

**AIX Partners I, LLC v AIX Energy, Inc.**

2013 NY Slip Op 32003(U)

August 22, 2013

Supreme Court, New York County

Docket Number: 651401/2012

Judge: Eileen Bransten

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SUPREME COURT OF THE STATE OF NEW YORK  
NEW YORK COUNTY

HON. EILEEN BRANSTEN  
J.S.C.

PRESENT: \_\_\_\_\_  
Justice

PART 3

Index Number : 651401/2012  
AIX PARTNERS I, LLC  
vs.  
AIX ENERGY, INC.  
SEQUENCE NUMBER : 001  
DISMISS

INDEX NO. 651401/2012  
MOTION DATE 4/4/2013  
MOTION SEQ. NO. 001

The following papers, numbered 1 to 3, were read on this motion to/for dismiss

Notice of Motion/Order to Show Cause — Affidavits — Exhibits \_\_\_\_\_ | No(s). 1  
Answering Affidavits — Exhibits \_\_\_\_\_ | No(s). 2  
Replying Affidavits \_\_\_\_\_ | No(s). 3

Upon the foregoing papers, it is ordered that this motion is

IS DECIDED

IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DECISION

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

Dated: 8-22-13

Eileen Bransten J.S.C.

- 1. CHECK ONE: .....  CASE DISPOSED  NON-FINAL DISPOSITION
- 2. CHECK AS APPROPRIATE: ..... MOTION IS:  GRANTED  DENIED  GRANTED IN PART  OTHER
- 3. CHECK IF APPROPRIATE: .....  SETTLE ORDER  SUBMIT ORDER
- DO NOT POST  FIDUCIARY APPOINTMENT  REFERENCE

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

-----X  
AIX PARTNERS I, LLC,

Plaintiff,

-against-

AIX ENERGY, INC.,

Defendant.

Index No. 651401/2012  
Third-Party Index No.  
590550/2012

-----X  
AIX ENERGY, INC.,

Third-Party Plaintiff,

Motion Date: 4/4/2013  
Motion Seq. No.: 001, 002

-against-

IROQUOIS CAPITAL OPPORTUNITY FUND, LP;  
IROQUOIS OPPORTUNITY MANAGEMENT, LLC;  
and GRUSHKO & MITTMAN, P.C.,

Third-Party Defendants.

-----X

**BRANSTEN, J.**

This matter comes before the Court on two motions: (1) an omnibus motion to dismiss brought by Counterclaim-Defendant AIX Partners I, LLC (“AIX Partners”) and Third-Party Defendants Iroquois Capital Opportunity Fund, LP and Iroquois Opportunity Management, LLC (collectively “Iroquois”) and (2) a motion to dismiss brought by Third Party-Defendant Grushko & Mittman, P.C. (“Grushko”). Defendant/Third-Party Plaintiff AIX Energy, Inc. (“AIX Energy”) opposes both motions.

For the reasons that follow, AIX Partners' motion is granted in part and denied in part, while the motions filed by Iroquois and Grushko are granted in their entirety.

## I. **Background**<sup>1</sup>

AIX Energy is a private oil and gas exploration company. (Third-Party Compl. ¶

1.) The instant litigation stems from a transaction between AIX Energy and Iroquois, a New York private equity investor, whereby AIX Energy sought funding for its exploration operations in Louisiana. *Id.* Iroquois agreed to provide this funding through AIX Partners, a special purpose entity created by Iroquois for this transaction. *Id.* This transaction was effectuated through a Participation Agreement, executed on November 16, 2010. *Id.* ¶ 29.

AIX Energy and Iroquois negotiated the terms of this transaction during the latter half of 2010, as AIX Energy's "financial situation was worsening." *Id.* ¶ 36. During the course of the parties' negotiations, AIX Energy alleges that it began to question Iroquois' sophistication and wondered "whether Iroquois was really capable of closing any deal at all." *Id.* at 37. Accordingly, AIX Energy insisted that the draft Participation Agreement include a representation that AIX Partners had "adequate capital to fund the entire Funding Limit." *Id.* at 38.

