

NORTH CAROLINA
COUNTY OF WAKE

IN THE GENERAL COURT OF JUSTICE
SUPERIOR COURT DIVISION
08 CVS 14393

LEE N. PALLES,

Plaintiff,

v.

HATTERAS INVESTMENT PARTNERS
LLC, HATTERAS INVESTMENT
MANAGEMENT LLC, HATTERAS
CAPITAL DISTRIBUTORS, LLC,
HATTERAS CAPITAL INVESTMENT
MANAGEMENT LLC, HATTERAS
CAPITAL INVESTMENT PARTNERS,
LLC, DAVID B. PERKINS, ROBERT
LANCE BAKER, ROBERT L.
WORTHINGTON, ROBERT B. BROWN,
ANDREW CHICA, JAMES MICHAEL
FIELDS, MICHAEL J. HUTTEN, NICOLE
L. PARKER and MILLISSA S. ALLEN,

Defendants.

MEMORANDUM OF LAW OF PLAINTIFF, LEE N. PALLES

This Memorandum is submitted on behalf of Plaintiff, Lee N. Palles (“*Palles*” or “*Plaintiff*”) in opposition to the motion of defendants to dismiss Palles’ Sixth, Seventh, Eighth, Ninth, Tenth, Eleventh, Thirteenth and Fourteenth claims for relief pursuant to North Carolina Rule of Civil Procedure 12(b)(6). For the following reasons, defendants’ motion to dismiss should be DENIED.

SUMMARY OF THE CASE AND THE FACTS

Defendants want to characterize this case as a mere breach of contract action. While there were certainly numerous breaches of contract in this case, the independent tortious actions of the Hatteras companies and their managing member take this case well beyond a mere breach of contract case.

In his amended verified complaint (the “*Amended Complaint*”), Palles asserts various

claims against five (5) affiliated limited liability companies, Hatteras Investment Partners LLC (“*HIP*”), Hatteras Investment Management LLC (“*HIM*”), Hatteras Capital Investment Partners, LLC (“*HCIP*”), Hatteras Capital Investment Management, LLC (“*HCIM*”), Hatteras Capital Distributors, LLC (“*HCD*”) (together the “*Hatteras companies*”), and against David B. Perkins (“*Perkins*”), the majority, controlling, and managing member of all Hatteras companies. At the present time, the only reason the other named individual defendants are included in this suit is because those individuals all appear in publicly-filed documents as currently owning an interest in one of the Hatteras companies, and Palles believes that those interests could be affected by the outcome of this litigation. (Amended Complaint §61).

As set out more fully in the Amended Complaint, the Hatteras companies are investment managers and brokers of various closed-end investment funds. Palles had been an executive employee of the Hatteras companies since the summer of 2006, having served as Chief Operating Officer of the first two Hatteras companies that were formed, *HIP* and *HIM*, and then later as Chief Financial Officer of all five Hatteras companies. Palles was also an investor and holder of a minority membership interest in all of the Hatteras companies, having invested over \$100,000 of his own money in these companies. (Amended Complaint §19 - 27).

Then, in February 2008, Perkins told Palles Perkins needed him to focus on developing the Hatteras venture funds. Perkins offered Palles a three-year employment term and assured him that his membership interests in the venture fund operating companies (*HCD*, *HCIP* and *HCIM*) would be secure well into the future. Palles accepted these terms and immediately began working in earnest to jump start the development of the venture funds. (Amended Complaint §31 - 33).

A week later, on February 15, 2008, to Palles’ surprise, Perkins tried to unilaterally change the terms of the new employment agreement, to which Palles did not consent. (Amended Complaint §34). Then, two weeks after that, on March 5, 2008, without any notice or warning, Perkins told Palles that his employment with the Hatteras companies was terminated and that all of his membership interests in the Hatteras companies were being redeemed. (Amended

Complaint §35). Palles refused to accept the terms of the release Perkins wanted him to accept because Palles had forecast that the future value of his employment and his membership interests would be far in excess of the amount Perkins was trying to force him to accept. (Amended Complaint §39).

Over the next few months, Palles repeatedly requested to inspect books and records of account of the Hatteras companies pursuant to his rights under the companies' operating agreements and applicable law. (Amended Complaint §40).

