**Alesco Preferred Funding VIII, Ltd. v ACP Re, Ltd.**

2021 NY Slip Op 30952(U)

March 25, 2021

Supreme Court, New York County

Docket Number: 655881/2017

Judge: Andrew Borrok

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# SUPREME COURT OF THE STATE OF NEW YORK
# NEW YORK COUNTY

**PRESENT:** **HON. ANDREW BORROK** **PART** **IAS MOTION 53EFM**

***Justice***

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**INDEX NO.** 655881/2017

**MOTION DATE** 01/17/2020, 01/17/2020

**MOTION SEQ. NO.** 004 005

ALESCO PREFERRED FUNDING VIII, LTD., ALESCO PREFERRED FUNDING XI, LTD., ALESCO PREFERRED FUNDING XII, LTD., ALESCO PREFERRED FUNDING XIII, LTD., ALESCO PREFERRED FUNDING XIV, LTD., HILDENE OPPORTUNITIES MASTER FUND II, LTD., NFC PARTNERS, LLC,NFC INSURANCE PARTNERS, LLC,WOLF RIVER OPPORTUNITY FUND LLC,WOLF RIVER PARTNER FUND, WT HOLDINGS, INC.,PREFERRED TERM SECURITIES XVI, LTD., PREFERRED TERM SECURITIES XXIII, LTD, PREFERRED TERM SECURITIES XXIV, LTD., PREFERRED TERM SECURITIES XXVIII, LTD.,

Plaintiff,

- v -

ACP RE, LTD., ACP RE HOLDINGS, LLC, AMTRUST FINANCIAL SERVICES, INC., CASTLEPOINT BERMUDA HOLDINGS, LTD., CASTLEPOINT MANAGEMENT CORP., INTEGON NATIONAL INSURANCE COMPANY, NATIONAL GENERAL HOLDINGS CORP., PRESERVER GROUP, INC., TECHNOLOGY INSURANCE COMPANY, INC., TOWER GROUP, INC., TOWER GROUP INTERNATIONAL, LTD., WILLIAM DOVE, WILLIAM FOX, WILLIAM HITSELBERGER, MICHAEL LEE, HERBERT LEMMER, ELLIOT OROL, WILLIAM ROBBIE, JAMES ROBERTS, STEVEN SCHUSTER, ROBERT SMITH, JAN VAN GORDER, AUSTIN YOUNG, MEGHAN ZEIGLER, GEORGE KARFUNKEL, LEAH KARFUNKEL, ESTATE OF MICHAEL KARFUNKEL, BARRY ZYSKIND, MICHAEL KARFUNKEL FAMILY 2005 TRUST, MICHAEL KARFUNKEL 2005 GRANTOR RETAINED ANNUITY TRUST

Defendant.

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**DECISION + ORDER ON MOTION**

The following e-filed documents, listed by NYSCEF document number (Motion 004) 188, 189, 190, 191, 192, 193, 198, 199, 200, 201, 202, 203, 204, 205, 215, 230

were read on this motion to/for DISMISS.

The following e-filed documents, listed by NYSCEF document number (Motion 005) 194, 195, 206, 207, 208, 216, 231

were read on this motion to/for DISMISS.

The critical issue on these motions to dismiss is the extent to which the amended complaint is barred by certain injunctions entered in a California conservation proceeding. Because the California court ruled in the May 2019 California Order (defined below) that virtually all of the claims in the original complaint "with the exception of the breach of contract claim against the TruPS Issuers, violate the terms of this Court's injunctions and court-approved releases, and may not be pursued" by the plaintiffs, (i) ACP Re, Ltd. (**ACP**), ACP Re Holdings, LLC, AmTrust Financial Services, Inc. (**AmTrust**); CastlePoint Bermuda Holdings, Ltd. (**CP Bermuda**), CastlePoint Management Corp. (**CP Management**), Integon National Insurance Company, National General Holdings Corp.; Preserver Group, Inc. (**Preserver**); Technology Insurance Company, Inc., Tower Group, Inc. (**Tower**), Tower Group International, Ltd. (**TGIL**), George Karfunkel, Leah Karfunkel, Estate Of Michael Karfunkel, Barry Zyskind, Michael Karfunkel Family 2005 Trust, and Michael Karfunkel 2005 Grantor Retained Annuity Trust's (together, the **Karfunkel Defendants**) motion (Mtn. Seq. No. 006) to dismiss the amended complaint pursuant to CPLR 3211(a)(1), (a)(3), (a)(5) and (a)(7), and (ii) William F. Dove, William F. Fox, Jr., William E. Hitselberger, Michael H. Lee, Herbert Lemmer, Elliot S. Orol, William A. Robbie, James E. Roberts, Steven W. Schuster, Robert S. Smith, Jan R. Van Gorder, Austin P. Young, III, and Meghan Zeigler's (together, the **Director & Officer Defendants**) motion (Mtn Seq. No. 007) to dismiss the amended complaint pursuant to CPLR 3211 (a)(1), (a)(3), (a)(5), (a)(7) and (a)(8) and Rule 3016(b) are granted in part, without prejudice, with respect to all claims except for breach of contract, tortious interference with contract and the stand alone fraud (the 1st through 4th causes of action).

