THE COMMERCIAL DIVISION LAW REPORT

A report on leading decisions issued by the Justices of the Commercial Division of the Supreme Court of the State of New York

Hon. Jonathan Lippman
Chief Judge of the State of New York

Hon. Ann Pfau
Chief Administrative Judge of the State of New York

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Arbitration; Federal Arbitration Act; scope of arbitration clause; effect of merger clause, choice of law clause, and forum selection clause; due process. Petitioner commenced the instant proceeding to confirm an arbitration award, and respondent cross-petitioned to vacate the award. Respondent argued that the arbitrator had exceeded his authority by interpreting the validity and scope of a release and settlement agreement entered into by the parties. The court rejected this argument. Even though the settlement agreement itself did not contain an arbitration clause, the court held that the arbitrator nonetheless had the authority to determine the validity and scope of the release because respondent had asserted claims under a prior contract that contained a valid arbitration clause. The court explained that where a contract includes a valid arbitration clause, the effect of a later settlement on a claim brought under the initial contract is for the arbitrator to determine. Moreover, the court held that the arbitration clause in this case, which broadly applied to "any dispute arising out of, or relating to" the parties' agreement, presumptively applied to the later settlement agreement because the settlement agreement implicated the parties' rights under the prior contract. The court found that respondent failed to rebut this presumption. The court explained that neither the merger clause nor the choice of law clause contained in the settlement agreement was inconsistent with the parties' prior agreement to arbitrate. Additionally, the court rejected respondent's reliance upon a dispute resolution clause in the settlement agreement, which provided that any legal proceeding arising out of or relating to the settlement agreement "will be brought in a United States District Court, or absent federal court jurisdiction, in a state court of competent jurisdiction." While this provision would govern in the event that both parties waived arbitration, the court held that it was not inconsistent with the parties' broad agreement to arbitrate all disputes. Finally, the court rejected respondent's argument that the arbitration was fundamentally unfair even though the arbitrator had failed to compel petitioner to produce certain documents and also limited the amount of time provided for the examination of the witnesses. Qwest Communications Company, LLC v. Geo-Group Communications, Inc., Index No. 651640/2010, 2/22/11 (Gammerman, J.H.O.).

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Banking; UCC 4-406; forgery; duties of bank and customer; statute of limitations. Defendant bank held two promissory notes executed by plaintiff corporation. Invoking a provision in the notes that permitted it to demand payment in full upon the occurrence of an event that, in the bank's judgment, adversely affected plaintiff's ability to repay its indebtedness, the bank declared plaintiff in default after plaintiff's bookkeeper was arrested for embezzlement. Plaintiff brought this action against the bookkeeper and the bank, alleging that it was the victim of fraud and forgery. Plaintiff alleged that the bookkeeper was not an authorized signatory on the account, yet the bank permitted her to improperly draw down on the line of credit and write forged checks. Plaintiff argued that the bank failed to utilize reasonable commercial standards or exercise ordinary care and sought a declaratory judgment that the bank was barred from enforcing any claim against it. The bank counterclaimed to recover the amounts due under both notes. The bank moved for summary judgment on its counterclaims and to dismiss plaintiff's claims. The court granted the motion. The court explained that under UCC 4-406, which sets forth a customer's and a bank's reciprocal duties of care, a customer must exercise reasonable care and promptness in examining account statements for forgery or fraud. A customer who fails to comply with these duties is barred from asserting a claim against the bank unless he or she can show that the bank failed to take ordinary care in paying an item. Although UCC 4-406(4) requires that any claim by a customer based on an altered or unauthorized signature must be brought within one year from the time the statement and item are made available to the customer, the court found that, in this case, the parties contracted to shorten the one-year time limit to 14 days. Because there was no dispute that plaintiff had failed to notify the bank of the forgery or fraud within 14 days of receiving its monthly statements, the court found that plaintiff's claims against the bank were time barred. Clemente Bros. Contracting Group. v. Hafner-Milazzo, Index No. 21385/2010, 2/8/11 (Emerson, J.).**

Contempt for failure to comply with a subpoena duces tecum and ad testificandum; Breach of contract, attorney's fees. Plaintiffs entered into a lease agreement with defendant for property in Queens that defendant intended to use for the retail sale of home and home office furniture. Plaintiffs brought suit against defendant, alleging that defendant had unjustifiably refused to accept either the tender of the subject premises or plaintiffs' assurances that the premises was available for occupancy pursuant to the lease agreement and applicable law. Defendant counterclaimed for breach of contract, alleging, inter alia, that plaintiffs had failed to provide the required occupancy certificates. Defendant also sought to recover, in a second counterclaim, attorney's fees, costs, and expenses pursuant to the lease agreement. Plaintiffs moved for summary judgment on the issue of liability on their breach of contract claim; defendant cross-moved for summary judgment on its counterclaims. The court denied plaintiffs' motion, granted defendant's cross-motion as to breach of contract, but denied the cross-motion as to attorneys' fees. It held that the Temporary Occupancy Certificate obtained by plaintiffs did not permit defendant to lawfully conduct retail sales

