SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: O. PETER SHERWOOD
Justice

PART 49

MMS USA HOLDINGS, INC.,

Plaintiff,

-against-

PRICEWATERHOUSECOOPERS LLC,

Defendant.

INDEX NO. 650382/2012

MOTION DATE Jan. 3, 2013

MOTION SEQ. NO. 002

MOTION CAL. NO. ______

The following papers, numbered 1 to ______ were read on this motion to dismiss the first amended complaint

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
Answering Affidavits — Exhibits	
Replying Affidavits	

Cross-Motion: ☐ Yes ☑ No

Upon the foregoing papers, the motion of defendant PricewaterhouseCoopers LLC for an order, pursuant to CPLR § 3211 (a) (5) and (7), dismissing the first amended complaint is decided in accordance with the accompanying decision and order.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: 3/19/13

O. P. Sherwood

O. PETER SHERWOOD, J.S.C.

Check one: ☑ FINAL DISPOSITION ☐ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

☐ SUBMIT ORDER/ JUDG. ☐ SETTLE ORDER/ JUDG.

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 49
--X

MMS USA HOLDINGS, INC.,

Plaintiff,

-against-

PRICEWATERHOUSECOOPERS LLP,

Defendant.

--X

DECISION AND ORDER

Index No. 650382/12

Mot. Seq. No. 002

O. PETER SHERWOOD, J.S.C.:

Defendant PricewaterhouseCoopers LLP (PWC) moves, pursuant to CPLR 3211 (a) (5) and (7), to dismiss plaintiff MMS USA Holdings, Inc.'s (MMS) first amended complaint, which seeks damages for alleged negligence and professional malpractice and breach of fiduciary duty, as well as punitive damages.

BACKGROUND

The facts are taken from the complaint, inasmuch as those facts must be accepted as true for purposes of this motion. MMS is a Delaware corporation which is a subsidiary of Publicis Groupe S.A. (Publicis), organized under the laws of France. On September 24, 2002, Publicis acquired a network of U.S. and international advertising companies. Publicis created Philadelphia Merger Corp. (Merger) for the purpose of owning those entities. Publicis then wished to consolidate Merger's non-U.S. subsidiaries with its own non-U.S. subsidiaries. Publicis worked with PWC to develop internal reorganizations whereby most of the foreign subsidiaries of Merger were transferred to foreign affiliates of Publicis. The subsidiaries were transferred to a Dutch holding company, now known as Publicis Groupe Holdings B.V. (BV), which already held most of Publicis's non-U.S. and non-French subsidiaries. The French subsidiaries were transferred to a French holding company. However, several of the foreign subsidiaries could not be transferred to BV in 2002.

On January 2, 2005, Merger changed its name to MMS. On November 27, 2005, MMS merged with and into Leo Burnett Worldwide, Inc., and the combined entity took the name MMS.

Beginning in 2000, MMS used PWC as its tax advisor. PWC prepared approximately 600 disclosures under the Internal Revenue Code of 1986, as amended (the Code), specifically with respect to section 367 (a) (Section 367), including: gain recognition agreements (GRAs); Forms 8838, entitled "Consent to Extend the Time to Assess Tax Under Section 367 - Gain Recognition Agreement" (Consent Form); and annual certifications that were filed with MMS's consolidated tax returns for tax years 2002 through 2007. Such filings were required under Section 367 in order to establish and maintain eligibility for certain exceptions to the recognition of tax gain. Included in its role, PWC advised MMS on the tax consequences of their cross-border transactions, and MMS relied on PWC with respect to whether and when a GRA was required, as well as for its preparation, and the preparation of Consent Forms and annual certifications.

In 2007, Publicis identified certain foreign subsidiaries of MMS to transfer to BV. Initially, the U.S. companies transferred their interests (US Interests) to a U.S. company, U.S. International Holding Company, Inc. (US Holding). On October 25, 2007, US Holding transferred the US Interests to a subsidiary of BV, Publicis Holding BV (Holdings BV) in exchange for Holding BV's common shares. This exchange was intended to fall within a non-recognition provision of Section 367. Holding BV then immediately transferred the US Interests to BV, in transactions intended to qualify as tax-free reorganizations under the Code.

