

SUPREME COURT - STATE OF NEW YORK
IAS TERM PART 16 NASSAU COUNTY

PRESENT:

HONORABLE LEONARD B. AUSTIN

Justice

**Motion R/D: 6-23-06
Submission Date: 7-12-06
Motion Sequence No.: 003,004/MOT D**

X
**WILLOUGHBY REHABILITATION AND
HEALTH CARE CENTER, LLC,
WOODMERE REHABILITATION AND
HEALTH CARE CENTER, INC.,
GOLDEN GATE REHABILITATION AND
HEALTH CARE CENTER, LLC,
EASTCHESTER-REHABILITATION AND
HEALTH CARE CENTER, LLC,
NASSAU OPERATING CO., LLC, PARK
AVENUE OPERATING CO., LLC,
TOWNHOUSE OPERATING CO., LLC,
THROGS NECK OPERATING CO., LLC,
NEW FRANKLIN REHABILITATION
AND HEALTH CARE FACILITY, LLC
and FORT TRYON REHABILITATION
AND HEALTH CARE FACILITY, LLC,**

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Plaintiffs,

- against -

HELEN WEBSTER,

Defendant.

X

ORDER

The following papers were read on Defendant's motion for the appointment of a temporary receiver for the Plaintiffs and on Defendant's motion for summary judgment dismissing the amended complaint:

Motion Sequence No. 3

Notice of Motion dated May 5, 2006;
Affirmation of Matthew Dollinger, Esq. dated May 5, 2006;
Affirmation of Helen Webster dated May 4, 2006;

Motion Sequence No. 4

Notice of Motion dated May 5, 2006;
Affirmation of Matthew Dollinger, Esq. dated May 5, 2006;
Affirmation of Helen Webster dated May 4, 2006;

Other Papers

Affirmation of Benjamin Landa dated June 23, 2006;
Affirmation of Matthew Dollinger, Esq. dated July 11, 2006;
Affirmation of Helen Webster dated July 10, 2006;
Affirmation of Helen Webster dated July 10, 2006;
Affirmation of Matthew Dollinger, Esq. dated July 11, 2006;
Affirmation of Ester Hellman dated July 10, 2006;
Plaintiff's Memorandum of Law in Opposition to motion for the Appointment of Receiver dated June 23, 2006;
Plaintiff's Memorandum of Law in Opposition to motion for Summary Judgment dated June 23, 2006.

Motion sequence Nos. 3 and 4 are consolidated for determination.

In Motion Sequence No. 3, Defendant moves pursuant to CPLR 6401 for the appointment of a temporary receiver for Plaintiffs Willoughby Rehabilitation and Health Care Center, LLC; Woodmere Rehabilitation and Health Care Center, Inc., Golden Gate Rehabilitation and Health Care Center, LLC; Eastchester Rehabilitation and Health Care Center, LLC; New Franklin Rehabilitation Health Care Facility, LLC; and Fort Tryon

Rehabilitation and Health Care Facility, LLC to supervise, oversee, manage and administer the fiscal operations of said entities and other ancillary relief requiring those entities to account to her for distributions made in 2004, 2005, 2006 and to pay over to her claimed share of said distributions.

In Motion sequence No. 4, Defendant moves for summary judgment dismissing the amended complaint pursuant to CPLR 3212 and for judgment in her favor on each of the counterclaims asserted in her answer.

BACKGROUND

This is an action in which each of the Plaintiffs, all of which are limited liability companies except Woodmere Rehabilitation and Health Care Center, Inc. (“Woodmere”). Each Defendant is in the business of operating skilled nursing home facilities in the New York metropolitan area.

In their complaint, Plaintiffs seek damages as well as specific performance predicated on Defendant’s alleged breach of the operating agreements of the limited liability companies and of various fiduciary duties arising from her course of conduct with regard to them; Defendant’s refusal to execute documents needed to complete refinancings of loans and purchase of facilities; and Defendant’s refusal to pay her share of capital calls, all of which purportedly jeopardized the financial condition, assets or fiscal soundness of the entities or their operators.