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"throughout the premises" as required by the lease agreement. Specifically, the Temporary Occupancy Certificate required that plaintiffs provide off-site accessory parking, which they did not do. Therefore, plaintiffs' statement that the conditions precedent to defendant' taking occupancy of the premises had been met constituted an anticipatory breach of the lease agreement. Correspondingly, defendant properly terminated the lease. The court denied defendant's cross-claim for attorneys' fees, holding that the relied-upon provision in the lease agreement was a "contractual indemnification clause" that did not authorize the recovery of attorneys' fees. Specifically, in that clause, plaintiffs had agreed to indemnify, defend, and hold harmless defendant upon plaintiffs' failure to comply with certain obligations under the lease agreement, "including attorneys' fees and disbursements incurred or suffered, by reason of any breach, violation, or nonperformance by plaintiffs." The court, however, held that the breach created only a right to terminate the lease agreement, which defendant had done. The court noted that there was no other provision in the lease providing for the recovery of attorney's fees, costs, and disbursements based upon a failure to make the premises available for occupancy. 84-16 Queens Boulevard Realty Corp. v. Furniture Company, Inc., Index No. 700054/09, 3/9/11 (Grays, J.).**

Contract; breach; frustration of purpose; CPLR § 3211(a)(1) and (a)(7). Plaintiff had entered into a written agreement with defendant to act as defendant's financial advisor and investment banker in connection with the proposed sale of certain student loan "toxic assets." The agreement entitled plaintiff to collect certain success fees if: (1) defendant sold the student loan assets to a party that had been introduced to defendant by plaintiff; or (2) plaintiff had not introduced the purchaser of the student loan assets to defendant but had performed substantially all of the services set forth in the agreement. Shortly after the parties entered into the agreement, the Swiss National Bank responded to the worldwide financial crisis by announcing the creation of a special fund entity (the "Stabilization Fund"). Defendant subsequently reached an agreement with the Swiss National Bank to transfer the student loan assets and other illiquid securities to the Stabilization Fund. Plaintiff thereafter brought the instant action for breach of contract and breach of the duty of good faith and fair dealing, claiming that the transfer of the student loan assets to the Stabilization Fund triggered its right to collect success fees under the parties' agreement. Defendant moved for an order dismissing the complaint on the ground that the purpose of the parties' agreement was frustrated when the Swiss National Bank created the Stabilization Fund. Plaintiff asserted that dismissal was premature because there were factual disputes relating to whether defendant's conduct necessitated the actions taken by the Swiss National Bank, whether the actions taken by the Swiss National Bank were anticipated by defendant, and whether the transaction with the Stabilization Fund was compelled by the Swiss government. The court granted defendant's motion, concluding that there was no question of fact as to whether the purpose of the parties' agreement had been frustrated. Specifically, the court found that the creation of the Stabilization Fund as the "result of the unprecedented worldwide financial events which occurred in September and October 2008 constituted an unforeseeable event which undermined the basic assumption and purpose of the . . . Agreement." Morpheus Capital Advisors LLC v. UBS AG, Index No. 650335/2009, 1/3/11 (Kapnick, J.).

Contract; breach; stock purchase; subscription agreement=s warranty of no differing agreement; sufficient internal accounting controls. Failure to plead damages. Negligent and fraudulent misrepresentation. Securities fraud by law firm partner. A criminal conspiracy to commit securities fraud gave rise to this uncertified class action. Corporate defendant had issued securities through a $12,250,000 private placement, and plaintiff had bought units. Investors were to receive unregistered, restricted securities they could not sell until the stock was registered. Corporate defendant represented in the subscription agreement that it "did not have any agreement...with other purchasers of the Units...on terms that differ substantially from those set forth in this Agreement." The defendant also represented the adequacy of its internal accounting controls. After the placement, the defendant had announced its inquiry into improper conduct by a former partner of the law firm representing it in the placement: the partner had caused shares of corporate defendant's stock to be issued without restrictive legends to entities he controlled and sold 1,500,000 of them publicly. According to plaintiff, the former partner's illegal conduct had caused the price of defendant's common stock and the value of warrants issued in the placement to fall. Plaintiff, seeking rescission and damages, sued corporate defendant for breach of contract and negligent and fraudulent misrepresentation and sued the law firm and former partner for tortious interference with contract. Plaintiff alleged that former partner defendant was an agent of the other defendants, that his misconduct had caused securities to be issued differing from those issued to plaintiff, that consequently the agreement's representation of "no additional agreements" amounted to negligent and fraudulent misrepresentation, and that the issuance of the unrestricted stock was a breach of warranty. Plaintiff further asserted that the corporate defendant had breached the warranties stating that its internal accounting controls were sufficient. Plaintiff's complaint relied in part on SEC filings in which corporate defendant had disclosed, among other things, criminal and civil SEC investigations of the former partner and his entities, as well as the allegations in the SEC complaint. It also alleged that corporate defendant had identified its own ineffective disclosure controls, including inadequate accounting staff and numerous weaknesses of financial reporting. Both the corporate defendant and the law firm moved to dismiss the complaint. The court found, even granting plaintiff every possible favorable inference, that plaintiff did not establish that corporate defendant had any differing agreement when the subscription agreement became effective. Indeed, the purported SEC allegations included that former partner defendant's entities had agreed to receive shares with restrictive legends, but that the former partner had issued an opinion letter that caused them to receive unrestricted securities. At best, the court said, plaintiff alleged that the former partner's entities had violated the no transfer agreements with corporate defendant. Claims that corporate defendant had breached its warranty of sufficient internal accounting controls failed, since plaintiff did not connect the lack of controls to the missing restrictive legends that allegedly led to its injury, and thus failed to plead a breach that was the proximate cause of an injury. Since no claim was stated for breach, the court did not need to decide whether the partner defendant's illegal acts should be imputed to corporate defendant on an agency theory. And since no differing agreement was sufficiently alleged, there was no basis for claiming negligent or fraudulent misrepresentation. The claim for negligent misrepresentation also was deficient because plaintiff failed to allege with particularity the requisite elements: a privity-like relationship, incorrect information, and reasonable reliance. The rescission claim, based on the insufficiently pled alleged misrepresentations, was also dismissed. The claim against law firm and former partner defendants for tortious interference with contract was dismissed based on plaintiff's failure to state a breach of contract claim. Sunrise Equity Partners, LP v. Betawave Corp., Index No. 602955/2009, 2/25/11 (Kornreich, J.).