PWC agreed to advise Publicis and MMS on the tax consequences of these exchanges pursuant to the Code, and the subsequent transfer to BV. PWC worked with Publicis and MMS to develop the plan for the exchange and transfer, provided instructions regarding the steps required to implement the plan, and described the tax consequences of the proposed exchange and transfer in a memorandum dated June 28, 2007 (the 2007 Memorandum). There was no separate engagement letter between MMS and PWC regarding this work.

PWC knew that MMS sought to accomplish these transfers only if they were eligible for tax-free treatment. One of the entities with respect to which the transfer was sought was Starcom Philippines (Starcom). PWC failed to inform MMS prior to the October 25, 2007 exchange that a transfer of the interest in Starcom would not be eligible for tax-free treatment. Hence, MMS engaged in that transfer. PWC also failed to inform MMS prior to the transfer that, upon the transfer of the US Interests to Holdings BV, MMS would be liable for taxes on the earnings accumulated by certain of the foreign subsidiaries involved in the transfer. MMS maintains that, had it been properly informed, it would not have engaged in the transfers. MMS contends that PWC was aware that the failure to properly advise it about the eligibility of subsidiaries' accumulated earnings for tax-free treatment would directly result in MMS transferring the shares, and consequently, in millions of dollars in increased tax liability for MMS.

The 2007 Memorandum also provided that PWC would prepare GRAs to the extent that they were required, and that PWC would determine which GRAs were required. MMS relied on PWC to prepare and supply it with the appropriate forms to be included as part of MMS's tax filing on September 15, 2008, for tax year 2007. However, PWC failed to prepare or provide the necessary GRAs. MMS first discovered this omission on October 1, 2008, at which time PWC agreed to review the transfers and to determine whether GRAs had been required. PWC determined that five entities were eligible for the GRA exception, including Starcom. PWC said it would seek (without charge to MMS) to have the transfer of interests not be treated as a taxable exchange on the ground that the failure to file the GRAs was for reasonable cause, and not willful neglect. PWC did not file that necessary request until May 4, 2009, over seven months after MMS discovered PWC's failure to provide the necessary forms. Further, PWC initially failed to take responsibility for the omission. MMS states that the IRS would give significant weight to an admission from PWC that MMS had justifiably relied on PWC to prepare any necessary GRAs.

In September 2009, PWC sent the IRS a letter as an addendum to the request for reasonable cause. In it, PWC also notified the IRS that the transfer with respect to Starcom was not eligible for the GRA exception to Section 367. Thus, the transfer resulted in a triggering event leaving MMS liable for taxes for the realized gain, which liability was approximately $950,000.

The IRS refused to grant reasonable cause relief because it was the second time that MMS had requested such relief for the failure to file GRAs. The prior failure to file GRAs was in connection with the 2002 reorganization, and was as a result of PWC's advice at that time. PWC had previously assured MMS that the IRS would likely grant the relief because MMS disclosed the failure to file prior to detection, and because it was an honest mistake.

In 2010, MMS became aware that PWC failed to prepare at least 10 annual certifications for certain transferred companies during tax years 2003 through 2007.

Publicis and its subsidiaries entered into an agreement with PWC to toll any statute of limitations from September 10, 2010 until March 15, 2011,

> "pertaining to any claim or defense concerning PwC's representation of, and provision of tax services to, PGSA in connection with the preparation and filing of (1) Section 367 disclosures (including, but not limited to, gain recognition agreements and associated and related documents such as Forms 8838, annual certifications and reasonable cause filings) (hereinafter 'Section 367 Disclosures') with respect to the October 2007 transfer of shares in eight non-U.S. subsidiaries to Publicis Holdings B.V., a company organized under the laws of the Kingdom of the Netherlands, and (2) annual certifications and notices of transfer with respect to the transactions listed on Attachment A hereto which may have been required to be filed with PGSA's U.S. federal tax returns for tax years 2003, 2004, 2005, 2006, 2007, and 2008..."

