

1301 Fannin Tenant, LLC v Internap Holding LLC

2022 NY Slip Op 31988(U)

June 23, 2022

Supreme Court, New York County

Docket Number: Index No. 656141/2021

Judge: Joel M. Cohen

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This opinion is uncorrected and not selected for official publication.

SUPREME COURT OF THE STATE OF NEW YORK
 COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 03M

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1301 FANNIN TENANT, LLC	INDEX NO. <u>656141/2021</u>
Plaintiff,	MOTION DATE <u>06/02/2022</u>
- v -	MOTION SEQ. NO. <u>002</u>
INTERNAP HOLDING LLC F/K/A INTERNAP CORPORATION,	DECISION + ORDER ON MOTION
Defendant.	
-----X	

HON. JOEL M. COHEN:

The following e-filed documents, listed by NYSCEF document number (Motion 002) 16, 17, 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, 32, 33 were read on this motion to DISMISS.

This is a breach of contract and fraud case. Plaintiff (1301 Fannin Tennant, LLC, or “Netrality”) agreed to purchase Defendant’s (Internap Holding LLC or “INAP”) Houston Data Center (“HDC”). An Asset Purchase Agreement (“APA”) was signed on April 27, 2020 and amended on May 31, 2020. As part of the deal, Netrality was to acquire all of INAP’s customers in the HDC, including its biggest customer, Nuance Communications (“Nuance”). Netrality alleges that INAP misrepresented the value of the Nuance customer relationship (and therefore of the transaction as a whole) by falsely stating that Nuance intended to *increase* its use of the HDC facility when in fact Nuance had advised INAP that it intended to *decrease* its use of that facility. INAP now moves to dismiss Netrality’s Complaint.

For the reasons that follow, Defendant's motion to dismiss is granted with respect to Plaintiff's Fifth Cause of Action (implied covenant of good faith and fair dealing) and Sixth Cause of Action (declaratory judgment), but is otherwise denied.

Background

Netrality asserts six causes of action against INAP: Fraudulent Misrepresentation, Fraudulent Concealment, Fraudulent Inducement, Breach of Contract, Breach of Covenant of Good Faith and Fair Dealing, and Declaratory Relief. Specifically, Netrality alleges that INAP knew prior to signing the APA that Nuance intended to "consolidate" its business *within* the HDC (reducing revenue), but nevertheless misled Netrality to believe that Nuance was going to consolidate its use of *other* facilities *into* the HDC (increasing revenue). Netrality alleges that but for these misrepresentations, Netrality would not have signed the APA with the agreed upon purchase price.

On July 30, 2020, Nuance gave written notice to Netrality stating its intention not to renew services in two of its three "cages" in the HDC. This letter was sent during the 60-day post-closing purchase price adjustment period laid out in the APA. The parties disagreed sharply on whether this development triggered a contractual adjustment to the purchase price. In accordance with the APA's dispute resolution procedures, they submitted the dispute to an independent accounting firm, RSM US LLP ("RSM").

RSM found that no purchase price adjustment was warranted under the terms of the agreement. Earlier this year, in a special proceeding, the Court granted INAP's petition to confirm RSM's award and denied Netrality's cross-motion to vacate that award (*Internap Holdings LLC v. 1301 Fannin Tenant, LLC*, Sup Ct NY County, Index No. 654961/2021 (NYSCEF Doc. No. 59, Mar. 3, 2022)).

Discussion

On a motion to dismiss, the Court must “accept as true the facts alleged in the complaint as well as all reasonable inferences that may be gleaned from the facts” (*Saska v Metro. Museum of Art*, 975 NYS2d 605, 612 [Sup Ct NY County 2013]; *see also Taboola, Inc. v RedOrbit, Inc.*, No. 65140/2017 NY Misc LEXIS 4546, at *2 [Sup Ct NY County Nov 17, 2017]). Claims that consist of bare legal conclusions with no factual specificity, however, are insufficient to survive a motion to dismiss (*Godfrey v Spano*, 13 NY3d 358, 373 [2009]). Additionally, CPLR 3016 (b) states that when an action is based off misrepresentation or fraud, the circumstances constituting the wrong shall be stated in detail (CPLR 3016 [b]). CPLR 3016 (b) is met when “the facts are sufficient to permit a reasonable inference of the alleged conduct” (*Pludeman v N. Leasing Sys., Inc.*, 890 NE2d 184, 187 [2008]).

I. Fraud

The Motion to Dismiss Netrality’s three fraud claims is denied. To plead a prima facie claim of fraud, a complaint must allege misrepresentation and/or concealment of a material fact, falsity, scienter on the part of the wrongdoer, justifiable reliance, and resulting injury (*IKB Intern S.A. v Morgan Stanley*, 142 AD3d 447, 448 [1st Dept 2016]).

