To be argued by: Justin A. Heller
Time requested: 10 minutes

Appellate Division Docket No. 2019-09157

New York Supreme Court
Appellate Division – Second Department

MAPLE MEDICAL LLP,

Plaintiff-Respondent,

- against -

JOSEPH SCOTT, D.O.,

Defendant-Appellant,

- and –

MEDICAL LIABILITY MUTUAL INSURANCE COMPANY,

Defendant.

APPELLANT'S BRIEF

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QUESTIONS PRESENTED (4)

1. Is Defendant-Appellant entitled to his share of the Cash Consideration paid in exchange for the extinguishment of his Policyholder Membership Interest in Medical Liability Mutual Insurance Company ("MLMIC"), pursuant to controlling New York Insurance Law (§ 7307[e][3]) , the MLMIC Plan of Conversion, the Decision of the New York State Department of Financial Services ("DFS") approving the Plan, and New York common law?

    Answer: The court below held that under the doctrine of *stare decisis*, it was bound to follow the decision in *Matter of Schaffer, Schonholz & Drossman, LLP v. Title* (171 A.D.3d 465 [1st Dep't 2019]), and denied Defendant-Appellant's motion, and granted Plaintiff-Respondent's cross-motion, for summary judgment.

2. Is Defendant-Appellant entitled to a determination that he would not be unjustly enriched by receiving his share of the Cash Consideration paid in exchange for the extinguishment of his MLMIC Policyholder Membership Interest?

    Answer: The court below held that Defendant-Appellant would be unjustly enriched by receiving his share of the Cash Consideration, based on the decision in *Schaffer*.

3. Was the court below bound by the First Department's decision in *Schaffer*?

   Answer: The court below held that it was bound to follow *Schaffer* under the doctrine of *stare decisis*.

4. Was Plaintiff entitled to immediate turnover of the Cash Consideration from MLMIC's escrow agent at the time summary judgment was granted in its favor, notwithstanding that (a) under the Plan of Conversion, MLMIC was required to hold the Cash Consideration in escrow "pending a non-appealable order," (b) the DFS approved the Plan's escrow process in its September 6, 2018 Decision and by its January 14, 2019 Order, and (c) the parties stipulated that "MLMIC shall hold the funds in escrow pending a further stipulation of the parties or a final non-appealable order or judgment of the Court"?

   Answer: The court below improperly disregarded the Plan and stipulation by ordering MLMIC to pay the Cash Consideration to Plaintiff, notwithstanding that its Decision/Order/Judgment was appealable.

NATURE OF THE CASE

Defendant-Appellant Joseph Scott, D.O. ("Defendant") submits this Brief in support of his appeal of the Decision/Order/Judgment of the Westchester County Supreme Court (Ecker, J.) dated July 5, 2019 and entered July 9, 2019 ("Decision") that denied Defendant's motion, and granted the cross-motion of Plaintiff-Respondent ("Plaintiff"), for summary judgment (R.8-12).

The question before the court below was straightforward. After MLMIC demutualized (resulting in the extinguishment of its Policyholders' Membership Interests), who was entitled to the Cash Consideration paid in exchange for Defendant's Policyholder Membership Interest: (i) *Defendant*, who became a MLMIC Policyholder—and thereby acquired a Membership Interest—as part of the bargained-for exchange of consideration under his Employment Agreement; or (ii) *Plaintiff*, which paid Defendant's MLMIC premiums pursuant to, and in exchange for his services under, the Employment Agreement? The answer to that question was simple, compelled by, *inter alia*, the statutory framework of the Insurance Law, the plain terms of the Employment Agreement, and controlling unjust enrichment law.

Simply put, as the Policyholder under (and thus owner of) his MLMIC policy, Insurance Law § 7307(e)(3) mandated that Defendant receive the Cash Consideration paid on account of the extinguishment of his Membership Interest.

This statutory right to the Consideration was incorporated into MLMIC's Plan of Conversion and confirmed in the DFS Decision approving the Plan—with the limited exceptions being where the Policyholder expressly designated the employer to receive the Consideration, or assigned it to the employer. Neither of those exceptions occurred here.

Faced with Defendant's clear entitlement to the Cash Consideration, Plaintiff sought to circumvent the Insurance Law, Plan of Conversion and DFS Decision by arguing that its appointment as Defendant's Policy Administrator and payment of his policy premiums made it the "policyholder" under the New York Insurance Law, and entitled it to the Consideration on a theory of unjust enrichment. Plaintiff's argument entirely ignored that (a) Defendant was the Policyholder, (b) as Policy Administrator, Plaintiff was merely Defendant's agent, conferred with only the limited rights set forth in the Policy Administrator Designation Form (none of which entitled it to the Consideration), (c) it paid the premiums as an express term of the parties' Employment Agreement, and (d) Defendant provided the contractually agreed-upon consideration for those premium payments. Simply put, Plaintiff's claim for unjust enrichment failed as a matter of black letter New York law because the premium payments forming the basis of its claim were governed by the Employment Agreement, and Defendant provided the agreed-upon consideration for those payments (i.e., his provision of services for Plaintiff's benefit).

Before the foregoing could be presented to the court below, however, the First Department issued a Decision in *Matter of Schaffer, Schonholz & Drossman, LLP v. Title* (171 A.D.3d 465 [1st Dep't 2019]) ("*Schaffer*") , which, in four sentences, summarily held that the doctor/policyholder would be unjustly enriched by receiving the Cash Consideration because her employer had paid her policy premiums. The First Department, acting as a court of original jurisdiction under CPLR 3222, did *not* cite to the Insurance Law, did *not* reference the MLMIC Plan of Conversion or the DFS Decision approving the Plan, did *not* rely upon *any* New York unjust enrichment law, and did not provide *any* reasoning for its conclusion. Instead, the First Department relied solely upon two ERISA cases, notwithstanding that (i) neither ERISA case involved a state law unjust enrichment claim, and (ii) *Schaffer* had nothing to do with ERISA.

Even though *Schaffer* was not binding on the court below because it (a) is distinguishable procedurally and factually, (b) conflicts with established Court of Appeals and Second Department unjust enrichment precedent, (c) was based on deficient legal arguments to the Appellate Division, and (d) relied solely upon inapposite ERISA cases, the court below held that it was bound to follow *Schaffer*, and granted summary judgment in favor of Plaintiff. While the court below added in dicta that "the conclusions drawn in the First Department's decision are persuasive," and that payment to Defendant would result in his unjust enrichment, like *Schaffer*, it provided no support for its conclusion based on established New York unjust enrichment law. (R.11). It is respectfully submitted that the court below erred in so holding. In any event, this Court certainly is not bound by another Appellate Division's decision and, for the reasons herein, should not follow *Schaffer*. *See, e.g. Mountain View Coach Lines, Inc. v. Storms*, 102 A.D.2d 663, 665 (2d Dep't 1984).

It bears emphasis that in contrast to *Schaffer* (and in turn the court below), three New York courts that have substantively analyzed the statutory and regulatory framework governing the MLMIC conversion—together with basic structure and operation of mutual insurance companies, and controlling unjust enrichment law—strongly support Defendant's entitlement to the Cash Consideration:

- *Maple-Gate Anesthesiologists, P.C. v. Nasrin* (96 N.Y.S.3d 837 [Sup. Ct. Erie Cty. 2019]) ("*Maple-Gate*"): In a well-reasoned decision relying on Insurance Law § 7307, the Plan of Conversion, the DFS Decision and established New York unjust enrichment law, the Erie County Supreme Court held that the policyholders were entitled to the Cash Consideration, and that based on facts similar to those herein, the employer's unjust enrichment claim must be dismissed.

