

Kumiva Group, LLC v Garda USA Inc.
2015 NY Slip Op 31388(U)
July 24, 2015
Supreme Court, New York County
Docket Number: 650386/06
Judge: Saliann Scarpulla
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 39

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KUMIVA GROUP, LLC, formerly known as
ATI SERVICES, LLC,

Plaintiff,

-against-

GARDA USA INC.,

Defendant.

-----X
GARDA USA INC. and ATI SYSTEMS
INTERNATIONAL, INC.,

Counterclaim and Cross-
Claim Plaintiffs,

-against-

RICHARD IRVIN and ROBERT IRVIN,

Cross-Claim Defendants.

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HON. SALIANN SCARPULLA, J.:

In an action arising out of the acquisition of an armored car company by merger, plaintiff Kumiva Group, LLC, formerly known ATI Services, LLC (Kumiva), moves for summary judgment on its complaint against defendant Garda USA Inc. (Garda) (motion seq. no. 016). Additionally, Kumiva, along with cross-claim defendants Richard Irvin and Robert Irvin, move for summary judgment dismissing Garda and ATI Systems International, Inc.'s counterclaims and cross-claims (motion seq. no. 017). Finally,

DECISION/ORDER
Index No. 650386/06
Motion Seq. No. 016, 017, 018

Garda moves to strike the expert reports of Kumiva's expert David A. Cace and preclude him from offering any expert opinion at trial (motion seq. no. 018). These motions are consolidated for disposition.

Background

On February 25, 2007, Garda acquired ATI Systems International, Inc. ("ATI") pursuant to an Agreement and Plan of Merger (the merger agreement). Kumiva is a representative of ATI's former shareholders. Prior to the merger agreement, ATI had recently acquired another armored car and cash handling business, CDC Systems, Inc. (CDC), through an asset purchase agreement.¹

The merger agreement provided that Garda purchase ATI for \$341,700,000, subject to certain post-closing adjustments. Specifically, the merger agreement provided that Garda would place \$40 million of the purchase price into an escrow account to fund the resolution of another action pending against ATI, and that any remaining funds would then be subject to a potential closing price adjustment based on ATI's net working capital ("NWC"). The other action was ultimately settled, and the parties agreed that all of the remaining funds had been properly disbursed, with the exception of \$6.25 million.

¹ Under the asset purchase agreement, ATI agreed to assume \$1.6 million of CDC's liabilities and to pay CDC up to \$25 million. ATI paid CDC \$15 million at closing, while the additional \$10 million was contingent on CDC contracts continuing to generate at least \$6 million per month. If the revenues remained at that level, ATI agreed to make earn-out payments of \$5 million within three and six months after closing. Both earn-out payments were made to CDC: one by ATI and one by Garda, after it acquired ATI.

Section 2.10(f) of the merger agreement provides that Garda is entitled to the remaining \$6.25 million in the event that ATI's net working capital upon closing was below \$35 million. On the other hand, if the net working capital was above \$35 million, Kumiva would be entitled to the remaining \$6.25 million balance. Furthermore, if ATI's net working capital exceeded \$41 million, Garda is obligated to assign a portion of its accounts receivable to Kumiva, in an amount by which the net working capital exceeded \$41 million, up to a \$9 million cap.

After failing to agree on the amount of ATI's net working capital upon closing, the parties, pursuant to Section 2.10(e)(ii) of the merger agreement, hired Deloitte Touche Tohmatsu Limited (Deloitte) to arbitrate the dispute and make a final, binding determination. On September 15, 2008, Deloitte issued a decision determining that ATI's net working capital at closing was \$45,161,217. Thus, under the merger agreement, Garda owed Kumiva \$6,250,000, plus an assignment of its accounts receivable totaling \$4,161,217.

Garda refused to pay those amounts to Kumiva. As a result, Kumiva commenced this action alleging that Garda breached the merger agreement by failing to disburse the \$6,250,000 from the escrow account and by failing to assign \$4,161,217 from its accounts receivable. In addition, Kumiva also seeks to recover \$77,923, the portion of Deloitte's bill that Garda is obligated to pay, which Kumiva paid in advance. According to Kumiva, Deloitte would not issue its findings unless its entire bill was paid, and, when

Garda refused to pay its share, Kumiva stepped in to pay the full amount in order to obtain Deloitte's report.

Garda asserts counterclaims against Kumiva and former ATI principals Richard Irvin and Robert Irvin for fraud, fraudulent inducement, fraudulent concealment, and breach of contract.² In the fraud claims Garda alleges that ATI concealed problems related to the integration of CDC into ATI, in order to induce Garda into purchasing ATI at an inflated price. Garda also claims that ATI concealed expenditures related to Richard Irvin's family, which also induced it to purchase ATI at an inflated price. Through these frauds, Garda alleges that Kumiva also breached the merger agreement.

