Buechel v Sovereignty, LLC
2019 NY Slip Op 31372(U)
May 16, 2019
Supreme Court, Tompkins County
Docket Number: 2016-0664
Judge: Eugene D. Faughnan
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[* 1]

At a Trial Term of the Supreme Court of the State of New York held in and for the Sixth Judicial District at the Tompkins County Courthouse, Ithaca, New York, on the 4th- 5th days of February, 2019.

PRESENT: HON. EUGENE D. FAUGHNAN
Justice Presiding

STATE OF NEW YORK
SUPREME COURT : TOMPKINS COUNTY

RICHARD E. BUECHEL and SHARON D. BUECHEL,

Plaintiffs,

-vs-

SOVEREIGNTY, LLC and ZACHARY M. SHULMAN,

Defendants.

SOVEREIGNTY, LLC and ZACHARY M. SHULMAN,

Counterclaim Plaintiffs,

-vs-

RICHARD E. BUECHEL and SHARON D. BUECHEL,

Counterclaim Defendants.

SOVEREIGNTY, LLC and ZACHARY M. SHULMAN

Third Party Plaintiffs

-vs-

IP CUSTOM PLASTICS, INC.,

Third Party Defendants.

DECISION AND ORDER

Index No. 2016-0664
RJI No. 2016-0617-M

[* 2]

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EUGENE D. FAUGHNAN, J.S.C.

This matter comes before the Court following a non-jury trial commenced on February 4, 2019 and completed on February 5, 2019. The Plaintiffs and Defendants have submitted post trial submissions and the Court has considered all submissions, trial testimony and documentary evidence.

This matter arises out of the sale of a business, IP Custom Plastics, Inc. ("IP") to Zachary Shulman ("Shulman") and Sovereignty, LLC ("Sovereignty"), Schulman's business entity. IP was wholly owned by Richard E Buechel and Sharon Buechel (collectively "Buechels" or "Plaintiffs"). The parties entered into an agreement for the sale of assets on January 5, 2016 and the deal was closed on March 1, 2016.

The relevant terms of the January 5, 2016 purchase agreement are relatively straight forward and in evidence. Shulman agreed to purchase the assets of IP (but not the building)[1]. Shulman's

[1]The building was retained by Plaintiffs and the space leased to Shulman and Sovereignty.

financing included a mortgage on his home for $226,000, the proceeds of which were paid to the Buechels at closing and three promissory notes were given to the Buechels by Shulman and Sovereignty of $120,000, $80,000 and $56,600. The $120,000 note was payable at 4% interest in monthly payments of $1,214.94 for a term of 10 years with payments to commence on April 1, 2016. The $80,000 note was payable at 4% interest in monthly payments of $809.96 for a term of 10 years with payments to commence on April 1, 2016. The $56,000 note was payable at $2,830 per month from July 1, 2016 to February 1, 2018 at which time the entire principal balance was due.

The Defendants defaulted on the installment payments that came due July 1, 2016. Buechels accelerated the maturity of the notes. They then commenced this action by the filing of a verified complaint on October 12, 2016. The issue was joined by the filing and service of a verified answer with counterclaims and third party claims against IP on November 2, 2016. Sovereignty ceased doing business in December of 2016.

The Plaintiffs' first three causes of action are for payment of the three notes at 4% interest. The fourth cause of action is for a breach of a training agreement wherein Richard Buechel agreed to provide instruction and training at $30.00 per hour and claims $300.00 in unpaid fees. The Fifth Cause of action was effectively mooted by the eviction of Defendants from the subject property and subsequent sale.[2]

Defendants' counterclaims and third party claims sound in fraud, negligent misrepresentation, breach of warranty and indemnification. Defendants seek rescission of the purchase agreement and monetary damages.

The parties do not dispute the authenticity of the notes signed by Shulman. Rather, Defendants argue that they are not payable due to fraud and misrepresentation. The Court will first address

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[2]Issues regarding the eviction of the Defendants and rents allegedly owed under the lease were sued in Ithaca City Court.