Contract; indemnification agreements; breach; interpretation. Procedure; summary judgment. Declaratory judgment. Attorneys' fees and costs. Plaintiff holding company had acquired the plaintiff subsidiary companies from defendant pursuant to a Purchase Service Agreement ("PSA"). Under the PSA, defendant was required to indemnify plaintiffs for all "Covered Losses" relating to third-party claims brought against the plaintiff subsidiary companies. The PSA excused defendant from its indemnity obligation if plaintiffs failed to use their "commercially reasonable efforts to mitigate any Covered Losses." Plaintiffs sued for breach of contract and for a declaratory judgment, alleging that defendant had breached the PSA by refusing to indemnify them for the amount paid to settle an arbitration proceeding brought against one of plaintiff subsidiary companies. Defendant asserted counterclaims alleging that by funding escrow accounts sufficient to ensure that the plaintiff subsidiary companies could cover any claims made against them, the plaintiff holding company had failed to use commercially reasonable efforts to mitigate defendant's exposure. Plaintiffs moved for summary judgment, and the court granted the motion. As an initial matter, the court rejected defendant's claim that summary judgment was premature. Although defendant argued that it was entitled to take discovery regarding the negotiations leading up to the execution of the PSA, the court held that the indemnification provision in the PSA was unambiguous and that no discovery was necessary. Based on the plain language of the indemnification provision, the court held that the parties clearly intended for the defendant to indemnify plaintiffs as against both payments and liabilities. Moreover, because defendant was obligated to indemnify both payments and liabilities, the court held that the creation of escrow accounts for the plaintiff subsidiary companies in no way affected defendant's indemnity obligation. The court, therefore, granted plaintiffs summary judgment on their breach of contract and declaratory judgment claims. Finally, the court held that plaintiffs' costs and expenses associated with the action, including their reasonable attorneys' fees, were included within the definition of "Covered Losses" and could be recovered by plaintiffs. <u>LPL Holdings, Inc. v. Pacific Life Insurance Company,</u> Index No. 603652/2009, 3/3/11 (Kapnick, J.).

Contract; loan agreement; collateral. UCC-1 filings; validity; error in secured party name. Third party possession of collateral. Plaintiff sought damages of nearly $4,000,000, and diamonds comprising collateral, in suit arising from a loan and security agreement and amendment with first corporate defendant. Second corporate defendant also had pledged diamonds as security. First defendant had agreed that its sales receivables would all be paid into a collateral account under plaintiff's control or else delivered to plaintiff's office but had not carried through. Plaintiff had declared a default. First defendant had promptly shipped diamonds pledged as collateral to an alleged affiliate in Israel, where the gems allegedly were subject to a security interest in favor of an Israeli bank. Previously, the court had granted plaintiff an order of seizure and temporary restraining order, and plaintiff had recovered some portion of the collateral. Here, plaintiff moved for partial summary judgment. On a cause of action against both corporations and an individual defendant for seizure of the diamonds pursuant to CPLR Article 71, the court found that plaintiff failed to submit an affidavit as required by the CPLR but was entitled to judgment based on the Commercial Division Rule 19-a statement, admissions by defendant's president, and its submission of the UCC-1 statements it had filed. The individual defendant, first defendant's president, was liable because he had admittedly taken part in the tortious conversion of inventory by transferring it to the entity in Israel. Defendants failed to raise a triable issue of fact. They did not demonstrate that actions pending in Israel would likely yield inconsistent results, and their contention that plaintiff's UCC-1 filings were ineffective was without merit. Even if the filings listed plaintiff's former and not current name, according to the Official Comment to UCC 9-506 the listing was not seriously misleading because searches are not conducted under the secured party's name. A potential creditor would see plaintiff's filing and be put on notice to investigate whether defendant's assets were encumbered. Further, the filings were valid as of the first date filed, in light of the duly filed continuation statements. Consequently, defendants' argument that other creditors' UCC-1 filings had priority also lacked merit. The court explained that although it had no personal jurisdiction over the Israeli bank allegedly in possession of the collateral, plaintiff, as secured party, was entitled to delivery of the collateral and to assert its right against a third party in possession. Plaintiff was awarded summary judgment on the cause of action, and defendants were directed to deliver the collateral shipped to Israel to plaintiff. An inquest was necessary to determine the value of the collateral recovered by plaintiff in order to assess its damages, if any. The court referred that issue, along with attorneys' fees, which plaintiff was awarded, to a Special Referee. <u>Gerber Finance, Inc. v. Oved Diamond Co., Ltd</u>., Index No. 600304/2010, 3/22/11 (Fried, J.).