- *Columbia Mem. Hosp. v. Hinds* (2019 NY Slip Op 51508(U) [Sup. Ct. Columbia County 2019]) ("*Hinds*"): The Columbia County Supreme Court held that *Schaffer* was distinguishable on its facts, and in any event the court was "free to correct prior erroneous interpretations of the law." (*Id.*, ¶¶5-6 [citing *In re Charles A. Field Delivery Serv.*, 66 N.Y.2d 516, 518-19(1985)]). The court affirmed that Insurance Law § 7307(e)(3) repeatedly refers to the Policyholders as those eligible to receive the Cash Consideration, and underscored that the Consideration, "by law, is not a return to the hospital of any insurance premiums it paid on behalf of the defendant, it represents the policyholder's share in MLMIC." *Id.*, ¶5.

- *Shoback v. Broome Obstetrics and Gynecology, P.C.* (Index No. EFCA2018003334 [Sup. Ct. Broome County Sept. 12, 2019]) ("*Shoback*")[1]: Although the Broome County Supreme Court concluded that it was bound to follow the *Schaffer* Decision even though it disagreed with it, it confirmed that "[t]he language of the Plan [of Conversion] is clear and unambiguous, and as such must be accorded the plain meaning of its terms"—namely that "plaintiff is entitled to the money." In short, the *Shoback* court held that "Defendant's argument - that it paid the premiums and as such is entitled to the funds, is unpersuasive." *Id.* at 4. The court stressed that the employer "paid the premiums as part of its obligation under the Employment Agreement," and plaintiff "provided services and in return defendant was confident that she was covered (and hence it was covered) in terms of malpractice insurance." *Id.* Simply put, the "arrangement benefitted both parties," and the mere fact that the Cash Consideration was "a 'windfall', or 'a pot of money

[1] A copy of the *Shoback* Decision is provided as an Addendum to this Brief.

no one expected or even envisioned'… does not, per se, render it illicit or unjust." *Id.* at 4-5.

Finally, the court below improperly ordered MLMIC's escrow agent to distribute the Cash Consideration to Plaintiff, notwithstanding that (a) under the Plan of Conversion, MLMIC was required to hold the Cash Consideration in escrow "pending a non-appealable order," (b) the DFS approved the Plan's escrow process in its September 6, 2018 Decision and by its January 14, 2019 Order (R. 140, para 5; R. 435, ¶(d)), and (c) by Stipulation dated May 6, 2019, the parties agreed that "MLMIC shall hold the funds in escrow pending a further stipulation of the parties or a final non-appealable order or judgment of the Court" (R. 473). For the reasons herein, Defendant respectfully requests that this Court decline to follow *Schaffer*, reverse the Decision of the court below, grant Defendant's Motion for summary judgment, deny Plaintiff's Cross-Motion for summary judgment, and order Plaintiff to turn the Cash Consideration over to Defendant.

STATEMENT OF FACTS

I. MLMIC's Ownership Structure.

Prior to its October 1, 2018 demutualization and conversion to a stock insurance company, MLMIC was a mutual insurance company (R. 66, para 1). A mutual insurance company is owned by its members, and the members are the individual policyholders (R. 69-70). *See* Insurance Law § 1211(a). Under MLMIC, the ownership interests of the Members/Policyholders are called "Policyholder Membership Interests"; and the Policyholder is the person listed as the "Insured" under their policy (R. 70).

II. Defendant's MLMIC Policy.

Defendant was employed as a physician with Plaintiff from August 20, 2012 until August 4, 2017 (R. 206, ¶2). During his employment with Plaintiff, Defendant was the sole Insured—and thus the sole Policyholder—under his individual MLMIC malpractice policy (R. 207, ¶4; R. 226). Under the terms of his Employment Agreement, one of the benefits that Plaintiff agreed to provide in exchange for Defendant's services was the payment of his malpractice insurance premiums (R. 22; R. 212, ¶2, R. 213, ¶7).

To effectuate payment of his MLMIC premiums, Defendant signed a Policy Administrator Designation Form designating Plaintiff as the "Policy Administrator" of his MLMIC policy (R. 207, ¶4; R. 222). The Policy Administrator Designation

Form expressly provided that the Policy Administrator would act as the agent of the insured—i.e., "for the paying of Premium[s], requesting changes in the policy, … and for receiving dividends and any return Premiums when due." (R. 222) In accordance with its contractual obligation, Plaintiff paid Defendant's MLMIC premiums on his behalf during his employment (R. 239, ¶5).

III. MLMIC's Conversion.

On July 16, 2016, MLMIC applied to the New York State Department of Financial Services ("DFS") for permission to file a plan to convert from a mutual insurance company to a stock insurance company (R. 142). Under Insurance Law § 7307(e)(3) , when a mutual insurance company converts to a stock insurance company, its plan of conversion:

> "shall also provide that each person who had a policy of insurance in effect at any time during the three year period immediately preceding the date of adoption of the resolution [to seek approval of the conversion] shall be entitled to receive in exchange for such equitable share, without additional payment, consideration payable in voting common shares of the insurer or other consideration, or both." (Emphasis added)

Rather than give Policyholders shares of the new stock insurance company, MLMIC's Plan of Conversion provided that the "Eligible Policyholders" (or their "Designees") would receive $2.502 billion in cash consideration ("Cash Consideration") for the extinguishment of their Policyholder Membership Interests (R. 66, para. 3, R. 77, ¶8.1). The MLMIC Plan of Conversion defined "Eligible

Policyholders" as Policyholders during the period July 15, 2013 through July 14, 2016; and "Designees" as Policy Administrators (or EPLIP Employers)[2] specifically designated by the Eligible Policyholder to receive the Cash Consideration (R. 68).

In addition, the Plan set forth a procedure by which a Policy Administrator could object to the distribution of the Cash Consideration to the Eligible Policyholders; and upon receipt of an objection, MLMIC would hold the Consideration in escrow pending receipt of (i) "joint written instructions" from the Eligible Policyholder and Policy Administrator, or (ii) a non-appealable court order or arbitration award respecting the distribution of such Consideration (R. 76 ¶6.3(f), R. 82 para. 4).

After holding an August 23, 2018 public hearing regarding MLMIC's proposed Plan of Conversion, the Superintendent of DFS issued a Decision dated September 6, 2018 (the "DFS Decision") approving the Plan (R. 162, R. 123). The DFS Decision authorized a closing of the conversion transaction only upon the approval of the Policyholders as of July 14, 2016 (R. 163, para 3 and n.1). The Policyholders approved the Plan of Conversion on September 14, 2018, and the transaction closed on October 1, 2018.[3]

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[2] Defendant's policy was not an Employee Professional Liability Insurance Policy (EPLIP); thus, any reference in the Plan of Conversion or DFS Decision to EPLIP Employers is irrelevant here and has been omitted.

[3] *See* "Record Date Policyholders Vote to Approve MLMIC Plan of Conversion," MLMIC Blog, available at https://www.mlmic.com/blog/physicians/policyholders-approve-conversion (last accessed 10/22/2019).

It is undisputed that Defendant was an Eligible Policyholder (R. 206-8 ¶¶3, 4, 8); that the amount of the Cash Consideration at issue is $128,148.92 (R. 29; R. 208 ¶8; R. 226); that Defendant did not make Plaintiff a "Designee" to receive his share of the Cash Consideration (R. 208, ¶8); that Plaintiff filed an objection to the distribution of the Cash Consideration to Defendant (R. 208, ¶9); and that MLMIC therefore held the money in escrow as required under the Plan and the DFS Decision, until the court below ordered MLMIC to turn the money over to Plaintiff. (R. 11).