In June 2008, defendants definitively told Palles that he was not allowed to inspect any books and records and claimed that Palles' interests in three of the Hatteras companies (HCIP, HCIM, and HCD) had been redeemed for cause on February 6, 2008, two days before Perkins had assured Palles that his interests in those companies would be secure. (Amended Complaint §40-41). When Palles' legal counsel told defendants that they had no right to redeem Palles' interests, with respect to HCD, defendants then tried to amend the HCD operating agreement to give Perkins the unfettered right to redeem Palles' interest, even though such an amendment would have required Palles' consent (which he did not give). (Amended Complaint §44).

Palles believes and so alleges that defendants took these actions to keep Palles from realizing the forecasted returns on his investments, and to divert such returns, along with his membership interests themselves, to Perkins or to others for Perkins' benefit. These actions were in breach of numerous contractual obligations to Palles, as well as improper, unfair, violative of Perkins' duty to exercise good faith, fraudulent, willful, and malicious. As such, defendants have committed, and Palles has properly alleged claims for various contract and tort claims, including breach of contract, wrongful interference with contract, fraud, constructive fraud, breach of fiduciary duty and the duty of good faith, conversion of personal property, punitive damages, and unfair and deceptive trade practices.

ARGUMENT

I. LEGAL STANDARD FOR 12(B)(6) MOTION TO DISMISS

For purposes of a motion to dismiss based upon Rule 12(b)(6) of the North Carolina Rules of Civil Procedure, allegations of fact from the complaint are taken as true. *Acosta v. Byrum*, 180 N.C.App. 562, 567, 638 S.E.2d 246, 250 (2006). In addition, the complaint must be liberally construed and the court should not dismiss the complaint unless it appears beyond a doubt that the plaintiff could not prove any set of facts to support the claim which would entitle her to relief. *Id.* A plaintiff need only allege the substantive elements of a valid claim in order to avoid dismissal for failure to state a claim upon which relief can be granted. *Id.* In practice, “[t]he system of notice pleading affords a sufficiently liberal construction of complaints so that few fail to survive a motion to dismiss.” *Ladd v. Estate of Kellenberger*, 314 N.C. 477, 481, 334 S.E.2d 751, 755 (1985).

An Amended Complaint was filed in this matter on November 12, 2008, which has the effect of superseding the original Complaint; consequently, the Court should consider the allegations of the Amended Complaint in determining whether defendants’ motion to dismiss is proper. *See Zenobile v. McKecuen*, 144 N.C. App. 104, 109, 548 S.E.2d 756, 759 (2001) (finding reversible error where trial court ruled on motion to dismiss before ruling on motion for leave to amend complaint); *Freeman v. Blue Cross and Blue Shield of North Carolina*, 123 N.C. App. 260, 262, 472 S.E.2d 595, 596 (1996) (stating allegations contained in complaint and amended complaint are taken as true for purposes of ruling on a motion to dismiss); *Hyder v. Dergance*, 76 N.C. App. 317, 319-20, 332 S.E.2d 713, 714 (1985) (affirming it is a general principle that an amended complaint has the effect of superseding the original complaint).

II. LEGAL DISCUSSION

As set out in more detail below, the granting of defendants’ Motion to Dismiss would be inappropriate at this stage of this case. First, Palles’ individual tort claims against Perkins are

based not just on his being the majority, controlling and managing member of the Hatteras companies, but on Perkins' personal wrongful acts for which he can be and is personally liable. Second, all tort claims alleged in the Amended Complaint are properly pled. Palles' claim against Perkins for wrongful termination of contract is proper because Perkins' wrongful interference was done so for his own personal benefit, thus negating his qualified privilege as managing member. Palles' fraud-based claims are also properly pled because the Amended Complaint makes clear, *inter alia*, that the Hatteras companies and Perkins, who had fiduciary obligations to Palles, never intended to keep the promises made to Palles in February 2008. Accordingly, because Palles properly pled claims for fraud, constructive fraud, breach of fiduciary duties, and also conversion, Palles' claim for punitive damages is properly pled. In addition, the allegations of defendants' misconduct point to the kind of bad faith business dealing which, if proved, could constitute an unfair trade practice within the meaning of section 75.1-1 of the General Statutes. Finally, the Amended Complaint sufficiently describes numerous breaches of contract by HCIM and HCIP.