Entity valuation; income approach. Dissolution; derivative action. Expert witness. Petitioner sought judicial dissolution of respondent corporations pursuant to Business Corporation Law § 1104-a. Respondents elected to purchase petitioner's interest in three of the respondent corporations, known as QCC, QEL and Amstel, requiring the court to perform a valuation of those corporations. Petitioner then initiated a derivative action claiming that the value of three other companies (the "disputed corporations") were assets of QCC and had to be included in the court's valuation. The valuation was suspended until the court held that petitioner's 25% ownership interest in QCC, QEL and Amstel needed to include the value of some of the disputed corporations. The court heard testimony from three valuation experts. The first expert was the independent appraiser appointed by the court, who described the independent appraisal performed by his firm. That appraisal determined that petitioner's interest in the three corporations was worth $1,495,000. The second expert, called by petitioner, testified that the expenses used by the independent appraiser were inaccurate and concluded that petitioner's interest in those same entities was between $1,999,000 and $2,571,000, depending on the use of various discounts for lack of marketability. The third expert, respondents' appraiser at an earlier hearing date, testified that the fair value of the three corporations amounted to a total of $575,000. Since respondents elected to exercise their statutory buy-out option of petitioner's interests, the court analyzed the valuation pursuant to BCL § 1118, rather than § 1104-a, which required that the court determine fair value as of the date prior to the date on which the petition was filed. The court held that "fair value" was a function of the "particular facts and circumstances" of the case, and that there was "no single formula for mechanical application." The court noted that without the power to appoint an independent appraiser in BCL § 1118, the expert opinions offered by each party would otherwise leave the court with "little meaningful guidance about an accurate valuation. The opinions of experts hired by the parties are of course suspect for reasons of bias, and a 'battle of partisan experts' often serves only to cloud the issues." Finding that the independent appraiser used an "income approach," which was both proper under New York law and, in the appraiser's opinion, most suitable for the entities at issue, the court held that the report of the independent appraiser was both credible and reliable. The court noted the appraiser's vast experience and careful methodology and placed "diminished weight" on petitioner's expert witness concerning the unreliability of the expenses used by the independent appraiser. The court also held that despite the historically low level of interest rates in the United States, it would not alter the statutory rate where the Legislature had not seen fit to do so. Finally, the court refused petitioner's request for attorneys' fees, noting that respondents elected to purchase petitioner's interests within 90 days of his filing of the petition for valuation and thus, pursuant to BCL § 1118, were not required to pay attorneys' fees and costs. The court therefore awarded petitioner $1,495,000 plus interest at the statutory rate from July 26, 2005. <u>In the Matter of the Application of Patrick Quadrozzi</u>, Index No. 16299/05, 2/10/11 (Grays, J.).**