## THE RELEVANT FACTS

This is the second motion to dismiss many of the claims that have been brought in this action. The plaintiffs, who are each holders of trust preferred securities known as **TruPS**, issued by trusts that were established by one of more of the issuer defendants: Tower, CP Bermuda, CP Management and Preserver (collectively, the **Issuers**), filed the original complaint in this action in September of 2017 (NYSCEF Doc. No. 6). Each of the Issuers is an insurance holding company that derived all of its revenue from operating insurance company subsidiaries (the **Insurance Companies**), whose deteriorating loss experience rendered them unable to pay dividends to the Issuers. The Issuers then became insolvent and unable to pay the TruPS. The TruPS have been in default for years. The plaintiffs claim they are owed more that $220 million, including interest. The defendants do not dispute that the plaintiffs may have breach of contract claims against the Issuers. The Issuers are, however, at this point, empty shell companies. The plaintiffs allege that the defendants are the alter egos or successors of the Issuers and assert claims for breach of contract, fraudulent conveyance and breach of fiduciary duty.

More specifically, the original complaint was asserted against all of the 31 defendants currently named in this action, plus ten additional defendants.[1] In the original complaint, the plaintiffs asserted the following ten causes of action: (i) breach of contract (against the Issuers, TGIL and ACP), (ii) tortious interference with contractual relations (against the Karfunkel Defendants), (iii) breach of fiduciary duty (against ACP and the Director & Officer Defendants), (iv) aiding and abetting breach of fiduciary duty (against the Karfunkel Defendants), (v) fraudulent

[1] The ten former defendants no longer named in the Amended Complaint are Trinette Weikl, Robert Karfunkel, Barry S. Karfunkel 2016 GST Trust, Barry D. Zyskind GST Trust, Chesed Foundation of America, Gevurah, 2012 Karfunkel Family Trust, Leah Karfunkel 2016-AMT GRAT, Robert M. Karfunkel 2016 GST Trust, and Teferes Foundation (NYSCEF Doc. No. 6).

conveyance (against the Kafunkel Defendants), (vi) conveyance made with intent to defraud (against the Karfunkel Defendants and Tower), (vii) conspiracy to commit fraudulent conveyance (against the Karfunkel Defendants, the Issuers and TGIL), (viii) quantum meruit/unjust enrichment (against the Karfunkel Defendants), (ix) alter ego liability (against the Karfunkel Defendants and ACP), and (x) successor liability (against the Karfunkel Defendants (NYSCEF Doc. No. 6, ¶¶ 271-329).

The claims in the amended complaint are not materially different from the ten causes of action asserted in the original complaint (*see* NYSCEF Doc. No. 6 at 68-77). As the plaintiffs themselves explained in their memorandum of law in support of their prior motion to amend (seq. no. 003), "the []Amended Complaint refines, clarifies, and in some places amplifies, but it does not dramatically change either the legal theories asserted or the facts relied upon" (NYSCEF Doc. No. 110 at 2). To wit, the gravamen of both the original complaint and the amended complaint is that in 2013 and 2014, the Karfunkel Defendants and certain entities that they dominate and control, which the plaintiffs allege function as a group and are alter egos of each other, sought to take advantage of Tower's financial distress by engaging in a series of transactions with Tower that triggered certain successor provisions of the Indentures, without having that successor entity expressly assume the TruPS' obligations and are seeking to avoid them now. The amended complaint asserts twelve causes of action as follows: (i) breach of contract (based on failure to pay TruPS, against the Issuers and the Issuers' successors, TGIL and ACP), (ii) breach of contract (based on alleged improper cash payment to shareholders, distribution of liquidation payments, against the Issuers and the Issuers' Successors, TGIL and ACP), (iii) tortious interference with contractual relations (against the Karfunkel Defendants),

(iv) fraud (against TGIL and the Officer & Director Defendants), (v) aiding and abetting fraud (against the Karfunkel Defendants), (vi) breach of fiduciary duty (against ACP, the Officer & Director Defendants), (vii) aiding and abetting breach of fiduciary duty (against the Karfunkel Defendants), (viii) fraudulent conveyance (based NY Debtor Creditor Law §§ 273-275 or such other forum equivalent as may apply against the Karfunkel Defendants, TGIL and the Issuers), (ix) conveyance made with intent to defraud (based on NY Debtor Creditor Law § 276 or such other forum equivalent as may apply against the Karfunkel Defendants, TGIL and the Issuers), (x) quantum meruit/unjust enrichment (against the Karfunkel Defendants, and the Director & Officer Defendants), (xi) alter ego liability (against the Karfunkel Defendants and ACP), and (xii) successor liability (against the Karfunkel Defendants) (NYSCEF Doc. No. 158 at 66-97). In other words, the amended complaint asserts essentially all of the same claims except that it contains two breach of contract claims (i.e., instead of one) against the Issuers, TGIL and ACP, and includes a stand alone fraud claim (whereas the original complaint only alleged claims for fraudulent conveyance, including conspiracy to commit fraudulent conveyance [the 5th -- 7th causes of action]).