Defendant admits to being a minority member – – or, in the case of Woodmere, a minority shareholder – – of each of the Plaintiff entities except Nassau Operating Co.,

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LLC (“Nassau”), Park Avenue Operating Co., LLC, (“Park Avenue”), Townhouse Operating Co., LLC (“Townhouse”) and Throgs Neck Operating Co., LLC (“Throgs Neck”), in which, she avers that she never acquired any interest and owes no contractual or other duty. Moreover, Defendant maintains that she was never a manager of any of the Plaintiff entities except Willoughby Rehabilitation and Health Care Center, LLC (“Willoughby”), where she was a co-managing member and Woodmere in which she serves as a director and Assistant Secretary.

The amended complaint originally contained twenty-three causes of action sounding in breach of contract, breach of fiduciary duty and specific performance. The fourth cause of action seeks a judicial declaration that Defendant is neither a managing member nor authorized to act on behalf of Willoughby. The remaining breach of contract and breach of fiduciary claims asserted by the Plaintiff entities are predicated on various purported acts of misconduct by Defendant including:

- her refusal to execute a reaffirmation and acknowledgment of her personal guarantee required by Fleet National Bank in connection with Willoughby’s conversion of a revolving line of credit to a fixed term loan;
- her illicit role in the falsification of patient review instruments and evaluations submitted to the New York Department of Health;
- her refusal to execute a previous participation certificate in connection with the application by Eastchester Rehabilitation and Health Care Center (“Eastchester”) for a HUD mortgage; and

- her refusal to pay her proportionate share of the capital calls made on all members of New Franklin Rehabilitation and Health Care Facility, LLC (“New Franklin”) and Fort Tryon Rehabilitation and Health Care Facility, LLC (“Fort Tryon”), the proceeds of which were to be used to credit lines to Amalgamated Bank.

Plaintiffs acknowledge that Defendant executed the previous participation certificate required as part of Golden Gate Rehabilitation and Health Care Center’s (“Golden Gate”) application for a mortgage from the United States Department of Housing and Urban Development (HUD) and have withdrawn the sixth, seventh and eighth causes of action of the amended complaint.

In her answer, Defendant asserts fifteen counterclaims predicated on the failure of the Plaintiff entities, except for Nassau, Park Avenue, Townhouse and Throgs Neck, to pay to her proportionate share of distributions which she asserts have wrongfully been withheld.

Given Defendant’s representation that she never acquired any interest in Nassau, Park Avenue, Townhouse or Throgs Neck, her attorney’s statement that she had no membership interest in same and Plaintiffs’ willingness to withdraw the respective claims of those entities upon Defendant’s conclusive and unequivocal written acknowledgment that “she is not and does not and will not seek to be a member of Nassau, Park Avenue, Townhouse or Throgs Neck,” the Court will not address the claims asserted in the eleventh through twenty-second causes of action for breach of contract, breach of fiduciary duty and specific performance deeming said causes of

action to have been withdrawn based on Defendant's admission before this Court.

Defendant seeks summary judgment dismissing the various remaining claims asserted against her by the Plaintiff entities based on various legal theories including, *inter alia*, the argument that two of the Plaintiff entities, Willoughby and Golden Gate (whose claims have been withdrawn) rely on articles of organization and operating agreements that were never approved but, rather, were questioned by the New York State Department of Health ("Department of Health") which must approve the membership, organization and operating documents of a potential nursing home operator.

DISCUSSION

A. Standing Under Limited Liability Company Law § 206

The admitted procedural defect arising out of Willoughby's failure to publish a copy of its articles of organization and otherwise comply with § 206 of the Limited Liability Company Law does not preclude Willoughby from bringing its claims against Defendant. A failure to comply with the requirements of § 206 does not constitute a jurisdictional defect warranting dismissal. Echelon Photography, LLC v. Dara Partners, L.P., 11 Misc.3d 1064(A), (Civ. Ct. NY Co. 2006); and Acquisition America VI, LLC v. Lamadore, 5 Misc. 3d 461, 463 (Civ. Ct. N.Y. Co. 2004).

The standing argument raised by Defendant is, therefore, lacking in merit. Willoughby has availed itself of the opportunity to cure afforded by the statute and

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represents that publication was complete five days after the submission date of this motion.

