

de Hernandez v Bank of Nova Scotia

2009 NY Slip Op 33476(U)

August 4, 2009

Supreme Court, New York County

Docket Number: 601518/06

Judge: Richard B. Lowe III

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 56

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RITA MARIA SANCHEZ DE HERNANDEZ, et al.

Plaintiffs,

Index No. 601518/06

- against -

BANK OF NOVA SCOTIA a/k/a SCOTIABANK,

Defendant.
-----X

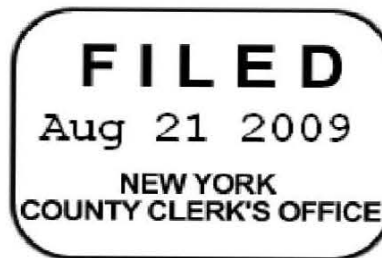
Hon. Richard B. Lowe, III

Defendant Bank of Nova Scotia moves for summary judgment dismissing the complaint.

Previously, defendant made two CPLR 3211 motions. The extensive background to this action was recited in the decisions determining those motions, dated August 8, 2008 (hereinafter, the August 2008 decision), and March 23, 2007 (the March 2007 decision). Only the facts necessary to determining this motion will be repeated here.

Remaining in the action is plaintiffs' claim for breach of contract, the other causes of action having been dismissed. The cause of action for breach of contract is based on the Existing Shareholders Agreement, also known as the Clean Up Guidelines (hereinafter, the Guidelines) (Graham Declaration, Ex. 16). The gravamen of the complaint is that the Guidelines entitled plaintiffs to receive stock in nonparty Banco Inverlat, a Mexican bank, and that defendant purchased the stock that plaintiffs should have received.

Nonparty Grupo Financiero Inverlat (GFI) is Banco Inverlat's parent company. In the 1990s, plaintiffs were shareholders in GFI. The bank experienced serious financial difficulty due to borrowers who could not repay their loans, among other reasons. In 1996, GFI and two



branches of the Mexican government entered into the Guidelines, which provided the means by which the bank would be reorganized and restored to financial health. The government agency most concerned with the reorganization was Fondo Bancario de Proteccion al Ahorro (FOBAPROA), a trust created to support distressed financial institutions. (In 1999, FOBAPROA was succeeded by Instituto para la Proteccion al Ahorro Bancario.)

The reorganization or clean-up of the bank, as described in the Guidelines, called for the shareholders, such as plaintiffs, to lose their equity interest in the bank, for FOBAPROA to become owner of all the former shareholders' shares, and for FOBAPROA to infuse capital into the bank to recapitalize it. All of this took place and GFI became indebted to FOBAPROA for the capital infusion. The bank was to repay FOBAPROA by collecting on troubled or non-performing loans, that is, loans in or close to default.

The Guidelines provided that, within a certain time, the shareholders would receive back a minimum of 9% of their prior shares. Shareholders were also given the possibility of receiving an additional 36% of their prior shares for a maximum of 45%. Whether and to what extent the shareholders would receive the additional 36% of their prior shares depended upon the reduction of GFI's debt to FOBAPROA, which in turn depended upon the bank's success in collecting on troubled loans. The more the bank collected on its troubled loans and reduced its debt to FOBAPROA, the more likely it was that the shareholders would recover up to 36% of their formerly owned shares. The Guidelines provided two alternative scenarios, Model A and Model B, of how to count and record the collection on the troubled loans. Each scenario had its own formula in the form of a mathematical fraction by which to determine whether the shareholders could recover any of the additional 36% of shares.

Pursuant to another agreement between FOBAPROA and defendant and as part of the recapitalization of the bank, defendant paid \$175 million for 10% of GFI's stock and for bonds that could be converted into an additional 45% of the stock in the future.

In March 2000, defendant and FOBAPROA signed an agreement to proceed under the Model B recovery scenario. That same month, KPMG, an accounting firm, issued a report based on the application of the Model B formula which found that the former shareholders were not entitled to receive any of the 36% of shares in the bank. According to KPMG's report, the bank did not collect enough money on the troubled loans to reduce GFI's debt to FOBAPROA to the level at which plaintiffs could receive any of the 36% of shares. Plaintiffs dispute this finding, alleging that the bank's collection was successful enough to entitle them to the shares. They allege that KPMG's report was the result of false financial information supplied by defendant.

In November 2000, defendant paid FOBAPROA \$40 million to exercise its right to convert its bonds into shares. Defendant thus became owner of 55% of the bank's shares. FOBAPROA still held 45%, of which 9% was the minimum provided for the shareholders.

In April 2003, FOBAPROA sold 36% of its shares to defendant at auction. Defendant thus became the main owner of the bank. In February 2004, the former shareholders received their 9% of GFI shares. Plaintiffs commenced this action alleging that they are entitled to the 36% that defendant purchased.

