Krauter & Co. v Ross
2019 NY Slip Op 30030(U)
January 4, 2019
Supreme Court, New York County
Docket Number: 160972/15
Judge: Tanya R. Kennedy

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 63

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KRAUTER & COMPANY,

Plaintiff,

Index No. 160972/15
Motion Sequence #002

- against -

NICHOLAS ROSS & ALWEX INC.,

Defendants.

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NICHOLAS ROSS & ALWEX INC.,

Counterclaimants,

- against -

KRAUTER & COMPANY, NEIL KRAUTER and MYLES BLOCK,

Counterclaim Defendants.

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TANYA R. KENNEDY, J.:

Plaintiff-Counterclaim Defendant Krauter & Company (Krauter), and Counterclaim Defendants Neil Krauter and Myles Block (Block) (collectively, movants) move for an order, pursuant to CPLR 3211 (a)(1) and (a)(7), dismissing the amended counterclaims asserted against them.

Defendants Nicholas Ross (Ross) and Alwex Inc. (Alwex) (together, counterclaimants) move for an order, pursuant to CPLR 3211 (a)(1) and (a)(7), dismissing all five causes of action in the amended complaint.

Amended Complaint

Krauter is a risk and insurance services firm, providing alternative risk management, risk financing, insurance brokerage, financial solutions, and insurance program management services for businesses, public entities, associations, professional services organizations, and private clients (amended complaint, ¶7).

While servicing its clients' personal insurance needs through its Private Client Services division, Krauter secures opportunities to serve such clients' business needs in commercial and other lines of insurance, as well as personal insurance needs (*id.*, ¶8). Alwex is a direct competitor of Krauter in many business segments, including Private Client Services (*id.*, ¶10).

On or about August 5, 2013, Ross commenced employment at Krauter as the head of Krauter's Private Client Services, New York division. Ross would later lead the Private Client Services division for Krauter nationwide (*id.*, ¶11). Ross was responsible for servicing and developing Krauter's Private Client Services clients and developing and maintaining a good business relationship with such clients (*id.*, ¶12).

Krauter's clients serviced by Ross were introduced to Ross by Krauter (*id.*, ¶13). Ross gained knowledge and had access to Krauter's confidential information and trade secrets including: (a) information concerning Krauter's Private Client Services operations; (b) Krauter's business strategies (i.e. rates and fees); and (c) detailed information about Krauter's clients, including, but not limited to, their personal address and contact information, social security numbers, banking and investment information, policy expiration dates, policy renewals, policy terms and conditions, information regarding the markets or sources with which insurance is placed, the amounts paid by such clients to Krauter, and leads and referrals to prospective Private Client Services clients (*id.*, ¶15).

Krauter disseminates policies to its employees that prohibit the use or disclosure of Krauter's confidential information and trade secrets for non-business purposes, requiring employees who have access to such confidential information and trade secrets to sign agreements that restrict their use or disclosure and restrict certain post-employment activities, and password protecting access to computers and systems containing Krauter's confidential information and trade secrets (*id.*, ¶17).

On or about September 10, 2014, Ross signed Krauter's Employee Confidentiality Agreement (Confidentiality Agreement) thereby agreeing not to use confidential information for a period of at least 18 months or the length of time in the "NDA"[1] signed by Krauter in the event Ross left Krauter to work for a competitor (*id.*, ¶¶18, 20).

On August 17, 2015, Ross submitted a letter of voluntary resignation, effective immediately. Immediately upon Ross's voluntary resignation from Krauter, he commenced employment at Alwex (*id.*, ¶22). Soon after Ross tendered his resignation, Krauter discovered that Ross, before his resignation, had copied digital files containing Krauter's client information from Krauter's computer and transferred the copied files onto two flash drives. Ross then deleted the files on Krauter's computer and took the copied files with him to his current employer Alwex (*id.*, ¶23). Krauter also discovered that Ross was actively soliciting several clients for Alwex whilst still employed by Krauter and serving as Krauter's Head of Private Client Services (*id.*, ¶24). As a result of Ross's coercive efforts, multiple Krauter clients have transferred their insurance and risk policies from Krauter to Alwex (*id.*, ¶29).

[1] NDA is not defined in the amended complaint.

On or August 18, 2015, Krauter sent a cease and desist letter to Ross, demanding that Ross: (1) cease and desist from using Krauter's confidential information stolen from Krauter and (2) to immediately return that information (*id.*, ¶31). Ross, directly or through others, continues to solicit and service clients of Krauter (*id.*, ¶32). Ross has not returned any of Krauter's confidential information or trade secrets and has succeeded, to date, in diverting hundreds of thousands of dollars of revenue from Krauter (*id.*, ¶¶33-34). For his benefit and the benefit of Alwex, Ross continues to use Krauter's confidential information and trade secrets (*id.*, ¶37).

The amended complaint contains five causes of action for: (1) breach of contract against Ross (solicitation and servicing of Krauter clients); (2) breach of contract against Ross (breach of confidentiality); (3) misappropriation of confidential information and trade secrets against Ross and Alwex; (4) tortious interference against Alwex; and (5) unfair competition against Ross and Alwex. Each cause of action also seeks injunctive relief.

Amended Answer of Ross and Alwex

Neil Krauter is the Chief Executive Officer of Krauter (amended answer, ¶45). Counterclaim Defendant Myles Block is Krauter's Chief Operating Officer (Block) (*id.*, ¶46).

