STATE OF NEW YORK
SUPREME COURT : COUNTY OF ERIE

KENNETH P. GOUCHIE AND
STEVEN P. FRANKEL,

Plaintiffs,

MEMORANDUM DECISION

vs.

Index No. 2007-8226

CREDITORS INTERCHANGE
RECEIVABLE MANAGEMENT, LLC,
AND DEBT RESOLVE, INC.,

Defendants.

BEFORE: **HON. JOHN M. CURRAN, J.S.C.**

APPEARANCES: **EDWARD J. SEPLAVY, ESQ.**
Attorney for Plaintiffs

HARRIS BEACH PLLC
Attorneys for Defendants
Daniel J. Moore, Esq., of Counsel
Gregory J. McDonald, Esq. of Counsel

CURRAN, J.

This action seeks recovery for damages allegedly arising out of the purchase by Defendant, Creditors Interchange Receivable Management, LLC, of plaintiffs' collection agency, Abrams & Swartz, Inc. Creditors Interchange Receivable Management, LLC has moved to dismiss the complaint against it in its entirety, based upon documentary evidence under CPLR 3211 (a) (1) and also based upon the failure to state a cause of action under CPLR 3211 (a) (7).

After due consideration, the Court grants the motion in its entirety.

BACKGROUND

According to the Complaint in this matter, Plaintiffs Kenneth P. Gouchie (hereinafter Gouchie) and Steven P. Frankel (hereinafter Frankel) were co-owners of Abrams & Swartz, Inc., a collection agency located in Somerset, Massachusetts that specialized in collection of past due commercial accounts (*see* Complaint ¶ 8). Creditors Interchange Receivable Management, LLC (hereinafter CIRM),[1] then a national consumer debt collection agency, allegedly contacted plaintiffs, seeking to acquire Abrams & Swartz's model for commercial collections, its existing collection contracts and accounts, its client lists, goodwill, and commercial collection expertise (*see* Complaint ¶¶9-10). Gary Holter, Chief Financial Officer of CIRM, traveled to Massachusetts and, after reviewing the business, offered plaintiffs a ten (10) percent equity share of the new CIRM Commercial Division in exchange for their business (*see id*. ¶¶ 10-11). Plaintiffs believed that, as of July 2005, their company had a fair market value of approximately $3,000,000 (*see* Complaint ¶ 8). They agreed to the offer because of the promised equity share and management positions, despite the fact that the salary and bonus structure offered to them would be less than they were currently earning in their own business (*see id*. ¶ 12).

CIRM drafted and prepared the Asset Purchase and Sale Agreement (*see* Plaintiffs' Affid. ¶ 5 & Holter Affid., Exhibit A) and two Employment Agreements (*see id*.

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[1] Defendant Debt Resolve, Inc., is named as a successor in interest to CIRM (*see* Complaint ¶ 4). However, it appears that the plan by Debt Resolve, Inc. to purchase CIRM was not carried out (*see* Moore Reply Affid., Exhibit 2), and therefore any claims stated by Plaintiff against Debt Resolve are without merit. Plaintiff does not argue otherwise.

Exhibits B & C). Allegedly, upon review of the documents, plaintiffs "confronted CIRM because the Buy-Sell Agreement did not state that Abrams & Swartz, Inc. was being acquired in exchange for [sic] ten percent equity ownership in CIRM" (Complaint ¶ 13). In response, CIRM personnel represented to plaintiffs that their investment was "completely secure as it was incorporated into the long term incentive provision of the employment contract", at Exhibit A to plaintiffs' Employment Agreements (Holter Affid., Exhibits B & C). Further, the value of the business was excluded from the Asset Purchase and Sale Agreement and incorporated into the Employment Agreements to avoid sales taxes (*see* Plaintiffs' Affid. ¶ 9).

The parties thereafter executed the three Agreements. Under the Asset Purchase and Sale Agreement, dated July 28, 2005, CIRM purchased all of Abram & Swartz's assets and equipment including collection accounts, office equipment, contracts, goodwill and leases, for a "total consideration" of $10,445 (*see* Holter Affid., Exhibit 1 [hereinafter Asset Purchase and Sale Agreement]). Schedule 1.2 of the Asset Purchase and Sale Agreement lists the equipment sold, which is valued at the precise amount of the purchase price for the entire business – $10,445 (see Asset Purchase & Sale Agreement § 2.1).

