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

PRESENT: C E Ramos Justice

PART 53

Index Number : 602081/2007

OSTER, AVI

VS.

KIRSCHNER, H. STEPHEN

SEQUENCE NUMBER : # 001

DISMISS

INDEX NO. 602081-07

MOTION DATE

MOTION SEQ. NO. #001

MOTION CAL. NO.

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

FILED
APR 23 2008
COUNTY CLERK'S OFFICE
NEW YORK

IS DISPOSED OF
IN ACCORDANCE WITH THE ACCOMPANYING
MEMORANDUM DECISION

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

Dated: 4/21/08

HON. CHARLES E. RAMOS J.S.C.

Check one: ☐ FINAL DISPOSITION ☑ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK:COMMERCIAL DIVISION
----------X
AVI OSTER and ANN OSTER,

Plaintiffs,

Index No. 602081/07

-against-

H. STEPHEN KIRSCHNER, THE WISER NOW CORP., MARK SHAPIRO, IRVING J. STITSKY, WILLIAM B. FOSTER, MARTIN P. UNGER, ESQ., CERTILMAN BALIN ADLER & HYMAN, LLC, ROBERT F. COHEN, ESQ., COHEN & WURTZ LLC, PHILIP L. CHAPMAN, ESQ., LUM, DANZIS, DRASCO & POSITAN, LLC, and JOHN and JANE DOES 1-100,

Defendants.
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Charles Edward Ramos, J.S.C.:

Motion sequence 001 and 002 are hereby consolidated for disposition.

In motion sequence 001, defendants Philip L. Chapman ("Chapman") and Lum, Danzis, Drasco & Positan LLC ("Lum") move pursuant to CPLR 3211(a)(7) to dismiss the seventh through eleventh causes of action of the complaint.

In motion sequence number 002, defendants Martin P. Unger ("Unger") and Certilman Balin Adler & Hyman, LLP ("Certilman") move pursuant to CPLR 3211(a)(1) and (7) to dismiss the complaint.

This action arises out of a collapsed fraudulent investment scheme. The motions to dismiss focus on the legal services provided by the co-defendants, Unger and Certilman (collectively the "Certilman Defendants") and Chapman and Lum (collectively the "Lum Defendants"), to Mark A. Shapiro ("Shapiro"), Irving J. Stitsky ("Stitsky"), and William B. Foster

("Foster")(collectively the "SSF Defendants"). The background in this decision will therefore focus on the legal services surrounding the alleged fraudulent transaction.

Background

The complaint alleges that during the period of November 2003 to March 2006, the SSF Defendants perpetrated a "Ponzi[1]" scheme through Cobalt Multifamily Investors I, LLC ("Cobalt Multifamily"). (Complaint ¶ 29).

Cobalt Multifamily was allegedly only one of numerous related entities (collectively "Cobalt[2]") formed by the SSF Defendants to further the Ponzi scheme. (Complaint ¶ 6).

H. Stephen Kirschner ("Kirschner") and his corporation, The Wiser Now Corp. (collectively the "Kirschner Defendants"), are alleged to have assisted the SSF Defendants by soliciting new investors. (Complaint ¶ 10).

The plaintiffs Avi Oster and Anna Oster (collectively the "Osters"), among others, were such investors. The Osters allegedly invested $1.9 million[3] in the fraudulent ventures. (Complaint ¶ 33).

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[1] In a "Ponzi" scheme, the money of new investors are used to pay off old investors until the scheme eventually breaks down when there is a lack of new investors.

[2] Cobalt consists of Cobalt Multifamily Co. I, LLC; Cobalt Capital Funding, LLC; Cobalt Financial, Inc.; Cobalt Property Services, LLC; Cobalt Capital Partners, LP; Cobalt Construction Services, LLC; and Vail Mountain Trust. (Complaint ¶ 4, 5)

[3] The Osters invested in varying amounts at varying times between November 1, 2004 until October 25, 2005. (Complaint ¶ 81-90).

The SSF Defendants and the Kirschner Defendants distributed various marketing materials containing fraudulent and misleading information about Cobalt and the investments. Among the materials were three private placement memorandums, dated December 29, 2003 (the "December 2003 PPM"), July 1, 2004 (the "July 2004 PPM"), and December 15, 2004 (the "December 2004 PPM"). The Osters also allege that an amendment (the "PPM Amendment") to the December 2004 PPM was drafted in December 2005, but backdated to November 30, 2005. (Complaint ¶ 37-8).

