

Able Energy, Inc. v Marcum & Kliegman LLP

2008 NY Slip Op 31363(U)

May 5, 2008

Supreme Court, New York County

Docket Number: 0603224/2007

Judge: Richard B. Lowe

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

PRESENT: HON. RICHARD B. LOWE, III

PART 56

Index Number : 603224/2007

ABLE ENERGY INC

vs

MARCUM & KLIEGMAN LLP.

Sequence Number : 001

DISMISS COMPLAINT

INDEX NO. _____

MOTION DATE 1/4/08

MOTION SEQ. NO. _____

MOTION CAL. NO. _____

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

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...

Answering Affidavits — Exhibits _____

Replying Affidavits _____

PAPERS NUMBERED

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered that this motion

FILED
MAY 13 2008

NEW YORK
COUNTY CLERK'S OFFICE

NOTION IS DECIDED IN ACCORDANCE
WITH ACCOMPANYING MEMORANDUM DECISION.

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

Dated: 1/20 5/5/08

HON. RICHARD B. LOWE, III
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: IAS PART 56

-----X
ABLE ENERGY, INC., a Delaware corporation and
GREGORY D. FROST,

Plaintiffs,

Index No. 603224/07

-against-

MARCUM & KLIEGMAN LLP, a limited liability
Partnership, STEPHEN FELDMAN, PAUL SHERMAN,
JEFFREY WEINER, STEVEN KRIETE, PHILIP
WEINER and GREGORY DIGULLIO,

Defendants.

-----X
RICHARD B. LOWE III, J. :

Defendants move pursuant to CPLR 3211(a)(7) for dismissal of the complaint.

Background

Plaintiff Able Energy, Inc. (Able) is a publicly traded Delaware corporation with its place of business in New York City. Plaintiff Gregory D. Frost (Frost) is the Chairman of the Board of Directors and Chief Executive Officer of Able. Able and defendant Marcum & Kliegman LLP (M&K) entered into three agreements between 2005 and 2007 to perform various functions, including an audit and review, as well as preparing an annual Form 10-K for the SEC. The complaint states that pursuant to an order of investigation, on August 30, 2006, the SEC issued subpoenas to Able and certain officers and directors of Able, including Frost.

Shortly thereafter, on September 28, 2006, Frost took a leave of absence as Chief Executive Officer, and resigned as Chairman. Plaintiffs allege that Frost originally resigned due to pressure from M&K, which had refused to complete its audit of Able. Plaintiffs also allege that M&K did not complete its audit or file the 10-K Report until April 12, 2007, nearly seven

months after the filing deadline. Furthermore, although M&K's fee for the completion of Able's year-end audit was to be between \$275,000 and \$325,000 as set forth in their agreement, Able claims that it was forced to pay over \$800,000 to M&K for the audit.

At the conclusion of this audit, M&K issued a letter providing that Able had fulfilled the requirements under the Sarbanes-Oxley Act and that M&K found no improper or illegal acts with regard to either Able, its management or its operations.

By agreement executed on April 3, 2007, M&K agreed to review Able's financial documents and to review and approve Able's Form 10-Q Report for the quarters ending September 30, 2006 and December 31, 2006. On May 24, 2007, Frost returned to his position as Chief Executive Officer of Able. Although M&K stated that it would conclude its review by mid-June 2007, Able was not able to file its Form 10-Q for the quarter ending September 30, 2006 until July 24, 2007 and its Form 10-Q for the quarter ending December 31, 2006 until July 31, 2007.

By agreement executed on July 12, 2007, M&K agreed to conduct an audit of Able's financials for the quarter ending March 31, 2007 and to review and approve Able's Form 10-Q for said quarter. On August 9, 2007, right before the report was filed, Able received three invoices from M&K charging Able an additional \$180,000 over and above the \$90,000 Able had allegedly agreed to pay M&K for its services under the second and third agreements. Plaintiffs claim that the invoices did not specify any description of the work allegedly conducted by M&K, other than a one line statement, did not specify the services provided, and did not specify the time expended. Upon receipt of the invoices, Frost sought to discuss the invoices with partners of M&K, but no meeting took place.

On August 10, 2007, M&K refused to release the latest Form 10-Q unless it received payment of the \$180,000 and unless Frost resigned as Chief Executive Officer of Able. Subsequently, Able's Board of Directors unanimously approved the termination of M&K as Able's independent auditor,

As required by SEC rules, on August 13, 2007, Able filed a Form 8-K with the SEC, announcing the termination of M&K as its auditor. Prior to the filing, Able sent a letter to M&K setting forth the reason for the termination and enclosing a copy of the Form 8-K. On August 24, 2007, M&K provided a letter to Able which stated, inter alia, that:

Mr. Frost may not have been completely forthright in his communications with us on matters related to the conduct of our audit and/or review procedures. Such matters included the SEC investigation ... as a result of [Defendants'] inability to rely on the representations of the Company's [Able's] CEO that have been provided to date, we are no longer willing to be associated with the condensed consolidated financial statements of the Company for the quarterly periods ended September 30, 2006 and December 31, 2006 and have withdrawn our completed reviews relating to such financial statements.