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<sup>1</sup> The facts described in this section are drawn from AIX Energy's allegations in its Counterclaims and Third-Party Complaint.

This “adequate capital” representation was “especially important given the ‘extras’ Iroquois was demanding to close a deal.” *Id.* These “extras” included an “exit provision,” allowing AIX Partners to demand the return of 150% of its investment if AIX Energy failed to register its common stock with a public stock exchange by December 31, 2011. *Id.* ¶ 40; AIX Energy Opp. Br. at 1. In addition, AIX Partners received warrants and a lockup agreement, restricting AIX Energy from selling common stock (collectively, with the “exit provision,” the “Extra Terms”). (Third-Party Compl. ¶ 40.)

While the parties initially agreed to a \$10.5 million investment, Iroquois later informed AIX Energy that it only would be able to provide \$8.351 million and that its payments would have to be made in two phases. (Counterclaim ¶ 36.) AIX Energy was unhappy with this change but agreed to pursue the smaller deal. *Id.* ¶ 35. Although the funding was to be provided in two installments, Iroquois repeated its “adequate capital” representation. *Id.* at ¶ 38.

Despite these representations, “on the eve of closing,” Iroquois representatives informed AIX Energy that AIX Partners would not be able to deposit the entire Phase I funding amount into escrow at closing. *Id.* ¶¶ 43, 45. Nonetheless, the parties went through with the closing and executed the Participation Agreement, the Lockup Agreement, and the Common Stock Purchase Warrant on November 16, 2010. *Id.* ¶ 52.

On April 27, 2012, AIX Partners commenced the instant breach of contract action, asserting that AIX Energy failed to comply with the “exit provision” of the Participation Agreement. Specifically, AIX Partners alleges that AIX Energy failed to list itself on a public exchange by December 31, 2011, and then failed to pay AIX Partners 150% of its investment as required by the “exit provision.”

AIX Energy interposed an Answer and five Counterclaims, each premised on the theory that Iroquois did not have “adequate capital” to close the funding deal. In particular, the Counterclaims assert fraud; breach of the Participation Agreement; and, breach of the implied warranty of good faith and fair dealing. AIX Energy also seeks a declaratory judgment that AIX Partners breached the Participation Agreement and that AIX Energy is therefore not obligated to perform thereunder; and a permanent injunction directing that the transaction documents are rescinded. AIX Partners’ motion to dismiss each of these five counterclaims is presently before the Court.

In addition to filing Counterclaims against AIX Partners, AIX Energy also filed a Third-Party Complaint against Iroquois and its counsel, Grushko & Mittman, P.C. (“Grushko”). The Third-Party Complaint’s allegations regarding Iroquois largely repeat the allegations in AIX Energy’s Counterclaims and assert claims against Iroquois for fraudulent misrepresentation and fraudulent concealment. As for Grushko, AIX Energy alleges that the law firm aided and abetted the fraud purportedly committed by AIX

Partners and Iroquois through its role as Escrow Agent for the transaction and that Grushko breached its fiduciary duty to AIX Energy. Iroquois and Grushko each seek dismissal of this Third-Party Complaint.

## II. Analysis

AIX Partners and Iroquois jointly filed a motion to dismiss the respective counts asserted against them in the Counterclaims and Third-Party Complaint. Grushko likewise seeks dismissal of the aiding and abetting fraud claim brought against it in the Third-Party Complaint. Since the claims against AIX Partners and Iroquois are substantially similar, they will be considered together below, and a discussion of Grushko's motion will follow.

### A. *Motion to Dismiss Standard*

On a motion to dismiss for failure to state a cause of action, the court must accept each and every allegation as true and liberally construe the allegations in the light most favorable to the pleading party. *Guggenheimer v. Ginzburg*, 43 N.Y.2d 268, 275 (1977); see CPLR 3211(a)(7). The Court "determine[s] only whether the facts as alleged fit within any cognizable legal theory." *Leon v. Martinez*, 84 N.Y.2d 83, 87-88 (1994). A motion to dismiss 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 *W. 232nd Owners Corp. v. Jennifer Realty Co.*, 98 N.Y.2d 144, 152 (2002) (internal quotation marks and citations omitted).

