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

PRESENT: Hon. KARLA MOSKOWITZ PART 3

Justice

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A. FISCHER,

Plaintiff

-against-

PRODIGI, INC., and CELLCARDS OF DELAWARE, L.L.C.

Defendants

---x

Index Number 603891/2006

Motion Date:

Motion Seq. No. 004

Motion Cal. No.

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 is decided in accordance with the accompanying Decision and Order.

Dated: July 23, 2007

KARLA MOSKOWITZ J.S.C.

Check one: ☐ FINAL DISPOSITION ☒ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: I.A.S. PART 3

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A. FISCHER,

Plaintiff, Index No. 603891/2006

-against-

PRODIGI, INC. and CELLCARDS OF DELAWARE, L.L.C., **DECISION and ORDER**

Defendants.

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KARLA MOSKOWITZ, J:

In this breach of contract action, defendant Cellcards of Delaware, L.L.C. ("Cellcards") moves pursuant to 3211(a)(1), 3211(a)(7) and 3016(b) to dismiss the third and fourth causes of action in the complaint.

The complaint alleges that, in 2003, Prodigi, Inc. ("Prodigi"), a Delaware corporation, hired plaintiff, Avery Fischer ("Fischer"), as general counsel and agreed to pay him for his services and to reimburse him for his business expenses. Prodigi terminated Fischer's employment in April 2004, and, according to the complaint, at that time, Prodigi owed Fischer $100,085.40 in compensation and an additional $2,334.31 for expenses. Prodigi has since paid Fischer $12,334.31, but Fischer alleges that Prodigi still owes him $90,085.

In August 2005, Prodigi entered into an asset purchase agreement (the "Agreement") with Cellcards pursuant to which Prodigi transferred all of its operating assets to Cellcards for $170,000. Fischer contends that Cellcards not only paid significantly less than the company was worth, but, in addition, Cellcards paid the $170,000 to the IRS for back taxes and to various other entities, rather than paying Prodigi or its shareholders. Fischer contends that, as a result of the Agreement, several of Prodigi's shareholders, who were also company officers, avoided personal

liability for Prodigi's tax liability and several of the shareholders/officers received employment offers from Cellcards and equity grants from Coinstar, Inc. ("Coinstar"), Cellcards' parent company.

The complaint alleges that, as a result of the asset purchase agreement, "Prodigi is without the financial wherewithal to pay the amounts due and owing Fischer." (Complaint, ¶ 24). It also alleges that Cellcards knew about Prodigi's liability to Fischer.

The complaint states four causes of action. The first two causes of action, that are solely against Prodigi for breach of contract and violation of the New York Labor Law, are not at issue here.

The third cause of action states a claim for fraudulent conveyance against both defendants. Fischer alleges that the asset transfer was "without good faith and/or without receiving a fair equivalent in exchange therefor"; that the conveyance rendered Prodigy insolvent; and that the agreement and conveyance were "made with the actual intent to hinder, delay or defraud Prodigi's creditors, including [Fischer]." (Complaint, ¶¶ 36-38). Fischer seeks monetary damages, an order setting aside the asset transfer, an attachment and attorneys' fees.

In the fourth cause of action, Fischer states a claim for successor liability against Cellcards based on his allegation that the Prodigi-Cellcards deal was, in fact, a de facto merger, not an asset purchase; that, as a result of the deal, Prodigi does not have adequate assets to meet the claims of its creditors, including Fischer; and that, as Prodigi's successor, Cellcards is liable to Fischer for Prodigi's obligation.

ARGUMENTS

In support of its motion to dismiss the fraudulent conveyance cause of action, Cellcards

argues that Fischer has not adequately pled insolvency. It also claims that, pursuant to Section 278 of the Debtor and Creditor Law, Fischer is only entitled to a money judgment or an attachment or an order setting aside the conveyance to the extent necessary to satisfy his claim and that his demand for all three remedies requires the court to dismiss the cause of action. In addition, Cellcards contends that Fischer's claim for attorneys' fees is only available if the court finds an actual fraudulent conveyance. Moreover, Cellcards argues that Fischer did not plead "actual fraudulent conveyance" with sufficient particularity. (CPLR 3016[b]).