Reference is made to a series of indentures (the **Indentures**) between (i) Tower Group, Inc. and U.S. Bank N.A., governing debentures issued to the Tower Group Statutory Trust I, dated May 15, 2003; (ii) Tower Group, Inc. and JPMorgan Chase Bank, governing debentures issued to the Tower Group Statutory Trust II, dated September 30, 2003; (iii) Tower Group, Inc. and Wilmington Trust Company, governing debentures issued to the Tower Group Statutory Trust III, dated December 15, 2004; (iv) Tower Group, Inc. and JPMorgan Chase Bank, governing debentures issued to the Tower Group Statutory Trust IV, dated December 21, 2004; (v)

Preserver Group, Inc. and Wilmington Trust Company, governing debentures issued to the Preserver Capital Trust I, dated May 26, 2004 (vi) CastlePoint Management Corp. and Wilmington Trust Company, governing debentures issued to the CastlePoint Management Statutory Trust I, dated December 1, 2006; (vii) CastlePoint Management Corp. and Wilmington Trust Company, governing debentures issued to the CastlePoint Management Statutory Trust II, dated December 14, 2006; and (viii) CastlePoint Bermuda Holdings, Ltd. and Wilmington Trust Company, governing debentures issued to the CastlePoint Bermuda Holdings Statutory Trust I, dated September 27, 2007 (NYSCEF Doc. Nos. 17-24).

The Indentures include provisions intended to protect investors from corporate transactions that may harm the ability of the Issuers to make the required payments to the trusts, which the trusts are obligated to pay to holders of the TruPS. These provisions require, among other things, that no consolidation, merger, sale or transfer of assets of the Issuer may occur unless the successor entity expressly assumes all obligations in the Indentures (Amend. Compl., NYSCEF Doc. No. 158, ¶¶ 59-61, citing e.g., §§ 3.7 and 11.1 of Ex. 2 to the Amend. Compl., NYSCEF Doc. No. 160). The Indentures also provide that successors and assigns are bound to their terms even in the absence of an express agreement to that effect (*id.*, ¶¶ 62-63, citing §§ 14.1 and 14.11 of Ex. 2 to the Amend. Compl., NYSCEF Doc. No. 160).

In connection with these transactions, the parties also entered into guarantees, which provide that the holders of the TruPS are intended third-party beneficiaries who may sue the Issuers directly for nonpayment (Amend. Compl., NYSCEF Doc. No. 158, ¶¶ 50-51; e.g., Ex. 3 to the Amend. Compl., NYSCEF Doc. No. 161). These guarantees also bind successors and assigns (*id.*, ¶ 64,

citing e.g., Ex. 3 to the Amend. Compl., NYSCEF Doc. No. 161, § 8.1). Plaintiffs maintain that these successor obligor provisions are intended to protect the TruPS holders from transactions that would increase the risk of the Indentures, i.e., exactly what happened here (*id.*, ¶¶ 65-70).

In March of 2013, Tower Group, Inc. completed a reverse-merger transaction with a Bermuda company (the **Canopius Transaction**). The successor company was renamed TGIL and became the ultimate parent company of Tower Group, whose operations continued in New York. Pursuant to public filings, TGIL concedes that it is the successor to Tower Group (*id.*, ¶ 83). In August of 2013, TGIL disclosed that its loss reserves had been misstated with respect to certain commercial lines business dating back to 2009 (*id.*, ¶¶ 101-106). However, the amended complaint alleges that its personal lines business remained a valuable asset, unrelated to the bad loss estimates, and the commercial lines business, thus, remained valuable notwithstanding any losses because of future earned premiums, renewal rights and runoff rights (*id.*, ¶ 107).

In November of 2013, TGIL's auditors warned that "there is substantial doubt about the Company's ability to continue as a going concern" (*id.*, ¶ 105). The Karfunkel Defendants allegedly saw this as an opportunity, and exploited TGIL's financial difficulties at the TruPS holders' expense. To wit, in 2014, they acquired TGIL and its insurance businesses through three related and interdependent agreements negotiated and executed in New York (*id.*, ¶¶ 7, 142, 192). TGIL was acquired by ACP for approximately $143 million (the **ACP Merger**) pursuant to an agreement and plan of merger dated January 3, 2014 (the **ACP Merger Agreement**; NYSCEG Doc. No. 120), pursuant to which ACP became the direct 100% owner of TGIL's capital stock (Amend. Compl., ¶¶ 143-44).

Following the execution of the ACP Merger Agreement, but before closing the transaction, TGIL disclosed that it was balance-sheet insolvent and that regulators were scrutinizing the company (*id.*, ¶ 164). However, ACP did not expressly assume or pay the TruPS notwithstanding the fact that defendants purportedly represented in securities disclosures that the ACP Merger "would" provide for the TruPS to be assumed or paid (*id.*, ¶¶ 9, 189, 269, 164, 193-98). Rather, to obtain approval of the ACP Merger, plaintiffs allege that the defendants misled insurance regulators by falsely assuring them that following the merger, ACP would "retain the liability related to the legacy Tower business" (*id.*, ¶¶ 183-84).

TGIL also agreed to certain reinsurance-related transactions and a transfer of renewal rights between the Insurance Companies and certain companies under common ownership with ACP (the **Reinsurance Transactions**). As a result of these Reinsurance Transactions, AmTrust and National General – which were controlled by the Karfunkel Defendants (*see* NYSCEF Doc. No. 200) – had the option to review Tower's existing portfolio and to handpick which policies AmTrust and National General wanted to reinsure (the **Reinsurance Agreements**) (NYSCEF Doc. No. 158, ¶¶ 150-153). The plaintiffs allege that this caused the Karfunkel Defendants to realize millions of dollars in net premiums on their own hand-picked, valuable insurance policies of Tower (*id.*, ¶¶ 343-50). Tower, however, was left to suffer hundreds of millions of dollars of losses on its remaining poorly performing policies.