Ross is an insurance broker and has been licensed as such since June 2011 by the State of New York. Since that time, he has focused his efforts on servicing clients for their property and casualty insurance needs. His clients have consisted of individuals, as well as corporations and professional service firms (*id.*, ¶47).

Ross started his insurance career at Global Coverage, Inc. (Global). When he left Global in August 2013, he had built up a successful following of approximately 100 clients (*id.*, ¶48). Ross left Global on amicable terms to join Krauter with the belief that Krauter provided a stronger platform and more resources for him to serve his growing client base. Nearly all of Ross's clients

followed Ross to Krauter and did so by executing a form of letter commonly referred to as a "Broker of Record Letter" informing the insurance carrier of the client's desire to change brokerage firms to Krauter from Global (*id.*, ¶49).

Apart from the offer letter, Employee Handbook and Confidentiality Agreement, there are no other written agreements between the parties governing the terms of employment, other than compensation adjustment notices. Most notably, there is no agreement restricting Ross from terminating his employment without notice, working for a competitor, soliciting clients or employees to join him at a competing insurance brokerage company, or from using information that Ross obtained prior to joining Krauter or from public sources while at Krauter. Moreover, there is no agreement between Ross and Krauter whereby Ross assigned or granted any ownership rights in his client relationships to Krauter (*id.*, ¶50). Also, upon joining Krauter, Ross imported his entire database of contacts onto the Krauter computer system into a file in Microsoft Outlook labeled under Ross's name (*id.*, ¶51).

Krauter's computer systems had three separate areas where data was stored and used by Ross. The first was the Outlook file where Ross maintained his own contacts, as well as his calendar. The second database was a drive on the Krauter system called the "H" drive and was labeled by Krauter's IT service with a file folder called the "Nick" drive. Other employees had file folders in the "H" drive so designated with their names. Krauter set up this drive so that Ross and other employees could maintain their client contact information, templates of insurance forms and copies of client's policy declaration pages, as well as other documents that they could create themselves. (*id.*, ¶52).

There was a shared drive labeled "K" for all employees to access, which however was phased out of use for the Private Client Services department in February 2015. The third database

was maintained in the firm-wide client management system. This system was powered by software from Applied Systems and known as the Epic database. The Epic database covered the entire client base of the firm and contained client information including contact information, but also information about client insurance policies such as the name of the carrier, the insurance coverage, and the insurance policy information (*id.*).

In or around March 2015, Krauter provided Ross with the non-exclusive use of a "Microsoft Surface Tablet computer (Tablet). The Tablet was supposed to be capable of remotely accessing the Krauter network, but it was often unable to do so and was unreliable, particularly as it pertained to the "Epic database," "Nick" drive, and "K" drive. Consequently, Ross made copies of some of the data that was on the "Nick" drive, as well as his own Outlook files, to access through an external USB flash drive while he was traveling or working from home. There is no prohibition in the Confidentiality Agreement from using data in such fashion (*id.*, ¶53).

Not long after commencing employment at Krauter, Ross began to experience frustration that representations Neil Krauter made about the firm and his position were not true (*id.*, ¶54). In the days leading up to Ross's resignation on August 17, 2015, Ross contacted a number of his clients, all of whom were clients that he either brought with him from Global or whom he personally procured through his own efforts while at Krauter. He informed those clients that he was considering leaving Krauter, and that if they so desired, he would arrange for them to switch to his new agency once he had begun his new employment (*id.*, ¶55).

From August 17, 2015 through to the present, Neil Krauter and Block, acting on behalf of Krauter and individually, have engaged in an aggressive and improper campaign to attack and malign Ross both professionally and personally and to interfere with his business relationship with Alwex, as well as Alwex's business relationships with Ross and others (*id.*, ¶56).

Specifically, Block, at Neil Krauter's direction, emailed a notice addressed to "Affected Clients, Markets, and Friends of the Firm," accusing Ross of criminal acts, including misappropriating sensitive client information, such as social security numbers, and violating the Confidentiality Agreement (Criminal Notice). The Criminal Notice mentioned that Krauter had reported Ross to the New York City Police Department and that an investigator may be in touch with the recipient. The Criminal Notice was allegedly sent to Ross's clients, referral sources and professional relationships such as CPA's and attorneys, and to nearly all of his personal and social contacts, including family, friends, parents at his children's school, school teachers and administrators, and former employers inside and outside the insurance industry (*id.*, ¶¶57-58).

The amended answer contains 11 counterclaims for: (1) violation of 18 U.S.C. §§2501 *et seq.*, 2520 and 2701 *et seq.* (the Electronic Communications Privacy Act); (2) violation of 18 U.S.C. §2701 *et seq.* (the Stored Communications Act; (3) violation of 18 U.S.C. §1030 *et seq.* (the Computer Fraud and Abuse Act); (4) violation of New York Penal Law §156.05 (Unauthorized Use of a Computer); (5) violation of New York Penal Law §156.10 (Computer Trespass); (6) violation of New York Penal Law §156.30 (Unlawful Duplication of Computer Related Material in the First Degree); (7) violation of New York Penal Law §156.35 (Criminal Possession of Computer Related Material); (8) tortious interference with contractual relations and business relationships; (9) defamation; (10) libel per se; and (11) conversion.

DISCUSSION

Cross-Motion to Dismiss the Amended Complaint

On a motion to dismiss pursuant to CPLR 3211(a)(1), the movant is required to establish that the documentary evidence conclusively refutes the party's claim (*see AG Capital Funding Partners, L.P. v State St. Bank & Trust Co.*, 5 NY3d 582, 590-591 [2005]).

