SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 49

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U.S. TSUBAKI HOLDINGS, INC., an Illinois corporation; CENTRAL CONVEYOR COMPANY, LLC, a limited liability company organized under the laws of Delaware,

Plaintiffs,

-against-

LARRY ESTES, an individual; KEVIN ESTES, an individual; JEFFREY DEBRABANDER, an individual; CHRISTOPHER ESTES, an individual; CENTRAL CONVEYOR HOLDINGS, INC., a Michigan Corporation; NEW STATE CAPITAL PARTNERS LLC, a limited liability company organized under the laws of Delaware; NS CCC ACQUISITION LLC, a limited liability company organized under the laws of Delaware; and NEW STATE MANAGEMENT LLC, a limited liability company organized under the laws of Delaware,

Defendants.

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Index No. 651597/2019

DECISION & ORDER
Mot. Seq. Nos. 006 & 007

O. PETER SHERWOOD, J.S.C.:

Defendants NS CCC Acquisition LLC (NSCCC), New State Capital Partners LLC (NSCP), and New State Management LLC (New State) (collectively, the New State defendants), bring a pre-answer motion to dismiss the amended complaint against them pursuant to CPLR 3211 (a)(1) and (7) (Motion Seq. No. 006). Defendants Larry Estes, Kevin Estes, Jeffrey DeBrabander, and Christopher Estes (the Estes defendants), and Central Conveyor Holdings, Inc. (CCH and with the Estes defendants, the Estes defendants), seek dismissal of the amended complaint against them pursuant to CPLR 3211 (a)(7) (Motion Seq. No. 007). Plaintiffs U.S. Tsubaki Holdings, Inc. (USTH) and Central Conveyor Company, LLC (Central Conveyor), oppose both motions. The motions are consolidated for decision.

In determining these motions, the court takes as true the allegations set forth in the 85-page amended complaint dated April 15, 2019. According to the 18 count amended complaint, this action "results from outrageously unlawful and unethical conduct" and "business practices" by defendants that occurred within Central Conveyor prior to and after USTH acquired it in June 2018, defendants' concealment of that conduct and practices, and the "objectively false representations and warranties made to USTH in connection with the sale" which "fraudulently induced USTH to purchase" Central Conveyor "when it otherwise would not have, or else would have done so only for a significantly discounted purchase price" (Amended Complaint, ¶¶ 1, 3 Doc. 30). [1] Most of the claims are due to be dismissed for the reasons discussed below.

BACKGROUND

Plaintiff USTH is a manufacturer headquartered and incorporated in Illinois (*id.* ¶ 12). Plaintiff Central Conveyor is a Delaware limited liability company with its primary facility located in Michigan that designs and manufactures customized material handling and conveyance systems for the automobile industry (*id.* ¶¶ 13, 25). USTH purchased Central Conveyor pursuant to a Purchase and Sale Agreement, dated as of April 24, 2018 (PSA) (*id.* ¶ 13). The PSA is "governed by and interpreted and enforced in accordance with the Laws of the State of New York, without giving effect to any choice of Law or conflict of Laws rules or provisions . . . that would cause the application of the Laws of any jurisdiction other than the State of New York" (*id.* ¶ 13, quoting PSA Section 10.6).

The individual Estes defendants held various roles in Central Conveyor. Larry Estes is its founder and former President (*id.* ¶ 15). Kevin Estes was its Chief Operating Officer. Jeffrey

[1] The reference "Doc" followed by a number refers to the record in this case filed at the New York State Courts Electronic Filing System (NYSCEF).

DeBrabander served as its Vice President of Sales & Estimating. Christopher Estes held a senior role in the Equipment Sustainment Division (*id.* ¶ 26).

Defendant NSCP, a private equity firm headquartered in New York (*id.* ¶ 19), consists of multiple legal entities, some of which are organized under Delaware law (*id.*). "On information and belief, these various entities function together to operate as a single entity, and likely act as alter egos of one another in various capacities" (*id.*). The amended complaint refers to NSCP, NSCCC and New State "individually and collectively as 'New State'" (*id.*).

New State held a majority interest in Central Conveyor and as such "chose Central Conveyor's executives, set its objectives, and maintained the Company's culture under its ownership and management" (*id.* ¶ 33). It served as "Manager" of Central Conveyor pursuant to a Management Services Agreement. Defendant NSCCC, a New State entity, represented Central Conveyor in all dealings with the IRS and other tax authorities (*id.* ¶ 31).

In 2017, New State and the other Defendants undertook the process of selling Central Conveyor via an auction, with New State leading the sales process and controlling which bids to select and negotiate (*id.* ¶¶ 34-35). NSCCC served as Sellers' Representative (*id.* ¶ 35). Plaintiff USTH, with its parent company and counsel, participated in this auction process (*id.* ¶ 36).

In conjunction with the auction process, Defendants provided several sales presentations, and touted Central Conveyor as possessing a large, loyal client base, strong customer relations, talented employees, strong growth and high revenue projections (*id.* ¶¶ 37-41). Plaintiffs allege that defendants' presentations affirmatively misrepresented the true nature of Central Conveyor's customer relations, employees, and sales projections (*id.*). With respect to customer relationships, these "were predicated in no small part on the payment of regular kickbacks and sometimes substantial bribes to customer employees for business" (*id.* ¶ 40). "On information

and belief, Defendants knew or were reckless with respect to the fact that any buyer with ethical and lawful business practices would be forced to cease offering financial payments to customer employees, and, as a result, would face challenges maintaining the same level of customer relationships absent those practices" (*id.* ¶ 40). The presentations did not reveal that Central Conveyor's "employees and independent contractors were being incentivized through compensation structured in ways that violated tax laws as well as union and pension obligations" (*id.* ¶ 41). Nor did the presentations disclose that its "strong culture" was "one of corruption, including rampant expense fraud, time card fraud, schemes to avoid union and pension obligations, and other misconduct that depended on dramatically flawed, and arguably non-existent, internal control systems and unethical leadership" (*id*), and that the historical revenue and other information in its financial statements "were predicated on widespread unlawful and unethical business practices" (*id.* ¶ 42).

Although New State allowed potential bidders to access electronic documentation via a "virtual data room" to conduct due diligence on Central Conveyor's financial status and the nature of its operations, the documents were doctored and the information misrepresented and concealed. The true nature of Central Conveyor's operations were peculiarly within defendants' knowledge (*id.* ¶¶ 43, 44). "Unaware that much of the information reviewed . . . was false or built upon a scheme of unlawful operations", USTH extended a $140 million bid to purchase Central Conveyor, which the Sellers accepted 2018 (*id.* ¶ 45). New State along with its legal counsel, served as the Sellers' Representative in the negotiations for the PSA (*id.* ¶ 46) and provided USTH with various representations, included in the PSA, that were crucial in USTH's decision to purchase Central Conveyor (*id.* ¶ 47). These representations included that: (i) Central Conveyor was in compliance with all laws relating to its business (PSA Sections 4.8, 4.12); (ii)

Seller's financial disclosures fairly presented Central Conveyor's financial condition (PSA Sections 4.5[a]); (iii) Central Conveyor maintained a "system of internal controls over financial reporting . . . designed to provide reasonable assurance that . . . transactions are recorded as necessary to permit the preparation of financial statements in conformity with GAAP [Generally Accepted Accounting Principles]", and it did not "maintain off the books accounts or more than one set of books, records or accounts" (quoting PSA Section 4.5[b]); (iv) Central Conveyor was in compliance with applicable ERISA requirements with no current or pending liability (PSA Section 4.11); (v) Sellers disclosed all material contracts which bound Central Conveyor, including contracts with any independent contractor with annual compensation in excess of $100,000 (PSA Section 4.9 [a][xiv]; (vi) Central Conveyor was not currently under tax audit or examination (PSA Section 4.15 [b]); (vii) Central Conveyor had no outstanding "material liability," including tax liability (PSA Sections 4.15[c], 4.17); and (viii) since December 31, 2017, there had been no "change or event" relating to Central Conveyor that had "resulted in, or would be reasonably expected to result in, a Material Adverse Effect (PSA Section 4.6) (*id.* ¶ 47).

The defendants who executed the PSA did so in various capacities under the following three categories: Sellers, Optionholders, who became Sellers upon the exercise of their options at closing, and Indirect Holders, who bound themselves to non-competition and non-solicitation provisions governing their post-employment conduct (PSA Section 6.10) (*id.* ¶¶ 49-50). The signatories included: Larry Estes, who executed the PSA as CCH's President, as an Indirect Holder, and as an Optionholder; NSCCC, as Seller; Kevin Estes, as Optionholder and an Indirect Holder; Jeffrey DeBrabander, as an Optionholder and Indirect Holder; and, Christopher Estes, as an Indirect Holder (*id.* ¶ 51). The defendants who also are Sellers under the PSA are CCH,

NSCCC, Larry Estes, Kevin Estes, and Jeffrey DeBrabander, and are collectively named as the "Seller Defendants" (*id.*).

Pursuant to PSA Section 2.3(c)(ii), Larry Estes, Michael Laisure (a non-party who was a former member of Central Conveyor Board of Directors), and the New State Directors were required to tender their resignations from Central Conveyor upon closing while Sellers Kevin Estes and Jeffrey DeBrabander, among others, remained employed (*id.* ¶ 53). In conjunction with the PSA, the Seller Defendants provided USTH with a Disclosure Schedule "in which they purported to provide an accounting" of Central Conveyor's material agreements, disclosure of Central Conveyor's noncompliance with applicable laws and legal disputes or proceedings, audited historical financial statements covering fiscal years 2015 through 2017, and other financial and operational information (*id.* ¶¶ 54-55).

At closing, New State, as Sellers' representative, signed and delivered a Closing Certificate which certified that the Sellers' representations and warranties in the PSA were still "true and correct" (*id.* ¶ 57). Unknown to USTH, Central Conveyor's financial and operational conditions at the time of the auction and sale were different than the Seller Defendants had represented. Since the closing, USTH has learned of widespread misconduct within Central Conveyor that defendants concealed during the acquisition process (*id.* ¶¶ 59-60). Such concealed information and false representations included that: (i) Central Conveyor regularly paid kickbacks to customers and their employees in exchange for customer contracts (*id.* ¶¶ 61-67); (ii) the historical financial statements were materially affected by the widespread unethical and unlawful practices (*id.* ¶ 68); (iii) the revenue projections provided were grossly overstated (*id.* ¶ 69); (iv) Work-in-Progress Schedules (WIP Schedules) were doctored to overstate project profitability (*id.* ¶ 71); and (v) Central Conveyor was subject to an audit by the Canada Revenue

Agency (¶¶ 72-73). Plaintiffs allege "on information and belief" that defendants "knew or were reckless with regard to the fact that" Central Conveyor "had this ongoing audit and exposure to tax liability at the time of Closing" (*id.* ¶ 73).

Additionally, (i) defendants caused Central Conveyor to repeatedly underreport its tax liability; (ii) Central Conveyor employees, including Kevin Estes and Jeffrey DeBrabander, regularly used company credit cards for personal use; and (iii) Central Conveyor employees, including Kevin Estes, Jeffrey DeBrabander, and Christopher Estes, engaged in widespread abuses in personal timesheet reporting. "Defendants were either directly involved in the submission and/or approval of these false expense reports and time sheets, or their managerial duties necessarily would have given rise to an awareness of this widespread practice" (*id.* ¶¶ 75-79).

Central Conveyor "historically engaged in certain unlawful and/or contract-breaching employment practices", including offering an alternative payment scheme ("Cash Option") to certain union employees which involved underreporting employee hours and compensation to the labor union to avoid union fees, in violation of collective bargaining agreements (*id.* ¶¶ 80-83). "On information and belief, Defendants had knowledge or else were reckless in failing to learn of the Company's practice of offering the Cash Option" (*id.* ¶ 82), and "were directly involved in orchestrating the use of this practice or had a managerial role over the Company that should have necessarily given rise to knowledge of this widespread practice" (*id.*).

