

Wax v S. Rothschild & Co., Inc.
2014 NY Slip Op 31437(U)
May 30, 2014
Sup Ct, New York County
Docket Number: 653850/2012
Judge: Shirley Werner Kornreich
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 54

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SANFORD WAX and SWAXX CORPORATION,

Index No.: 653850/2012

Plaintiffs,

DECISION & ORDER

-against-

S. ROTHSCHILD & CO., INC.,

Defendant.

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SHIRLEY WERNER KORNREICH, J.:

Defendant S. Rothschild & Co., Inc. (Rothschild) moves, pursuant to CPLR 3212, for (1) partial summary judgment on liability on its counterclaims against plaintiffs Sanford Wax and Swaxx Corporation (Swaxx); and (2) dismissal of the Complaint. Defendant’s motion is granted in part and denied in part for the reasons that follow.

I. Factual Background & Procedural History

Unless otherwise noted, the following facts are undisputed.

Wax is the sole owner of Swaxx, a business that manufactured and distributed men’s outerwear under licenses from non-parties Elie Tahari Ltd. (Tahari) and Philips Van Heusen Corporation (PVH). Rothschild is a much larger clothing distributor, which also sells outerwear. On March 8, 2012, the parties entered into two contracts governing the sale of Swaxx’s business to Rothschild: (1) an Asset Purchase Agreement (the APA), under which Swaxx sold its assets to Rothschild for \$550,000, \$275,000 of which was due at closing and the balance payable in equal installments of \$137,500 in the first and second years after closing; and (2) an Employment Agreement (the EA), under which Wax was hired as the President of the men’s outerwear business purchased. The EA ran through March 8, 2017 and entitles Wax to a \$215,000 annual

base salary, reimbursement of reasonable business expenses, up to \$25,000 for the use of an automobile, and an “earn out” bonus equal to 25% of the defined annual “Net Division Profits” of the men’s outerwear business. Additionally, Swaxx’s Tahari and PVH licenses were assigned to Rothschild, and Rothschild moved into Swaxx’s office.

Wax was paid the initial \$275,000 and was employed by Rothschild until September 4, 2012, when he was fired for cause. On November 7, 2012, plaintiffs commenced this action, asserting claims for unpaid compensation under the APA and EA with declaratory judgment, breach of contract, and unjust enrichment causes of action. Rothschild filed an Answer on December 21, 2012, in which it asserted five counterclaims: (1) breach of the APA; (2) breach of the EA; (3) a declaratory judgment that no further money is owed to plaintiffs under the APA and EA; (4) a declaratory judgment that Wax remains bound by the APA and EA’s restrictive covenants; and (5) a permanent injunction enforcing such restrictive covenants against Wax. No motions to dismiss were filed, leaving all claims intact coming into this motion. However, at oral argument, plaintiffs withdrew their declaratory judgment and unjust enrichment claims. *See* 4/3/14 Tr. at 16.

Rothschild’s Answer alleged, and discovery confirmed, that there was ample cause to fire Wax. Plaintiffs breached the APA by failing to disclose all of Swaxx’s pre-closing debts and, to the extent some of its creditors were identified, the amount of the debt was understated. Plaintiffs also overstated Swaxx’s revenues.¹ Moreover, Wax breached the EA by secretly threatening Rothschild’s liaison to its Chinese suppliers in an attempt to evade his debts, an attempt that cause significant economic harm to Rothschild.

¹ For instance, Swaxx overstated its sales to PVH by approximately \$950,000.

Pursuant to section 2.2 of the APA, Swaxx agreed to remain liable for its defined pre-closing liabilities (the Retained Liabilities). Section 8.1 obligates plaintiffs to indemnify Rothschild for any losses related to the Retained Liabilities. As a result, if Rothschild had to pay (as it did) Swaxx's creditors a debt included in the Retained Liabilities, plaintiffs are liable to Rothschild for that amount.

Plaintiffs also made representations and warranties to Rothschild in Article V of the APA.² Rothschild alleges that plaintiffs breached two warranties, sections 5.1(l) & (m), which provide:

[Swaxx] has made its [financial records through December 31, 2010 (the Financial Statements)] available to [Rothschild]. The Financial Statements fairly present the financial condition and operating results of [Swaxx] as of [December 31, 2010]. Except as reflected in the Financial Statements or as set forth in *Schedule 5.1(l)* hereto [*italics in original; hereinafter, the Schedule*], [Swaxx] has no liabilities or obligations ... [that exceed \$5,000. The Schedule] sets forth a complete and accurate list as of [March 8, 2012] of all liabilities and obligations of [Swaxx] which ... exceed [\$5,000].