Plaintiffs state that at no time prior to August 24, 2007 did defendants assert or imply that Frost was not forthright in his communications on matters related to M&K's audit or any other matter. Defendants forwarded the letter to the SEC on August 29, 2007. As a result, Able was required, under applicable SEC regulations, to file the letter on an amended Form 8-K and thus, disseminate to the public the alleged misrepresentations contained in defendants' letter.

Plaintiffs commenced this action on October 1, 2007. They assert the following causes of action: breach of contract (brought against M&K); breach of the covenant of good faith and fair dealing (brought against M&K); breach of fiduciary duty (brought against all defendants);

negligence (brought against all defendants); gross negligence (brought against all defendants); and defamation (brought against all defendants).

Defendants seek dismissal of the complaint on three grounds. First, they argue that plaintiffs' causes of action for breach of contract, breach of covenant of good faith and fair dealing, breach of fiduciary duty and gross negligence must be dismissed as duplicative of plaintiffs' negligence claim. The claims allegedly rely upon the same facts and do not plead distinct damages. Second, they contend that in the negligence claim, plaintiffs failed to plead how they have been damaged as the proximate result of any conduct by defendants. Third, defendants argue that the defamation claims must be dismissed because M&K's communications are absolutely privileged. By sending the letter to the SEC, defendants claim that they are immunized from legal action, because the letter was a communication to a public forum which was investigating plaintiffs in its quasi-judicial capacity.

Discussion

Negligence

The court will first determine the validity of the negligence claim. In order to establish a prima facie case of negligence, plaintiffs must demonstrate: (1) the existence of a duty on defendants' part as to plaintiffs; (2) a breach of this duty; (3) an injury to plaintiff as a result thereof. (*Gaeta v City of New York*, 213 AD2d 509, 510 [2d Dept 1995]). An injured plaintiff may recover from defendant all damages flowing from and as a natural consequence of a wrongful act, so long as damages may be ascertained with reasonable certainty. (*See Behrens v Metropolitan Opera Ass'n, Inc.*, 18 AD3d 47, 50 [1st Dept 2005]). Here, defendants contend that plaintiffs do not and cannot assert that damages can be ascertained by alleged wrongful acts on

defendants' part.

In opposition to the motion, plaintiffs claim to have the right to allege alternative theories during the pleading stage. Plaintiff argue that their negligence claim is valid and cite the following: Defendants failed to discharge their responsibilities in a reasonable manner and failed to exercise that degree of skill and care that reasonable professionals of similar standing would exercise under the circumstance presented. (Complaint at par. 86). As a result of defendants' conduct, plaintiff could not file its March 31, 2007 Form 10- Q Report. Had Able filed the report, absent defendants' wrongful and improper interference, it would have achieved filing compliance for the first time in approximately eleven months. As a result of Able's inability to file the Report and thereby achieve filing compliance, it was unable, among other things, to apply for listing on the OTC Bulletin Board, file a registration statement, enter into any acquisition or merger agreement or obtain institutional financing (Complaint¶ 47).

Upon review, the court finds that plaintiffs' assertion of damages in this claim to be speculative and remote. No actual transactions have been effected by defendants' alleged conduct. Plaintiffs have not clearly alleged monetary loss with respect to this negligence. Thus, the negligence claim is dismissed.

Breach of Contract and Breach of the Implied Covenant of Good Faith and Fair Dealing

Defendants assert that the breach of contract claim and the breach of the implied covenant of good faith and fair dealing claim should be dismissed because they are duplicative of the negligence claim. Plaintiffs contend that their breach of contract claim is not based upon the same allegations as the negligence claim. They argue that the breach of contract claim is largely predicated upon their allegations that M&K overcharged Able for its services, and that M&K

ultimately failed to provide services that served as consideration for the second and third Retainer Agreements. Plaintiffs also argue that the damages for this breach consists of the amount Able was allegedly overcharged and the costs incurred by Able to retain another accounting firm to perform a review of its financial statements.

Plaintiffs state that a claim for breach of the implied duty of good faith and fair dealing can stand on its own when M&K exercise a contractual right as part of a scheme to realize gains that the contract implicitly denied or to deprive plaintiffs of the fruit of its bargain. Even if there was no breach of contract, plaintiffs aver that M&K still acted in bad faith by maliciously exercising its discretionary rights.