Moreover, where the motion to dismiss is based on documentary evidence under CPLR 3211(a)(1), the claim will be dismissed “if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law.” *Leon v. Martinez*, 84 N.Y.2d at 88; *see also 150 Broadway N.Y. Assoc., L.P. v. Bodner*, 14 A.D.3d 1, 5 (1st Dep’t 2004). Where, as here, the defendants have presented documentary evidence, the court is required to determine “whether the proponent of the pleading has a cause of action, not whether he has stated one.” *Ark Bryant Park Corp. v. Bryant Park Restoration Corp.*, 285 A.D.2d 143, 150 (1st Dep’t 2001) (internal quotation mark and citation omitted).

B. *AIX Partners and Iroquois’ Motion to Dismiss*

1. Fraud Claims

AIX Energy brings fraud claims against both AIX Partners and Iroquois, stemming from the same purported misrepresentation – that AIX Partners “has adequate capital to fund the entire Funding Limit.” While AIX Energy asserts that it was induced to enter into the transaction by this representation, the Complaint states that it was aware of its

falsity “on the eve” of the transaction’s closing. Accordingly, AIX Energy fails to state a fraud claim.

“The elements of a cause of action for fraud require a material misrepresentation of a fact, knowledge of its falsity, an intent to induce reliance, justifiable reliance by the plaintiff and damages.” *Eurycleia Partners, LP v. Seward & Kissel, LLP*, 12 N.Y.3d 553, 559 (2009). In this case, AIX Energy has failed to plead the fourth element – justifiable reliance.

While “the justifiable reliance prong of a claim of fraud can be sufficiently alleged where [a party] ‘has gone to the trouble’ of insisting on a written agreement that includes warranties that certain facts are true,” *Vision China Media Inc. v. S’holder Rep. Serv., LLC*, – A.D.3d –, 967 N.Y.S.2d 338, 344 (1st Dep’t 2013), a party cannot justifiably rely upon warranties it knew to be false at the time of contract. *See Ponzini v. Gatz*, 155 A.D.2d 590, 591 (2d Dep’t 1989) (holding plaintiff’s reliance on contractual warranty unreasonable as a matter of law where plaintiff’s attorney had actual knowledge that the representation was false); *see also DDJ Mgmt., LLC v. Rhone Grp. L.L.C.*, 15 N.Y.3d 147, 155 (2010) (citing *Ponzini v. Gatz*); *NMIQ LLC v. OmniSky Corp.*, 31 A.D.3d 315, 316 (1st Dep’t 2006) (deeming reliance upon representation that defendant had sufficient capital to continue its operations through 2001 and into 2002 unreasonable

where plaintiff received independent analyst reports warning that defendant would need capital as early as the third quarter of 2001).

Taking the facts pleaded in the Counterclaims and Third-Party Complaint as true, AIX Energy was told by AIX Partners “on the eve of closing” that “AIX Partners was unable to deposit” the \$3.4 million it had agreed to provide. *See* Counterclaim ¶ 45; *see also* Third-Party Compl. ¶ 65. Thus, AIX Energy had actual knowledge on the eve of closing from AIX Partners itself that AIX Partners lacked “adequate capital to fund the entire Funding Limit” of \$8.351 million. Accordingly, AIX Energy’s reliance on this “adequate capital” representation was unjustifiable as a matter of law, dooming the fraud claims asserted against AIX Partners and Iroquois. Therefore, Counterclaim One and Counts One and Two of the Third-Party Complaint are dismissed.

## 2. Breach of Contract

AIX Energy next brings a breach of contract claim, again premised on the “adequate capital” representation in the Participation Agreement. AIX Energy maintains that breach of this representation warrants rescission of the Participation Agreement. In opposition, AIX Partners asserts that the breach claim fails to plead damages and that, in any event, AIX Energy waived AIX Partner’s noncompliance with the “adequate capital representation.”

a. *Damages*

As a threshold matter, the elements of a breach of contract claim include the existence of a contract, plaintiff's performance thereunder, defendant's breach thereof, and resulting damages. *Harris v. Seward Park Hous. Corp.*, 79 A.D.3d 425, 426 (1st Dep't 2010). Here, only the damages element is in dispute.