Between the PSA's execution and the closing, Central Conveyor entered into an agreement with LJ, LLC (LJ), an entity owned by Larry Estes (the Estes Agreement), which contemplated payments in the amount of $300,000 by Central Conveyor to LJ over a two-year period in exchange for services provided by Larry Estes as an independent contractor (*id.* ¶¶ 87-

88). "The existence of the Estes Agreement was concealed from USTH during the acquisition process, notwithstanding explicit representations and warranties requiring Seller Defendants to disclose" such a contract and requiring Larry Estes to resign from Central Conveyor as a condition of closing (*id.* ¶ 89).

"Given the foregoing activities, the following representations and warranties provided by the Seller Defendants pursuant to Article IV of the PSA were false when they were made by the Seller Defendants" (*id.* ¶ 92): (i) "PSA Section 4.5 (Accuracy of Company Accounting)" (*id.* ¶¶ 93-94); (ii) "PSA Section 4.6 (Disclosure of Material Adverse Events)" (*id.* ¶¶ 95-96); (iii) "PSA Section 4.8 (Compliance with All Laws)" (*id.* ¶ 96); (iv) "PSA Section 4.9 (No Undisclosed Contracts)" (*id.* ¶¶ 97-98); (v) "PSA Section 4.11 (Compliance with Employee Benefits Withholding)" (*id.* ¶¶ 99); (vi) "PSA Section 4.12 (Compliance with Employment Laws)" (*id.* ¶ 100); (vii) "PSA Section 4.15 (No Undisclosed Audits; Compliance with Respect to Tax Matters)" (*id.* ¶ 101-102); and (viii) "PSA Section 4.17 (No Material Liabilities)" (*id.* ¶ 103).

Following the closing and pursuant to Section 2.4 of the PSA, the PSA parties entered into a Purchase Price Adjustment process, during which USTH learned about the Estes Agreement and began to question defendants' financial disclosures (*id.* ¶ 104). During this time, USTH also realized that defendants' revenue forecast was overstated (*id.* ¶ 105). Pursuant to its rights under PSA Section 2.4 and beginning in October 2018, USTH made repeated requests to New State for information regarding the Estes Agreement and the defendants' financial disclosures provided during the diligence period (*id.* ¶ 106). With respect to the Estes Agreement, New State, as Sellers' Representative, asserted on October 5 and December 3, 2018 that Sellers had no knowledge of the Estes Agreement and argued that USTH had executed the Estes Agreement as it was executed in writing on the closing date (*id.* ¶ 107). With respect to

USTH's requests regarding the financial disclosures' inaccuracies, New State responded with "evasion and inaction" (*id.* ¶ 108). New State "ignored" USTH's November 16, 2018 request for information, and following USTH's repeated request set forth in a letter dated December 17, 2018, New State responded on December 23, 2018, that it was "reviewing the issue" and "will revert back in due course" (*id.* ¶ 108). On March 18, 2019, New State informed USTH that it did not have "any information concerning inaccuracies in projections, that, as a general matter, it did not have "possession, custody or control over all information that may be available to a particular Seller," that it could "pass along USTH's requests to Sellers," but that it was "not obligated under the [PSA] or otherwise to conduct document gathering or an investigation on [USTH's] behalf" (*id.*)

In January 2019, Central Conveyor terminated the employment of Kevin Estes, Jeffrey DeBrabander, and Christopher Estes for cause (*id.* ¶¶ 110-116) which they dispute (*see id.* ¶ 117). Following the terminations, Kevin Estes and Jeffrey DeBrabander have failed to return electronic devices owned by Central Conveyor which, upon information and belief, contain confidential, proprietary, and/or trade secret information belonging to Central Conveyor (*id.* ¶¶ 118, 120). Additionally, following his employment termination, on information and belief and based on forensic analysis, Christopher Estes, in violation of his Employment Agreement, copied Central Conveyor's confidential information from his company-issued laptop to his personal external hard drive, including 41 GB of data from the desktop and 45,000 email messages from Central Conveyor's Outlook account (*id.* ¶¶ 122, 124). The downloaded and retained files include: (i) a compiled list of more than 500 customer contacts; (ii) proprietary blueprints, drawings, and schematics not shared with customers; (iii) non-public compilations regarding parts suppliers, pricing for spare parts, and wage data paid for certain services; (iv) quotes to

customers revealing Central Conveyor's pricing information and profit margins; and (v) customer agreements (*id.* ¶ 123).

Kevin Estes, DeBrabander, and Christopher Estes also are subject to non-competition and non-solicitation provisions pursuant to Sections 6(a) and (b) of their Employment Agreements and Section 6.10 of the PSA (*id.* ¶ 135-137). Christopher Estes has already engaged in conduct breaching PSA Section 6.10, as he was hired at a company that engages in a similar business and is headquartered fewer than twenty-five miles away from Central Conveyor (*id.* ¶ 138).

THE CLAIMS ASSERTED IN THE AMENDED COMPLAINT

The amended complaint alleges a total of 18 separate causes of action, with USTH asserting 11, Central Conveyor asserting six, and USTH and Central Conveyor jointly asserting one.

A. Claims by USTH

The first 3 causes of action, are asserted by USTH against the Seller Defendants, NSCP, New State, and Christopher Estes and are respectively labelled as fraudulent inducement, fraudulent misrepresentation, and fraudulent concealment. As against NSCP, New State, and Christopher Estes, USTH asserts a claim for aiding and abetting fraud (fourth cause of action). As against the Seller Defendants, USTH asserts claims for relief for breach of contract and for breach of implied covenant of good faith and fair dealing (the fifth and sixth claims, respectively). Additionally, USTH asserts the seventh claim, labelled as unjust enrichment, against the Seller Defendants, New State defendants, Christopher Estes, and Larry Estes. USTH asserts the ninth cause of action for declaratory relief, with respect to PSA Section 6.10, against Kevin Estes, Christopher Estes, and DeBrabander. In the tenth cause of action, USTH alleges a breach of contract claim against Christopher Estes. The eleventh and twelfth claims are asserted

by USTH against both Kevin Estes and DeBrabander for declaratory relief as to Employment Agreement Section 6(a), and declaratory relief with respect to their termination for cause.

B. Claims by Central Conveyor

Central Conveyor brings the eighth and thirteenth causes of action against DeBrabander and Kevin Estes for conversion and breach of contract. It asserts the fifteenth, sixteenth, and seventeenth claims against Christopher Estes for: (i) violation of the Computer Fraud and Abuse Act, 18 USC 1030, *et seq.*; (ii) violation of the Michigan Uniform Trade Secrets Act, MCL 445.1091, *et seq.*; (iii) and violation of the Defend Trade Secrets Act, 18 USC 1836, *et seq.* In the eighteenth cause of action, Central Conveyor asserts a claim for relief against Christopher Estes and Larry Estes for trespass to chattels.

C. Claim by Both Plaintiffs

Both USTH and Central Conveyor allege the fourteenth claim, labelled as breach of fiduciary duty, as against Kevin Estes and Jeffrey DeBrabander.

THE MOTIONS TO DISMISS

"In the posture of defendants' CPLR 3211 motion to dismiss, [the court's] task is to determine whether plaintiffs' pleadings state a cause of action. The motion must be denied if from the pleadings' four corners factual allegations are discerned which taken together manifest any cause of action cognizable at law" (*511 West 232nd Owners Corp. v Jennifer Realty Corp.*, 98 NY2d 144, 151-152 [2002] [internal quotation marks and citations omitted]). The court must "liberally construe the complaint and accept as true the facts alleged in the complaint and any submissions in opposition to the dismissal motion," and "accord plaintiffs the benefit of every possible favorable inference" (*id.* at 152 [internal citations omitted]). "Whether a plaintiff can

ultimately establish its allegations is not a part of the calculus in determining a motion to dismiss" (*EBC I, Inc. v Goldman, Sachs & Co.*, 5 NY3d 11, 19 [2005]).

Similarly, in a CPLR 3211 (a)(1) motion, the alleged facts are regarded as true and plaintiff is afforded the benefit of every favorable inference (see *Leon v Martinez*, 84 NY2d 83, 87-88 [1994]). It is, however, "well settled that bare legal conclusions and factual claims, which are either inherently incredible or flatly contradicted by documentary evidence . . . are not presumed to be true on a motion to dismiss for legal insufficiency" (*O'Donnell, Fox & Gartner v R-2000 Corp.*, 198 AD2d 154, 154 (1st Dept. 1993). Dismissal "is warranted only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law" *(Leon,* 84 NY2d at 87-88*)*. The motion "may be appropriately granted only where the documentary evidence *utterly refutes* plaintiff's factual allegations, *conclusively establishing* a defense as a matter of law" (*McCully v Jersey Partners, Inc.*, 60 AD3d 562, 562 [1st Dept 2009]).

A. <u>The Fraud Claims (First, Second and Third Causes of Action)</u>

1. <u>The First Cause of Action, Fraudulent Inducement</u>

In the first cause of action, USTH asserts a fraudulent inducement claim against the Seller Defendants, NSCP, and New State, and a claim labeled as "fraudulent inducement through civil conspiracy" against NSCP, New State, and Christopher Estes. It asserts that these Defendants made or conspired to make false and misleading material misrepresentations about Central Conveyor's operations, its compliance with law and Company policy, and its financial state (Amended Complaint, ¶ 141). "[T]hey concealed rampant unlawful and unethical conduct and miscast the Company's actual financial condition, hiding from USTH facts that were uniquely within Defendants' knowledge and that USTH, despite its reasonable investigation

during the due diligence period, could not and did not discover" (*id.*) At paragraphs 92 through 103, the amended complaint alleges that these defendants, "as alter egos," made numerous misrepresentations to USTH about Central Conveyor's financial health and operations that either misstated or omitted key facts (*id.* ¶ 142). In July 2017 sales presentations defendants asserted that Central Conveyor's success was predicated on strong customer relationships (*id.* ¶ 143). "In fact, certain Defendants – including some of the Seller Defendants," secured business with "customers through a series of illegal and unethical kickbacks, and, in some instances, outright bribes" (*id.* ¶ 144). These sales presentations also stated that Central Conveyor "outmatched competitors in terms of its 'human capital" and its 'ability to quickly mobilize a large workforce'" (*id.* ¶ 145). Defendants failed to disclose that "certain Company managers," including "some" of the Seller Defendants, incentivized and mobilized its workforce and independent contractors by offering the Cash Option and permitting employees to seek reimbursement or to use company credit cards for personal expenses and to submit false time sheets (*id.* ¶ 145).

In PSA Sections 4.8, 4.12, 4.5(a), 4.5(b), 4.11, 4.9(a)(xiv), 4.15(b), 4.15(e), 4.17, and 4.6 (*id.* ¶ 147), Defendants made a number of representations and warranties that "were false when made, and, upon information and belief, the Seller Defendants knew that they were false, or else were reckless as to their falsity of these representations" (*id.* ¶ 148). Further, in connection with the negotiation of the PSA and collateral to it, the Seller Defendants provided USTH with a Disclosure Statement, containing statements that, as detailed in paragraphs 54-55, were false when made (*id.* ¶ 149). The conduct of the Seller Defendants, NSCP, and New State throughout the auction and sale process and the PSA's negotiation, "was part of one continuous fraudulent scheme" to induce USTH to enter the PSA and close on the purchase (*id.* ¶ 151).

Defendants knew that USTH would rely, and USTH reasonably relied, on the misrepresentations made by them (*id.* ¶¶ 152-153). "The facts that these Defendants misrepresented were peculiarly within their control and exclusive knowledge," and the facts were not disclosed and were actively concealed (*id.* ¶ 153). Despite USTH's "engaging in reasonable pre-closing due diligence and independent review", it "had no ability to discover the falsity of the representations prior to purchase" (*id.*).

Under the label of fraudulent inducement through civil conspiracy, the amended complaint further alleges that "upon information and belief," NSCP and New State "(via PSA signatory [New State founder] David Blechman)" and Christopher Estes "intentionally entered into an agreement with Seller Defendants to fraudulently induce USTH to purchase" Central Conveyor "by providing false representations, as described above," and "each defendant committed an overt act in furtherance of this conspiracy, resulting in harm to USTH" (*id.* ¶ 155). At all times during the acquisition process, NSCP and New State assisted in the communication of fraudulent misrepresentations to USTH, knew the statements to be false or were reckless as to their falsity, and made the statements to induce USTH to enter into the PSA (*id.* ¶ 156).