A. The Naming Of Perkins As An Individual Defendant Is Proper Because He Was The Managing Member Of All Hatteras Companies And Because Such Claims Against Perkins Are Alleged Based On Perkins' Independent Wrongful Actions.

As recited by the North Carolina Court of Appeals in *Babb vs. Bynum & Murphrey, PLLC*, 82 N.C.App. 750, 753, 643 S.E.2d 55, 57 (2007):

“The Limited Liability Company Act (‘Act’) states:

A person who is a member, manager, director, executive, or any combination thereof of a limited liability company is not liable for the obligations of a limited liability company solely by reason of being a member, manager, director, or executive and does not become so by participating, in whatever capacity, in the management or control of the business. A member, manager, director, or executive may, however, become personally liable by reason of that person's *own acts or conduct*.

N.C. Gen.Stat. § 57C-3-30(a) (2005) (emphasis added [in the opinion])”

In *Babb*, the court refused to hold a law partner personally liable for the wrongful acts of his partner of which he knew nothing about. In this case, though, the claims made against Perkins are based on his “*own acts or conduct*” including (i) his inducing, without justification, the Hatteras companies to breach their contractual obligations to Palles, (ii) his fraudulent misrepresentations to Palles concerning Palles’ continued ownership of his membership interests, (iii) his using his position of trust and confidence to bring about transactions that were detrimental to Palles and beneficial to Perkins, and (iv) his failing to act in good faith in dealing with Palles, all of which were to avoid having to pay Palles salary, benefits, and distributions on account of membership interests to which Palles was lawfully entitled, and to instead wrongfully divert such distributions, and such membership interests themselves, to Perkins for his own benefit or to others for Perkins’ benefit. (Amended Complaint §78, 82, 90, and 94).

None of the cases cited by defendants are similar or apposite to this case. *Hamby v. Profile Products, L.L.C.*, 361 N.C. 630, 652 S.E.2d 231 (2007), involved an employee’s work-related injury claim, where the court held the injured employee’s claim against the sole member of his employer (which sole member was also an LLC) was barred by the exclusivity provisions of the Workers’ Compensation Act. In *Page v. Roscoe, LLC*, 128 N.C.App. 678, 497 S.E.2d 422 (1998), the plaintiff in effect only alleged that the individual defendant should be liable because he was a member of the LLC. Finally, in *Spaulding vs. Honeywell, Int’l, Inc.*, 184 N.C.App 317, 646 S.E.2d 645 (2007), the court dismissed claims only against the non-manager member of the defendant LLC.

As stated above, Palles’ claims against Perkins relate both to (i) Perkins’ role as *managing and controlling* member of the Hatteras companies (not Perkins’ being merely a member), and (ii) Perkins’ own willful, fraudulent, malicious and wrongful acts and conduct that were taken to personally benefit Perkins at the expense of Palles. These claims are exactly the type of claims that are allowed to be brought against individual managers of limited liability companies pursuant to the

last sentence of N.C. Gen.Stat. § 57C-3-30(a).

B. Palles' Fraud Claim Satisfies Rule 9(b) And is Based on More Than a Mere Contract Claim.

In its motion to dismiss for failure to state a claim, defendants argue that plaintiff's fraud claim does not satisfy the heightened pleading requirements of Rule 9(b). Further, defendants contend that Palles' claims for fraud, constructive fraud, and negligent misrepresentation should be dismissed because the wrongful conduct arises out of Palles' contractual relationship with defendants and the facts supporting the tort claims sustain no more than a breach of contract claim. It is interesting that defendants cite the case of *Food Lion, LLC v. Schuster Mktg Corp.*, 382 F. Supp. 2d 793 (E.D.N.C. 2005) because the plaintiff in that case (in response to defendant's counterclaims for fraud, etc.) had made the same arguments as the defendants make in this case. That court, however, rejected Food Lion, LLC's contentions and held that the allegations of defendant's counterclaims did sufficiently plead a cause of action for fraud, and that the behavior alleged could constitute an independent tort. *Food Lion, LLC* at 799-800.

