

VO2Max, LLC v Greenhouse Intl., LLC

2008 NY Slip Op 32598(U)

September 24, 2008

Supreme Court, New York County

Docket Number: 0102624/2007

Judge: Richard B. Lowe

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SCANNED ON 9/30/2008
SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: _____
Justice

PART 56

VO2 Max LLC

INDEX NO. 102624/07

MOTION DATE 8/5/08

- v -

MOTION SEQ. NO. 005

Greenhouse International

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 ...

PAPERS NUMBERED

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

SEP 30 2008

COUNTY CLERK'S OFFICE
NEW YORK

Dated: 9/24/08

HON. RICHARD B. LOWE, III

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 REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: I.A.S. PART 56

-----X
VO2MAX, LLC,

Plaintiff,

-against-

GREENHOUSE INTERNATIONAL, LLC
and GREENHOUSE NUTRITIONALS, LLC

Defendants.

RICHARD B. LOWE III, J:

In this breach of contract action, plaintiff-counterclaim defendant VO2Max, LLC (“VO2Max”) and counterclaim defendant George Marom (“Marom”), managing member of VO2Max (collectively “counterclaim defendants”), move pursuant to CPLR 3211(a)(1) and (7) to dismiss the counterclaims asserted by Greenhouse Nutritionals, LLC (“Nutritionals”).

BACKGROUND

VO2Max owns all of the rights and intellectual property relating to an appetite suppressant known as Blokk which is delivered to the body through the application of a lip balm or lip gloss. In April, 2006, VO2Max and defendant Greenhouse International, LLC (“International”) entered into a distribution and License Agreement (“the License Agreement”) wherein International, as licensee, agreed to pay VO2Max, the licensor, royalty fees on dates certain (Sharma Aff., Ex. A, para. 3.2) and to spend a minimum of one million dollars in the first year of its marketing campaign for Blokk. (Sharma Aff., Ex. A, para 4.1[a]).

Paragraph 13.2 of the License Agreement permits International to assign its interest in the License Agreement and in July, 2006, pursuant to an “Assignment Agreement And First Addendum to Distribution And License Agreement” (the “Addendum”), International, as

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licensee assigned all of its rights, title and interest in the License Agreement to Nutritionals

The complaint alleges that the defendants defaulted on their obligations under the contract in that neither defendant made the \$125,000 minimum royalty payment that was due on December 31, 2006 and neither defendant expended the minimum \$1 million in marketing. The complaint states causes of action for breach of contract and specific performance against both defendants.

Nutritionals answered and asserted four counterclaims against VO2Max and Marom. The first counterclaim, alleging fraud in the inducement, claims that, prior to entering into the agreement, Marom represented that: 1) provisional patent applications and utility patent applications had already been filed; 2) the Blokk formula was "ingredient specific" and had patent protection; 3) manufacturing for Blokk was in place and the product was ready for immediate production; 4) VO2Max had conducted an independent study that confirmed Blokk's safety and effectiveness; 5) Blokk was ready to market and did not require FDA or state approval and 6) VO2Max was one of two exclusive distributors of imported Hoodia, a major ingredient of Blokk. Nutritionals asserts that these representations were material and that International justifiably relied on these representations when it entered into the License Agreement that was subsequently assigned to Nutritionals. It also claims that the representations were false and that Nutritionals has been damaged thereby.

The second counterclaim for breach of contract alleges that VO2Max breached: 1) Section 2.8 of the License Agreement¹ because VO2Max has failed to make any disclosure

¹ Section 2.8 of the License Agreement states:

LICENSOR has filed a provisional patent application

regarding the provisional patent application and has failed to cooperate with Nutritionals to maximize Blokk's intellectual property protection; 2) Section 2.4 of the License Agreement which guarantees that the per unit price for the product will not exceed two dollars (\$2.00); 3) Section 4.5 of the agreement because VO2Max failed to maintain product liability insurance in an amount consistent with industry standards; and 4) Sections 3.2 and 5.2 of the agreement which limit plaintiff's remedies for breach of the License Agreement to termination of the agreement. Nutritionals also alleges that VO2Max breached the representations in the License Agreement that the product was ready to market and that no FDA approval was necessary.

The third counterclaim states a cause of action for quantum meruit and the fourth counterclaim, asserted against Marom, alleges operation through an unlawful corporate veil.

In May, 2007, VO2Max and Marom answered, generally denying the allegations in the counterclaims.

CONTENTIONS

In support of the motion to dismiss the counterclaims, VO2Max and Marom argue that the fraud counterclaim fails because it is duplicative of the breach of contract claim and that Nutritionals could not have justifiably relied on the alleged verbal representations because the agreement is an "as is" license with a merger clause and a provision which prohibits oral modifications. In addition, it states that Nutritionals cannot complain that it reasonably relied on the alleged representations because it failed to conduct any due diligence to verify the accuracy

LICENSOR will upon signing of this agreement make full disclosure to the LICENSEE on the status of all patent applications and plans for any office action responses or new applications . . . , and the parties will work in good faith to protect the Product's intellectual property rights.

of the statements.

