized'" (*Benihana of Tokyo, Inc. v Benihana, Inc.*, 891 A2d 150, 174-175 [Del Ch 2005]). The complaint merely alleges that William Ungar was 96 years old at the time, and that he generally followed the wishes of the Sterns/Mosers. But "a consistent and unvaried pattern of deferring to anything" the controlling person wants is insufficient, by itself, to establish a lack of independence (*see In re Tyson Foods, Inc.*, 919 A2d 563, 588 [Del Ch 2007]). The additional allegation that William Ungar was 96 is not grounds for inferring any lack of independence. Accordingly, plaintiffs have failed to establish that a majority of the board was interested or lacked independence; at most, they have alleged that two of the five directors were interested.

Plaintiffs also argue that the business judgment rule "is irrelevant and inapplicable to the facts of this case." In this regard, plaintiffs advance three arguments: (1) a number of courts have refused to dismiss complaints when defendants invoke the business judgment rule, because it is an affirmative defense; (2) 8 Del C § 144, and not the business judgment rule, apply to the facts of this case; and (3) the court must apply enhanced *Revlon* scrutiny to the facts of this case, because the transactions contemplated by the board involved a sale of control. I address these arguments in turn.

Regarding the first argument, plaintiff cites *In re Tower Air, Inc.*, 416 F3d 229, 238 [3d Cir 2005] where the Third Circuit has stated, "[g]enerally speaking, we will not rely on an affirmative defense such as the business judgment rule to trigger dismissal of a complaint under Rule 12(b)(6)". The decision which interpreted Fed. R. Civ. P. Rule 12(b)(6), is inconsistent with the law of Delaware where the Federal Rules of Civil Procedure do not apply. In Delaware, "the business judgment rule 'operates as both a procedural guide for litigants and a substantive rule' . . . . As a procedural guide [it] places the initial burden of proof on the plaintiff" (*Cinerama Inc. v Technicolor, Inc.*, 663 A2d 1156, 1162 [Del 1995]). "On a motion to dismiss, the pled facts must support a reasonable inference that in making the challenged decision, the board of directors breached either its duty of loyalty or its duty of care" (*Gantler v Stephens*, 965 A2d 695, 706 [Del 2009]). Accordingly, Delaware courts, and New York courts applying Delaware law, routinely dismiss complaints on motions to dismiss where plaintiffs fail to rebut the presumptions of the business judgment rule (*see, e.g.*, *In re Tyson Foods, Inc.*, 919 A2d 563, 587-588 [Del Ch 2007]; *HF Lexington KY LLC v Wildcat Synergy Mgr. LLC*, 35 Misc 3d 1210(A) [Sup Ct, NY County 2012, Fried, J.]).

As to the argument that the business judgment rule applies only when a decision is made by a majority of independent, disinterested directors, plaintiffs cite to *In re Network Access Solutions, Corp.* (330 BR 67, 77 [Bankr D Del 2005]), where the court held that "[t]he decision of a majority of the disinterested directors to execute a transaction with an interested director is subject to the business judgment rule." Plaintiffs reason that this court's analysis must focus on three directors: William Ungar, Levy and Florette Shaashua. Since three members make a majority of NEC's board, and since these three board members split 2-1 in deciding whether to block the high-yield alternative, plaintiffs contend that there were not enough disinterested director votes to approve the transaction. In plaintiffs' view, the vote among the three directors would have to be 3-0, with three (3) constituting a majority of the board, to apply the business judgment rule. Thus, at no point in time was there majority support among the independent, disinterested directors to block the high-yield option. This reasoning is flawed. *Network Access Solutions*, on which plaintiffs rely, itself relies on 8 Del C § 144. That statute is inapplicable to the facts of this case. 8 Del C § 144 (Interested directors; quorum) states, in relevant part:

> (a) No contract or transaction between a corporation and 1 or more of its directors or officers, or between a corporation and any other corporation, partnership, association, or other organization in which 1 or more of its directors or officers, are directors or officers, or have a financial interest, shall be void or voidable solely for this reason, or solely because the director or officer is present at or participates in the meeting of the board or committee which authorizes the contract or transaction, or solely because any such director's or officer's votes are counted for such purpose, if:
>
> > (1) The material facts as to the director's or officer's relationship or interest and as to the contract or transaction are disclosed or are known to the board of directors or the committee, and the board or committee in good faith authorizes the contract or transaction by the affirmative votes of a majority of the disinterested directors, even though the disinterested directors be less than a quorum