In the absence of a contrary legislative intent, the Court views the – albeit belated – publication of Willoughby’s notice to satisfy Limited Liability Company Law § 206 which, in relevant part, provides:

Failure to cause such notice to be published and to file such proof within one hundred twenty days of the effective date of the articles shall prohibit the limited liability company from maintaining any action or special proceeding in this state unless and until such limited liability company causes such notice to be published and files such proof of publication.

Similar “unless and until” language can be found in Business Corporation Law § 1312 (a) which similarly bars an unauthorized foreign corporation from maintaining an action in New York unless and until it has been authorized to do so. Since the failure to be authorized to do business in New York is not a jurisdictional defect, subsequent compliance with the statute warrants *nunc pro tunc* application averting dismissal of the action. See, Manhattan Fuel Co., Inc. v. New England Petroleum Corp., 422 F.Supp. 797, 801 (SDNY 1976), *aff’d.*, 578 F.2d 1368 (2nd Cir. 1978). See also, Barklee Realty Co. v. Pataki, 309 A.D. 2d 310 (1st Dept. 2003).

Likewise, when a corporation loses its authority to do business in New York by virtue of its dissolution by proclamation for failure to pay its franchise taxes pursuant to Tax Law § 203-a, the payment of taxes and penalties restores it to *de jure* status *nunc pro tunc*. See, Propp v. Chaya Amusement Corp., 155 A.D. 2d 251 (1st Dept. 1989).

Thus, upon Willoughby's compliance with Limited Liability Company Law § 206, it has standing to prosecute this action

B. Fiduciary Duty¹

A limited liability company is hybrid business entity having attributes of both a corporation and a partnership. Its owners are its members. Limited Liability Company Law § 417(a) provides that the members of an LLC "shall adopt a written operating agreement relating to the business of the company, the conduct of its affairs and the rights and powers of its members." The operating agreement is, therefore, the primary document defining the rights of members, the duties of managers and the financial arrangements of the limited liability company. Rich, *Practice Commentaries*, 32A Limited Liability Company Law Section 1.A, p. 4, (McKinney's, 2006); and Lio v. Mingyi Zhong, 10 Misc.3d 1068(A) (Sup. Ct., N.Y. Co. 2006).

Pursuant to Limited Liability Company Law § 409, "a manager shall perform his or her duties as a manager * * * in good faith and with a degree of care that an ordinary prudent person in a like position would use under similar circumstances." The acts of working in concert and managing a limited liability company clearly gives rise to a relationship among the members which is analogous to that of partners who, as fiduciaries of one another, owe a duty of undivided loyalty to the partnership's interests. Birnbaum v. Birnbaum, 73 N.Y. 2d 461, 466, *rearg. den.*, 74 N.Y. 2d 843 (1989). See

¹The analysis with regard to Defendant's fiduciary duty to Willoughby, as discussed herein, is no different than her duty to each of the limited liability companies in which she is a member.

also, Meinhard v. Salmon, 249 N.Y. 458, 463-4 (1928).

A partner, and by analogy, a member of a limited liability company, has a fiduciary obligation to others in the partnership or limited liability company which bars not only blatant self-dealing, but also requires avoidance of situations in which the fiduciary's personal interest might possibly conflict with the interests of those to whom the fiduciary owes a duty of loyalty. Salm v Feldstein, 20 A.D. 3d 469, 470 (2nd Dept. 2005); and Nathanson v Nathanson, 20 A.D. 3d 403, 404 (2nd Dept. 2005).

Although Defendant maintains that the mere membership in a limited liability company does not impose a fiduciary duty on its members, she offers no authority to support this proposition. It is not mandatory that a fiduciary relationship be formalized in writing. Any inquiry into whether such obligation exists among the parties to a business arrangement is "necessarily fact specific to a particular case." Weiner v Lazard Freres & Co., 241 A.D. 2d 114, 122 (1st Dept. 1998).

Review of the Willoughby operating agreement establishes that the fiduciary duty concept is encompassed within the very language of § 5.5 which provides, in pertinent part:

"[t]he Managing Members will perform their duties as Managing Members in good faith, in a manner it reasonably believes to be in the best interests of the Company. * * * The Managing Members will not be liable to the Company or any Member for any loss or damage sustained by the Company

or Member, unless the loss or damage will have been the result of fraud, deceit, gross negligence, willful misconduct,

breach of fiduciary duty or a wrongful taking by the
Managing Members.”