In *Food Lion, LLC*, the defendant alleged that plaintiff made representations that were "false and misleading and were known to [plaintiff] and its representative, Jason Ramsey, to be false and misleading when made in that [plaintiff] had no present intention to perform at the time they were made." Defendant also alleged that "based on [plaintiff's] representations, [defendant] was induced to grant [plaintiff] certain promotional allowances . . ." As the court stated, "[t]hus, defendant claims to have relied on the representations of the plaintiff to its detriment, and describes how it relied. Moreover, the counterclaim contains factual allegations from which it could be inferred that such reliance was reasonable." *Food Lion, LLC* at 798.

The court held that these allegations were sufficient to state a claim for fraud and to constitute a tort independent of defendant's contract claims. In so deciding, the court cited, among other North Carolina state court cases, the case of *Williams v. Williams*, 220 N.C. 806, 18 S.E.2d 364 (1942), and stated "[o]f particular relevance to the case at bar, *Williams* stands for the proposition that an action for fraud could be sustained based on a promise made with no intention that it be carried out." See also, *Britt v. Britt*, 320 NC 573, 359 SE 2d 467 (1987) ("Evidence of a promise which is not fulfilled is not sufficient to support a finding of a false representation unless the evidence shows the promisor made the promise with no intention of fulfilling it").

Similarly, in the Amended Complaint, Palles alleges that the defendants' statements, representations, and promises to Palles on February 6, 2008 and February 8, 2008 were false and misleading at the time they were made, and were known by the defendants to be false and misleading when made because the defendants obviously had no intention at that time of carrying out their promise to allow Palles to continue to own his current membership interests in HCD, HCIP and HCIM after Palles' three-year employment term. (Amended Complaint § 82). Palles also alleges that defendants made these statements, promises and representations with the knowledge and intent that Palles would act in reliance on them by agreeing to an amended employment agreement that did not specifically include a restatement of Palles' then existing membership interests in HCIM, HCIP and HCD, and Palles did in fact agree to such terms to his detriment (the detriment being that it resulted in defendants' wrongfully claiming that they had the right to redeem Palles' membership interests, and then actually wrongfully redeeming Palles' membership interests and diverting such interests, along with distributions on account of such

interests, to Perkins or to others for Perkins' benefit). (Amended Complaint § 83-84). Moreover, the Amended Complaint alleges that such reliance was reasonable because, *inter alia*, Perkins controlled all Hatteras companies, Perkins had just offered Palles a three (3) year employment term with the Hatteras companies, and Perkins had not theretofore divulged that he had already wrongfully redeemed Palles' membership interests in HCIM, HCIP and HCD on February 6, 2008, nor otherwise given Palles any indication that Perkins had or was planning to wrongfully seek to deprive Palles of Palles' right to continuing interests in these Hatteras companies. (Amended Complaint § 84).

Like in *Food Lion, LLC* and the cases cited therein, these allegations by Palles satisfy the heightened pleading requirements of Rule 9(b), and the defendants' behavior alleged, if proved, would constitute a tort independent of the contract claims. Accordingly, defendants' motion to dismiss Palles' fraud claim should be denied.

C. Palles has sufficiently pled his claim for constructive fraud.

Defendants do not challenge that Perkins, as the managing, majority and controlling member of all the Hatteras companies, had a relationship of trust and confidence with Palles, who was a minority and non-managing member. However, by just reciting paragraphs 89 - 91 of the Complaint and seemingly ignoring the 88 prior paragraphs that were incorporated by reference into Palles' constructive fraud claim, defendants argue that the Complaint fails to sufficiently detail how Perkins used his position of trust and confidence to the detriment of Palles and the benefit of Perkins. The Complaint read as a whole answers the specific questions defendants argue must be answered to properly state a claim.