[* 4]

the issues raised in Defendants' Counterclaims and third party claims as their resolution is dispositive of all issues in this matter.

"The elements of a fraud cause of action consist of 'a misrepresentation or a material omission of fact which was false and known to be false by [the] defendant, made for the purpose of inducing the other party to rely upon it, justifiable reliance of the other party on the misrepresentation or material omission, and injury.'" *Pasternack v. Laboratory Corp. of Am. Holdings*, 27 NY3d 817, 827 (2016) (citation omitted). However, "if the facts represented are not matters peculiarly within the [party's] knowledge, and the [other party] has the means available to [him] of knowing, by the exercise of ordinary intelligence, the truth or the real quality of the subject of the representation, [he] must make use of those means, or [he] will not be heard to complain that [he] was induced to enter into the transaction by misrepresentations" *ACA Fin. Guar. Corp. v. Goldman*, Sachs & Co., 25 NY3d 1043, 1044 (2015) *quoting Schumaker v. Mather*, 133 NY 590, 596 (1892). Moreover, "when the party to whom a misrepresentation is made has hints of its falsity, a heightened degree of diligence is required of it. It cannot reasonably rely on such representations without making additional inquiry to determine their accuracy." *Centro Empresarial Cempresa S.A. v. América Móvil, S.A.B. de C.V.*, 17 NY3d 269, 279 (2011), *quoting Global Mins. & Metals Corp. v. Holme*, 35 AD3d 93, 100 (1st Dept. 2006), *lv denied* 8 NY3d 804 (2007).

In the present matter, the Court notes that pursuant to the asset purchase agreement, the parties agreed that the Buechels would make available various documents including tax returns, payable and receivable receipts and internal balance sheets related to statements of income. It is with regard to this last category that Defendants complain. Specifically, Defendants allege that Plaintiffs withheld statements pertaining to sales for 2015. They argue that in doing so, Plaintiffs concealed a 20% drop in gross revenue which, if known, would have caused Defendants to either renegotiate the agreement or withdraw the purchase offer.

Shulman testified that he requested the 2015 sales numbers on numerous occasions without

success. He also testified that David Moore ("Moore"), the real estate agent who was brokering the sale of the business, advised him that the sales in the business were down by 5% from 2014 to 2015. However, Moore testified that he never told Shulman that the business was down by 5%. Rather, Moore testified that Shulman only asked about a particular customer, Hi-Speed. In response, in late December of 2015, Moore advised him that Hi-Speed business was down from $349,000 in 2014 to $261,000 in 2015. This exchange was documented in text messages between Shulman and Moore (Exhibit 14). Moore further advised sales revenue had also declined from 2013 to 2014. Specifically, sales to Hi-Speed were $420,000 in 2013 representing a $71,000 decrease in 2014 over the prior year. In other words, Defendants were made aware of a decrease in sales to Hi-Speed of $159,000 from 2013 thru 2015. It is conceded by all parties that Hi-Speed was a major customer and a significant source of revenue for IP. In 2013, Hi-Speed accounted for approximately 67% of the gross sales of the business, and in 2014 approximately 66% of gross sales. Between 2014 and 2015, overall gross sales for IP fell by approximately $101,000, $88,000 of which was attributable to the decline in sales to Hi-Speed of which Shulman was advised. Moreover, there was a clear trend line of decreased sales to Hi-Speed which was readily apparent to Shulman.

Shulman asserts that the failure of Plaintiffs to provide the gross sales figures for the business represents fraud. He argues that he made numerous requests for the 2015 sales figures that went unfulfilled. Shulman's accountant, Richard Romer ("Romer") testified that in January of 2016, he visited the IP facility to review financial documentation as part of the due diligence prior to the closing. He was tasked with analyzing the finances of IP. This included reviewing tax information for 2010, 2011 and 2012 as well as tax returns for 2013 and 2014. He concluded that the company "seemed profitable" and a "reasonable company". He proceeded on the assumption that sales were down 5% from 2014 to 2015 based upon information provided by Shulman[3]. Romer noted that IP's sales between 2013 and 2014 were down by approximately $100,000 overall, so he wanted to review 2015 figures. He testified that he was unable to review

[3]Although several of Defendants' witnesses cite the 5% reduction figure, they all source the figure to Shulman.