Under an Employment Agreement, dated August 1, 2005, Gouchie became Group Division Manager of the new CIRM Commercial Division, created out of Abrams & Swartz (*see* Holter Affid., Exhibit B ¶ 1). His annual base salary was $50,000 and he was eligible to earn a monthly bonus "in accordance with the criteria established" by CIRM (*id*. ¶¶ 5.1, 5.3 & Exhibit B). His employment was for an initial five-year term, renewable yearly thereafter, but could nonetheless be terminated with or without cause by CIRM at any time, upon the payment of severance benefits if the termination was without cause (*see id.* ¶¶4, 9.2, 10, 11-12).

Under an Employment Agreement similar to Gouchie's, Frankel became director of Sales of the Commercial Division (*see* Holter Affid., Exhibit C ¶ 1).

Under paragraph 6.2 of the Employment Agreements,

> Employee may be entitled to participate in the Long-Term Incentive Plan that may be adopted and maintained by the Company during the Employment Term. **The Company shall not be obligated for any reason to develop, implement or maintain any such Long-Term Incentive Plan for the benefit of the Employee. Any participation by the Employee under any such plan shall be determined by the terms and provisions of the plan. An illustration of the Long-Term Incentive Plan is attached hereto as Exhibit "A"**

(Holter Affid., Exhibits B & C, ¶ 6.2 [emphasis supplied]).

Exhibit A to both Employment Agreements provides an "Illustration" of the Long-Term Incentive Plan:

> Ten Percent (10%) of the value of the Commercial Division of Creditors Interchange Receivable Management, LLC (as acquired from Abrams & Swartz, Inc.), as the same is determined by the trailing 12-month EBITDA of the Commercial Division at the time of a liquidity event to Credint [sic] Holdings LLC, as such liquidity event is determined by Credint Holdings LLC in its discretion. The value shall be paid by Company to Employee within thirty (30) days of the closing of any liquidity event and [sic] the receipt of the proceeds of such liquidity event by Company, which ever is longer.

(Holter Affid., Exhibits B & C, Exhibit A). No such long-term incentive program, if developed, was ever offered to plaintiffs.

Both Employment Agreements provided that the plaintiffs would not be relocated out of the general vicinity of Somerset, Massachusetts absent mutual consent (*see id*. Exhibits B & C ¶ 8). Any disputes under the Employment Agreements were required to be submitted to arbitration (*see id*. ¶ 15.12).

Although the parties dispute whether the language of the Asset Purchase and Sale Agreement was negotiated among them, defendant does not deny, in its reply papers, plaintiffs' statement in their responding affidavit that the Employment Agreements were entirely drafted by defendant without any input by plaintiffs (*see* Plaintiffs' Affid. ¶ 11).

Gouchie was terminated for "cause," and therefore without severance benefits, on May 10, 2006 (*see* Complaint ¶¶25-27). The Somerset office was closed the same day and the business moved to Ohio; after Frankel had attempted to work out of his kitchen for some months, without support staff, he resigned (*see id.* ¶¶28-29, 31).

Plaintiffs filed their Complaint on August 23, 2007, and CIRM served its motion to dismiss in lieu of answering. Gouchie instituted a claim in arbitration with respect to his Employment Agreement; that claim was settled on October 2, 2007 (*see* Moore Reply Affid., Exhibit 1).

At oral argument on the motion to dismiss, the Court was informed that Frankel had served a notice of intent to arbitrate concerning his Employment Agreement.