The Amended Complaint, though, leaves no question as to how Perkins used his position to benefit himself to Palles' detriment. Palles alleges in the Amended Complaint that Perkins:

- (i) told Palles on or about February 8, 2008 that Palles would continue to own the

current membership interest percentages in HCD, HCIP and HCIM when Perkins never intended to honor that agreement,

- (ii) failed to provide written notice of the alleged redemptions of Palles' membership interests until June 12, 2008, more than four months after the alleged redemptions,
- (iii) had HCIM and HCIP pay Palles his liquidating shares therein of \$0 and \$0 respectively, when the value of Palles' capital accounts in those companies for 2008 were greater than \$0, and then failing and refusing to provide Palles with any books and records of these companies to enable Palles confirm the value of his liquidating shares,
- (iv) falsely claimed that Palles' membership interests in HCIM and HCIP had been redeemed for cause on February 6, 2008 and claimed that Palles was entitled to no other interest in HCIM and HCIP other than the sums of \$0 and \$0, and
- (v) allowed HCD to first wrongfully attempt to redeem Palles' membership interest in exchange for \$1,000.00, and then attempted to amend the HCD Operating Agreement to give HCD the right of forcible redemption, knowing that such amendment without Palles' consent was in contravention of the HCD Operating Agreement and the North Carolina Limited Liability Company Act, and then claimed that Palles' membership interest therein was being redeemed for fair value effective July 10, 2008, but then refusing to even disclose HCD's determination of fair valuation (as he had promised to do) and refusing to allow Palles to inspect any books or records of HCD to enable Palles to evaluate HCD's determination of value.

(Amended Complaint § 90).

The Amended Complaint also makes clear that the foregoing actions by Perkins were taken for the purpose of avoiding having to pay Palles distributions on account of membership interests to which Palles was lawfully entitled, and to instead wrongfully divert such distributions and such membership interests themselves to Perkins for his own benefit or to others for Perkins' benefit. *Id.*

In *Branch Banking & Trust Co. v. Lighthouse Financial Corp.*, 2005 NCBC 3 (N.C.Super.Ct. July 13, 2005), the Business Court, in denying a motion to dismiss a claim for constructive fraud, held that the “[claimant] has alleged fraud by BB & T and specifically alleged that the fraudulent acts were taken to benefit BB & T to the detriment of [claimant]” and,

as such, “[t]here are sufficient allegations to preclude judgment on these claims at this stage in the proceedings.” *Branch Banking & Trust Co.*, 2005 NCBC at ¶ 8.

Similarly, in this case, Palles has alleged fraud by the Hatteras companies and by Perkins and specifically alleged that the fraudulent acts were taken to benefit the Hatteras companies and Perkins to the detriment of Palles. (Amended Complaint §81 - 85). Thus, there are sufficient allegations to preclude judgment on these claims at this stage in the proceedings and the motion of the defendants should be denied.

D. Palles’ Claim for Wrongful Interference with Contract was Properly Pled and Should not be Dismissed.

Defendants argue in their brief, and cite cases from other states to support their argument, that Palles cannot assert a wrongful interference with contract claim against Perkins because he is managing member of the Hatteras companies. Defendants’ argument, though, along with the out-of-state cases they cite, is contrary to established North Carolina law. In *Embree Constr. Group, Inc. v. Rafcor, Inc.*, 330 N.C. 487, 411 S.E.2d 916 (1992), the North Carolina Supreme Court held that the plaintiff in that case stated a valid claim for wrongful interference with contract against officers and directors of a corporation by alleging that such officers and directors induced their corporation to breach its contract with plaintiff for their own personal benefit. *Id.* at 501, 411 S.E.2d at 926. The Court made clear that while “[o]fficers, directors, shareholders, and other corporate fiduciaries have a qualified privilege to interfere with contractual relations between the corporation and a third party,’ such privilege is overcome when the means or the officer’s motives are improper, and that “those who act for their *own* benefit may be held personally liable.” *Id.* at 498-499, 411 S.E.2d at 924.

In this case, Palles alleged the existence of valid contracts between himself and the Hatteras companies, that Perkins knew of these contracts and intentionally induced the Hatteras companies not to perform or to breach such contracts for the purpose of avoiding having to pay Palles salary and benefits (with regard to the employment contract), and distributions on account of membership

interests to which Palles was lawfully entitled, and to instead wrongfully divert such distributions, and such membership interests themselves, to Perkins for his own benefit or to others for Perkins' benefit, and that in so doing he acted without justification and to Palles' detriment. (Amended Complaint §§75-80). Just as the Supreme Court so held in *Embree*, Palles' allegations "give sufficient notice of the events on which the claim is based to enable defendants to respond and prepare for trial and are 'sufficient to satisfy the substantive elements of the claim' of tortious interference with contract." *Id.* at 501, 411 S.E.2d at 926.

