Robinson v Oz Master Fund, Ltd.
2015 NY Slip Op 31942(U)
October 16, 2015
Supreme Court, New York County
Docket Number: 654009/13
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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TIMOTHY ROBINSON and WHORL, LLC (as Successor and assignee of BIOPAY, LLC),

Plaintiff,

-against-

OZ MASTER FUND, LTD., DENARIUS TOUCH, L.L.C., PLAINFIELD SPECIAL SITUATIONS MASTERFUND LIMITED, PLAINFIELD ASSET MANAGEMENT, HIGHBRIDGE INTERNATIONAL LLC, OZ FINANCIAL INVESTORS II, INC., PLAINFIELD DIRECT WEST IV LLC, and PLAINFIELD DIRECT LLC,

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DECISION/ORDER
Index No. 654009/13
Mot. Seq. Nos. 001 & 002

HON. SALIANN SCARPULLA, J.:

In a case involving a company that has been dissolved through bankruptcy proceedings, defendants Oz Master Fund, Ltd. ("Oz Master"), Denarius Touch ("Denarius"), L.L.C., Highbridge International LLC ("Highbridge"), and Oz Financial Investors II, Inc. ("Oz Financial II") (collectively, the "Oz defendants"), move, pursuant to CPLR 3211, to dismiss the complaint (motion seq. no. 001). Defendants Plainfield Special Situations Master Fund, Ltd. ("Plainfield Master"), Plainfield Asset Management ("Plainfield AM"), Plainfield Direct West IV, LLC ("Plainfield Direct IV"), and Plainfield Direct, LLC ("Plainfield Direct") (collectively, the "Plainfield defendants") also move to dismiss the complaint (motion seq. no. 002). Motion sequence numbers 001 and 002 are consolidated for disposition.

This action is rooted in a 2005 acquisition of a company that offered biometric payment services by another company engaged in the same business. Biopay, LLC ("Biopay"), the acquired company, received $15 million in cash and an additional $67 million in notes owed to its successor, Whorl, LLC ("Whorl"). Solidus Networks Inc. ("Solidus"), the acquiring company, defaulted on the notes in 2007 and was placed into bankruptcy. In bankruptcy, the claims of more senior creditors exhausted Solidus's assets, and Whorl and Timothy Robinson ("Robinson"), the principal of Biopay and Whorl, received nothing. Robinson and Whorl instituted this action against Solidus's more senior creditors, and related entities.

Solidus's acquisition of Biopay was structured through a complex series of agreements. Solidus, through an Asset Purchase Agreement ("APA") entered into between itself and Robinson and Biopay, acquired substantially all of Biopay's assets in December 2005. At the same time, defendants Oz Master, Denarius, Highbridge, and Plainfield Master (collectively, the "senior creditors"), as well as others, entered into an Amended and Restated Securities Purchase Agreement ("SPA"), under which Solidus, among other things, authorized $75 million in senior secured promissory notes to the senior creditors. On the same date, Solidus entered into a "Consent and Agreement" (the "Consent Agreement") with the senior creditors allowing it to acquire Biopay through the APA.

The deal was structured so that Biopay's intellectual property, including patents related to its biometric transaction business, was placed in an entity related to Solidus that the parties refer to as the "IP Sub." Whorl's notes were to be secured by stock in the IP Sub, and the parties refer to this arrangement as the "Biopay Lien." In the Consent Agreement, the senior creditors acknowledged that the equity and assets of the IP Sub were not to be considered collateral under the SPA until Solidus had paid the money it owed to Whorl. Specifically, the Consent Agreement provided:

> [Solidus] hereby acknowledges and agrees that, concurrently with the termination of the BioPay Lien, (x) [Solidus] shall cause the IP Sub to become a "Grantor" under the [APA] and (y) all of the assets of the IP Sub and all equity securities of the IP Sub shall thereafter be "Collateral" as such term is defined in the [SPA]. The [senior creditors] hereby acknowledge and agree that, so long as the BioPay Lien remains in effect, neither the equity securities of the IP Sub nor the assets acquired by the IP Sub in the BioPay Acquisition shall be "Collateral" as such term is defined in the [SPA], except that "Collateral" shall include a second priority lien on the [sic] all equity securities of the IP Sub.

The following month, in January 2006, Solidus, Biopay, and the senior creditors entered into a subordination agreement (the "Subordination Agreement"), which, among other things, made clear that the Biopay notes were subordinate to the senior creditor notes. At the same time, Solidus and the IP Sub entered into a pledge agreement (the "Pledge Agreement"), under which Solidus and the IP Sub pledged that they would not encumber the assets held by the IP Sub with few exceptions that are not relevant here.

