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

PRESENT: HON. RICHARD B. LOWE III PART 56

0604255/2004

GLOBAL ASSET MANAGEMENT LLC
VS
ARCADIA RESOURCES, INC.

INDEX NO. _____

MOTION DATE 6/24/05

MOTION SEQ. NO. _____

MOTION CAL. NO. _____

SEQ 1

SUMMARY JUDGMENT

C

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	

Cross-Motion: ☐ Yes ☐ No

Upon the foregoing papers, it is ordered that this motion

MOTION IS DECIDED IN ACCORDANCE
WITH ACCOMPANYING MEMORANDUM DECISION

FILED
JAN 25 2006
COUNTY CLERK'S OFFICE

HON. RICHARD B. LOWE, III

Dated: 1/18/06

J.S.C.

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

Check one: ☒ FINAL DISPOSITION ☐ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 56

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GLOBAL ASSET MANAGEMENT LLC,

Plaintiff,

- against - Index No. 604255/2004

ARCADIA RESOURCES, INC.,

Defendant.

----------X

HON. RICHARD B. LOWE, III:

In this action alleging breach of contract, plaintiff moves for summary judgment on the complaint, pursuant to CPLR 3212, and for an award of its costs and attorneys' fees. Defendant cross-moves: (1) pursuant to CPLR 3025 (b), for leave to amend its answer to assert two additional affirmative defenses and a counterclaim for reformation of contract; and (2) pursuant to CPLR 3212, for summary judgment dismissing the complaint.

FACTUAL ALLEGATIONS

Defendant Arcadia Resources, Inc. (ARI) is the successor by merger (the Merger) and by name change of an entity known as Critical Home Care, Inc. (CHC; CHC or ARI, hereinafter, Arcadia). Prior to the Merger, Arcadia was party to a consulting agreement with Rockwell Capital Partners, LLC (Rockwell), an investment banking firm allegedly affiliated with plaintiff Global Asset Management LLC (Global). In contemplation of the Merger, Rockwell and Arcadia entered into a release agreement dated April 21, 2004 (the Release), which provided, in part, that:

> [Rockwell] ... as RELEASOR in consideration of the sum of [t]en dollars, 250,000 Common Shares of [Arcadia] issued to [Global], a Registration Rights Agreement to register said shares [by July 20, 2004] and other good and valuable consideration ... received from [Arcadia] as RELEASEE, receipt of which is hereby acknowledged, releases and discharges [Arcadia] ... from all ... causes of action, ... contracts, ... agreements, ... claims, and demands whatsoever ....

(Elliott Affid., Ex. A, at 1.)

Global executed a document (the Registration Rights Agreement), appended to the Release, which provided that Global was acquiring the 250,000 shares of Arcadia common stock referred to in the Release (the Shares) for investment purposes only, and that:

> [Arcadia] agrees to register the [Shares] [by July 20, 2004]. In the event that [Arcadia] fails to file an SB-2 [by July 20, 2004], [Arcadia] will pay [Global] penalty shares equal to 100,000 shares per month or the prorated portion for any period after and until the SB-2 is filed.

(Elliott Affid., Ex. A, at 2 [the quoted provision, hereinafter, the Registration Clause].) It appears that Arcadia did not execute the Registration Rights Agreement. However, Arcadia does not dispute that the Release and the Registration Rights Agreement comprised a contractual agreement, which is binding upon Arcadia as a general matter, and which should be applied to determine the parties' respective rights and obligations with regard to the claims asserted in the complaint (*see* Arcadia Reply Mem. of Law, at 2, 13).

The Registration Clause expressly contemplated that the unregistered Shares would be registered with the Securities and Exchange Commission (SEC) by means of a filing on SEC Form SB-2, a form which is available for use by entities qualifying as "small business issuers" under SEC regulations. Arcadia had allegedly qualified as a "small business issuer" for some period of time prior to the date upon which it entered into the Release, and believed that it would continue to qualify as such for some period of time after that date, and following the impending Merger. However, the SEC allegedly advised Arcadia, soon after the Merger was completed, that the Merger had rendered it ineligible to use Form SB-2, and that it would have to use SEC Form S-1 -- which is purportedly more complex and requires more preparation time than Form SB-2 -- to register its securities. Allegedly for that reason, Arcadia did not file a Form SB-2 registration statement for the Shares with the SEC by July 20, 2004, as contemplated by the Registration Clause but, instead, filed a Form S-1 registration statement covering the Shares on or about August 27, 2004.