The December 2003 PPM, July 2004 PPM, December 2004 PPM (collectively the "PPMs") and the PPM Amendment were allegedly used with the other misleading marketing materials to bolster the history and reputation of Cobalt, to induce investors into investing, and provide false assurances that the investments were profitable. (Complaint ¶ 56-62). Furthermore, the PPMs were allegedly intentionally drafted to omit the criminal backgrounds of Shapiro and Stitsky. (Complaint ¶ 47-54).

The Osters additionally allege, upon information and belief, that the Certilman Defendants and the Lum Defendants knew or should have known of the fraud and should have acted to protect the investors. (Complaint ¶ 94-6). In addition, the Certilman and Lum Defendants both failed to properly advise Cobalt of the New Jersey Securities Act (the "NJSA") registration requirements, which allowed the fraud upon the investors to continue. (Complaint ¶ 112, 137-8).

Both the Certilman Defendants and Lum Defendants allegedly

drafted parts of the fraudulent PPMs and the PPM Amendment or approved the issuance of the PPMs. (Complaint ¶ 121, 130).

The Certilman Defendants were allegedly aware of the criminal backgrounds of Shapiro and Stitsky, but failed to advise Cobalt to disclose those facts to its investors. Additionally, the Certilman Defendants allegedly failed to disclose in the PPM Amendment, that Cobalt's office had been raided by the FBI, thereby enabling Cobalt to continue soliciting investors by providing an opinion letter, dated December 23, 2005 (the "December 2005 Letter"). (Complaint ¶ 108-24). Furthermore, the Certilman Defendants visited the Cobalt offices to advise that the PPMs were properly filed and reassure the sales force to continue its solicitation of investors. (Complaint ¶ 120).

The Osters allege that the Lum Defendants also knew or should have known about the ongoing fraudulent conduct, but failed to inform the investors. Additionally, the Lum Defendants are alleged to have failed to verify and confirm that the investments and the marketing materials were accurate and legitimate. (Complaint ¶ 125-38).

In late March 2006, the SSF Defendants were indicted, causing the scheme to collapse and exposing the fraudulent activities to the investors. (Complaint ¶ 93).

Discussion

"Dismissal under CPLR 3211(a)(1) is warranted 'only if the documentary evidence submitted conclusively established a defense to the asserted claims as a matter of law.'" (*Leon v Martinez*, 84

NY2d 83, 87-88 [1994]).

When assessing the adequacy of a complaint on a motion to dismiss pursuant to CPLR 3211(a)(7), a court must afford the pleadings a liberal construction, accept the allegations of the complaint as true, and provide the plaintiff "the benefit of every possible favorable inference." (*id.*)

Whether a plaintiff can ultimately establish its allegations is not part of the calculus in determining a motion to dismiss. *Id.* 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." (*Guggenheimer v Ginzburg*, 43 NY2d 268, 275 [1977]).

The Certilman Defendant's Motion to Dismiss

The Certilman Defendants move pursuant to CPLR 3211(a)(1) and (7) to dismiss the complaint.

The Osters' complaint contains eleven causes of action, however, only the second, fourth, fifth, sixth, and seventh through eleventh causes of action are alleged against the Certilman Defendants. The seventh through eleventh causes of action arise from violations of the "NJSA," therefore requiring the application of New Jersey law.

The Certilman Defendants argue that New York law should be applied for the second, fourth, fifth, and sixth causes of action because the Osters' causes of action pertain to the legal services rendered by the Certilman Defendants' for a New York client, Cobalt.

The Osters contend that New Jersey law should be applied to the remaining causes of action against the Certilman Defendants because the Osters reside in New Jersey and the injury stemming from the Certilman Defendant's actions had its greatest impact in New Jersey.

Choice of Law

New York uses the "interests analysis" approach in resolving choice of law issues. Under the "interests analysis" approach, the law of the jurisdiction having the greatest interest in the litigation will be applied. (*Istim, Inc. v Chemical Bank*, 78 NY2d 342, 347-8 [1991]). Furthermore, only the facts or contacts relating to the purpose of the law in conflict are significant in defining a state interest. *id.*

The first step of the "interests analysis" approach is identifying the purposes of the statutes and the policies it promotes. Then, based on the facts involving the statutes in issue, a determination is made as to which state has a greater interest in having its laws applied. (*id.*).

If conduct-regulating laws are in conflict, the law of the jurisdiction where the tort occurred will generally be applied because that jurisdiction has the greatest interest in regulating behavior within its borders. (*Cooney v Osgood Mach., Inc.*, 81 NY2d 66, 72 [1993]). Here, the laws at issue concern the regulation of the conduct of attorneys in New York.

