MMX-17-CV-5009315-S	:	**SUPERIOR COURT**
	:	
MCHUGH, CHAPMAN & VARGAS, LLC	:	**JUDICIAL DISTRICT OF**
	:	
VS.	:	**MIDDLESEX AT MIDDLETOWN**
	:	
SEAN M. MCHUGH	:	**JUNE 20, 2017**

MEMORANDUM OF LAW IN SUPPORT OF
MOTION TO DISMISS

The defendant, Sean M. McHugh, submits this memorandum of law in support of his motion of even date to dismiss this matter.

I. Background.

This matter was commenced by PJR papers filed on April 10, 2017. By special assignment (102.00), the PJR hearing has been scheduled for a hearing on July 11, 2017.

This is a dispute between two attorneys at the law firm McHugh Chapman & Vargas, LLC (the "Firm"): David S. Chapman and Mr. McHugh, who is the founder of the Firm. Mr. Chapman apparently believes he has been shorted in the compensation due to him from the Firm. Logically, one would expect him to pursue a claim, in his own name, against the Firm. If Mr. Chapman believes he was underpaid by the Firm in the amount of $X, it should be a straightforward exercise to pursue a claim, in his own name, against that entity in that amount.

But that is not the path Mr. Chapman has taken. Instead, he has chosen the more tortuous route of purporting to bring suit derivatively in the name of the Firm against Mr. McHugh, who

handles the Firm's finances and who, according to Mr. Chapman, has taken excessive compensation for himself. Mr. Chapman has commenced these proceedings, in the name of the Firm, based on the premise that he is a member of the Firm. (Complaint, ¶8.)[1] The proposed Complaint is in six (6) counts, sounding in breach of fiduciary duty; conversion; civil theft; unjust enrichment; tortious interference; and unfair trade practice.

Mr. McHugh denies that Mr. Chapman is a member of the Firm. Rather, Mr. Chapman holds only an economic interest in the Firm, not full membership status. Accordingly, Mr. Chapman lacks standing to prosecute this action derivatively in the name of the Firm. It follows that this court lacks subject-matter jurisdiction over the cause, and the case should be dismissed.

II. Argument.

A. Legal Standard for a Motion to Dismiss, generally.

A motion to dismiss is the appropriate vehicle for attacking the jurisdiction of the court, "essentially asserting that the plaintiff cannot as a matter of law and fact state a cause of action that should be heard by the court." Gurliacci v. Mayer, 218 Conn. 531, 544 (1991).

"Jurisdiction of the subject-matter is the power [of the court] to hear and determine cases of the general class to which the proceedings in question belong.…" (Internal quotation marks omitted.) Doe v. Roe, 246 Conn. 652, 661 (1998). "[O]nce the question of subject matter jurisdiction has been raised, 'cognizance of it must be taken and the matter passed upon before it

[1] Mr.Chapman does not claim to be a manager of the Firm.

can move one further step in the cause; as any movement is necessarily the exercise of jurisdiction.' (citation omitted)." Schaghticoke Tribal Nation v. Harrison, 264 Conn. 829, 839 n.6 (2003).

A "motion to dismiss admits all facts well pleaded and invokes any record that accompanies the motion, including supporting affidavits that contain undisputed facts…. If a resolution of a disputed fact is necessary to determine the existence of standing when raised by a motion to dismiss, a hearing may be held in which evidence is taken." May v. Coffey, 291 Conn. 106, 108-09 (2009).

B. Standing, generally, as an element of subject matter jurisdiction.

"If a party is found to lack standing, the court is without subject matter jurisdiction to determine the cause." Tomilson v. Board of Education, 226 Conn. 704, 717 (1993). A defendant may challenge a plaintiff's standing. Barrett v. Southern Connecticut Gas Co., 172 Conn. 362, 370 (1977). Once the issue has been put into play, the plaintiff bears the burden of proving that he has standing. Sadlowski v. Manchester, 235 Conn. 637, 648-49 (1995). "It is the burden of the party who seeks the exercise of jurisdiction in his favor ... clearly to allege facts demonstrating that he is a proper party to invoke judicial resolution of the dispute." May v. Coffey, 291 Conn. 106, 113 (2009).

> Standing is the legal right to set judicial machinery in motion. One cannot rightfully invoke the jurisdiction of the court unless he [or she] has, in an individual or representative capacity, some real interest in the cause of action, or a legal or equitable right, title or interest in the subject matter of the controversy … When standing is put in issue, the question is whether the person whose standing is challenged is a proper party to request an adjudication of the issue … Standing requires no more than a colorable claim of injury; a [party] ordinarily establishes … standing by allegations of injury. ...