E. Palles Has Sufficiently Pled a Claim for Punitive Damages.

Punitive damages may be awarded if the claimant proves that the defendant is liable for compensatory damages and that one of the following aggravating factors was present and was related to the injury for which compensatory damages were awarded: (1) Fraud, (2) Malice or (3) Willful or wanton conduct. N.C.G.S.A. § 1D-15.

As set out in N.C.G.S.A. § 1D-5:

(5) "Malice" means a sense of personal ill will toward the claimant that activated or incited the defendant to perform the act or undertake the conduct that resulted in harm to the claimant.

(7) "Willful or wanton conduct" means the conscious and intentional disregard of and indifference to the rights and safety of others, which the defendant knows or should know is reasonably likely to result in injury, damage, or other harm.

Further as the court stated in *Food Lion, LLC v. Schuster Mktg Corp.*, 382 F. Supp. 2d 793, 800 (E.D.N.C. 2005):

"Thus, the North Carolina Supreme Court has allowed a claim for punitive damages to stand where fraudulent misrepresentations accompanying a breach of contract were sufficiently alleged. *See Oestreicher v. Stores*, 290 N.C. 118, 225 S.E.2d 797 (1976)."

As discussed above, Palles' claims for fraud and constructive fraud have been properly pled and thus form the basis of a punitive damages claim. See also *Terry v. Terry*, 273 S.E.2d 674, 302 N.C. 77

(1981) (constructive fraud claims, which were based on confidential relationship and which were sufficient to withstand motion to dismiss for lack of particularity, also constituted a sufficient basis to withstand a motion to dismiss as regards claim for punitive damages).

In addition to Palles' claims for fraud and constructive fraud, Palles has specifically alleged and pled that defendants acted willfully and with malice towards Palles. (Amended Complaint § 107). The facts in the Amended Complaint unquestionably show a sense of personal ill will toward Palles and a conscious and intentional disregard of and indifference to Palles' rights, which defendants knew would result in Palles' incurring and suffering loss and damages.¹

Because Palles has sufficiently pled his entitlement to compensatory damages along with the aggravating factors of fraud, malice and willful conduct related to Palles' damages, defendants' motion to dismiss Palles' claim for punitive damages should be denied.

F. Defendants' Misconduct Does Constitute a Violation of the Unfair and Deceptive Trade Practices Act.

“Under section 75-1.1 of the General Statutes, “[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are declared unlawful.” N.C. Gen.Stat. § 75-1.1(a) (1999). The statute defines “commerce” as “all business activities, however denominated.” N.C.G.S. § 75-1.1(b).” *Walker v. Sloan*, 137 N.C.App. 387, 395, 529 S.E.2d 236, 243 (2000). As defendants cited in their brief, to state a claim for unfair and/or deceptive trade practices, a plaintiff must allege that (1) the defendants committed an unfair or deceptive act or practice, or an unfair method of competition, (2) in or affecting commerce, (3) which proximately caused actual injury to the plaintiff. *Pleasant Valley*

¹ See *Zubaidi v. Earl L. Pickett Enterprises, Inc.*, 164 N.C.App. 107, 595 S.E.2d 190 (2004), appeal dismissed, review denied 359 N.C. 76, 605 S.E.2d 151 (Original and amended complaint filed by new operators of convenience store, in their action against former operators for breach of a lease/purchase agreement, gave sufficient notice of new operators' intent to seek punitive damages; original complaint alleged that former operators' actions in breaching agreement were "deceitful, malicious and willful," amended complaint set forth facts to support operators' claims, including alleged fraudulent statements made by former operators, and both complaints requested court to impose punitive damages against former operators for their "wanton, reckless and malicious" actions).

Promenade v. Lechmere, Inc., 120 N.C.App. 650, 464 S.E.2d 47 (1995). Palles has made all of these allegations.

