

Barnett v Seth Berkowitz Serve U Brands Inc.

2019 NY Slip Op 32257(U)

July 29, 2019

Supreme Court, New York County

Docket Number: 654313/2018

Judge: Saliann Scarpulla

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART IAS MOTION 39EFM

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JARED BARNETT,

Plaintiff,

- v -

SETH BERKOWITZ SERVE U BRANDS INC., INSOMNIA
COOKIES, LLC, INSOMNIA COOKIES HOLDINGS,
LLC, JOHN DOE, JANE DOE, ABC, INC.

Defendant.

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INDEX NO. 654313/2018

MOTION DATE N/A

MOTION SEQ. NO. 002

**DECISION + ORDER ON
MOTION**

HON. SALIANN SCARPULLA:

The following e-filed documents, listed by NYSCEF document number (Motion 002) 35, 36, 37, 38, 41,
42, 43, 44, 45, 46, 47, 48, 49, 50, 52

were read on this motion to/for DISMISSAL.

Defendants Seth Berkowitz (“Berkowitz”), Serve U Brands, Inc. (“SUB”),
Insomnia Cookies, LLC (“Insomnia”) and Insomnia Cookies Holdings, LLC,
 (“Holdings”) (SUB, Insomnia and Holdings are collectively referred to as “Company
Defendants” and together with Berkowitz, “Defendants”), move to dismiss the Amended
Complaint of plaintiff Jared Barnett (“Barnett”) pursuant to CPLR 3211(a)(1), (5) and
(7).

Background

Barnett and Berkowitz co-founded Insomnia, a Pennsylvania LLC, to engage in
the business of baking and delivering cookies. By March 2006, Barnett and Berkowitz
owned 29.332% and 44.000% equity interests in Insomnia, respectively.

In 2006, differences arose between Barnett and Berkowitz, so they agreed that Barnett would sell his equity interest to Berkowitz. Barnett alleges that, on May 4, 2006, Berkowitz confirmed the terms of the sale in an attachment to an email (the “May 2006 email”), which included, among other things, that Barnett would receive “all economic benefits of a 5% member in Insomnia Cookies, LLC.”

On or about June 8, 2006, Barnett and Berkowitz signed a Buy-Out Agreement (the “Buy-Out Agreement”), pursuant to which: (a) Barnett resigned as manager of Insomnia; and (b) Berkowitz acquired Barnett’s equity interest in Insomnia in exchange for (i) payments to Barnett aggregating \$90,000, and (ii) Barnett retaining a seller benefit (the “Retained Seller Benefit”) of 6.8% non-voting interest in the proceeds received by Berkowitz as a result of any Insomnia “Liquidation Event.”¹

¹ The Buy-Out Agreement provides that a “Liquidation Event” shall be deemed to be the consummation and completion of any transaction or series of transactions which results in the majority transfer of the equity interests held by [Berkowitz] in [Insomnia] on the date hereof (after giving effect to the sale of the Equity Interest to [Berkowitz]) to a bona fide third party purchaser. A “Liquidation Event” shall also be deemed to include any dividends in cash or non-cash form (it being understood that any non-cash dividends shall be held by [Berkowitz] for the benefit of [Barnett] until such time as it is reasonably practicable to convey such interests to [Barnett]) which may be declared based on [Berkowitz’s] equity interests in [Insomnia]. A restructuring, financing, recapitalization or other structuring transaction which has the effect of diluting the interests of [Berkowitz] shall not be deemed a Liquidation Event. In addition, any sale, conveyance, lien, encumbrance or other transaction relating to [Berkowitz’s] equity interest in [Insomnia] for the purpose of satisfying [Berkowitz’s] obligations to [Barnett] under this Agreement shall not be deemed a Liquidation Event. Payment of any Retained Seller Benefit shall be in the same type of consideration received by [Berkowitz] in the Liquidation Event, or, in the case the consideration being rendered is intellectual property (exclusive of contractual rights), such consideration shall be reflected as a proportionate right to receive further proceeds deriving from ownership of such intellectual property. Retained Seller Benefit shall not include any

On or about September 17, 2018, Krispy Kreme acquired Holdings² (the “Krispy Kreme Transaction”), which Barnett alleges resulted in a Liquidation Event under the Buy-Out Agreement. Barnett alleges that Berkowitz received more than \$29 million in connection with the Krispy Kreme Transaction but Barnett did not receive any money pursuant to the Buy-Out Agreement.