ACP, as the new owner of TGIL, agreed to related-party deals with AmTrust and National General to transfer Tower's renewal rights for future business following the close of the ACP

Merger (the **Renewal Rights Agreements**; *id.*, ¶¶ 156-59). The plaintiffs allege that through these Renewal Rights Agreements, the Karfunkel Defendants acquired Tower's valuable book of business going forward, which the Karfunkel Defendants have publicly stated "is a well-performing book of business and, as we expected, has contributed to [AmTrust's and National General's] financial and operating performance" (*id.,* ¶ 343).

In short, the plaintiffs allege that the ACP Merger Agreement resulted in TGIL shareholders (including TGIL officers and board members) being paid $143 million for shares that were otherwise worthless due to balance sheet insolvency, as part of a plan to strip TGIL of its valuable insurance policies and renewal rights to the Karfunkel Defendants (*id.*, ¶¶ 10, 144, 177). Thus, the Karfunkel Defendants allegedly realized hundreds of millions in value to themselves, and left the Issuers with over $220 million in TruPS obligations that they had no ability to repay (*id.*, ¶¶ 343-46).

In 2016, the Issuers stopped making payments under the TruPS and the Trustees sent notices of Events of Default and acceleration under the TruPS Indentures (*id.*, ¶¶ 214-216).

The Amended Complaint also alleges that in 2016, the Karfunkel Defendants arranged for the operating insurance subsidiaries of the Tower Group – known as CastlePoint National Insurance Company (**CastlePoint**) and the related **Constituent Companies** that were merged into CastlePoint – to be placed into conservatorship, which is a form of statutory receivership, in California (the **Conservatorship;** *id.*, ¶ 224). Under the Conservation Agreement, signed July 28, 2016, the Michael Karfunkel Family 2005 Trust (the **Karfunkel Trust**) — an indirect

shareholder of ACP, AmTrust and National General — agreed to make a cash payment of $200 million to the CastlePoint estate, subject to certain offsets (NYSCEF Doc. No. 74, §§ 1.1. 3.2, 5.1). Affiliates of AmTrust and National General also agreed, among other things, to provide administrative services to CastlePoint, free of charge, for up to two years (*id.*, § 3.1.). In exchange, the Commissioner, as receiver, agreed to terminate a stop-loss reinsurance agreement and to certain other conditions, including (i) releases of the Insurance Companies' claims against the Karfunkel Trust, AmTrust and National General and their affiliates, and their respective directors, officers, shareholders and others, and (ii) injunctions barring creditors and other interested parties from bringing claims arising out of the management and operation of the Insurance Companies (*id*., §§ 3.3, 8.1.2, 8.2.4, 8.4[ii], 9.1.1). This Conservation Agreement was incorporated into a Plan of Conservation and Liquidation for CastlePoint National Insurance Company (the **Plan**; NYSCEF Doc. No. 75), dated July 28, 2016. The Plan was that was submitted to the California court overseeing the Conservation. In an order dated September 13, 2016 (the **September 2016 Order**), the California court approved the Plan and Conservation Agreement (NYSCEF Doc. No. 76). The court also entered a number of injunctions, including barring "[a]ll creditors of CastlePoint and other interested parties," except the Commissioner, from asserting claims arising out of the "management and operation" of the Insurance Companies against the Karfunkel Trust, AmTrust, National General, and their affiliates, shareholders, officers and directors (among others) (*id.*, § 22).

By order dated March 30, 2017 (the **March 2017 Liquidation Order**; NYSCEF Doc. No. 37), CastlePoint was adjudicated insolvent and the conservation was converted into a liquidation. Pursuant to the March 2017 Liquidation Order:

> Title to all of the assets of CastlePoint, wherever situated and including any and all assets held in the names of any company that is a predecessor by merger with CastlePoint, shall be and hereby are vested in the Liquidator, in his official capacity as such, including without limitation real and personal property, deposits, certificates of deposit, bank accounts, mutual funds, securities, contracts, rights of actions, books, records and other assets of any and every type and nature, wherever situated, presently in CastlePoint's possession and/or those which may be discovered hereafter

(NYSCEF Doc. No. 37, ¶ 5).

The March 2017 Liquidation Order also enjoined all persons, other than the Commissioner, from "the transaction of CastlePoint's business or disposition of its property" (*id.,* ¶ 20), and from "interfer[ing] with the possession of or management by the Liquidator of the property and assets" of CastlePoint (*id.*, ¶ 23).

When the plaintiffs filed the original complaint in September of 2017, the defendants moved to dismiss (mtn. seq. nos. 001-002), arguing, among other things, that the action was barred by the California court's injunctions because, they argued, the assets that were allegedly transferred were Insurance Company assets and not assets of the Issuers themselves.

At oral argument on the motions to dismiss, this court (Ramos, J.) stayed the action pending the California court's ruling on the scope of the March 2017 Liquidation Order (*May 15, 2018 Tr.*, NYSCEF Doc. Nos. 104-05). Plaintiffs filed a motion in California seeking an order that the stay issued in the conservation did not apply to their claims in the instant action. The California court (Schulman, J.) issued an order dated May 16, 2019 (the **May 2019 California Order;** NYSCEF Doc. No. 202) largely denying the relief requested:

> all of Movants' [i.e., plaintiffs'] claims, with the exception of the breach of contract claim against the TruPS Issuers, violate the terms of this Court's injunctions and court-approved releases, and may not be pursued by Movants

(*id.*, 202 at 7, 2).

