408-20 Fulton St. LLC v Shore

2009 NY Slip Op 32354(U)

October 9, 2009

Supreme Court, New York County

Docket Number: 603398/2008

Judge: Judith J. Gische

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SCANNED ON 10/14/2009

[* 1]

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

PRESENT: JUDITH J. GISCHE, J.S.C.
Justice

PART 10

Index Number : 603398/2008

408-20 FULTON STREET LLC

vs

SHORE, STEVEN

Sequence Number : 002

DISMISS

INDEX NO. ______

MOTION DATE ______

MOTION SEQ. NO. 2

MOTION CAL. NO. ______

The following papers, numbered ____ 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 annexed decision/order.

FILED
OCT 14 2009
COUNTY CLERK'S OFFICE

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

Dated: 10/9/09

JUDITH J. GISCHE, J.S.C.
J.S.C.

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: Part 10

--x

408-20 Fulton Street LLC,

Plaintiff,

-against-

Steven Shore, Barry Prevor, Giuseppe (Joe) Soccodato and Douglas Calvin,

Defendants.

--x

Decision/Order
Index No.: 603398/2008
Seq. No. : 002

Present:
Hon. Judith J. Gische
J.S.C.

Recitation, as required by CPLR 2219 [a], of the papers considered in the review of this (these) motion(s):

FILED
OCT 14 2009
COUNTY CLERK'S OFFICE
NEW YORK

Papers	**Numbered**
Def's n/m dismiss, DC affid, exhs	1
JEB affirm in opp, exhs	2
GS affid	3
8/27/09 Transcript	4
10/7/09 Correspondence, Stipulation	5

Upon the foregoing papers, the decision and order of the court is as follows:

Plaintiff is the owner of real property located at 408 Fulton Street, Brooklyn, New York (the "premises"). Plaintiff rented a portion of the premises to Steve & Barry's New York LLC ("S&B NY"), an affiliate of Steve & Barry's LLC ("S&B"), on or about May 7, 2008, pursuant to a written lease (the "Lease"). In this action, plaintiff seeks to hold the defendants liable for fraud and negligent misrepresentation in connection with the lease.

The defendants are principals or employees of S&B. Steven Shore and Barry

Prevor co-founded, owned and were co-Chief Executive Offiers of S&B, Guiseppe (Joe) Soccodato was Chief Financial Officer and Douglas Calvin was Director of Real Estate for S&B.

The defendants now jointly move to dismiss plaintiff's amended verified complaint pursuant to CPLR § 3211 (a) (1) and (7).[1] Alternatively, the defendants seek summary judgment pursuant to CPLR § 3212. Plaintiff opposes the motion in its entirety.

Issue has been joined and the note of issue has not yet been filed. Therefore, summary judgment relief is available. CPLR § 3212. Brill v. City of New York, 2 NY3d 648 (2004).

The Lease required plaintiff to pay S&B NY a $3 million "Construction Allowance". Section 6.A. of the Lease specifically provided as follows:

> Subject to the terms and conditions Set forth in this Article 6, Landlord shall pay a construction allowance of $3,000,000 as an inducement to [S&B NY] to lease the [premises], to provide the service contemplated pursuant to this lease and for the purpose of constructing or improving qualified long-term property for use in [S&B NY]'s trade or business at the [premises].
>
> ...
>
> The Construction Allowance shall be paid to [S&B NY] as follows: (I) one-third (1/3) of the Construction Allowance shall be paid to [S&B NY] within ten (10) days following the execution and delivery of the Lease by Landlord and Tenant; (ii) upon completion of fifty percent (50%) of [S&B NY's] work, Landlord shall disburse or cause ot be disbursed to [S&B NY] an amount equal to one-third (1/3) of the Construction Allowance; and (iii)

[1] The court notes that although the defendants failed to submit a copy of their Verified Answer to the motion papers, as required by CPLR § 3212 (b), the parties have agreed to stipulate that the Verified Answer be added to the record on the motion (Stipulation dated 10/7/09). The court therefore deems the Verified Answer as having been made a part of the motion papers.