Cellcards argues for dismissal of the fourth cause of action alleging successor liability because Fischer does not adequately plead all the elements of a "de facto merger" and that the Agreement demonstrates that Cellcards purchased Prodigi's assets and that the deal was not a "de facto" merger or "mere continuation" of Prodigi.

In opposition to dismissal, Fischer argues, as to the third cause of action, that he has properly pled both constructive and actual fraudulent conveyance in sufficient detail and that deficiencies in the prayer for relief, if any, have no effect on the sufficiency of the allegations of fraudulent conveyance. As to the fourth cause of action for successor liability, Fischer contends that he has adequately pled all the elements of "de facto" merger and "mere continuation."

DISCUSSION

On a motion addressed to the sufficiency of the pleadings, the court must accept every factual allegation as true and liberally construe the allegations in a light most favorable to the pleading party. (*Guggenheimer v Ginzburg,* 43 N.Y.2d 268 [1977]; *see* CPLR 3211[a][7]). "We . . . determine only whether the facts as alleged fit within any cognizable legal theory." (*Leon v Martinez,* 84 N.Y.2d 83, 87-88 [1994]). "The motion must be denied if from the pleadings' four

corners 'factual allegations are discerned which taken together manifest any cause of action cognizable at law.'" (*511 West 232nd Owners Corp. v Jennifer Realty Co.*, 98 N.Y.2d 144, 151-152 [2002] [internal citations omitted]).

However, the court is not required to accept factual allegations that documentary evidence plainly contradicts. (*Bishop v Maurer*, 33 A.D.3d 497 [1st Dept. 2006]; *Robinson v Robinson*, 303 A.D.2d 234 [2d Dept. 2003]; *Ozdemir v Caithness Corp.*, 285 A.D.2d 961 [3d Dept. 2001]).

A. Choice of Law

In the matter before the court, plaintiff is a New York domiciliary, and the defendants are a Delaware Corporation and a Delaware limited liability company. Thus, the court must determine whether New York or Delaware law governs this action.

1. Fraudulent Conveyance

The Delaware statute governing fraudulent conveyances (6 Del. C. §§ 1301, *et seq*)[1] and

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[1] 6 Del. C. § 1304(a), titled Transfer Fraudulent as to Present and Future Creditors, provides:

(a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

(1) With actual intent to hinder, delay or defraud any creditor of the debtor; or

(2) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:

a. Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or

b. Intended to incur, or believed or reasonably should have believed that the debtor would incur, debts beyond the debtor's ability to pay as they became due.

New York's fraudulent conveyance law (Debtor and Creditor Law §§ 273 and 276, *infra*) are not substantially similar. Accordingly, because a conflict exists between the two laws, in the absence of applicable contractual choice-of-law provisions, "New York has adopted an 'interest analysis' that requires that 'the law of the jurisdiction having the greatest interest in the litigation be applied.'" (*Intercontinental Planning, Ltd. v Daystrom, Inc.*, 24 N.Y.2d 372 [1969]). Courts must make two separate inquiries to determine the greater interest: (1) what are the significant contacts and in which jurisdiction are they located; and (2) whether the purpose of the law is to regulate conduct or allocate loss. (*Padula v Lilarn Properties Corp.*, 84 N.Y.2d 519 [1994][citing *Schultz v Boy Scouts of America, Inc.*, 65 N.Y.2d 189 [1985]).