Plaintiffs moved for reconsideration. This motion was denied. The plaintiffs have appealed. The appeal is pending.

For the avoidance of doubt, on reconsideration, the California court (Schulman, J.) suggested that the court's ruling was limited to the claims asserted in the complaint before him (i.e., the original complaint) and not to any claims that might be asserted in an amended pleading as that was not before the court at that time (NYSCEF Doc. No. 203 at 21:5-8). The court did not suggest, however, that merely interposing the same claims into an "amended" pleading will render claims that it had deemed impermissible, permissible because they were recycled into a new pleading. Thus, as noted above, the May 2019 California Order remains critical to the disposition of the instant motions (NYSCEF Doc. No. 158).

The defendants again move to dismiss, arguing that the amended complaint continues to allege claims based on allegations that the "proceeds" of the TruPS and the "renewal rights" were improperly transferred from the "Tower group of companies" to TGIL (e.g., NYSCEF Doc. No. 158, ¶¶ 262, 314). The defendants maintain that these are essentially claims of improper conveyance and are precisely what the California court held the plaintiffs were enjoined from asserting.

In connection with the Director & Officer Defendants' motion to dismiss, the defendants also raise additional defenses, to wit: that (i) the court lacks personal jurisdiction over the Director & Officer Defendants, (ii) the claims of all but two of the plaintiffs are barred by the "Solely Corporate Obligations" Clause in the Indentures, (iii) the plaintiffs lack standing to sue derivatively because they have no pleaded demand or excuse of demand, and (iv) the plaintiffs' derivative claims on behalf of Tower Group and TGIL are barred by the judgment in a prior 2014 Derivative Action (as further discussed below).

Each of the Director & Officer Defendants is or was at one time a director or officer of one of the Issuers, or their parent company TGIL. As discussed above, the amended complaint asserts three causes of action — fraud (the fourth cause of action), breach of fiduciary duty (the sixth cause of action), and unjust enrichment (the tenth cause of action) — against one or more of the Director & Officer Defendants.

The amended complaint alleges that defendants Fox, Lee, Robbie, Schuster, Smith, Van Gorder and Young – who were TGIL directors at the time the relevant transactions were approved – acted wrongfully in approving the 2014 Merger and related transactions. In addition, the amended complaint alleges that defendants Fox, Hitselberger and Orol signed certain transaction documents and/or were otherwise involved in the merger negotiations. The amended complaint does not allege any role in the transactions at issue for defendants Dove, Lemmer, Roberts and Ziegler. Mr. Lemmer was not a director or officer at the time that the transactions at issue were approved.

Four of the defendants -- Robbie, Smith, Van Gorder, and Young (the **Non-Resident Directors**) -- are all non-New York residents. The amended complaint alleges that they violated their fiduciary duties or committed fraud in connection with the 2014 transactions (NYSCEF Doc. No. 158, ¶¶ 275, 291-93).

Additionally, all of the instruments governing the plaintiffs' TruPS except those held by Wolf River Opportunity Fund LLC and Wolf River Partner Fund (together, the **Wolf River Plaintiffs**) contain identical "solely corporate obligations" clauses in the indentures governing the claims underlying their securities. The defendants argue that these clauses waive the claims asserted herein by all the plaintiffs other than the Wolf River Plaintiffs. To wit:

> **Indenture and Debentures Solely Corporate Obligations.** No recourse for the payment of the principal of or premium, if any, or interest on any Debenture, or for any claim based thereon or otherwise in respect thereof, and ***no recourse under or upon any obligation, covenant or agreement of the Company in this Indenture*** or in any supplemental indenture, or in any such Debenture, or because of the creation of any indebtedness represented thereby, ***shall be had against any*** incorporator, stockholder, employee, ***officer or director***, as such, past, present or future, of the Company ***or of any successor Person of the Company, either directly or through the Company or any successor Person of the Company***, whether by virtue of any constitution, statute or rule of law, or by the enforcement of any assessment or penalty or otherwise, ***it being expressly understood that all such liability is hereby expressly waived and released as a condition of, and as a consideration for, the execution of this Indenture and the issue of the Debentures***

(NYSCEF Doc. Nos. 17, 19–20, 22– 24, § 13.1; Doc. 21, § 12.1).

The Director & Officer Defendants also argue that as creditors, plaintiffs lack standing as a matter of law to sue for breach of fiduciary duty directly and the amended complaint fails to adequately plead derivative standing (and, no such claim may be maintained against the Bermuda entities at all). The Director & Officer Defendants also maintain that to the extent that

the claims are asserted derivatively, they are barred by a settlement of a prior derivative and class action asserted by two TGIL shareholders in March of 2014 (the **2014 Derivative Action**) on behalf of TGIL and Tower and their shareholders (NYSCEF Doc. No. 72) where the complaint in that action challenged as a breach of fiduciary duty to TGIL and Tower, the TGIL Board's actions in pursuing the 2014 Merger (*id.*, ¶¶ 10-17). Among the defendants named in the 2014 Derivative Action were Lee, Fox, Robbie, Schuster, Smith, Van Gorder and Young (*id.*, ¶¶ 23, 26-31).