It is well established that New York has the greatest interest in regulating the practice of law by New York attorneys.

(*Engleke v. Brown Rudnick Berlack Israels, LLP*, 45 AD3d 324, 326 [1st Dept 2007]).

It is undisputed that the Certilman Defendants, who are New York attorneys, provided the legal services to a New York client, Cobalt, in New York. The Osters were not clients of the Certilman Defendants and the complaint fails to allege any communications between the Certilman Defendants and the Osters. The only nexus between the Certilman Defendants and the Osters is Cobalt. The Certilman Defendants provided legal services to Cobalt, while the Osters invested in Cobalt.

New York clearly has the dominant interest for the application of its laws, and New York law applies to the determination of second, fourth, fifth, and sixth causes of action.

The Common-Law Causes of Action

The second, fourth, and fifth causes of action are for conspiracy and aiding and abetting common law fraud, conspiracy and aiding and abetting breach of fiduciary duty of the SSF Defendants, and conversion and conspiracy and aiding and abetting conversion, respectively.

"[C]onspiracy to commit a tort is never of itself a cause of action." (*Brackett v Griswold*, 112 NY 454, 467 [1889]). "Allegations of conspiracy are permitted only to connect the actions of separate defendants with an otherwise actionable tort." (*Alexander & Alexander, Inc. v Fritzen*, 68 NY2d 968 [1986]). The complaint only alleges the conspiracy, but fails to

allege any of the underlying actionable torts.

Aider and abettor liability attaches to the defendant only when the defendant provides substantial assistance to the primary violator. (*Kaufman v Cohen*, 307 AD2d 113, 126 [1st Dept 2003]) Substantial assistance occurs when one affirmatively assists, helps conceal or fails to act when required to do so, thereby enabling the tort to occur. *id.* However, the mere inaction of an alleged aider and abettor constitutes substantial assistance only if the defendant owes a fiduciary duty directly to the plaintiff. (*id.*). The complaint fails to allege any substantial assistance, actual knowledge, or fiduciary relationship to support the aiding and abetting causes of action.

Pursuant to CPLR 3016 [b], "a cause of action or defense is based upon misrepresentation, fraud, mistake, wilful default, breach of trust or undue influence, the circumstances constituting the wrong shall be stated in detail."

The Osters fail to allege any actionable conduct of the Certilman Defendants with specificity. Additionally, the Osters fail to allege the required elements of the underlying fraud, breach of fiduciary duty, or conversion necessary to attach third-party liability to the Certilman Defendants. Rather, the complaint contains only conclusory allegations without any factual support.

Maintaining a cause of action for conspiracy and aiding and abetting requires an underlying actionable tort. (*Hoag v Chancellor, Inc.*, 246 AD2d 224, 230 [1st Dept 1998]) (Conspiracy

cannot form the basis of an independent cause of action); (*Kaufman* at 125) (Aiding and abetting a tort requires an underlying actionable tort). Furthermore, "[a]ctual knowledge, as opposed to merely constructive knowledge, is required and a plaintiff may not merely rely on conclusory and sparse allegations that the aider or abettor knew or should have known about the tort. (*Brasseur v Speranza*, 21 AD3d 297, 299 [1st Dept 2005]).

Therefore, because the Osters failed to allege the elements of the underlying actionable torts or any actionable conduct with specificity, the second, fourth, and fifth causes of action are all defectively pled as a matter of law.

Negligence

The Osters' sixth cause of action is for negligence. The Osters allege that the Certilman Defendants were negligent in providing legal services to Cobalt. The allegations are not plead with specificity and consist of vague and conclusory statements. Furthermore, the allegations are that the Certilman Defendants were negligent in their duty to provide legal services to Cobalt. This allegation establishes privity between Cobalt and the Certilman Defendants and consequently, the Certilman Defendants owed no duty to the Osters.

In order to sustain a cause of action for negligent misrepresentation or attorney malpractice, there must be a relationship of actual privity or a relationship that otherwise closely resembles privity. (*AG Capital Funding Partners, L.P. v*

State St. Bank & Trust Co., 5 NY3d 582, 595 [2005]). Absent privity, maintaining a cause of action for attorney malpractice requires a claim of fraud, collusion, malicious acts, or other special circumstances. (*id.*).

The Osters fail to allege privity or any special circumstances that would warrant the sixth cause of action to survive dismissal. Accordingly, the sixth cause of action is dismissed.