(8 Del C § 144). In interpreting this statute, the court in *Network Access Solutions* stated that "[t]o establish protection under section 144, however, requires evidence that the transfers had the approval of a disinterested majority of the board of directors and that approval was a sound exercise of the directors' business judgment" (*Network Access Solutions*, 330 BR at 78). Section 144 creates a "safe harbor," the intent of which "is to remove the taint of a director's self-interest in a transaction where there is an approving vote of a majority of the informed and disinterested directors" (*id.*) The safe harbor applies only to completed transactions in which the director defendants stood on both sides of the transaction. Here, the high-yield alternative was not a completed transaction. Indeed, the transaction was never completed. Moreover, R. Moser and D. Stern were not on both sides of the

high-yield alternative "transaction." As defendants note, if anyone could be said to be on both sides of the high-yield alternative, it was Levy. The safe harbor created by 8 Del C § 144 is inapplicable.

In their third argument, plaintiffs aver that since the transactions contemplated by the board involved a sale of control, the board's actions must be judged pursuant to the enhanced scrutiny required under *Revlon, Inc. v MacAndrews & Forbes Holdings, Inc.* (506 A2d 173 [Del 1986]), and not the business judgment rule. In a sale or change of control transaction, the duty of the board changes from the preservation of the "corporate entity to the maximization of the company's value at a sale for the stockholders' benefit" (*id.* at 182). In such a circumstance, directors "have the obligation of acting reasonably to seek the transaction offering the best value reasonably available to the stockholders" (*Paramount Communications Inc. v QVC Network Inc.*, 637 A2d 34, 43 [Del 1993]). *Revlon* is inapplicable to the facts of this case. The transaction at issue in this case is the high-yield alternative, the purpose of which was to *avoid* a sale or change of control transaction. *Revlon* duties apply only when a sale or change of control becomes inevitable, which plaintiffs specifically contend was not the case (Complaint ¶ 37). Because plaintiffs have not rebutted the business judgment rule presumption, the third cause of action must be dismissed.

3. Aiding and Abetting Claims

The Second Cause of Action alleges aiding and abetting breach of fiduciary duties against D. Stern and R. Moser. The Fourth Cause of Action alleges aiding and abetting breach of fiduciary duties against L. Stern and N. Moser. In Delaware, a claim for aiding and abetting breach of fiduciary duty has four elements: "(1) the existence of a fiduciary relationship; (2) the breach of a duty by the fiduciary; (3) the knowing participation in the breach by the defendant, who is not a fiduciary; and (4) damages to the plaintiff resulting from the concerted action of the fiduciary and the nonfiduciary" (*In re Jevic Holding Corp.*, 2011 WL 4345204, *13 [Bankr D Del Sept. 15, 2011]).

The very definition of a cause of action for aiding and abetting breach of fiduciary duty mandates dismissal of the second cause of action because it is uncontested that D. Stern and R. Moser were fiduciaries. The third element of the claim requires plaintiffs to allege "the knowing participation in the breach by the defendant, *who is not a fiduciary*" (*id.* [emphasis added]) Since D. Stern and R. Moser were fiduciaries, the claim must be dismissed (*In re Verestar, Inc.*, 343 BR 444, 482 [Bankr SDNY 2006] [applying Delaware law, holding that "a claim for aiding and abetting breach of fiduciary duty can only be sustained against a non-fiduciary"]).

Turning to the fourth cause of action (aiding and abetting breach of fiduciary duties against L. Stern and N. Moser), the claim must be dismissed because, as described above, plaintiffs fail to adequately allege an underlying breach of fiduciary duty, a required element of the claim.

C. Gawrylewski and LM

Two claims are asserted against Gawrylewski and LM: the First (breach of fiduciary duties) and Fifth (negligence) Causes of Action.

1. Breach of Fiduciary Duty

As to the First Cause of Action, to state a claim for breach of fiduciary duty in Delaware, plaintiffs must plead: (1) the existence of a fiduciary relationship; (2) misconduct by the fiduciary; and (3) damages. In connection with this claim, Gawrylewski raises two arguments, each of which, he asserts, mandates its dismissal: (1) the complaint fails to allege any conduct by Gawrylewski constituting a breach of his fiduciary duties; and (2) plaintiffs fail to allege any connection between any purported breach of a fiduciary duty by Gawrylewski and any loss suffered by plaintiffs.

With regard to his first argument, Gawrylewski contends that plaintiffs have not provided particularized allegations of misconduct sufficient to rebut the business judgment rule presumptions. Indeed, Gawrylewski argues that the only portion of the complaint where plaintiffs allege Gawrylewski breached his duty of loyalty is a single allegation that he "aligned himself with various bidders to obtain employment and a control position with the successful bidder" (Complaint ¶ 20). Gawrylewski argues that plaintiffs fail (1) to identify the various bidders, (2) to allege any specific relationship between Gawrylewski and such bidders, (3) to allege that he had obtained or would obtain any personal benefits from any such bidder, (4) to identify any transaction or agreement between Gawrylewski and any such bidder, and (5) to allege that he actually caused NEC to enter into any transaction with any entity in which he had any interest at all.