2. The Second Cause of Action, Fraudulent Misrepresentation

The second cause of action alleges fraudulent misrepresentation against the Seller Defendants, NSCP, and New State. USTH alleges "[u]pon information and belief," that defendants NSCP, New State, and Christopher Estes entered into an agreement with the "Seller Defendants" to fraudulently induce USTH to purchase Central Conveyor by providing the described false representations, each defendant committed an overt act in furtherance of the conspiracy as described, and "all of these Defendants are liable for the fraudulent misrepresentations committed by each other in furtherance of the conspiracy" (*id.* ¶ 163).

3. The Third Cause of Action, "Fraudulent Concealment"

In the third cause of action, plaintiffs allege that the Seller Defendants made numerous representations to USTH regarding Central Conveyor's financial health and operations, omitted key facts, and concealed violations of legal and ethical requirements and restrictions (*id.* ¶ 166). "Seller Defendants had a duty to disclose the truth about the Company's finances and operations because they had superior knowledge of these facts, these facts were not readily available to USTH despite USTH's reasonable due diligence, because they chose to disclose some facts and could not do so selectively, and Seller Defendants knew that USTH was purchasing Central Conveyor on the basis of its mistaken knowledge about the Company" (*id.* ¶ 167).

4. The Contentions of the New State Defendants

The New State defendants argue that USTH's claims for fraudulent inducement, misrepresentations, and concealment fail on a number of grounds and must be dismissed. They argue that, fundamentally, USTH is attempting to turn an ordinary contract claim which is subject to strict contractual limitations on liability and damages, into a fraud claim based on alleged misrepresentations and omissions made outside the contract that purportedly induced it to purchase Central Conveyor. But USTH is a sophisticated party and expressly disclaimed reliance on the very information that forms the heart of its claims. They additionally argue that the fraud claims about representations and warranties in the PSA are duplicative of the contract claim. Further: (1) USTH has not identified the specific misstatements made by NSCCC or the other New State entities; (2) its improper lumping together of all defendants does not satisfy fraud pleading requirements; and (3) USTH has not alleged any facts that support veil piercing or conspiracy theories. These defendants also assert that the fraud claims fail because they are not

pleaded with detail as required by CPLR 3016(b), and fail to allege the elements for fraudulent misrepresentation, fraudulent inducement, and fraudulent concealment.

The fraud claims based on alleged misstatements and omissions made in sales materials, due diligence, and financial projections fail for multiple independent reasons. First, USTH cannot establish justifiable reliance. It is a sophisticated entity that "made its own analysis and decision" based on its "access to the books, records, facilities and personnel of the Company and its Subsidiaries for purposes of conducting its due diligence" (PSA Section 5.7). The parties agreed that, outside of the PSA, NSCCC has not made "any representation or warranty," including with respect to any Evaluation Material," which specifically includes sales presentations and information in the data room (PSA Section 4.26). USTH expressly disclaimed reliance on any such statements (PSA Section 10.5).

Although these causes of action assert that defendants had peculiar knowledge of the alleged facts forming the basis of the fraud claims, the "peculiar knowledge" exception to the disclaimer of reliance is applied stringently to sophisticated buyers. The exception does not apply where plaintiffs have not alleged any facts from which it could be inferred that defendant's access to the relevant information was superior, where plaintiff does not allege it was denied access to that information, and where a sophisticated buyer conducted due diligence and does not provide an explanation for why the truth was outside its reach. Here, USTH expressly affirmed that it had access to Central Conveyor's books, records, and personnel and the opportunity to conduct diligence, and USTH fails to allege any facts showing that NSCCC had specific knowledge of a particular fact, much less why the truth was outside its reach. Second, USTH has failed to plead the elements of fraud for each defendant. USTH attributes the alleged misconduct to Central Conveyor, the Estes defendants, and unnamed employees, and then alleges that the

misstatements were found in presentations made by the "Defendants" (Amended Complaint ¶¶ 37-40). These lumped-together allegations are insufficient to state a misstatement claim individually against NSCCC, NSCP, or New State. USTH also fails to name the party to whom the alleged misrepresentations were made, which is fatal. USTH's omissions claims also fail because USTH and the New State defendant(s) stood at arms-length, and, therefore, no duty was owed and the concealment claim must be dismissed.

Further, given the absence of allegations connecting the New State defendant(s) to the alleged employee misconduct, USTH fails to allege facts supporting the scienter claims and instead relies on allegations made on "information and belief" and accordingly fails to plead any facts from which an inference could be made.

USTH's allegations that New State managed Central Conveyor are insufficient. NSCCC, New State, NSCP, and Central Conveyor are separate legal entities, and the fact that NSCCC was a large investor does not relieve USTH of its obligation to allege all elements of fraud as to each defendant. The Management Services Agreement (MSA) between New State Management and Central Conveyor, cited by plaintiffs, highlights the flaw in USTH's case. It states that New State is an "independent contractor," and that it "shall have no authority to enter into any agreement or to make any representation, commitment or warranty binding upon the Company or to obtain or incur any right, obligation or liability on behalf of the Company" (Doc. No. 75, Affirmation in Support of Anthony P. Ferrara [Ferrara Aff.], Exhibit 9, at 3).

USTH also makes conclusory statements, on "information and belief," that certain defendants should be considered "alter egos" of other defendants (Amended Complaint, ¶ 19). Not only did USTH specifically covenant not to sue NSCCC affiliates under a veil piercing

theory (PSA Section 10.3), USTH also fails to allege any facts to support a veil piercing claim under Delaware law, which governs this issue.

Moreover, USTH failed to allege any facts that tie NSCCC to the underlying employee misconduct, and, therefore, has not made allegations that would lead to a reasonable inference that NSCCC had knowledge of any facts that could form a fraud claim. The representations and warranties (R & Ws) were made "severally (based on each Seller's Pro-Rata Share), but not jointly," and NSCCC did not assume liability for misstatements by the Estes defendants or other Sellers.

As to USTH's claims based "[u]pon information and belief" that NSCP and New State entered into an agreement with Christopher Estes to fraudulently induce USTH to purchase Central Conveyor (*id.* ¶¶ 155, 163, 170), USTH's barebones conclusory allegations do not state a claim. USTH failed to allege a cognizable tort against NSCCC, and there are no factual allegations of conspiratorial conduct between Christopher Estes, NSCP and New State. USTH cannot avoid the stringent pleading requirement for fraud with conclusory allegations of "conspiracy."

5. Contentions of the Estes Defendants

The Estes defendants seek dismissal of the fraud claims on grounds that are similar to those argued by the New State Defendants and will not be described here. Similar to the New State defendants, the Estes defendants argue that each of these claims fail because: (i) they are improperly pleaded on information and belief; (ii) they otherwise rely on vague, unspecific allegations of purported misconduct; and, (iii) they improperly generally assert the Estes defendants' collective participation in and knowledge of misconduct and mismanagement. These claims also fail to meet CPLR 3016(b)'s heightened pleading standard for fraud.

6. Plaintiffs' Contentions in Opposition

USTH argues that it states the elements of fraud claims in that it alleges that at least fifteen representations and warrantees (R & W) defendants made in the PSA were (i) misrepresentations or material omissions of fact, (ii) that defendants knew were false, (iii) that were made for the purpose of inducing USTH's reliance, (iv) on which USTH justifiably relied, and (v) that caused USTH to suffer damages (Opp. Br. at 14, Doc. 96).

USTH asserts that defendants are not insulated from fraud liability for their outright and intentional lies, especially where, as here, the fraud claims seek a different remedy against a different group of defendants than the breach of contract claim, and where plaintiffs expressly reserved the right to pursue that remedy in the PSA. In the instant case the allegations are not duplicative of a breach of contract claim as they concern contractual misrepresentations of then present and material facts that are collateral to the contract and are sufficient to support a separate fraud claim based on the false R & Ws.

Moreover, the fraud claim is not duplicative of the contract claim as USTH proceeds against additional parties who did not sign the PSA but participated in the broader scheme that culminated in the giving of false R & Ws, and USTH seeks remedies that are different from those available on its breach of contract claim (*id.* at 17). Under the breach of contract claim, USTH can only hold each Seller defendant severally liable for its pro rata share of the damages, but on the fraud claim, USTH can recover the entirety of its damages from each and every defendant who is found liable (*id.* at 18).

Additionally, the fraud and contract claims are not duplicative because USTH expressly reserved the right to bring such claims by insisting that the sole remedy provision does not apply "in the case of fraud" (PSA Section 9.2[g]). This provision does not merely state that in the event

of fraud USTH is not limited to recovering from the Indemnity Escrow Fund and the R & W Insurance Policy, it states that USTH may bring a cause of action for fraud. Defendants' argument reads this fraud carve-out language out of the negotiated agreement, violating settled principles of contract law (Opp. Br. at 19, Doc. 96). The provision is unambiguous. In any event, the parties' negotiating history with respect to this language supports USTH's reading (Doc. 98, Affirmation of Elizabeth A. Edmondson in Support of Consolidated Opposition [Edmondson Aff.] ¶ 8).

Plaintiffs further argue that the question of what constitutes reasonable reliance generally is not a question of law that can be determined on a motion to dismiss, as it is fact-intensive. Here, determining whether USTH can assert reasonable reliance in the face of the contractual disclaimer cannot be resolved as a matter of law on these dismissal motions (Doc. 96 at 21).

Contrary to the New State defendants' assertion, the merger clause in the PSA does not disclaim reliance on any of the alleged misrepresentations in the PSA (*id.* at 22). The fraud claim is based on a cohesive and coordinated scheme among defendants to hide unlawful conduct involving misrepresentations made before the PSA and in the PSA. The misrepresentations and falsehoods were included in the contract as R & Ws. Under the plain terms of the PSA, USTH was entitled to rely on them and specifically bargained for this right (Edmondson Aff. ¶ 7). While USTH did its "own analysis" and did its "due diligence," both were undertaken "in reliance on the representations and warranties of the Sellers expressly set forth in this Agreement" (PSA Section 5.7).

Additionally, even absent this bargained-for language, the contractual disclaimer is unenforceable under the "special facts" doctrine. Under this doctrine, which applies regardless of the level of the sophistication of the parties, a contractual non-reliance provision does not shield

a defendant's fraudulent conduct where, as here, the hidden or misstated material was peculiarly within defendants' knowledge. The doctrine applies regardless of the level of sophistication of the parties. At the pleading stage, a plaintiff need only allege that the fraudulent conduct was uniquely in the defendant's control and could not have been discovered by the plaintiff through the exercise of ordinary diligence.

Plaintiffs assert that USTH has alleged sufficient facts to establish that the defendants had access to the "special facts" that USTH lacked. USTH alleged that the information it eventually discovered evidencing the fraud was not public or discernible from the public records and alleged that a complete and authentic picture of Central Conveyor's operations and financial condition could not have been ascertained based on the documents provided via the "virtual data room." Additionally, defendants' knowledge was not limited to what was in the virtual data room. The Estes defendants controlled Central Conveyor for many years prior to New State's acquisition, worked at the company for many years, and had a hand in every part of the business– including the misconduct that USTH alleges was integral to its business model. As majority stakeholder, the New State defendants controlled Central Conveyor, and had absolute and unfettered access to its records and personnel. Taken together, these allegations are more than sufficient to allege "special facts" within defendants' knowledge.

Plaintiffs further argue that contrary to defendants' contentions, USTH has alleged facts sufficient to plead a fraud claim against each and every defendant. First, USTH's allegations made on information and belief are in addition to, not in lieu of, specific allegations supporting scienter and an inference of intent. Second, the allegations are sufficiently detailed as USTH pleaded pages of detail about the misconduct that made the R & Ws false, reproduced the written and detailed misrepresentations, explained why it is reasonable to infer that defendants knew the

R & Ws were false, and explained that defendants had a substantial financial motive to induce USTH to rely on the misrepresentations.