In his Amended Complaint Barnett pleads nine causes of action for: (i) breach of contract; (ii) breach of the implied covenant of good faith and fair dealing; (iii) interference with contractual relations; (iv) contractual indemnification; (v) declaratory judgment; (vi) injunctive relief; (vii) breach of fiduciary duty; (viii) fraud and misrepresentation; and (ix) accounting. Defendants now move to dismiss the Amended Complaint, arguing that Barnett has failed to state and claims and that documentary evidence disproves his claims as a matter of law.

Discussion

Breach of Contract Against Berkowitz

Defendants assert that the first six causes of action in the Amended Complaint, which are based on Berkowitz’s alleged breach of a purported obligation to give 5% economic benefit to Barnett, must be dismissed based on documentary evidence because the explicit language in the Buy-Out Agreement flatly contradicts Barnett’s allegations.

rights to receive further consideration from a Liquidation Event or otherwise that is part of any rights of [Berkowitz] to receive salaries, bonuses, options, earn-outs, contingencies or milestones.”

² Holdings was organized for the purpose of holding 100% of membership interests of Insomnia.

Defendants also allege that Barnett, by relying on the May 2006 email, is attempting to circumvent the unambiguous terms of the Buy-Out Agreement.

Barnett counters that the operative and enforceable agreement between the parties includes both the Buy-Out Agreement and the May 2006 email and only by reference to the May 2006 email can the full agreement of the parties and their intentions be determined. Barnett further states that because both documents cover the same subject matter and were executed for the same purpose they must be interpreted together.

“The fundamental rule of contract interpretation is that agreements are construed in accord with the parties' intent, and ‘[t]he best evidence of what parties to a written agreement intend is what they say in their writing.’ Thus, a written agreement that is clear and unambiguous on its face must be enforced according to the plain terms, and extrinsic evidence of the parties' intent may be considered only if the agreement is ambiguous.” *Riverside South Planning Corp. v. CRP/Extell Riverside LP*, 60 AD3d 61, 66 (1st Dept 2008), *affd* 13 NY3d 398 (2009) (citations omitted). Here, the Buy-Out Agreement is a complete, unambiguous agreement, negotiated and executed by Barnett and Berkowitz. There is no ambiguity in the language of the Buy-Out Agreement, which clearly sets out the terms agreed upon by both Barnett and Berkowitz.

The issue then is whether Barnett has pleaded a cause of action for breach of the Buy-Out Agreement. Barnett alleges that, after execution of the Buy-Out Agreement, Berkowitz owned 73.332% of the equity interest in Insomnia, and Barnett owned a 6.8% non-voting interest in the proceeds received by Berkowitz as a result of any Insomnia

“Liquidation Event.” Barnett further alleges that a Liquidation Event occurred when Holdings acquired Insomnia, and Berkowitz has failed to pay Barnett for his interest in the proceeds of that Liquidation Event.³ At this pre-answer motion to dismiss stage, Barnett has sufficiently pled that there is an underlying contract (the Buy-Out Agreement), which entitles Barnett to 6.8% interest in Berkowitz’s equity interest and that Barnett was not paid any such benefit after a Liquidation Event (including the Krispy Kreme Transaction). Defendants’ documentary evidence does not conclusively establish a defense to the breach of contract cause of action as a matter of law and therefore I deny dismissal of Barnett’s breach of contract cause of action.

**Breach of the Implied Covenant of
Good Faith and Fair Dealing Against Berkowitz**

“[I]mplicit in every contract is a covenant of good faith and fair dealing, which encompasses any promises that a reasonable promisee would understand to be included,” *New York Univ. v Cont. Ins. Co.*, 87 NY2d 308, 318 (1995) (citations omitted), and which “is breached only where one party to a contract seeks to prevent its performance by, or to withhold its benefits from, the other.” *Collard v Inc. Vil. of Flower Hill*, 75 AD2d 631, 632 (2d Dept 1980), *affd*, 52 NY2d 594 (1981) (citations omitted). “Such a cause of action is not necessarily duplicative of a cause of action alleging a breach of contract.” *Gutierrez v. Gov't Employees Ins. Co.*, 136 AD3d 975, 976 (2d Dept 2016) (citation omitted).

³ Barnett explains that 6.8% of Berkowitz’s 73.332% equity interest would be the equivalent of a 5% interest in the Company, which is consistent with the May 2006 e-mail.

The Defendants assert that Barnett's second cause of action should be dismissed as duplicative because Barnett alleges both a breach of contract and a breach of the implied covenant of good faith and fair dealing based on the same facts, and he seeks identical relief on these claims.