Affirmation of McLean, exhibit C, at 1, ¶ 2.

MMS claims that, as a result of PWC's failures, it was required to report additional capital gains relating to four of the exchanges, incurring additional tax liability of $30.2 million plus interest. Had MMS known that it would be liable for these taxes, it would not have transferred the shares in the subsidiaries, thereby avoiding at least $4 million of liability attributable to their accumulated earnings, and $6.9 million of liability caused by PWC's failure to prepare GRAs.

MMS sets forth two causes of action. The first is for negligence and professional malpractice, based upon PWC's failure to live up to its touted expertise in tax planning, by failing to exercise due professional care in rendering tax advice and services in connection with determining the need for GRAs, and preparing those that were needed and timely delivering them to MMS for filing. Additionally, MMS maintains that PWC did not exercise due professional care in seeking a determination from the IRS that the failure to file the GRAs was due to reasonable cause. MMS further contends that PWC did not fulfill its duty to advise MMS regarding the transfer of an interest in Starcom, by neglecting to advise MMS that the transfer would be ineligible for tax-free treatment.

The second cause of action asserts a claim for breach of fiduciary duty. MMS contends that PWC breached its fiduciary duty to MMS in not exercising due care and diligence in the performance of its duty to render tax advice, and then failing to act in good faith in the sole interest of MMS when seeking a determination from the IRS that the failure to file the GRAs was due to reasonable cause. By delaying the letter to the IRS for over seven months, and then neglecting to properly accept responsibility for the omission of the GRAs, PWC was allegedly protecting its own interests rather than securing MMS's position. MMS additionally contends that PWC breached its fiduciary duty in failing to provide proper information and tax advice regarding Stardom. Had PWC properly advised MMS, MMS would not have engaged in the transfer, and would not have incurred the tax obligation.

MMS seeks actual, compensatory, incidental and consequential damages of over $35 million. It also seeks punitive damages, costs and disbursements, including attorneys' and experts' fees, and interest.

DISCUSSION

Recoverable Damages

PWC contends that MMS is seeking consequential damages, consisting of capital gains tax for the GRAs claim, capital gains tax for the Starcom transfer, taxes on accumulated earnings, and punitive damages, none of which are recoverable. MMS responds that it is not seeking consequential damages, and that it does not set forth a breach of contract claim, therefore, PWC's argument, which is based upon the standard used for breach of contract, is without merit.

MMS avers that the tax liability that it faced as a result of PWC's failure to execute its plan by preparing GRAs for the 2007 tax year is "the natural and probable consequence of the breach" by PWC, and, therefore, constitutes general damages rather than consequential damages. *Kenford Co. v County of Erie,* 73 NY2d 312, 319 (1989) (*Kenford II*). Such damages are not subject to the pleading requirements for consequential damages. *Bi-Economy Mkt., Inc. v Harleysville Ins. Co. of N.Y.,* 10 NY3d 187, 192 (2008); *American List Corp. v U.S. News & World Report,* 75 NY2d 38, 42-44 (1989); *Estate of Coppersmith v Blue Cross & Blue Shield of Greater N.Y.*, 177 AD2d 373, 374 (1st Dept 1991).

MMS emphasizes the differences in the situation between this case and *Kenford II.* Here, MMS engaged the services of PWC to create and implement a plan to minimize tax consequences. PWC failed to implement the plan, resulting in MMS having to discharge a tax obligation that PWC's plan was designed to avoid. In *Kenford II*, on the other hand, the plaintiff sought damages from the county for the anticipated appreciation in the value of land that it had bought near a proposed stadium when the proposal for the stadium collapsed. *Kenford II*, 73 NY2d at 318. The county had not made its plans for the plaintiff's benefit, nor did it structure the plaintiff's real estate purchase. Thus, the two cases are not analogous.