ARGUMENT

I. DEFENDANT IS ENTITLED TO THE CASH CONSIDERATION PAID ON ACCOUNT OF HIS MLMIC MEMBERSHIP INTEREST, WARRANTING SUMMARY JUDGMENT AS TO HIS CAUSE OF ACTION FOR DECLARATORY JUDGMENT

A. As an Eligible Policyholder, Defendant is Entitled to the Cash Consideration.

As Policyholder, Defendant indisputably was the owner of his Policyholder Membership Interest,[4] and was thus entitled to receive his share of the Cash Consideration. This right is codified in Insurance Law § 7307(e)(3) , which provides that when a mutual insurance company converts to a stock insurance company, its plan of conversion shall include:

> "[t]he manner and basis of exchanging the equitable share of each eligible mutual policyholder for securities or other consideration, or both, of the stock corporation into which the mutual insurer is to be converted and the disposition of any unclaimed shares. The plan shall also provide that each person who had a policy of insurance in effect at any time during the three year period immediately preceding the date of adoption of the resolution [to seek approval of the conversion] shall be entitled to receive in exchange for such equitable share, without additional payment, consideration payable in voting common shares of the insurer or other consideration, or both." (Emphasis added).

[4] *See, supra*, Statement of Facts (at I) (MLMIC is owned by its Members, the Policyholders, who hold "Policyholder Membership Interests." The Plan of Conversion defines "Policyholder" as the person listed as the "Insured" under their policy. Here, Defendant was the sole Insured under his MLMIC policy and, thus, the owner of his Policyholder Membership Interest).

This requirement of the Insurance Law was incorporated into MLMIC's Plan of Conversion:

- "Eligible Policyholders, or their Designees, will receive Cash Consideration in consideration of the extinguishment of their Policyholder Membership Interest." (R. 66, para. 3).

- The Cash Consideration shall be paid to eligible policyholders "in respect of the extinguishment of all Policyholder Membership Interests." (R. 67, para. 2).

- "Each Eligible Policyholder (or its Designee) shall receive a cash payment equal to the applicable Conversion Payment." (R. 77, ¶8.2).

In its September 6, 2018 Decision, the DFS confirmed the foregoing:

- "A Mutual insurance company is owned by and operated for the benefit of its policyholders. A policyholder's ownership interest in a mutual insurance company is known as a 'membership interest'…. Membership interests … exist only in connection with a policyholder's ownership of a policy." (R. 164 ¶II[B]).

- "[I]nstead of receiving stock in the converted stock company, MLMIC's Eligible Policyholders will receive cash consideration." (R. 165 ¶II[B][1]).

In sum, the Insurance Law, the MLMIC Plan of Conversion, and the DFS Decision unequivocally provide that as an Eligible Policyholder, Defendant is entitled to receive his share of the Cash Consideration. *See Maple-Gate*, 96 N.Y.S.3d at 841 ("Insurance Law § 7307 does not confer an ownership interest in…the cash consideration to anyone other than the policyholder."). *See also Shoback*, at 4 ("The language of the Plan is clear and unambiguous, and as such must be accorded the plain meaning of its terms. According to those terms, [the Policyholder] is entitled to the money." [Citation omitted]); *Hinds*, 2019 NY Slip Op 51508(U), ¶¶ 1-2 ("The DFS Decision confirmed…that it is in the Insurance Law 7307 (e)(3) which explicitly defines those policyholders who are eligible to receive the purchase price consideration."); *Commonwealth of the N. Mariana Is. v. Canadian Imperial Bank of Commerce*, 21 N.Y.3d 55, 60-62 (2013) ("[W]here the statutory language is clear and unambiguous, the court should construe it so as to give effect to the plain meaning of the words used." [Citation omitted.]).

B. The Role of Policy Administrator Does Not Confer a Right to Receive or Share in the Cash Consideration.

Plaintiff's claimed entitlement to the Cash Consideration rests on the fact that it was Defendant's Policy Administrator and, in that capacity, paid his MLMIC insurance premiums (s*ee, e.g.*, R. 23, ¶¶27-29; R. 239, ¶5; R. 244, ¶27). It bears emphasis that a Policy Administrator is the "agent" of the Policyholder and is only conferred limited rights respecting the policy—i.e., "for the paying of Premium[s], requesting changes in the policy, … and for receiving dividends and any return Premiums when due" (R. 207 ¶4; R. 222; see also R. 185, para. 3). None of those limited rights entitled Plaintiff to the Cash Consideration, as set forth herein.

Moreover, since the Insurance Law, the MLMIC Plan of Conversion, and the DFS Decision make clear that the *Eligible Policyholders* are entitled to the Cash Consideration (*see, supra*), it is axiomatic that a *Policy Administrator* is not, by virtue of its limited rights as the Policyholder's agent, entitled to receive or share in the Cash Consideration. Indeed, MLMIC repeatedly emphasized that a Policy Administrator may receive Cash Consideration only if the Policyholder expressly designates as such:

- Policyholder Information Statement: "The amount distributable to Eligible Policyholders shall be paid directly to each Eligible Policyholder unless such Eligible Policyholder has affirmatively designated in writing (using a designation form to be provided by MLMIC) a Policy Administrator …to receive such amount on its behalf …." (R. 131 ¶A.5; *see also* R. 132-133 ¶A.12).

- Plan of Conversion: "The amount distributable to each Eligible Policyholder shall be paid directly to such Eligible Policyholder unless such Eligible Policyholder has affirmatively designated a Policy Administrator … to receive such amount on its behalf, in which case such amount shall be distributed to such Designee." (R. 76 ¶6.3[f]).[5]

Notably, MLMIC explained to its constituents that prior Policy Administrator designations did not entitle those Administrators to receive the Cash Consideration. (*See* R. 224 [June 29, 2018 MLMIC Notice]: "[C]urrent policy administrator designations on file with MLMIC do not extend to the distribution of the cash amounts allocated to eligible policyholders.")[6]

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[5] It is undisputed that Defendant did not sign the Consent Form required by MLMIC to make Plaintiff a "Designee" for receipt of the Cash Consideration (R. 26, ¶47; R. 46, ¶110; R. 208, ¶8).

[6] *See also* "MLMIC Provides Clarification of Ability to Make Assignments of Cash Consideration"; MLMIC Blog, August 7, 2018, accessible at https://www.mlmic.com/blog/dentists/clarification-of-ability-to-make-assignments-of-cash-consideration ("[T]he previous appointments do not extend to the distribution of the cash consideration.").

In short, there is nothing about the status of the Policy Administrator/agent that confers any right to receive the proceeds of the Policyholder/principal's Membership Interest. Clearly, if a Policy Administrator were entitled to the Cash Consideration by reason of its prior appointment, the Plan of Conversion would have provided so. <u>It did not – the Plan requires an express designation by the Policyholder</u>. *See Bank of N.Y. v. Janowick*, 470 F.3d 264, 274 (6th Cir. 2006) ("the mutual company's demutualization plan defines…rights [to proceeds]."). *See also Shoback*, p.3. ("The rights to the proceeds of a demutualization of a mutual insurance company are defined by the company's 'Conversion Plan'." [citing *Bank of N.Y.*]); *Maple-Gate*, 96 N.Y.S.3d at 841-42 ("Being designated as the policy administrator did <u>not</u> make the plaintiff a policyholder, did <u>not</u> make the plaintiff a member of MLMIC and did <u>not</u> entitle the plaintiff to the cash consideration." [Emphasis added]).