"The damages for which a party may recover for a breach of contract are such as ordinarily and naturally flow from the non-performance. They must be proximate and certain, or capable of certain ascertainment, and not remote, speculative or contingent." *Fruition, Inc. v. Rhoda Lee, Inc.*, 1 A.D.3d 124, 125 (1st Dep't 2003). In the instant counterclaim, AIX Energy states that it suffered damages relating "not only to amounts it expended in connection with the Transaction Documents, but ... also to the contractual terms it was required to enter into, to the lost business opportunities that AIX Energy ended up foregoing, and to the costs of finding replacement funding for AIX Energy's business." (Counterclaim ¶ 79.) Further, AIX Energy represents in its briefing that the primary relief sought for this claim is rescission.

To the extent that AIX Energy seeks damages for costs incurred prior to the execution of the transaction, such a request for relief is unavailing. *See S&S Mach. Corp. v. Wuban Heavy Duty Mach. Tool Grp. Co., Ltd.*, 2012 WL 958528, at \*8 (E.D.N.Y. Jan. 13, 2012) (applying New York law and holding that plaintiff not entitled to recover

contract negotiation expenses incurred prior to execution since they were not a “natural and probable consequence of the breach” and were not “contemplated by the parties”).

Moreover, AIX Energy’s request for rescission fails as pleaded. Rescission is an equitable remedy, “invoked only when there is lacking [a] complete and adequate remedy at law and where the status quo may be substantially restored.” *Rudman v. Cowles Commc’n*, 30 N.Y.2d 1, 13 (1971). Here, AIX Energy’s demand for relief is, at bottom, a request for monetary damages. Accordingly, AIX Energy has an adequate remedy at law for the breaches asserted.

At this juncture, the Court cannot pass on the remainder of AIX Energy’s damages claim. While AIX Partners disputes whether such damages are “sensible,” *see* AIX Partners Moving Br. at 19, this Court cannot join in such a conclusion on this motion to dismiss. Instead, the inquiry is simply whether AIX Energy has pleaded proximate and certain damages flowing from breach of the “adequate capital” representation, not whether it has demonstrated its entitlement to them. AIX Energy’s entitlement to damages will be better assessed on a motion for summary judgment.

b. *Waiver*

The remaining issue is whether AIX Energy waived its right to recover under the Participation Agreement, notwithstanding its pleading of damages, as discussed above. AIX Energy pleads that it agreed with AIX Partners that payments would be made in two phases under the Participation Agreement. When AIX Partners was unable to make its Phase I payments, the parties entered into a Modification Agreement, allowing AIX Partners to complete Phase I in two stages.

In support of its motion to dismiss, AIX Partners argues that AIX Energy waived AIX Partners' non-compliance with the "adequate capital" representation through its: (1) agreement to accept AIX Partners' deferred funding of Phase I under the Modification Agreement; and (2) continued drawing down of the Phase I monies provided by AIX Partners without objection.

"Contractual rights may be waived if they are knowingly, voluntarily and intentionally abandoned." *Fundamental Portfolio Advisors, Inc. v. Tocqueville Asset Mgt., L.P.*, 7 N.Y.3d 96, 104 (2006). However, "waiver should not be lightly presumed and must be based on a clear manifestation of intent to relinquish a contractual protection." *Id.* Here, the parties modified the Participation Agreement's timetable for the payment of the Phase I funds, extending it and creating two new dates for payment: December 2, 2010 and December 30, 2010. As a result of this modification, AIX Energy

waived its right to enforce the payment dates set forth in the Participation Agreement, since it agreed that the Phase I payments could be made on December 2 and December 30.