Further, the Osters' failure to allege any common law causes of action renders the arguments pertaining to the Martin Act moot.

The New Jersey Causes of Action

The seventh through eleventh causes of action are for aiding and abetting violations of NJSA § 49:3-71(a)(1) through (5). New Jersey law will be applied for these causes of action.

As a preliminary matter, it should be noted that"[t]he rights and remedies provided by this [the NJSA] are in addition to any other rights or remedies that may exist at law or in equity, but [the NJSA] does not create any cause of action not specified in this section." (NJSA § 49:3-71 [j]). This Court's interpretation of the statute would conclude that there is no cause of action for aider or abettor liability under the NJSA. However, for purposes of completeness, this Court will address the arguments presented by the parties.

NJSA § 49:3-71(a) states:

"(a) Any person who:

> (1) Offers, sells or purchases a security in violation of subsection (b) of section 8, subsection (a) of section 9 or section 13 of P.L.. 1967, c. 93 (C. 49:3-55, 49:3-56, or 49:3-60), or
> (2) Offers, sells or purchases a security by means of any untrue statement of material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading (the buyer not knowing of the untruth or omission), or
> (3) offers, sells or purchases a security by employing any device, scheme, or artifice to defraud, or
> (4) offers, sells or purchases a security by engaging in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person, or
> (5) engages in the business of advising others, for compensation, either directly or through publications or writings, as to the value of securities, or as to the advisability of investing in, purchasing or selling securities, or who, for compensation and as a part of a regular business, issues or promulgates analyses or reports concerning securities (i) in willful violation of this act or of any rule or order promulgated pursuant to this act, or (ii) employs any device, scheme or artifice to defraud the other person or engages in any act, practice or course of business or conduct which operates or would operate as a fraud or deceit on the other person, is liable as set forth in subsection (c) of this section" (NJSA § 49:3-71 [a]).

Since the Certilman Defendants were not the offeror, seller, or purchaser of the securities at issue, NJSA § 49:3-71(a) is not applicable. The Osters seventh through eleventh causes of action appear to seek recovery pursuant to NJSA § 49:3-71(d), which states:

> "Every person who directly or indirectly controls a seller liable under subsection (a) of this section, every partner, officer, or

> director of such a seller, or investment adviser, every person occupying a similar status or performing similar functions, every employee of such a seller or investment adviser who materially aids in the sale or in the conduct giving rise to the liability, and every broker-dealer, investment adviser, investment adviser representative or agent who materially aids in the sale or conduct are also liable jointly and severally with and to the same extent as the seller or investment adviser, unless the nonseller who is so liable sustains the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the existence of the facts under paragraphs (1) through (5) of subsection (a) of this section which give rise to liability. There is contribution as in cases of contract among the several persons so liable." (emphasis added) (NJSA § 49:3-71 [d]).

"Federal securities law concepts are used to define 'control person' under the New Jersey statute." (*Abrams v Ohio Cas. Ins. Co.*, 322 NJ Super 330, 337 *cert. denied* 162 NJ 139 [1999]). "Control person liability under federal law has been construed to require a showing of active participation in management." (*id.*).

Control is defined by the Securities and Exchange Commission as "the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise." (17 CFR § 230.405 [1999]).

The United States Supreme Court held that the scope of the term "seller" extends beyond "an owner who passes title or some other interest in a security to a buyer for value." (*Pinter v Dahl*, 486 US 622, 642 [1988]). The Court then expanded seller liability to a broker or other person whose motivation to

successfully solicit the purchase is based "at least in part by a desire to serve his or her own financial interest or those of the security's owner." (*Id.* at 647).

Pursuant to NJSA § 49:3-71(d), there is secondary liability for persons who: (1) are directly or indirectly controlling a seller liable under NJSA § 49:3-71(a), (2) are partners or employees of the person directly or indirectly controlling the seller, if they materially aid the sale or conduct, or (3) are an agent of the person directly or indirectly controlling the seller, if they materially aid the sale or conduct.

The Osters argue that the Certilman Defendants qualify as "agents" under the NJSA and therefore, fall within the NJSA's jurisdiction.

The Certilman Defendants contend that they are beyond the scope of the NJSA because they are not agents as defined by the NJSA and that the Osters fail to state a cause of action under the NJSA.

The NJSA defines "agent" as: "any individual other than a broker-dealer, who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales of securities." (NJSA § 49:3-49 [b]).