VO2Max and Marom contend that the breach of contract claim must be dismissed because it is negated by documentary evidence which demonstrates: 1) that VO2Max disclosed information regarding the patent application; 2) that it maintained adequate product liability insurance coverage and 3) that the price per unit for the product did not exceed two dollars (\$2.00). It also claims that the exclusive remedy provision of the contract is not applicable in this case because the complaint alleges that Nutritionals engaged in "willful conduct". Moreover, it states that the contract does not contain a representation that the product was ready to market and/or did not need FDA or state approval.

Further, the counterclaim defendants argue that the quasi-contract claim for quantum meruit will not lie because the matter is controlled by contract and that the allegations of "unlawful operation through a corporate veil" do not state a cause of action.

In opposition to the motion, Nutritionals contends that it stated all the necessary elements of a fraud claim with sufficient particularity. It also claims that its reliance on VO2Max's statements was justified because: 1) it was unable to conduct due diligence to test the accuracy of the alleged misrepresentations in that provisional patent applications are not published or publicly available and; 2) it did not have access to the product, information about the manufacturer or access to the alleged independent study until after it signed the License Agreement. Nutritionals also argues that the fraud claim is not precluded by the merger clause in the contract or the breach of contract claim because the fraud claim is based on VO2Max's extraneous misrepresentations that induced International to enter into the contract and that New York law recognizes that such extraneous conduct may support an independent tort claim and/or

that a “boilerplate” general merger clause is ineffective to exclude parol evidence of fraud in the inducement .

In addition, Nutritionals claims that it has sufficiently stated all of the elements of the claims of breach of contract, quantum meruit and corporate veil piercing and that those claims should not be dismissed at the pleading stage.

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, “a CPLR 3211 dismissal may be granted where the documentary evidence conclusively establishes a defense to the asserted claims as a matter of law.” (*Goldman v. Metropolitan Life Ins. Co.*, 5 N.Y.3d 561, 571 [2005]). Moreover, allegations that consist of “bare legal conclusions or that are “inherently incredible” need not be accepted as true. (See, e.g. *Beattie v. Brown & Wood*, 243 A.D.2d 395 [1st Dept 1997][citations omitted])

Fraud in the Inducement

To plead a viable cause of action for fraud arising out of a contractual relationship, plaintiff must allege a breach of duty that is collateral or extraneous to the contract (*Krantz v.*

Chateau Stores of Canada, Ltd., 256 A.D.2d 186, 187 [1st Dept 1998]; *see also, e.g. Rivas v. Amerimed*, 34 A.D.3d 250 [1st Dept 2006]). A plaintiff cannot recast a breach of contract action as one for fraudulent inducement. (*Weitz v. Smith*, 231 A.D.2d 518, 519 [2nd Dept. 1996]). Where the fraud claim is premised on the alleged breach of contract, it is subject to dismissal. (*Metropolitan Trans. Authority v. Triumph Advertising Products*, 116 A.D.2d 526, 527 [1st Dept 1987]).

The branches of the fraud claim that allege that VO2Max misrepresented the status of the patent application and that Blokk was ready for immediate production are dismissed because those claims arise from the contract. To the extent that Nutritionals claims that the provisions in the contract are untrue, that is a claim for breach of contract, not a claim for fraud or fraudulent inducement. “A cause of action for fraud does not lie where the only fraud claim relates to a breach of contract [.]” (*Ross v. DeLorenzo*, 28 A.D.3d 631, 636 [2nd Dept 2006]).

In addition, the branches of the fraud claim based on the allegations that VO2Max misrepresented that the Blokk formulation had patent protection in place; that VO2Max had conducted an independent study of Blokk’s safety; that VO2Max was one of two exclusive distributors of Hoodia and that Blokk was ready to market without FDA approval are also dismissed.

It is well settled that a sophisticated party entering into a transaction has a greater burden than an average contracting person to undertake due diligence to check the facts represented by the other party. (*See, e.g., Valassis Communications, Inc. V. Weimer*, 304 A.D.2d 448, 449 [1st Dept 2003]). “A party will not be relieved of the consequences of his own failure to proceed with diligence or exercise caution with respect to a business transaction.” (*Cantor Fitzgerald Inc.*

v. Cantor Fitzgerald Sec., 268 A.D.2d 324, 326 [1st Dept 2000] *aff'd* 95 N.Y.2d 919 [2000]).