In determining a motion to dismiss pursuant to CPLR 3211(a)(7), the court is required to "afford the pleadings a liberal construction, accept the allegations of the complaint as true and provide plaintiff the benefit of every possible favorable inference" (*id.* at 591) [internal citations and quotation marks omitted].

First and Second Causes of Action **(Breach of Contract)**

The first cause of action alleges that Ross breached the Confidentiality Agreement by the "solicitation and servicing of Krauter clients" (amended complaint, ¶45).

The second cause of action alleges that Ross breached the Confidentiality Agreement by "failing to return, using, and/or disclosing to Alwex confidential Information and trade secrets [belonging] to Krauter" (*id.*, ¶51).

The complaint, *inter alia*, alleges that: (1) "[s]oon after Ross tendered his resignation to Krauter, Krauter discovered that Ross, before his resignation, had copied digital files containing Krauter's client information from Krauter's computer and transferred the copied files onto two (2) flash drives" and "then deleted the files on Krauter's computer and took the copied files with him to his current employer Alwex;" (2) "Krauter also discovered that Ross was actively soliciting several clients for Alwex whilst still employed by Krauter and serving as Krauter's head of Private Client Services;" (3) "[a]s a result of Ross' coercive efforts, multiple Krauter clients have transferred their insurance and risk policies from Krauter to Alwex;" (4) "Alwex and Ross were aware that Ross was bound to non-solicitation and confidentiality covenants with Krauter, which continue to govern Ross's conduct following his employment with Krauter;" and (5) "[f]or his benefit and the benefit of Alwex, Ross continues to use Krauter's confidential information and trade secrets" (id., ¶¶23, 24, 29, 30, 37).

The Confidentiality Agreement defines "Confidential Information" as

> "any information of any kind, nature, or description concerning any matters affecting or relating to Employee's services for or knowledge about, the business, or operations of Krauter & Company, its clients and prospects, and/or the products, plans, processes, intellectual property (*including nonpublic contact information obtained during the Employees [sic] term of employment at Krauter & Company*) or other data of Krauter & Company" (Confidentiality Agreement, at 1 [emphasis added]).

Counterclaimants assert that confidential information is limited to "nonpublic contact information obtained during the Employees [sic] term of employment at Krauter & Company" and that the amended complaint fails to adequately allege that Ross appropriated such information Supporting Memorandum, p. 9, ¶3). However, counterclaimants impermissibly seek inferences to be drawn in their favor as the movant by such assertion (*see AG Capital Funding Partners, L.P. v State St. Bank & Trust Co., supra* at 591; *Leon v Martinez*, 84 NY2d 83, 87 [1994] [every possible favorable inference is to be drawn in favor of non-movant]).

Drawing all inferences in favor of the non-movant militates against dismissal. For example, the amended complaint alleges that Ross breached the Confidentiality Agreement by the "soliciting and servicing of Krauter's clients." The amended complaint alleges, among other things, that Ross's coercive efforts caused multiple Krauter clients to transfer their insurance and risk policies from Krauter to Alwex. There is no basis to infer from the amended complaint that Ross effectuated this by using public information.

The elements of a breach of contract claim are "the existence of a contract, the plaintiff's performance thereunder, the defendant's breach thereof, and resulting damages" (*Harris v Seward Park Hous. Corp.*, 79 AD3d 425, 426 [1st Dept 2010]). The amended complaint adequately alleges all essential elements of a cause of action to recover damages for breach of contract.

Third Cause of Action **(Misappropriation of Confidential Information and Trade Secrets)**

The third cause of action alleges misappropriation of confidential information and trade secrets against Ross and Alwex.

To prevail on such claim, a plaintiff must demonstrate: "(1) that it possessed a trade secret, and (2) that the defendants used that trade secret in breach of an agreement, confidential relationship or duty, or as a result of discovery by improper means" (*Schroeder v Pinterest Inc.*, 133 AD3d 12, 27 [1st Dept 2015] [internal quotation marks and citation omitted]). A trade secret is "any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it" (*Ashland Mgt. v Janien*, 82 NY2d 395, 407 [1993], quoting Restatement of Torts § 757, comment b).

The movants allege that Ross was the head of Krauter's Private Client Services Division, and gained knowledge and had access to Krauter's confidential information and trade secrets including: (1) information concerning Krauter's Private Client Services operations; (2) Krauter's business strategies (i.e. rates and fees); and (3) detailed information about Krauter's clients, including personal addresses and contact information, social security numbers, banking and investment information, policy expiration dates, renewals, terms and conditions, information regarding the markets or sources with which insurance is placed, the amounts paid by such clients to Krauter, and leads and referrals to prospective Private Client Services clients (amended complaint, ¶15). Further, movants allege, *inter alia*, that Ross "has used and disseminated Krauter's confidential information and trade secrets, for the purpose of contacting, soliciting and/or servicing Krauter's clients" (*id.*, ¶40).

When read in the light most favorable to movants, the amended complaint sets forth a claim for misappropriation of trade secrets as against Ross (*see Ashland Mgt. v Janien*, *supra* at 407).

However, movants have failed to state a valid claim for misappropriation of trade secrets as against Alwex since the amended complaint is devoid of any allegation of an agreement and/or confidential relationship between Krauter and Alwex (*see Schroeder v Pinterest, Inc. supra* at 28). Therefore, the third cause of action is dismissed as against Alwex.