Originally, plaintiffs asserted several tort claims. Defendant made a CPLR 3211 motion to dismiss the claims based on the statute of limitations. In the March 2007 decision, the court granted the motion to the extent of dismissing on limitations grounds the claims for fraud, negligent misrepresentation, and tortious interference with contract, and denied the motion as to

the claims for breach of fiduciary duty, imposition of a constructive trust, and conversion. The tortious interference claim was dismissed for the additional reason that, as the court determined, defendant was a party to the Guidelines and a party cannot tortiously interfere with a contract to which it is a party.

Defendant made another motion to dismiss, arguing that Mexican law applied to the case and that the remaining claims did not exist under Mexican law. The court agreed with this argument, and in the August 2008 decision, dismissed the fiduciary duty, constructive trust and conversion claims. That decision was not the end of the case, however, as the court determined that the complaint included a claim for breach of the Guidelines. In the August 2008 decision, the court, sua sponte, allowed plaintiffs to assert a new claim based on breach of the Guidelines. Plaintiffs amended their complaint.

Now defendant moves for summary judgment as follows: 1) the statute of limitations on the breach of contract claim elapsed more than six years before the lawsuit was first filed on May 1, 2006; 2) defendant was not a party to the Guidelines and has no obligations thereunder to plaintiffs; 3) there is no evidence that defendant made false statements regarding the financial information that went into KPMG's report or otherwise manipulated the information; 4) after it is corrected for two errors, the Model B formula as applied by plaintiffs' own expert demonstrates that plaintiffs were not entitled to the shares that they seek; and 5) six of the plaintiffs must be dismissed from this action as they lack capacity to sue.

This decision will proceed on the assumption that defendant was a party to the Guidelines. First for determination is whether the August 2008 decision established the law of the case in regard to plaintiffs' remaining cause of action. In the August 2008 decision, the court

found that plaintiffs had a cause of action for breach of contract as third-party beneficiaries under the Guidelines, and that the breach claim accrued in 2003, the year that defendant purchased the 36% of shares that plaintiffs seek. Plaintiffs set the accrual date in 2004; however, they contend that the August 2008 decision established the law of the case in regard to the overall timeliness of the contract claim.

Where a court has determined an issue, the doctrine of law of the case precludes the parties from relitigating the same issue (*Martin v City of Cohoes*, 37 NY2d 162, 165 [1975]). For the duration of the case, the determination of the issue is binding on the parties (*id.*), provided that they had a full and fair opportunity to litigate the issue (*People v Evans*, 94 NY2d 499, 502 [2000]). If the issue was not fully litigated, meaning that it was not determined on the merits, it is not binding as law of the case (*McCoy v Metropolitan Transp. Auth.*, 53 AD3d 457, 458 [1st Dept 2008]).

Allowing the amendment of a pleading or denying a defendant's motion to dismiss the pleading does not establish the law of the case with regard to a subsequent motion for summary judgment (*James v R & G Hacking Corp.*, 39 AD3d 385, 386 [1st Dept 2007]; *Kidd v Delta Funding Corp.*, 299 AD2d 457, 457 [2d Dept 2002]). Unlike a motion for summary judgment, the motions to dismiss and to amend a pleading do not look to the sufficiency of the evidence supporting the pleading (*Kidd*, 299 AD2d at 457; *Baskin and Sears, P.C. v Lyons*, 188 AD2d 307, 307 [1st Dept 1992]; *Tenzer, Greenblatt, Fallon & Kaplan v Capri Jewelry*, 128 AD2d 467, 469 [1st Dept 1987]). The last two motions are used to determine if the plaintiff has made enough allegations to be allowed to proceed with its case and to look for proof to support its claims.

In this case, the determination in the August 2008 decision was based on the court's finding that plaintiffs' allegations constituted a timely contractual cause of action. Plaintiffs were allowed to amend their complaint accordingly. The determination was made pursuant to defendant's motion to dismiss. The determination was not based on an examination of the evidence and was not a determination on the merits. Defendant did not have an opportunity to contest the determination until this motion. Therefore, the August 2008 decision is not law of the case in regard to the timeliness of the contract claim.

A cause of action does not accrue until all of the facts necessary to sustaining the cause of action have occurred so that the complaining party would be entitled to obtain relief in court (*see Matter of Motor Veh. Acc. Indem. Corp. v Aetna Cas. & Sur. Co.*, 89 NY2d 214, 221 [1996]). In a breach of contract case, the cause of action begins to run from the date of the breach and expires six years later (CPLR 213 [2]; *Ely-Cruikshank Co. v Bank of Montreal*, 81 NY2d 399, 402 [1993]). The cause of action accrues at the time of the breach, even if the non-breaching party does not know of the breach when it occurs and is not damaged by the breach until after it occurs (*id.* at 402, 403). Here, the original complaint was interposed on May 1, 2006. For the breach claim to be timely, the act constituting the breach must have occurred from May 1, 2000 forward.