Fraud; damages; out of pocket rule; pecuniary loss; damages; business oppportunity. Contract; breach; no ambiguity, fiduciary duty; no relationship. Plaintiff, a venture capitalist, asserted causes of action for fraudulent misrepresentation, breach of contract, and breach of fiduciary duty against defendants, a dried fruit and nut company and its CEO. Defendants solicited plaintiff to invest in defendant company in exchange for a promissory note giving plaintiff the option to convert the amount due under the note into stock under a conversion agreement. When it became apparent that the represented value and financial solvency of defendant had been inflated, plaintiff sought to convert part of the note into stock. Defendants refused to recognize the conversion and instead repaid the entire balance of the note at its maturity, plus interest at the contractual rate. Defendants alleged that the conversion agreement did not allow partial conversion. Defendants moved for summary judgment on the basis that plaintiff could not prove damages to support fraud and that plaintiff's breach of contract claim could not be supported by the terms of the conversion agreement. Defendants also argued that the cause of action for breach of fiduciary duty must be dismissed because an ordinary debtor and noteholder, such as plaintiff, does not share a fiduciary relationship. The court, in granting the motion for summary judgment, held that the out of pocket rule, as it applies to fraud, requires that a party suffer damages of an actual pecuniary loss as a direct result of a wrong and that a loss cannot just be the loss of an alternative contractual bargain or that a party might have suffered a loss. Plaintiff's argument that its fraud damages were based upon a loss of business opportunity due to the misrepresentations of defendant's value was therefore speculative and unpersuasive and, since defendant repaid the entire amount under the note, plaintiff had not suffered an actual pecuniary loss. As to the breach of contract claim, the court held that the conversion agreement did not contain an ambiguity and therefore had to be interpreted as a matter of law. Since defendant's ability to make a partial prepayment was contingent on the parties' mutual agreement, there was no basis to believe that the agreement would allow unilateral partial prepayment or partial conversion. Lastly, in connection with the breach of fiduciary duty claim, the court rejected plaintiff's argument that the parties acted as a joint venture creating a fiduciary relationship, noting that the critical component of a joint venture is the sharing of profits and losses and the mutual control of management. Since the parties merely had a loan agreement, plaintiff failed to allege sufficient facts to support the finding of a joint venture. The relationship between an ordinary debtor and a note-holder creditor generally does not create a fiduciary duty. The mere fact that defendants knew plaintiff was a joint venture capital firm also does not create a fiduciary relationship. <u>Eitan Ventures, LLC v. Peeled, Inc.</u> Index No. 603151/2009, 1/3/11 (Ramos, J.).

Fraud; fraudulent inducement; fraudulent concealment; justifiable reliance. Suborning of investment ratings agencies; disclaimer clauses may not be invoked to defeat justifiable reliance where agencies

allegedly suborned. Ratification of agreement; right to seek recision. Waiver of jury trial does not apply in fraudulent inducement. Collateralized debt obligation (CDO). Mortgage bonds. The court sustained fraud claims that a sophisticated institutional investor brought against a top financial services firm. Defendant allegedly had designed a product it called the Supersenior Swap as senior security in a hybrid collateralized debt obligation (CDO) composed of real estate mortgages. Allegedly having learned that the rating agencies had changed their models in response to the lowering standards of mortgage originators and consequent lowering quality of mortgage bonds, defendant had worked to get its assets "grandfathered" in under the old rating methodologies, for which it paid the agencies up to three times what it would have normally. Allegedly knowing that its ratings were false and misleading and likely to be downgraded, defendant had marketed the Supersenior Swap to plaintiff as an almost risk-free investment, backed by mortgage bonds more stable than AAA rated bonds, and sold plaintiff a mirror credit default swap tied to the Supersenior Swap. Here, on a motion to dismiss, defendant argued that no actionable statements were alleged. The court explained that pleading fraud requires allegations of a material misrepresentation of fact, knowledge of its falsity, an intent to induce reliance, justifiable reliance by plaintiff, and damages. In regard to the fraud and fraudulent inducement causes of action, it found that defendant's alleged knowledge and statements constituted bare material misrepresentations of fact made to induce the purchase of an investment security. Plaintiff alleged in sufficient detail that defendant knew that the Supersenior Swap was a highly risky, if not troubled, investment, and plaintiff pointedly alleged that flaws in the ratings process that made the investment appear safe were due, in part, to defendant's influence. Stating that defendant had had a duty to disclose, among other things, the "grandfathering" of ratings methodologies and payment of extraordinary fees, even though in the circumstances it was not a fiduciary, the court also declined to dismiss the cause of action for fraudulent concealment. Defendant next argued that plaintiff was precluded from pleading justifiable reliance. Defendant contended that the transaction document executed by plaintiff, which stated among other things that plaintiff was not relying on defendant's statements and would conduct its own due diligence, put the matter well within the ambit of the recent ruling in *MBIA Ins. Co. v Merrill Lynch, Pierce, Fenner & Smith Inc.*, (81 AD 3d 419 [1st Dept 2011]) that dismissed fraud claims based on plaintiff's representations. Defendant also pointed to caveats in its marketing material. The court agreed that prophylactic legends with regard to sophistication in investment transaction documents, along with representations concerning due diligence, may negate justifiable reliance in some common law fraud actions. However, plaintiff's core allegation that defendant had corrupted the ratings agencies posited circumstances that neither due diligence nor analysis by the most sophisticated investors could uncover. The court noted that defendant's pitchbook compounded plaintiff's disadvantage; the pitchbook said that the CDO had no operating history and directed requests for more information to defendant, which then could control the information. The court cited a case involving analogous circumstances, which held that disclaimers and due diligence requirements were invalid if the information needed to confirm or disprove the validity of ratings was peculiarly within the defendant's knowledge. Additionally, the reasonableness of plaintiff's alleged reliance on the ratings was fact intensive and not best determined at this stage. Finally, in relation to the fraud claims, the court found that plaintiff amply pled scienter. It also declined to dismiss on the ground that plaintiff's execution of an agreement constituted ratification causing plaintiff to lose its right to seek rescission, because plaintiff had explicitly reserved its remedies, and, further, the issue was replete with questions of fact. The court did dismiss the causes of action against a separate defendant entity and employees, finding the allegations conclusory. It then considered defendant's motion to strike plaintiff's demand for a jury trial. Plaintiff argued that its damages could be proved at jury trial. The transaction document stated that each party waived its right to a jury trial, but such waivers do not apply to a claim of fraudulent inducement challenging the validity of an agreement. The demand for a jury trial was struck with respect only to the other causes of action. <u>China Development Industrial Bank v. Morgan Stanley & Co. Inc</u>., Index No. 650957/21010, 2/25/11 (Schweitzer, J.).