The 2014 Derivative Action was removed to federal court and consolidated with two class actions already pending in that court (*see* NYSCEF Doc. No. 73, Annexed Stipulation). In 2016, the parties in the consolidated action agreed to a settlement of all claims, whether direct or derivative on behalf of TGIL or Tower, that were or could have been asserted in connection with the merger and related transactions (*id.* at 8). The settlement was approved by the United States District Court by order and judgment dated April 14, 2016, which provided that, "[t]he Consolidated Action is hereby dismissed on the merits and with prejudice … in full and final discharge of any and all claims and obligations that were or could have been asserted in the Consolidated Action against Defendants" (NYSCEF Doc. No. 73, ¶ 7).

Finally, all of the defendants argue that the claims asserted herein are barred, in part, by injunctions issued in California with respect to the Conservatorship, and, in any event, that plaintiffs fail to plead the breach of fiduciary duty and fraud claims with sufficient particularity.

## DISCUSSION

I. The Karfunkel Defendants and the Corporate Defendants' Motion to Dismiss (Mtn. Seq. No. 004) is Granted Except with Respect to the First through Fourth Causes of Action

**The California Injunctions Do Not Bar the Breach of Contract Claims, the Tortious Interference with Contract and the Fraud Claims**

The defendants' argument that the first cause of action asserted in the amended complaint is virtually identical to the first cause of action in the original complaint and is therefore enjoined pursuant to the May 2019 California Order fails (*compare* Compl, ¶¶ 271-76 *with* Amend. Compl., ¶¶ 231-49). The May 2019 California Order ***specifically recognized*** that a breach of contract against the TruPS Issuers ***may be maintained***. In other words, the May 2019 California Order expressly excluded breach of contract claims by the plaintiffs against the Issuers (hereinafter, the **Excluded Claims**). Thus, inasmuch as the breach of contract claims in the amended complaint are asserted against the Issuers, they are Excluded Claims and not barred by the terms of any California injunctions. To the extent that the amended complaint alleges that TGIL and ACP are liable as successor entities, the Excluded Claims may be maintained against these defendants as well at this juncture.

The tortious interference with contract claim is also a claim relating to the alleged breach of contract, and therefore may go forward as well.

However, inasmuch as the plaintiffs previously asserted claims for breach of fiduciary duty, aiding and abetting breach of fiduciary duty, fraudulent conveyance, conveyance made with

intent to defraud, and quantum meruit, the California court found ***those*** claims to be barred by the injunctions issued in connection with the Conservatorship.

Full faith and credit must be afforded that determination (*Givens v Kingsbridge Heights Care Ctr., Inc.*, 171 AD3d 569, 569-70 ["stay issued by a foreign court 'enjoining claims against insureds of an insolvent liability insurer is entitled to full faith and credit, and has the effect of suspending all proceedings against the insurer as of its effective date'"]). If the plaintiffs disagree with the May 2019 California Order, their remedy lies in an appeal.

**The Amended Complaint States Claims for Breach of Contract Claims and Tortious Interference with Contract**

There is no meaningful dispute that the Issuers are in default on their obligations with respect to the TruPS and that plaintiffs may sue to pursue their claims for payment. The amended complaint alleges that TGIL publicly acknowledged that it is the successor to Tower following the 2013 Canopius Transaction (NYSCEF Doc. No. 158, ¶¶ 82-83) and this claim was not enjoined in California. Therefore, the plaintiffs may assert breach of contract claims pursuant to §§ 14.1 and 14.11, 11.1 and 11.2 of the Indentures. As noted above, section 14.1 provides:

> Successors. All of the covenants, stipulations, promises and agreements of the Company in this Indenture ***shall bind its successors and assigns whether expressed or not.***

(NYSCEF Doc. No. 17-24, § 14.1 [emphasis added]).

Section 14.11 provides:

> **Assignment**. The Company will have the right at all times to assign any of its rights or obligations under this Indenture to a direct or indirect wholly owned Subsidiary of the Company, provided that, in the event of any such assignment, the Company will remain liable for all such obligations. Subject to the foregoing, this Indenture is binding upon and

> inures to the benefit of the parties hereto and their respective successors and assigns. This Indenture may not otherwise be assigned by the parties hereto.

(*id.,* § 14.11).

"Consolidation, Merger, Sale, Conveyance and Lease" is also addressed:

> **Successor Entity to be Substituted.** In case of any such consolidation, merger, sale, conveyance, transfer or other disposition and upon the assumption by the successor entity, by supplemental indenture, executed and delivered to the Trustee and satisfactory in form to the Trustee, of the due and punctual payment of the principal of and premium, if any, and interest on all of the Debentures and the due and punctual performance and observance of all of the covenants and conditions of this Indenture to be performed or observed by the Company, such successor entity shall succeed to and be substituted for the Company, with the same effect as if it had been named herein as the Company, and thereupon the predecessor entity shall be relieved of any further liability or obligation hereunder or upon the Debentures. Such successor entity thereupon may cause to be signed, and may issue in its own name, any or all of the Debentures issuable hereunder which theretofore shall not have been signed by the Company and delivered to the Trustee or the Authenticating Agent; and, upon the order of such successor entity instead of the Company and subject to all the terms, conditions and limitations in this Indenture prescribed, the Trustee or the Authenticating Agent shall authenticate and deliver any Debentures which previously shall have been signed and delivered by the officers of the Company, to the Trustee or the Authenticating Agent for authentication, and any Debentures which such successor entity thereafter shall cause to be signed and delivered to the Trustee or the Authenticating Agent for that purpose. All the Debentures so issued shall in all respects have the same legal rank and benefit under this Indenture as the Debentures theretofore or thereafter issued in accordance with the terms of this Indenture as though all of such Debentures had been issued at the date of the execution hereof

(NYSCEF Doc. No. 17, § 11.2, similar provision at NYSCEF 19, 20, 22, 23, 24 § 11.2; NYSCEF Doc. No. 18, §§ 8.2 (a) & (b) Successor Company Substituted; NYSCEF Doc. No. 21, § 10.02; see also chart, NYSCEF Doc. No. 7 at 8).