However, AIX Partners points to no additional waiver beyond this modification. AIX Partners states that AIX Energy continued drawing down Phase I monies without objection, but this uncited statement in AIX Partners' briefing does not provide a basis to grant its motion to dismiss. On a CPLR 3211 motion, the Court must focus on the facts as pleaded in the four corners of the Complaint and take all inferences in favor of the non-moving party. *Guggenheimer v. Ginzburg*, 43 N.Y.2d 268, 275 (1977). Conversely, AIX Partners here requests that the Court accept this unsupported assertion from its briefing and construe it in its favor. Having provided no additional support for its waiver defense, the Court cannot hold that AIX Partners' waiver argument bars the breach of contract claim as a matter of law, except as discussed above.

3. Breach of the Implied Covenant of Good Faith and Fair Dealing

The Counterclaims next assert a breach of the covenant of good faith and fair dealing, premised on the same allegations as its breach of contract claim, i.e. that the parties entered into a contract and that AIX Partners failed to perform under that contract. (Counterclaims ¶¶ 80-83.) In addition, this claim seeks the same damages as the breach

of contract claim. *Id.* ¶ 85. Accordingly, since the breach of the implied covenant claim “merely duplicates” the breach of contract claim, it is dismissed. *Empire State Bldg. Assoc. v. Trump*, 247 A.D.2d 214, 214 (1st Dep’t 1998).

#### 4. Declaratory Judgment

Likewise, AIX Energy’s declaratory judgment request is duplicative of its breach of contract claim and is dismissed. Through this claim, AIX Energy seeks a declaration that AIX Partners breached the Participation Agreement, and that the agreement is therefore rescinded. These allegations parrot the breach of contract claim and seek the same relief. *See Wildenstein v. 5H & Co., Inc.*, 97 A.D.3d 488, 491 (1st Dep’t 2012) (“[T]he first two causes of action seek declarations that the contract is void and unenforceable. The seventh cause of action for breach of contract seeks, not only compensatory damages, but also a declaration that the contract is void and unenforceable. Accordingly, the first and second causes of action should have been dismissed as duplicative.”); *Artech Info. Sys. LLC v. Tee*, 280 A.D.2d 117, 125 (1st Dep’t 2001) (dismissing declaratory judgment claim where “cause of action for breach of contract ... affords an adequate remedy.”). Accordingly, Counterclaim Four is dismissed.

5. Permanent Injunction

AIX Energy next seeks a permanent injunction, directing that the transaction documents are rescinded and that AIX Partners must return the Warrants granted under the Participation Agreement to AIX Energy. For the reasons stated above, AIX Energy is not entitled to rescission. Moreover, AIX Energy is not entitled to injunctive relief, since the damages sought through this claim, and this action generally, are monetary in nature. *See Mini Mint Inc. v. Citigroup, Inc.*, 83 A.D.3d 596, 597 (1st Dep't 2011) (holding that plaintiff failed to state prima facie claim for permanent injunction requiring landlord to fully repair premises following water leak where lessee had adequate remedy at law – money damages for losses associated with water leak). While AIX Energy attempts to dress its claim in equitable terms, its cause of action lies in breach of contract and its remedies are at law. Accordingly, Counterclaim Five is dismissed as duplicative of the breach of contract claim.

C. *Grushko's Motion to Dismiss*

1. Aiding and Abetting Fraud

Count Three of the Third-Party Complaint asserts that Grushko aided and abetted the fraud purportedly committed by Iroquois and AIX Partners against AIX Energy.

Among the requisite elements of an aiding and abetting fraud claim is the existence of an

underlying fraud. *See Stanfield Offshore Leveraged Assets, Ltd. v. Metro. Life Ins. Co.*, 64 A.D.3d 472, 476 (1st Dep't 2009). Since the underlying fraud claim asserted here has been dismissed, *see infra* Section II.B.1, this claim is likewise dismissed.

## 2. Breach of Fiduciary Duty

The foundational element of a breach of fiduciary duty claim is the existence of a fiduciary relationship. *See, e.g., Burry v. Madison Park Owner LLC*, 84 A.D.3d 699, 700 (1st Dep't 2011). While AIX Energy alleges that Grushko was the escrow agent for the funding transaction, this title, in and of itself, does not impose fiduciary obligations on Grushko.

