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COURT OF APPEALS

STATE OF NEW YORK

FUNDAMENTAL LONG TERM CARE
HOLDINGS, LLC, et al.,

Appellants,

-against-

No. 22

CAMMEBY'S FUNDING LLC, et al.,

Respondents.

20 Eagle Street
Albany, New York 12207
January 10, 2013

Before:

CHIEF JUDGE JONATHAN LIPPMAN
ASSOCIATE JUDGE VICTORIA A. GRAFFEO
ASSOCIATE JUDGE SUSAN PHILLIPS READ
ASSOCIATE JUDGE ROBERT S. SMITH
ASSOCIATE JUDGE EUGENE F. PIGOTT, JR.

Appearances:

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Official Court Transcriber

1 CHIEF JUDGE LIPPMAN: We're going to start
2 with number 22, Fundamental Long Care (sic) Holdings.

3 Counselor, would you like any rebuttal
4 time?

5 MR. REITER: Four minutes, please, Your
6 Honor.

7 CHIEF JUDGE LIPPMAN: Four minutes, sure.
8 Go ahead.

9 MR. REITER: May it please the court, my
10 name is Allen Reiter, and along with my colleagues
11 Jennifer Bougher and Asari Aniagolu, we represent the
12 appellants in this case.

13 The legal issue presented on this appeal is
14 whether when two unambiguous and consistent
15 agreements establish the entirety of the rights and
16 the obligations of the parties to a transaction, all
17 of the terms of both agreements must be considered in
18 determining those rights and obligations.

19 JUDGE READ: Does the parol evidence rule
20 have anything to with this case, then, in your view?

21 MR. REITER: The parol evidence rule has
22 nothing to do with this case.

23 JUDGE READ: You agree with your adversary
24 about that?

25 MR. REITER: We absolutely agree with that.

1 JUDGE READ: Okay.

2 MR. REITER: In their brief, they said the
3 two agreements are consistent.

4 CHIEF JUDGE LIPPMAN: What are you doing
5 with the merger agreement? What's with that?

6 MR. REITER: The merger agreement - - -

7 CHIEF JUDGE LIPPMAN: How do you get around
8 that?

9 MR. REITER: The merger agreement would
10 apply only if the option that is at issue here
11 covered the grounds that are covered by the operating
12 agreement. But there is a clear demarcation between
13 what the option provides and what the operating
14 agreement provides. The option, in a sense, brings
15 you up and across the threshold. It gives you the
16 right, once Mr. Schron exercised it, to become a
17 member of Fundamental.

18 Once he crosses that threshold and becomes
19 a member, the operating agreement applies and all of
20 its terms apply to him.

21 JUDGE GRAFFEO: Is there any cross-
22 reference? Can you point to any language in the
23 agreement that would indicate these two are to be
24 considered jointly?

25 MR. REITER: They - - - Your Honor, they

1 apply together because of the terms that are in both
2 of them, where the same language is used.

3 CHIEF JUDGE LIPPMAN: But doesn't the plain
4 language of the option agreement, including the
5 merger clause, make clear that any prior agreements
6 don't matter and are of no value?

7 MR. REITER: It would, except for the key
8 terms in paragraph 6 or section 6 of the option,
9 which link directly to paragraph 3.3 of the operating
10 agreement. Section 6 of the option makes it clear
11 that after the exercise of the option, units are
12 issued to Mr. Schron. Read completely by itself,
13 that term has no special meaning. But it does have a
14 special meaning when you have to consider the
15 operating agreement which applies to Mr. Schron - - -

16 JUDGE SMITH: Why do you - - -

17 MR. REITER: - - - as a matter of law.

18 JUDGE SMITH: - - - have to consider the
19 operating agreement at all? Mr. Schron's not a party
20 to it.

21 MR. REITER: He's not a party to it until
22 he exercises the option. In the analogy I tried to
23 draw earlier, Your Honor, the option - - - exercising
24 the option brings Mr. Schron into the house. Once
25 he's into the house, he's now a member of

1 Fundamental. Once he's a member of Fundamental, the
2 operating agreement applies to him. And there's a
3 link - - -

4 JUDGE GRAFFEO: It would have been pretty
5 easy to say that, wouldn't it? To have put that in
6 option?

7 MR. REITER: It would have been surplusage,
8 because it's already provided by the linkage between
9 paragraph 6 of the option and paragraph 3.3 of the
10 operating agreement. By the same token - - -

11 JUDGE GRAFFEO: What party - - - did the
12 same party draft both of these agreements?

13 MR. REITER: It is not - - - there's no
14 evidence in the record with respect to who the
15 drafters were of the option. But the operating
16 agreement applies to Mr. Schron as a matter of law,
17 under New York or Delaware law, regardless of whether
18 he signed it. But it only applies once he became a
19 member.