Additionally, the claims are not vague and conclusory and are sufficiently individualized. As the majority of the misrepresentations were made in the PSA, they were made to USTH as buyer. USTH alleges that all the defendants were either owners, directors, officers, or key employees, and some were several of the above. Accordingly, USTH has pleaded facts sufficient to support an inference that each defendant knew of the fraud. Under USTH's theory of fraud, it need not catalog exactly which instances of misconduct each defendant knew. USTH has alleged a series of interrelated events that comprise the scheme and that defendants were all key players in that overall scheme. The Estes defendant are members of a single family that owned and ran the company. The New State defendants were not passive investors but rather critical stakeholders who were highly compensated for managing Central Conveyor. To the extent the allegations do not differentiate among the defendants, it is because such allegations are common to all defendants or to the group of defendants against whom they are pleaded.

Plaintiffs argue that contrary to the Seller Defendants' arguments, USTH has alleged fraud as against NSCP and New State regardless of whether they were signatories to the PSA, as they participated in the fraudulent scheme that involved the making of the misrepresentations. USTH has alleged that NSCP and New State knew the facts represented and alleged were false or gave an untrue picture of the company's financial condition, and USTH reasonably relied on these defendants, which are affiliated with NSCCC and intimately involved with Central Conveyor's business operations. Additionally, USTH specifically reserved the right to sue non-signatories "for claims arising from fraud" (PSA Section 10.3; Edmondson Aff. ¶ 9). With respect to Christopher Estes, USTH alleged that he knew the R & Ws were not true because he

himself participated in the fraudulent conduct and knew these R & Ws were false. USTH further alleged that as a signatory to the PSA and an Indirect Holder, and as a family member of the Seller Defendants, he knew the R & Ws were being made.

Plaintiffs additionally argue that contrary to defendants' contention, the omission claims do not fail because the transaction was conducted at arms-length. That USTH is a sophisticated party did not relieve defendants' obligation to disclose material facts, as USTH specifically contracted to protect itself by requiring that defendants disclose such material facts. Additionally, USTH adequately alleged that defendants had a duty to disclose as their fraudulent misconduct was peculiarly within their knowledge and USTH could not have discovered the misconduct through ordinary diligence.

7. The Reply Papers

In their reply, the New State defendants repeat that they demonstrated that USTH's fraud claims based on statements outside the PSA are barred by an express contract provision in which USTH clearly and unambiguously disclaimed reliance and the fraud claims based on representations and warranties in the PSA are duplicative of the contract claim. Contrary to USTH's assertions, the PSA does not guarantee it the right to assert duplicative contract claims based on R & Ws or to claim reliance on information upon which it promised not to rely. They further argue that they also demonstrated that while the amended complaint is replete with allegations of bad acts by the Estes defendants, there are no allegations that anyone at New State participated in them and USTH impermissibly lumps together all the defendants to obscure this flaw. The New State defendants argue that USTH concedes in its opposition that only the Estes defendants personally participated in the misconduct and abandons its alter ego theory. USTH also fails to make individualized allegations against NSCC, NSCP, and New State that would

show that each was aware of the Estes defendants' conduct, and instead relies on broad, grouped allegations of ownership, management fees, and board seats. These allegations are not enough to plead fraud. Additionally, NSCP and New State argue that as USTH failed to address their arguments seeking dismissal of USTH's fraud claims against them predicated on an alleged conspiracy. USTH conceded that those claims should be dismissed.

USTH, a sophisticated party, did not defeat their arguments that the claims based on statements allegedly made in the negotiations should be dismissed. The bargain between the parties is set forth in the PSA (Sections 4.26, 5.7, 4.26, and 10.5), and these contractual provisions destroy the essential element of reasonable reliance. USTH cannot rely on alleged statements made outside the PSA. Here the question of reasonable reliance is not a factual one. The PSA's specific disclaimer destroys reliance and compels dismissal at the pleading stage.

Additionally, the New State defendants reply that the court should reject USTH's argument that the specific disclaimer of reliance is unenforceable under the "special facts" doctrine. USTH acknowledged in the PSA that it was provided access to company documents and personnel and fails to state how the evidence of alleged fraud was not discoverable.

The New State defendants further reply that they established that USTH impermissibly lumps defendants together. There are no allegations that New State engaged in the underlying misconduct; the allegations are made against the Estes defendants who worked for Central Conveyor and not NSCCC, New State, or NSCP. New State and NSCP are all separate legal entities, and plaintiffs have not alleged any facts to support an alter ego theory. With respect to alleged misstatements made outside the PSA, USTH does not allege who, from which legally separate New State entity, made what allegedly false statement and when. Moreover, all the fraud claims are made against the lumped-together New State defendants without any specific

allegations that support a reasonable inference that each separate legal entity had knowledge of the underlying conduct allegedly carried out by the Estes defendants. USTH's allegations of scienter based on information and belief are insufficient to support a reasonable inference of fraud and scienter.

With respect to USTH's omission-based fraud claims, USTH does not dispute that this was an arms-length transaction, but claims that the existence of representations in the PSA gives rise to the duty to disclose. The parties agreed on the scope of R & Ws, and the presence of the R & Ws does not give rise to an omission claim. Similarly, a duty to speak does not arise under the "special facts" doctrine. USTH fails to allege facts to support an inference that each of the New State defendants had knowledge, much less peculiar knowledge, of acts that could not be discovered by plaintiffs.

8. Analysis

"A claim rooted in fraud must be pleaded with the requisite particularity under CPLR 3016(b)" (*Eurycleia Partners, LP v Seward & Kissel, LLP*, 12 NY3d 553, 559 [2009]). "The circumstances constituting the fraud must be stated in detail" (*Small v Lorillard Tobacco Co., Inc.*, 94 NY2d 43, 57 [1999], citing CPLR 3016[b]). "The elements of a cause of action for fraud require a material misrepresentation of a fact, knowledge of its falsity, an intent to induce reliance, justifiable reliance by the plaintiff and damages" (*Eurycleia Partners, Inc.*, 12 NY3d at 559 [internal citations omitted]). "Although there is certainly no requirement of 'unassailable proof' at the pleading stage, the complaint must 'allege the basic facts to establish the elements of the cause of action" (*Eurycleia Partners, LP,* 12 NY3d at 559, quoting *Pludeman v Northern Leasing Sys., Inc.*, 10 NY3d 486, 492 [2008]). "CPLR 3016 (b) is satisfied when the facts suffice

to permit a 'reasonable inference' of the alleged misconduct" (*Eurycleia Partners, LP,* 12 NY3d at 559).

"In a fraudulent inducement claim, the alleged misrepresentation should be one of then-present fact, which would be extraneous to the contract and involve a duty separate from or in addition to that imposed by the contract, and not merely a misrepresented intent to perform" (*Hawthorne Group v RRE Ventures,* 7 AD3d 320, 323-24 [1st Dept 2004] [internal citations omitted]).

"The elements of fraudulent misrepresentation are: (1) the defendant made a material false representation, (2) the defendant intended to defraud the plaintiffs thereby, (3) the plaintiffs reasonably relied upon the representation, and (4) the plaintiffs suffered damage as a result of their reliance" (*J.A.O. Acquisition Corp. v Stavitsky,* 18 AD3d 389, 390 [1st Dept 2005]).

To state a legally cognizable claim for fraudulent concealment, the complaint must allege, in addition to the four elements for fraudulent misrepresentation, "that the defendant had a duty to disclose material information and that it failed to do so" (*P.T. Bank Cent. Asia v ABN AMRO Bank N.V.,* 301 AD2d 373, 376 [1st Dept 2003]).

Even affording the amended complaint a liberal construction, accepting the allegations as true and according plaintiffs the benefit of every possible favorable inference, the court finds that the amended complaint fails to state causes of action for fraudulent inducement, fraudulent misrepresentation, or fraudulent concealment and it is duplicative of the contract claims against the Seller Defendants. First, the amended complaint fails to meet the heightened pleading standard of CPLR 3016(b) for a number of reasons. First, the amended complaint "did not attribute specific misrepresentations or wrongdoing" to a particular defendant "but, rather, impermissibly lumped" the defendants together (*RKA Film Financing, LLC v Kavanaugh,* 171

AD3d 678, 678 [1st Dept 2019] [internal citations omitted]. Fraud must be claimed with specificity "as to each individual defendant" (*MP Cool Invs. Ltd. v Forkosh,* 142 AD3d 286, 291 [1st Dept. 2016]) which the amended complaint fails to do.

Second, the allegations are impermissibly made on information and belief. "Statements made in pleadings upon information and belief are not sufficient to establish the necessary quantum of proof to sustain allegations of fraud" (*Facebook, Inc. v DLA Piper LLP (US)*, 134 AD3d 610, 615 (1st Dept 2015]). Allegations in the amended complaint lack the requisite particularity and are therefore deficient.

Third, the amended complaint fails to satisfy the pleading requirements of CPLR 3016(b) as to the elements of scienter and knowledge. "The allegations of scienter here were not pleaded with the requisite particularity, but are conclusory, and scienter may not reasonably be inferred from the circumstantial evidence relied on by plaintiffs" (*Fried v Lehman Brothers Real Estate Assocs. III, L.P.*, 156 AD3d 464, 465 [1st Dept 2017], *lv denied* 31 NY3d 1137 [2018]). A claim will be dismissed where, as here, the "allegations as to scienter are conclusory and factually insufficient" (*Facebook, Inc.*, 134 AD3d at 615). Additionally, a complaint asserting a fraud claim based on an allegation that a particular defendant orchestrated the fraudulent act(s) committed by others is insufficient when it fails "to allege any specific facts that, if true, would give rise to a reasonable inference" of some connection between the particular defendant and the fraudulent act(s) and that a particular defendant had knowledge of the underlying misconduct by other defendants (*Cronos Group LTD.* v *XComIp, LLC*, 156 AD3d 54, 61 [1st Dept 2017]).

A cause of action for fraud against the Seller Defendants simply does not arise when, as here, the only alleged fraud is a breach of contract (*see Carle Place Union Free School District v Bat-Jae Const., Inc.*, 28 AD 3d 596 [2d Dept 2006]). Further, a fraud claim is not stated where

the complaint merely alleges that defendant entered the contract while lacking an intention to perform it (*see New York University v Continental Ins. Co.*, 87 NY 2d 308 [1995]). Absent allegations of misrepresentations that are extraneous to the terms of the parties' contract, which are not present here, these claims must be dismissed as duplicative of the breach of contract claims (*see HSH Norbank AG v UBS AG*, 95 AD 3d 185 [1st Dept 2012]). The plaintiffs also argue they have stated claims for fraud because they have pleaded "special facts" that were within dependents' knowledge. However, mere disparity of knowledge between sophisticated business entities does not trigger a duty to disclose (*see Societe Nationale D' Exploitation Industrielle Des Tabacs et Allumettes v Salomon Bros. Intern., Ltd,* 268 AD 2d 373 [1st Dept 2000]). Plaintiffs acknowledge they had access to Central Conveyors books, records and personnel and the opportunity to conduct due diligence prior to the closing. The "special facts" exception does not apply.

The allegations also fail to state a cause of action in fraud against NSCP and New State neither of which was a party to the alleged fraudulent representations. According to the amended complaint, these defendants "participated" in the misrepresentations "included in the contract as R&Ws" (Opp. Br. at 17, Doc. 96) and are alter egos of NSCCC and one another. Plaintiffs, however, fail to allege any facts to support either veil piercing or participation. The court need not decide whether, as asserted by the New State defendants, the issue of veil piercing is governed by the laws of Delaware, as it is the state of incorporation for all three New State defendants, or the law of New York under the PSA or the paramount interest test. The amended complaint simply fails to allege facts to support the alter ego allegations under the law of either state. "To state a veil-piercing claim under Delaware law, a plaintiff must plead facts supporting an inference that a corporation, through its alter ego, has created a sham entity designed to

defraud investors and creditors" (*Walnut Hous. Assoc. 2003 L.P. v MCAP Walnut Hous. LLC*, 136 AD3d 403, 404 (1st Dept 2016]). "Generally . . . piercing the corporate veil requires a showing that: (1) the owners exercised complete domination of the corporation in respect to the transaction attacked; and (2) that such domination was used to commit a fraud or wrong against the plaintiff which resulted in plaintiff's injury" (*Morris v New York State Dept. of Taxation and Fin.*, 82 NY2d 135, 141 [1993]). Plaintiffs have failed to plead any such facts.