Discussion

I. Kumiva, Robert Irvin, and Richard Irvin's Motion for Summary Judgment Dismissing Garda's Counterclaims and Cross-Claims

A. Fraud, Fraudulent Inducement, and Fraudulent Concealment

"The elements of a cause of action for fraud require a material representation of a fact, knowledge of its falsity, an intent to induce reliance, justifiable reliance . . . and damages." *Eurycleia Partners, LP v. Seward & Kissel, LLP*, 12 N.Y.3d 553, 559 (2009).

The elements of fraudulent inducement are substantially the same. *See Perrotti v.*

Becker, Glynn, Melamed & Muffly LLP, 82 A.D.3d 495, 498 (1st Dep't 2011). "A cause

² On July 8, 2010, Justice Barbara Kapnick granted Kumiva's motion to dismiss Garda's unjust enrichment, conversion, and breach of fiduciary counterclaims, but denied the motion with respect to Garda's fraud claims against Kumiva, Robert Irvin, and Richard Irvin, and Garda's breach of contract claim against Kumiva.

of action for fraudulent concealment requires, in addition . . . an allegation that the defendant had a duty to disclose material information and that it failed to do so.”

Mandarin Trading Ltd. v. Wildenstein, 16 N.Y.3d 173 (2011).

Kumiva argues that Garda’s fraud counterclaim should be dismissed because Garda fails to show damages, justifiable reliance, or a material representation. Initially, nothing in the record shows that ATI had any obligation to disclose expenditures related to the Irvin family. Thus, there was no fraudulent concealment of this information and Garda’s fraud claims related to those expenditures are dismissed. Accordingly, the following discussion relates exclusively to Garda’s claims related to ATI’s integration of CDC.

Damages

First, Kumiva contends that Garda’s fraud claim should be dismissed because there is no evidence of any damages suffered by Garda that are compensable in fraud. To support its claim of damages, Garda submits the expert report of Simon Platt (Platt), a forensic accountant, who opines that ATI’s alleged misrepresentations led to a miscalculation of Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA), that, if corrected, would have entitled Garda to a purchase price reduction “of approximately \$36 million.” Garda also submits an expert report from JT Atkins (Atkins), who opines that, if Garda had better knowledge about the CDC integration and the alleged need to fire Richard Irvin, then Garda would have calculated ATI’s EBITDA differently and “this would have resulted in an \$81.0 million purchase price reduction.”

Neither Platt nor Atkins offer a valuation of ATI at the time that Garda acquired it. Instead, Garda and its experts argue that it was entitled to a price reduction based on the difficulties ATI had integrating CDC. However, the out-of-pocket rule precludes Garda from seeking damages based on the possibility of a “better” deal.

Under the out-of-pocket rule, “the true measure of damages for fraud is indemnity for the actual pecuniary loss sustained as a direct result of the wrong,” and “there can be no recovery of profits which would have been realized in the absence of fraud.” *Tradex Global Master Fund SPC LTD v. Titan Capital Group III, LP*, 95 A.D.3d 586, 587 (1st Dep’t 2012). Here, as Garda has failed to submit a valuation of ATI at the time of the acquisition, it has presented no evidence that it had any out-of-pocket loss as a result of acquiring ATI, i.e., that it paid more for ATI than it was worth. Instead, it seeks to prove that it could have made an even more profitable deal if not for the alleged misrepresentations. As these are not proper fraud damages, Garda fails, as a matter of law, to show injury.

Garda contends that Kumiva’s argument as to damages is barred under CPLR 3211(e) because Kumiva failed to raise it at the motion to dismiss stage. Garda cites to *Miller v. Schreyer*, which held that “CPLR 3211(e) permits only one motion to dismiss on the basis of CPLR 3211 (a)(7) for failure to state a cause of action.” 257 A.D.2d 358, 361 (1st Dep’t 1999. Kumiva is not arguing that Garda has failed to state a cause of action, it is arguing that the evidence does not support its claims. Thus, Kumiva’s damages argument is not barred by CPLR 3211(e).

Justifiable Reliance

Kumiva also argues that Garda fails to establish its fraud claim because the CDC integration problems were disclosed prior to acquisition, and the various disclaimers in the merger agreement preclude Garda from showing that it justifiably relied on any alleged misrepresentations. In Section 3.24 of the merger agreement, ATI disclaimed any representation or warranties not embodied in the merger agreement.

Further, Section 4.8(a) specifies that, with respect to the accuracy or completeness of information shared with Garda during the acquisition process, ATI and its officers, shareholders, and personnel will not be “subject to any liability (whether in contract or in tort), except as specifically set forth in this agreement.” Section 4.8(b) provides that ATI “makes no representation or warranty with respect to such estimates, projections and other forecasts and plans [i.e., those exchanged during Garda’s investigation of ATI], including the reasonableness of the assumptions underlying such estimates, budgets, projections and forecasts.”