The complaint alleges that plaintiffs were both parties and third-party beneficiaries to the Guidelines. It alleges that defendant breached the Guidelines by failing to act in good faith in recording the collection of troubled loans and by providing false information on the collection of the troubled loans to Mexican government officials and KPMG. The false information resulted in calculations showing that plaintiffs were not entitled to the 36% of shares. Plaintiff's

responses to interrogatories identified March 2000 as being the month when the false information was conveyed. Plaintiffs further allege that defendant's efforts to manipulate the results of the KPMG report began in 1997. According to defendant, March 2000 was when defendant allegedly breached the Guidelines and, as more than six years passed between March 2000 and May 2006, the complaint is time-barred.

Plaintiffs argue that the breach occurred in 2004. Before plaintiffs could enforce their rights under the Guidelines in court, they first had to be declared eligible. The first eligibility decisions were published on January 28, 2004. It was in 2004 that plaintiffs received their 9% of shares in GFI. According to plaintiffs, their right to the shares did not vest until 2004. They state that the limitations period on their claim began to run at that time, since it was not until then that all the facts necessary to sustaining their claim came into being.

The only breach alleged here is the supplying of false information. Once defendant supplied the false information that resulted in calculations showing that plaintiffs were not entitled to the shares, plaintiffs could not receive the shares in 2004 or at any other time. As the alleged breach occurred in March 2000, the contract claim is untimely. The result is the same if the breach is alleged to be the issuing of the KPMG report containing the allegedly erroneous calculations.

Plaintiffs contend that defendant had a continuing duty to manage the clean-up of the bank for the benefit of plaintiffs and that its duties continued until 2004, when plaintiffs received their 9% shares. However, plaintiffs do not allege any other breaches of contract apart from the giving of false information (*see Beller v William Penn Life Ins. Co. of N.Y.*, 8 AD3d 310, 314 [2d Dept 2004]) [the claims for damages accrued each time that the defendant breached the

continuing duties imposed by contract to consider the factors comprising the cost of insurance before changing rates, and to review the cost of insurance rates at least once every five years to determine if a change should be made]; *Orville v Newski, Inc.*, 155 AD2d 799 [3d Dept 1989] [a breach of the contract occurred each year in which defendant failed to make an annually required payment]).

Plaintiffs miss the distinction between a single wrong which has continuing effects and a series of independent, distinct wrongs. Once the calculations based on the allegedly false information were issued, what followed was the effect of the initial breach.

This case is akin to one cited by defendant, *Welwart v Dataware Elecs. Corp.* (277 AD2d 372, 373 [2d Dept 2000]), where the limitations period on the contract claim was measured from the date of the initial breach when defendants deprived plaintiff of his right to shares and began to divert profits away from the plaintiff. Separate causes of action did not accrue each time that profits were diverted. Also instructive is *Amirthmasebi v Benyamini* (306 AD2d 363, 363 [2d Dept 2003]), where the plaintiff claimed a share of the proceeds from a real estate closing. The contractual cause of action accrued on the date of the closing, which was when the proceeds were first owed to plaintiff. The claim did not accrue in the future when the proceeds were paid to another party. In *Fu v Publishers Clearing House* (2009 NY Slip Op 30318[U], 2009 WL 423800 [Sup Ct, NY County 2009]), the contract claim accrued at the time that plaintiff should have been declared the winner of a contest, not each time that the defendant failed to pay her the prize money. The plaintiff's right to payment was never established. That omission was the breach that started the accrual. In this case, plaintiffs' right to the 36% of shares was not established because of the breach of supplying false information. The effect of the breach was

that plaintiffs did not receive the shares.

In addition, plaintiffs' "position overlooks the distinction between a breach and the ability to cure a breach" (*First Am. Title Ins. Co. of New York v Fiserv Fulfillment Services, Inc.*, 2008 WL 3833831, *3, 2008 US Dist. LEXIS 63010, *7 [SD NY 2008]). That defendant could have corrected the initial breach does not mean the failure to do so over the years was also a breach.

In view of the foregoing determinations, the court does not reach the other bases for summary judgment advanced by defendant.

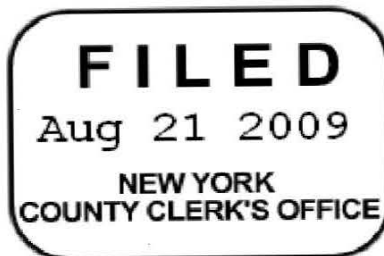
It is hereby

ORDERED that defendant's motion for summary judgment is granted and the complaint is dismissed; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

No costs.

Dated: August 4, 2009



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A handwritten signature in black ink, appearing to be 'J.S.G.', written over a horizontal line.

J.S.G.