C. <u>Plaintiff's Payment of Premiums Did Not Confer a Right to the Cash Consideration.</u>

Plaintiff's contention that its payment of Defendant's premiums entitled it to the Cash Consideration is incorrect for several reasons.

First, as explained above, a Policy Administrator by definition pays the policy premiums; and, despite payment of premiums, the Plan of Conversion (as well as Insurance Law § 7307[e][3] and the DFS Decision) expressly provided that the Consideration was to be paid to Eligible Policyholders, and not to Policy

Administrators unless specifically so designated.

Second, Plaintiff's contention misunderstands the basic structure and operation of a mutual insurance company. It is well-settled that policyholders under a mutual insurance company "receive both membership interests … and contract rights." *Bank of N.Y.*, 470 F.3d at 267. Membership interests are acquired "at no cost" as "an incident of the structure of mutual insurance policies." *Dorrance v. U.S.*, 809 F.3d 479, 481 & 485 (9th Cir. 2015). On the other hand, "premium payments go toward the actual cost of the…[contractual] insurance benefits provided," with any surplus returned as premium refunds.[7] *Id*. The foregoing was expressly recognized by the Supreme Court in *Shoback*:

> "Policyholders in a mutual insurance company acquire two separate types of rights - contractual rights and membership rights. The contractual rights are paid for by the premiums, and pay for the cost of the insurance itself. …
>
> The membership rights are acquired at "no cost", and are in fact, a benefit of being the policyholder, *Dorrance v. United States*, at 485. They do not arise as a result of paying the premiums, but are intrinsic to the owner of the policy, the policyholder." *Shoback*, at 4 (citing *Dorrance*).

The *Shoback* court's discussion of *Dorrance* was apt given the Ninth Circuit Court of Appeals' holding therein).:

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[7] *See also Dorrance*, 809 F.3d at 487-88 (quoting IRS Revenue Ruling 71-233 ["Payment by each policyholder of the premiums called for by the insurance contracts issued by X represents payment for the cost of insurance and an investment in his contract but <u>not an investment in the assets of X</u>. His proprietary interest in the assets of X arises solely by virtue of the fact that he is a policyholder of X." (Emphasis added)]).

> "The membership rights were assigned a monetary value at the time of the exchange only as a consequence of the demutualization process. The error of the Dorrances and the district court was to assume that the value received upon demutualization was linked with some premium value paid by the policyholders in the past. But the stock the Dorrances received in exchange for the membership rights cannot be understood as a partial return on their past premium payments and it is well understood that policyholders do not contribute capital to the companies." *Dorrance*, 809 F.3d at 486 (emphasis added))..

Like in *Dorrance*, Defendant's MLMIC premiums were <u>not</u> paid for or allocated to his Policyholder Membership Interest. Thus, Plaintiff's argument that its payment of premiums entitled it to the Cash Consideration from the extinguishment of Defendant's Membership Interest is unavailing. *See Shoback*, at 4 (discussing *Dorrance* and noting that "[Employer's] argument - that it paid the premiums and as such is entitled to the funds, is unpersuasive.").

Third, Plaintiff's payment of Defendant's MLMIC premiums was a contractual obligation under the Employment Agreement, for which Plaintiff received a bargained-for exchange of consideration: Defendant agreed to devote his professional services (and generate revenue) on behalf of Plaintiff; and, in exchange, Plaintiff agreed to pay Defendant compensation and, among other things, administer and pay the premiums on his MLMIC Policy (R. 212-213, ¶¶ 2, 4, 7.a).

Plaintiff does not dispute that it received what it bargained for – Defendant's services, and the resulting revenue – and in turn, Defendant received, among other things, a MLMIC insurance policy, which included a Membership Interest in

MLMIC. Any interest that Plaintiff alleges to have in Defendant's Membership Interest—which was incidental to the MLMIC Policy he obtained under his Employment Agreement—would need to have been, but was not, provided for in his Employment Agreement. Further, as the *Shoback* court observed:

> "[Employer] paid the premiums as part of its obligation under the Employment Agreement with [employee]. She provided services and in return [employer] was confident that she was covered (and hence it was covered) in terms of malpractice insurance. This arrangement benefited both parties." *Shoback*, at 4.

Finally, Plaintiff's argument that it is entitled to the Cash Consideration because it received dividends or premium refunds in its capacity as Policy Administrator (*see, e.g.*, R. 240, ¶5.g.) is plainly without merit. Mutual insurance company dividends "bear[] no relation to a dividend upon stock…" (*Menin v. N.Y. Life Ins. Co.*, 188 Misc. 870, 871 [Sup. Ct. N.Y. Cty. 1941]); they are "a partial return" of premiums. *Towne Bus Corp. v. Ins. Co. of Greater N.Y.*, 18 Misc. 3d 1121(A), 2008 NY Slip Op 50149(U), ¶ 4 (Sup. Ct. N.Y. Cty. Jan. 18, 2008); *Dorrance*, 809 F.3d at 481. As explained in detail above, the MLMIC payout represents cash consideration payable to Policyholders in exchange for the extinguishment of their Policyholder Membership Interests. The Consideration is therefore clearly not a dividend/premium refund. *See Dorrance*, 809 F.3d at 486 ("But the stock the Dorrances received in exchange for the membership rights cannot be understood as a partial return on their past premium payments…." [Emphasis added]). *See also Hinds*, 2019 NY Slip Op 51508(U), ¶ 5 ("This cash contribution, by law, is not a return to the hospital of any insurance premiums it paid on behalf of the defendant, it represents the policyholder's share in MLMIC."); *Maple-Gate*, 96 N.Y.S.3d at 841 ("Unlike a [premium] refund, the cash consideration was clearly intended to be in exchange for the extinguishment of the defendants' membership interest in MLMIC."). As such, Plaintiff's receipt of dividends/premium refunds is entirely irrelevant to Defendant's entitlement to the Cash Consideration.

D. DFS Flatly Rejected That the Payor of Premiums Is Entitled to the Cash Consideration Under the Insurance Law or Plan of Conversion.

Plaintiff erroneously argued to the court below that it was the "policyholder" because it paid the premiums on the Policy (R. 26-27 ¶¶50-53, R. 240, ¶5[l]). As described below, Plaintiff made this very same argument at the DFS Hearing on the approval of the Plan of Conversion, and the DFS flatly rejected Plaintiff's position. Plaintiff then brought an Article 78 proceeding challenging the DFS Decision, and the Supreme Court (Westchester County) confirmed that the DFS Decision had a rational basis for its Decision.

At the DFS hearing on the proposed Plan of Conversion, Plaintiff argued that, under Insurance Law § 7307(e)(3) , the payors of the premiums (and not the Policyholders) are entitled to the Cash Consideration (R. 184 para. 3). The DFS flatly rejected Plaintiff's position in the DFS Decision:

> "One commenter [Maple Medical LLP] referred to the provision in Insurance Law § 7307(e) stating that in calculating each such person's equitable share one must factor in the amount 'such policyholder has properly and timely *paid* to the insurer on insurance policies in effect during the three years immediately preceding…' (emphasis added). The commenter suggested that this means that the person that paid the premium is automatically entitled to the proceeds of the sale. The Superintendent finds that this is **not determinative** because the same provision refers to the 'policyholder,' which might or might not be the person who paid the premiums." (*Id.* [emphasis added].)

Notably, Plaintiff relied on the same § 7307(e)(3) excerpt in its arguments to the court below (*see, e.g.* R. 26-27 ¶¶50-53).