In all interest analyses, "the significant contacts are, almost exclusively, the parties' domiciles and the locus of the tort." (*Schultz*, 65 N.Y.2d at 193). In cases involving conduct regulating laws, such as the fraudulent conveyance allegations in this case, if the parties are domiciled in different states, the locus of the tort will almost always be determinative. (*Padula v Lilarn Properties Corp.*, 84 N.Y.2d at 522). Moreover, the New York Fraudulent Conveyance Act "was enacted to enable creditors to know with certainty that they could rely upon property of their debtors, even if situated in another jurisdiction." (*Advanced Portfolio Techs, Ltd.*, 1996 WL 51190, **5-6 [S.D.N.Y. 1996] [citations omitted]). Hence, "it is established that New York has an especially strong interest in applying its law when one of its domiciliaries alleges that he has been defrauded." (*Id.*).

Here, the defendants are a Delaware corporation and a Delaware limited liability company. Fischer is a New York resident who presumably worked in New York and suffered injury in New York. The parties do not identify where Fischer worked, but, because both

defendants are licensed to do business in New York and Fischer is a New York resident, the court assumes that Fischer's alleged injury occurred in New York. Accordingly, New York law applies to Fischer's fraudulent conveyance claim.

2. Successor Liability

Both litigants use New York Law in their arguments on this issue. The laws of Delaware and New York are substantially the same on the issue of successor liability. (*Compare Corporate Property Assoc. 8, L.P. v Amersig Graphics, Inc* , 1994 WL 148269 [Del. Ch. 1994] and *Washington Mutual Bank, F.A. v SIB Mortgage Corp.*, 21 A.D.3d 953 [1st Dept. 2005]). Because these laws are the same, the court need not address the choice of law issue regarding this cause of action. (*Dick v New York Life Ins. Co.*, 359 U.S. 437, 445, fn. 7 [1959]).

B. Fraudulent Conveyance

New York's version of the Uniform Fraudulent Conveyance Act, that is codified in the New York Debtor and Creditor Law ("DCL") §§ 270-81, governs Fischer's cause of action for fraudulent conveyance. In this state, a claim for fraudulent conveyance may allege constructive fraud or actual fraud. As to constructive fraud, DCL § 273 provides:

> Every conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent is fraudulent as to creditors without regard to his actual intent if the conveyance is made or the obligation is incurred without fair consideration.

As to actual fraud, DCL § 276 states:

> Every conveyance made and every obligation incurred with actual intent, as distinguished from intent presumed in law, to hinder, delay, or defraud either present or future creditors, is fraudulent as to both present and future creditors.

Cellcards' claim that Fischer has not pled constructive fraud, or insolvency, with sufficient particularity is without merit. CPLR Section 3016(b) requires that, when a cause of action is based on fraud, "the circumstances of the wrong shall be stated in detail." The complaint alleges that Prodigi transferred its operating assets to Cellcards for $170,000; that defendants valued Prodigi's assets at $425,288; that defendants significantly undervalued the assets Prodigi transferred; that Cellcards did not pay the $170,000 to Prodigi or its shareholders (Complaint, §§ 15-17); and that, as a result of the Agreement and conveyance, "Prodigi is without the financial wherewithal to pay the amounts due and owing Fischer" (*Id.* ¶ 24). Even under a heightened pleading standard, these allegations are sufficient to put Cellcards on notice of the transactions and occurrences constituting the alleged wrong. (*Foley v D'Agostini,* 21 A.D.2d 60 [1st Dept. 1964]; *see also Lanzi v Brooks,* 43 N.Y.2d 778, 779 [1977] [CPLR 3016(b) "requires only that the misconduct complained of be set forth in sufficient detail to clearly inform the defendant with respect to the incidents complained of"]; *Jered Contracting Corp. v New York City Transit Authority,* 22 N.Y.2d 187, 194 [1968] [acknowledging that it "is almost impossible to state in detail the circumstances constituting a fraud" when those circumstances "are peculiarly within the knowledge" of the moving party]).