A motion to dismiss pursuant to CPLR 3211(a)(1) may be granted only where "the documentary evidence utterly refutes plaintiff's factual allegations, conclusively establishing a defense as a matter of law" (*Goshen v Mutual Life Ins. Co. of N.Y.*, 98 NY2d 314, 326 [2002]). However, the documentary evidence does not conclusively dispose of this claim as against Ross.

Fourth Cause of Action **(Tortious Interference)**

The fourth cause of action is against Alwex for tortious interference with contractual and business relations. The amended complaint alleges that Alwex procured Krauter's confidential and proprietary information and induced Ross to solicit and service Krauter's clients, thereby causing breaches of the non-solicitation and confidentiality agreements that Krauter entered into with Ross and caused the breaches of the contractual and common law duties owed to Krauter by Ross and has otherwise interfered with Krauter's business relationships *(id.*, ¶72).

A claim for tortious interference with contract requires "the existence of a valid contract between the plaintiff and a third party, defendant's knowledge of that contract, defendant's intentional procurement of the third-party's breach of the contract without justification, actual breach of the contract, and damages resulting therefrom" (*Lama Holding Co. v Smith Barney*, 88 NY2d 413, 424 [1996]).

"[W]here there is an existing, enforceable contract and a defendant's deliberate interference results in a breach of that contract, a plaintiff may recover damages for tortious interference with contractual relations even if the defendant was engaged in lawful behavior" (*NBT Bancorp v*

Fleet/Norstar Fin. Group, 87 NY2d 614, 621 [1996]). This Court has previously determined that the amended complaint sets forth causes of action for breach of contract between Ross and Krauter and the allegations herein sets forth Alwex's tortious interference with the contractual relationship between Ross and Krauter.

However, the amended complaint fails to sufficiently allege tortious interference with business relations. "[W]here a suit is based on interference with a nonbinding relationship. . . [c]onduct that is not criminal or tortious will generally be 'lawful' and thus insufficiently 'culpable' to create liability for interference with prospective contracts or other nonbinding economic relations" (*Carvel Corp. v Noonan*, 3 NY3d 182, 190 [2004] [internal quotation marks and citation omitted]).

The amended complaint does not allege that Alwex was motivated by anything other than its economic self-interest when it welcomed Ross and the clients he brought with him from Krauter. Here, the amended complaint "fails to allege the requisite malice—that [Alwex] acted solely to harm [Krauter], or that the conduct constituted a crime or independent tort or was otherwise egregious," which is required for a claim for tortious interference with business relations (*Phoenix Capital Invs. LLC v Ellington Mgt. Group, L.L.C.*, 51 AD3d 549, 551 [1st Dept 2008]). Accordingly, the fourth cause of action as asserted against Alwex for tortious interference with business relations is dismissed.

Fifth Cause of Action **(Unfair Competition)**

The fifth cause of action is against Ross and Alwex for unfair competition. The movants allege that Ross and Alwex "knowingly and maliciously competed unfairly with Krauter, including their conduct in stealing, using, disclosing and/or misappropriating Krauter's confidential information and trade secrets" (amended complaint, ¶2).

Where, as here, the claim is based on allegations of misappropriation of confidential information, "[movants] must show that the [counterclaimants] solicited the [movants'] customers where the customer list was a trade secret, or where the [counterclaimants] engaged in wrongful conduct, such as physically taking or copying files or using confidential information" (*Baldeo v Majeed*, 150 AD3d 942, 944 [2d Dept 2017] [internal quotation marks and citations omitted]).

"Under New York law, [a]n unfair competition claim involving misappropriation usually concerns the taking and use of the plaintiff's property to compete against the plaintiff's own use of the same property. "The term 'commercial advantage' has been used interchangeably with 'property' within the meaning of the misappropriation theory" (*ITC Ltd. v Punchgini, Inc.*, 9 NY3d 467, 478 [2007] [internal quotation marks and citations omitted]).

To sustain this claim, movants must establish that they took sufficient precautionary measures to ensure that the information remained secret (*Edelman v Starwood Capital Group, LLC*, 70 AD3d 246, 249 [1st Dept 2009] ["The claim for misappropriation of proprietary information falls short because plaintiffs did not allege that Edelman took sufficient precautionary measures to ensure that the information remained secret, particularly after they abandoned the acquisition plan."]).

The amended complaint alleges that "Krauter goes to great lengths to protect its confidential information and trade secrets, such as promulgating and disseminating policies to its employees that prohibit the use or disclosure of Krauter's confidential information and trade secrets for non-business purposes, requiring employees who have access to such confidential information and trade secrets to sign agreements that restrict their use or disclosure or Krauter's confidential information and trade secrets and restrict certain post-employment activities . . ." (*id.*, ¶17). These

allegations establish that movants implemented sufficient precautionary measures to ensure that the information remained secret (*Edelman v Starwood Capital Group, LLC*, *supra* at 249).

However, movants must further "set forth the requisite showing of bad-faith misappropriation of a commercial advantage" (*Ahead Realty LLC v India House, Inc.*, 92 AD3d 424, 425 [1st Dept 2012]). Counterclaimants argue that movants fail to allege sufficient facts to establish bad faith, which necessitates dismissal. This argument must fail because this cause of action is based upon the counterclaimants' improper use of confidential information and trade secrets, which sets forth a valid claim for misappropriation of confidential information *(see Bender Ins. Agency v Treiber Ins. Agency*, 283 AD2d 448, 450-451 [2d Dept 2001]; *CBS Corp. v Dumsday*, 268 AD2d 350, 353 [1st Dept 2000]). Accordingly, movants have set forth a valid claim for unfair competition.