Nutritionals does not deny that it is a sophisticated company with experience in marketing and that it was represented by counsel during negotiation of the License Agreement. In the circumstances here, Nutritionals had a duty to exercise ordinary intelligence and conduct an independent appraisal of the risk it was assuming. (*Abrahami v. UPC Constr. Co.*, 224 A.D.2d at 234). A party has not been defrauded when his or her own lack of due care is responsible for the predicament. (*Rodas v. Manitaras*, 159 A.D.2d 341, 343 [1st Dept 1990]). Indeed, if a party has been put on notice of the existence of material facts which have not been documented in the agreement and that party nevertheless proceeds with the transaction without securing documentation or inserting appropriate language in the agreement for his or her protection, he or she may be deemed to have willingly assumed the business risk that the facts may not be as represented. (*Rodas v. Manitaras*, 159 A.D.2d at 343; *Curran, Cooney, Penney, Inc. v. Young & Koomans*, 183 A.D.2d 742 [2nd Dept 1992]; *Chase Manhattan Bank v. New Hampshire Ins. Co.*, 193 Misc.2d 580 [Sup. Ct. N.Y. County 2002])

In *Rodas*, plaintiff sought rescission of a sale and lease agreement for a restaurant business on the ground that defendants falsely represented that the weekly income of the business was \$20,000 and that the false representation induced them to enter into the contract. There, as here, plaintiff requested an opportunity to examine certain business records and was refused access to the records. In that case the court stated:

It is apparent that they were aware that the income of the business was a material fact in [sic] which they had received no documentation. In entering into the contract with the assistance of counsel and without conducting an examination of the books and records, plaintiffs clearly assumed the risk that the documentation might not support the \$20,000

weekly income that was represented to them.
(*Rodas v. Manitaras*, 159 A.D.2d at 342)

In dismissing the fraud claim, the court stated that plaintiff could have protected itself by either insisting on examination of the books and records as a condition of closing or including a condition subsequent in the contract that provided that the sale could be rescinded if the actual weekly sales were significantly less than represented by the defendants.

In this case, Nutritionals claims that it requested and was refused access to information regarding the Blokk formulation, the product manufacturer, the alleged independent study and the need for FDA/state approval. As in *Rodas*, Nutritionals was aware that it had not received information about matters that it now claims were material to its decision to enter into the contract and, here, as in *Rodas*, it could have protected itself by insisting on receipt of the information prior to closing or by inserting appropriate "condition subsequent" language in the License Agreement. (See, *Global Minerals & Metals Corp. v. Holme*, 35 A.D.3d 93, 100 [1st Dept 2006][“when a party to whom a misrepresentation is made, has hints of its falsity, a heightened degree of diligence is required of it.”]) Instead of insisting on these protections, Nutritionals entered into an “as is” License Agreement that contained no representations and warranties about the matters it claims were material. In addition, the License Agreement contains a merger clause that states the License Agreement is the entire agreement and that it, “supersedes any prior understanding and agreements, oral or written, between such parties, regarding the subject matter hereof.” (Sharma Aff., Ex. A Section 13.6)

Under the circumstances, Nutritionals cannot demonstrate that it reasonably relied on VO2Max’s alleged oral representations and, accordingly, the first counterclaim alleging fraud in the inducement is dismissed.

Breach of Contract

The second counterclaim properly alleges breach of the License Agreement, setting forth (a) the formation of an agreement; (2) performance by the counterclaim plaintiff ; (3) breach of Sections 2.4, 2.8, 3.2, 4.5 and 5.2 of the License Agreement by the counterclaim defendants and (4) damages resulting from the breach. (*Morris v. 702 East Fifth Street HDFC*, 46 A.D.3d 478, 479 [1st Dept 2007])

Counterclaim defendants' argument that the documentary evidence negates this cause of action is without merit. First, as to the provisional patent application (Section 2.8), VO2Max has not produced a copy of the patent application or proof that it was filed. Rather, it has attached a draft copy of some data that was presumably filed with the provisional patent application (Sharma Aff, Ex. D[1]). This evidence does not conclusively establish a defense to the breach of contract claim because it does not demonstrate that VO2Max "has filed a provisional patent application with the United States Patent and Trademark Office, which application has been assigned application number" (Sharma Aff, Ex. A, Section 2.8) VO2Max has not provided an application number or an application cover sheet to prove that it fulfilled its obligation under the License Agreement.

