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

PRESENT: Hon. SHEILA ABDUS-SALAAM PART 13
*Justice*

I. Reich Family Limited Partnership

- v -

McDermott, Will & Emery

INDEX NO. 101921/03

MOTION DATE 7/1/03

MOTION SEQ. NO. 02

MOTION CAL. NO. 40

The following papers, numbered 1 to _____ were read on this motion to/for _____

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

SCANNED
OCT 17 2003

Cross-Motion: ☐ Yes ☐ No

Upon the foregoing papers it is ordered that this motion by defendants for an order pursuant to CPR 3211 (a) (7) dismissing the complaint is granted only to the extent indicated below:

This is an action alleging legal malpractice, breach of fiduciary duty, negligent misrepresentation, negligence and fraud primarily in connection with an opinion letter that was authored by defendant law firm McDermott, Will & Emery with respect to a transaction between its client, non-party SpectruMedix Corporation, and plaintiff, an investor in that company. The amended complaint alleges that in 2001, SpectruMedix was in dire financial straits and that one of its directors contacted Ilan Reich, a general partner of plaintiff I. Reich Family Limited Partnership to determine if Reich would provide financing to the company. Reich responded that he would invest $1 million and take control of the company on the condition that Joseph Adlerstein, who was then Chairman, CEO and principal shareholder of the company, was removed. The defendant law firm, as counsel to the company, provided plaintiff with information and negotiated the terms of the transaction. It also issued an opinion letter to plaintiff with respect to the

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE
DATED: J.S.C.

transaction.

The amended complaint further alleges that defendant orchestrated the July 9, 2002 meeting that included Adlerstein's ouster and Board approval of the Reich LP transaction, and that defendant advised the other Board members that they did not need to keep Adlerstein advised of the Reich LP transaction or to inform him that the transaction would be voted on at the July 9th meeting. At the meeting, Adlerstein was removed from his offices as Chairman and CEO and replaced by Reich. Immediately following the completion of the Reich LP transaction, Reich LP exercised its rights as majority stockholder and removed Adlerstein from the Board.

Adlerstein subsequently filed suit in the Court of Chancery of the State of Delaware against the Board members and Spectrumedix to invalidate the actions taken at the July 9th meeting, and following a trial of the action, the Court issued a decision which inter alia, required that the actions taken by the Board on July 9, 2001 be undone and declared Adlerstein to be the Chairman and CEO of the company. According to the complaint, following extensive mediation efforts and additional litigation, Reich LP, together with SpectruMedix and other entities, entered in to a settlement agreement requiring payments to Adlerstein amounting to $1.85 million and a non-dilutable 15% equity interest in the company. Plaintiff alleges that "[a]s a direct and proximate result of [defendant's] wrongdoing, Reich LP has incurred extensive damages. Not only is Reich LP's original $1 million investment worthless, Reich LP was required to pay $500,000 to defend against the lawsuit brought by Adlerstein, and to enter into a $1.85 million Settlement with Adlerstein. Thus far, SpectruMedix LLC (with monies advanced by Reich LP) has paid Adlerstein $200,000 under the Settlement. Further, in an effort to salvage its investment in SpectruMedix, Reich LP has invested an additional $2.5 million into the company and its successor."(Amended complaint, ¶ 38).

The first cause of action sounds in attorney malpractice. It is alleged that defendant had a duty to plaintiff to render competent legal advice in providing the opinion letter, that defendant breached its duty by providing an opinion letter containing advice that was incorrect, and that as a result of this breach, plaintiff sustained damages. Based upon the lack of contractual privity between the parties, and the fact that it was clear from the opinion letter that defendant was acting as

counsel to SpectruMedix, defendant asserts that the first cause of action fails to state a viable claim for legal malpractice (see generally Burton v. Rogovin, 262 AD2d 72; Solondz v. Barash, 225 AD2d 996; Mason Tenders District Council Pension Fund v. Messera, 4 F. Supp.2d 293 [S.D.N.Y. 1998]). However, in Prudential Ins. Co. v. Dewey, Ballantine, Bushby, Palmer & Wood (80 NY2d 377), cited by plaintiff, the Court of Appeals reiterated its prior holdings that "before a party may recover in tort for pecuniary loss sustained as a result of another's negligent misrepresentations there must be a showing that there was either actual privity of contract between the parties or a relationship so close as to approach that of privity (citations omitted)."(id. p. 382). In Prudential, the Court discussed an attorney's duty of care to a non-client in the context of a claim for negligent misrepresentation. In determining whether the relationship between the parties "was sufficiently close to support liability"(p. 382), it applied prior decisional law on the liability of parties not in privity. The Court noted that in European Am. Bank & Trust Co. v. Strauhs & Kaye (65 NY2d 536), the prerequisites of a cause of action for negligence had been satisfied because the defendant accountants had been aware of the purpose of the advice they were providing to plaintiff, had known the identity of the plaintiff, had known that the plaintiff would rely on their services, and had evinced their understanding of that reliance