In general, “comprehensive disclaimers contained in carefully drafted documents executed by sophisticated commercial parties are sufficient to insulate sellers from tort liability.” *Loreley Fin. (Jersey) No. 3 Ltd. v. Citigroup Global Mkts. Inc.*, 119 A.D.3d 136, 138 (1st Dep’t 2014); *see also HSH Nordbank AG v. UBS AG*, 95 A.D.3d 185 (1st Dep’t 2012). If sophisticated parties wish to preserve fraud claims, courts have instructed them to insert an “appropriate prophylactic provision to ensure against the possibility of misrepresentation.” *ACA Fin. Guar. Corp. v. Goldman, Sachs & Co.*, 106 A.D.3d 494,

494 (1st Dep't 2013); *see also* *Centro Empresarial Cempresa S.A. v América Móvil, S.A.B. de C.V.*, 76 A.D.3d 310, 320-321 (1st Dep't 2010), *aff'd* 17 N.Y.3d 269 (2011) (“plaintiffs may truly be said to have willingly assumed the business risk that the facts may not be as represented” where they entered into a transaction “in reliance on defendants’ unverified representation concerning [defendant’s] financial condition, without inserting . . . a prophylactic provision to ensure against the possibility of misrepresentation” (internal quotation marks and citations omitted)).

Based on the parties’ submissions, it is clear that ATI disclosed the difficulties that it was having with the CDC integration to Garda prior to acquisition. In the disclosure schedules attached to the merger agreement, it was specifically disclosed that ATI’s acquisition of CDC resulted in “several start-up issues . . . which caused some financial losses and some potential lost business.” Moreover, on January 23, 2007, Garda was advised by PricewaterhouseCoopers (PwC), which performed financial and tax due diligence on ATI for Garda, that “it is too early to assess the effectiveness of the integration plan and the results being generated.” Nevertheless, Garda decided to go ahead with the acquisition in the following month.

Here, Garda determined to acquire ATI shortly after ATI acquired CDC. It signed a merger agreement with comprehensive disclaimers and it did not condition the disclaimers on the truth of information exchanged between the parties prior to the agreement. Thus, Garda willingly assumed the business risk that the facts about the CDC integration exchanged prior to the merger agreement may not have been as represented.

Centro Empresarial Cempresa S.A., 76 A.D.3d at 310. As such, Garda has failed, as a matter of law, to show reasonable reliance on any information exchanged prior to the merger agreement.

Material Misrepresentation

Putting aside the alleged misrepresentations prior to the merger which Garda could not, as a matter of law, have relied on, Garda also argues that the disclosure regarding CDC in the merger agreement was itself a misrepresentation. That disclosure, referred to above, provided that “there were several start-up issues including deposits being misrouted, lost or delayed, which caused some financial losses and some potential lost business.” Disclosure Schedule, ¶ 3.7(13). Garda argues that this representation is false because it uses the past tense. However, nothing in the disclosure states that the integration problems were definitively resolved.

Garda also argues that the disclosure was false because it uses the qualifier “potential” to refer to lost business. CDC had a branch in Trenton that ATI closed after acquiring CDC. ATI had difficulty integrating CDC’s former business with its own in this area and lost some clients as a result. However, the record shows that ATI, at the time of the merger, was still trying to maintain relations or win back clients who were upset by the integration problems. Thus, the use of “potential” does not transform the disclosure into a false representation. As such, the disclosure was not a material misrepresentation.

At bottom, Garda's fraud claims must be dismissed because it did not suffer any compensable damages from purchasing ATI, and could not have reasonably relied on any misrepresentations made by ATI. I therefore grant Kumiva, Richard Irvin, and Robert Irvin's motion for summary judgment dismissing the fraud counterclaim and cross-claims against them.

B. Breach of Contract

Garda alleges that Kumiva breached Section 3.6(a) of the merger agreement by providing inaccurate and incomplete books, records, and financial statements for ATI. Kumiva contends that this claim should be dismissed because Garda has no evidence of any books, records, or financial statements that contain any representations. Kumiva also points out that any spreadsheets exchanged during due diligence are not financial statements covered by Section 3.6(a).

Under Section 3.6(a) of the merger agreement, ATI was obligated to deliver to Garda "correct and complete copies of the Financial Statements." The term "Financial Statements" is defined by the merger agreement as "Audited Financial Statements and the Interim Financial Statements." Merger Agreement, § 1.1.

The Audited Financial Statements, are defined as: "the audited consolidated balance sheets of the Company [ATI] and its Subsidiaries at December 31, 2005 and 2004, and the audited consolidated statements of operations, shareholder equity and cash flows . . . together with the notes thereto." The Interim Financial Statements are defined as "the unaudited consolidated balance sheet of the

Company and its Subsidiaries at October 31, 2006, and the unaudited consolidated statements of operations, shareholder's equity and cash flow of the Company and its Subsidiaries for the ten month period then ended.”