Jurisdiction; general; sufficient start by defendants in showing parent did business through subsidiary. Jurisdiction; long arm (CPLR 302 (a) (1) and (2)); forum non conveniens. Contract; mandate agreement; liability of non-signatory parent for breach. Tortious interference with contract. Plaintiff, a Singapore company in the pulp mill industry, sued a parent corporation in New York and its Singapore subsidiary for breach of contract, negligent misrepresentation, and related wrongs. Plaintiff had wanted to acquire an Indonesian paper mill operator;defendants were interested in arranging finance. Plaintiff alleged that it had told the Singapore defendant that NGOs (non-governmental organizations) had pressured an earlier finance arranger to withdraw, and why. Plaintiff claimed it had told defendants that its next finance arranger could not pull out due to the same pressure. According to plaintiff, the Singapore defendant got approval from the New York defendant to arrange financing and confirmed that an agreement would not be terminated due to NGO pressure. Plaintiff and Singapore defendant had entered into a mandate agreement that provided that it could not be terminated before six months. Subsequently, according to plaintiff, the Singapore defendant let it be known that the New York defendant wanted to ensure that an NGO campaign would not harm its reputation and that an environmental report was going to be prepared for the New York defendant. Plaintiff also said there had been at least one meeting involving a New York representative and made other allegations concerning the New York defendant's involvement. Singapore defendant terminated the agreement before six months had elapsed. Plaintiff claimed that the termination and lack of finance arranger prevented the acquisition despite support from investors, caused its stock price to crash, and brought about other harm including the squandering of funds on due diligence. Defendants moved to dismiss the complaint on the grounds that it failed to state a claim against the New York defendant, Singapore was a more convenient forum for the claims against the Singapore defendant, and the Singapore defendant was not subject to personal jurisdiction in New York. The court first considered the issue of personal jurisdiction. Plaintiff argued, among other things, that the court should consider the transaction's center of gravity and take into account that the New York defendant imposed policies on its subsidiaries, that the two might maintain consolidated books, and the like. Defendants argued that plaintiff could not show that Singapore defendant was a "mere department" of New York defendant. The court found however, that plaintiff put forth two declarations supporting its argument that the Singapore defendant was subject to jurisdiction based on the parent-subsidiary relationship. It explained that agency may not be inferred from the mere existence of that relationship, but plaintiffs who made a sufficient start in showing that defendants did business in New York through subsidiaries should be allowed to learn whether the complex corporate relationships at play involved the parents' exercise of control. The court ruled, therefore, that plaintiff could conduct limited jurisdictional discovery. However, it found that plaintiff failed to allege that the Singapore defendant had transacted business in New York or committed a tortious act here and declined to exercise long-arm jurisdiction. Since an unresolved jurisdictional question awaited discovery, the court did not reach the issue of dismissal based on forum non conveniens and turned to the substantive claims against the New York defendant. Defendants argued to dismiss the breach of contract claim on the ground that the New York defendant was not a signatory. Plaintiff pointed to a statement in the agreement that the offering would be subject to a final internal approval, which plaintiff said referred to the New York defendant; it contended that the agreement's overall language supported an affiliation argument. Because a non-signatory parent corporation can be held liable as a party to its subsidiary's contract if the parent's conduct shows an intent to be bound, the court decided that it was premature to dismiss the claim. A claim for negligent misrepresentation failed to allege a special relationship and was dismissed, as was one for fraud and fraudulent inducement, because the representations, even had they been alleged in adequate detail and taken as true, did not pertain to material facts. In regard to a claim for tortious interference with contract, pled in alternative to breach, the court, in sustaining the claim, clarified that plaintiff only had to plead intent to induce a breach without economic justification and damages. Defendants argued that an economic interest defense was established by plaintiff's own allegations, which acknowledged that the New York defendant's actions were to protect its reputation. Plaintiff responded that it would be premature to consider defendants' defense to the claim, and it survived. With respect to the breach and tortious interference claims against the New York defendant, the court found that the causation and damages prongs had been adequately pled. <u>United Fiber System Ltd. v. Merrill Lunch & Co., Inc</u>., Index No. 106102/2009, 1/10/11 (Kapnick, J.).