No representation or warranty made by [plaintiffs] in [the APA] ... contains an untrue statement of a material fact or omits to state a material fact necessary to make the statements [in the APA] ... not false or misleading.

Dkt. 23 at 12-13. The Schedule states that “[Swaxx] has \$192,884 of outstanding accounts claimed to be payable in respect of goods that were delivered on an open account basis ... In addition, [Swaxx] is liable to the Companies set forth below for the amounts indicated opposite each company name.” Dkt. 23 at 28. The Schedule then itemizes 23 debts owed, totaling

² It is well settled that a buyer has the right to rely on representations and warranties, and, unlike a fraud claim (which is not alleged), it does not matter whether the buyer's reliance was reasonable. *CBS Inc. v Ziff-Davis Pub. Co.*, 75 NY2d 496, 503 (1990). Indeed, Section 5.3 of the APA memorializes this understand by stating that “[n]o investigation by [Rothschild] shall affect the representations and warranties of [plaintiffs].”

\$360,925.45. It is undisputed³ that Swaxx owed \$80,000 to JPMorgan Chase, at least \$275,000 to Rosenthal & Rosenthal (Rosenthal), and approximately \$50,000 to Belk, Inc. (Belk).⁴ These debts are not listed on the Schedule. Belk was Swaxx's biggest client, and, thus, an essential client for Rothschild. Belk demanded that Rothschild pay Swaxx's \$50,000 debt or it would cease doing business with Rothschild. Rothschild paid the debt, which is a Retained Liability under section 2.2.

Next, it is undisputed that Swaxx also owed \$288,709.84 to a Chinese supplier called "Shanghai Eidie." This debt, again, was not disclosed on the Schedule. Swaxx did disclose debts to four other Chinese vendors (totaling approximately \$100,000 less than the amount owed to Shanghai Eidie) but, as Wax himself testified, the debt disclosed was not that of Shanghai Eidie.⁵ Moreover, there is no doubt that Wax believed he owed \$288,709.84 to Shanghai Eidie because he admitted this to Helen Ding in an email sent on June 13, 2012 (among many others).

³ The court reviewed the substantial record of emails and the parties' deposition transcripts. Though, in their memorandum of law, plaintiffs assert numerous baseless challenges to the existence and amount of these debts, the documentary evidence conclusively establishes that there is no question of fact that these debts existed and were not disclosed, in violation of the APA.

⁴ The APA's identification of Rosenthal as Swaxx's receivables factor and Belk as a client is immaterial to whether plaintiffs breached the APA by failing to disclose the amount of the debt owed to these companies.

⁵ Wax also testified that the Schedule's account of the debt owed to the listed Chinese companies was inaccurate, another breach of the APA. However, this does not affect this motion since it is undisputed that the Shanghai Eidie debt, among others, was not disclosed. Indeed, there is no need to completely ascertain the full scope of the Schedule's inaccuracies. The proof on this motion is more than sufficient to determine that Wax breached the APA. Damages are not at issue on this motion.

Ding was Wax's longtime liaison to Swaxx's suppliers in China. Ding, who lives in China and speaks Chinese, communicated with the Chinese suppliers on behalf of Swaxx and was the conduit for Swaxx's payments to those suppliers. After the merger with Rothschild, Wax continued using Ding to do business on behalf of Rothschild. Ding knew about Swaxx's debts to Shanghai Eidie and constantly urged Wax to pay them. Wax, however, concerned that Rothschild might find out, insisted that he and Ding communicate exclusively through Wax's personal email address, and not use his Rothschild work email. In discovery, plaintiffs produced the voluminous record of Ding's communications with Wax. Rothschild submitted them in support of the instant motion. The emails reveal that Wax intentionally hid the Shanghai Eidie debt from Rothschild.

Things fell apart for Wax toward the end of August 2012. Rothschild had paid its Chinese vendors a deposit of approximately \$200,000 for new merchandise, but the vendors were refusing to ship the goods to the U.S. unless Wax paid the Shanghai Eidie debt. Ding conveyed the situation to Wax, who did not disclose this information to Rothschild. Meantime, Rothschild's merchandise was scheduled to be shipped on August 28, 2012. If the merchandise was not shipped by that date, Rothschild could not deliver it on time to its customers. This, naturally, would seriously affect Rothschild's relationship with its customers. Wax understood this. Hence, he furiously demanded that Ding ensure delivery. Wax threatened that if the merchandise was not shipped, he would not pay off the Shanghai Eidie debt and Ding would likely lose her job. Wax's demands were rebuffed, the merchandise was not shipped, and Rothschild lost its \$200,000 deposit and sales. When Rothschild became aware of Wax's concealment of the Shanghai Eidie debt debacle, Wax was fired. His Notice of Termination,

dated September 4, 2012, specifically recounted this incident as the justification for his termination.⁶ Wax was accused of acting “fraudulently and dishonestly” and “with willful and gross negligence.”