As of May 10, 2005, the SEC had still not declared the Form S-1 registration statement to be effective. However, Arcadia asserts that the Shares have been freely saleable and fully liquid since April 21, 2005 under SEC Rule 144, notwithstanding the fact that the SEC had not yet declared the Form S-1 registration statement to be effective as of that date. Rule 144 provides for the unregistered resale of certain restricted securities after a one-year holding period, subject to the

satisfaction of various conditions.

The complaint alleges that, because Arcadia did not file a registration statement for the Shares until August 27, 2004 -- approximately 1.25 months after the July 20, 2004 deadline set forth in the Release and in the Registration Clause -- Arcadia became obligated to deliver 125,000 additional shares of its common stock (the Additional Shares) to Global, pursuant to the formula set forth in the Registration Clause. Arcadia claims that it has no obligation to deliver the Additional Shares to Global. The complaint asserts two causes of action alleging breach of contract and unjust enrichment.

DISCUSSION

Global's motion for summery judgment is denied and, insofar as Arcadia cross-moves for summary judgment dismissing the complaint, its cross motion is granted.

Global's first cause of action alleges that Arcadia is liable for breach of contract by reason of its failure to deliver the Additional Shares to Global, as provided for in the Registration Clause. Arcadia does not dispute Global's contention that it is an intended third-party beneficiary of the Release, with the right to enforce the Registration Clause as a general matter. However, the first cause of action is dismissed because, under a liquidated damages analysis, the Registration Clause's provision for the payment of the Additional Shares to Global is an unenforceable penalty.

The Registration Clause is, in effect, a liquidated damages provision, because it provides for an amount of "compensation which, the parties have agreed, should be paid in order to satisfy any loss or injury flowing from a breach of their contract" (*Truck Rent-A-Center, Inc. v Puritan Farms 2nd, Inc.*, 41 NY2d 420, 423-424 [1977]). Global's contention that the Registration Clause is not a liquidated damages provision, because it does not provide for the payment of a stipulated amount of damages in the event of a breach of contract, is without merit. The Release states that "a Registration Rights Agreement to register [the Shares] [by July 20, 2004]" was part of the consideration given for Rockwell's release of its claims against Arcadia. Pursuant to the Registration Clause, Arcadia "agree[d] to register the [Shares] [by July 20, 2004]." Arcadia could

not actually guarantee that it would register the Shares by any particular date, inasmuch as the registration of securities requires action not only by an issuer of securities, who files a registration statement with the SEC, but also by the SEC, which determines if and when the registration statement shall be declared effective. However, Global and Arcadia agree that, pursuant to the Release and the Registration Rights Agreement, Arcadia promised, and had a contractual obligation, at least, to file a registration statement covering the Shares by July 20, 2004 (*see* Pl. Mem. of Law, at 1; Def. Mem. of Law, at 1, 11). Thus, Arcadia's failure to file a registration statement covering the Shares by July 20, 2004 would be a breach of contract.

Further, the Registration Clause stipulated an amount of damages that Arcadia would pay Global in the event of such a breach of contract, namely "penalty shares equal to 100,000 shares per month or the prorated portion for any period after [July 20, 2004] and until the [registration statement was] filed." Global itself refers to the Additional Shares as "damages," fixed by the formula set forth in the Registration Clause, which Arcadia was required to pay as a result of its late performance (*see* Pl. Reply Mem. of Law, at 9). The fact that the damages were stipulated in terms of securities, rather than in monetary terms, did not render them any the less liquidated damages (*see e.g. Bradford v New York Times Co.*, 501 F2d 51, 57 [2d Cir 1974]; *Lease Corp. of Am. Inc. v Resnick*, 288 AD2d 533, 534 [3d Dept 2001]).

Whether the liquidated damages stipulated in the Registration Clause are enforceable, or are an unenforceable penalty, presents a question of law for the court, requiring due consideration of the nature of the parties' contract and of the surrounding circumstances (*see JMD Holding Corp. v Congress Fin. Corp.*, 4 NY3d 373, 379 [2005]; *LeRoy v Sayers*, 217 AD2d 63, 70 [1st Dept 1995]). That the Registration Clause refers to the Additional Shares as "penalty shares" is not alone dispositive of the question of whether they constituted a penalty rather than enforceable liquidated damages (*see Mosler Safe Co. v Maiden Lane Safe Deposit Co.*, 199 NY 479, 485 [1910]). Rather, regardless of the terminology used by the parties:

> [a] contractual provision fixing damages in the event of breach will be sustained if the amount liquidated bears a reasonable proportion to the probable loss and the

> amount of actual loss is incapable or difficult of precise estimation. If, however, the amount fixed is plainly or grossly disproportionate to the probable loss, the provision calls for a penalty and will not be enforced.