20 Reading the option by itself might lead you
21 to the conclusion that - - -

22 JUDGE SMITH: But only - - - it only
23 applies once he became a member, then how can his - -
24 - but the option agreement gives him the right to
25 become a member, how can he - - - how can he have to

1 pay market value before becoming a member?

2 MR. REITER: At the - - - well, at the time
3 he purported to exercise the option, Mr. Schron
4 informed Fundamental that he was not going to pay
5 anything beyond 1,000 dollars. Had he simply said
6 I'll comply with the operating agreement, there would
7 have been a closing. He would have become a member
8 and then at that closing, after the necessary
9 regulatory - - -

10 JUDGE SMITH: Well, he doesn't become a
11 member until he owns the units.

12 MR. REITER: That is correct. And upon - -
13 -

14 JUDGE SMITH: And the option agreement says
15 he gets the units for 1,000 bucks.

16 MR. REITER: It doesn't say that. The
17 1,000 dollars that is set forth in the option
18 agreement is the price for exercising the option.
19 Because Fundamental is a privately held company - - -

20 JUDGE READ: Well, what's the ten dollars
21 for, then?

22 MR. REITER: The ten dollars is for him to
23 have the option at all. He's not obligated to
24 exercise it. But if he chooses to exercise it, it
25 costs him 1,000 dollars. There's a real value there,

1 because as a privately held - - -

2 JUDGE SMITH: And what - - -

3 MR. REITER: - - - company - - -

4 JUDGE SMITH: The option itself costs ten
5 dollars. The exercise costs 1,000. What costs
6 market value?

7 MR. REITER: The market value applies once
8 he exercises the option, pursuant to paragraph 3.3 of
9 the operating agreement. Because of the linkage - -
10 - because of the same language that appears - - -

11 JUDGE SMITH: You're saying he exercises
12 the option but does not thereby acquire the units?
13 It's an option to acquire units.

14 MR. REITER: Once he exercises the option,
15 the operating agreement reflects, and the option
16 reflects, that units of interest are to be issued to
17 him. Those are terms of art, because paragraph 3.3
18 of the operating agreement says upon the issuance of
19 new units, whether to an existing member or to a new
20 member, the person who is the recipient of those
21 units must pay fair market value, as determined in
22 accordance with GAAP, as provided for.

23 JUDGE SMITH: Your clients could have
24 amended the operating agreement, if they wanted to,
25 right?

1 MR. REITER: They could have. But they
2 didn't.

3 JUDGE SMITH: And the option agreement
4 could have provided that the - - - that Forman and
5 Grunstein shall make such amendments to the operating
6 agreement as are necessary to permit this option to
7 take effect.

8 MR. REITER: The option agreement could
9 also have - - -

10 JUDGE SMITH: It almost says that, doesn't
11 it?

12 MR. REITER: Well, the op - - - well,
13 actually, it doesn't say "to take effect", and that's
14 critical. Because all it talks about is that they're
15 obligated to amend the operating agreement to reflect
16 the issuance of the units. And as I mentioned
17 earlier, "issuance" is the key term here, because
18 it's the issuance that triggers the capital
19 contribution requirements in paragraph 3.3.

20 By the same token, the option could have
21 stated, regardless of the provisions of paragraph
22 3.3, Mr. Schron's price for purchasing these shares
23 is 1,000 dollars. It doesn't say that.