Barnett argues in opposition that: (i) within a month of the Buy-Out Agreement, Berkowitz sold back to Insomnia 3% of his equity interests in Insomnia for a purchase price of \$90,000; (ii) Berkowitz created additional classes and subclasses of equity interest and issued such interests to himself, to the exclusion of Barnett; (iii) Berkowitz repeatedly retained, and denied Barnett the financial benefit of the option to acquire from other members of Insomnia a pro rata share of equity interests in Insomnia; and (iv) Berkowitz sold his Sub-class B-4 membership interests to non-third party bona fide purchasers, instead of selling other similar interests that he had awarded to himself or created for his own benefit. Barnett contends that Berkowitz's bad faith actions have rendered Barnett unable to adequately enforce his rights under the Buy-Out Agreement.

Based on the foregoing, Barnett has sufficiently pled facts showing that: (i) subsequent to the Buy-Out Agreement, Berkowitz created additional classes of equity interests and sold his Sub-class B-4 membership interests in Insomnia, among other things, allegedly retaining financial benefits and for the purpose of excluding Barnett; and (ii) Berkowitz's actions resulted in Barnett's deprivation of benefits due under the Buy-Out Agreement. These allegations sufficiently set out a purported breach by Berkowitz of his obligation to perform the Buy-Out Agreement in good faith, resulting in

the withholding of benefits due to Barnett under the Buy-Out Agreement. Moreover, this cause of action is not duplicative of Barnett's breach of contract cause of action.

Interference with Contractual Relations Against The Company Defendants

Defendants assert, *inter alia*, that Barnett's interference with contractual relations cause of action should be dismissed because the Amended Complaint does not indicate how Company Defendants "procured" a breach by Berkowitz and/or failed to satisfy Berkowitz's obligations under the Buy-Out Agreement. Barnett argues that the Company Defendants procured Berkowitz's breaches of the Buy-Out Agreement by, *inter alia*, failing to offer to Barnett the right to acquire equity interests in Insomnia; failing to enforce the obligation of members to offer to Barnett a pro rata portion of equity interests in Insomnia; and by failing to disburse to Barnett his interest in distributions made by Insomnia in violation of the terms of the Buy-Out Agreement.

To plead a cause of action for tortious interference with contract, a plaintiff must allege "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 Inc.*, 88 NY2d 413, 424 (1996) (citations omitted). "Specifically, a plaintiff must allege that the contract would not have been breached 'but for' the defendant's conduct." *Burrowes v Combs*, 25 AD3d 370, 373 (1st Dept 2006).

The Buy-Out Agreement did not oblige the Company Defendants to offer to Barnett the right to acquire equity interest or to disburse any distributions made by

Insomnia, nor did the Company Defendants have any obligation, contractual or otherwise, to ensure that Berkowitz did so. And Barnett does not plead facts showing how the Company Defendants caused Berkowitz to breach the Buy-Out Agreement. These deficiencies are fatal to Barnett's interference with contractual relations cause of action, and that cause of action is therefore dismissed.

Contractual Indemnification Against Berkowitz

Defendants assert that Barnett's cause of action for contractual indemnification is duplicative of the breach of contract claim and that Barnett is improperly seeking to recover his attorney's fees in this action. Barnett counters that the Buy-Out Agreement entitles Barnett to contractual indemnification by Berkowitz, which includes any losses or claims incurred by Barnett in seeking to enforce his rights under the Buy-Out Agreement, including attorney's fees.

“Inasmuch as a promise by one party to a contract to indemnify the other for attorney's fees incurred in litigation between them is contrary to the well-understood rule that parties are responsible for their own attorney's fees, the court should not infer a party's intention to waive the benefit of the rule unless the intention to do so is unmistakably clear from the language of the promise.” *Hooper Assoc., Ltd. v. AGS Computers, Inc.*, 74 NY2d 487, 492 (1989); *see Gotham Partners, L.P. v. High River Ltd. Partnership*, 76 AD3d 203, 207-09 (1st Dept 2010) (“For an indemnification clause to serve as an attorney's fees provision with respect to disputes between parties to the contract, the provision must *unequivocally* be meant to cover claims between the

contracting parties . . . [and] the intention to authorize an award of fees to the prevailing party in such circumstances must be virtually inescapable.”).