2015 figures as he was told by Sharon Buechel that the figures were not available.

Upon cross- examination, Romer testified that following his review of IP's financials, he offered no opinion to Shulman as to whether he should close the deal. This is significant as Shulman testified that he relied on his accountant, among others, in deciding to close the deal notwithstanding the absence of 2015 sales figures. Romer did advise Shulman that he did not review the 2015 and conceded that in light of the decline in sales from 2013 to 2014, a review of 2015 sales figures would be of interest. It is unclear, although unlikely, that Shulman advised Romer of the approximately $90,000 decrease in sales to Hi-Speed in 2015.

Regarding the 2015 sales figures, Sharon Buechel testified that they were not available at, or before, Romer's financial review on January 21, 2016. She did not print a report of 2015 sales. However, she did testify that her QuickBooks program was open and made available to Romer. She was unsure whether he reviewed it. She also testified that she was unable to provide profit and loss reports from QuickBooks as payroll information was not maintained on that program.

Jeffrey Dobbin ("Dobbin"), is a vice president of lending at CFCU, an area credit union which provided Shulman with a home mortgage that funded the cash at the closing of the IP sale. Dobbin testified that he asked Shulman for IP financial records including 2015 sales information. Despite not receiving the 2015 sales figures, Shulman's home mortgage was approved based upon the value of his home and CFCU's assessment of Shulman's ability to repay the loan. Dobbins denied advising Shulman regarding the wisdom of purchasing IP.

Defendants argue that the failure to provide the 2015 gross sales figures represents a material omission of fact constituting fraud. They point to the contract for the sale of assets as evidence of the Plaintiffs' obligation to disclose the sales figures. However, even if the Court concluded that Sharon Buechel did not make the sales figures available to Romer, the failure to provide the sales figures would have been a basis for Defendants to refuse to close the sale. Defendants were represented by counsel and had the advice of an accountant. Defendants chose to proceed

notwithstanding their knowledge of the significant decrease in sales to IP's biggest customer between 2014 and 2015. This single customer decrease ultimately accounted for 89% of IP's gross sales reduction. Moreover, Defendants proceeded without insisting on the production of 2015 sales figures prior to closing.

Additionally, the Court finds that Defendants did not detrimentally rely on a representation of an overall 5% decrease in sales revenue. First, the Court does not find Shulman's testimony regarding Moore making this representation credible. It is specifically contradicted by Moore's testimony who is a disinterested witness. Moreover, it is significantly called into question in light of the documentary proof that Moore advised Shulman of the $90,000 reduction in sales to a company accounting for two-thirds of IP's gross sales.

For the reasons set forth herein, the Court finds that Defendants failed to establish, by clear and convincing evidence (*Simcuski v. Saeli*, 44 NY2d 442), that Plaintiffs fraudulently induced them purchase IP. Shulman, with the assistance of counsel and an accountant, knowingly proceeded to close despite not having 2015 gross sales figures. Defendants failed to exercise due diligence in the time leading to the closing. It might be suggested that Shulman accepted the risk of not knowing what the sales figures were for 2015. However, in reality, he was fully aware of the drop in sales to Hi-Speed which accounted for the vast majority of the 2015 shortfall. Therefore, based on the testimony and evidence, the Court finds that there was no fraud and rules in favor of Plaintiffs and against the Defendants with respect to the Defendants' counterclaim based on fraud. Accordingly, Defendants' First Counterclaim is dismissed.