Nor have plaintiffs otherwise stated causes of action in fraud as against NSCP and New State. Other than generalized and conclusory allegations, alleged by category of lumped together defendants. USTII fails to allege the requisite facts so as to state causes of action in fraud against these two defendants. For example, there is no particularized factual allegation as to a misrepresentation made by these two non-signatories of the PSA at any stage of the transaction. The amended complaint further lacks a particularized factual allegation as to the elements of scienter, knowledge of the alleged misconduct by other defendants, and the existence of a duty. Nor has the amended complaint alleged circumstances under which these elements can be inferred.

Plaintiffs did not respond to defendants' arguments seeking to dismiss the claims for civil conspiracy as asserted in the first through third causes of action against NSCP, New State, and Christopher Estes. Accordingly, the civil conspiracy claims against them are dismissed. Dismissal of these claims is also appropriate as "[a] mere conspiracy to commit a [tort] is never of itself a cause of action" (*Alexander & Alexander of New York, Inc. v Fritzen*, 68 NY2d 968, 969 [1986] [internal quotation marks and citations omitted]). "Civil conspiracy is not recognized as an independent tort in this State" (*Mamoon v Dot Net Inc.*, 135 AD3d 656, 658 [1st Dept 2016] [internal quotation marks and citation omitted]). Moreover, these three claims lack the

requisite specificity, as only generalized, conclusory and collective allegations, based on information and belief, are asserted. Such allegations are insufficient. In light of the foregoing, the court need not address movants' other grounds for dismissal. Accordingly, the motions of the New State defendants and the Estes defendants to dismiss the first, second and third causes of action shall be granted.

B. Aiding and Abetting Fraud (Fourth Cause of Action)

As the fourth cause of action, USTH asserts an aiding and abetting fraud claim against NSCP, New State, and Christopher Estes upon information and belief, that these defendants knew that the Seller Defendants made knowingly or recklessly false misrepresentations and omissions regarding Central Conveyor's operations and financial conditions to induce USTH to enter into the sale (*id.* ¶ 173). NSCP affirmatively assisted the Seller Defendants in perpetrating this fraud by acting as Sellers' Representative, and it and New State affirmatively assisted in perpetrating the fraud by conveying to USTH misrepresentations in Article IV of the PSA that they knew to be false (*id.* ¶ 174). "Upon information and belief," the "foregoing conduct was undertaken with the willful, malicious, and oppressive intention to defraud USTH," and these "actions proximately caused the harm upon which Seller Defendants' primary liability for fraud is predicated" (*id.* ¶ 176).

Read liberally and with every favorable inference, the amended complaint fails if for no other reason that as discussed above, the amended complaint fails to state the existence of an underlying fraud. Further, it fails to satisfy the specificity requirements of CPLR 3016(b), does not adequately allege that these defendants had knowledge of the fraud and that they provided substantial assistance in the commission of the fraud. An aiding-and-abetting claim based on nondisclosure, silence or inaction requires an allegation of a duty to act (*Hoffman v RSM U.S.*

LLP, 169 AD3d 522, 523-24 [1st Dept 2019]). "To the extent the alleged assistance provided to the primary wrongdoer consisted of inaction, it was insufficient to support the aiding and abetting claims" (*Balanced Return Fund Ltd. v Royal Bank of Canada*, 138 AD3d 542,543 (1st Dept 2016) [internal citation omitted]). Insofar as Plaintiff alleges aiding and abetting fraud by omission, USTH inadequately alleged that these defendants owed it a duty to act. Accordingly, the motions to dismiss the fourth cause of action shall be granted.

C. Breach of Contract (Fifth Cause of Action)

1. Allegations

In the fifth cause of action, USTH alleges breach of contract against the Seller Defendants. It alleges that the Seller Defendants executed extensive representations and warranties contained in Article IV of the PSA, on which USTH reasonably relied (Amended Complaint, ¶¶ 177-179). During the acquisition process, it obtained, through negotiation, guarantees regarding numerous aspects of Central Conveyor's finances and operations, which USTA reasonably relied upon to formulate a fair price for Central Conveyor (*id.* ¶ 179). The Seller Defendants breached these representations and warranties, and, as previously set forth, numerous of them were materially false when made, specifically PSA Sections 4.5, 4.6, 4.8, 4.9, 4.11, 4.15 and 4.17 (*id.* ¶ 180). Except with respect to the Canada tax problem, for which Sellers' Representative have asked for more to time to evaluate, Seller has refused all indemnity demands from USTH (*id.*). The breach of warranties has caused USTH "extensive injuries," and the misconduct within Central Conveyor "has exposed USTH to extensive losses and liabilities for which it seeks recovery from Seller Defendants" (*id.* ¶ 181).

2. The Contentions Raised on the Motion of the New State Defendants

The New State defendants argue that USTH's breach of contract claim against NSCCC

fails to state a cause of action. USTH agreed that, absent fraud, it was bound by the strict limitations on liability and damages set forth in the PSA, including (i) indemnification as the contractual remedy, (ii) the definition of a covered loss, and (iii) the requirements of a demand identifying the loss. The PSA also obligates USTH to provide the requisite documentation and access to employees to permit defendants to access the claim. USTH ignored the provisions of the PSA and instead brought this complaint.

Article IX of the PSA provides that indemnification is the "sole and exclusive remedy" for a breach of the representations and warranties (R & W) contained in the PSA. It requires that USTH specifically identify a "Loss" before the indemnification obligation is triggered. Section 9.2(a) provides that Sellers, subject to various limitations, are to indemnify USTH from "any loss, liability, claim, charge, action, suit, proceeding, assessed interest, penalty, damage, Tax or expense (each a "Loss" and collectively, "Losses"), resulting from . . . (i) any breach of or inaccuracy in any representation or warranty . . . made by Sellers in Article IV." Section 9.5 requires USTH to provide an indemnification demand that "state[s] that the Indemnitee [USTH] has paid or properly accrued Losses or anticipates that it will incur liability for Losses" subject to indemnification, and "specif[ies] in reasonable detail each individual item of Loss included in the amount so stated, the date such item was paid or properly accrued," and other information.

As part of the "Indemnification Procedures for Non-Third Party Claims," the PSA requires that the party seeking indemnification "cooperate and assist the Indemnitor in determining the validity of any claim for indemnity by the Indemnity," including "providing reasonable access to and copies of information, records and documents relating to such matters, and (as reasonably requested by the Indemnitor) furnishing employees to assist in the

investigation, defense and resolution of such matters and providing legal and business assistance with respect to such matters" (*id*).

USTH served two indemnification demands. NSCCC argues that the first, dated February 8, 2019, sought indemnification for various direct claims, and USTH "conceded" in that demand letter that it was not identifying actual incurred Losses, but was instead identifying "buckets of anticipated Losses" (Supporting Memorandum of Law, 19). On February 15, 2019, NSCCC denied the indemnification requests because the Losses were not specified with the required detail and the claim was premature. NSCCC also requested information to enable it to evaluate the claims. In particular, it requested documents and access to employees. USTH failed to meet the condition precedents for indemnification. While NSCCC "followed the precise protocol set forth in the PSA" (*id.*), USTH did not and instead sued. USTH's claim "is thus legally insufficient because" it "has not– -and cannot––allege that essential conditions for indemnification have been satisfied" (*id.* 19).

NSCCC additionally argues that USTH's second demand letter, dated February 28, 2019, is similarly premature, as it sought indemnification for a third-party claim by the Canada Revenue Agency. NSCCC did not breach its indemnification obligation as the parties have agreed to hold in abeyance NSCCC's response while USTH works to resolve the claims (*id.*). Moreover, USTH has not alleged compliance with the prerequisite that claims "with respect to Pre-Closing Taxes must, if and to the extent coverage is available under the R & W Policy, be first brought under the R & W Policy" (PSA Section 9.2 [b] Doc. No. 77).

In opposition, plaintiffs contend that PSA Article IX, does not impose any precondition to suit and the PSA may not be read to so require. While PSA Section 9.2(g) limits USTH's

remedy, it does not prescribe when USTH may sue. Plaintiffs further disagree with NSCCC's reading and application of other indemnification provisions.

In reply, NSCCC argues that the salient question is whether the indemnification obligation has been triggered such that USTH can sue for breach of the indemnity provision, and for the reasons stated USTH's claim is premature. NSCCC further argues that USTH ignores PSA Sections 9.2 (a) and 9.5, which address the need for a "Loss," the incurring of that Loss, and notice identifying the Loss, before the indemnification obligation arises.

NSCCC further argues that, on the contract claim, USTH can only recover from the Indemnity Escrow Fund, and then from the representation and warranty insurance policy. USTH failed to make a timely claim to the Escrow Agent such that the Indemnity Escrow Fund would remain preserved, as required under the parties' Escrow Agreement. Those funds have been released and USTH's claims must now be addressed to the R & W Policy.

3. The Contentions Raised in Connection with the Motion of the Estes Defendants

Similar to the New State defendants, the Estes defendants argue that this cause of action fails as a matter of law as it fails to plead damages proximately caused by any of the Estes defendants. They assert that USTH fails to plead cognizable damages, and instead "pleads a laundry list of purportedly breached representations and warranties," followed by "boilerplate recitations of damages" which "fail even notice pleading requirements under New York law" (Doc. No. 73, Memorandum of Law in Support, at 10). "USTH must plead facts linking each alleged breach by an Estes Defendant to an injury caused by that breach, because proximate cause is an element of breach of contract," and USTH's failure to do so is fatal to the contract claim (*id*).

4. Analysis

To sustain a cause of cause of action for breach of contract, a plaintiff must show: (i) an agreement; (ii) plaintiff's performance; (iii) defendant's breach of that agreement; and (iv) damages (*see Furia v Furia,* 116 AD2d 694 [2d Dept 1986]). Reading allegations in the amended complaint liberally, as true, and as a whole, plaintiff has successfully alleged that the Seller Defendants and USTH entered into the PSA which provided for warranties and representations by the Seller Defendants, USTH performed its obligation(s), the Seller Defendants breached the representations and warranties in that it is exposed to a "claim . . . penalty, damage or expense" (PSA Section 9.2[a]), and USTH suffered harm and damages as a result. It alleges it is entitled to be indemnified for losses it "anticipates that it will incur" (*id.* at 9.5). The specific losses are identified in the first demand letter dated February 8, 2019 (see Doc. No. 80).

The New State defendants have not demonstrated in their motion that the claim should be dismissed as premature or that USTH failed to follow the PSA's indemnification procedures. The documents they submitted do not conclusively establish these defenses and entitlement to dismissal as a matter of law. At this early stage of the proceedings, whether USTH can ultimately prove its contract claim, whether USTH followed the indemnity procedures in the PSA, and whether USTH can recover the damages are not issues before the court.

Because USTH has stated a cause of action for breach of contract and the documentary evidence provided does not "utterly refute" Plaintiff's claim, the motions to dismiss the fifth cause of action shall be denied.

D. Breach of Implied Covenant of Good Faith and Fair Dealing and Unjust Enrichment (Sixth and Seventh Causes of Action)

1. The Allegations and Contentions

The sixth cause of action is brought by USTH against the Seller Defendants and alleges that, to the extent that the misconduct alleged in the first, second, third, and fifth causes of action is not found to be a breach of the PSA itself, the conduct is a breach of the implied covenant of good faith and fair dealing (Amended Complaint, ¶ 183). USTH alleges that the Seller Defendants owed a duty to act in good faith and to deal fairly in the contract's performance, yet, "upon information and belief," they: (i) actively and in bad faith concealed from USTH the Estes Agreement; (ii) agreed to and planned to covertly enter into the Estes Agreement to have Central Conveyor pay Larry Estes after closing an additional $300,000; and (iii) carefully studied the PSA's provisions in an attempt to create a payment obligation that, if timed correctly, would not technically breach the PSA (*id.* ¶ 185). This bad-faith surreptitious behavior was not negotiated or agreed to by USTH, and, with the other misconduct, "injured USTH's ability to receive the fruits of its purchase, namely, a company unencumbered by unknown and undisclosed contracts" (*id.* ¶ 186).