In June 2007, Solidus failed to pay amounts it owed to Whorl under the secured notes. However, prior to the default, Whorl had not perfected its interest in the IP Sub stock.[1] In November 2007, Solidus was placed into involuntary bankruptcy, while the IP

[1] Plaintiffs sued their attorneys in connection with this failure and settled before trial.

Sub was placed into voluntary bankruptcy. Subsequently, the senior lenders provided an additional $13.5 million to Solidus in the form of debtor-in-possession ("DIP") financing. Denarius and Highbridge entered into the DIP financing directly, while Oz Master entered through Oz Financial II and the Plainfield defendants entered the DIP financing through Plainfield Direct IV. Plaintiffs allege that Oz Financial II and Plainfield Direct IV were created for the purpose of entering into the DIP financing. The DIP financing required the IP Sub to act as a primary guarantor of the obligations of Solidus under the DIP financing, and granted the senior lenders a security interest senior to that held by Whorl. Shortly thereafter, Solidus defaulted under the DIP financing. In the bankruptcy proceedings, the assets of the IP Sub were liquidated for the benefit of the senior creditors.

In February 2014, plaintiffs filed the complaint which seeks recovery under four causes of action. First, plaintiffs allege that defendants breached the Subordination Agreement. Second, plaintiffs allege that they are entitled to recovery under the Consent Agreement as a third-party beneficiary. Third, plaintiffs allege that defendants breached the covenant of good faith and fair dealing. Fourth, plaintiffs claim they are entitled to recovery against the defendants under an unjust enrichment theory.

Discussion

"When determining a motion to dismiss, the court must accept the facts as alleged in the complaint as true, accord plaintiffs the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory" (*Goldman v Metro. Life Ins. Co.*, 5 NY3d 561, 570-71 [2005] [internal quotations and citations omitted]). "Dismissal under CPLR 3211 (a) (1) is warranted 'only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law'" (*511 W. 232nd Owners Corp. v Jennifer Realty Co.*, 98 NY2d 144, 152 [2002], quoting *Leon v Martinez*, 84 NY2d 83, 88 [1994]).

I. Breach of the Subordination Agreement

Initially, the Plainfield defendants argue that Plainfield AM and Plainfield Direct IV cannot be liable under the Subordination Agreement because they were not parties to it. Next, the Plainfield defendants argue that plaintiffs fail to allege a breach of the Subordination Agreement.

Similarly, the Oz defendants argue that plaintiffs fail to allege a breach of the Subordination Agreement. The Oz defendants further argue that plaintiffs' attempt to allege that the defendants breached the Subordination Agreement through a breach of the Consent Agreement fails, because the terms of the Consent Agreement were not explicitly incorporated into the Subordination Agreement.

As to a direct breach, plaintiffs reference sections 3 (a) (iii), 7, and 11 (b) of the Subordination Agreement. Section 3 (a) (iii) of the Subordination Agreement provides that Biopay "agrees not to initiate, prosecute or participate in any claim, action or other proceeding challenging the enforceability, validity, perfection or priority of the Senior Secured Obligations or any liens and security interests securing the Senior Secured Obligations except to protect the first priority perfected security interest of the BioPay

Lien." This provision does not place any obligation on the senior creditors, it merely states that Whorl is not precluded from bringing a claim to protect its interest in the BioPay Lien. Thus, defendants could not have breached this provision.

Similarly, sections 7 and 11 (b) of the Subordination Agreement do not place an affirmative obligation on the senior creditors. As such, plaintiffs cannot allege breach of the agreement based on these sections.

Plaintiffs additionally argue that defendants breached the Subordination Agreement through a breach of the Consent Agreement. This argument is built on the contention that the terms of the Consent Agreement must be read into the Subordination Agreement. In support of such a reading, plaintiffs rely, among others cases, on *Brax Capital Group, LLC v WinWin Gaming, Inc.*, which held that "documents executed at about the same time and covering the same subject matter are to be interpreted together, even if one does not incorporate the terms of the other by reference, and even if they are not executed on the same date, so long as they are substantially contemporaneous" (83 AD3d 591, 592 [1st Dept 2011] [internal quotation marks and citation omitted]).