DISCUSSION

(A) Standards on Motion to Dismiss

When considering a motion to dismiss based upon documentary evidence pursuant to CPLR 3211 (a) (1), the Court may grant the motion "where documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law" (*Held v Kaufman*, 91 NY2d 425, 430-431 [1998], quoting *Leon v Martinez*, 84 NY2d 83, 88 [1994]). In considering whether the plaintiff has stated a claim under CPLR 3211 (a) (7), the court must deny "[t]he motion . . . if from the pleadings' four corners 'factual allegations are discerned which taken together manifest any cause of action cognizable at law'" (*511 West 232nd Owners Corp. v Jennifer Realty Co.*, 98 NY2d 144, 151-152 [2002], quoting *Polonetsky v Better Homes Depot*, 97 NY2d 46, 54 [2001]). Further, the court must "liberally construe the complaint . . . and accept as true the facts alleged in the complaint and any submissions in opposition to the dismissal motion" (*511 West 232nd Owners Corp.*, 98 NY2d at 162 [internal citations omitted]). Nonetheless, "allegations consisting of bare legal conclusions, as well as factual claims inherently incredible or flatly contradicted by documentary evidence are not entitled to such consideration" (*Caniglia v Chicago Tribune-New York News Syndicate Inc.*, 204 AD2d 233, 233-234 [1st Dept 1994]).

(B) <u>Complaint</u>

The Complaint contains three causes of action. The first cause of action alleges that plaintiffs were induced by fraud to enter into the Agreements. The second cause of action alleges breach of fiduciary duties to plaintiffs by the majority shareholders of CIRM. The third cause of action is unidentifiable, but could be read to assert oppressive conduct by majority shareholders toward plaintiffs, a breach of contract or a failure of consideration.

(C) <u>First Cause of Action</u>

The first cause of action alleges that CIRM fraudulently induced plaintiffs to sell Abrams & Swartz, a collection agency worth $3,000,000, in exchange for five-year employment agreements and a $10,445 flat fee payment, by promising plaintiffs secure management positions in a new Commercial Division of defendant corporation, along with a ten percent equity interest in that division and a share of earnings from it (*see* Complaint ¶¶13, 17, 34-38).[2]

To maintain a cause of action for fraudulent inducement of contract, plaintiffs must prove the representation of a material existing fact, falsity, scienter, deception and injury (*see Century 21, Inc. v F.W. Woolworth Co.*, 181 AD2d 620, 625 [1st Dept 1992], citing *Channel Master Corp. v Aluminum Ltd. Sales*, 4 NY2d 403, 406-407 [1958]). In other words, plaintiffs must allege "a material representation, known to be false, made with the intention of inducing reliance, upon which [plaintiffs] actually relie[d], consequentially sustaining a detriment" (*Merrill Lynch, Pierce, Fenner & Smith, Inc. v Wise Metals Group, LLC*, 19 AD3d 273, 275 [1st Dept 2005]). Plaintiff also must prove that its reliance was reasonable (*see Orlando v Kukielka*, 40 AD3d 829, 831 [2d Dept 2007] [finding no reasonable reliance as a matter of law]).

Defendant contends first that plaintiffs have no separate cause of action for fraud because such a cause of action is duplicative of a claim for breach of contract. It is well-settled that a cause of action for fraud does not arise "when the only fraud charged relates to a breach of contract" (*Tesoro Petroleum Corp. v Holborn Oil Co.,* 108 AD2d 607 [1st Dept 1985], *appeal dismissed* 65 NY2d 637 [1985]). "To plead a viable cause of action for fraud arising out

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[2] At times in their papers, plaintiffs claim entitlement to ten percent of the stock of the entire defendant corporation, not merely of the Commercial Division. For purposes of the analysis here, the difference is irrelevant.

of a contractual relationship, the plaintiff must allege a breach of duty **which is collateral or extraneous to the contract** between the parties" (*Krantz v Chateau Stores of Canada, Ltd.*, 256 AD2d 186, 187 [1st Dept 1998] [emphasis supplied & internal quotation marks omitted]). In this case, however, the Complaint specifically alleges that defendant made promises before and after the execution of the written agreements that were **not** incorporated therein, i.e. that plaintiffs were guaranteed an equity interest in CIRM along with management responsibility and control (*see* Complaint ¶¶ 13, 17, 34-36).

Plaintiffs admit that they realized before signing any of the Agreements that the Asset Purchase and Sale Agreement "did not state that Abrams & Swartz Inc. was being acquired in exchange for ten percent equity ownership in [defendant]" (Complaint ¶ 13). However, the Complaint appears to allege that plaintiffs were induced to proceed with the sale and to execute the three Agreements because defendant's agent represented that their "investment" in exchange for a ten percent interest in the new Commercial Division of CIRM was completely "secure," because it was incorporated into the long term incentive provisions of the Employment Agreements (*id.*).