Rothschild considered Wax’s actions to be fraudulent because it understood that his communications with Ding on his personal email was an indication that he intended to deceive the company. Rothschild maintained that the termination of the EA for Wax’s dishonest acts does not require a cure period. In this litigation, Rothschild further avers that Wax’s breaches were incurable since he caused the company irreparable harm – the destruction of its customer relationships due to the missed shipments from China.

Wax, on the other hand, avers that a cure period is necessary. He argues that Rothschild’s failure to afford him one negates the “for-cause” designation of his termination, thereby entitling him to the balance of his compensation under the EA.⁷

The parties’ dispute over Wax’s termination is governed by section 5(c) of the EA, which sets forth when and how Wax can be terminated for cause:

[Rothschild] shall have the right to terminate [the EA] and [Wax’s] employment hereunder for Cause (as defined below) upon giving notice of termination to [Wax] in accordance with the terms of this Agreement. For purposes of this Agreement, “Cause” shall mean the determination by the CEO, in good faith and in the exercise of his reasonable judgment, that [Wax] has committed an act or

⁶ Wax makes no legitimate effort to justify himself. Instead, Wax’s primary defense is that Rothschild had buyer’s remorse and was looking to find a reason to get rid of him from day one. Regardless, even if Rothschild really was chomping at the bit to fire Wax, Wax gave Rothschild a perfectly legitimate opportunity to do so.

⁷ Though not raised by the parties, the “faithless servant” doctrine might also bar Wax’s claim for further compensation under the EA. See *Visual Arts Found., Inc. v Egnasko*, 91 AD3d 578, 579 (1st Dept 2012), accord *Lamdin v Broadway Surface Adv. Corp.*, 272 NY 133, 138 (1936). In any event, as discussed below, Wax’s breach of the EA is not curable.

acts which constitute (i) willful misconduct or gross negligence which is, or reasonably could be, expected to be injurious or counter to the interests of or to the business, operations or reputation of [Rothschild]; (ii) a fraudulent or dishonest act, whether or not related to [Wax's] duties hereunder, or a felony; (iii) unless instructed or consented to by [Rothschild], engaging in one or more acts, or omitting to act, which is, or reasonably could be, expected to be damaging to the Company or any of its Affiliates, including, without limitation, causing [Rothschild] to be in material breach of any of the Lease, [the Tahari and PVH licenses,] and any other license agreement or material contract to which [Rothschild] is, or shall become, a party; (iv) the failure to perform [Wax's] duties as set forth in Section 3(a) of this Agreement and as assigned from time to time by the Company; (v) any material violation of the [Wax's] published policies or procedures in effect from time to time; (vi) during the [first two years of Wax's employment], a breach of any representation, warranty, covenant or agreement of [plaintiffs] contained in the [APA] resulting in damage to [Rothschild] after giving effect to all recoveries and other amounts received by [Rothschild], including indemnification by [plaintiffs], other than a breach of Section 6.3 [Non-competition and Non-solicitation] of the [APA], for which no such recoveries or other amounts shall be factored into such damage determination; provided, however, if such recoveries and other amounts are not received by [Rothschild] within 30 days of Rothschild's notice to [Wax] of such breach, [Rothschild], shall have the right to terminate this Agreement and [Wax's] employment hereunder at any time thereafter; or (vii) a breach of any material provision of this Agreement (including, without limitation, any failure to perform [Wax's] duties under Section 3(a) and any breach or threatened breach of the provisions of Section 8). Notwithstanding the foregoing, no termination by [Rothschild], of this Agreement or [Wax's] employment hereunder shall be deemed to be for Cause under any of clauses (i), (ii), (iii), (iv), (v) or (vii) unless there shall have been delivered to [Wax] a notice from the CEO stating that [Wax] has engaged in conduct described in any of clauses (i), (ii), (iii), (iv), (v) or (vii) of this Section 5(c), specifying such conduct in reasonable detail and providing Executive with a period of at least [30] days to cure the deficiency leading to the determination of Cause, if such deficiency is curable; provided, however, that there shall be no cure period in connection with [Wax's] commission of a dishonest act or felony, a breach of Section 6.3 [Non-competition and Non-solicitation] of the Purchase Agreement or a breach of Section 8 of this Agreement.