(*JMD Holding Corp. v Congress Fin. Corp.*, 4 NY3d at 380 [citation and internal quotation marks omitted]).[1] Thus, in order to establish that a contractual provision fixing damages is an unenforceable penalty, a party must demonstrate either that the damages flowing from a prospective breach of the contract were readily ascertainable at the time when the contract was entered into, or that the stipulated damages are plainly disproportionate to the losses foreseeably resulting from the breach (*id.*; *see also LeRoy v Sayers*, 217 AD2d at 69-70).

Here, the amount stipulated as liquidated damages constituted a penalty, because it did not bear a reasonable relation to the actual amount of probable damage that Global would sustain in the event of Arcadia's failure to file a registration statement for the Shares by July 20, 2004. It was presumably foreseeable, at the time when Rockwell and Arcadia entered into the Release, that the amount of Global's damages in the event of Arcadia's delay in filing the registration statement would depend principally upon the amount of any actual change in the value of Arcadia's stock between July 20, 2004 and the belated date upon which Arcadia ultimately did file the registration statement.[2]

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[1]A liquidated damages provision which provides for an amount plainly disproportionate to real damage is a penalty, because it "is not intended to provide fair compensation but to secure performance by the compulsion of the very disproportion" (*Truck Rent-A-Center, Inc. v Puritan Farms 2nd, Inc.*, 41 NY2d at 424).

[2]The United States Court of Appeals for the Second Circuit considered a clause in one case which provided that:

> If the Registration Statement to be filed by CUC in 1968 ... shall not become effective on or before the expiration of 60 days from the Closing Date, and the Effective Date Market Value is less than the Market Value, CUM shall deliver to the Stockholder on the effective date such additional number of shares (which would be shares enough to compensate for any drop in the price of the CUM stock after that 60 day period).

(*Lipsky v Commonwealth United Corp.*, 551 F2d 887, 896 n 15 [2d Cir 1976].) The court noted that the provision compensated the affected party "for any loss due to registration delay," but observed that the provision was not a liquidated damages clause, because it had nothing to do, in that case, with a party's breach of the contract (*id.*).

However, the Registration Clause stipulates damages merely in terms of a number of shares of Arcadia's common stock which increases in proportion to the duration of Arcadia's delay in filing the registration statement, regardless of whether the value of the Shares held by Global have decreased or increased during the period of delay, and regardless of whether their change in value has been substantial or negligible. Thus, the stipulated damages bear no reasonable relationship to, and are plainly disproportionate to, the amount of Global's damages foreseeably resulting from any delay in the registration of the Shares (*cf. LeRoy v Sayers*, 217 AD2d at 70-71 [finding a liquidated damages clause to be an unenforceable penalty where the clause awarded the same exorbitant sum regardless of the season in which the breach occurred, whereas the amount of the foreseeable damages resulting from a breach varied substantially with the season]).

Enforcement of the liquidated damages provision would be inappropriate in this instance, additionally, inasmuch as Global has failed to offer any evidence indicating that it sustained any actual damages as a result of Arcadia's delay in filing a registration statement for the Shares (*see Consolidated Rail Corp. v MASP Equip. Corp.*, 67 NY2d 35, 40 [1986] [stating that the trial court should not have assessed liquidated damages "[i]n the absence of ... any proof of actual damage sustained"]). According to data agreed upon by the parties, the closing price of Arcadia common stock rose from $ .92 per share on July 20, 2004 to $2.00 on March 24, 2005, the last date for which information has been submitted (*see* Fallah Affid., ¶ 11 and Ex. E; Joint Statement Pursuant to Commercial Division Rule 19-a, ¶ 9).

Global argues that the Registration Clause is not a liquidated damages clause because the Additional Shares are payable by Arcadia not in the event of a breach of contract but, rather, as part of an alternative means of performance under the parties' contract. According to Global, the parties' contract permitted Arcadia to perform by electing either to file a registration statement for the Shares by July 20, 2004 or, alternatively, to file a registration statement for the Shares after July 20, 2004, in which case Arcadia would also have to deliver a number of "penalty shares" to Global, in accordance with the prorated formula specified in the Registration Clause. Thus, Global argues, the

Additional Shares were merely the agreed upon price to be paid by Arcadia for its decision to file the registration statement after July 20, 2004.