> Standing is established by showing that the party claiming it is authorized by statute to bring suit or is classically aggrieved. … The fundamental test for determining aggrievement encompasses a well-settled twofold determination: first, the party claiming aggrievement must successfully demonstrate a specific, personal and legal interest in [the subject matter of the challenged action], as distinguished from a general interest, such as is the concern of all members of the community as a whole. Second, the party claiming aggrievement must successfully establish that this specific personal and legal interest has been specially and injuriously affected by the [challenged action]… Aggrievement is established if there is a possibility, as distinguished from a certainty, that some legally protected interest … has been adversely affected.

May, *supra*, 291 Conn. at 112-13 (2009). (Citations and internal punctuation omitted.)

C. Standing to pursue a derivative claim on behalf of an LLC.

A "distinction must be made between the right of a shareholder to bring suit in an individual capacity as the sole party injured, and his right to sue derivatively on behalf of the [company] alleged to be injured." Yanow v. Teal Industries, Inc., 178 Conn. 262, 281-82 (1979).

The universe of people who can bring suit in the name of a limited liability company is defined by C.G.S. § 34-187: members and managers. That statute provides in relevant part as follows:

> (a) Except as otherwise provided in an operating agreement, suit on behalf of the limited liability company may be brought in the name of the limited liability company by: (1) any member or members of a limited liability company … who are authorized to sue by a vote of a majority in interest of the members … or (2) any manager or managers of a limited liability company, if the articles of organization vest management of the limited liability company in one or more managers, who are authorized to sue by the vote required pursuant to section 34-142.

Id. The statutes make a distinction between (i) full members of a limited liability company and (ii) persons who hold, by way of an assignment of a member's interest, only an economic, non-voting interest. Pursuant to C.G.S. § 34-170, "Assignment of membership interest":

> (a) Except as provided in writing in an operating agreement … an assignment entitles the assignee to receive, to the extent assigned, only the distributions to which the assignor would be entitled … [but] an assignment of a limited liability company membership interest does not … entitle the assignee to participate in the management and affairs of the limited liability company or to become or exercise any rights of a member.

Id. C.G.S. § 34-172 provides that for an assignee to become a full member, further overt action is required:

> [A]n assignee of an interest in a limited liability company may become a member if and to the extent that (1) the assignor gives the assignee that right in accordance with authority described in the operating agreement, (2) unless otherwise provided in writing in an operating agreement, at least a majority in interest of the members, other than the assignor, consent, or (3) ***if the limited liability company has only one member, the assignor gives the assignee the right to become a member***.

Id. (Emphasis added.)

D. Facts.

References to "Affidavit" are to the affidavit of Mr. McHugh, which is being filed herewith.

Mr. McHugh began a legal practice as a sole practitioner in 1995. (Affidavit, ¶ 3.) In 2005, he hired Mr. Chapman as an employee attorney. (*Id*., ¶ 4.) On December 18, 2006, Mr. McHugh established the Firm as a single-member LLC – with Mr. McHugh as the sole member – under the name McHugh & Chapman, LLC. (*Id*., ¶ 5; Exhibit 1 thereto, CONCORD listing showing date of creation; and Exhibit 2 thereto, CONCORD listing showing name-change history.) In 2008, Mr.

McHugh hired Attorney John Montalbano, and the name of the Firm was changed to McHugh, Chapman & Montalbano, LLC. (Affidavit, ¶ 6, and Exhibit 2 thereto.) (In December of 2013, the name of the Firm was changed to its current name, McHugh Chapman & Vargas, LLC. Affidavit, ¶ 7, and Exhibit 2 thereto.)

In 2009, Mr. McHugh drafted and signed an Operating Agreement for the Firm. (Affidavit, ¶ 8, and Exhibit 3 thereto, Operating Agreement.) In Article IV, Article V and Exhibit B, the Operating Agreement identifies Mr. McHugh as the sole member. (*Id*.) The Operating Agreement has never been amended or cancelled. (Affidavit, ¶ 8.)

In or about 2010, Mr. McHugh assigned to Mr. Chapman a partial interest in the Firm, giving Mr. Chapman an economic interest of about 1/3. (Affidavit, ¶ 9.) Mr. McHugh did not intend to assign to Mr. Chapman membership rights such as the right to participate in the management of the Firm, or any interest above and beyond an economic interest in the Firm. (Affidavit, ¶ 9.)

Section 10.2 of the Firm's Operating Agreement provides as follows:

> Section 10.2 – Transferee Not Member in Absence of Consent of Holders of Majority Interest. Notwithstanding anything contained herein to the contrary, if members, other than the Transferring Member, holding one hundred percent of the Company Interests held by members other than the Transferring Member do not approve, by written consent, of the proposed sale or gift of the Transferring Member's Membership Interest to a transferee or donee who is not a Member immediately prior to the sale or gift, then the proposed transferee or donee shall have no right to participate in the management of the business and affairs of the Company or to become a Member, then the transferee or donee may only become an Economic Interest Owner. ***No transfer of a Member's interest in the Company (including any transfer of the Economic Interest or any other transfer which has not been approved by written consent of the Members holding a Majority Interest) shall be effective unless and until written notice (including the name and address of the proposed transferee or donee and the date of such transfer) has been provided to the Company and the non-transferring Members.***

Id. (Emphasis added.) To the best of Mr. McHugh's knowledge and belief, no such written notice about Mr. Chapman's would-be membership interest has been issued. (Affidavit, ¶ 11.)