Moreover, that Fischer may have requested improper relief does not require the court to dismiss the fraudulent conveyance cause of action. (*Phalen v Theatrical Protective Union No. 1,* 22 N.Y2d 34, 41 [1968]). DCL § 278, that governs Fischer's potential remedy in this action, provides:

> 1. Where a conveyance or obligation is fraudulent as to a creditor, such creditor, when his claim has matured, may,

> as against any person except a purchaser for fair consideration without knowledge of the fraud at the time of the purchase, ...
>
> a. Have the conveyance set aside or obligation annulled to the extent necessary to satisfy his claim, or
>
> b. Disregard the conveyance and attach or levy execution upon the property conveyed.

Moreover, the case law establishes that "where the assets fraudulently transferred no longer exist or are no longer in possession of the transferee, a money judgment may be entered in an amount up to the value of the fraudulently transferred assets." (*Neshwat v Salem*, 365 F. Supp.2d 508,521 [S.D.N.Y. 2005]; *Lending Textile, Inc. v All Purpose Accessories, Ltd.*, 174 Misc. 2d 318 [App. Term., 1st Dept 1997]) .

Cellcards is correct in its assertion that Fischer is not entitled to set aside the conveyance and attach Cellcards' property and collect a money judgment. However, that Fischer has requested relief in the conjunctive rather than in the disjunctive does not require the court to dismiss the cause of action. In *Phalan*, the Court of Appeals stated:

> Our determination that petitioners have. . . requested relief to which they are not entitled does not, however, serve to put them out of court. . . . [T]heir failure to request the appropriate relief is not a bar to their receiving whatever relief they may be entitled to. . . . CPLR 3017 (subd. [a]) provides in part, that a court "may grant any type of relief within its jurisdiction appropriate to the proof whether or not demanded." (22 N.Y. 2d at 41).

Accordingly, the court denies that branch of Cellcards' motion that seeks to dismiss the fraudulent conveyance cause of action.

C. Successor Liability

As a general rule, the purchaser of a corporation's assets does not, as a result of the

purchase, become liable for the seller's torts or contracts. (*Schumacher v Richard Shear Co.*, 59 N.Y.2d 239, 244-45 [1983]; *Fitzgerald v Fahnestock Co.*, 286 A.D.2d 573 [1st Dept 2001] [applying *Schumacher* to breach of contract actions]). However, "a corporation may be liable for the torts [or contracts] of its predecessor if (1) it expressly or impliedly assumed the predecessor's tort [or contract] liability, (2) there was a consolidation or merger of the seller and purchaser, (3) the purchaser corporation is a mere continuation of the selling corporation, or (4) the transaction is entered into fraudulently to escape such obligations." (*Schumacher*, 59 N.Y. 2d at 244- 245).

"A de facto merger occurs when a transaction, although not in the form of a merger, is in substance 'a consolidation or merger of seller and purchaser.'" (*Cargo Partner AG v Albatrans, Inc.*, 352 F.3d 41, 45 [2d Cir 2003] quoting *Schumacher*, 59 N.Y. 2d at 245). "The purpose of the doctrine of de facto merger is to avoid [the] patent injustice which might befall a party simply because a merger has been called something else." (*Cargo Partners AG*, 352 F.3d at 46 [citations and quotations omitted]).

"'The hallmarks of a de facto merger are: (1) continuity of ownership; (2) cessation of ordinary business and dissolution of the acquired corporation as soon as possible; (3) assumption by the successor of the liabilities ordinarily necessary for the uninterrupted continuation of the business of the acquired corporation; and (4) continuity of management, personnel, physical location, assets and general business operation.'" (*Washington Mutual Bank, F.A. v SIB Mortgage Corp.*, 21 A.D.3d 953, 954 [1st Dept. 2005], quoting *Fitgerald v Fahnestock & Co.*, 286 A.D.2d 573, 574 [1st Dept 2001]). In actions sounding in contract, such as the one before the court, "continuity of ownership is the essence of merger." (*Washington Mutual Bank F.A.*, 21

A.D. 3d at 954).