> Landlord shall disburse or cause to be disbursed the remaining one-third (1/3) of the Construction Allowance within ten (10) days after the delivery to Landlord of (w) a temporary certificate of occupancy, (x) final lien waivers from the general contractor and any contractors performing work costing more than $5,000, (y) a certification from [S&B NY's] Architect that [S&B NY's] Initial Alterations have been completed, and (z) [S&B NY] lawfully opening for business in the Premises, fully fixtured.

Plaintiff alleges that the defendants induced plaintiff to enter into the lease and pay $1 million upon execution with false and misleading financial statements which overstated S&B NY's inventory, with false and misleading explanations for the fraudulent financial statements; with intentional misstatements about how and when the first installment of the Construction Allowance would be used; and by omitting material facts about [S&B NY's] financial condition.

Plaintiff claims that the 2006 and 2007 Financial Statements were fraudulent because the "Inventories" asset was "improperly inflated" in the following ways:

> [1] Inventories were maintained artificially high by "failing to take appropriate reserves for obsolescence" and
>
> [2] Inventories including costs "directly associated with the procurement of inventory" and/or "operating costs" in the "Inventories" asset.

Concerning the Construction Allowance, plaintiff maintains that at or about the lease execution, it expressed reservations about paying $1 million before commencement of construction. The defendants, however, expressly represented that "Steve & Barry's needed funds immediately upon lease execution for the purchase of elevators and escalators since those items had a long lead time and had to be ordered well in advance of any planned store opening." Plaintiff alleges that:

> In light of the elaborate improvements that Defendants represented that

> [S&B] intended to carry out, Plaintiff finally agreed in February 2008 to pay, as part of the lease, a $3 million construction allowance, in several installments as construction progressed.

On or about July 9, 2008, two months after execution of the Lease and only 47 days after S&B NY accepted plaintiff's $1 million payment, S&B and its affiliates filed for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code in the United States Bankruptcy Court for the Southern District of New York.

Plaintiff further alleges that S&B committed a "scheme to obtain hundreds of millions of dollars from landlords in up-front tenant-improvement payments."

Plaintiff has asserted two causes of action respectively for: [1] fraud and "fraud conspiracy"; and [2] negligent misrepresentation.

Discussion

Motion to dismiss pursuant to CPLR § 3211

Even though issue has been joined, the court will first consider whether dismissal is warranted pursuant to CPLR § 3211. The court accepts the facts as alleged by plaintiff as true, affording them the benefit of every possible favorable inference (EBC I, Inc v Goldman, Sachs & Co., 5 NY3d 11, 19 [2005]; Sokoloff v Harriman Estates Development Corp., 96 NY2d 409, 414 [2001]; P.T. Bank Central Asia v ABN AMRO Bank NV, 301 AD2d 373, 375-6 [1st Dept 2003]), unless clearly contradicted by evidence submitted in connection with the motion (see Zanett Lombardier, Ltd v Maslow, 29 AD3d 495 [1st Dept 2006]).

Plaintiff's first cause of action for fraud claim is premised upon the following alleged misstatements of material fact, to wit:

> [a] misrepresentations in the Financials, including but not limited to the

line items for "Inventories," "Total assets", "Total stockholders' equity," and "Total liabilities and stockholders' equity";

[b] Soccodato's March 20, 2008 email to Sutton responding to his inquiry and explaining why the inventory figure reported by S&B and its affiliates was unusually high; and

[c] Calvin's statement on or about April 8, 2008 that [the] defendants would use the first installment of the Construction Allowance to purchase elevators and escalators.

To state a cause of action for fraudulent inducement, it is sufficient that the claim alleges a material representation, known to be false, made with the intention of inducing reliance, upon which the victim actually relies, consequentially sustaining a detriment (Channel Master Corp. v Aluminium Ltd. Sales, 4 NY2d 403, 406-408 [1958]; Megaris Furs v Gimbel Bros., 172 AD2d 209, 213 [1991]). Although corporate officers may not be held liable for the mere negligent failure to discover misrepresentations made on the company's behalf, liability will attach if they participate in or have actual knowledge of the fraud (Polonetsky v Better Homes Depot, Inc., 97 NY2d 46 [2001]; People v Apple Health and Sports Clubs, Ltd., Inc., 80 NY2d 803 [1992]; Marine Midland Bank v John E. Russo Produce Co., Inc., 50 NY2d 31 [1980]).