The documents, however, plainly do not secure such a right in plaintiffs. Rather, the Asset Purchase and Sale Agreement provides for the purchase of all of Abram & Swartz's collection accounts, office equipment, contracts, goodwill and leases, for a flat fee of $10,445 (*see* Asset Purchase and Sale Agreement § 2.1 & Schedules). Further, the Employment Agreements place complete discretion in defendant whether to establish a long term incentive program and whether to even award it to plaintiffs (*see* Holter Affid., Exhibits B & C, ¶ 6.2). The Employment Agreements provide only an "Illustration" of what plaintiffs might receive were such a program to be implemented, i.e. ten (10) percent of the "value" of the Commercial Division, but only upon an undefined "liquidity event" (*see* Holter Affid., Exhibits B & C, Exhibit A). The "Illustration" of the long term incentive program, the only mechanism under which plaintiffs would receive an equity interest in the new Commercial Division, does not require a transfer of stock to plaintiffs under any circumstances.

The Agreements also contradict the other representations allegedly made by defendants. To the extent plaintiffs allege they were entitled to "job security" (Complaint ¶ 35), the Employment Agreements, while providing for five-year terms, are terminable at will (Holter Affid., Exhibits B & C, ¶ 9.2). The allegations that plaintiffs were assured that they would "maintain control over the new Commercial Division" and have only certain supervisors (Complaint ¶ 4), are contrary to the language of the Employment Agreements, which state that plaintiffs will perform "such duties and responsibilities as may from time to time be reasonably assigned to Employee by the Company." (Holter Affid., Exhibits B & C, ¶ 2).

The Court determines that plaintiffs cannot as a matter of law establish the necessary reasonable reliance upon the alleged misrepresentations, because "where . . . an express provision in the written contract contradicts the claimed oral representations in a meaningful fashion, . . . the conflict between the provisions of the written contract and the oral representations negates the claim of reliance upon the latter" (*Bango v Naughton*, 184 AD2d 961, 963 [3rd Dept 1992] [motion to dismiss]; *accord C-Kitchen Associates Inc. v The Travelers Ins. Co*., 11 AD3d 961, 961-962 [4th Dept 2004] [summary judgment]). Here, as discussed above, the Agreements contradict in a clear and meaningful way the oral representations upon which plaintiffs seek to rely. Thus, even after accepting all of plaintiffs' allegations as true, the

Court must conclude as a matter of law that plaintiffs cannot establish reasonable reliance upon the alleged representations thereby negating a key element of their first cause of action. The motion is therefore granted as to the first cause of action.

(D) **<u>Second Cause of Action</u>**

The second cause of action alleges that the majority shareholders of CIRM owed a fiduciary duty to plaintiffs as minority shareholders. Although majority shareholders in so-called close corporations may owe minority shareholders a fiduciary duty (*see generally Richbell Information Servs., Inc. v Jupiter Partners, L.P.*, 309 AD2d 288 [1st Dept 2003]), the majority shareholders are not parties to the action. More importantly, it is undisputed that, regardless of what plaintiffs may have been orally promised, plaintiffs never obtained any shares of CIRM. Rather, the failure to transfer any ownership interest in CIRM to plaintiffs is the gist of the Complaint. Thus, plaintiffs are not shareholders, and therefore, fiduciary duties that may exist among shareholders are inapplicable in the current situation.

Even reading into the Complaint an allegation that CIRM as purchaser of plaintiffs' business, owed plaintiffs a fiduciary duty, the law would imply no fiduciary duty between the parties to the instant Agreements. An ordinary contractual relationship gives rise to no fiduciary duties (*see Mid-Island Hosp, Inc. v Empire Blue Cross and Blue Shield*, 276 F3d 123, 130 [2d Cir 2002], *cert denied* 537 US 882 [2002] [applying New York law]). Although plaintiffs' brief asserts that the contracts were not "at arms length", plaintiffs' Complaint alleges no basis for a special relationship of trust and confidence between CIRM and plaintiffs (*cf. Matter of Greiff*, 92 NY2d 341, 345-346 [1998] [relationship between parties to a prenuptial agreement]; *Matter of Gordon v Bialystoker Center*, 45 NY2d 692, 699 [1978] [relationship between nursing home and patient who transferred funds to home]), and plaintiffs' affidavit in opposition to the motion adds nothing on this point. Plaintiffs were owners of a business that CIRM sought to purchase; CIRM valued the business and decided to purchase it. No special relationship may be implied therein.