Following issuance of the DFS Decision, Plaintiff commenced an Article 78 proceeding (*Matter of Maple Medical LLP, et al. v. New York State Dept. of Fin. Servs., et al.* [Index No. 65929/2018, Sup. Ct. Westchester County]) to challenge the Plan of Conversion's definition of "Policyholder" and its approval by the DFS Decision. Plaintiff argued that Insurance Law § 7307(e)(3) requires that "policyholders be defined under the conversion plan as the parties who actually paid the premiums and not the doctors who are insured under the policies." (R. 203 para. 3). The Westchester County Supreme Court refused to disturb the DFS Decision, holding that DFS had a rational basis for approving the Plan, including its definition of Policyholders (and their entitlement to the Cash Consideration) (*id.*). *See also Maple-Gate*, 96 N.Y.S.3d at 842 ("The DFS Decision reiterated that it was the policyholder who was entitled to the cash consideration.").

In sum, while Insurance Law § 7307(e)(3) "sets forth a formula regarding how to calculate the amount of consideration the policyholder would receive…[,] [n]o distinction is made between a policyholder who pays the premium out of his own pocket versus a policyholder whose employer pays the premium as part of an employee compensation package." *Maple-Gate*, 96 N.Y.S.3d at 841 (emphasis added). *See also Hinds*, 2019 NY Slip Op 51508(U), ¶ 4 (quoting *Maple-Gate*). Accordingly, as noted above, the Maple-Gate court concluded that "Insurance Law § 7307 does not confer an ownership interest in the stock or to the cash consideration to anyone other than the policyholder." *Maple-Gate* at 841 (emphasis added).

E. Defendant Did Not Assign His Membership Interest or Right to the Cash Consideration to Plaintiff.

As explained above, the payment of premiums does not entitle a Policy Administrator to the Cash Consideration, and the Plan provides that the Consideration is to be paid to the Policyholder unless the Policyholder has expressly designated the Policy Administrator to receive it. *See, e.g.*, *Maple-Gate*, 96 N.Y.S.3d at 841-42 ("Being designated as the policy administrator did not make the plaintiff a policyholder, did not make the plaintiff a member of MLMIC and did not entitle the plaintiff to the cash consideration.").

Accordingly, the Plan's objection and escrow provisions cannot be interpreted to mean an employer could have a valid claim to the Cash Consideration by virtue of its status as Policy Administrator or payment of Premiums. Such a construction would be entirely circular and would eviscerate the plain terms of the Plan. Instead, "[m]ore was required." *Id.* at 842. That "more" was delineated in the DFS Decision:

> "Insurance Law § 7307(e)(3) defines the policyholders eligible to be paid their proportional shares of the purchase price, but also recognizes that such policyholders may have *assigned* such legal right to other persons. Therefore, the plan appropriately includes an objection and escrow procedure for the resolution of disputes for those persons who dispute whether the policyholder is entitled to the payment in a given case." (R. 149 para. 4 [emphasis added]).

See also Maple-Gate, 96 N.Y.S.3d at 842 (DFS Decision recognized that Policyholders may have assigned their legal right to the Cash Consideration to others, and "tied eligibility for the… escrow process to when the policyholder had, in fact, assigned the right to cash consideration….").

Consistent with the foregoing, MLMIC's June 2018 Notice to Policyholders stated: "If there is a preference to have such distributions paid to a policy administrator as a matter of convenience or *as a result of contractual obligations* between you and your policy administrator, please execute the enclosed consent form…." (R. 224 [emphasis added]).

As the *Maple-Gate* court underscored, where there is no signed consent or assignment, "this alone is fatal to the [practice's] claim that it is entitled to the cash consideration." 96 N.Y.S.3d at 842. Here, it is undisputed that Defendant did <u>not</u> sign the Consent Form, and there is no allegation—let alone any evidence (there being none)—that Defendant agreed to assign to Plaintiff his Membership Interest or right to the Consideration.

Based on the foregoing, Defendant respectfully submits that Plaintiff's administration of Defendant's MLMIC Policy (including payment of premiums on his behalf) did not and does not entitle it to Defendant's share of the Cash Consideration. Rather, as the Eligible Policyholder, Defendant is entitled to the Consideration from the extinguishment of his MLMIC Membership Interest. Accordingly, the court below erred in granting summary judgment in favor of Plaintiff rather than in Defendant's favor.

II. *SCHAFFER* SHOULD NOT HAVE BEEN FOLLOWED BY THE COURT BELOW, AND INDEED THIS COURT IS NOT BOUND BY AND SHOULD NOT FOLLOW IT.

In *Schaffer*, the First Department—hearing the case in the first instance, on submitted facts, pursuant to CPLR 3222 —summarily held in four-sentences that the doctor/policyholder would be unjustly enriched if she received the Cash Consideration. The First Department reached its determination without considering or citing the New York Insurance Law, the Plan of Conversion, the DFS Decision, or New York unjust enrichment law, and without providing any reasoning for its conclusions. The *Schaffer* court's failure to cite to the Insurance Law, which expressly provides that mutual insurance companies are owned by their members, the policyholders (§ 1211) ., and must receive consideration in exchange for their membership interests (§ 7307) , is glaring.[8]

Nevertheless, the court below held that it was bound to blindly follow the First Department's Decision in *Schaffer*, and granted summary judgment in favor of Plaintiff. While the court below added in dicta that "the conclusions drawn in the First Department's decision are persuasive," and that payment to Defendant would result in his unjust enrichment, like *Schaffer*, it provided no rationale for its Decision or how it comports with controlling New York Insurance or unjust enrichment law.

Schaffer, however, was not binding on the court below because it is distinguishable procedurally and factually from this case, conflicts with established Court of Appeals and Second Department unjust enrichment precedent, was based on deficient legal arguments, and relied solely upon inapposite ERISA cases to decide a non-ERISA matter governed by state law. Moreover, it is axiomatic that, in any event, the First Department's Decision in *Schaffer* is not binding on <u>this</u> Court and should not be followed for the reasons herein.

A. <u>The Unique Procedural Posture and Facts in *Schaffer* Are Distinguishable.</u>

In *Schaffer*, the parties commenced an action under CPLR 3222 and requested that the First Department hear the case and issue a declaratory judgment based solely on stipulated facts. By contrast, the parties here are not operating under the unique

[8] This is most likely attributable to the fact that neither of the parties in the *Schaffer* case ever cited to or discussed Insurance Law § 7307 in their briefs (*see, infra*, Point II[D]).

procedural posture of CPLR 3222. Moreover, in *Schaffer*, the parties stipulated that the MLMIC policy was issued to the employer (the doctor had been "added onto the professional liability insurance policy issued to Schaffer, Schonholz & Drossman LLP") (R. 314-315, ¶12). Here, it is undisputed that Defendant's policy was an individual policy, and Defendant was the sole Insured and sole Policyholder under his policy (R. 207, ¶4; R. 226). This distinguishing fact is significant inasmuch as (a) here, Defendant's claims are premised on his being the sole Policyholder, and therefore the sole owner of his MLMIC Membership Interest, and (b) the ERISA cases relied upon by the *Schaffer* court concerned group insurance policies issued to employers, rather than the individual MLMIC policy issued to Defendant herein.

B. The Lower Court's (and *Schaffer* Court's) Conclusion That Defendant Did Not Bargain for the Consideration Fundamentally Misunderstands That He Bargained for His MLMIC Policy and Received His Membership Interest as an Incident Thereto.