In addition, the question of whether the product can be manufactured for \$2.00 cannot be determined at this stage of the litigation. Nutritionals claims the cost of manufacture is \$2.06 and VO2Max asserts that the manufacturing costs only \$2.00. VO2Max attaches an October 3, 2006 email from Marom to a Nutritionals employee as proof of the manufacturing cost. (Sharma Aff. Ex. D[6]) However, this email does not provide irrefutable documentation that Blokk can be manufactured for \$2.00 and it does not conclusively establish that "label cost of \$.06/unit"

should not be considered part of the manufacturing cost. At the pleading stage, counterclaim plaintiffs must be given the benefit of every possible inference. (*Goldman v. Metropolitan Life Ins. Co.*, 5 N.Y.3d 561, 570-571 [2005])

Moreover, although VO2Max has produced evidence that it maintained a \$5,000,000 product liability policy (Sharma Aff., Ex. 10) it does not provide proof that this amount of insurance is “consistent with industry standards for a consumer product in the nature of the Product.” (Sharma Aff, Ex. A, Section 4.5)

Accordingly, Nutritionals has properly pleaded a claim for breach of Sections 2.4, 2.8 and 3.5 of the License Agreement.

However, that branch of the breach of contract counterclaim that alleges that VO2Max breached the License Agreement by bringing this litigation is dismissed. The clear language of Section 5.2 states, “in the absence of fraud or willful misconduct, [termination of the agreement] shall be LICENSOR’s sole and exclusive remedy.” (Sharma Aff., Ex. A, Section 5.2) The complaint in this action alleges that Nutritionals’ breach of the agreement was willful, and so the exclusivity clause is not a bar to the action.

In addition, although Nutritionals asserts that VO2Max claimed that Blokk was ready to market and did not need FDA approval, the License Agreement is devoid of a representation or warranty regarding Blokk’s marketability and/or FDA approval. Accordingly, that branch of the breach of contract claim must also be dismissed.

Quantum Meruit

It is well settled that when a valid and enforceable written contract governs a given subject matter, recovery in quasi-contract is precluded. (*Goldman v. Metropolitan Life Ins., Co.*,

5 N.Y.3d at 746-747; *Clark Fitzpatrick, Inc. v. Long Island Rail Road Co.*, 70 N.Y.2d 382 [1987]). In this case it is undisputed that a License Agreement existed which governed the amounts due the parties under that agreement. Therefore, Nutritionals' quasi-contract counterclaim for quantum meruit must be dismissed. (*Cox v. NAP Construction Co., Inc.*, 10 N.Y.3d 592 [2008], 2008 WL 2276160 at *7)

Operation through an Unlawful Corporate Veil

The fourth counterclaim² seeking to pierce the corporate veil is dismissed. In order to pierce the corporate veil, Nutritionals must plead and prove that the owner of the corporation completely dominated the corporation in regard to the transaction involved and that the domination was used to commit a fraud or wrongdoing against Nutritionals and that Nutritionals was damaged thereby. (*Matter of Morris v. New York State Department of Taxation and Finance*, 82 N.Y.2d 135 [1993]; *Old Republic National Title Ins. Co. v. Moskowitz*, 297 A.D.2d 724 [2nd Dept 2002]). Domination, without the additional showing that the domination led to fraud, inequity or malfeasance, is insufficient to support piercing the corporate veil. (*TNS Holdings v. MKI Sec. Corp.*, 92 N.Y.2d 335, 339 [1998])

Here, Nutritionals has not alleged, with the requisite particularity, facts that establish that Marom, through his domination, "abused the privilege of doing business in the corporate form to perpetrate a wrong or injustice against [Nutritionals] such that a court of equity will intervene." (*Sheridan Broadcasting Corp. V. Small*, 19 A.D.3d 331, 332-333, quoting *Matter of Morris*, 82 N.Y.2d at 142) The counterclaim, which is plead "on information and belief" simply alleges, in a conclusory fashion, that the corporation is undercapitalized, does not observe corporate

² Incorrectly denominated in the Answer and Counterclaims as the third cause of action.

formalities, and that VO2Max was created so that Marom could transfer funds and property from the corporation to himself. These general allegations will not suffice to sustain a counterclaim to pierce the corporate veil. (See, *Sheridan Broadcasting Corp. v. Small*, 19 A.D.3d 331; *Hamlet on Olde Oyster Bay Home Owners Ass'n. v Holiday Organization, Inc.*, 2006 WL 1982603 at *14 [App. Term 1st Dept])

Because the court finds that the above discussion is dispositive of the issues in this case, it will not address the parties additional arguments.

Accordingly, it is ORDERED that counterclaim defendants' motion to dismiss the counterclaims is granted to the extent that the first counterclaim alleging fraud in the inducement, the third counterclaim for quantum meruit and the final counterclaim seeking to pierce the corporate veil are dismissed in their entirety and; it is further

ORDERED that the branches of the breach of contract counterclaim that are based on Section 3.2 and 5.2 of the License Agreement and allegations that the product was ready to market and/or did not require FDA approval are also dismissed and; it is further

ORDERED that the motion is otherwise denied.

This decision constitutes the order of the court.

DATE: September 24, 2008

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