24 JUDGE PIGOTT: Could you have changed it,
25 then - - - following up on what Judge Smith asked

1 you, if you can change the operating agreement, could
2 you then change it in anticipation of the exercise of
3 the option, either in favor of or against the
4 proposed option owner? In other words, if you think
5 - - - if you want - - - if you want the person who
6 owns the option to come in, you can say, well, why
7 don't we amend the operating agreement to make it
8 easy for that person to come in? If you don't want
9 them, you can say why don't we amend the operating
10 agreement to make it impossible for them to come in.
11 And the only people that can control that would be
12 you, because they're not a party to the operating
13 agreement until they exercise the option.

14 MR. REITER: The owners of Fundamental
15 could have amended the operating agreement to say,
16 with respect to the option agreement given to Mr.
17 Schron, he only has to pay 1,000 dollars.

18 JUDGE SMITH: Could there have been - - - I
19 think Judge Pigott's question is, could they also
20 have amended it to say that you have to pay twice
21 market value?

22 MR. REITER: I was about to turn to that.
23 I - - - although that issue is not before this court,
24 because it never happened. I think it would raise a
25 serious question with respect to paragraph 5 of the

1 option agreement, which provides that the owners of
2 Fundamental shall not enter into any agreement that
3 would impair the rights granted by the option - - -

4 JUDGE SMITH: It doesn't say "the owners",
5 it says "the issuer", right?

6 MR. REITER: Well, the issuer. In effect,
7 Fundamental, under the guidance of its owners, had
8 they done what Judge Pigott is suggesting, might have
9 fallen astray of paragraph 5. But that issue is not
10 before us. It never happened.

11 What we have before us are two unambiguous
12 agreements. It's conceded by respondents that these
13 agreements are consistent, that there is no
14 inconsistency between them, that the parol evidence
15 rule doesn't apply.

16 JUDGE GRAFFEO: You've used the term
17 "issuance" several times. What is - - - in your
18 mind, what does it mean to be a member?

19 MR. REITER: I believe that that's a
20 weakness in the way the agreement is written. But a
21 member without units doesn't have any meaning at all.
22 Had Mr. Schron - - -

23 JUDGE GRAFFEO: Because section 4 says,
24 "Upon the exercise of the option, the option holder
25 or its designee shall be admitted as a member." So

1 that's a meaningless paragraph?

2 MR. REITER: Well, I don't think, at the
3 time that was drafted, the expectation was that a
4 person would, at the time the option was exercised,
5 at the same time, state that the option holder would
6 refuse to comply with the operating agreement.
7 That's not a - - - there wasn't an expectation - - -
8 I think we can draw that conclusion - - - that that
9 would happen.

10 And so it created - - - it created an issue
11 that was resolved by Mr. Schron's refusal. Because
12 once he refused, right up front - - -

13 JUDGE GRAFFEO: I don't know if I follow
14 yet what "member" means.

15 MR. REITER: Well, a member, ordinarily,
16 would be entitled to shares and would be entitled to
17 share in all the benefits, but also have all the
18 obligations of membership. The agreement
19 contemplated that Mr. Schron would exercise the
20 option. There would be regulatory approvals
21 required. And then there would be a closing.

22 JUDGE GRAFFEO: So if he paid the 1,000
23 dollars, he'd become a member?

24 MR. REITER: Had he simply paid the 1,000
25 dollars, and not said anything else - - - there's

1 actually a second issue out there, because there are,
2 as the agreement provides, required regulatory
3 approvals that must be obtained before he can become
4 a member. And those are inconsistent with respect to
5 his instantly becoming a member, because under
6 certain circumstances, becoming a member
7 instantaneously might have led to a violation of the
8 many rules and regulations that govern healthcare
9 facilities.

10 And Fundamental's operating companies
11 operate in many different states, and there are many
12 - - - there's a whole rubric of rules that differ
13 from state to state and change from time to time.

14 JUDGE PIGOTT: Under your - - - I
15 apologize. Under your analysis, if the option had
16 been exercised the day it was granted, what is the
17 dollar amount that we'd be talking about?

18 MR. REITER: I don't know what the dollar
19 amount would be. Article - - - paragraph 3.3 calls
20 for GAAP evaluation of what that would be.