The financial statements

Plaintiff's fraud claim premised upon the financial statements arises, in part, from S&B's inclusion of operating expenses in inventory which plaintiff argues resulted in improper inflation. This claim fails based upon documentary evidence because it is undisputed that the inclusion of operating expenses in inventory was expressly disclosed in the financial statements themselves. Therefore, any claim of a misrepresentation arising from the inclusion of operating expenses is belied by this

undisputed fact (Leon, *supra*).

To the extent that plaintiff claims that the defendants' estimate for obsolescence in connection with the Inventory numbers did not comply with Generally Accepted Account Practices, this claim is not stated with the requisite specificity because, among other reasons, plaintiff has not identified the alleged auditing standard that was violated. CPLR § 3016.

Soccodato's statement

Plaintiff next claims that Soccodato committed fraud by virtue of an email response to an inquiry made by Jeff Sutton, President of the corporation that controls plaintiff. On March 20, 2008, Sutton wrote an email to Soccodato asking the following:

> Could you explain to me your inventory positions at Jan 31st of each year? The levels of inventory seemed extremely high relative to cost of goods sold for the year. I believe inventory in house on Jan 31st was approx one and a half years of cost of goods sold. That seems very high for any time of the year and especially on Jan 31st which is a time that I would think that you would have your lowest inventory level.

Soccodato replied by email that same day as follows:

> Jeff,
>
> Because we are vertically integrated and source around the world, our lead time for orders is long and we often experience delays in receipts. Our inventories are ordered in advance to support new stores scheduled to be opened in future months.
>
> Vertical integration also means that we often carry the typical inventories of both a wholesaler and a retailer. For instance, we stock large quantities of blank goods at screenprint and embroidery facilities in the USA, solely to supply our own stores. Other retailers would generally purchase the finished products from their suppliers and thus eliminate the need for these duplicate inventories, although the cost structure of their goods would be substantially higher.
>
> Our inventory last year was also particularly high because we were

> building inventories in preparation for the launch of several new celebrity lines that launched during 2007. Current inventory per store levels are approximately 20% lower than last year.

Plaintiff claims, therefore, that Soccodato's statements in this email were "false and misleading" because they presented facially plausible explanations for high inventory numbers while concealing and failing to disclose that S&B failed to account for obsolescence and was otherwise not financially sound. Plaintiff claims that the various representations made by Soccodato were false, in light of the fact that S&B declared bankruptcy only a few weeks after the Lease was executed. Under the liberal pleading standard of CPLR § 3211, this claim sufficiently alleges a claim for the fraudulent inducement of the Lease.

The court rejects the defendants' argument that plaintiff's claim is merely one for breach of contract, and should therefore be dismissed. Although a fraud claim should be dismissed as redundant when it merely restates a breach of contract claim (First Bank of Americas v. Motor Car Funding, Inc., 257 AD2d 287 [1st Dept 1999]), a fraud claim related to a breach of contract can be properly stated if the allegations in support of the claim concern representations collateral or extraneous to the Lease. Morgan v. A.O. Smith Corp., 221 AD2d 422 (2d Dept 1995). Here, plaintiff's fraud claim concerns the alleged representations by the defendants with respect to the present financial condition of S&B NY, which were made to induce plaintiff to enter into the lease. These allegations are distinct from an ordinary breach of contract claim.

The defendants also contend that plaintiff did not rely on Soccodato's statement, but even if plaintiff did, such reliance was unreasonable. The defendants have provided a letter from Sutton asking for "updated financials so that we can finalize this

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transaction." The defendants maintain that since plaintiff executed the Lease without ever receiving financial statements for 2008, then plaintiff "obviously understood that it could not rely on the general statement regarding sales in [Soccodato's 3/20/08 email]"

To prevail on a claim of fraud, a plaintiff must show that it actually relied on the purported fraudulent statements and that its reliance was reasonable or justifiable (see Harris v. Camilleri, 77 AD2d 861 [2d Dept 1980]). A party cannot claim reliance on a misrepresentation when he or she could have discovered the truth with due diligence (see East 15360 Corp. v. Provident Loan Socy. of N.Y., 177 AD2d 280 [1st Dept 1991]).