Although defendant argues here that the Court in Prudential did not hold that the plaintiff had stated a claim for legal malpractice, but had only addressed the claim for negligent misrepresentation, the Court concluded in that case that a duty of care had been owed to plaintiff, but that the facts did not prove a breach of that duty. It clearly recognized, in applying the concepts of duty of care, and breach of that duty, as did the Appellate Division in the underlying decision (170 AD2d 108, 118), that under certain circumstances, an attorney can be liable to third parties, not in privity, for harm caused by professional negligence.

In Prudential , id., the Court of Appeals held that when there is no contractual privity between the parties, a party can assert a negligence claim against an attorney where there is an awareness that an attorney's statement is to be used for a specific purpose, reliance on the statement, and some conduct linking the attorneys to the non-client evincing their understanding of that reliance

(p. 384). The allegations of this pleading include all three of these criteria. Thus, plaintiff has stated a cognizable claim for malpractice as well as for negligent misrepresentation (the second cause of action).

The fifth cause of action for breach of fiduciary duty also states a viable claim. As noted, the plaintiff has alleged a relationship between it and defendant that is "so close as to approach privity."(Prudential, id., p. 382).The allegations of the complaint indicate that defendant was acting as special counsel to SpectruMedix when it issued the opinion letter to plaintiff and otherwise worked with plaintiff on the transaction. It is also alleged that defendant "orchestrated the July 9, 2002 meeting, including Adlerstein's ouster and the Board approval of the Reich LP transaction" (¶ 25) and that it advised the Board members that they did not need to inform Adlerstein of the Reich LP transaction or to notify him that it was being voted on at the July meeting. In its decision invalidating the actions taken at the July Board meeting, the Court of Chancery concluded that Adlerstein had been entitled to know ahead of time of the planned transaction, and that "this right to advance notice derives from a basic requirement of our corporation law that boards of directors conduct their affairs in a manner that satisfies standards of fairness."( Decision, p. 24).

The opinion letter stated that each of the transaction documents had been duly authorized by all necessary corporate action on the part of the Company. Yet, as a result of the decision of the Court of Chancery, the transaction was invalidated on the basis that the corporation had not provided Adlerstein with the required notice of the planned transaction.

In Lewis v. Rosenfeld (138 F. Supp. 2d 466 [S.D.N.Y. 2001]), cited by plaintiff, the court did not hold that the defendant attorneys owed a fiduciary duty to the non-client plaintiff, but discussed the theoretical liability of attorneys based on opinion letters. Significantly, the District Court noted that courts have applied the criteria for a negligent misrepresentation claim in determining whether an attorney owes a fiduciary duty to a non-client, and specifically to the situation where an attorney, at the client's request, issues an opinion letter which is relied on by a third party (id., p. 480). In support of dismissal of the breach of fiduciary duty cause of action defendant has argued that "it defies logic that a law firm, which

arising out of defendant's ownership interest in the company, the fact that certain partners of defendant were debtors to the company, and defendant's prior representation of Adlerstein. In view of the relationship between defendant and plaintiff, where defendant was providing an opinion letter to plaintiff and advising plaintiff with respect to the transaction with the company, defendant owed plaintiff a duty of disclosure (see generally 900 Unlimited, Inc.v. MCI Telecommunications Corp, 215 AD2d 227). However, these allegations of concealment are insufficient to establish the necessary causation between defendant's purported fraud and plaintiff's loss, or loss causation (see Laub v. Faessel, 297 AD2d 28). Plaintiff's injury did not arise from defendant's nondisclosure of ownership interests in the company, or a conflict of interest, but from the invalidation of the transaction that was ordered by the Chancery Court. Accordingly, the fourth cause of action is sustained only to the extent that it alleges that defendant made fraudulent misrepresentations of fact in the Opinion letter.

Based upon the foregoing, the motion is granted only to the extent indicated above. Defendant is directed to serve an answer to the complaint within 20 days after service of a copy of this order with notice of entry.

ENTER:

Dated: October 10, 2003

J.S.C.

Check one: ☐ FINAL DISPOSITION ☒ NON-FINAL DISPOSITION