21 JUDGE PIGOTT: Right.

22 MR. REITER: And I don't have those
23 numbers, so I can't tell you. And I'm not an
24 accountant, so I'm unable to tell you what that
25 number would have been. And obviously here, the fact

1 that we have an implausible number - - -

2 JUDGE READ: Well, how much did your
3 clients pay for their interest?

4 MR. REITER: They put in fifty dollars
5 each. But then they spent their time working on this
6 company. And the full details of its financial
7 aspect and the condition it was in at the time are
8 really not before this court. What we do have are
9 these two agreements - - -

10 JUDGE SMITH: Did they - - - did they pay
11 money to get the assets?

12 MR. REITER: I believe they undertook debt
13 to get these assets, which ultimately had to pay off,
14 and obviously it was a burden - - -

15 JUDGE SMITH: If I could just ask you a
16 different question. Is discovery still going on
17 below?

18 MR. REITER: Actually, on January 8th, just
19 a couple of days ago, the Appellate Division reversed
20 the grant of discovery, finding that the discovery
21 that had been sought by the respondents and had been
22 ordered by Justice Sherwood, did not apply to any of
23 the pleadings in the case, therefore did not fit the
24 requirements of 3101 of the CPLR.

25 JUDGE SMITH: So are you - - - if there's

1 no - - - if this judgment were affirmed, then you
2 would - - - there'd be nothing left to do except
3 close?

4 MR. REITER: There never was anything left
5 to do except close. If this judgment is affirmed - -
6 -

7 JUDGE SMITH: Then how come you were having
8 discovery until the day before yesterday?

9 MR. REITER: We weren't having discovery
10 until the day before yesterday. The respondents,
11 based upon pure speculation, contended that their
12 counterclaim encompassed claims of potential
13 financial malfeasance. Those claims were never in
14 their counterclaim. We are going - - -

15 JUDGE SMITH: And has the Appellate
16 Division now definitively rejected that?

17 MR. REITER: Absolutely.

18 JUDGE SMITH: So - - -

19 MR. REITER: That issue is gone.

20 JUDGE SMITH: - - - so it's final now. I'm
21 still not quite so sure it was final when we granted
22 leave.

23 MR. REITER: It was final then, because the
24 order below that granted discovery was improvidently
25 granted, as recognized now by the Appellate Division.

1 There was nothing then and there is nothing now in
2 the pleadings - - -

3 CHIEF JUDGE LIPPMAN: Okay, counselor.

4 MR. REITER: - - - to be litigated.

5 CHIEF JUDGE LIPPMAN: Okay, counselor,
6 thanks.

7 MR. REITER: Thank you very much.

8 MR. ENGEL: May it please the court, Steven
9 Engel for the respondents.

10 Let me start with Judge Smith's comment
11 that the option here sets forth in unambiguous terms
12 the price that Cam Funding or its designee must pay
13 in order to acquire the units. My brother says that
14 we concede that the option and the operating
15 agreement are consistent. We believe that they're
16 consistent, as we understand these agreements.

17 If one were to adopt the view of my brother
18 here, of Fundamental and the appellants, they're
19 directly inconsistent. The option says - - -

20 JUDGE SMITH: Suppose they're inconsistent.
21 Why does that matter, because you're only a party to
22 one of them?

23 MR. ENGEL: Well, I think - - - well, I
24 think that is correct. And what is more, is that the
25 parties to the operating agreement have signed a

1 separate obligation. The LLC Act said every LLC must
2 have an operating agreement. The law is very clear,
3 though, that those operating agreements are contracts
4 among the members, and standard principles of
5 contract law apply.

6 And so if the members and the company sign
7 a separate agreement with a third party, such as the
8 Fundamental option, they can vary.

9 CHIEF JUDGE LIPPMAN: Really, what's
10 indicated in the option agreement, if the option
11 agreement - - - if the intent of the option agreement
12 was to bounce over to the term of the operating
13 agreement, if that was the intent expressed, that
14 would be okay, right? The question is whether - - -

15 MR. ENGEL: Yes.

16 CHIEF JUDGE LIPPMAN: - - - whether the
17 party's intention is clear in the option agreement to
18 be bound solely by the option terms.

19 MR. ENGEL: And I agree with you, Your
20 Honor. And what I'd - - -

21 CHIEF JUDGE LIPPMAN: That's your position,
22 right?

23 MR. ENGEL: Sure. I would say that section
24 15 of the option sets forth, in no uncertain terms,
25 that the Fundamental option is the "entire

1 agreement". This is the merger clause. It is the
2 entire agreement governing my client's - - -

3 CHIEF JUDGE LIPPMAN: Could - - - but the
4 option agreement could say on so and so term, you go
5 over to the operating agreement to look at what it
6 says?