Notwithstanding her status as a minority, managing member of Willoughby, Defendant contends that the first, second and third causes of action of the amended complaint (breach of contract, breach of fiduciary duty and specific performance) must fail, as a matter of law, because nothing in the Willoughby operating agreement required that she execute any document in connection with converting a revolving line of credit to a fixed term loan. The record suggests a contrary view. While Willoughby’s counsel disagreed with Fleet Bank’s attorney as to whether or not the original guarantees continued to cover the amendment to the loan, the bank requested that the members reaffirm their original guarantees. Given such request, and the language of § 5.3.2 of the Willoughby operating agreement, which states:

“[t]he Managing Members will obtain Requisite Consent before taking any of the following actions: Borrowing money secured by a mortgage or other encumbrance on the Company Property in which case no member may unreasonably withhold his consent to such Borrowing by the Company,”

the question of whether Defendant’s failure to execute the reaffirmation agreement constitutes a breach of fiduciary duty, as well as a breach of her obligations as a managing member of Willoughby to not “unreasonably withhold consent” *vis-a-vis* borrowing, are factual issues which cannot be summarily decided.

C. Summary Judgment

The proponent of a motion for summary judgment 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 N.Y. 2d 1062 (1993); Anwar v. Hellman Mgt., 14 A.D. 3d 470 (2nd Dept. 2005); and Widmaier v. Master Products Mfg., 9 A.D. 3d 362 (2nd Dept. 2004). In considering such a motion, the court must view the evidence in the light most favorable to the non-moving party and must afford the party every favorable inference that can be drawn from the evidence. Schuhmann v McBride, 23 A.D. 3d 542, 543 (2nd Dept. 2005); and Louniakov v. M.R.O.D. Realty Corp., 282 A.D. 2d 657 (2nd Dept. 2001). Failure to make the required showing mandates denial of the motion regardless of the sufficiency of the opposing papers. JMD Holding Corp. v. Congress Financial Corp., 4 N.Y. 3d 373, 384 (2005); and Casa Bosco, Inc. v. 118-01 Metropolitan Ave. Realty Corp., 28 A.D. 3d 698, 699 (2nd Dept. 2006). Here, Defendant's conclusory assertions in support of summary judgment fail to establish the absence of any triable issues of fact.

In the absence of ambiguity which obscures the intention of the parties to a contract, the interpretation of that contract and the obligations of the parties thereto are questions of law; not fact. R/S Assoc. v. New York Job Dev. Auth., 98 N.Y. 2d 29, 32, *rearg. den.*, 98 N.Y. 2d 693 (2002). Where parties memorialize their agreement in a clear, complete document, their writing should, as a rule, be enforced according to its terms. W.W.W. Assoc. v. Giancontieri, 77 N.Y. 2d 157, 162 (1990). See also, Greenfield v. Philles Records Inc., 98 N.Y. 2d 562 (2002). The court will give a

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practical interpretation to the language employed and the parties' reasonable expectations. AFBT-II, LLC v Country Village of Mooney Pond, Inc., 305 A.D. 2d 340, 342 (2nd Dept. 2003).

Within every contract is an implied covenant of good faith and fair dealing. Dalton v. Educational Testing Service, 87 N.Y. 2d 384 (1995); 1-10 Industry Assocs. LLC v. Trim Corporation of America, 297 A.D. 2d 630 (2nd Dept. 2002); and Aventine Inv. Management Inc. v. Canadian Imperial Bank of Commerce, 265 A.D. 2d 513, 513-514 (2nd Dept. 1999). The covenant is breached when a party to a contract acts in a manner, though not expressly forbidden by any contractual provision, would deprive the other party of the right to receive the benefits under their agreement. Jaffe v. Paramount Communications Inc., 222 A.D. 2d 17, 22-23 (1st Dept. 1996).

Notwithstanding Defendant's argument to the contrary, conversion of Willoughby's line of credit to a fixed term loan comes within the ambit of "borrowing by the company" and the "reasonableness" of her refusal to perform the tasks purportedly necessary to effect such borrowing is clearly at issue.