Request for Injunctive Relief

Each cause of action in the amended complaint seeks monetary damages, as well as injunctive relief. With respect to the request for injunctive relief, movants maintain that they are entitled to an injunction to prevent movants from: (1) "irreparably harming and unlawfully competing with Krauter to its severe detriment;" (2) "misappropriating Krauter's confidential information and trade secrets;" and (3) "interfering with Krauter's contractual and business relationships, including those with Ross." (amended complaint, ¶¶ 43, 68, 80).

"A permanent injunction is a drastic remedy which may be granted only where the [movants] demonstrates that [they] will suffer irreparable harm absent the injunction" (*Parry v Murphy*, 79 AD 3d 713, 715 [2d Dept 2010] [internal quotation marks and citations omitted). "Irreparable injury, for purposes of equity, has been held to mean any injury for which money damages

are insufficient" (*Peyton v PWV Acquisition LLC,* 39 Misc 3d 1228[A], *3 [Sup Ct, NY County May 20, 2013, Singh, J.]).

"Case law reflects that, in general, an injury is considered irreparable if the harm in question cannot be undone. Such an interpretation in consistent with the definition of the word 'irreparable,' which means 'impossible to repair, rectify or amend.'" (*id.*, at *3, quoting American Heritage Dictionary of the English Language 954 [3d ed 1992]). While counterclaimants allege money damages in excess of $200,000 in each cause of action, "[e]conomic loss, which is compensable by money damages, does not constitute irreparable harm" (*EdCia Corp. v McCormack*, 44 AD3d 991, 994 [2d Dept 2007]). Therefore, the claim for injunctive relief under each cause of action is dismissed.

Motion to Dismiss Counterclaims

***First Counterclaim* (Electronic Communications Privacy Act)**

The first counterclaim alleges a violation of 18 U.S.C. §§ 2501, 2520 and 2701 (the Electronic Communications Privacy Act [ECPA]). Counterclaimants allege that movants violated the ECPA by improperly using Krauter's computer equipment, software and network to access and disclose Ross's personal contacts, non-business contacts, and other personal and non-business data contained in Ross's Outlook database (Ross Data) to distribute the Criminal Notice, a non-business purpose, in violation of the movants' own standards of practice and procedure as set forth in the Krauter Employee Handbook. The counterclaimants also allege that the computer and network hardware movants used to improperly access the Ross Data were an "electronic device" within the meaning of 18 U.S.C. § 2510(5), which was used to "intercept" the Ross Data within the meaning of 18 U.S.C. § 2511, in violation of this chapter of the ECPA.

18 U.S.C. §2707 provides for a civil cause of action for violation of the ECPA (*see Lopez v First Union Nat. Bank of Florida*, 129 F3d 1186, 1189 [11th Cir 1997]). Counterclaimants must establish that the movants "intentionally intercept[ed], endeavore[d] to intercept, or procure[d] any other person to intercept or endeavor to intercept, any wire, oral, or electronic communication" (18 U.S.C. §2511[1][a]).

Movants argue that the first counterclaim should be dismissed because the Ross Data does not constitute an "electronic communication" within the meaning of 18 U.S.C. § 2511(1) and because the counterclaimants failed to sufficiently plead any interception of an "electronic communication." Movants also argue that a wrongful interception requires "acquisition contemporaneous with transmission" of a communication (*Konop v Hawaiian Airlines, Inc.* (302 F3d 868, 878 [9th Cir. 2002]). Further, movants maintain that the first counterclaim should be dismissed because counterclaimants fail to set forth any facts to support their allegations.

An "electronic communication" is defined under 18 U.S.C. § 2510(12) as "any transfer of signs, signals, writings, images, sounds, data, or intelligence of any nature transmitted in whole or in part by a wire, radio, electromagnetic, photoelectronic or photooptical system that affects interstate or foreign commerce." Further, 18 U.S.C. 2510(4) defines "intercept" as "the aural or other acquisition of the contents of any wire, electronic, or oral communication through the use of any electronic, mechanical or other device." Here, counterclaimants adequately set forth a valid claim for violation of the ECPA.

Krauter and Block allegedly collected and utilized the Ross Data a second time to distribute the Criminal Notice. While the movants concede that Krauter first acquired the Ross Data when Ross transmitted such data to Krauter's information system to use same for business purposes, this Court may draw the reasonable inference that movants contemporaneously acquired the Ross Data

following the termination of his employment and transmitted such data without Ross's consent for a non-business purpose (*see generally MatlinPatterson ATA Holdings LLC v Federal Express Corp.*, 87 AD3d 836, 839 [1st Dept 2011] [on a CPLR 3211(a)(7) motion to dismiss, "the court must accept all of the allegations in the complaint as true, and, drawing all inferences from those allegations in the light most favorable to the plaintiff, determine whether a cognizable cause of action can be discerned therein, not whether one has been properly stated"]).