(D) Third Cause of Action

It is not entirely clear what the basis is for the third cause of action, which alleges that defendant "oppressed and defeated the plaintiffs' reasonable expectations that ownership in CIRM would entitle them to job security, a share of the corporate earnings, and a place in corporate management" (Complaint ¶ 45). The cause of action also asserts that defendant denied plaintiffs any return on their investment (*id.* ¶ 50). Defendant contends that, to the extent the third cause of action purports to assert a breach of contract of the Asset Purchase and Sales Agreement[3], that cause of action must be dismissed as a matter of law because plaintiffs have failed to allege a breach.

As noted earlier, reviewing the three Agreements in their entirety, they unambiguously do not obligate CIRM to transfer any ownership interest in CIRM to plaintiffs. The sole consideration for the asset purchase of Abrams & Swartz was the amount paid for the physical assets of $10,445 and the requirement that the parties enter into the Employment Agreements (*see* Asset Purchase and Sale Agreement §§ 7.11, 9.2 [c], [d]). "Mere assertion by one that contract language means something to him, where it is otherwise clear, unequivocal and understandable when read in connection with the whole contract, is not in and of itself

[3] As noted, any disputes under the Employment Agreements were required to be submitted to arbitration (*see* Employment Agreements ¶ 15.12).

enough to raise a triable issue of fact" (*Bethlehem Steel Co. v Turner Constr. Co.*, 2 NY2d 456, 460 [1957]; *see Goldman v Metropolitan Life Ins. Co.*, 5 NY3d 561, 571 [2005]).

If a party has discretion under the contract whether to perform a particular act, its failure to perform that act does not give rise to a breach of contract (*see Nikitovich v O'Neal*, 40 AD3d 300 [1st Dept 2007]; *DeSimone v Siena College*, 243 AD2d 1037 [3rd Dept 1997]). Plaintiffs have not raised any other basis for breach of the Asset Purchase and Sale Agreement.

Plaintiffs argue, however, that any interpretation of the Agreements that does not obligate CIRM to transfer stock to plaintiffs in exchange for the asset purchase renders the Asset Purchase and Sale Agreement an illusory contract (*see* Plaintiffs' Memo of Law at 4-6, citing *Ruppert v Secretary of U. S. Dept. of Health and Human Services*, 671 FSupp 151, 166 [EDNY 1987], *rev'd in part on other grounds*, 871 F2d 1172 [2d Cir 1989]). That is because, in plaintiffs' view, the essential purpose of the transaction was to sell plaintiffs' business for shares of CIRM.

The Court determines that, read together, the Agreements are not illusory (*see generally Apfel v Prudential Bache Securities Inc.*, 81 NY2d 470, 476 [1993]). "[T]he parties to a contract are free to make their bargain, even if the consideration exchanged is grossly unequal or of dubious value" (*see id*. at 475). The stated consideration for the Asset Purchase is $10,445 plus the five year Employment Agreements. Those Agreements, any disputes under which are subject to arbitration, are not illusory either. Although they permit termination of plaintiffs' employment at defendant's option at any time with or without cause, they also require defendant to make severance payments if plaintiffs are terminated without cause prior to the end of the fifth year, the total of which payments diminish the longer the employment lasts (*see* Holter Affid., Exhibits B & C, ¶ 10). "Absent fraud or unconscionability, the adequacy of consideration is not a proper subject for judicial scrutiny" (*Apfel*, 81 NY2d at 476, citing *Spaulding v Benenati*, 57 NY2d 418, 423 [1982]). For the foregoing reasons, the third cause of action must be dismissed.

Defendant shall submit an Order and Judgment on notice to plaintiffs.

DATED: March 28, 2008

HON. JOHN M. CURRAN, J.S.C.