Grushko served as legal counsel to Iroquois and AIX Partners for the transaction. (Third-Party Compl. ¶ 5.) In addition, Grushko acted as escrow agent to disburse funds to AIX Energy after AIX Partners deposited funds pursuant to the parties' Escrow and Modification Agreements. *Id.* ¶¶ 70, 91. Although Grushko was not their counsel, AIX Energy asserts that Grushko breached a fiduciary duty to them by not disclosing Iroquois' failure to deposit funds to the escrow account as required by the Escrow Agreement. *Id.* ¶ 153.

Since the Third-Party Complaint pleads that Iroquois failed to deposit funds in the escrow account, no escrow was created; therefore, Grushko owed no fiduciary duty to

AIX Energy as an escrow agent. *See Muscara v. Lamberti*, 133 A.D.2d 362, 363 (2d Dep't 1987) ("Absent delivery of the subject of the escrow, however, no escrow is created and the fiduciary duty of the designated escrow agent does not come into existence."); *Egnotovich v. Katten Muchin Zavis & Roseman LLP*, 18 Misc.3d 1120(a), at \*9 (Sup. Ct. N.Y. Cnty. 2008) ("An escrow agent has no fiduciary duty to a depositor prior to receiving a depositor's money."). Accordingly, AIX Energy's breach of fiduciary duty claim is denied.

### **III. Conclusion and Order**

For the foregoing reasons, the motions to dismiss filed by Third-Party Defendants Iroquois and Grushko are granted and the Third-Party Complaint is dismissed.

Counterclaim-Defendant AIX Partners' motion to dismiss is granted as to the fraud, breach of the implied covenant of good faith and fair dealing, declaratory judgment and permanent injunction claims and is denied as to the breach of contract claim, except to the extent that AIX Energy's request for rescission is denied.

Accordingly, it is

ORDERED that the motion to dismiss filed by Counterclaim-Defendant AIX Partners I, LLC (motion seq. no. 001) is granted as to Counterclaims One, Three, Four and Five and is denied as to Counterclaim Two; and it is further

ORDERED that Counterclaim-Defendant is directed to serve an answer to the complaint within 20 days after service of a copy of this order with notice of entry; and it is further

ORDERED that counsel for Counterclaim-Defendant and Counterclaim-Plaintiff are directed to appear for a preliminary conference in Room 442, 60 Centre Street, on October 15, 2013 at 10 AM; and it is further

ORDERED that the motion to dismiss filed by Third-Party Defendants Iroquois Capital Opportunity Fund, LP and Iroquois Opportunity Management, LLC ("Iroquois") (motion seq. no. 001) is granted; and it is further

ORDERED that Third Party-Defendant Grushko & Mittman, P.C.'s motion to dismiss (motion seq. no. 002) is granted; and it is further

ORDERED that the Third-Party Complaint is dismissed in its entirety; and it is further

ORDERED that Third-Party Plaintiff is granted leave to serve an amended complaint so as to replead counts one through four within 20 days after service on plaintiff's attorney of a copy of this order with notice of entry; and it is further

ORDERED that, in the event that Third-Party Plaintiff fails to serve and file an amended complaint in conformity herewith within such time, leave to replead shall be deemed denied, and the Clerk, upon service of a copy of this order with notice of entry

*AIX Partners, I, LLC v. AIX Energy, Inc.*

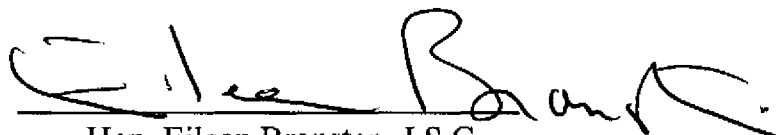
Index No. 651401/2012

Page 18 of 18

and an affirmation/affidavit by counsel for each Third-Party Defendant attesting to such non-compliance, is directed to enter judgment dismissing the action, with prejudice, and with costs and disbursements to the Third-Party Defendants as taxed by the Clerk.

Dated: New York, New York  
August 22 2013

ENTER:

A handwritten signature in black ink, appearing to read "Eileen Bransten", written over a horizontal line.

Hon. Eileen Bransten, J.S.C.