Accepting the facts alleged as true, as the court must on a motion to dismiss, the plaintiffs have stated a claim for breach of contract and may assert claims for breaches of the successor obligor provisions.

The plaintiffs may also maintain the claim for tortious interference with contract. As discussed above, this appears to be part of the Excluded Claims and is not now asserted against any of the underlying insurance companies involved in the Conservatorship. This cause of action is asserted against the Issuers and their successors. The elements of a claim for tortious interference with contract are (1) the existence of a valid contract, (2) a defendant's knowledge of that contract, (3) the defendant's intentional procurement of a breach and (4) damages (*Tri-Star Lighting Corp. v Goldstein*, 151 AD3d 1102 [2d Dept 2017]). The amended complaint plainly sets forth the existence of a contract and a breach thereof, and alleges the intentional procurement of such breach by the Karfunkel Defendants and resulting damages. Whether or not economic interest may be a defense to this claim cannot be determined at this pre-discovery stage. In any event, this not a defense to tortious interference with ***existing*** (as opposed to prospective) contract (*White Plains Coat & Apron Co., Inc. v Cintas Corp.*, 8 NY3d 422, 426-27 [2007] [explaining greater protection is afforded to an interest in an existing contract than to the less substantive, more speculative interest in a prospective relationship]).

**The Amended Complaint States a Claim for Fraud**

The fraud claims previously asserted are precluded by the May 2019 California Order, as discussed *supra*. However, the amended complaint also asserts a new and independent fraud claim based on the purportedly fraudulent statements contained in the proxy statement, i.e., that TGIL represented that the ACP Merger "***would*** … provide for the assumption or repayment of the Company's indebtedness, including …. the Company's $325 million in outstanding principal of trust preferred securities" (NYSCEF Doc. No. 158, ¶¶ 9, 189, 268). This is sufficient to assert a fraud claim at the pleading stage. The defendants' argument that this statement is not

actionable because it was directed only at its shareholders, and not its creditors, as it was contained in a proxy statement, is not a basis to dismiss at this point. A representation made to a third party may be actionable if made with the intention to deceive a plaintiff (*Pasternak,* 27 NY3d at 829). Whether the plaintiffs here would have attempted to stop the ACP Merger (or even could have) had they not been misled by the above representation in the proxy statement is an issue of fact that cannot be determined on a motion to dismiss (*see Sterling Natl Bank v Ernst & Young LLP,* 62 AD3d 584, 584 [1st Dept 2009]). Accordingly, the motion to dismiss the fraud claim is denied. As nothing in the May 2019 California Order addresses this claim, it may go forward.

II. The Director & Officer Defendants' Motion to Dismiss (Mtn. Seq. No. 005) is Granted

**The Court Lack Personal Jurisdiction Over Non-Resident Defendants**

The four non-resident Director & Officer Defendants – Robbie, Smith, Van Gorder and Young (together, the **Non-Resident Defendants**) – are not subject to this court's jurisdiction as they do not reside in New York, did not take any action in support of the relevant transactions in New York, and did not cause any injury in New York.

The plaintiffs' argument that that court has specific jurisdiction over the Non-Resident Defendants pursuant to CPLR § 302(a) because these defendants (i) participated in certain meetings telephonically and (ii) committed tortious acts in New York (i.e., breaches of fiduciary duty) via their telephonic participation in these board meetings fails. The plaintiffs claim this is "purposeful" activity in New York with an "articulable nexus" to the claims asserted (*citing C.*

*Mahendra (NY) LLC v National Gold & Diamond Ctr., Inc.*, 125 AD3d 454, 457 [1st Dept 2015]).

The general rule is that personal jurisdiction is not acquired over the directors of a company when they conduct their directorial duties outside of the state (*SNS Bank, N.V. v Citibank, N.A.*, 7 AD3d 352, 353 [1st Dept 2004] [affirming dismissal of action against non-resident directors and denial of jurisdictional discovery by trial court]). Attending a meeting in New York – even in person – may also be insufficient. A "substantial nexus between the business transacted here and the cause of action sued upon" is required (*id.* [quotation and citation omitted]). The fact that a company is subject to jurisdiction in New York does not mean that its directors have also subjected themselves to New York jurisdiction (*id.* at 354). Moreover, as the First Department has recognized, "the courts of this state have generally held telephone communications to be insufficient for finding purposeful activity conferring personal jurisdiction" (*C. Mahendra*, 125 AD3d at 458 [citing *Arouh v Budget Leasing, Inc.*, 63 AD3d 506 [1st Dept 2009], *Liberatore v Calvino*, 293 AD2d 217, 220 [1st Dept 2002]). Although the plaintiffs rely on *C. Mahendra, supra,* to argue that telephone contact ***may*** be sufficient, that case does not change the result here. The defendant in that case repeated***ly*** called into New York to negotiate essential contract terms and to place numerous orders, totaling millions of dollars, over the course of several years, which the Court found was sufficiently purposeful activity so as to confer jurisdiction. Here, no such purposeful contracts are alleged. The Non-Resident Defendants merely telephoned into some meetings from out of state. No further connection is alleged. This is insufficient to confer jurisdiction (*see also, Fischbarg v Doucet*, 9 NY3d 375, 380 [2007] [defendant must through

volitional acts avail itself of privilege of conducting business in NY to invoke benefits and protections of its laws]).