In reply, PWC states that taxes are in the nature of consequential damages, even if they were directly caused by PWC's allegedly faulty tax services. Consequential damages are damages "which [special] circumstances make probable, though apart from such circumstances they would be unusual." *Czarnikow-Rionda Co. v Federal Sugar Ref. Co.*, 255 NY 33, 42 (1930) (internal quotation marks and citation omitted). The general damages, thus, are the fees paid for the allegedly improper service, whereas the tax consequences, which resulted from MSS's dealings with the tax authorities rather than with PWC, are consequential damages.

There is authority that holds that damages resulting from the client's dealings with a third party, as opposed to with the defendant, constitute consequential damages rather than general damages. *See e.g. 437 Madison Ave. Assoc. v A.T. Kearney, Inc.*, 127 Misc 2d 37, 38-39 (App Term, 1st Dept 1985). However, even if a third party is not involved, general damages refer to damages based upon the value of performance, not on the value of the consequences of that performance, or the failure to perform. *See* Dan B. Dobbs, Remedies § 12.4 (1) (2d ed 1993) (Consequential or special damages "are distinguished from general damages, which are based on the value of the performance itself, not on the value of some consequence that performance may produce"). As a result, the damages that MMS seeks are consequential damages, not general damages.

MMS contends that it is bringing a negligence and malpractice cause of action, not an action for breach of contract, and, therefore, the standards applied to breach of contract actions are not applicable. However, the standards for recovering for a malpractice action use the same standards as those set forth in *Kenford II*. *See Crystal Clear Dev., LLC v Devon Architects of N.Y., P.C.*, 97 AD3d 716, 718 (2d Dept 2012) (consequential damages disallowed under both the contract cause of action and the professional malpractice cause of action). Indeed, as pointed out by PWC, without the contractual relationship between the parties, there would be no duty to serve as a basis for the tort of malpractice. *Pilewski v Solymosy*, 266 AD2d 83, 85 (1st Dept 1999). Thus, MMS has failed to adequately plead a basis to recover the consequential damages that it incurred.

Taxes as Damages

PWC contends that New York law does not recognize taxes as recoverable damages, and that, therefore, MMS cannot recover taxes or tax interest in a tort lawsuit. *Menard M. Gertler, M.D., P.C. v Sol Masch & Co.*, 40 AD3d 282, 283 (1st Dept 2007). The reason for the rule is that the taxes did not result from the alleged misrepresentation or actions of the defendant, but from the taxable events in which the taxpayer engaged. *Fownes Bros. & Co., Inc. v JPMorgan Chase & Co.*, 92 AD3d 582, 583 (1st Dept 2012). Further, recovery will not be allowed where it would result in a windfall to the plaintiff. For example, if the taxable event for which it seeks to recover damages would mean that it could later make use of the stepped up basis of that asset, and transfer or distribute it without incurring a subsequent tax liability. Reimbursing tax liability so that the plaintiff would be in a better position than if he had not engaged in the transaction is not permitted. *Gaslow v KPMG LLP*, 19 AD3d 264, 265 (1st Dept 2005). PWC also points out that the tax advantage that MMS sought in these transactions would not have avoided the tax entirely, but merely deferred it.

MMS argues that taxes are sometimes recoverable against accountants, particularly when the client would not have incurred the tax liability but for the error of the tax professional. MMS maintains that PWC is speculating about a later disposition of the assets when it asserts that MMS will benefit from having paid the taxes. However, MMS asserts that there is no reason to speculate that another corporate action, that would have caused MMS to incur the same tax liability, was inevitable. Rather, the court should recognize that MMS sought, and paid for, tax advice because it would have reaped a significant benefit had PWC abided by its obligation to implement the plan it had advised MMS to follow.

While there is no question that MMS had sought to defer its tax liability, and that, accepting the allegations as true, PWC failed to implement the strategy that would have resulted in such benefit, MMS has not adequately pleaded that there would be no windfall to it if it were to recover damages in the form of reimbursement of its tax liability. MMS does not deny that it now has a stepped up basis in the assets, and were it to transfer them, it would benefit from having that stepped up basis. The fact that it may not choose to do so does not alter the fact that it would be in a better position, were it to recover the sought after damages, than it would have been had the transactions not taken place. Under these circumstances, recovery of the taxes paid is not permitted. *Gaslow*, 19 AD3d at 265.