Underlying the lower court's Decision (based on *Schaffer*) is the misconception that Defendant did not "bargain" for the Cash Consideration. Even putting aside that the employer did not bargain for the Consideration,[9] the above conclusion is fundamentally at odds with the terms of the parties' Employment

[9] It is beyond cavil that Plaintiff did not bargain for Defendant's Membership Interest or the proceeds thereof (i.e., the Cash Consideration). As Defendant's Policy Administrator, Plaintiff was merely Defendant's "agent" and was entitled to receive dividends/refunded premiums only. The Cash Consideration is not a dividend/premium refund. (*See, supra*, Point I[C]).

Agreement, the basic structure and operation of a mutual insurance company, and the corresponding statutory scheme under the Insurance Law.

In accordance with the Employment Agreement, Defendant agreed to provide his professional services in exchange for, among other things, Plaintiff's agreement to provide him with (and pay for) a malpractice policy (R. 206-207, ¶¶ 2 - 4; R. 212, ¶¶2, 4, 7.a). When Plaintiff selected MLMIC as the insurer, Defendant received the rights that came with his MLMIC policy. As explained above (at Points I[A] & [C]), under the Insurance Law, "when the [policyholders], at the [employer's] behest, signed up for professional liability policies issued by MLMIC, they acquired certain rights and benefits, <u>including membership in MLMIC</u>." *Maple-Gate*, 96 N.Y.S.3d at 841 (emphasis added). *See also Shoback*, at 4 ("Policyholders in a mutual insurance company acquire two separate types of rights – contractual rights and membership rights."). As also explained above (at Point I[A]), the Insurance Law and Plan of Conversion are clear that when a mutual insurance company converts to a stock insurance company, the policyholders are entitled to the cash consideration paid on account of the extinguishment of their membership interests.

Schaffer (and in turn the lower court) notably ignored these basic concepts by disconnecting the Membership Interest from the MLMIC policy and positing that the employee did not bargain for the inherent rights attendant to becoming a MLMIC policyholder. But in so doing, the *Schaffer* and lower court disregarded that (a) under the Insurance Law, the employee obtained a Membership Interest by virtue of becoming--and when he or she became--a MLMIC Policyholder, and (b) the employer's payment of its employee's MLMIC premiums was part of a bargained-for exchange of consideration under the employment agreement.[10]

In sum, the argument that Defendant did not "bargain" for the Membership Interest or Cash Consideration is unavailing. Defendant bargained for a malpractice policy. Plaintiff places great emphasis on the fact that it selected and procured Defendant's MLMIC Policy (R. 23 ¶¶ 14-16, R. 239 ¶¶ 5.a.-d.). Plaintiff fails to recognize that when it elected to provide Defendant with a MLMIC policy, he received a Membership Interest and all of the attendant rights of a MLMIC Policyholder. Those rights included the right to receive Cash Consideration in exchange for the extinguishment of his Membership Interest.[11]

C. ***Schaffer* Was Not Binding on the Court Below (and Should Not Be Followed by This Court) Because It Conflicts with Established Court of Appeals and Second Department Precedent.**

It is axiomatic that a trial court is not required to follow another Appellate Division department's decision where the Court of Appeals or its own department

[10] Indeed, the *Schaffer* court did not reference the parties' employment agreement at all.

[11] The controlling provisions of the Insurance Law (§§ 1211. and 7307) were enacted in 1984. Accordingly, Plaintiff knew (or should have known)--and cannot claim ignorance--as to the fact that Defendant obtained a Policyholder Membership Interest as an incident to becoming (and by virtue of becoming) a Policyholder, and that upon demutualization, the Policyholders would be entitled to the Cash Consideration under the Insurance Law.

has pronounced a contrary rule of law. *See generally Mountain View Coach Lines, Inc. v. Storms,* 102 A.D.2d 663, 664 (2d Dep't 1984); *Vidal v. Maldonado*, 23 Misc. 3d 186, 213 (Sup. Ct. Bronx Cty. 2008). Here, *Schaffer*'s holding--that the policyholder's receipt of the Cash Consideration would constitute unjust enrichment--was not binding on the court below (and should not be followed by this Court) because it conflicts with established Court of Appeals and Second Department precedent.

It is well-settled that the unjust enrichment "doctrine is a narrow one; it is 'not a catchall cause of action to be used when others fail.'" *E.J. Brooks Co. v. Cambridge Sec. Seals*, 31 N.Y.3d 441, 455 (2018). An allegation that a party "received benefits, standing alone, is insufficient to establish a cause of action to recover damages for unjust enrichment…. Critical is that under the circumstances and as between the two parties to the transaction the enrichment be unjust." *Goel v. Ramachandran*, 111 A.D.3d 783, 791 (2d Dep't 2013) (internal citations omitted).[12]

The typical unjust enrichment cases are those where defendant received a benefit from plaintiff "'without adequately compensating plaintiff therefor'" (*Smith v. Chase Manhattan Bank, USA, N.A.*, 293 A.D.2d 598, 600 [2d Dep't 2002]), or those "in which the defendant, though guilty of no wrongdoing, has received money

[12] *See also Clark v. Daby*, 300 A.D.2d 732, 732 (3d Dep't 2002) ("the mere fact that the plaintiff's activities bestowed a benefit on the defendant is insufficient to establish a cause of action for unjust enrichment").

to which he or she is not entitled." *E.J. Brooks Co.*, 31 N.Y.3d at 455; *see also Maple-Gate*, 96 N.Y.S.3d at 841 ("an unjust enrichment claim presupposes that the plaintiff has an ownership interest in the property or benefit it seeks to recover from the defendants."). Neither situation applies here.

First, as explained above, under the Employment Agreement, Defendant agreed to devote his professional services to generating revenue for Plaintiff, in exchange for which Plaintiff agreed to provide Defendant with, among other things, his malpractice policy. Plaintiff was therefore compensated for, and cannot base an unjust enrichment claim on, its payment of premiums. *See Smith*, 293 A.D.2d at 600 (no unjust enrichment claim where "the benefits received were less than what these purchasers bargained for."); *Fruchthandler v. Green*, 233 A.D.2d 214, 215 (1st Dep't 1996) (dismissing plaintiff's unjust enrichment claim because defendant provided consideration for the benefit plaintiff provided).

Second, *Schaffer* (and the court below) failed to explain how Defendant's receipt of money rightfully belonging to him under the Insurance Law, Plan of Conversion and DFS Decision is improper or inequitable, or how the Cash Consideration belongs to Plaintiff (something the defendant in *Schaffer* did not even allege). *See CDR Creances S.A. v. Euro-Am. Lodging Corp.*, 40 A.D.3d 421, 422 (1st Dep't 2007) ("unjust enrichment cause of action was properly dismissed for failure to identify any improper benefit"); *Clifford R. Gray, Inc. v. LeChase Constr.*

Servs., LLC, 31 A.D.3d 983, 988 (3d Dep't 2006) ("[P]laintiff asserts no facts suggesting that defendant is in possession of money or property belonging to plaintiff."); *A & A Assocs. v. Olympic Plumbing & Heating Corp.*, 306 A.D.2d 296, 297 (2d Dep't 2003) (Plaintiff raised no issue of fact as to whether respondents derived a benefit that belonged to plaintiff, which is necessary for an unjust enrichment claim.). *See also Shoback* at 4-5 (The fact that the Cash Consideration is "a 'windfall' does not, per se, render it illicit or unjust. The Court is certainly inclined to agree with the plain language of the Plan and the Insurance Law that in this case, plaintiff, the policyholder should be entitled to receive [the Consideration].").