Gawrylewski next avers that even if plaintiffs had adequately alleged that a breach fiduciary duty, the claim should be dismissed because plaintiffs have not adequately alleged any causal connection between his actions and any harm to the plaintiffs. Defendants note that the complaint does not allege that pursuing the high-yield alternative would necessarily have resulted in a different outcome for NEC. Rather, it merely alleges that defendants "refus[ed] to consider all options that might have averted the Company's Chapter 11 filing and ultimate disastrous sale and liquidation"

(Complaint ¶ 9). Defendants aver that such speculation is insufficient to maintain a claim, particularly where plaintiffs do not and cannot allege that NEC would have obtained required approvals for the high-yield alternative, such as from GECC. The First Department has held that in stating a cause of action for breach of fiduciary duty, a "plaintiff must establish that the alleged . . . misconduct w[as] the direct and proximate cause of the losses claimed" (*Laub v Faessel*, 297 AD2d 28, 30-31 [1st Dept 2002], citing *R.M. Newell Co. v Rice*, 236 AD2d 843 [4th Dept 1997], *lv denied* 90 NY2d 807 [other citations omitted]; *see also RNK Capital LLC v Natsource LLC*, 76 AD3d 840, 842 [1st Dept 2010] [dismissing claim for lost profits arising out of alleged breach of fiduciary duty where "plaintiffs' ability to realize profits from the allegedly usurped investment opportunity was contingent on certain conduct by third parties and authorization from a government-sanctioned oversight entity, both of which were highly uncertain and well beyond the scope of defendants' influence or control"]). Here, the alleged damages are too attenuated for the claim to stand. In order to prove damages, plaintiffs would have to demonstrate that the high-yield alternative would have been approved, and further that it would have resulted in the avoidance of a Chapter 11 bankruptcy filing. Plaintiffs cannot prove either.

2. Negligence

As to the Fifth Cause of Action for negligence against Gawrylewski and LM, defendants argue that the claim must fail for the same reasons that the breach of fiduciary duty claim fails. Under Delaware law, "[a] claim that a corporate manager acted with gross negligence is the same as a claim that she breached her fiduciary duty of care" (*In re Citigroup Inc. Shareholder Derivative Litig.*, 964 A2d 106, 114 n 6 [Del Ch 2009], quoting *Albert v Alex Brown Mgmt. Servs., Inc.*, 2004 WL 2050527, *6 [Del Super Sept. 15, 2004]). "In the duty of care context gross negligence has been defined as 'reckless indifference to or a deliberate disregard of the whole body of stockholders or actions which are without the bounds of reason.'" (*Benihana of Tokyo*, 891 A2d at 192, quoting *Tomczak v Morton Thiokol, Inc.*, 1990 WL 42607, *12 [Del Ch Apr. 5, 1990]). "Because duty of care violations are actionable only if the directors acted with gross negligence, and because in most instances money damages are unavailable to a plaintiff who theoretically could prove a duty of care violation, such violations are rarely found" (*Benihana of Tokyo*, 891 A2d at 192). "The fiduciary duty of due care requires that directors of a Delaware corporation 'use that amount of care which ordinarily careful and prudent men would use in similar circumstances,' and 'consider all material information reasonably available' in making business decisions, and that deficiencies in the directors' process are actionable only if the directors' actions are grossly negligent" (*In re Walt Disney Co. Derivative Litig.*, 907 A2d 693, 749 [Del Ch 2005]).

Because the First Cause of Action cannot withstand scrutiny, the Fifth Cause of Action must fall as well even if plaintiffs properly allege misconduct as they have not adequately alleged damages. Accordingly, this claim must be dismissed.

CONCLUSION

This is a classic case for application of the business judgment rule. While the defendants' business decisions might ultimately have been unwise, under Delaware law, the court may not second-guess the board's decision making where it is essentially uncontested that a majority of the board was disinterested. Accordingly, the complaint must be dismissed in its entirety. It is hereby

ORDERED that defendants' motions to dismiss the complaint are GRANTED and the complaint is dismissed with costs and disbursements to defendants as taxed by the Clerk upon the submission of an appropriate bill of costs; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

This constitutes the decision and order of the court.

DATED: June 27, 2013

ENTER,

O.P. Sherwood

O. PETER SHERWOOD
J.S.C.