The indemnity clause in the Buy-Out Agreement does not reference attorney’s fees at all, nor does it refer exclusively or unequivocally to claims between the parties. Instead, the indemnity clause merely states “[Berkowitz] shall indemnify, after the Closing Date, [Barnett] for any losses or claims which may be incurred by [Barnett] relating to any breach of any representation made by [Berkowitz] in this Agreement, breach of any covenant or obligation of [Berkowitz] contained in this Agreement or any third-party claims which may arise from this Agreement.”

Because the indemnity clause in the Buy-Out Agreement does not exclusively or unequivocally contemplate payment of attorney’s fees and does not relate solely to claims between the parties, the indemnity clause does not meet the rigorous requirement of *Hooper* and Barnett’s claim under the indemnity clause is therefore dismissed.

Declaratory Judgment and Injunction Against All Defendants

Defendants argue that Barnett’s causes of action for a declaratory judgment and a permanent injunction do not lie because Barnett has an adequate remedy for money damages. “A cause of action for a declaratory judgment is unnecessary and inappropriate when the plaintiff has an adequate, alternative remedy in another form of action, such as breach of contract.” *Apple Records, Inc. v Capitol Records, Inc.*, 137 AD2d 50, 54 (1st Dept 1988). Moreover, where alleged injuries “are compensable by money damages [they] cannot serve as a basis for a finding of irreparable harm.” *Cent. Park Sightseeing*

LLC v New Yorkers for Clean, Livable & Safe Streets, Inc., 157 AD3d 28, 33 n.1 (1st Dept 2017) (citation omitted).

Here, Barnett's causes of action for a declaratory judgment and an injunction parrot the breach of contract cause of action, and Barnett's alleged injuries are wholly compensable by monetary damages. For these reasons, Barnett's declaratory judgment and injunctive relief causes of action are dismissed as unnecessary.

Breach of Fiduciary Duty and Accounting

Defendants argue that the Buy-Out Agreement is an arms-length business transaction, and that the parties did not create a trust, with its accompanying fiduciary duties, thereunder. In fact, Barnett held no interest in Insomnia after the Buy-Out Agreement and any dilution of Berkowitz's equity interest, even if undertaken by Berkowitz directly, would not have constituted a breach of fiduciary duty.

Barnett argues that the terms of the Buy-Out Agreement make it clear that a trust was created. Barnett is the beneficiary; Berkowitz, the trustee; the 6.8% of Berkowitz's interest in Insomnia along with distributions or interests that Barnett would thereafter acquire on account of his equity interest in Insomnia is the Trust property and upon closing of the transaction under the Buy-Out Agreement, there was actual delivery or legal assignment of the Trust property to Berkowitz.

To plead a breach of fiduciary duty, a plaintiff must plead "the existence of a fiduciary relationship, misconduct by the other party, and damages directly caused by that party's misconduct." *Pokoik v Pokoik*, 115 AD3d 428, 429 (1st Dept 2014) (citation omitted). "A fiduciary relationship exists between two persons when one of them is

under a duty to act for or to give advice for the benefit of another upon matters within the scope of the relation” but generally does not arise “between those involved in arm’s length business transactions.” *EBC I, Inc. v. Goldman, Sachs & Co.*, 5 NY3d 11, 19 (2005) (citations and quotation marks omitted). “If the parties . . . do not create their own relationship of higher trust, courts should not ordinarily transport them to the higher realm of relationship and fashion the stricter duty for them.” *Id.* at 20.

The Buy-Out Agreement is a contract between two former owners of a limited liability company. Apart from Berkowitz’s contractual obligation to pay Barnett in the event of a Liquidation Event, Barnett did not retain any other right or benefit under the Buy-Out Agreement and the Buy-Out Agreement did not put Berkowitz under a duty to act for the benefit of Barnett. Because the essential element of a breach of fiduciary duty cause of action – the existence of a fiduciary duty – has not been adequately pled, this cause of action is dismissed. Further, because Barnett failed to allege the existence of a fiduciary relationship, which is an essential element of an accounting cause of action, the accounting cause of action is also dismissed. *See Castellotti v Free*, 138 AD3d 198, 210 (1st Dept 2016).

Fraud

Defendants assert that Barnett’s fraud and misrepresentation cause of action is not pled with sufficient particularity as required by CPLR 3016(b) and that the fraud claim is time-barred as all of the allegations of fraud occurred in 2006.

In opposition, Barnett argues that Berkowitz made several affirmative statements to Barnett in 2006, to induce Barnett to enter into the Buy-Out Agreement, including: (i)

the troubled financial condition of Insomnia; (ii) Barnett's equity interest would be diluted, unless Barnett agreed to sell his interest to Berkowitz; (iii) Berkowitz proposed a Buy-Out structure whereby Barnett would retain 5% financial benefits of Insomnia; and (iv) reduction of Insomnia's expenses in only having to pay one manager's salary.