Dkt. 23 at 32-33. As explained below, the parties dispute the need to provide a cure period given the seeming overlap of conduct which constitutes a dishonest act with other misconduct authorizing termination for cause, the latter of which requires notice while the former does not.

Finally, less than three months after Wax was fired, on November 26, 2012, Tahari, one of the very companies that licensed its brand to Swaxx, hired Wax as a consultant. On January 26, 2013, Tahari hired Wax as its “director of production for all outerwear, leather and fur.” Wax then poached an employee named Jennifer Senger from Rothschild. Rothschild maintains that going to work for Tahari and hiring Senger violated the restrictive covenants in section 6.3 of the APA and section 8(b) of the EA, which prohibit working for a competitor and soliciting Rothschild’s employees. In opposition, Wax challenges the enforceability of these restrictive covenants, and also avers that he is not actually competing with Rothschild since his work with Tahari does not overlap with Rothschild’s business.

II. Discussion

Summary judgment may be granted only when it is clear that no triable issue of fact exists. *Alvarez v Prospect Hosp.*, 68 NY2d 320, 325 (1986). The burden is upon the moving party to make a *prima facie* showing of entitlement to summary judgment as a matter of law. *Zuckerman v City of New York*, 49 NY2d 557, 562 (1980); *Friends of Animals, Inc. v Associated Fur Mfrs., Inc.*, 46 NY2d 1065, 1067 (1979). A failure to make such a *prima facie* showing requires a denial of the motion, regardless of the sufficiency of the opposing papers. *Ayotte v Gervasio*, 81 NY2d 1062, 1063 (1993). If a *prima facie* showing has been made, the burden shifts to the opposing party to produce evidence sufficient to establish the existence of material issues of fact. *Alvarez*, 68 NY2d at 324; *Zuckerman*, 49 NY2d at 562. The papers submitted in support of and in opposition to a summary judgment motion are examined in the light most favorable to the party opposing the motion. *Martin v Briggs*, 235 AD2d 192, 196 (1st Dept 1997). Mere conclusions, unsubstantiated allegations, or expressions of hope are insufficient to

defeat a summary judgment motion. *Zuckerman*, 49 NY2d at 562. Upon the completion of the court's examination of all the documents submitted in connection with a summary judgment motion, the motion must be denied if there is any doubt as to the existence of a triable issue of fact. *Rotuba Extruders, Inc. v Ceppos*, 46 NY2d 223, 231 (1978).

A. Plaintiffs' Breach of the APA

Summary judgment on liability is granted to Rothschild. There is no question of fact that plaintiffs both omitted significant liabilities from the Schedule and overstated Swaxx's income, thereby violating sections 5.1(l) & (m) of the APA. Additionally, there is no question of fact that Rothschild incurred out-of-pocket damages arising from Retained Liabilities, such as its payment to Belk and loss of its deposit with its Chinese suppliers. The full scope of Rothschild's damages is unclear and, in any event, is not at issue on this motion.⁸ Summary judgment on plaintiffs' breach of the APA is granted, thereby precluding plaintiffs from asserting any further claim against Rothschild thereunder. Hence, plaintiffs' claim for the two remaining \$137,500 payments is dismissed.

B. Wax's Breach of the EA

Numerous, "for-cause" grounds existed to fire Wax under section 5(c) of the EA. The evidence conclusively demonstrates that Wax committed willful misconduct and gross

⁸ It is unclear if plaintiffs are liable for consequential damages, which are recoverable when they "were reasonably contemplated by the parties." See *Bi-Economy Market, Inc. v Harleystown Ins. Co. of N.Y.*, 10 NY3d 187, 193 (2008). Here, section 8.1 of the APA provides that plaintiffs must indemnify Rothschild for losses "incurred by [Rothschild] and result from or arise from, relate to or are otherwise incurred in connection with [] the failure of [plaintiffs] to pay, perform or discharge the Retained Liabilities" (emphasis added). However, Rothschild's recovery is limited by section 8.3 of the APA (Limitation on Indemnification), yet may, for instance, include the repayment amounts set forth in section 7(g) of the EA.

negligence that damaged the company [§ 5(c)(i)], committed fraudulent and dishonest acts [§5(c)(ii)], engaged in acts “which ... reasonably could be [] expected to be damaging to the Company” [§5(c)(iii)], and acted in violation of subsections (iv), (v), (vi), and (vii). However, it is also undisputed that Wax was not given a 30-day notice and opportunity to cure. Thus, as the end of section 5(c) provides, Wax’s termination will not be deemed “for-cause” unless he committed “a dishonest act or felony, a breach of Section 6.3 [Non-competition and Non-solicitation] of the Purchase Agreement or a breach of Section 8 of this Agreement.” As discussed earlier, Wax’s termination letter did indeed indicate that no cure period was being given since Wax was fired for dishonest acts.