Here, the documentary evidence establishes that there is no continuity of ownership. The majority shareholders in Prodigi do not have an ownership interest in Cellcards. According to the complaint, Coinstar, Cellcards' parent, is the 100% owner of Cellcards. (Complaint, ¶ 22). Moreover, the Agreement (pp. 8-10) demonstrates that Cellcards purchased Prodigi's assets for cash, not stock, and that Cellcards paid the purchase price to the IRS and several other entities to satisfy some of Prodigi's debts. That the Agreement granted three of Prodigi's shareholders, who own a total of thirty percent of Prodigi's stock, an option to purchase a small amount of shares in Coinstar is insufficient to establish continuity of ownership because the complaint does not allege that the shareholders who own the other seventy percent of Prodigi ever became shareholders of, or have any ownership interest in, Cellcards or Coinstar. (*See Washington Mutual Bank, F.A. v SIB Mortgage Corp,* 2004 WL 1433133, *2 [Sup. Ct. N.Y. County 2004]). Fischer also does not allege that the three shareholders who received stock options in Coinstar ever exercised their options or that they continue to profit from Prodigi in any way. (*New York v National Services Industries, Inc.*, 460 F.3d 201 [2nd Cir 2006]).

Moreover, that five of Prodigi's shareholders received employment offers from Cellcards is irrelevant to the issue of continuity of ownership. (*Kretzmer v Firesafe Products Corp.*, 24 A.D.3d 158, 159 [1st Dept. 2005]). In *Employee Relations Assoc. Inc. v Xperius* (196 Misc. 2d 485, 487-488 [Sup. Ct. Monroe County 2003]), the court found that just because both the President and Chief Financial Officer of the predecessor corporation held identical positions at the successor corporation "says nothing about ownership."

In addition, even though the complaint alleges that, pursuant to the Agreement, Cellcards

granted the remainder of the Prodigi shareholders certain contingent consideration, the complaint also states that Cellcards has failed to pay the shareholders this consideration (Complaint, ¶18). Moreover, the complaint does not allege that Cellcards and Prodigi have the same management, personnel, assets and physical location. (*See Kretzmer v Firesafe Products, Corp.*, 24 A.D.3d at 159).

Plaintiff's reliance on *Schumacher v Richards Shear Co., Inc.* (59 N.Y.2d 239 [1983]) for the proposition that Cellcards can be held liable as a "mere continuation" of Prodigi is unavailing because, as the *Schumacher* court explained, the mere continuation exception "refers to corporate reorganization, however, where only one corporation survives the transaction; the predecessor corporation must be extinguished." In this case, it appears that Prodigi survived the transaction as a distinct, though meager, entity. (*Id.* at 245). Accordingly, the "mere continuation" exception is inapplicable.

Fischer does state facts sufficient to satisfy the fourth exception regarding successor liability – that is, that Prodigi and Cellcards entered into the Agreement fraudulently so that Prodigi could escape its contractual obligations. The complaint alleges that Prodigi transferred its operating assets to Cellcards for $170,000; that defendants valued Prodigi's assets at $425,288; that defendants significantly undervalued the assets Prodigi transferred; that Cellcards did not pay the $170,000 to Prodigi or its shareholders (Complaint, ¶¶ 15-17); that, as a result of the Agreement and conveyance, "Prodigi is without the financial wherewithal to pay the amounts due and owing Fischer" (Complaint, ¶ 24); and that the Agreement was made with the "actual intent to hinder, delay or defraud Prodigi's creditors" (Complaint, ¶ 38). Here, as in the fraudulent conveyance cause of action, the allegations are sufficient to apprise Cellcards of the

circumstances constituting the fraud.

Accordingly, it is

ORDERED that defendant Cellcards' motion to dismiss the third and fourth causes of action as against it is denied.

This decision constitutes the order of the court.

Dated: July 23, 2007

J.S.C.