Barnett states that Berkowitz knew such statements were false because he was aware that an equity investment of \$1,550,000 was going to be made in Insomnia; Insomnia was going to create additional classes of equity that would dilute his then existing equity interests in Insomnia; and Berkowitz was in negotiations with other potential investors in Insomnia to limit his involvement and to increase his annual salary to \$175,000. Barnett claims that these alleged false statements are a sufficient basis upon which to plead a fraud claim

To plead a cause of action for fraud, the complaint must allege "a misrepresentation or a material omission of fact which was false and known to be false by 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." *Genger v Genger*, 152 AD3d 444, 445 (1st Dept 2017) (citation and quotation marks omitted). "[A] fraud-based action must be commenced within six years of the fraud or within two years from the time the plaintiff discovered the fraud or could with reasonable diligence have discovered it." *Sargiss v Magarelli*, 12 NY3d 527, 532 (2009) (citations and quotation marks omitted). "Where a plaintiff relies upon the two-year discovery exception to the six-year limitations period, the burden of establishing that the fraud could not have been discovered prior to the two-year period before the commencement of

the action rests on the plaintiff who seeks the benefit of the exception.” *Cannariato v. Cannariato*, 136 AD3d 627, 627 (2d Dept 2016) (citations and quotation marks omitted); accord *Endervelt v Slade*, 214 AD2d 456, 457 (1st Dept 1995).

Barnett alleges that Berkowitz’s fraudulent conduct first came to Barnett’s attention when Berkowitz was ordered by me on August 31, 2018, to provide information about Berkowitz’s equity interest, and information respecting Insomnia and its business. Therefore, according to Barnett, the statute of limitations on his fraud cause of action began running after August 2018.

Under the plain terms of the Buy-Out Agreement, Berkowitz was under no obligation to disclose to Barnett any information regarding the sale of Berkowitz’s equity interests in Insomnia. And Barnett made no effort to get any information about his Retained Seller Benefit from Berkowitz between execution of the Buyout Agreement in 2006 and the commencement of this action in 2018. As Barnett has not alleged facts to show that he sought to obtain information about his Retained Seller Benefit for more than ten years before commencing this action, Barnett has not met his burden of showing that Berkowitz’s alleged fraud could not have been discovered, even with the benefit of the discovery rule, prior to expiration of the statute of limitations. *See Cannariato*, 136 AD3d at 627-28. Barnett’s fraud cause of action is thus dismissed as time-barred.

In accordance with the foregoing, it is

ORDERED that motion of defendants Seth Berkowitz,, Serve U Brands, Inc., Insomnia Cookies, LLC and Insomnia Cookies Holdings, LLC to dismiss the amended

complaint of plaintiff Jared Barnett is granted as to the third through ninth causes of action; and those causes of actions are severed and dismissed, and it is further

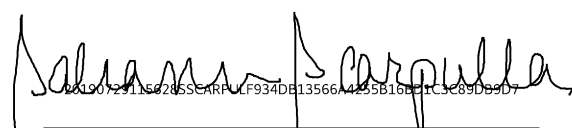
ORDERED that defendants' motion to dismiss is denied as to the first and second causes of action; and it is further

ORDERED that defendant is directed to serve an answer to the amended complaint within twenty (20) days after service of a copy of this order with notice of entry; and it is further

ORDERED that counsel for the parties are directed to appear for a preliminary conference in Room 208, 60 Centre Street, New York, New York on Wednesday, August 28, 2019 at 2.15pm.

This constitutes the decision and order of the Court.

7/29/2019
DATE


SALIANN SCARPULLA, J.S.C.

CHECK ONE:	<input type="checkbox"/>	CASE DISPOSED	<input checked="" type="checkbox"/>	NON-FINAL DISPOSITION	
	<input type="checkbox"/>	GRANTED	<input type="checkbox"/>	GRANTED IN PART	<input type="checkbox"/> OTHER
APPLICATION:	<input type="checkbox"/>	SETTLE ORDER	<input type="checkbox"/>	SUBMIT ORDER	
CHECK IF APPROPRIATE:	<input type="checkbox"/>	INCLUDES TRANSFER/REASSIGN	<input type="checkbox"/>	FIDUCIARY APPOINTMENT	<input type="checkbox"/> REFERENCE