Here, Netrality adequately alleges that INAP falsely represented that Nuance’s “consolidation” plans would result in an *increase* in revenue for the HDC (*i.e.*, consolidating Nuance’s use of space from other facilities *to* the HDC) when, in fact, INAP understood that Nuance’s plans would *decrease* revenue at the HDC (*i.e.*, consolidating Nuance’s use of space *within* the HDC). Netrality alleges that this representation was confirmed by INAP executive Joe Dufresne (NYSCEF Doc No. 2, complaint at 21). If further alleges that it first learned the

truth about Nuance's downsizing plans from INAP's Brian Fleming after closing, and that Mr. Fleming confirmed that "INAP" was aware of those plans before the signing of the APA (*id* at 39-40, 43). Although the facts remain to be proven, these allegations are sufficient to plead a fraud claim (*see IKB Int'l S.A.*, 142 AD3d at 450).

Netrality also adequately pleads that it justifiably relied on INAP's alleged misrepresentation. Netrality alleges that it relied upon INAP's representations with respect to Nuance's plans in agreeing to the Purchase Price (*see* NYSCEF Doc No. 2, complaint at 16, 18). Netrality also alleges that it was forced to rely solely upon INAP's representations because INAP prohibited Netrality from communicating directly with customers such as Nuance (*id.* at 28, 55). In those circumstances, the Court cannot conclude as a matter of law that Netrality's alleged reliance on INAP's representations was unreasonable (*see Basis Yield Alpha Fund Master v Stanley*, 136 AD3d 136, 143 [1st Dept 2015]).

Netrality also adequately alleges that it suffered damages. Netrality alleges that but for the misrepresentation, Netrality would not have agreed to a purchase price that was based in material part on expected revenues from Nuance, which was INAP's largest customer at the HDC (*see Garendeau Realty Owner, LLC v 14 Lincoln Place, LLC*, 253 AD2d 403, 404 [2d Dept 2019], NYSCEF Doc No. 2, complaint at 26).

II. Breach of Contract

The Motion to Dismiss Netrality's breach of contract claim is denied. Netrality adequately states a claim that INAP breached §§ 3.6 and 3.14 of the APA.

To establish a *prima facie* case for breach of contract, Netrality must adequately allege that there was an existing contract, that plaintiff performed its duties under the contract, that the defendant breached its duty under the contract, and that there were resulting damages (*Park v*

Kim, 205 AD3d 429 [1st Dept 2022], citing *Harris v Seward Park Hous. Corp.*, 79 AD3d 425, 426 [1st Dept 2010]). INAP argues that Netrality fails to allege a breach, that Netrality's breach of contract claim is time-barred, and that Netrality fails to allege that it incurred damages. These arguments are unavailing.

First, Netrality has stated an adequate claim that INAP breached § 3.6 of the APA. In Section 3.6 (c) INAP represents that there has not been any Material Adverse Effect ("MAE"), which is defined as "any change, effect, event, occurrence, state of facts or development that, individually or in the aggregate, has a material adverse effect upon . . . the financial condition, business, assets, properties, or results of operations of the Houston Data Center" (NYSCEF Doc No. 19 at 14). INAP argues that there is no MAE since there has not been an actual effect to the HDC's finances or business. That is, however, a fact question that cannot be resolved on a motion to dismiss. Taking the factual allegations of the Complaint as true and giving Netrality the benefit of reasonable inferences drawn therefrom, the "consolidation" of the HDC's largest customer could be deemed material from the long-term perspective of a reasonable acquiror (*see In re IBP, Inc. Shareholders Litig.*, 789 A2d 14, 68 [Del. Ch. 2001], applying New York Law). In these circumstances, the purported change in circumstances impacting the HDC's largest customer – which allegedly was not communicated to Netrality until after closing – is sufficient to state a claim.

Additionally, Netrality has stated a viable claim of breach of § 3.14 of the APA. In that section, INAP represented that it had not received any written notice or oral notice (to specified INAP executives) that any of INAP's Customers will reduce materially its business with Seller in respect of the HDC (NYSCEF Doc No. 19 at 17). INAP argues that Netrality has not sufficiently alleged that Netrality received the required notice of Nuance's plans or that Nuance's

“consolidation” would materially reduce its business. Again, however, these are questions of fact that the Court cannot resolve on a motion to dismiss. Netrality alleges that INAP’s Brian Fleming disclosed that “Nuance had told INAP of its intent to reduce down to one cage well in advance of the execution of the APA and Closing” (NYSCEF Doc No. 2, complaint at 43). The question whether “INAP” included Mr. Aquino or Mr. Sicoli is a matter for discovery. Similarly, the materiality of Nuance’s consolidation of its business at the HDC is a question for discovery, not dismissal.