7 MR. ENGEL: Sure. It could.

8 CHIEF JUDGE LIPPMAN: It could. You're
9 just saying it didn't?

10 MR. ENGEL: Well, in fact, the only
11 reference to the operating agreement at all in the
12 option is a requirement that Grunstein, Forman, and
13 Fundamental amend their operating agreement to
14 reflect the issuance of the shares. And this is - -
15 - the option could not be clearer that Cam Funding or
16 its designee may come into Fundamental, for 1,000
17 dollars - - - and I can assure you and I think we can
18 all be certain, that these sophisticated parties here
19 would not have given up a third of their company or
20 offered up a third of their company, for 1,000
21 dollars in express consideration, and then hidden the
22 fact that in a separate agreement, Cam Funding has to
23 pay tens and tens of millions of dollars,
24 potentially.

25 JUDGE SMITH: You're saying, if they were

1 really entitled to all that money, they would have
2 mentioned it in the option?

3 MR. ENGEL: I think it is certain that they
4 would have.

5 JUDGE SMITH: But isn't it a little weird
6 to buy a third of a valuable company for 1,000
7 dollars, any way you slice it?

8 MR. ENGEL: Well, I think, at the time, as
9 the court has raised, Grunstein and Forman had put in
10 fifty dollars. They also, as the record is clear - -
11 -

12 JUDGE SMITH: Well, but they assumed debt,
13 which is ten million or something.

14 MR. ENGEL: They didn't assume any personal
15 debt. Fundamental assumed debt which was secured by
16 the assets that Fundamental was acquiring in this
17 transaction. Grunstein and Forman had no more risk
18 than the equity they put in. In fact, as Grunstein
19 and Forman do admit in the record - - -

20 JUDGE SMITH: Well, then what you're
21 telling me is that the assets that they acquired were
22 underwater at the time they acquired them?

23 MR. ENGEL: Well, the lender was - - - and
24 this is - - - this starts to get outside of the
25 record - - - they were able to work out a deal with

1 the lender that the lender had sufficient security
2 with the receivables of the company that they were
3 acquiring, that the lender had - - -

4 CHIEF JUDGE LIPPMAN: So what happened - -
5 -

6 MR. ENGEL: - - - did not require equity.

7 CHIEF JUDGE LIPPMAN: So what happened now?
8 From your view, the arrangement now is commercially
9 undesirable, and so now they want to get you to that
10 provision of the operating agreement?

11 MR. ENGEL: Oh, sure. There's no question.

12 CHIEF JUDGE LIPPMAN: Because - - -

13 MR. ENGEL: Oh - - -

14 CHIEF JUDGE LIPPMAN: - - - while then it
15 might have made sense, today it doesn't. Is that
16 your - - -

17 MR. ENGEL: Well, I - - - sure. Well, then
18 they had no choice. They needed my client's consent
19 to go forward with the deal in this. And while they
20 contest that here, they do concede that at the time
21 my client received the option, he executed the
22 consent on behalf of the landlord to the business
23 transaction that formed Fundamental. They say - - -

24 JUDGE SMITH: Is that in the record?

25 MR. ENGEL: Yes, in the record in Mr.

1 Forman's affidavit, which is - - - I believe it's in
2 the 470s or so. Forman says we didn't need - - - and
3 I can provide the court with the precise cite - - -

4 JUDGE SMITH: Don't worry about it. Go
5 ahead.

6 MR. ENGEL: But - - -

7 JUDGE READ: Before I forget it, let me - -
8 - in your brief you said it was nonfinal. Do you
9 agree, now, that this is a final order?

10 MR. ENGEL: No. I mean - - -

11 JUDGE READ: You still don't think it's a
12 final order?

13 MR. ENGEL: It's still not final. What we
14 have had, since the court granted review, is multiple
15 hearings in front of Justice Sherwood. Justice
16 Sherwood has issued two separate orders after a
17 contested briefing and oral argument. Yes, the First
18 Department did issue a decision vacating Justice
19 Sherwood's order two days ago, although, in fact - -
20 - and the oral argument at the First Department is
21 recorded and available at the court - - - the First
22 Department made clear that the reason they were
23 vacating the discovery order is the liberal rules for
24 amendment. They invited us to amend our cross-claims
25 prior to pursuing the discovery.