Defendants do not argue Palles' contention that they committed unfair and deceptive acts which caused injury to Palles. Defendants' sole argument is that their unfair and deceptive acts were not "in or affecting commerce." Defendants claim that internal corporate disputes are outside the scope of Unfair and Deceptive Trade Practices Act ("UDTPA"), and they cite several cases for the proposition that securities transactions and employer-employee relationships are not "in or affecting commerce" and thus not actionable under the UDTPA.

However, in *Walker v. Sloan*, the North Carolina Court of Appeals held that members of an employee group stated a UDTPA claim against two board members of the employer, and against the employer itself, based on allegations dealing with internal disputes and the employer-employee relationship. *Walker*, 137 N.C.App. at 396, 529 S.E.2d at 243. In that case, the employee group members, who were trying to buy out the stockholders of the employer, alleged that two board members (one of whom was in managing control of the company) used unfair tactics to try to thwart the group's buyout attempt, including terminating their employment. *Id.* The complaint in that case further alleged that the board members' acts "were in or affecting commerce" and "proximately caused injury to the plaintiffs, consisting of lost profits, lost wages and other benefits and income, and expenses including attorneys fees." *Id.*

The court stated that "the allegations of [the board members'] misconduct, on their face, point to the kind of bad faith business dealing which, if proved, could constitute an unfair trade practice within the meaning of section 75.1-1 of the General Statutes. Thus, plaintiffs have successfully stated a claim for unfair trade practices against [the board members]. The complaint also sufficiently alleges an unfair trade practice claim against [employer] on the basis of respondeat superior." *Id.*

Likewise, in this case, Palles alleges similar conduct on the part of defendants, including improperly terminating Palles' employment, making fraudulent misrepresentations, falsely

claiming that Palles' membership interests had been redeemed for cause, and wrongfully seeking to deprive Palles of property and interests to which he was entitled, all for the improper benefit of Perkins. Palles also alleges that such acts and conduct "were in or affecting commerce" and "proximately caused Palles to suffer and incur actual damages, including damages to the extent of any salary and benefits Palles should have but did not receive, and distributions that have been made by HCD, HCIM, and HCIP to which Palles should have, but did not receive, along with the value of the membership interests themselves. (Amended Complaint § 105).

Based on the facts and holding of *Walker v. Sloan*, the acts and conduct of Perkins and the Hatteras companies were in violation of the UDTPA, and defendants' motion to dismiss such claim should be denied.

F. Palles Has Sufficiently Pled Claims Related to HCIM and HCIP.

In the Amended Complaint, Palles makes several claims relating to HCIP and HCIM, the operating entities for the Hatteras Late Stage VC Fund I, L.P.: (i) multiple breaches of contract, (ii) demand for examination of the companies' books and records of account, and (iii) breach by Perkins of his fiduciary duty and duty of good faith. Defendants seemingly argue, though, that Palles cannot state a breach of contract claim against HCIM and HCIP because (a) their respective operating agreements allow Perkins to redeem Palles' membership interests at any time, and (b) Palles never alleged Perkins committed bad faith and, in any event, Perkins was allowed to redeem Palles' membership interests in bad faith. These arguments fail for several reasons.

First, the terms of these operating agreements were amended by the promises made by the Hatteras companies on February 8, 2008, specifically, that Palles' membership interests would not be redeemed even after Palles' three-year employment term. (Amended Complaint at § 32). Second, the HCIM and HCIP Operating Agreements both provide that upon redemption of a member's membership interest, such member would be entitled to a Liquidating Share on

account of such membership interest (defined as the closing balance of such Member's Capital Account for the year of determination), and upon the redemption of Palles' membership interest by the managing members other than for cause, Palles would still be entitled to receive 5% of the Remaining Proceeds upon a Sale Event when the managing members distributed such proceeds to the members. (Amended Complaint at § 67). Thus, even if HCIM and HCIP did have the right to redeem Palles' membership interests therein, which is denied, HCIM and HCIP still breached their operating agreements by (i) falsely claiming that Palles' capital account balances in HCIM and HCIP for 2008 were \$0 and \$0 and thus failing to pay Palles the true value of Palles' Liquidating Shares, and (ii) by stating in its June 12, 2008 letter that \$0 and \$0 was the sum total of Palles' respective interests in HCIM and HCIM, and failing to acknowledge that Palles was and is still entitled to receive 5% of the Remaining Proceeds from a Sale Event involving HCIM. (Amended Complaint at § 69).