The integration clause of the Subordination Agreement provides that "[t]his Agreement and the agreements and documents referred to herein contain the entire agreement of the parties and supersede any and all prior agreements among the parties with respect to the subject matter hereof." The Subordination Agreement refers several times to the Consent Agreement.

In the relevant language in the Consent Agreement, which was executed approximately one month before the Subordination Agreement and was between Solidus and the senior creditors, the senior creditors acknowledged that the assets of the IP Sub were not to be considered collateral under the SPA until Solidus had paid the money it owed to Whorl. The SPA defines collateral as "all of the property of whatever kind and nature pledged as collateral under any Security Document."

Here, while the Consent Agreement should be read in conjunction with the Subordination Agreement, the senior creditors do not make any promises to plaintiffs in the Consent Agreement. Thus, nothing in the Consent Agreement creates a breach of the Subordination Agreement. Similarly, the Pledge Agreement does not contain any obligation running from defendants to plaintiffs, but instead contains promises from Solidus and the IP Sub to plaintiffs. Thus, as plaintiffs fail to allege a specific breach that is not contradicted by the relevant contracts, plaintiffs' first cause of action for breach of the Subordination Agreement is dismissed.

II. Breach of the Consent Agreement Under a Third-Party Beneficiary Theory

Plaintiffs seek to recover under the Consent Agreement even though they were not a party to that agreement. To recover for a breach of contract as a third party beneficiary, a party must show:

> (1) the existence of a valid and binding contract between other parties, (2) that the contract was intended for [its] benefit, and (3) that the benefit to [it] is sufficiently immediate . . . to indicate the assumption by the contracting parties of a duty to compensate [it] if the benefit is lost

(*Mandarin Trading Ltd. v Wildenstein*, 16 NY3d 173, 182 [2011] [internal quotation marks and citation omitted]).

Here, plaintiffs cannot satisfy the second element because the senior creditors entered into the Consent Agreement for the benefit of Solidus rather than the benefit of Whorl and Robinson. Solidus could not acquire BioPay without the permission of the senior creditors, so the Consent Agreement was entered into for that purpose. There is no indication in the Consent Agreement that it was entered into for Whorl's benefit and that the parties intended Whorl to be able to recover for any breaches. As such, plaintiffs' second cause of action for breach of the Consent Agreement is dismissed.

III. Breach of the Covenant of Good Faith and Fair Dealing

Plaintiffs allege that defendants violated the covenant of good faith and fair dealing by maneuvering to deprive plaintiffs of the protections of the various transaction agreements by securing the DIP loan with the assets of the IP Sub as collateral.

Courts have long read a covenant of good faith and fair dealing into contracts:

> In New York, all contracts imply a covenant of good faith and fair dealing in the course of performance. This covenant embraces a pledge that neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract. While the duties of good faith and fair dealing do not imply obligations inconsistent with other terms of the contractual relationship, they do encompass any promises which a reasonable person in the position of the promisee would be justified in understanding were included

(*DMF Gramercy Enters., Inc. v Lillian Troy 1999 Trust*, 123 AD3d 210, 215 [1st Dept 2014] [internal quotation marks and citation omitted]).

The Oz defendants argue that plaintiffs were never promised that they would receive the IP Sub's assets and, therefore, they could not have been deprived of a benefit they were not promised. The Plainfield defendants argue that the Court cannot write a term into the contract that the parties did not agree upon. Both sets of defendants argue that the good faith and fair dealing claim is duplicative of the contractual claims. However, the dispositive argument is made by the Plainfield defendants, who contend that, under CPLR 3211 (a) (5), plaintiffs' claims are barred by the order of the bankruptcy court and the doctrines of collateral estoppel and *res judicata*.[2]

While the bankruptcy court noted that it was not determining whether defendants violated the terms of any of the inter-creditor agreements at issue here, it did find that the DIP financing was negotiated in good faith. It is conceptually impossible for defendants to have negotiated the DIP financing, the instrument by which they established a more senior claim than plaintiffs on the IP Sub's assets, in good faith for purposes of the bankruptcy proceeding, and in bad faith for purposes of a subsequent claim by plaintiffs.

[2] Although this argument was not specifically advanced by the Oz defendants, I search the record and dismiss this cause of action as against both defendants.