1 The summary order doesn't say this, but it
2 is in the - - - it is in the oral argument. Plainly,
3 there's been litigation on these issues since the
4 court granted review. I can assure you that if the
5 court affirms, Fundamental will continue to contest
6 regulatory issues.

7 Justice Sherwood's order, which is in our -
8 - - his multiple orders are in our supplemental
9 appendix - - - sets forth detailed procedures for
10 resolving any disputes. We don't actually believe
11 that there are any regulatory issues, but as we've
12 seen, the appellants will raise argument after
13 argument with respect to this option and with respect
14 to the appeal that you're about to hear right after
15 this one, involving the SVCare option.

16 JUDGE READ: So what should we do?

17 MR. ENGEL: Well, I - - - if - - - our
18 position is the court lacks jurisdiction. And the
19 Appellate Division could have granted leave to appeal
20 to this court, but they did not. And jurisdiction is
21 a threshold issue. So we certainly think that in our
22 view the appropriate course would be to dismiss for
23 lack of jurisdiction. Obviously, if the court feels
24 differently, we believe the Appellate Division's
25 ruling should be affirmed.

1 I would note, in reference to the SVCare
2 option, there is no better argument against the
3 absurdity of the appellant's argument here than the
4 terms of the SVCare option itself.

5 Here, the argument is Schron would pay
6 1,000 dollars - - - it's not the strike price for the
7 option, it's merely the invitation to pay the capital
8 contribution. The SVCare option has the exact same
9 language on this issue, and the SVCare option says
10 that the consideration is 100 million dollars.

11 JUDGE SMITH: Well, actually, it says it's
12 100 million dollars, but it's paid to the issuer for
13 99.999 percent of the stock.

14 MR. ENGEL: That's right.

15 JUDGE SMITH: That's - - - of the million,
16 they're paying 900 - - - they're paying all but 1,000
17 to themselves.

18 MR. ENGEL: It's essentially a capital
19 contribution, I mean, in that amount. I mean,
20 essentially the 100 million is given to the company,
21 which is, similarly, what we have here. The 1,000
22 dollars is paid to the issuer. But there - - -

23 JUDGE SMITH: Basically, they're both
24 1,000-dollar deals, aren't they?

25 MR. ENGEL: Well - - -

1 JUDGE SMITH: 1,000 dollars to - - - you're
2 only really parting with 1,000 bucks in each case.

3 MR. ENGEL: Well, I think if you - - - if
4 you forgive - - - if you're forgiving 100 million
5 dollars that a separate entity has separately loaned,
6 that is a - - -

7 JUDGE SMITH: I know.

8 MR. ENGEL: - - - that is - - - you know,
9 that's a large chunk of change; it's through the
10 assumption of debt, rather than cash. And you also
11 do get the company as such, and therefore might be
12 able to receive some of it back. But it's - - - one
13 has to reach into the pocket and put in the money.

14 But their argument before Justice Sherwood
15 on the same provision in the SVCare option, the same
16 SVCare operating agreement, was gee, you know what
17 Schron got in the SVCare option? He got the right to
18 pay 100 million dollars and then turn around and make
19 a capital contribution equal to the 200 million
20 dollars that the company is worth. So the SVCare
21 option gives them nothing more than the right to pay
22 100 million dollars more than the company.

23 Now, I could make this up as a
24 hypothetical, but this is precisely the argument
25 that's within the record below concerning the option

1 that's in front of the court on the next appeal. It
2 is, respectfully, an absurd argument that these
3 parties would have put it - - - would have put - - -
4 would have hidden the strike price in this option.

5 The parties to the Fundamental option are
6 sophisticated businessmen. They understood what they
7 were doing. They said consideration is 1,000
8 dollars. Upon that payment - - -

9 JUDGE SMITH: Tell me again, though, what
10 the business purpose, from their point of view, what
11 did they get out of giving you a 1,000-dollar option
12 to buy a third of the company?