Similarly, a factual issue exists with respect to whether Defendant breached her duty of care as a managing member of Willoughby predicated on her alleged involvement in the falsification of patient review instruments ("PRIs") prepared by the assessor she retained to evaluate and score the level of care and assistance required by each of Willoughby's patients in light of their daily activities, medical condition and required care. According to Plaintiffs, a review by an outside, independent consultant of

selected samples of the PRIs prepared by the assessor hired by Defendant revealed that the patient scores were artificially inflated and the documentation to back up those scores was either lacking or falsified. Willoughby alleges that, had the erroneous assessments been submitted to the Department of Health, it would have failed its next audit and could have been exposed to civil and criminal charges. Moreover, as a consequence of the faulty PRI's, Willoughby asserts it incurred the expense of retaining an expert to investigate, review and correct the work performed by the assessor hired by Defendant. Whether, and the extent to which, PRI's were erroneously prepared and Defendant's part, if any, in said misconduct is for the trier of fact to decide.

With respect to the fourth cause of action, the question of whether Defendant has been removed as a co-managing member of Willoughby in accordance with the requirements of the Willoughby operating agreement and whether she is entitled to damages for unpaid salary as set forth in her third, fourth and fifth counterclaims, are disputed issues which will be resolved at trial.

According to the amended complaint, Defendant is a director and assistant secretary of Woodmere which has requested mortgage financing from Fleet National Bank in order to close on the purchase of a piece of property adjacent to the Woodmere facility on which it intends to construct an addition. Woodmere, and its nominee, 1040 Central Avenue Realty, LLC, have allegedly been forced to extend the closing date, at a cost of \$100,000, and are at risk of forfeiting the contract deposit because of Defendant's failure to provide necessary documentation and otherwise cooperate with

the effort to insure that the various Plaintiff entities, of which she is a member, are able to meet their financial obligations to Fleet Bank. According to Plaintiffs, Defendant's conduct is especially egregious because Fleet Bank has conditioned mortgage financing the subject purchase on all of the Plaintiff entities' being brought current in their financial obligations to Fleet as required by the cross-default provisions contained in their various loan documents.

Defendant's status as an officer and director of Woodmere imposes on her a fiduciary duty to the corporation to act in its best interest and not deprive it of any corporate opportunity. Blank v. Blank, 256 A.D. 2d 688, 694-5 (3rd Dept. 1998); and Howard v. Carr, 222 A.D. 2d 843, 845 (3rd Dept. 1995). Defendant has proffered no basis to summarily dismiss the breach of fiduciary claim asserted in the fifth cause of action.

Although Defendant contends that the Eastchester operating agreement does not expressly obligate her or any other member to execute a HUD previous participation agreement in connection with Eastchester's application to refinance an existing mortgage with North Fork Bank in order to obtain more advantageous terms, a factual issue exists as to whether her refusal to do so constitutes a breach of fiduciary duty owed by a member of a limited liability company to the company and other members. As such, the ninth and tenth causes of action for breach of fiduciary duty and specific performance cannot be summarily dismissed.

In the twenty-third through twenty-sixth causes of action, New Franklin and Fort

Tryon each assert claims for breach of contract and breach of fiduciary duty predicated on Defendant's refusal to pay her proportionate share of capital calls made on all members of those companies in June, 2004. The proceeds were used to retire credit lines with Amalgamated Bank, in order to avoid a possible violation of the companies' financial covenants under their respective mortgages with North Fork Bank. Without denying that she did not meet these capital calls, Defendant argues that she was under no obligation to do so because the causes of action are based on amended operating agreements dated May 12, 2003, which were never approved by the Department of Health and are, therefore, ineffective and unenforceable. This Court disagrees.

A comparison of § 8.2 of the New Franklin and Fort Tryon amended operating agreements and § 8.2 of the original operating agreements establishes that they are identical in relevant part. They each read as follows:

Amended Operating Agreements	Original Operating Agreements
"Following the Closing, additional capital contributions, if any, will be made only in cash, only in proportion to the relative Economic Interest of all Members required to make capital contributions and upon Requisite Consent, which consent may not be unreasonably withheld by any member."	"Additional Capital Contributions, if any, except as provided for in Section 8.2.1 will be made only in cash, only in proportion to the relative Economic Interests of all Members required to make capital contributions and upon Requisite Consent, which consent may not be unreasonably withheld by any Member."