Whorl filed a claim in the bankruptcy proceeding and filed an objection to the order of the bankruptcy court, and, thus, had an opportunity to litigate this issue before the bankruptcy court (*see generally Ryan v New York Tel. Co.*, 62 NY2d 494, 500 [1984]; *see also McNeary v Senecal*, 197 AD2d 835, 836 [3d Dept 1993] [holding that "[p]rinciples of res judicata and collateral estoppel apply to decisions of Bankruptcy Court"). The bankruptcy court decided this issue against Whorl by finding that the DIP financing had been negotiated in good faith. Thus, plaintiffs are collaterally estopped by the order of the bankruptcy proceeding from bringing a claim for breach of the covenant of good faith and fair dealing and the third cause of action is dismissed.

IV. Unjust Enrichment

Plaintiffs claim that defendants were unjustly enriched through a scheme to maneuver around plaintiffs' claim to the IP Sub's assets.

To maintain an unjust enrichment cause of action, "[a] plaintiff must show 'that (1) the other party was enriched, (2) at that party's expense, and (3) that it is against equity and good conscience to permit [the other party] to retain what is sought to be recovered'" (*Mandarin Trading*, 16 NY3d at 182 [internal quotation marks and citation omitted]).

Both sets of defendants argue that the unjust enrichment claim is barred by the various agreements related to Solidus's acquisition of Biopay. In support of this argument, the Plainfield defendants cite to *Basis Yield Alpha Fund (Master) v Goldman*

Sachs Group, Inc., among other case, in which the court dismissed a claim for unjust enrichment, holding "[t]he theory is one created in law in the absence of any agreement" (115 AD3d 128, 141 [1st Dept 2014]).

The Oz defendants argue that plaintiffs fail to allege the second element. That is, the Oz defendants argue that the disposition of assets through bankruptcy proceedings were not at plaintiffs' expense, as Whorl's unperfected security interest was not enough to provide it with a right to the IP Sub's assets. Moreover, the Oz defendants highlight the bankruptcy court's approval of the sale of IP Sub's assets "free and clear of all Liens and Claims" and its note that the assets were sold for "fair consideration."

In opposition, plaintiffs argue that there is a dispute as to whether various agreements cover the entirety of the current dispute. Plaintiffs argue, citing to *Art & Fashion Group Corp. v Cyclops Production, Inc.*, 120 AD3d 436 [1st Dept 2014]), that they are allowed to plead in the alternative, and that, accordingly, dismissal of this cause of action is premature. Plaintiffs also cite to *Philips International Investments, LLC v Pektor*, for the proposition that an unjust enrichment claim "depends upon *broad* considerations of equity and justice" (117 AD3d 1, 7 [1st Dept 2014] [internal quotation marks and citation omitted]).

Art & Fashion Group Corp. cited a Second Department case for the proposition that "'(w)here . . . there is a bona fide dispute as to the existence of a contract . . . a plaintiff may proceed upon a theory of quasi contract as well as contract, and will not be required to elect his or her remedies'" (120 AD3d at 439 [citation omitted]). Here, there is no dispute that the parties have a contract. Therefore, the unjust enrichment claim is barred by the existence of the Subordination Agreement.

While two of the defendants were not signatories of the Subordination Agreement, the unjust enrichment claims are barred against them as well. Oz Financial II and Plainfield Direct IV, the two entities allegedly created to enter into the DIP financing, have too weak a connection to plaintiffs to sustain a claim for unjust enrichment (*see Georgia Malone & Co., Inc. v Rieder*, 19 NY3d 511, 516 [2012] [stating that in order to maintain an unjust enrichment claim "there must exist a relationship or connection between the parties that is not too attenuated"] [internal quotation marks and citation omitted]). That is, their only connection to plaintiffs is through entities whose relationship with plaintiffs is governed by contract. Moreover, in the absence of a contractual breach, plaintiffs are asking the court to look at the same facts the bankruptcy court looked at and come to a different conclusion as to the disposition of the IP Sub's assets. While the courts equitable powers under this cause of action are broad, they are not that broad.

Accordingly, it is

ORDERED that motions to dismiss of defendants Oz Master Fund, Ltd., Denarius Touch, L.L.C., Highbridge International LLC, and Oz Financial Investors II, Inc. (motion seq. no. 001); and of defendants Plainfield Special Situations Master Fund, Ltd., Plainfield Asset Management, Plainfield Direct West IV, LLC, and Plainfield Direct, LLC (motion seq. no. 002) are granted and the complaint is dismissed in its entirety; and it further

ORDERED that the Clerk of Court is directed to enter judgment accordingly.

This constitutes the Decision and Order of this Court.

Dated: October 16, 2015

ENTER:

J.S.C.

HON. SALIANN SCARPULLA