<u>Breach of Fiduciary Duty</u>

PWC maintains that, in addition to MMS's failure to allege recoverable damages, the breach of fiduciary duty cause of action should be dismissed as duplicative of the malpractice claim, and because MMS failed to allege facts to support a finding that PWC had a fiduciary duty to MMS.

A cause of action asserting a breach of fiduciary duty is duplicative of a cause of action for malpractice where it is based upon the same set of facts, and seeks the same damages. *X Cosmetics Plus Group, Ltd. v Traub*, ___ AD3d ___, 2013 WL 709302, *6 (1st Dept 2013). MMS argues that the breach of fiduciary duty claim is not duplicative of the malpractice claim because they focus on different aspects of PWC's failures. The malpractice claim is based upon PWC's failure: to determine whether there was a need for GRAs, and to prepare and timely deliver them to MMS; to determine that the transfer of an interest in Starcom would not be eligible for tax-free treatment; and to advise MMS that the transfer of the US Interests would cause MMS to be liable for taxes on earnings accumulated by the foreign subsidiaries. The breach of fiduciary duty claim is based upon PWC allegedly not acting in MMS's interest in seeking a determination from the IRS that the failure to file the GRAs was due to reasonable cause.

While MMS seeks to make this distinction in its opposing papers, its complaint does not. In fact, MMS refers to all of the alleged wrongs by PWC in both causes of action. Therefore, the breach of fiduciary duty is duplicative of the malpractice cause of action.

The court also notes that, in order to support the cause of action for breach of fiduciary duty based solely on PWC's failure to timely seek reasonable cause relief, MMS would have to show that, but for PWC's delay in acknowledging that MMS had acted reasonably and in good faith in relying on PWC in failing to provide GRAs, the IRS would have granted such relief. MMS has not offered any factual allegations to support such a conclusion. In fact, since PWC ultimately did provide the letter, and the IRS denied the relief due to MMS's "serial offender" status rather than due to MMS's delay in seeking relief, MMS has set forth factual allegations that would require dismissal of the breach of fiduciary claim.

In addition, PWC asserts that MMS fails to allege that MMS had anything other than an ordinary accountant/client relationship. Such a relationship is not a fiduciary relationship. The fact that PWC had expertise that MMS did not have does not convert the relationship to that of a fiduciary. *RNK Capital LLC v Natsource LLC*, 76 AD3d 840, 842 (1st Dept 2010); *Batas v Prudential Ins. Co. of Am.*, 281 AD2d 260, 264 (1st Dept 2001). Otherwise, any professional expertise would qualify as a fiduciary relationship, and all accountants, attorneys, or any other professionals would automatically be subject to fiduciary status.

Here, PWC is not alleged to have been an investment advisor to MMS, but only a tax advisor. MMS has failed to cite any support for its proposition that such a relationship suffices to create a fiduciary relationship. The cases that it cites are inapposite. *DeRossi v Rubinstein*, 233 AD2d 220, 221 (1st Dept 1996) (question of fact whether neophyte investor's reliance on the defendant for tax and investment advice created fiduciary relationship); *Lavin v Kaufman, Greenhut, Lebowitz & Forman*, 226 AD2d 107, 108-109 (1st Dept 1996) (accountant provided investment services knowing that the plaintiff would follow his advice, and placed her investment at risk while protecting other clients); *Herbert H. Post & Co. v Sidney Bitterman, Inc.*, 219 AD2d 214, 225 (1st Dept 1996) (accountant acted simultaneously as a tax shelter investment advisor).

Consequently, even had MMS adequately pleaded recoverable damages, the breach of fiduciary duty claim would, nonetheless, be dismissed.