Courts have held contractual provisions providing for the payment of a stipulated sum to be enforceable, in certain instances, where the contract was an "alternative performance" contract, which permitted a promisor to perform in either one manner or another, but required the promisor to pay the stipulated sum if the promisor performed in one manner rather than the other.[3] More specifically, a provision which requires a promisor to pay a stipulated sum for the promisor's failure to complete performance within a specified time will generally be construed as a valid liquidated damages clause, rather than an unenforceable penalty, so long as the amount stipulated is not unreasonable, considering the circumstances surrounding the contract (*see e.g. X.L.O. Concrete Corp. v John T. Brady and Co.*, 104 AD2d 181, 183 [1st Dept 1984], *affd* 66 NY2d 970 [1985]).

However, a contract, merely because it is alternative in form, "cannot be used as a cover for the enforcement of a penalty" (36 NY Jur 2d, Damages § 170). Accordingly, where a contract stipulates an amount of damages which is payable in the event of a delay in performance, but "the amount stipulated ... when compared with the value of the subject matter of the contract and the resulting damages reasonably to be anticipated from the breach is plainly disproportionate to the probable consequences of the breach, ... [then] it should be construed as a penalty" (*id.*, § 174; *see also X.L.O. Concrete Corp. v John T. Brady and Co.*, 104 AD2d at 183-184). The Registration Clause provides for a penalty, rather than for enforceable liquidated damages, because it stipulates

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[3]*See e.g. Hasbrouck v Van Winkle* (261 App Div 679, 682 [3d Dept 1941], *affd* 289 NY 595 [1942]), in which the court noted that:

> Where the agreement of the promisor is to do a certain thing or in default thereof to pay a certain sum of money, our courts, on his failure to do the particular thing, consider him as having had his election, and hold him liable to pay the agreed sum of money. This form of contract, while approaching very near to a stipulation for a penalty for nonperformance, is distinguishable therefrom and enforced according to its terms, and is considered as giving the promisor the election to refuse to do the act and in lieu thereof to pay the amount agreed.

an amount of damages which, as previously stated, bears no reasonable relation to, and is plainly disproportionate to, Global's probable loss in the event of Arcadia's failure to file a registration statement for the shares by July 20, 2004.

It is generally the case, when a liquidated damages clause is rejected as being a penalty, that "recovery is limited to actual damages proven"; "the rest of the agreement stands, and the injured party is remitted to the conventional damage remedy for breach of that agreement, just as if the provision had not been included" (*JMD Holding Corp. v Congress Fin. Corp.*, 4 NY3d at 380 [citations and internal quotation marks omitted]). Thus, a plaintiff whose claim for liquidated damages is found not to be viable is not thereby precluded from the opportunity to establish actual damages resulting from a breach of contract (*see e.g. Pyramid Ctrs. and Co. Ltd. v Kinney Shoe Corp.*, 244 AD2d 625, 627 [3d Dept 1997]; *National Telecanvass Assoc., Ltd. v Smith*, 98 AD2d 796, 798 [2d Dept 1983]).

However, dismissal of Global's breach of contract claim is nevertheless appropriate, inasmuch as: (1) that claim alleges Arcadia's breach of contract solely by reason of, and seeks to recover damages based solely upon, Arcadia's refusal to deliver the Additional Shares, which the court finds to be an unenforceable penalty; (2) that claim does not allege Arcadia's breach of contract by reason of, or seek to recover damages based upon, Arcadia's failure to file a registration statement for the Shares by July 20, 2004; and (3) even in response to Arcadia's argument that the liquidated damages provision in the Registration Clause is unenforceable specifically upon the ground that Global has failed to adequately identify any damages which it actually sustained as a result of Arcadia's failure to file the registration statement for the Shares by July 20, 2004, Global has failed to adequately identify any such damages.