Third, defendants argue that Perkins, as managing member, had no duty to exercise good faith in its dealings with Palles, including the decision to redeem Palles' membership interests. Such claim is incorrect. The operating agreements of HIM, HIP, HCIP and HCIM all state in Section 2.05 that

The Company, Managing Members and their Affiliates (collectively the "Exculpated Parties") shall not be liable to any Member or the Company for mistakes of judgment or for any action or inaction, unless such mistakes, action or inaction arise out of, or are attributable to, the gross negligence, willful misconduct *or bad faith of the Exculpated Party*. (emphasis added)

In addition, the operating agreements of HCIM and HIP state in Section 2.09 that:

Each Member hereby agrees that any standard of care or duty imposed in this Agreement or any other agreement contemplated herein or under the Act or any other applicable law, rule or regulation shall be modified, waived or limited in each case as required to permit the Managing Member to act under this Agreement or any other agreement contemplated herein and to make any decision pursuant to the authority prescribed in this Agreement *so long as such action or decision does not constitute* willful misconduct, gross negligence or *bad faith* and is reasonably believed by the Managing Members to be consistent with the overall purposes of the Company.

(emphasis added)

(Amended Complaint § 93). As such, Perkins, as managing member, had a duty to make decisions concerning Palles, including the decision to redeem his membership interests, in good faith.

Fourth, Defendants argue that Palles' Sixth Claim for Relief does not allege that the decision to redeem Palles' interests in HCIP and HCIM was made in bad faith. While defendants are correct that the Sixth Claim for Relief does not allege bad faith, they are incorrect that such claim is not included anywhere in the Complaint. In his Twelfth Claim for Relief, which defendants have not sought to dismiss, Palles clearly and sufficiently alleges and sets out how Perkins intentionally failed to deal with Palles in respect to the affairs of the Hatteras companies openly, fairly, honestly, and with the utmost good faith. (Amended Complaint §§ 92-96).

As properly alleged in the Amended Complaint, HCIM and HCIP breached multiple contractual obligations to Palles, and Perkins breach his duty to use good faith in his dealings with Palles, and, as such, defendants' motion to dismiss these claims for relief should be denied.

CONCLUSION

Contrary to defendants' contentions, Palles' Amended Complaint more than sufficiently states all the substantive elements of Palles' claims for fraud, constructive fraud, negligent misrepresentation, wrongful interference with contract, punitive damages, unfair and deceptive trade practice, and breach of contract and accounting with respect to HCIP and HCIM. For the foregoing reasons, as more fully set out above in this Memorandum, Palles respectfully requests that defendants' Motion to Dismiss be DENIED IN FULL.

This is the 12th day November, 2008.

/s/ Keith A. Satsky

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CERTIFICATE OF SERVICE

This is to certify that the undersigned has on this, a regular business day, served a copy of the foregoing *Memorandum of Law* upon all other parties to this cause by:

- XXXX Depositing a copy hereof, enclosed in a post-paid wrapper, in the United States mail addressed to each party's attorney as follows:

- _____ Hand delivering a copy hereof to the following attorney(s) for each other party:

- _____ Leaving a copy hereof at the following office(s) of the attorney(s) for each other party with a partner or employee:

- _____ Sending a copy hereof to the office(s) of the attorney(s) for each other party by telefacsimile transmittal at the following facsimile number(s), each of which were received by 5:00 p.m. EST, as evidenced by the attached telefacsimile receipt confirmation(s).

- _____ Electronic transmission of a copy of this document to the following email address:

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This the 12th day of November, 2008.

/s/ Keith A. Satsky
Keith A. Satsky, Esq.
Satsky & Silverstein, LLP
Attorneys for Plaintiff

CERTIFICATE OF COMPLIANCE

Pursuant to Rule 15.8 of the General Rules of Practice and Procedure for the North Carolina Business Court, the undersigned hereby certifies that the foregoing Memorandum of Law is less than 7,500 words (excluding the case caption, signature blocks, this Certificate of Compliance and the Certificate of Service) as reported by the word-processing software.

This the 12th day November, 2008.

/s/ Keith A. Satsky
Keith A. Satsky