Here, the claimed lack of approval of the amended operating agreements, the necessity of which Plaintiffs refute, does not serve to relieve Defendant of her obligation with regard to capital calls of New Republic and Fort Tryon under the original operating

agreements nor does it require summary dismissal of the twenty-third through twenty-sixth causes of action. To the extent necessary, Plaintiffs are granted leave to amend said claims to reference both of the original operating agreements as well as amended operating agreements.

It appears, as Plaintiffs maintain, that pursuant to Public Health Law § 2801-a(4)(b), Department of Health approval was not required where, as here, the proposed change in membership did not involve the transfer of a ten percent or more interest in the limited liability companies to any one person. Moreover, the remedies allowed in Article VIII (§ 8.3) of both the New Republic and Fort Tryon amended operating agreements upon the failure of a member to make an additional capital contribution are not exclusive and are without prejudice “to any other right or remedy of the Company.” The original operating agreements fail to state that the loan mechanism provided for in § 8.2.1 is the sole remedy available to non-defaulting members of the company.

Under the circumstances, the question of whether Defendant’s refusal to fund her share of the companies’ additional capital needs constitutes a breach of the operating agreements and her fiduciary duty thereunder are for the trier of fact to resolve.

D. Temporary Receiver

CPLR 6401(a) permits the court to appoint a temporary receiver to preserve specific identifiable property during the pendency of an action where there is a danger that the property will be removed from the state, lost, materially injured or destroyed. Such an extreme remedy may only be invoked in cases where the moving party has

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made a clear evidentiary showing of the necessity of the conservation of property and protection of the interests of that party. Lee v. 183 Port Richmond Ave. Realty, Inc., 303 A.D. 2d 379, 380 (2nd Dept. 2003); and Modern Collection Assoc., Inc. v. Capital Group, Inc., 140 A.D. 2d 594 (2nd Dept. 1988). Defendant offers nothing to suggest, much less demonstrate, any danger of irreparable loss, that Plaintiffs are on the verge of insolvency and might well dissipate monies owed her or that the well being or continued vitality of the Plaintiff entities is, in any way, threatened.

While generally a temporary receiver will not be appointed if the relief sought is money damages (Brody v. Mills, 278 App. Div. 771 [2nd Dept. 1951]), a temporary receiver may be appointed, if the subject of the action is a specific fund of money and there is a showing that the fund [or property] is in danger of being materially injured or destroyed. Meurer v. Meurer, 21 A.D. 2d 778 (1st Dept. 1964). Such is not the case here. Nor is it appropriate to seek the appointment of a temporary receiver whose stated purpose is affording the moving party the ultimate relief sought in the action. See, SHS Baisley LLC v. Res Land, Inc., 18 A.D. 3d 727 (2nd Dept. 2005). Here, the temporary receiver Defendant seeks would among other things, have the power to pay disputed distributions to her. Given the competing claims of the parties, it would be highly inappropriate to compel a result on this motion which may not be available to Defendant on the trial of this matter and which is contrary to the limited statutory purpose of a temporary receiver.

If future accounting reveals that the Plaintiff entities owe Defendant any damages, after a determination on the merits of her counterclaims, and applying set offs, should Plaintiffs prevail on any of the claims in chief, there is no indication that Plaintiff entities would not be able to satisfy a judgment in Defendant's favor.

Accordingly, it is,

ORDERED, that Defendant's motion for summary judgment dismissing the amended complaint is **denied**; and it is further,

ORDERED, that the sixth, seventh, eighth and eleventh through twenty-second causes of action having been withdrawn by Plaintiffs, the action shall continue as to the first through fifth, ninth, tenth and twenty-third through twenty-sixth causes of action; and it is further,

ORDERED, that Defendant's motion for appointment of a temporary receiver is **denied**.

This constitutes the decision and Order of the Court.

Dated: Mineola, NY
October 26, 2006

Hon. LEONARD B. AUSTIN, J.S.C.