Inasmuch as the plaintiffs also seek to assert specific jurisdiction based on injury within the state, TGIL is a Bermudian company, the shareholder vote that ultimately approved the merger transaction took place in Bermuda, and none of the plaintiffs are New York entities (NYSCEF Doc. No. 158, ¶¶ 82, 17; NYSCEF Doc. No. 165). Simply put, none of the Non-Resident Directors, acting outside of New York in connection with their directorship of Bermuda company, could reasonably have expected to be haled into court in New York in connection with the approval of the transactions in question (*World Wide Volkswagen Corp. v Woodson*, 444 US 286, 297 [1980]). Thus, the amended complaint is dismissed against the Non-Resident Directors.

**No Facts Against Defendants Dove, Lemmer, Robers and Ziegler are Alleged**

The amended complaint is also dismissed as against defendants Dove, Lemmer, Roberts and Ziegler because, as noted above, the plaintiffs do not allege any role in the transactions at issue as against these defendants and Mr. Lemmer was not even a director or officer at the time that the transactions at issue were approved.

**Standing and the Breach of Fiduciary Duty Claims**

The court need not address the standing issues asserted by the Director & Officer Defendants with respect to the breach of fiduciary duty claims because these claims were previously alleged in the original complaint and are thus barred by the May 2019 California Order.

**The "Solely Corporate Obligations" Clause Bars the Remainder of the Claims Against the Director & Officer Defendants Except as to the Wolf River Plaintiffs**

The Director & Officer Defendants also argue that the plaintiffs' claims against them are barred by the "Solely Corporate Obligations" clause contained in all of the indentures other than those for the Wolf River Plaintiffs. As set forth above, this clause provides that "[n]o recourse … upon any obligation, covenant, or agreement … in this Indenture" shall be had "directly or through the Company" (i.e., directly or derivatively) against any "incorporator, stockholder, employee, officer or director" of the Issuers or their successors (NYSCEF Doc. Nos. 17, 19-20, 22-23, § 13.1; NYSCEF Doc. No. 21, § 12.1).

The plaintiffs, relying on *Small v Sullivan*, 245 NY 343 (1927), maintain that it is "black letter law" that such clauses do not bar breach of fiduciary duty and fraud claims against officers and directors of debenture issuers. Their reliance is misplaced. In *Small*, the Court of Appeals, confronted with a different no recourse provision in a trust agreement, concluded that, "it did not and could not cover the future fraudulent acts of the directors" (245 NY at 356). The Court reasoned:

> The complaint as we have indicated alleges a consolidation conceived and executed in fraud, and for the willful and intentional purpose of procuring the assets and income of the corporations. The consolidation was long after the making of the trust agreement. The directors could not willfully and fraudulently destroy or convert property held as security for these bonds, whether it was pledged to the trustee or was the general assets of the corporation, and then plead that they were protected by an agreement that they should not be liable for their acts. ***The agreement did not relate to such future acts***.

(*id.* at 356-57 [emphasis added]).

Here, in contrast, the "solely corporate obligations" clause expressly applies to "future" obligations. As such, the fraud claims, to the extent they are asserted against the Director & Officer Defendants, are dismissed except to the extent they are asserted by the Wolf River Plaintiffs.

**The 2014 Derivative Action Does Not Bar This Action**

Finally, the Director and Officer Defendants also argue that the instant claims against them are barred by the 2014 Derivative Action which alleges a claim for breach of fiduciary duty against TGIL's for pursuing the 2014 Merger (NYSCEF Doc. No. 72, ¶¶ 10-17). However, as that prior action was brought by TGIL ***shareholders*** and the instant action is brought by TGIL ***creditors,*** it cannot serve as a bar. The plaintiff creditors in the instant action simply could not have asserted their claims in the 2014 Derivative Action because they were not shareholders of TGIL, but creditors.

Accordingly, it is

ORDERED that the motion seq. 004 is granted in part and the claims other than the breach of contract (1st and 2nd cause of action), aiding and abetting breach of contract and the claim for fraud are ordered held in abeyance and stayed; and it is further

ORDERED that the motion seq. 005 is granted in part and the claims against defendants Robbie, Smith, Van Gorder, Young, Dove, Lemmer, Roberts and Ziegler are dismissed, and the claims for breach of fiduciary duty are dismissed, and the claims for fraud are dismissed except as to the Wolf River Plaintiffs as set forth above; and it is further

ORDERED that the parties are directed to settle order on notice and the non-dismissed defendants are directed to file an answer to the surviving claims within 30 days of this decision and order; and it is further

ORDERED that the parties are directed to appear for a remote conference on May 10, 2021 at 11:30 AM.

DATED: March 25, 2021

ENTER:

Hon. Andrew Borrok
J.S.C. Hon. Andrew Borrok