Nonetheless, Wax argues that section 5(c) is ambiguous because so much, if not all of the enumerated conduct that is grounds for termination can fairly be labeled a “dishonest act”. In other words, Wax argues, if all bad acts that warrant for-cause termination are considered dishonest, the cure period requirement would be rendered meaningless.

It is well established that contracts “are construed in accord with the parties’ intent.” *Greenfield v Philles Records, Inc.*, 98 NY2d 562, 569 (2002). “The best evidence of what parties to a written agreement intend is what they say in their writing. Therefore, a written agreement that is complete, clear and unambiguous on its face must be enforced according to the plain meaning of its terms.” *Id.* (citations omitted). “A contract is unambiguous if the language it uses has ‘a definite and precise meaning, unattended by danger of misconception in the purport of the [agreement] itself, and concerning which there is no reasonable basis for a difference of opinion.” *Id.*, quoting *Breed v Ins. Co. of N. Am.*, 46 NY2d 351, 355 (1978).

Just as the parties bargained for there to be instances of for-cause termination where a cure period is needed, they likewise bargained for there to be instances where no cure period is needed. To be sure, Wax's breaches are incurable, since the damage he caused to Rothschild's customer relations and industry reputation is inherently irreparable. Yet, even if there was some theoretical way to erase these deeds from the minds of the relevant market participants and restore Rothschild's reputation, Wax's actions were clearly "dishonest acts". Indeed, Wax's dishonesty concerned the very gravamen of the APA – the representations and warranties that were essential to the merger – and the fact that Wax not only lied about those representations, but that such lies caused further harm to Rothschild's business, in part because of Wax's continued employment and his conduct as an employee, is a species of dishonesty that no reasonable finder of fact could conclude was contemplated to be subject to a cure period. Simply put, if there is a universe of dishonesty that does not merit a cure period, Wax's actions are part of it.

Once it was revealed that Wax committed substantial APA breaches and that, from the outset, Wax abrogated his duty of loyalty to the company by allowing his personal debts to compromise Rothschild's business, no reasonable employer could feel that such a dearth of loyalty is a curable offense. Summary judgment, therefore, is granted to Rothschild on Wax's breach of the EA, and Wax's claim for further compensation under the EA is dismissed.

C. Wax's Breach of the Restrictive Covenants

There are questions of fact regarding Wax's breach of the EA's restrictive covenants, such as if his work with Tahari is a "competitive business" as defined by the EA. Regardless, a covenant barring Wax or Senger from working for Tahari is unenforceable.

“In order to be enforceable, an anticompetitive covenant ancillary to an employment agreement must be reasonable in time and area, necessary to protect the employer’s legitimate interests, not harmful to the public, and not unreasonably burdensome to the employee.” *Crown It Services, Inc. v Koval-Olsen*, 11 AD3d 263, 264 (1st Dept 2004), citing *BDO Seidman v Hirshberg*, 93 NY2d 382 (1999). The Court of Appeals “has limited the cognizable employer interests under the [reasonableness prong] to the protection against misappropriation of the employer’s trade secrets or of confidential customer lists, or protection from competition by a former employee whose services are unique or extraordinary.” *BDO Seidman*, 93 NY2d at 389. Moreover, a restriction on a former employee’s ability to work for a competitor is invalid unless the employee’s services were “unique or extraordinary” or if the job is considered a “learned profession” (such as law or accounting). *Id.* at 389-90.

Wax is not a member of a learned profession. Moreover, the record here indicates that Wax not only was replaceable but also that he was a detriment given the debt he owed in China and his poor reputation. Accordingly, it is

ORDERED that the motion by defendant S. Rothschild & Co., Inc. for partial summary judgment on liability against plaintiffs Sanford Wax and Swaxx Corporation is (1) granted on plaintiffs’ breaches of the APA and EA to the extent discussed in this decision; (2) denied on the breach of the restrictive covenants; and (3) in searching the record, the court *sua sponte* grants summary judgment to plaintiffs and holds that the covenants prohibiting Wax from working for Tahari are unenforceable; and it is further

ORDERED that the parties are directed to appear in Part 54 for a status conference on

June 24, 2014 at 11:00 a.m.

Dated: May 30, 2014

ENTER:


SHIRLEY WERNER KORNREICH
J.S.C