The Osters allege upon information and belief that the Certilman Defendants drafted some of the PPMs and met with Cobalt on numerous occasions to advise their sales force that it was legal to continue soliciting investors. (Complaint ¶ 120). There are no further allegations that would create an agency

relationship between Cobalt and the Certilman Defendants.

Additionally, NJSA 49:3-71(d) requires that the agent materially aid the sale of securities. (NJSA 49:3-71 [d]). An agent's involvement in the sale must be "considerable, significant, or substantial" in order for liability to be imposed. (*Nicholas v Saul Stone & Co., LLC*, 1998 WL 341111036 at 19 [NJ 1998]).

There are no allegations of any conduct undertaken by the Certilman Defendants that can be viewed as considerable, significant, or substantial to the sale of the securities. (*Zendell v Newport Oil Corp.*, 226 NJ Super 431. 440-1 [App. Div. 1988]) (no liability for a law firm that was not a general partner in the venture; never acted as a broker, selling agent, or underwriter; and the law firm had no managerial position or financial investment in the seller).

Aider and abettor liability attaches when one "knows that another's conduct constitutes a breach of duty and gives substantial assistance or encouragement to the other in furtherance of the conduct." (*State, Dep't of Treasury, Div. of Inv. ex rel. McCormac v Qwest Communications Intern., Inc.*, 387 NJ Super 469, 481 [App. Div. 2006]). However, the conduct of the actor must in itself be tortious. (*Id.* at 482-3). "One who innocently, rightfully and carefully does an act that has the effect of furthering the tortious conduct or cooperating in the tortious design of another is not for that reason subject to liability." (*id.*).

Consequently, the seventh through eleventh causes of action for aiding and abetting must be dismissed because the complaint lacks of any allegations of substantial and knowing assistance by the Certilman Defendants.

The Lum Defendants

The Lum Defendants move pursuant to CPLR 3211(a)(7) to dismiss the seventh through eleventh causes of action of the complaint.

The Lum Defendants are a New Jersey law firm that provided legal services to Cobalt. Like the Certilman Defendants, there are no allegations that the Lum Defendants offered, sold, or purchased any securities. Therefore, the Osters must seek recovery pursuant to NJSA 49:3-71(d).

The Osters assert that the Lum Defendants materially aided the fraud by taking on the role of escrow agent for the transactions. However, it is not alleged that the Lum Defendants failed in their duty as escrow agents, but rather, that the Lum Defendants, as escrow agents, owed a duty to investigate and disclose the fraud to the Osters.

This Court finds this argument unavailing. The allegations that the Lum Defendants' role as an escrow agent somehow rises to materially aiding the fraud is illogical. There is nothing in the complaint to suggest that if the Lum Defendants were not the escrow agents, that the fraud would not have occurred.

As previously stated, an agent's involvement in the sale must be "considerable, significant, or substantial" in order for

liability to be imposed. (*Nicholas* at 19).

Despite the allegations by the Osters, it is clear that the Lum Defendants are not "agents" as defined by the NJSA. Therefore, the seventh through eleventh causes of action are dismissed for the same reasons as the Certilman Defendants.

Replead

The Osters also request the leave to replead causes of action in the event the complaint is dismissed. At this time, the Osters have not established sufficient grounds to justify the granting of leave to replead. (CPLR 3211 [e]). Upon the submission of affidavits, if so advised, demonstrating good grounds for the assertion of the claim, leave to plead will be considered.

Accordingly, it is

ORDERED, that Philip L. Chapman and Lum Danzis Drasco & Positan, LLC's motion to dismiss the seventh through eleventh causes of action is granted, and it is further,

ORDERED, that the defendants Philip L. Chapman and Lum Danzis Drasco & Positan, LLC are directed to serve an answer to the remaining causes of action asserted against them within 10 days after service of a copy of this order with Notice of Entry.

ORDERED, Martin P. Unger and Certilman Balin Adler & Hyman LLC's motion to dismiss the complaint is granted, and the complaint is dismissed as to them, it is further,

ORDERED, that upon the submission of an affidavit setting forth good grounds for repleading, that plaintiff may be granted

leave to serve an amended complaint within 10 days after obtaining the Court's permission, which date can be no later than 20 days after the service on plaintiffs of this order and Notice of Entry. In the event that plaintiff fails to obtain the court's permission to serve an amended complaint within such time, leave to replead shall be deemed denied and the action dismissed as to defendants Philip L. Chapman, Martin P. Unger, Lum Danzis Drasco & Positan, LLC, and Certilman Balin Adler & Hyman LLC.

Dated: April 21, 2008

J.S.C.

HON. CHARLES E. RAMOS