Moreover, under established Court of Appeals and Second Department precedent, an unjust enrichment claim is precluded where the claim arises out of the subject matter of a written agreement:

> "'[T]he theory of unjust enrichment lies as a quasi-contract claim.' It is an obligation imposed by equity to prevent injustice, in the absence of an actual agreement between the parties concerned. Where the parties executed a valid and enforceable written contract governing a particular subject matter, recovery on a theory of unjust enrichment for events arising out of that subject matter is ordinarily precluded.'" *IDT Corp. v. Morgan Stanley Dean Witter & Co.*, 12 N.Y.3d 132, 142 (2009).[13]

[13] *See also ISS Action, Inc. v. Tutor Perini Corp.*, 170 A.D.3d 686, 690 (2d Dep't 2019) ("'[A] party may not recover in quantum meruit or unjust enrichment where the parties have entered into a contract that governs the subject matter.'" [citation omitted]); *Rayham v. Multiplan*, Inc., 153 A.D.3d 865, 869 (2d Dep't 2017) (An unjust enrichment cause of action "cannot be maintained if there is a valid, enforceable contract governing the same subject matter….").

Plaintiff's unjust enrichment claim is squarely based on having provided Defendant with his MLMIC policy and paid his premiums pursuant to the Employment Agreement. However, the Agreement unequivocally defined the parties' rights and obligations as to his policy and the premium payments. Specifically, Defendant agreed to provide full-time medical services to Plaintiff's patients and generate revenue for Plaintiff; and in return, Plaintiff agreed to, *inter alia*, provide and pay for his malpractice policy. Moreover, since Plaintiff agreed to pay Defendant's premiums as part of the bargained-for, contractual exchange of consideration, and Defendant acquired a Membership Interest as an incident to being a Policyholder, then that Membership Interest was part and parcel of the contractual benefit that Plaintiff provided in exchange for his services.

The foregoing is also supported by the long-established New York rule of construction that "'unless a contract provides otherwise, the law in force at the time the agreement is entered into becomes as much a part of the agreement as though it were expressed or referred to therein.'" *Burns v. Burns*, 163 A.D.3d 210, 213 (4th Dep't 2018) (*quoting Dolman v. United States Tr. Co.*, 2 N.Y.2d 110, 116 [1956]). *See also Kasen v. Morrell*, 6 A.D.2d 816, 817 (2d Dep't 1958) (same). In other words, Plaintiff's agreement to provide Defendant with (and pay for) a malpractice insurance policy must be "interpreted consistently with the corresponding statutory scheme." *Burns*, 163 A.D.3d at 213. That statutory scheme confirms that Defendant obtained a Membership Interest when he became, and by virtue of his becoming, a MLMIC Policyholder; and when that Membership Interest was extinguished, he was entitled to the Cash Consideration paid for it. *See* Insurance Law § 1211(a) . (a mutual insurance company is owned by its members, and the members are the policyholders) & § 7307[e][3]) (upon demutualization, policyholders are entitled to consideration in exchange for the extinguishment of their membership interests).

In sum, since the Employment Agreement indisputably governed Plaintiff's payment of premiums, its unjust enrichment claim based on those same payments fails as a matter of law. *See IDT Corp.*, 12 N.Y.3d at 142 (dismissal of unjust enrichment claim was warranted because plaintiff's payment of the fees at issue "arose from services governed by an engagement letter"); *ISS Action, Inc.*, 170 A.D.3d at 690 (Summary judgment dismissing unjust enrichment claim was proper because "defendant established, prima facie, that the payment of applicable taxes was expressly provided for in the parties' agreements. Indeed, the plaintiff's complaint alleges as much.") .

D. <u>Only Limited Arguments Were Presented to the First Department in the *Schaffer* Case.</u>

Even assuming *arguendo* that *Schaffer* did not conflict with the above controlling precedent, *Schaffer* would still <u>not</u> have been binding precedent on the court below.

It is well-settled that "a case 'is precedent only as to those questions presented, considered and squarely decided.'" *Wellbilt Equip. Corp. v. Fireman*, 275 A.D.2d 162, 168 (1st Dep't 2000) (emphasis added); *Goddard v. Martino*, 40 Misc. 3d 1050, 1057 (Sup. Ct. Dutchess Cty. 2013).[14] In *Schaffer*, the parties' Briefs presented extremely deficient arguments that, among other things, lacked any citation to the controlling statute and case law, and omitted documentary evidence (*e.g.*, DFS Decision)—thereby eviscerating any precedential value of the decision.

Specifically, petitioner-employer's opening Brief (a) was entirely devoid of any reference to the controlling statute governing demutualization (Insurance Law § 7307[e][3]) , the MLMIC Plan of Conversion, or the DFS Decision, (b) failed to cite any New York case law as to the employer's alleged entitlement to the Cash Consideration, and (c) did not argue—let alone use the words—unjust enrichment (R. 324-342). Instead, the employer selectively quoted inapposite ERISA cases (which involved questions of Federal law unique to ERISA employee benefit plans) to support its conclusory argument that it was entitled to the Cash Consideration based on its payment of the doctor's MLMIC premiums (*id.*).

In opposition, the doctor simply argued that she was entitled to the Consideration because she was the named Policyholder, (a) without explaining *why*

[14] *See also Yellow Book of Ny L.P. v. Dimilia*, 188 Misc. 2d 489, 495 (Dist. Ct. Nassau Cty. 2001); *Williams v. AGK Commc'ns, Inc.*, 143 Misc. 2d 845, 848 (Sup. Ct. Onondaga Cty. 1989).

under the Insurance Law, the Plan of Conversion, the DFS Decision, and New York law, (b) without citing § 7307(e)(3) or any New York case law, and (c) without referencing unjust enrichment (R. 343-356). On reply, the employer impermissibly argued unjust enrichment for the first time and, in support thereof, cited (a) non-binding arbitration decisions,[15] (b) dicta from a Connecticut case concerning only the question of arbitrability under the parties' contract,[16] (c) inapposite ERISA cases, and (d) one distinguishable First Department case[17] (R. 357-374).

Based on the above limited briefing, and relying solely upon two ERISA cases,[18] the First Department issued a Decision that, *in four sentences*, summarily held that the doctor would be unjustly enriched by receiving the Cash Consideration. *Schaffer*, 171 A.D.3d 465. Again, the First Department cited no New York Insurance Law, made no reference to the Plan of Conversion or the DFS Decision, relied upon no New York unjust enrichment law, and provided no reasoning for its

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[15] *See New York Cent. Mut. Fire Ins. Co. v. 563 Grand Med., P.C.*, 4 Misc. 3d 1020(A) (Sup. Ct. Otsego Cty. 2004) ("These [arbitration] decisions have no precedential value as they are not determinations of law, and because an arbitrator is not bound by substantive law or rules of evidence.").

[16] *Town of N. Haven v. N. Haven Educ. Ass'n*, 2004 Conn. Super. LEXIS 15 (Conn. Super. Ct. Jan. 5, 2004).

[17] *Castellotti v. Free* (138 A.D.3d 198 [1st Dep't 2016]) (a) was an appeal of a motion to dismiss (and thus did not reach the merits of the unjust enrichment claim), (b) involved an alleged oral agreement that failed under the statute of frauds (as opposed to the controlling Employment Agreement at issue herein), and did not involve the unjust enrichment arguments made by Plaintiff below (or herein).

[18] *See, infra*, Point II(E).

conclusion. *Id.* Significantly, "a precedent is less binding if [like *Schaffer*] it is little more than an ipse dixit, a conclusory assertion of result, perhaps supported by no more than generalized platitudes." *People v. Hobson*, 39 N.Y.2d 479, 490 (1976).