With respect to that branch of the motion to dismiss pursuant to CPLR 3211(a)(1), movants have failed to present any "documentary evidence and undisputed facts [which] negate or dispose of claims" set forth in the first counterclaim or "conclusively establish a defense" (*Zanett Lombardier, Ltd. v Maslow*, 29 AD3d 495, 495 [1st Dept 2006]). As counterclaimants correctly argue, movants may argue at a later juncture that the evidence is insufficient to support the first counterclaim once the parties engage in discovery. Therefore, the first counterclaim sets forth a valid cause of action for violation of the ECPA.

Second Counterclaim **(Stored Communications Act)**

The second counterclaim alleges a violation of 18 U.S.C. § 2701 (the Stored Communications Act [SCA]). Counterclaimants allege that movants wrongfully accessed and obtained Ross Data without authorization and/or in a manner exceeding authorization to access, use, review, and disclose the Ross Data for non-business purposes, to wit: dissemination of the Criminal Notice. 18 U.S.C. §2707(a) provides a civil cause of action for violation of the SCA (*see Council on American-Islamic Relations Action Network, Inc. v Gaubatz*, 31 F Supp 3d 237, 270 [D.D.C. 2014]).

To set forth a cause of action under the SCA, counterclaimants must allege that a person "(1) intentionally accesses without authorization a facility through which an electronic communication service is provided; or (2) intentionally exceeds an authorization to access that facility; and

thereby obtains, alters, or prevents authorized access to a wire or electronic communication while it is in electronic storage in such system . . ." (18 U.S.C.§ 2701[a]).

Movants argue that counterclaimants fail to sufficiently plead intentional access without authorization. In support of such argument, movants cite *Shefts v Petrakis* (758 F Supp 2d 620, 635 [C.D. Ill. 2010]) wherein the court held that an employer's access to employee work emails were authorized because the employee manual stated that emails received on company equipment were subject to monitoring, and that the employee had no reasonable expectation of privacy in those work emails *(see Williams v Rosenblatt Sec. Inc.*, 136 F Supp 3d 593, 607 [S.D.N.Y. 2015]).

Movants contend that the Krauter Employee Handbook explicitly informed employees of Krauter's authority to access the computer system and any files on the computer at any time. However, this argument is not persuasive since counterclaimants allege that the Ross Data was utilized to distribute the Criminal Notice after Ross ended his employment with the Krauter firm (*see generally Van Alstyne v Electronic Scriptorium, Ltd.*, 560 F3d 199 [4th Cir 2009]).

Similarly, unpersuasive is movants' argument that counterclaimants fail to plead access to a facility, an essential element of the claim under the SCA. Although movants argue that Krauter's computer system is a personal computing device and not a facility, courts have concluded that an employer's computer system is a "facility" within the meaning of the SCA (*see Lazette v Kulmatycki*, 949 F Supp 2d 748, 755 [N.D. Ohio 2013]).

Movants also argue that counterclaimants fail to plead any wire or electronic communication while in storage was obtained, altered, or that counterclaimants were prevented authorized access to any communication. However, contrary to movants' contention, "electronic communication" is defined under 18 U.S.C. § 2510(12) as "any transfer of signs, signals, writings, images,

sounds, data, or intelligence of any nature transmitted in whole or in part by a wire, radio, electromagnetic, photoelectronic or photooptical system that affects interstate or foreign commerce."

"Electronic storage" is defined as "any temporary, intermediate storage of a wire or electronic communication incidental to the electronic transmission thereof" (18 U.S.C.§ 2510(17)]. The allegations that Ross uploaded the Ross Data to the Krauter firm's computer system and updated them sufficiently establish that they were "electronic communication[s]" in "electronic storage" under the SCA. As such, the second counterclaim sets forth a valid cause of action for violation of the SCA.

Third Counterclaim **(Computer Fraud and Abuse Act)**

The third counterclaim alleges a violation of 18 U.S.C. § 1030 *et seq*. (the Computer Fraud and Abuse Act) (CFAA). Counterclaimants allege that movants violated the CFAA by improperly, knowingly and intentionally causing the transmission of commands and instructions to and on said protected computers, computer networks, and mobile devices to access, collect, transmit, use, and disclose Ross Data without authorization or in a manner that exceeded authorization by Ross and authorization to access, collect, disclose, and transmit said data pursuant to the Employee Handbook. Counterclaimants further allege that the wrongful conduct occurred in August 2015; that Ross first learned of such conduct on or about August 24, 2015; and that Ross sustained, *inter alia*, at least $5,000 in economic damages during the one-year period following movants' actions.

To state a claim under the CFAA, counterclaimants must allege that movants: (1) "knowingly and with intent to defraud"; (2) "accessed a protected computer"; (3) "without authorization or exceeded their authorized access"; (4) "and by means of such conduct furthered the intended fraud and obtained anything of value"; and (5) "caused loss to 1 or more persons during any 1-year period . . . aggregating at least $5,000 in value" (*Associated Mtge. Bankers, Inc. v Calcon*

Mut. Mtge. LLC, 159 F Supp 3d 324, 333 [E.D.N.Y. 2016] [internal quotation marks and citations omitted].

"The CFAA defines a loss as any reasonable cost to any victim, including the cost of responding to an offense, conducting a damages assessment, and restoring the data, program, system, or information to its [prior] condition and any revenue lost, cost incurred, or other consequential damages incurred" (*Obeid v La Mack*, 2018 WL 2059653, *30 [S.D.N.Y., May 1, 2018, Swain, J.] [internal quotation marks and citations omitted]).

This counterclaim is not validly stated because "[a]ny recoverable damage or loss under the CFAA must be directly caused by computer impairment or damage" (*id.*). No such claim is present here. Therefore, the third counterclaim is dismissed.