The defendants' argument is unavailing because it cannot establish, as a matter of law, that plaintiff's receipt of financial information for 2008 would have revealed the truth about the allegedly false representations made by Soccodatto. Plaintiff has otherwise alleged that it discharged its own affirmative duty to exercise ordinary intelligence and conduct an independent appraisal of the risks it assumed under the Lease which is sufficient for pleading purposes (see DDJ Management, LLC v. Rhone Group L.L.C., 60 AD3d 421 [1st Dept 2009]). The issue of whether plaintiff's reliance on Soccodatto's statement was justifiable remains to be determined at a later stage of this litigation.

Calvin's statement

Plaintiff's remaining claim is that it was induced to execute the Lease by a specific misrepresentation allegedly made by Calvin that "the $3 million Construction Allowance was necessary to pay for, among other things, escalators and an elevator

that would allow access to all floors of the Premises." Calvin allegedly made this misrepresentation during:

> a conference call on April 8, 2008 among [Jeff] Sutton [President of a corporation that controls plaintiff], Defendant Calvin, and others, Calvin expressed a sense of urgency about the execution of the lease and insisted that Steve & Barry's receive the first $1 million of the Construction Allowance at the time the lease was executed.

In the complaint, plaintiff alleges that:

> Calvin specifically represented that [S&B] needed funds immediately upon Lease execution for the purchase of elevators and escalators since those items had a long lead time and had to be ordered well in advance of any planned store opening.

Plaintiff then claims that S&B was in "extreme financial difficulty" at the time of Calvin's statements "about the reasons for requiring an immediate payment of $1 million." Plaintiff further alleges that S&B did not spend the Construction Allowance to pay for escalators or an elevator but commingled these funds with other funds for general operating purposes and to keep the company "afloat."

The court has already addressed plaintiff's claim that the defendants' misrepresented S&B NY's financial condition to induce plaintiff to enter into the Lease. However, to the extent that plaintiff claims that the defendants made fraudulent misrepresentations by "express[ing] a sense of urgency", representing that S&B NY would purchase elevators and escalators with the first installment of the Construction Allowance and otherwise failing to use the Construction Allowance for construction purposes only, these claims fail for the following reasons. Calvin's statements fall within the realm of non-actionable statements of future expectation or performance, rather than a misrepresentation of present fact, made to induce plaintiff to execute the

Lease.

The element of falsity is necessarily missing from plaintiff's allegations as well. In order to commence and even complete the construction contemplated by Section 6 of the Lease, S&B NY must be"afloat." Moreover, Section 6 did not contain an express provision requiring the Construction Allowance to be used solely for constructing improvements on the premises, or otherwise held in escrow or trust. To allow this purported fraud claim to proceed beyond the pleading stage would in effect rewrite the Lease itself, something that is otherwise expressly prohibited by the merger clause contained therein.

Each defendant's individual liability

The court rejects the defendants' argument that plaintiff's conspiracy claim should be dismissed, because plaintiff maintains that it has not alleged a substantive tort of conspiracy. Plaintiff's claims against Prevor and Shore remain because plaintiff has alleged a sufficient connection between the actions of these individual defendants with the fraud claim predicated upon Soccodato's statement. While the only actionable misrepresentation was made by Soccodato, plaintiff's claims against Prevor and Shore arise from inferences drawn from their positions and responsibilities at S&B and/or S&B NY, and who allegedly were the "architects" of the "scheme to obtain hundreds of millions of dollars from landlords in up-front tenant-improvement payments. (see Bernstein v Kelso & Co., Inc., 231 AD2d 314 [1st Dept 1997]). Under the circumstances, where the facts are "peculiarly within the knowledge of the party against whom the [fraud] is being asserted" (Jered Contr. Corp. v New York City Tr. Auth., 22 N.Y.2d 187, 194 [1968]), it is impossible at this stage for plaintiff to state the

circumstances in more detail because only the defendants may know the details (Grumman Aerospace Corp. v Rice, 196 AD2d 572 [2d Dept 1993]). Further detail may be revealed during discovery. In this situation, CPLR § 3016 is not to be so strictly interpreted as to prevent an otherwise valid cause of action. Id; *cf* Glatzer v. Scapptura, 116 AD2d 697 (2d Dept 1986).