<u>Starcom Claims</u>

PWC maintains that the claims regarding Starcom and the accumulated earnings are time-barred. Those claims are subject to a three-year statute of limitations, regardless of how they are denominated, because they are accounting malpractice claims. *Ackerman v Price Waterhouse*, 84 NY2d 535, 541 (1994). That period begins to run upon the client's receipt of the work product. *Id.* These claims are based upon PWC's alleged failure to inform MMS of the tax consequences prior to the transfer of October 25, 2007. This action was not filed until February 2012. Therefore, far more than three years elapsed.

PWC disputes MMS's position that the tolling agreement that it entered into with MMS applies to Starcom or to the accumulated earnings claim. MMS seeks to have the court read the tolling agreement broadly, arguing that the advice regarding Starcom and the accumulated earnings "cannot be teased apart from the advice on GRAs." Memorandum in opposition at 24.

The tolling agreement must be construed in accordance with its language. It is, by its terms, limited to the provision of tax services in connection with the preparation and filing of Section 367 disclosures, and the annual certifications and notices of transfer which may have been required. Neither the Starcom transaction, which was not eligible for Section 367 treatment, nor the accumulated earnings, which were also not eligible for Section 367 treatment, are covered by the tolling provision.

MMS argues that, in any event, the doctrine of continuous representation should apply. Since MMS was still receiving services from PWC with respect to these transactions, at least until the final determination of the IRS in September 2010, the statute of limitations did not begin to run until that time. *Williamson v PricewaterhouseCoopers LLP*, 9 NY3d 1, 8 (2007).

PWC avers that the continuous representation doctrine does not apply with respect to Starcom and the accumulated earnings, since the corrective action that PWC was attempting was not with respect to those transactions.

In order for continuous representation to apply, the services that PWC was providing would have to be with respect to the particular problem giving rise to the claims, not merely a continuing professional relationship. *Id.* at 11; *see also Apple Bank for Sav. v PricewaterhouseCoopers LLP*, 70 AD3d 438, 438 (1st Dept 2010). Here, PWC was involved in a continuing relationship with respect to seeking reasonable cause relief regarding the GRAs. However, its services during this time were not addressed to corrective measures regarding either the Starcom transaction, or the accumulated earnings. Thus, the Starcom claim and the accumulated earnings claim are not affected by PWC's later actions. Consequently, those claims are time-barred.

Punitive Damages

PWC seeks to dismiss the claim for punitive damages, arguing that MMS cannot demonstrate that its conduct was "intentional and deliberate, and has the character of outrage frequently associated with crime." *Prozeralik v Capital Cities Communications*, 82 NY2d 466, 479 (1993) (internal quotation marks and citation omitted). There is no allegation in the complaint that PWC's conduct was deliberate and intentional, or malicious, or actuated by reprehensible or evil motives. *Apple Bank for Sav. v PricewaterhouseCoopers LLP*, 70 AD3d at 438.

MMS counters that punitive damages may be sought where the conduct was deliberate, reprehensible, improperly motivated, wantonly dishonest and outrageous. *Ross v Louise Wise Servs., Inc.*, 8 NY3d 478, 489 (2007). MMS maintains that it has pled this adequately, particularly with regard to PWC's failure to seek reasonable cause relief from the IRS for over seven months following the discovery of its failure to prepare the GRAs required.

At this stage of the litigation, if there were a viable claim for negligence or malpractice, or for breach of fiduciary duty, it would be premature to dismiss this request, despite the difficulty in proving the requisite standard. If the finder of fact were to find that PWC failed to seek reasonable cause relief for dishonest reasons, it is possible that MMS would be entitled to punitive damages.

Such relief could only be granted, of course, if there were a cause of action surviving on which the punitive damages could rest. Here, there is no such surviving claim. Therefore, the request for punitive damages is also dismissed.

CONCLUSION

Accordingly, it is hereby

ORDERED that the motion of defendant PricewaterhouseCoopers LLP to dismiss the complaint is **GRANTED**, and the complaint is **DISMISSED** with costs and disbursements, as taxed by the Clerk of the Court, and the Clerk is directed to enter judgment accordingly.

DATED: 3/19/13

ENTER,

O. P. Sherwood

O. PETER SHERWOOD
J.S.C.