Garda fails to raise any issue of fact as to whether Kumiva made any misrepresentations as to financial statements covered by Section 3.6(a) of the merger agreement. Accordingly, Garda's breach of contract counterclaim against Kumiva is dismissed.

II. Kumiva's Motion for Summary Judgment On Its Complaint

Kumiva separately moves for summary judgment on its complaint. In the complaint, Kumiva seeks to recover \$6,250,000 from the escrow account (first cause of action), \$4,161,217 from Garda's accounts receivable (second cause of action), and \$77,923 in fees that Kumiva paid in advance to Deloitte on Garda's behalf.

With the dismissal of Garda's counterclaims, Kumiva is entitled to the payouts it seeks under the merger agreement. Specifically, Kumiva is entitled to the \$6,250,000 from the escrow account and \$4,161,217 from Garda's accounts receivable. Garda breached Section 2.10(f) by failing to pay these amounts after Deloitte's final and binding determination of ATI's net working capital at the time of the merger. Thus, Kumiva's motion seeking summary judgment on its first and second causes of action is granted.

Garda contends that summary judgment is inappropriate because Kumiva owes it \$636,000. This figure is comprised of \$500,000 in deposit losses that Kumiva allegedly left off the opening balance sheet submitted to Deloitte, and \$136,000 in customer credits

that were approved prior to the merger. Neither of these alleged sums affect Kumiva's entitlement to the \$6,250,000 held in escrow or the \$4,161,217 in accounts receivable. With respect to the \$500,000 in deposit losses, Garda is improperly trying to overturn the final and binding determination by Deloitte. As to the \$136,000 in customer credits, Garda provides no basis for recovering a liability that was incurred in the normal course of business.

Kumiva also makes a *prima facie* showing of entitlement to judgment as a matter of law on the portion of Deloitte's bill owed by Garda, but paid by Kumiva. Kumiva relies on the affidavit of Robert Irvin who states that because "Deloitte would not issue its final decision until all fees were paid, Kumiva paid not only its share but also the \$77,923 owed by Garda in order to get Deloitte's decision."

Section 2.10(e)(ii) of the merger agreement states, in relevant part, that "[t]he fees and expenses of the Auditor shall be allocated ratably among the Representative, on the one hand, and the Parent, on the other hand, in the same proportion that the aggregate dollar amount of items unsuccessfully disputed by each party." Garda breached this provision by failing to pay Deloitte. As Garda has not rebutted Kumiva's showing that it was damaged in the amount of \$77,923 by this breach, Kumiva is entitled to summary judgement on its third cause of action for breach of contract.

III. Garda's Motion to Strike and Preclude Kumiva's Expert

Garda's motion to strike and preclude the opinions of Kumiva's expert David Cace is moot, in light of my decision to grant Kumiva's motions for summary judgment.

Even if the motion were not moot, Garda is not entitled to the remedy it seeks. Expert testimony is admissible where it “would help to clarify an issue calling for professional or technical knowledge, possessed by the expert and beyond the ken of the typical juror.”

People v. Williams, 20 N.Y.3d 579, 583-584 (2013) (internal quotation marks and citation omitted). Here, Cace holds himself out as an expert in auditing, accounting, and forensic accounting. Garda argues that his testimony should be struck because he is not an expert in valuations, investment banking, due diligence and mergers and acquisitions. However, Garda’s challenges go to the weight of Cace’s testimony rather than its admissibility. *People v Oddone*, 22 N.Y.3d 369, 376 (2013).

In accordance with the foregoing, it is

ORDERED that plaintiff Kumiva Group, LLC’s motion for summary judgment on the complaint against defendant Garda USA Inc. (motion seq. No. 016) is granted in the total amount of \$10,489,140; and it is further

ORDERED that the Clerk of the Court is directed to enter judgment in favor of plaintiff Kumiva Group, LLC and against defendant Garda USA Inc. in the amount of \$10,489,140, with interest at the statutory rate from October 24, 2008, until the date of the decision on this motion, together with costs and disbursements as taxed by the Clerk upon submission of an appropriate bill of costs; and it is further

ORDERED that plaintiff Kumiva Group, LLC and cross-claim defendants Richard Irvin and Robert Irvin’s motion for summary judgment dismissing all counterclaims and cross-claims (motion seq. No. 017) is granted; and it is further

ORDERED that defendant Garda USA Inc.'s motion to strike the expert reports of Kumiva's expert David A. Cace and preclude him from offering any expert opinion at trial (motion seq. No. 018) is denied as moot.

This constitutes the decision and order of the Court.

DATE : July 24, 2015


SCARPULLA, SALIANN, JSC