The complaint's second cause of action, alleging unjust enrichment, is also dismissed. That claim asserts that Arcadia has been unjustly enriched, at Global's expense, in the amount of the value of the Additional Shares which Arcadia should have delivered to Global but, instead, retained. Global's two causes of action for breach of contract and unjust enrichment actually assert

inconsistent alternative theories, inasmuch as "[t]he existence of a valid and enforceable written contract governing a particular subject matter ordinarily precludes recovery in quasi contract for events arising out of the same subject matter" (*Unisys Corp. v Hercules Inc.*, 224 AD2d 365, 367 [1st Dept 1996] [citation and internal quotation marks omitted]). A plaintiff may, as a matter of statute, plead inconsistent alternative theories of recovery in a complaint (*see* CPLR 3014; *Jones Lang Wootton USA v LeBoeuf, Lamb, Greene & MacRae*, 243 AD2d 168, 177 [1st Dept 1998]). However, a plaintiff is required to elect among inconsistent positions upon submission of a motion for summary judgment, "the grant of which is the procedural equivalent of a trial" (*Unisys Corp. v Hercules Inc.*, 224 AD2d at 367 [citation and internal quotation marks omitted]).

In moving for summary judgment, Global effectively elected to pursue its breach of contract claim, rather than its inconsistent unjust enrichment claim. Global's memorandum of law in support discusses only Global's breach of contract claim, and not its unjust enrichment claim. Global's reply memorandum of law argues, in support of its unjust enrichment claim, merely that the claim is properly pleaded in the alternative because, if the Registration Clause's provision for the payment of the Additional Shares is determined by the court to be either invalid or unenforceable, then its unjust enrichment claim should be allowed to proceed.[4] However, nowhere in the papers in support of its motion for summary judgment has Global maintained that the Registration Clause's provision for the payment of the Additional Shares is unenforceable and, accordingly, Global "cannot establish its claim for damages based upon the inconsistent theory of unjust enrichment" (*Unisys Corp. v Hercules Inc.*, 224 AD2d at 367).

Global's unjust enrichment claim must be dismissed, in any event, because it is indistinguishable from, and may not be used to enforce the agreement which is the basis of, the nonviable breach of contract claim asserted in the complaint's first cause of action (*see Goldstein v CIBC World Mkts. Corp.*, 6 AD3d 295, 296 [1st Dept 2004]; *Andrews v Cerberus Partners*, 271

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[4]Of course, "[a]rguments advanced for the first time in reply papers are entitled to no consideration by a court entertaining a summary judgment motion" (*Lumbermens Mut. Cas. Co. v Morse Shoe Co.*, 218 AD2d 624, 626 [1st Dept 1995]).

AD2d 348, 348 [1st Dept 2000]; *Fallon v McKeon*, 230 AD2d 629, 630 [1st Dept 1996]; *Martin H. Bauman Assoc., Inc. v H & M Intl. Transp., Inc.*, 171 AD2d 479, 484 [1st Dept 1991]).

The branch of Global's motion which seeks an award of its costs and attorneys' fees is denied, inasmuch as Global has neither succeeded on the merits of its claims nor articulated any statutory, contractual, or other basis for such an award.

Arcadia cross-moves for leave to amend its answer to assert: a new eleventh affirmative defense, which alleges that the Registration Clause's provision for the payment of the Additional Shares is an unenforceable penalty rather than a valid liquidated damages clause; a new twelfth affirmative defense, which alleges that Global's claims are barred because the Registration Clause was the result of mutual mistake, i.e., the parties' purported mistaken belief that the Shares could be registered by means of a Form SB-2; and a new counterclaim seeking reformation of the Release and/or the Registration Clause -- based upon the aforementioned purported mutual mistake -- to reflect the fact that a Form S-1 had to be used to register the Shares, and to permit filing of the Form S-1 for the Shares up until the date upon which it was actually filed.

However, the branch of Arcadia's cross motion which seeks leave to amend its answer is denied as moot, inasmuch as the branch of Arcadia's cross motion which seeks summary judgment dismissing the complaint is being granted, essentially upon the ground asserted in the eleventh affirmative defense which Arcadia proposes to add by means of an amended answer. Summary judgment may be granted on an unpleaded defense where, as here, "the opponent of the motion has not been surprised and [has] fully opposed the motion" (*Joan Hansen & Co. v Everlast World's Boxing Headquarters Corp.*, 2 AD3d 266, 267 [1st Dept 2003]; *see also Rogoff v San Juan Racing Assn., Inc.*, 54 NY2d 883, 885 [1981]).

CONCLUSION AND ORDER

For the foregoing reasons, it is hereby

ORDERED that plaintiff's motion is denied; and it is further

ORDERED that defendant's cross motion for leave to amend its answer and for summary

judgment dismissing the complaint is granted, but only to the extent that the complaint is dismissed; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

Dated: January 18, 2006

ENTER:

J.S.C.

HON. RICHARD B. LOWE, III