13 MR. ENGEL: I mean, essentially, they had
14 no - - - they had no opportunity to make this
15 purchase without the consent of the landlord. Again,
16 they contest this issue. I mean, what I would submit
17 is where an option is unambiguous, and its terms are
18 clear, their latter-day perceptions of the fairness
19 of the original deal are irrelevant. And that's - -
20 - this court has held this in the Greenfield case,
21 you know, among other cases.

22 So - - - but if one wants to actually take
23 them on their own terms - - -

24 JUDGE SMITH: Well, but you - - - but if
25 this were a simple deal to sell 333 million dollars

1 for 1,000 dollars, you might - - - you might think it
2 looked a little strange?

3 MR. ENGEL: You might think that
4 sophisticated businessmen would go slowly before
5 making that transaction. The truth here, though, is
6 at this time they had put in 50 dollars each into
7 this company. They charged him 1,000 dollars for his
8 option. That was the deal. The deal made sense at
9 the time for reasonable reasons.

10 They concede that he issued this covenant
11 not to sue around the time he got the option, even
12 though, just as they invent a capital - - - a market-
13 value requirement from the operating agreement, they
14 say gee, he just did that because he's a nice guy and
15 had his other reasons.

16 But the deal was clear. When the option -
17 - - they don't even, I would submit, take the
18 position that the option is ambiguous at all. They
19 say the option is clear, it just doesn't cover this
20 special territory. Once you acquire the shares, once
21 you're admitted to the company, well - - - and once
22 you've paid your 1,000 dollars in consideration under
23 the option, this other requirement kicks in.

24 CHIEF JUDGE LIPPMAN: What does - - - what
25 does "member" means to you?

1 MR. ENGEL: Member means owner. I mean,
2 it's a defined term under the LLC Act. And the
3 members are the owners of the company.

4 JUDGE SMITH: If - - - you would say it
5 would stay "stockholder" if it were a corporation?

6 MR. ENGEL: Yes. I mean, that's - - - that
7 would be my - - - you know, one other thing on the
8 operating agreement, which I'm surprised it was not
9 even addressed by my brother in their reply brief at
10 all. Section 4.1(b)(16) of the operating agreement
11 makes perfectly clear that the managers, which are
12 Grunstein and Forman, acting together, may issue the
13 sha - - - may issue additional shares without
14 limitation on any terms and conditions that they
15 approve, including with respect to the capital
16 contributions and/or consideration required. It's
17 right there.

18 It's - - - they focus on 3.3 as a supposed
19 immutable requirement. 3.3 states a default rule.
20 That is, if Grunstein and Forman don't agree on what
21 to do, they have the operating agreement; the
22 operating agreement says - - - putting aside the
23 option - - - new shares should be issued based on at
24 least a market value contribution. It actually
25 doesn't even say they should be released for market

1 value. The actual words are "at least". That's the
2 default rule.

3 But when they agree, when they are acting
4 together, 4.1(b)(16) says very clearly, they may do
5 it without limitation on any terms on which they
6 agree. They exercised that authority. They
7 exercised that authority under the option. It's
8 signed by Grunstein. It's signed by Forman. It's
9 signed by Fundamental. The price is 1,000 dollars.
10 And this is really just a latter-day effort to wiggle
11 out of the deal.

12 If there are no further questions, I'll - -
13 -

14 CHIEF JUDGE LIPPMAN: Thank you, counselor.

15 MR. ENGEL: Thank you.

16 CHIEF JUDGE LIPPMAN: Counsel, is 3.3 a
17 default provision?

18 MR. REITER: It is a default provision.
19 And clearly the managers and owners of Fundamental
20 could have changed it. The issue really before this
21 court is, did they? The reason that the evidence
22 shows that they did not is because of the application
23 of the two - - - or the interplay of section 6, which
24 requires an amendment just to reflect the issuance of
25 the shares, and what the term "issuance" means in the

1 operating agreement.