The Operating Agreement also provides, at section 5.1, that the Firm is to be managed by its members, not a manager. (*Id*.) Following his partial assignment to Mr. Chapman, consistent with his continued status as sole member, Mr. McHugh has continued to unilaterally oversee the management and affairs of the Firm, handling such matters himself, handling them jointly with or through his wife Lori McHugh and/or Meghan Woods (both of whom are attorneys at the Firm), or delegating tasks to others. (Affidavit, ¶ 12.) More particularly, and without limitation, Mr. McHugh has handled and continues to handle and/or supervise the following, in some instances in conjunction with or as delegated to Lori and/or Ms. Woods:

- The investigation, management and resolution of all employee complaints and claims against the Firm and/or Mr. Chapman specifically;
- The investigation, management and resolution of unemployment compensation claims against the Firm;
- The investigation, management and resolution (including retaining and working with counsel, handling discovery responses, negotiating settlements and signing releases) of all formal complaints and lawsuits against the firm, which have included a lawsuit by Mr. Montalbano against the Firm, and a malpractice claim against the Firm and a former attorney at the Firm, which remains pending;
- Changes of the Firm's name;
- Negotiation and execution of the Firm's premises leases, and dealing with the landlord on such items as repairs;

- Approving the payment of Firm expenses, and issuing and signing the checks;
- Firm payroll;
- Hiring and firing of Firm employees, including attorneys;
- Setting of the Firm's weekly schedule and deciding which attorneys shall handle which hearings;
- Setting office rules;
- Negotiating and setting all employee salaries and bonuses;
- Considering and deciding employee requests to leave early, come in late, take time off and/or work overtime;
- Negotiating, approving and executing vendor contracts for such items as copier, shredding, water delivery, stationery, office supplies, furniture, postage machine, phone service, and phone system;
- Negotiating, approving and executing Firm worker's compensation and professional liability insurance;
- Maintaining records of employee time off;
- Assigning and changing employee work duties; and
- Supervising the creation and alteration of the Firm's website and commercials.

(Affidavit, ¶ 13.)

For the life of the Firm, it has not conducted member meetings, nor has it held member votes. (Id., ¶ 14.)

In sum, Mr. McHugh granted to Mr. Chapman, and Mr. Chapman holds nothing more than, an assignee interest in the Firm, as per C.G.S. § 34-170. Mr. McHugh did not take the distinct

second step, as required by C.G.S. §34-172 and the Operating Agreement, of granting to Mr. Chapman the further status of membership.[2]

Between C.G.S. § 34-172's requirement that a sole member expressly "give[] the assignee the right to become a member" and the requirement of section 10.2 of the Operating Agreement for a "written notice" to that effect, it should be clear that, absent an instrument that clearly documents the transfer of a membership interest, Mr. Chapman cannot sustain his proof of membership status. The present case provides a perfect example of why, to avoid confusion and chaos, clear and unambiguous documentation should be required.

E. Because Mr. Chapman is not a member of the Firm, he does not have authority to pursue this derivative action on its behalf.

Returning to C.G.S. § 34-187, an action may be commenced and prosecuted on behalf of a limited liability company only by its managers or members. Mr. Chapman makes no claim to the status of manager, the Operating Agreement vests management of the Firm in its member(s), and the evidence clearly shows that Mr. Chapman has not functioned as a manager. Furthermore, as detailed above, Mr. Chapman holds only an assignee economic interest in the Firm. He is not a member of the Firm, and therefore cannot serve as its derivative plaintiff.

[2] Mr. McHugh acknowledges signing and/or approving certain Firm documents that identify Mr. Chapman as a member, in instances where the document did not lend itself to distinctions between a true member and a person holding an assigned economic interest. For example, on the annual K-1's issued by the Firm to Mr. Chapman and incorporated into the Firm's tax returns, the box for "General Partner or LLC Member-Manager" is checked, which Mr. McHugh understands to be the most-nearly-accurate option for a holder of an economic interest, and thus the correct one to check. (Affidavit, ¶ 15.)

Because this suit is unauthorized per the applicable statute, the plaintiff lacks standing, and the court lacks jurisdiction over the cause. Mr. Chapman is free to pursue his claims in his own name.

III. Conclusion and Statement of Relief Requested.

For the foregoing reasons, the defendant respectfully submits that this matter should be dismissed.

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CERTIFICATION

I hereby certify that copies of the foregoing motion and of the supporting affidavit and memorandum of law were or will immediately be mailed or delivered electronically or non-electronically on June 20, 2017, to the following counsel of record and that written consent for electronic delivery was received from the same.

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