Finally, INAP’s argument that Netrality’s claim is time-barred under Article 6 of the APA is unavailing. Under that provision, the representations and warranties contained in §§ 3.6 and 3.14 of the APA “[s]hall survive for a period of time ending on that date which is twelve (12) months after the Closing Date,” or May 31, 2021 (NYSCEF Doc No. 19 at 29). Even assuming this provision is applicable (given that the representation is alleged to have been inaccurate as of the closing date), here Netrality adequately alleges that it gave INAP written notice of its claim on September 10, 2020.

III. Good Faith and Fair Dealing

Netrality’s claim for breach of the implied covenant of good faith and fair dealing is dismissed.

“Implicit in all contracts is a covenant of good faith and fair dealing in the course of contract performance,” which imputes “any promises which a reasonable person in the position of the promisee would be justified in understanding were included” (*Dalton v Educational Testing Serv.*, 87 NY2d 384, 389-90 [1995]). This includes covenants not to “do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract” (*id.*, quoting *Kirke La Shelle Co. v Paul Armstrong Co.*, 263 NY 79, 87 [1933]),

and “not to act arbitrarily or irrationally in exercising ... discretion” (*id.*). However, “[t]he duty of good faith and fair dealing does not imply obligations inconsistent with contractual provisions (*Gottwald v Sebert*, 193 AD3d 573, 582 [1st Dept 2021]) or “that were not bargained for” (*King Penguin Opportunity Fund III, LLC v Spectrum Group Mgt. LLC*, 187 AD3d 688, 690 [1st Dept 2020]). Nor can it “impose obligations ... beyond the express terms of the parties’ agreement” (*Darabont v AMC Network Entertainment LLC*, 193 AD3d 500 [1st Dept 2021]). Stated differently, an implied covenant claim “may not be used as a substitute for a nonviable claim of breach of contract” (*StarVest Partners II, L.P. v Emportal, Inc.*, 101 AD3d 610, 613 [1st Dept 2012]). Moreover, a claim for breach of the implied covenant will be dismissed if it “relies on the same facts that form the basis for the breach of contract claim and seek[s] the exact same damages” (*320 W. 115 Realty LLC v All Bldg. Constr. Corp.*, 194 AD3d 511, 512 [1st Dept 2021] [citation omitted]). To warrant dismissal, “[t]he conduct alleged in the two causes of action need not be identical in every respect. It is enough that they arise from the same operative facts” (*Mill Fin., LLC v Gillett*, 122 AD3d 98, 104-05 [1st Dept 2014]).

Netrality’s claim seems to be that INAP acted unreasonably during the RSM arbitration. Its claims in that regard are better suited for an argument to vacate the RSM award, which has already been confirmed. Its allegations do not support an independent claim for breach of the implied covenant.

IV. Declaratory Relief

Finally, Netrality’s claim for declaratory relief is dismissed on the ground that it is duplicative of its claims for breach of contract and fraud (*Nationstar Mtge., LLC v Ocwen Loan Servicing, LLC*, 194 AD3d 490, 493 [1st Dept 2021]). There is no meaningful forward-looking relief being sought that is distinct and independent from the other claims.

Accordingly, it is

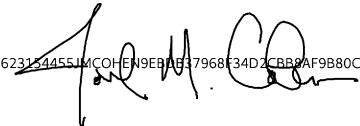
ORDERED that Defendant’s motion to dismiss is granted with respect to Plaintiff’s Fifth Cause of Action (implied covenant of good faith and fair dealing) and Sixth Cause of Action (declaratory judgment), but is otherwise denied; it is further

ORDERED that Defendant answer the remaining claims in the Complaint within 21 days of this Decision and Order; and it is further

ORDERED that the parties appear for a Preliminary Conference on August 2, 2022 at 10:30 a.m., with the parties circulating dial-in information to chambers at SFC-Part3@nycourts.gov in advance of the conference.¹

This constitutes the Decision and Order of the Court.

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JOEL M. COHEN, J.S.C.

6/23/2022

DATE

CHECK ONE:

CASE DISPOSED

NON-FINAL DISPOSITION

GRANTED

DENIED

GRANTED IN PART

OTHER

APPLICATION:

SETTLE ORDER

SUBMIT ORDER

CHECK IF APPROPRIATE:

INCLUDES TRANSFER/REASSIGN

FIDUCIARY APPOINTMENT

REFERENCE

¹ If the parties agree on a proposed preliminary conference order in advance of the conference date (consistent with the guidelines in the Part 3 model preliminary conference order, available online), they may file the proposed order and email a courtesy copy to chambers with a request to so-order in lieu of holding the conference.