Limited liability companies; dissolution; winding up; operating agreement. Petitioner filed a petition pursuant to Limited Liability Company Law ("LLC Law") § 703 for the judicial winding up of the affairs of a limited liability company. Respondent argued that the company had not been dissolved and that petitioner should have applied for judicial dissolution under LLC Law § 702. The court granted petitioner's application. Although the parties agreed that the operating agreement for the limited liability company had been terminated, respondent argued that the termination of the agreement did not result in the dissolution of the company. The court rejected this argument, explaining that the members of the company could not have intended for the company to continue without an operating agreement. Thus, the court determined that the limited liability company was dissolved upon termination of the agreement. The court held alternatively that the disagreement among the members was so "fundamental and intractable" that dissolution pursuant to LLC Law § 702 was warranted. Because petitioner had alleged irregularities relating to a parcel of property that had been purchased by the limited liability company, the court granted petitioner's application that the court supervise the winding up of the company. In re Fassa Corp., Index No. 018824/2010, 2/1/11 (Bucaria, J.).**

Personal jurisdiction; consent to jurisdiction; CPLR 302(a)(1). Motion to dismiss; documentary evidence; CPLR 3211(a)(1). Plaintiff, a New York company, sued defendant, a Florida resident, for the return of money that plaintiff paid to purchase defendant's beneficial interest in a trust, which in turn owned a life insurance policy insuring defendant's life. Defendant moved to dismiss the complaint pursuant to CPLR 3211(a)(1) and (8), arguing that documentary evidence conclusively established that he was not obligated to refund the payment, and that the court lacked personal jurisdiction over him. The court held that it had personal jurisdiction over defendant but dismissed the complaint based on documentary evidence. With respect to defendant's jurisdictional argument, the court held that defendant had consented to be sued in New York when he signed the trust agreement. The trust agreement provided that courts in New York City "shall have exclusive jurisdiction to hear and determine any claims or disputes between the parties pertaining to this Agreement or to any matter arising out of or relating to this Agreement." Although defendant claimed that this forum selection clause did not apply because plaintiff was not a party to the trust agreement at its inception and the parties' dispute allegedly did not arise out of the trust agreement, the court rejected both arguments. The court explained that once defendant sold his beneficial interest in the trust to plaintiff, plaintiff became bound by, and was entitled to invoke, the terms of the trust agreement. Additionally, the court held that the instant action arose out of or was related to the trust agreement because the parties' dispute related to the contemplated transfer of trust assets to a new beneficiary. Moreover, even if defendant had not consented to jurisdiction in New York, the court found that the complaint alleged facts sufficient to establish long-arm jurisdiction pursuant to CPLR § 302(a)(1). Although defendant never had traveled to New York in connection with the transaction, the court held that by purchasing an insurance policy from a New York company, creating a trust pursuant to New York law, and selling his rights as a beneficiary of the trust to a New York company pursuant to an agreement that was governed by New York law, defendant purposely availed himself of the benefits of the laws of New York sufficient to justify the exercise of jurisdiction. The court, however, granted defendant's motion to dismiss based on documentary evidence. According to the transfer agreement under which defendant sold his interest in the trust to plaintiff, plaintiff had the right to demand the return of its money if the life insurance policy that was owned by the trust was voided by the insurance company within two years of the policy's issuance. Defendant presented documentary evidence showing that the insurance policy was voided more than two years after its issuance as part of the settlement of a separate lawsuit in Florida. LPC Holdings I LP v. Gillman, Index No. 650830/2010, 1/3/11 (Gammerman, J.H.O.).

Procedure; motion to dismiss; CPLR 3211(a)(7); CPLR 3211(a)(1); time for making motion. Lien Law; foreclosure of mechanic's lien; diversion of trust funds; trust accounting. Fraudulent conveyances. Plaintiff corporation brought the instant action against the developer of a residential community, the developer's officers, and individuals who had purchased homes in the residential community. Plaintiff sought to foreclose on a mechanic's lien and also asked the court to award damages for the alleged unlawful diversion of trust funds, order a trust fund accounting, and award damages for the alleged fraudulent conveyance of certain real property. Defendants moved to dismiss, and the court granted the motion. The court, first, denied defendants' motion to dismiss the complaint based on documentary evidence, pursuant to CPLR 3211(a)(1), as untimely because defendants did not make the motion within the time required to serve their answer to the complaint. The court, however, granted defendants' motion to dismiss the complaint for failure to state a claim, pursuant to CPLR 3211(a)(7). With respect to the first cause of action, seeking foreclosure of plaintiff's mechanic's lien, the court held that the lien was invalid and thus unenforceable because the construction consulting services provided by plaintiff were not lienable within the meaning of the Lien Law. The court also dismissed plaintiff's second cause of action for the unlawful diversion of funds in a trust, which had been established by the defendant developer, pursuant to Article 3-A of the Lien Law, as well as plaintiff's third cause of action for a trust fund accounting. The court explained that in order to maintain causes of action for the diversion of trust funds and for a trust fund accounting, plaintiff had to be a beneficiary of the trust. Under the Lien Law, a contractor may be a beneficiary of a trust if the trustee is obligated, either by contract or because of a mechanic's lien, to pay the contractor's claims for payment out of the trust assets. But the court held that plaintiff failed to allege any basis upon which the trustee was obligated to pay its claim from the trust. The court also dismissed the fourth cause of action to recover damages based upon an alleged fraudulent conveyance of certain real property under the Debtor and Creditor Law on the ground that plaintiff failed to allege that any conveyance rendered the developer defendant insolvent or that any conveyance was made with actual intent to "hinder, delay, or defraud either present or future creditors." Enbe Construction Group, Inc. v. Queens College Point Holdings, LLC, Index No. 22790/2010, 2/10/11 (Kitzes, J.).**