Soccodato is liable for his own torts (Polonetsky v Better Homes Depot, Inc., *supra*). As to Calvin, however, since plaintiff's allegations against him are not actionable, and plaintiff has not otherwise alleged a basis for liability against him or his part in the alleged conspiracy to defraud, the first cause of action is dismissed as to Calvin, only.

Negligent misrepresentation

Plaintiff's second cause of action for negligent misrepresentation must be dismissed. Plaintiff has utterly failed to establish that any of the defendants owed it a duty. Here, the parties had no relationship other than as a result of an arms length transaction to negotiate and enter into a Lease. Therefore, a negligent misrepresentation claim does not lie (see Parisi v. Metroflag Polo, LLC, 51 AD3d 424 [1st Dept 2008]). The cases cited by plaintiff do not support its argument that a duty to speak with care existed within the context of this singular arms-length transaction. The financials and related information that the defendants provided to plaintiff is not specialized data preparation addressed in Kimmel v. Schaefer, 89 NY2d 257 (1996). Nor is plaintiff an "unsophisticated consumer" such as was the case in Smith v. Ameriquest Mortgage Co., 60 AD3d 1037 (2d Dept 2009). Accordingly, defendants' motion is granted and the second cause of action is hereby dismissed in its entirety.

<u>Alternative relief pursuant to CPLR § 3212</u>

The defendants have alternatively moved for summary judgment. The sole remaining claim under this court's analysis is for fraud, arising from Soccodato's statement, and it is asserted against Soccodato, Prevor and Shore.

On a motion for summary judgment, the proponent bears the initial burden of setting forth evidentiary facts to prove a *prima facie* case that would entitle it to judgment in its favor, without the need for a trial. CPLR § 3212; <u>Winegrad v. NYU Medical Center</u>, 64 NY2d 851 (1985); <u>Zuckerman v. City of New York</u>, 49 NY2d 557, 562 (1980). Only if it meets this burden, will it then shift to the party opposing summary judgment who must then establish the existence of material issues of fact, through evidentiary proof in admissible form, that would require a trial of this action. <u>Zuckerman v. City of New York</u>, *supra.* If the proponent fails to make out its *prima facie* case for summary judgment, however, then its motion must be denied, regardless of the sufficiency of the opposing papers. <u>Alvarez v. Prospect Hospital</u>, 68 NY2d 320 (1986); <u>Ayotte v. Gervasio</u>, 81 NY2d 1062 (1993).

Granting a motion for summary judgment is the functional equivalent of a trial, therefore it is a drastic remedy that should not be granted where there is any doubt as to the existence of a triable issue. <u>Rotuba Extruders v. Ceppos</u>, 46 NY2d 223 (1977). Under CPLR 3212(f), the court may deny a motion for summary judgment if it appears that "facts essential to justify opposition may exist but cannot then be stated."

Documents have not been exchanged and depositions have not yet been held. Plaintiff is entitled to obtain necessary discovery to substantiate its claims against Soccodato and to ascertain whether there are grounds to hold Shore and Prevor liable

thereby. Accordingly, summary adjudication is not warranted at this time.

Conclusion

In accordance herewith, it is hereby:

ORDERED that defendant's motion to dismiss the complaint is granted only to the following extent:

[1] plaintiff's second cause of action for negligent misrepresentation is dismissed; and it is further

[2] the complaint is dismissed as to defendant Douglas Calvin; and it is further

ORDERED that defendant's motion is otherwise denied.

The clerk is hereby directed to enter judgment in accordance herewith.

The court hereby schedules a preliminary conference to be held on October 29, 2009 at 9:30 a.m. in Part 10. All remaining parties are directed to appear at that time.

Any requested relief which has not been addressed herein has been considered and is hereby expressly denied.

This shall constitute the decision and order of the Court.

Dated: New York, New York
October 9, 2009

So Ordered:

HON. JUDITH J. GISCHE, J.S.C.

FILED
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