USTH brings the seventh cause of action in unjust enrichment against the Seller Defendants, New State Capital Partners LLC, New State Management LLC, Christopher Estes, and Larry Estes. It incorporates its prior allegations and asserts that these defendants are all parties who benefitted financially and were enriched by, and profited from, the sale of Central Conveyor to USTH: the Seller Defendants, who directly profited; the other named New State defendants, who profited indirectly as affiliates of NSCCC, a Seller and former majority stakeholder in Central Conveyor; Christopher Estes, an indirect holder who benefited from the sale via his father and family members; and Larry Estes, a party to a fraudulently entered into contract who received "not insignificant payments and has claimed the right to payments totaling $300,000, which he was not entitled to receive" (*id.* ¶ 189).

USTH asserts that, as set forth in paragraphs 45 through 103, "upon information and belief," these defendants benefitted and were enriched from the sale at USTH's expense by actively misleading USTH or concealing key facts from it regarding the "true nature" of Central Conveyor's operations and financial conditions (*id.* ¶ 190). Had USTH "understood" Central Conveyor's "true financial condition" as well as "the nature and scope of the unlawful practices taking place within the Company," it would not have purchased it or would have done so at a far lower price (*id.* ¶ 190). "Equity and good conscience cannot allow" these defendants "to retain the ill-gotten profit they received, directly or indirectly" from Central Conveyor's sale to USTH, and USTH seeks restitution in an amount to be determined at trial (*id.* ¶ 191).

2. Analysis

As argued by the New State defendants and the Estes defendants, these claims should be dismissed. The claim for breach of the implied covenant of good faith and fair dealing is impermissibly duplicative of the contract claim, as it arises from the same facts (*Amcan Holdings, Inc. v Canadian Imperial Bank of Commerce*, 70 AD3d 423, 426 (1st Dept 2010]; *Logan Advisors, LLC v Patriarch Partners, LLC*, 63 AD3d 440, 443 [1st Dept 2009]; *Feigen v Advance Capital Mgmt. Corp.*, 150 AD2d 281, 283 [1st Dept 1989]), and plaintiffs do not dispute the contract's existence, which covers the parties' dispute (*Clark-Fitzpatrick, Inc. v Long Is. R.R. Co.*, 70 NY2d 382, 389 [1987]). Similarly, "[a]n unjust enrichment claim is not available where it simply duplicates, or replaces, a conventional contract or tort claim" (*Corsello v Verizon New York, Inc.*, 18 NY3d 777, 790-791 [2012] [internal citations omitted]).

Even reading the allegations liberally and with every favorable inference, the court finds that plaintiffs fail to state these causes of actions. Plaintiffs' arguments to the contrary are unavailing and these claims cannot survive.

E. The Estes Defendants' Motion on the Remaining Causes of Action

1. Lack of Nexus

Initially, the Estes defendants assert that the claims for breach of fiduciary duty and breach of the Employment Agreements lack nexus to New York. They also argue for dismissal on this ground as against certain defendants for the following causes of action: conversion (alleged against DeBrabander and Kevin Estes); misappropriation of trade secrets under Michigan state and federal law (as against Christopher Estes) and trespass to chattels (alleged against Larry Estes and Christopher Estes) (Memorandum of Law in Support of Motion, at 18, 21 n 7-8, 10 [Doc. No. 73]).

The Estes defendants assert that these claims have no nexus to New York because the alleged breaches, wrongs or harm arose out of post-PSA transactions, and took place in Michigan. They assert that these causes of action relate, as applicable, to: the Employment Agreements; the relationship between these Michigan based individual defendants and Central Conveyor, a company organized under the laws of Delaware with its principal place of business in Michigan, and these Michigan-based individual defendants. They contend that there is no nexus between New York and these causes of action, and therefore no basis for this court's jurisdiction (Reply Memorandum, 8-12 [Doc. No. 106]).

Plaintiffs respond that the court has jurisdiction over these claims pursuant to the PSA's forum selection clause. The PSA provides for the "exclusive jurisdiction" of a New York court "for the purposes of any suit . . . arising out of this Agreement or any transactions contemplated hereby" (PSA Section 10.7). The Employment Agreements are transactions "contemplated" by the PSA as they are "contingent upon, and shall become effective immediately following" the closing, "pursuant to" the PSA (Employment Agreements, at 1 [Doc. Nos. 71 and 72]).

Additionally, the Employment Agreements were executed concurrently with the PSA (*id.* at 15) and provide for bonuses that are directly tied to the transfer of Central Conveyor's ownership pursuant to the PSA (*id.* Section 5). Plaintiffs argue that as these defendants' duties and compensation under their Employment Agreements are intrinsically linked to the PSA, plaintiffs' claims for breach of contract and breach of fiduciary duty belong in this court. Within the context of the conversion claim, plaintiffs argue that it implicates property that was the subject of the transaction memorialized in the PSA, and therefore this claim also belongs in this court.

The Estes defendants reply that as Central Conveyor is not a party to the PSA, it cannot rely on that forum selection clause. While in their moving papers they seek dismissal as to only specified causes of action against specified defendants due to a lack of nexus to and jurisdiction in New York, in their reply papers they assert that the court "lacks jurisdiction over the claims brought by Central Conveyor against the Estes Defendants and should dismiss" the eighth, eleventh, twelfth, thirteenth, fourteenth, fifteenth, sixteenth, seventeenth, and eighteenth counts (Reply Memorandum of Law, at 8).

The Estes defendants have not met their burden in showing that these causes of action should be dismissed pursuant to CPLR 3211 (a)(8) for lack of nexus to New York. The PSA contains a broad New York forum clause which provides that "each Party hereto irrevocably submits to the exclusive jurisdiction of any state or federal court located within the County of New York for the purposes of any suit, action or proceeding arising out of this Agreement or any transaction contemplated hereby, and agrees to commence any such action, suit or proceeding only in such courts" (PSA Section 10.7). Kevin Estes, Larry Estes, Christopher Estes and Jeffrey DeBrabander, in various capacities, are all signatories to the PSA, and the sale of Central Conveyor to USTH is its subject matter. The Employment Agreements are transactions

contemplated by the PSA because they are "contingent upon, and shall become effective immediately following" the Closing, "pursuant to" the PSA (Employment Agreements, at 1), and they were executed concurrently with the PSA. The court also notes that the Employment Agreements do not contain a forum selection clause. That part of the Estes defendants' CPLR 3211 (a)(8) motion seeking to dismiss certain causes of action due to lack of nexus shall be denied.

2. In the Conversion (Eighth Cause of Action)

The eighth claim concerns the return of a Microsoft Surface Pro 3 laptop computer (laptop) and a key fob to the company's 2018 Dodge Ram Pickup truck held by Jeffrey DeBrabander, and a laptop and an Allworx desktop phone retained by Kevin Estes (collectively, company property) (Amended Complaint, ¶¶ 192-194). The amended complaint alleges that pursuant to section 6(f) of the Employment Agreements, Central Conveyor remains the owner of the company property, and DeBrabander and Kevin Estes are required to return it "promptly" upon termination (*id.* ¶¶ 195-196). Despite Central Conveyor's requests and multiple demands, DeBrabander and Kevin Estes continue to possess company property, and their "continued possession constitutes an unauthorized and wrongful assumption of control and dominion" over Central Conveyor's "unconditional possession of property, to the exclusion of" its possessory right (*id.* ¶¶ 197-198). The Estes defendants argue that the conversion claim must be dismissed as it does not allege any wrong distinct from defendants' contractual obligations under the Employment Agreements. They argue, accordingly, that the conversion claim is duplicative and the alleged wrongful acts cannot support an independent claim for conversion.

Plaintiffs respond that these defendants owe a duty independent of the Employment Agreements not to retain company property, and that, accordingly, the cause of action for conversion is not duplicative of the contract claim and the motion should be denied.

This branch of the motion must be granted. The conversion claim is duplicative of the contract claim. While "a conversion claim cannot be brought where the property right alleged to have been converted arises entirely from the [plaintiff's] contractual rights, a conversion claim and contract claims are not always incompatible" (*Llewellyn-Jones v Metro Prop. Group, LLC*, 22 F Supp 3d 760, 788 [ED Mich 2014] [internal quotations marks and citations omitted]). A party's conduct may result in both a tort for common law conversion and a breach of contact, "so long as the defendant's conduct constituted a breach of duty separate and distinct from the breach of contract" (*id.*; see also *Fesseha v TD Waterhouse Inv. Servs., Inc.*, 305 AD2d 268, 269 [1st Dept 2003]). Here, the amended complaint does not sufficiently allege independent facts that give rise to a claim for the common law tort of conversion liability. This part of the Estes defendants' motion is granted.

3. Declaratory Relief (PSA Section 6.10) (Ninth Cause of Action)

In the ninth cause of action, USTH seeks declaratory relief against Kevin Estes, Jeffrey DeBrabander, and Christopher Estes, with respect to PSA Section 6.10, which includes non-competition and non-solicitation provisions (Amended Complaint, ¶ 199-206). USTH alleges that, pursuant to CPLR 3001, a justifiable controversy exists regarding enforceability of this section (Amended Complaint, ¶ 206), as Christopher Estes has already breached the provision by his employment with a competitor (*id.* ¶ 200), and Kevin Estes and DeBrabander have asserted that these provisions are void and unenforceable (*id.* ¶ 201).

As plaintiffs correctly note, the Estes defendants do not address this cause of action in their supporting memorandum of law (Plaintiffs' Memorandum of Law in Opposition, at 35 n 7). Neither the language in the notice of motion nor the Estes defendants' blanket, all-purpose request within the supporting papers for dismissal, is sufficient to meet movants' burden with respect to this cause of action for declaratory relief.

In any event, this claim is sufficiently pleaded to state a cause of action for declaratory relief. CPLR 3001 states that "[t]he supreme court may render a declaratory judgment having the effect of a final judgment as to the rights and other legal relations of the parties to a justiciable controversy whether or not further relief is or could be claimed." To the extent, if at all, the Estes defendants' motion can be read as seeking to dismiss the ninth cause of action, it is denied.

4. Breach of Contract (Tenth Cause of Action)

The tenth cause of action alleges that, following termination of his employment from Central Conveyor, Christopher Estes, in violation of PSA Section 6.10, took employment at Commercial Contracting Corporation (CCC), a competing company that is located roughly 25 miles from Central Conveyor (Amended Complaint, ¶¶ 207-211). USTH alleges that this breach has exposed USTH to losses and liabilities and exposes it to the risk of immediate and irreparable, non-quantifiable harm for which monetary compensation is inadequate (*id.* ¶ 211).

As correctly noted by plaintiffs, the Estes defendants do not address this cause of action in their supporting memorandum of law (Plaintiffs' Memorandum of Law in Opposition, at 35 n 7). It is unclear whether the Estes defendants attempt to do so in their reply memorandum of law, which reference arguments that were made with respect to the fifth cause of action and replies to plaintiffs' arguments regarding same. The court will not consider new grounds for relief or new non-responsive arguments raised for the first time in reply papers. The Estes defendants' general

request as set forth in their notice of motion to dismiss the amended complaint, without a particularized argument within their supporting papers for this relief as to tenth cause of action, is insufficient to meet movants' burden.

To sustain a cause of cause of action for breach of contract, a plaintiff must show: (i) an agreement; (ii) plaintiff's performance; (iii) defendant's breach of that agreement; and (iv) damages (*see Furia v Furia,* 116 AD2d 694 [2d Dept 1986]). Here, reading the amended complaint's allegations liberally, as true, and as a whole, plaintiff successfully asserts a cause of action for breach of contract. The Estes defendants' motion to dismiss this cause of action shall be denied.