Within every contract is an implied covenant of good faith and fair dealing, and when the contract contemplates the exercise of discretion, this pledge includes a promise not to act arbitrarily or irrationally in exercising that discretion. (*AFBT-II, LLC v Country Village on Mooney Pond, Inc*, 305 AD2d 340, 342 [2d Dept 2003]).

The court finds that plaintiffs have alleged a breach of contract claim, with respect to the alleged overcharge. This has not been alleged in the negligence claim. However, the breach of the implied covenant shall be dismissed as to there is no demonstration of discretionary rights being abused by M&K.

Breach of Fiduciary Duty

As for the breach of fiduciary duty claim, defendants state that it is duplicative of the negligence claim. They also assert that a relationship between an accountant firm and its client is not a fiduciary one. Plaintiffs assert that there are exceptions to the rule that accountants are not fiduciaries, particularly where accountants act maliciously or fraudulently toward their clients.

As a general rule, accountants are not fiduciaries as to their clients, except when the accountants are directly involved in managing the client's investment. (*Caprer v Nussbaum*, 36 AD3d 176, 194 [2d Dept 2006]). This is not the case here. Plaintiffs cite *Nate B. & Frances Spingold Foundation v Wallin, Simon, Black & Co.*, 184 AD2d 464, 465 (1st Dept 1992). That decision holds that where the allegations include knowledge and concealment of illegal acts and diversions of funds, a claim for breach of fiduciary duty can stand against an accountant. The complaint does not alleged illegal acts and defendants are not placed on such a level of liability. Therefore, the claim for breach of fiduciary duty is dismissed on the ground of a lack of a fiduciary relationship.

Gross Negligence

Plaintiffs do not specifically address the gross negligence claim which defendants seek to dismiss. As they do not apparently challenge the argument made by defendants, this claim shall be dismissed.

Absolute Privilege

The last issue involves the application of privilege, specifically absolute privilege. An absolute privilege affords a speaker or writer immunity from liability for an otherwise defamatory statement to which the privilege applies, regardless of the motive with which the statement was made. (*Sexter & Warmflash, P.C. v Margrabe*, 38 AD3d 163, 170, [1st Dept 2007] *citations omitted*). The absolute privilege conferred upon participants in judicial, legislative or executive proceedings applies to those involved in administrative proceedings in which the administrative body performs quasi-judicial functions, such as the holding of hearings which result in remedial action. (*Schettino v Alter*, 140 AD2d 600, 601[2d Dept 1988]). Statements

made by parties, attorneys or witnesses in the course of a judicial or quasi-judicial proceeding are absolutely privileged, notwithstanding the motive with which they are made, so long as they are material and pertinent to the issue to be resolved in the proceeding. (*Sinrod v Stone*, 20 AD3d 560, 561 [2d Dept 2005]).

Defendants argue that the letter, which was published and sent as part of a 8-K Report to the SEC, was pertinent to the SEC's investigation of plaintiffs, which they insist is an ongoing quasi-judicial proceeding. They contend that the contents of this letter are subject to an absolute privilege. In opposition, plaintiffs argue that the letter was sent to SEC's Division of Corporate Finance, which does not conduct investigations, and oversees the collection of and reviews Forms 8-K and other public filings. If the letter was sent to SEC's Enforcement Division, which conducts investigations, the letter allegedly would be subject to such a privilege. Furthermore, plaintiffs state that the SEC has not commenced any such proceeding as to the subject matter of the letter or the 8-K Report.

The court finds that defendants do not have an absolute privilege with respect to the letter. Defendants are not participants in the SEC's quasi-judicial proceeding and the letter was not sent to the Enforcement Division. The letter is not sufficiently pertinent to the ongoing investigation conducted by the SEC. There is no absolute privilege applicable to the letter.

In a footnote in their memorandum, defendants state that the defamation claim is brought against all the defendants, including the individual defendants. Defendants contend that the letter cannot attach liability to the individual defendants. The court agrees. The letter was signed by M&K, a limited liability partnership, and not by the individual defendants. Only M&K is liable for defamation.

Conclusion

Accordingly, it is

ORDERED that defendants' motion to dismiss is granted with respect to the third cause of action (breach of the covenant of good faith and fair dealing), the fourth cause of action (breach of fiduciary duty), the fifth cause of action (negligence) and the sixth cause of action (gross negligence); and it is further

ORDERED that the seventh and eighth causes of action (defamation) are dismissed as against the individual defendants; and it is further

ORDERED that the remainder of the action shall continue; and it is further

ORDERED that defendant Marcum & Kliegmen, LLP is directed to serve an answer to the complaint within 10 days after service of a copy of this order with notice of entry; and it is further

ORDERED that the Clerk of the Court is directed to enter judgment accordingly.

DATED: May 5, 2008

ENTERED


HON. RICHARD B. LOWE, III

J.S.C.

FILED
MAY 13 2008

NEW YORK
COUNTY CLERK'S OFFICE