Professional malpractice; construction and design; negligence; breach of contract; statute of limitations. Insurance; surety claims; performance bonds; rehabilitation orders. Procedure; conversion of motion to dismiss to motion for summary judgment; motion for leave to amend. Plaintiff brought suit against the various contractors, architects, engineers, and sureties involved in the design and construction of two piers. The court granted the motion of one of the plumbing contractor defendants for a more definite statement, finding that the complaint alleged in only conclusory terms that the defendant was "negligent in the performance of the work [it] was required to perform and that [it was] paid for work that was not properly completed." The court also granted the motion by certain defendants that had provided architectural and construction management services for the project to dismiss the negligence and breach of contract claims against them as time-barred. The court explained that whether cast in terms of contract or tort, claims of professional malpractice against an architect for defective design or construction are governed by a three-year statute of limitations, which accrues when the work is completed, not when the defective condition is discovered. Because the architectural defendants had completed their work more than five years before the instant action was commenced, the court dismissed the claims asserted against those defendants. The court, however, denied the motion made by a second group of architectural defendants to dismiss on statute of limitations grounds. Although styled as a motion to dismiss, the court treated the motion as one for summary judgment given that it was made after the defendants had answered and the parties had "laid bare their proof." Because there was a factual dispute regarding when the second group of architectural defendants ceased working on the construction project, the court held that it could not determine as a matter of law that plaintiff's claims were time-barred. The court dismissed as time-barred plaintiff's claim against a surety company defendant that had guaranteed the performance of one of the plumbing defendants. The terms of the performance bond required that any suit on the bond had to be brought within one year of the date when the plumbing defendant last performed plumbing services, and the court found that the instant action was commenced more than two years after the plumbing defendant had stopped work. The court also granted the motion to dismiss of two insolvent insurance company defendants on the ground that both were subject to orders of rehabilitation enjoining the commencement of any actions or proceedings against them. Additionally, the court dismissed all claims against two remaining insurance company defendants, finding that the evidence established that those defendants had not issued any performance bond in connection with the construction project. Finally, the court denied plaintiff's cross-motion for leave to amend, holding that plaintiff's proposed additional defendant was not united in interest with the current defendants and that the proposed amended complaint failed to "cure any of the deficiencies found in the original complaint or revive any of the dismissed causes of action." Village of Greenport v. Manning Plumbing & Heating Corp., Index No. 26981/2009, 2/08/11 (Emerson, J.).**

Spoliation. Electronic evidence; emails. The court granted plaintiff's spoliation motion and directed that an adverse inference instruction be made before trial based upon defendant's destruction of computer hard drives after the action was commenced, as well as defendant's failure to produce computers allegedly containing relevant electronic evidence. Plaintiff argued that the hard drives of certain computers belonging to defendant were replaced or reformatted during the pendency of this litigation. Plaintiff also argued that defendant destroyed emails and other documents relevant to the claims in its complaint. Defendant countered that no relevant emails referring to plaintiff were lost, deleted, or destroyed within the given time period. The court determined that plaintiff made a clear and convincing showing that, after the action had been commenced, the computer hard drives were reformatted or otherwise deleted so as to raise a strong inference that access to data that existed prior to reformatting or deletion was no longer available to plaintiff. The court further found that defendant proferred no explanation for how this happened and concluded that the deletion was done intentionally or at least recklessly. It also found that defendant had an obligation to preserve certain emails relevant to plaintiff's claims and that it failed to meet this obligation by supposedly transferring data. Although defendant argued that the destruction of the hard drives was of no moment because the data on the computers had been manually transferred to new hard drives, the court cited precedent suggesting that there could be no assurance that all of the data, both the emails that were "live" and "deleted" but still capable of being retrieved from the hard drive, had been transferred. Pramer, SCA v. Abaplus International Corporation, Index No. 603336/04, 1/21/11 (Schweitzer, J.).

The complete texts of decisions discussed in the *Law Report* are available by hyperlink on the website of the Commercial Division at www.nycourts.gov/comdiv (under the "Law Report" section), and on the home page of the New York State Bar Association's Commercial and Federal Litigation Section at www.nysba.org (and following links). Members of the Commercial and Federal Litigation Section may sign up at the Section's home page to receive copies of the *Report* by e-mail automatically. The decisions as they appear on the home pages have not been edited and may differ from the final text published in the official reports by the State Reporter.

**** The decisions discussed have been posted in PDF format, but the reader should be aware that these PDF copies may not be exact images of the original signed text as filed in the County Clerk's Office.**