5. Declaratory Relief for Breach of Employment Agreements (Eleventh & Twelfth Causes of Action)

In the eleventh cause of action, as against Kevin Estes and DeBrabander, USTH seeks a declaration that the non-competition clauses of the Employment Agreements, as set forth in Section 6(a) (Doc. Nos. 71 & 72), are enforceable and that these defendants are bound by its restrictions (Amended Complaint, ¶¶ 212-220). USTH alleges, *inter alia,* that defendants have taken the position that these provisions are void and unenforceable (*id.* ¶ 215), and that pursuant to CPLR 3001, a justifiable controversy exists regarding the provision's enforceability.

In the twelfth cause of action, USTH alleges, *inter alia*, that, pursuant to CPLR 3001, a justiciable controversy exists regarding Kevin Estes and DeBrabander's employment termination for cause, pursuant to Section 7 of their Employment Agreements, as these defendants have taken the position that their employment termination was not for cause and that Central Conveyor owes them severance pay (*id.* ¶¶ 221-226). USTH requests a judicial declaration that

Central Conveyor "was entitled to, and did" terminate the employment of Kevin Estes and DeBrabander for cause, pursuant to Section 7 of their Employment Agreements (*id.* ¶ 226).

The Estes defendants move to dismiss these claims for lack of standing, as USTH is not a party to the Employment Agreements and is not an intended beneficiary (see CPLR 3001). Section 10(o) of the Employment Agreements, includes a provision disclaiming enforcement by third parties.

In response, plaintiffs state only that the "Court should decline to dismiss the claims on this technical ground," or, alternatively, grant them leave to amend to plead on behalf of Central Conveyor (Doc. 96, at 37 n 9). The Estes defendants reply that granting leave to amend "would be futile, given the lack of jurisdiction over claims between Central Conveyor and the Estes Defendants" (Doc 106, at 10 n 10).

The motion shall be granted with leave to replead. USTH lacks standing as it is not a party to the Employment Agreements. Standing is not merely a technical requirement and dismissal here is appropriate. The Estes defendants have not shown why amending these claims so as to assert them on behalf of Central Conveyor fails to state causes of action pursuant to CPLR 3001. That branch of the motion seeking dismissal of the eleventh and twelfth causes of action shall be granted with leave to replead.

6. Breach of Contract (Thirteenth Cause of Action)

In the thirteenth cause of action, Central Conveyor alleges that Kevin Estes and DeBrabander breached Section 6(f) of their Employment Agreements by failing to return computers containing "confidential, proprietary, and potentially trade secret" information (*id.* ¶¶ 231-232). They "may also be in possession of thumb drives and external hard drives that could potentially contain" such information (*id.* ¶ 232). Further, pursuant to Section 2 of their

Employment Agreements, Kevin Estes and DeBrabander were each required to "serve the Company and its subsidiaries faithfully and to the best of his ability" (*id.* ¶ 236). They breached this obligation by their participation in the customer kickback scheme, the illegal "Cash Option," false time card submissions, a fraudulent scheme to conceal the Estes Agreement, improper use of company assets for personal expenses, and other conduct which constituted grounds for and necessitated their employment terminations for cause (*id.* ¶ 238).

The Estes defendants argue that Central Conveyor's claim "fails because it does not plausibly allege damages arising from any breach of their respective employment agreements" (Memorandum of Law in Support, at 16). Plaintiffs fail to adequately plead any cognizable damages and instead only generally allege exposure to losses and liabilities. This claim is defective as it alleges damages purportedly suffered by USTH, not Central Conveyor. USTH is not a party to the Employment Agreement and cannot enforce its terms. Additionally, the claim is "facially defective" because it claims damages for amounts paid to these defendants during the time period in which they were in breach, Illinois law does not allow an employer to claw back an employee's pay, and the only remedy available is employment termination for cause.

Central Conveyor argues that it has pleaded cognizable damages pursuant to Illinois law, which requires that a plaintiff must allege the existence of damages resulting from the breach, but does not require that a plaintiff plead a legal theory for calculating the damages. Central Conveyor has cleared this bar by alleging losses and liabilities attributable to the improper retention of its property and these defendants' active engagement in illegal and unethical conduct.

USTH is not a party to the Employment Agreements and cannot assert a claim for damages. The claim shall be dismissed on this ground, with leave to amend paragraphs 235 and 239 of the Amended Complaint so as to substitute Central Conveyor in lieu of USTH.

That branch of the Estes defendants' motion seeking to dismiss the thirteenth cause of action shall be denied. Reading the allegations of this claim liberally, as a whole, and as true, and affording the claim the benefit of every possible inference, the claim survives. Central Conveyor has sufficiently alleged the elements for breach of contract, including damages, under Illinois law, which governs under Section 10(a) of the Employment Agreements. The allegations also meet the pleading standards to breach of contract under New York Law (see *Bankers Life & Cas. Co. v Am. Senior Benefits LLC*, 2017 IL App [1st] 160687, *4) [internal citation omitted]). Whether Illinois law allows for the claw back these defendants wages need not be decided at this time, as Central Conveyor otherwise sufficiently alleges damages. This and issues as to whether plaintiff Central Conveyor can prove its claim and its damages shall be left to another stage of the proceedings.

7. Breach of Fiduciary Duty (Fourteenth Cause of Action)

As to the fourteenth cause of action for breach of fiduciary duty, plaintiffs assert that until their terminations, Kevin Estes and DeBrabrander served Central Conveyor as, respectively, Chief Operating Officer and Vice President of Sales & Estimating, and owed a fiduciary duty to the company (Amended Complaint, ¶¶ 241-242). These defendants breached their fiduciary duties by engaging in unlawful activities, listed above (*see* Background, *supra* at 6-7), a fraudulent scheme to conceal the Estes Agreement and the improper use of Central Conveyor's assets for personal expenses (*id.* ¶ 243). The misconduct continued after the closing, including Kevin Estes' charging $9,000 of a $25,000 bill for personal accounting services to Central

Conveyor's credit card and charging other large amounts for personal vacation and travel; DeBrabander expensing similar amounts for theatre/event tickets, travel, meals, and significant liquor purchases which "upon information and belief, were expended for illegitimate and/or personal purposes." DeBrabander also "approv[ed] false time cards of employees including Christopher Estes" (*id.* ¶ 244).

As to USTH's claim for breach of fiduciary duty, the claim shall be dismissed for failure to state a cause of action because a fiduciary relationship does not exist between parties involved in an arm's length commercial transaction as is the case between the USTH and the Estes defendants (*see Northeast Gen. Corp. v Wellington Adv., Inc.* 82 NY2d 158, 162 [1993]). Regarding Central Conveyor's claim for breach of fiduciary duty, the Estes defendants assert that the claim should be dismissed because the "purported fiduciary relationship between Michigan-based officers of a Michigan based company, organized under Delaware law, has no nexus to New York, nor have Plaintiffs attempted to plead one" (Memorandum of Law in Support, at 14). The court has previously addressed this argument and finds to the contrary.

The Estes defendants have not asserted that the amended complaint suffers from any other pleading infirmity or fails to state a cause of action. Nor do they argue that the court in determining this part of the motion, should apply the law of another state which differs from the law of New York (whether that law is that of Michigan, New York, or Illinois).[2]

In New York, plaintiffs who bring a claim for breach of fiduciary duty, "must allege that (1) defendant owed them a fiduciary duty, (2) defendant conducted misconduct, and (3) they suffered damages caused by that misconduct" (*Burry v Madison Park Owner LLC* (84 AD3d

[2] Pursuant to Section 10 (a) of the Employment Agreements [Doc. Nos. 71 and 72], the law of Illinois governs the Employment Agreements and the "legal relations thus created between the parties hereto."

699, 699-700 [1st Dept 2011] [internal citations omitted]). A fiduciary relationship "is grounded in a higher level of trust than normally present in the marketplace between those involved in arm's length business transactions" (*EBC I, Inc. v Goldman, Sachs & Co.*, 5 NY3d at 19). "[I]t is elemental that a fiduciary owes a duty of undivided and undiluted loyalty to those whose interests the fiduciary is to protect" (*Birnbaum v Birnbaum*, 73 NY2d 461, 466 [1989] [internal citations omitted]). Corporate officers are in a fiduciary relationship with that corporation, owe their corporation undivided and unqualified loyalty, should not profit personally at the corporation's expense, and must discharge their duties in good faith (*see Foley v D'Agostino*, 21 AD2d 60, 66-67 [1st Dept 1964]). Determining whether a fiduciary relationship exists "inevitably requires a fact-specific inquiry" (*Eurycleia Partners, LP*, 12 NY3d at 561).

Reading the allegations liberally, assuming them to be true, and affording every favorable inference, the amended complaint sufficiently sets forth Central Conveyor's cause of action for breach of fiduciary duty. It alleges that: (i) Kevin Estes and DeBrabander, as corporate officers, owed a fiduciary duty to the company; (ii) these defendants engaged in misconduct, by, *inter alia*, participating in the customer kickback scheme and multiple unlawful employment related schemes as listed above; and (iii) Central Conveyor suffered damages by reason of their misconduct. The claims asserted by USTH shall be dismissed while those asserted by Central Conveyor survive.

8. Computer Fraud and Abuse Act (Fifteenth Cause of Action)

In the fifteenth cause of action, Central Conveyor asserts a violation of the Computer Fraud and Abuse Act (18 USC § 1030, et seq.) (CFAA) as against Christopher Estes. Central Conveyor alleges that after Christopher Estes's employment was terminated on January 30, 2019, he failed to immediately return the company owned laptop computer (company laptop) and

continued to access it without authorization for several days (Amended Complaint, ¶ 247). The company laptop was used to conduct Central Conveyor's business across the United States, including Christopher Estes' management of sales to customers located in multiple states (*id.* ¶ 248).

Additionally, Christopher Estes intentionally accessed the company laptop to copy files onto a personal hard drive, thereby obtaining information he was not then authorized to access (*id.* ¶ 249), and downloaded files and deleted contents of his email account, "all with an intent to defraud" Central Conveyor by "stealing" its property and information (*id.* ¶ 250). While Central Company was able to restore the contents of this email account, Christopher Estes was successful at obtaining Central Conveyor's data and "thus furthered this fraud and obtained a thing of value through these acts" (*id.* ¶ 250). These "acts were part of a broader pattern of conduct evidencing an intent to defraud which included, among other things, seeking to gain access to the Company's computer network through the account of Central Conveyor's CEO, Rick Wells" (*id.*) Central Conveyor "incurred losses far exceeding $5,000 as a result of Christopher Estes' intentional and unauthorized conduct" (*id.* ¶ 251). In particular, plaintiffs expended "considerable resources far in excess of $5,000 in responding to Christopher Estes' conduct and conducting a forensic review to assess the scope of his activity" (*id.*).

The Estes defendants argue that this cause of action must be dismissed as Central Conveyor failed to plead "damage or loss" in excess of $5,000, as required by the CFAA or to provide facts to show impairment to the integrity or availability of data, a program, a system or information.

Plaintiffs reply that they have sufficiently pleaded damage or loss to satisfying the statutory requirements. Plaintiffs also assert that they are still "uncovering data stolen" by

Christopher Estes through their forensic review of company devices (Doc. 96, at 41 n 12). Plaintiff's point to correspondence, actions, and events following the court's April 8, 2019 order that, *inter alia*, directed the Estes defendants to return company-owned devices in their possession, to search for devices containing plaintiffs' data, and to immediately make available for plaintiffs' forensic analysis any devices that they are aware of that contain any of plaintiffs' documents or data (Doc. 47).

In their reply, the Estes defendants argue that plaintiffs attempt to revive this (and other) claims by relying on the Sullivan Affirmation (Doc. 97), and to smear them, by focusing on their conduct after the complaint was filed. They contest the substance of the Sullivan affirmation, assert that the affirmation is irrelevant, and that plaintiffs' "bluster and exaggerated outrage regarding the devices are merely a distraction from the actual issues here—Plaintiffs' deficiently pled claims" (Doc. 106, at 12).