Defendants also make a claim for negligent misrepresentation. "A claim for negligent misrepresentation requires the plaintiff to demonstrate (1) the existence of a special or privity-like relationship imposing a duty on the defendant to impart correct information to the plaintiff; (2) that the information was incorrect; and (3) reasonable reliance on the information." *J.A.O. Acquisition Corp. v. Stavitsky*, 8 NY3d 144, 148 (2007); *see Parrott v. Coopers & Lybrand*, 95 NY2d 479, 484 (2000); *Murphy v. Kuhn*, 90 NY2d 266, 270 (1997). "A cause of

action based upon negligent misrepresentation requires not only carelessness in imparting words upon which others rely to their damage, but also that such information be 'expressed directly, with knowledge or notice that it will be acted upon, to one whom the author is bound by some relation of duty, arising out of contract or otherwise, to act with care if he acts at all.'" *Chase Manhattan Bank v. Edwards*, 87 AD2d 935, 936 (3rd Dept. 1982), *aff'd* 59 NY2d 817 (1983), *quoting White v. Guarente*, 43 NY2d 356, 363 (1977).

In the present matter, the primary allegation of negligent misrepresentation is Moore advising Shulman that gross sales were down in 2015 by 5% from 2014. However, as noted above, the only person making that allegation is Shulman. Granted, Dobbins and Romer both repeat the allegation but they have no first hand knowledge of Moore's alleged representation. Moore specifically denies the allegation and points to his text message to Shulman in which he advised that 2015 sales to Hi-Speed were down by $90,000.

The Court finds the testimony of Moore to be more credible based upon the documentary evidence, and the fact that Shulman was well aware of the significance of Hi-Speed sales to the overall profitability of IP[4]. Therefore the Court concludes that the Defendants have failed to prove that any negligent misrepresentation was made by Plaintiffs or their agents. Based on the Court's resolution of the credibility issue in favor of Moore (a non-party), it necessarily follows that the Court finds that the information provided to the Defendants was not incorrect. Accordingly, the claim for negligent misrepresentation has not been proved. Therefore, Defendants' Second Counterclaim is dismissed.

For the same reasons as outlined above, the Defendants' Third Counterclaim for breach of warranty and Fourth Counterclaim for indemnification must fail. Both the Third and Fourth Counterclaims are premised on misconduct by Plaintiffs in the form of fraud or misrepresentations concerning the finances of IP, which allegations were not proven at trial. The

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[4]IP sales to Hi-Speed decreased nearly 50% between 2013 and 2015.

Court finds the Defendants have failed to prove that Plaintiffs made material misrepresentations or omissions. The Defendants did not receive the 2015 sales figures prior to closing, but failed in performing their due diligence by insisting on receipt prior to closing. Therefore, Defendants' Third and Fourth Counterclaims are dismissed.

Based upon all the foregoing, Defendants' claim for rescission is dismissed and the Defendants' claim for damages is denied.

With regard to the Plaintiffs' claims, no evidence has been submitted to question the validity of the notes signed by Shulman. Rather, Defendants have sought through defenses and counterclaims to negate their enforceability or to seek offset against their claims. Therefore, Plaintiffs are entitled to a finding in their favor with respect to the notes.

Based upon the Court's findings regarding Defendants' Counterclaims, the Court finds that Plaintiffs are entitled to a judgment on their First Cause of Action for 117,547.02 in principal with interest accruing at 4% since June 1, 2016. Plaintiffs are entitled to a judgment on their Second Cause of Action for $78,364.68 in principal with interest accruing at 4% since June 1, 2016. Plaintiffs are entitled to a judgment on their Third Cause of Action for $56,600 in principal. With regard to Plaintiffs' Fourth Cause of Action, seeking judgment for $300.00 presumably representing 10 hours of consulting work at $30.00 per hour, the Court finds in favor of the Defendants based upon a lack of evidence supporting that claim.

This constitutes the **DECISION AND ORDER** of the Court. The transmittal of copies of this Decision and Order by the Court shall not constitute notice of entry (see CPLR 5513).

Dated: May 16, 2019
Ithaca, New York

HON. EUGENE D. FAUGHNAN
Supreme Court Justice