Fourth, Fifth, Sixth, and Seventh Counterclaims **(New York Penal Law)**

The fourth, fifth, sixth, and seventh counterclaims allege violations of New York Penal Law § 156.05 (Unauthorized Computer Use); New York Penal Law § 156.10 (Computer Trespass); New York Penal Law § 156.30 (Unlawful Duplication of Computer Related Material in the First Degree); and New York Penal Law § 156.35 (Criminal Possession of Computer Related Material), respectively.

These four counterclaims claims are dismissed as there is no private right of action under New York Penal Law §156 (*see Casey Sys., Inc. v Firecom, Inc.*, 1995 WL 704964, *3, [S.D.N.Y., Nov 29, 1995, Duffy, J.]).

Eighth Counterclaim **(Tortious Interference with Business Relations)**

Counterclaimants allege that movants maliciously disseminated the Criminal Notice to Ross's entire Outlook contacts database, which included contacts for clients that Ross brought to Krauter and/or developed, or was working to develop while at Krauter, with the intention to, and

did, interfere with and prevent the performance of future agreements/contracts/business relationships between counterclaimants and existing and potential new clients, resulting in cancellations.

The "tort of interference with business relations applies to those situations where the third party would have entered into or extended a contractual relationship with plaintiff but for the intentional and wrongful acts of the defendant" (*WFB Telecom. v NYNEX Corp.*, 188 AD2d 257, 257 [1st Dept 1992]). Here, counterclaimants have failed to allege any "specific prospective relationship with which [movants] interfered," which necessitates dismissal of the eighth counterclaim (*Bus. Networks of New York v Complete Network Solutions*, 265 AD2d 194, 195 [1st Dept 1999]).

Ninth Counterclaim (Defamation)

Counterclaimants allege that statements set forth in the Criminal Notice and in certain emails wrongfully defamed Ross. According to counterclaimants, movants allegedly stated in the Criminal Notice that Ross had "wrongfully taken over three thousand files from our secure server" that "may contain your personal information, including but not limited to, social security numbers, dates of birth;" that this information had been "misappropriated" by Ross;" and that, as a result of such actions, "the NYPD (New York Police Department) (is) taking every step possible to ensure that all legal measures are taken" (amended answer, ¶112).

Counterclaimants further allege that Neil Krauter sent emails to Wexelman using the phrase "for this theft by [Ross]," "and use of stolen confidential data . . . we hereby demand that your firms' use of our data cease immediately and that it be returned asap" (id., ¶114).

Under New York law, defamation is the injury to a person's reputation, either by written or oral expression (*see Morrison v National Broadcasting Co.*, 19 NY 2d 453 [1967]). The elements of a defamation claim are (1) a false statement; (2) published without privilege or authorization to a third party; (3) constituting fault as judged by, at a minimum, a negligence standard, and (4)

either causing special harm or constituting defamation per se (*Dillon v City of New York*, 261 AD2d 34, 38 [1st Dept 1999], citing Restatement of Torts [Second] §558). "Making a false statement that tends to expose a person to public contempt, hatred, ridicule, aversion or disgrace constitutes defamation" (*Thomas H. v Paul B.*, 18 NY3d 580, 584 [2012]). Further, "[a] statement is defamatory on its face when it suggests improper performance of one's professional duties or unprofessional conduct" (*Frechtman v Gutterman*, 115 AD3d 102, 104 [1st Dept 2014] [internal citations and quotation marks omitted]).

Movants argue that CPLR 3016 (a) requires that in a defamation action, "the particular words complained of … be set forth in the complaint." The amended answer satisfies this requirement by alleging the following:

- "[I]n the late evening of August 17th Neil Krauter emailed Harvey Wexelman ('Wexelman'), President of Alwex, accusing Ross of stealing confidential data and threatening to add Alwex to a lawsuit unless it responded by the morning."
- "The next morning Neil Krauter emailed Ross and Wexelman again demanding a response by 11 am combined this time with a threat to report the matter to the appropriate authorities including the police."
- "Hours later Neil Krauter emailed Wexelman and Ross again 'Nick, please expect a visit from the NYPD at home and office this week."
- "On Monday, August 24th at approximately 10:33am, counterclaim defendant Block, at the direction of and with the authority of plaintiff and counterclaim defendant Neil Krauter emailed out a notice addressed to 'Affected Clients, Markets, and Friends of the Firm' wherein it accused Ross of criminal acts, including misappropriating sensitive client information such as social security numbers and violating the Confidentiality Agreement ('the Criminal Notice'). The Criminal Notice mentioned that Krauter had reported Ross to the New York City Police Department and that an investigator may be in touch with the recipient."
- "The Criminal Notice was sent not only to Ross's clients, but also to his referral sources and professional relationships such as CPA's and attorneys and also sent to nearly all, if not all, of his personal and social contacts including but not limited to: family, friends, parents at his children's school, school teachers and administrators, and former employers inside and outside the insurance industry"

(amended answer, ¶¶ 56-58).

The allegation that Ross had "wrongfully taken over three thousand files from our secure server" that "may contain your personal information, including but not limited to, social security numbers, dates of birth;" that this information had been "misappropriated" by Ross; and that, as a result, the NYPD is "taking every step possible to ensure that all legal measures are taken" implies that a crime was committed and may be defamatory (*LeBlanc v Skinner*, 103 AD3d 202, 214 [2d Dept 2012] ["false published allegation that a person committed a serious crime is also a ground for asserting a cause of action to recover damages for defamation per se"]).