The Estes defendants also assert that the Sullivan Affirmation "contains allegations related to devices owned by a Delaware LLC headquartered in Michigan and the retention of those devices by Michigan-resident former employees" (*id.*), and that this court is not the proper forum to resolve these disputes. They further assert that any "purported facts" raised in the Sullivan Affirmation about the devices and the Estes defendants' conduct as to the devices' return "do not serve to establish jurisdiction over Central Conveyor's claims in this Court" (*id.*).

The motion seeking to dismiss the CFAA claim for failure to state a cause of action is denied. The statute criminalizes, *inter alia*, "intentionally access[ing] a computer without authorization . . . and thereby obtain[ing] . . . information from any protected computer" (18 USC § 1030 [a][2][C]), and "intentionally access[ing] a protected computer without authorization, and as a result of such conduct, caus[ing] damage and loss" (18 USC § 1030 [a][5][C]). Additionally,

the CFAA provides a civil cause of action if a defendant's wrongful conduct causes one of the enumerated types of loss or damage as set forth in the statute (18 USC § 1030 [g]). The statutory definition of loss includes "any reasonable cost to any victim, including the cost of responding to an offense, conducting a damage assessment, and restoring the data program, system, or information to its condition prior to the offense" (18 USC § 1030 [e][11])." Under the CFAA, the term loss includes costs of investigating security breaches and responding to the offense, regardless of whether there is any actual data damage or service interruption (*Univ. Sports Pub. Co. v Playmakers Media Co.*, 725 F Supp 2d 378, 387 [SD NY 2010]).

The amended complaint alleges, among other things, that following termination of his employment, Christopher Estes intentionally and without authorization accessed the company laptop and obtained information, which conduct resulted in Central Conveyor incurring losses far exceeding $5,000 in responding to his conduct and for a forensic review. The court previously addressed the Estes defendants' arguments regarding nexus and forum. Reading the allegations liberally and as true, the amended complaint sufficiently sets forth a cause of action under the CFAA. The fifteenth cause of action survives.

9. Misappropriation of Trade Secrets (Sixteenth and Seventeenth Cause of Action)

In the sixteenth cause of action for violation of the Michigan Uniform Trade Secrets Act (M.C.L. § 445.1091, *et seq.* [MUTSA]), Central Conveyor alleges that during his tenure as its employee and throughout his employment, Christopher Estes had access to proprietary and trade secret information, including: employee compensation data, pricing and customer proposals, customer lists, contractual agreements, intellectual property, financial statements or data, production processes and prototypes, engineering data and information and marketing/sales strategies (Amended Complaint, ¶ 253). Following his termination, Christopher Estes accessed

this company information without authorization (*id.* ¶ 254), and, between January 30, 2019 and February 4, 2019, he transferred large swaths of the data to a personal hard drive (*id*). He then unsuccessfully attempted to delete certain data from the company-owned laptop computer prior to his returning it on February 14, 2019 (*id*).

In the seventeenth cause of action, Central Conveyor alleges essentially the same conduct which it states violated the Defend Trade Secrets Act (DTSA), 18 USC Section 1836, *et seq.* (*id.* ¶¶ 266-71).

The Estes defendants argue that these two causes of action should be dismissed as Central Conveyor failed to adequately allege trade secret misappropriation. They assert that the elements for trade secret misappropriation under MUTSA and DTSA substantially overlap and, under both statutes, a plaintiff must establish the existence of a trade secret, defendant's acquisition of the trade secret, and unauthorized use of the trade secret. The allegations concerning a customer list and "detailed schematics" are insufficient to show that these qualify as trade secrets. Central Conveyor failed to set forth details showing that the customer list was anything other than a compilation of customer names, contact information, and other basic publicly available information. They additionally argue that allegations regarding the schematics are vague and fail to provide sufficient details regarding the nature of the schematics, such as to what they relate, when they were created, and with whom they may have been shared. General, categorical descriptions of alleged trade secrets are insufficient to state a claim.

Plaintiffs argue that the allegations are sufficient to state causes of action under both statutes. The amended complaint not only alleges that Christopher Estes misappropriated customer lists and detailed schematics, it also alleges that he stole "quotes to customers which reveal non-public pricing information as well as the Company's profit margins" and "customer

agreements" (Amended Complaint, ¶ 123), which have been held to constitute trade secrets. Additionally, Christopher Estes misappropriated "non-public compilations of information regarding parts, suppliers, pricing for spare parts, and wage data paid for certain services" (*id.*), a trade secret category that the Estes defendants failed to address.

Further, with respect to whether a customer list qualifies as a trade secret, the cases cited by the Estes defendants were in the context of motions for a temporary restraining order and summary judgment, not a motion to dismiss, and the courts examined the nature of the particular customer lists before them in determining that those customer lists were not trade secrets as they were compiled from public sources, or otherwise were not trade secrets as the former employee was not bound by a confidentiality agreement. With respect to the detailed schematics, that allegation, in context, reads that Christopher Estes misappropriated "numerous proprietary blueprints, drawings, and schematics, including detailed drawings that were not shared with customers" (*id.* ¶ 123), and therefore, at the pleading stage, the amended complaint sufficiently spelled out the nature of the trade secrets clearly enough without divulging its content.

The Estes defendants' motion to dismiss these two claims is denied. The elements for trade secret misappropriation under MUTSA and DTSA overlap as both require a plaintiff to show the existence of a trade secret, defendant's acquisition of the trade secret, and unauthorized use of the trade secret (*compare* MCL 443.1902-1905 and *Polytorx, LLC v Univ. of Michigan Regents,* No. 318151, 2015 WL 2144800, at *6 [Mich Ct App 2015] *with* 18 USC 1839(5) and *Free Country Ltd. v Drennen*, 235 F Supp 3d 559, 565 [SD NY 2016]). MUTSA "defines a trade secret as 'any information, including a formula, pattern, compilation, program, device, method, technique, or process' that 'derives independent economic value . . . from not being generally known to . . . other persons who can obtain economic value from its disclosure or use' and is 'the

subject of efforts that are reasonable under the circumstances to maintain its secrecy'" (*Polytorx, LLC*, 2015 WL 2144800, at *6). Under the DTSA, a party must show "an unconsented disclosure or use of a trade secret by one who (i) used improper means to acquire the secret, or, (ii) at the time of disclosure, knew or had reason to know that the trade secret was acquired through improper means, under circumstances giving rise to a duty to maintain the secrecy of the trade secret, or derived from or through a person who owed such a duty" (*Free Country Ltd v Drennen*, 235 F Supp 3d 559, 565 [SD NY 2016]).

Reading the allegations liberally and assuming them to be true for purposes of this motion, plaintiff Central Conveyor has sufficiently pleaded these causes of action. Whether it can ultimately prove violations of the MUTSA and DTSA is not now before the court. The Estes defendants' motion to dismiss the sixteenth and seventeenth causes of action is denied.

10. Trespass to Chattels (Eighteenth Cause of Action)

In the eighteenth cause of action, Central Conveyor alleges trespass to chattels as against Christopher Estes and Larry Estes. The claim is based on the facts described above in connection with the failure to return company laptops and misappropriation of information stored thereon (Amended Complaint, ¶¶ 273-78). The Estes defendants argue that the amended complaint fails to allege the essential element of actual damages, as it fails to allege any harm to the property and alleges only a temporary deprivation of access to the devices. In support, they cite both Michigan and New York cases. Plaintiffs respond that the amended complaint states a cause of action, as it alleges actual damages in that, as applicable, these defendants deprived Central Conveyor access to its devices, deprived the company of the password to access the device, or copied onto a personal hard drive company data not shared with competitors.

At the pleading stage, liberally construing the allegations and taking the allegations as true, the court finds that plaintiffs have stated a cause of action for common law trespass to chattels, the elements for which are similar whether the governing law be that of Illinois, New York, or Michigan. "Trespass to chattels involves an injury to or interference with possession of personal property" (*Glen Ellyn Pharmacy, Inc. v Kloudscript, Inc.*, 2019 WL 6467319, *3 [ND Ill 2019], and the tort can be committed by "intentionally (a) dispossessing another of the chattel, or (b) using or intermeddling with a chattel in the possession of another" (*id.*) (citing Restatement [Second] of Torts § 217). "To establish a trespass to chattels, [plaintiff] must prove that [defendant] intentionally, and without justification or consent, physically interfered with the use and enjoyment of personal property in [plaintiff's] possession and that [plaintiff] was harmed thereby" (*School of Visual Arts v Kuprewicz*, 3 Misc 3d 278, 281[Sup Ct New York County 2003, Richter, J.]; *see also Jackie's Enters., Inc. v Belleville*, 165 AD3d 1567, 1572 [3d Dept 2018]; *J. Doe No. 1 v CBS Broadcasting, Inc.*, 24 AD3d 215, 215 [1st Dept 2005]; *Price v High Pointe Company, Inc.*, 493 Mich 238, 253 n 8 [2013]). The element of harm or damages can be met in circumstances where the owner is deprived of possession of the chattel, which, by necessity, causes actual damage (*id.*).

Here, Central Conveyor has successfully alleged a cause of action. Whether and to what extent the alleged wrong continued beyond the April 8, 2019 order, whether the harm or damages sustained by Central Conveyor is nominal or substantial, and whether plaintiffs can ultimately prove their allegations, are not issues to be addressed at this stage of the litigation. The Estes' defendants' motion to dismiss this claim for failure to state a cause of action is denied.

CONCLUSION

A. The Motion of the New State Defendants (Mot. Seq. No. 006)

The New State defendants' motion to dismiss (Mot. Seq. No. 006) is granted as to the first, second, third, fourth, sixth and seventh causes of action and denied as to the fifth cause of action.

B. The Motion of the Estes Defendants (Mot. Seq. No. 007)

The Estes defendants' motion to dismiss (Mot. Seq. No. 007) is granted in part and otherwise denied as described below. The first, second, third, fourth, sixth, seventh, eighth, eleventh and twelfth causes of action are dismissed. The motion is denied as to the fifth, ninth, tenth, thirteenth, fifteenth, sixteenth, seventeenth, and eighteenth causes of action. Plaintiffs are granted leave to amend the thirteenth cause of action to correct the apparent clerical errors appearing in paragraphs 235 and 239, so as to substitute the name of Central Conveyor in lieu of USTH. Plaintiffs may replead the eleventh and twelfth causes of action to substitute Central Conveyor as the plaintiff employer. As to the fourteenth cause of action, the motion is granted with respect to the claim asserted by plaintiff USTH and denied with respect to the cause of action asserted by Central Conveyor.

Accordingly, it is hereby

ORDERED that the motion of the New State defendants to dismiss (Mot. Seq. No. 006) is granted as to the First, Second, Third, Fourth, Sixth and Seventh causes of action and otherwise denied; and it is further

ORDERED that the motion of the Estes defendants to dismiss (Mot. Seq. No. 007) is granted as to the First, Second, Third, Fourth, Sixth, Seventh and Eighth causes of action; and it is further

ORDERED that the motion is granted as to the Eleventh, Twelfth, Thirteenth and Fourteenth causes of action with leave to replead as described in the "conclusion" section of this decision and order; and it is further

ORDERED that plaintiffs may serve and file a second amended complaint, within 20 days of movants' service of notice of entry and answers shall be served and e-filed within 20 days thereafter; and it is further

ORDERED that if plaintiffs do not file a second amended complaint in a timely manner the remaining defendants shall serve and file their answer to the remaining allegations in the amended complaint within 40 days of service of notice of entry of this order; and it is further

ORDERED that all parties shall appear for a preliminary conference on October 27, 2020, at 10:30 am in Part 49, Courtroom 252, 60 Centre Street, New York, New York, but if Part 49 is open not for in-person appearances counsel shall appear on that day remotely as provided by the court. On or about October 21, 2020 Plaintiff's counsel shall contact Mr. Rivera (mrivera@nycourts.gov) to confirm the time of appearance and provide e-mail addresses for all scheduled participants.

Dated: August 17, 2020

O. PETER SHERWOOD, J.S.C.