2 Had the - - - had Fundamental decided to
3 give rights to Mr. Schron to buy this company,
4 however - - - to buy a third of this company, however
5 implausible that is, for 1,000 dollars - - -

6 CHIEF JUDGE LIPPMAN: It wasn't implausible
7 at the time, was it?

8 MR. REITER: Well, it was implausible at
9 the time, because - - -

10 CHIEF JUDGE LIPPMAN: Was it implausible at
11 the time?

12 MR. REITER: - - - from a realistic
13 standpoint, why would they bother to ask him for
14 1,000 dollars?

15 JUDGE SMITH: Well, he says you couldn't do
16 the deal without him.

17 MR. REITER: There's nothing in the record
18 that supports that conclusion. That is - - - that is
19 a contested fact, and it is outside of the record.
20 The fact that his - - -

21 JUDGE SMITH: Well, but - - -

22 MR. REITER: - - - consent - - -

23 JUDGE SMITH: - - - even if it's conte - -
24 - I mean, you're trying to show that the reading that
25 some people might give to this agreement is absurd.

1 There's at least a nonabsurd possibility, which is
2 that you had to let him in, essentially, for free, or
3 you couldn't make the deal at all.

4 MR. REITER: Well, I have two responses to
5 that, Your Honor. First, there's nothing in the
6 record that supports that at all. We're both here
7 saying please decide this case based upon the record
8 that is before the court, which is based upon these
9 agreements. And as we all know, as a cardinal rule -
10 - -

11 JUDGE SMITH: Well, it is - - - it is in
12 the record. I mean, there is something - - - his
13 deposition testimony is in there, in which he
14 essentially says that, as I understand.

15 MR. REITER: But there is - - -

16 JUDGE SMITH: But it's contested, I grant
17 you.

18 MR. REITER: - - - it is contested. But
19 obviously, one might go and ask for consent, just to
20 make sure that the issue wouldn't arise in the
21 future. It isn't necessarily obtained because one
22 requires it. It's a - - - but people do belt-and-
23 suspenders in transactions. And it would be equally
24 reasonable that they simply wanted to make sure that
25 they weren't challenged.

1 The key for us to this is that each part of
2 an agreement that applies, and there's no doubt that
3 both agreements apply here, must be given meaning.
4 The rights and obligations that Mr. Schron had
5 imposed upon him and that he received, only applied
6 to him once he became a member.

7 JUDGE SMITH: Well, I mean, why - - - is
8 the rule that it must be given meaning, is it really
9 applicable, where he's only a party to one of them?

10 MR. REITER: It is, because under - - -
11 whether it's New York law or Delaware law, that
12 applies. Once you become a member, which is what
13 they are saying, and it's provided for in the option,
14 the operating agreement applies to all of its
15 members, as a matter of law.

16 JUDGE PIGOTT: Reduced to its simplest, I
17 guess, what you're saying is that for the 1,000
18 dollars, this man was given the option - - - you
19 can't buy stock in Fundamental. It's not on the
20 stock exchange. So for 1,000 dollars, you now have
21 the right to buy the stock. You can buy it the day
22 after the option for a dollar; you can buy in five
23 years for ten. When you decided to exercise the
24 option, guess what? It's going to cost you.

25 MR. REITER: Absolutely right. In other

1 words - - - and it is - - - as your statement really
2 suggests, on the one hand as well, it's implausible
3 to believe that for the price of a flat-screen TV or
4 a middle-level computer, you can buy one third of a
5 company, which, at the time, had a constellation of
6 healthcare facilities to it.

7 That implausibility alone doesn't decide
8 this case. But I suggest to you, and I submit that
9 it raises a red flag as to whether their
10 interpretation does make sense. And it requires us
11 to go to the text. And in New York law, it's a
12 cardinal rule that every word in agreements that
13 apply must be given meaning.

14 If that rule is applied here, 3.3
15 absolutely applies to Mr. Schron. He must comply
16 with it, having exercised the option. And he cannot
17 escape it, because the operating agreement applies to
18 him as a matter of law, once he becomes a member,
19 which is his contention.

20 CHIEF JUDGE LIPPMAN: Okay, counselor.

21 MR. REITER: Thank you very much.

22 CHIEF JUDGE LIPPMAN: Thank you.

23 (Court is adjourned)

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C E R T I F I C A T I O N

I, Penina Wolicki, certify that the foregoing transcript of proceedings in the Court of Appeals of Fundamental Long Term Care Holdings, LLC v. Cammeby's Funding LLC, No. 22 was prepared using the required transcription equipment and is a true and accurate record of the proceedings.

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