Movants also argue that the statements at issue constitute the affirmative defense of truth because Ross admitted to taking client information from Krauter's computer system and failed to return Krauter's property as outlined in the Employee Handbook. Inasmuch as the falsity of the statement is an element of a defamation claim, the statement's truth or substantial truth is an absolute defense (*Stepanov v Dow Jones & Co., Inc.*, 120 AD3d 28, 34 [1st Dept 2014]). Here, however, the defense of truth raises an issue of fact.

Counterclaimants persuasively argue that while Ross may have "admitted to taking client information," which belonged to him, and he was entitled to retain, does not render Krauter's accusations that he "stole" or "misappropriated" that information true since Ross has not made any admissions. Rather, Ross alleges that he properly transferred data from Krauter's computer system to his Krauter-issued Tablet for working out of the office during his employment at Krauter, which was consistent with Krauter's policies and procedures.

Movants further argue that the emails between Neil Krauter and Wexelman were private and not published to a third-party, which is a necessary element of a defamation claim. However, as counterclaimants correctly contend, the fact that Krauter's statements were read by someone other than Ross sufficiently meets the requirement of publication to a third-party (*see Ostrowe v*

Lee, 256 NY 36, 38 [1931]; *Hirschfeld v Institutional Inv.*, 208 AD2d 380, 381 [1st Dept 1994]). Counterclaimants persuasively contend that Ross was the subject of the statements set forth in the emails and that Wexelman is a third party with respect to Krauter and Ross. Accordingly, the ninth counterclaim sets forth a valid cause of action for defamation.

Tenth Counterclaim (Libel)

The elements of a libel cause of action are: (1) a false and defamatory statement of fact; (2) regarding the plaintiff; (3) which is published to a third party; and which (4) results in injury to the plaintiff (*see Idema v Wager*, 120 F Supp 2d 361, 365 [S.D.N.Y. 2000]; *Penn Warranty Corp. v DiGiovanni*, 10 Misc3d 998, 1002 [Sup Ct, NY County 2005]). The statements set forth in the Criminal Notice and emails, as alleged herein, appear to be libelous per se, in that they accuse Ross of wrongful and/or criminal conduct. "The general rule is that words tending to disparage a person in his or her office, profession or trade are libelous per se" (*Bowes v Magna Concepts*, 166 AD2d 347, 348 [1st Dept 1990]).

This Court has already rejected movants' arguments in the preceding section of this opinion that the affirmative defense of truth defeats such a claim and that the challenged statements in the emails were not published to a third-party. Therefore, the tenth counterclaim sets forth a valid cause of action for libel.

Eleventh Counterclaim (Conversion)

Counterclaimants allege that movants intentionally interfered with the Ross Data stored in his Outlook database, exercising dominion and control over it by collecting Ross Data; accessing it without authorization or exceeding authorization; and using it to send the Criminal Notice to all contacts in the Ross Data, including nonbusiness and personal contacts; and failing and refusing

to return it to Ross. Further, counterclaimants allege that such conduct deprived counterclaimants of possession or use of Ross's personal property in question, in that Ross has been unable to access or retrieve Ross Data from movants' servers or computer networks, and thereby unable to use same in his employment with Alwex, causing counterclaimants economic damages through the loss of commissions and other remuneration from contacts in said data.

Movants argue that Ross does not have a possessory right or interest over data maintained at Krauter because he received the Krauter Employee Handbook detailing Krauter's ownership and authorization to access to data maintained on the Krauter's computer system.

A cause of action for conversion is the "unauthorized assumption and exercise of the right and ownership over goods belonging to another to the exclusion of the owner's rights" (*State of New York v Seventh Regiment Fund,* 98 NY 2d 249, 259 [2002] [internal quotation marks and citations omitted]).

"Two key elements of conversion are (1) plaintiff's possessory right or interest in the property and (2) defendant's dominion over the property or interference with it, in derogation of plaintiff's rights" (*Colavito v New York Organ Donor Network, Inc.*, 8 NY3d 43, 50 [2006]). Moreover, under New York law, intangible property, such as electronic records stored on a computer, are subject to a claim of conversion (*see Thyroff v Nationwide Mut. Ins. Co.*, 8 NY3d 283, 292-293 [2007]).

Here, counterclaimants sufficiently pled all of the required elements of a claim for conversion. Moreover, contrary to movants' contention, the documentary evidence (Employee Handbook) does not effectively dispose of this counterclaim since factual issues exists regarding Ross's possessory rights and movants' unauthorized access and use of the Ross Data, as well as the usurpation of Ross's ownership rights.

Accordingly, it is

ORDERED that the motion to dismiss the counterclaims is granted to the extent of dismissing the third through eighth counterclaims; and it is further

ORDERED that the cross-motion to dismiss the amended complaint is granted to the extent of dismissing the third cause of action as asserted against Alwex; the fourth cause of action as asserted against Alwex for tortious interference with business relations; and the claim for injunctive relief as asserted in all causes of action; and it is further

ORDERED that the parties are directed to appear for a status conference on February 27, 2019 at 2:15 p.m.

This constitutes the Decision and Order of the Court.

Dated: January 4, 2019

ENTER:

Hon. Tanya R. Kennedy
J.S.C.

TANYA R. KENNEDY
J.S.C.