In short, it is beyond cavil that the issues raised before the court below (and herein)—including that Insurance Law § 7307(e)(3) , the Plan of Conversion and the DFS Decision warrant a declaratory judgment in Defendant's favor; that MLMIC premiums were not paid for, or allocated to, the Membership Interests, but rather were paid for as part of the contractual exchange of consideration between the parties; and that Plaintiff's contractual obligation to pay Defendant's premiums as part of their exchange of consideration precludes Plaintiff's unjust enrichment claim—were "neither briefed nor presented to the [First Department] for adjudication," nor were they "squarely decided." *Wellbilt Equip. Corp.*, 275 A.D.2d at 168. *See also Goddard*, 40 Misc. 3d at 1057 ("There is no indication that this issue was ever presented to or considered by the Third Department, and it was certainly never squarely decided.").[19] As such, *Schaffer* was not binding precedent on the court below and, likewise, should have no precedential value on this appeal.

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[19] *See also Rodriguez v. City of N.Y.*, 31 N.Y.3d 312, 321-22 (2018) ("Thoma never addressed the precise question" at bar; "[t]he decision itself never considered the import of article 14-A….").

E. <u>The ERISA Cases Cited in *Schaffer* Are Plainly Inapposite.</u>

The two ERISA cases cited in *Schaffer*—(i) *Ruocco v. Bateman, Eichler, Hill, Richards, Inc.* (903 F.2d 1232 [9th Cir. 1990]) ("*<u>Ruocco</u>*"); and (ii) *Chi. Truck Drivers, Helpers & Warehouse Workers Union (Indep.) Health & Welfare Fund v. Local 710, Int'l Brotherhood. of Teamsters* (2005 U.S. Dist. LEXIS 42877 [N.D. Ill. Mar. 4, 2005]) ("*<u>Chi. Truck</u>*")—are plainly inapposite because <u>neither involved a state law unjust enrichment claim</u>.[20]

Instead, both *Ruocco* and *Chi. Truck* concerned whether demutualization proceeds were ERISA "plan assets"—a question clearly not involved here. Whether the proceeds were "plan assets" was material because ERISA plan assets generally cannot "inure to the benefit of any employer and shall be held for the exclusive purposes of providing benefits to participants in the plan and their beneficiaries…." 29 U.S.C. § 1103(c)(1). Ultimately, the *Ruocco* and *Chi. Truck* courts determined whether the demutualization proceeds were plan assets (and if so, to whom they were entitled) by looking to the applicable Department of Labor ("**DOL**") ERISA

[20] Indeed, ERISA would have preempted a state law unjust enrichment claim. *See* 29 U.S.C. § 1132(a)(3) [ERISA § 502(a)(3)]; *Cleghorn v. Blue Shield*, 408 F.3d 1222, 1225 (9th Cir. 2005).

advisory opinions,[21] ERISA statutes,[22] and any contracts or legal instrument related to the ERISA plans.

Significantly, neither *Ruocco* nor *Chi. Truck* references any plan-related contracts or documentation that provided guidance as to the distribution of the demutualization proceeds. By contrast, in the instant case, the Plan of Conversion and the DFS Decision, as well as Insurance Law §§ 1211(a) . and 7307(e)(3) , expressly provide that (a) the Policyholders are the owners of their Membership Interests, and (b) absent a designation or assignment to the Policy Administrator (neither of which occurred here), the Policyholders are entitled to the Cash Consideration paid on account of the extinguishment of their Membership Interests. *See RLJCS Enters. v. Prof'l Benefit Trust, Inc.*, 438 F. Supp. 2d 903, 912 (Dist. Ct. N.D. Ill. 2006) (declining to "balance the equities" as in *Ruocco* because "in the instant case, there was a contract that governed the administration of the Trust, and that contract stated that the Trust, not the plaintiffs, owned the policies.").

Simply put, the foregoing demonstrates that the facts and legal issues in *Ruocco* and *Chi. Truck* bear no resemblance to those here. ERISA is not implicated

[21] *Ruocco* pre-dated the applicable ERISA advisory opinions (cited in *Chi. Truck*), and it appears that neither the ERISA statutes, nor any plan-related documents, provided any direction as to the distribution of demutualization funds. As such, the court resorted to balancing the equities. In *Chi. Truck*, however, the court was guided by the DOL ERISA advisory opinions. 2005 U.S. Dist. LEXIS 42877 at ¶¶ 8-10, 20-21.

[22] In *Chi. Truck*, the demutualization funds were considered plan assets of the In-House Pension Plan, but the funds reverted to the employer pursuant to ERISA's residual asset rule (29 U.S.C. § 1344[d]).

in the instant case; thus, the determinations in *Ruocco* and *Chi. Truck* as to ERISA plan assets are neither relevant nor persuasive. Rather, it is Insurance Law § 7307(e)(3) , the Plan of Conversion, the DFS Decision, established New York unjust enrichment law, and the employment agreement that govern. Moreover, as opposed to *Ruocco* and *Chi. Truck*, the Plan of Conversion (and § 7307 and the DFS Decision) provided that absent a designation or assignment in favor of the Policy Administrator, the Cash Consideration was to be distributed to <u>Policyholders</u>. (*See, supra*, Point I[E]). Accordingly, *Schaffer*'s reliance on the above ERISA cases was misplaced.

In sum, Defendant respectfully submits that *Schaffer* was not binding on, and should not have been followed by, the lower court—and should not be followed by this Court. At best, *Schaffer* is an "'errant footprint barely hardened overnight'" which the Court should avoid treating "'as an inescapable mold for future travel.'" *People v. Gonzales*, 96 A.D.2d 847, 848 (2d Dep't 1983) (quoting *Hobson*, 39 N.Y.2d at 488).

III. THE NEW YORK COURTS THAT HAVE SUBSTANTIVELY ANALYZED THE CONTROLLING STATUTORY AUTHORITY AND DOCUMENTARY EVIDENCE SUPPORT DEFENDANT'S POSITION.

It bears emphasis that the New York courts that have substantively analyzed the controlling statutory and documentary authority, together with the basic structure and operation of mutual insurance companies and controlling unjust enrichment law—all as described herein—support Defendant's position here. Specifically, in *Maple-Gate Anesthesiologists, P.C. v. Nasrin* (96 N.Y.S.3d 837 [Sup. Ct. Erie Cty. 2019]), the Erie County Supreme Court ardently dismissed the complaint of a medical practice that claimed it was entitled to the Cash Consideration based on its payment of premiums. In so doing, the *Maple-Gate* court, among other things, (a) confirmed that "Insurance Law § 7307 does not confer an ownership interest … to the cash consideration to anyone other than the policyholder," (b) stressed that unlike a premium refund (to which the practice had been entitled as Policy Administrator), "the cash consideration was clearly intended to be in exchange for the extinguishment of the defendants' membership interest in MLMIC," and (c) held that "[b]eing designated as the policy administrator did not make the plaintiff [employer] a policyholder, did not make the plaintiff a member of MLMIC and did not entitle the plaintiff to the cash consideration." 96 N.Y.S.3d at 841-42.

In *Columbia Mem'l Hosp. v. Hinds* (2019 NY Slip Op 51508(U), ¶¶ 1-2 [Sup. Ct. Columbia Cty. 2019]), the court affirmed that Insurance Law § 7307(e)(3) "repeatedly refers to those eligible for cash consideration as the 'policyholder,'' and that the statute makes no distinction "'between a policyholder who pays the premium out of his own pocket versus a policyholder whose employer pays the premium as part of an employee compensation package.'" *Id.*, ¶ 4 (quoting *Maple-Gate*) . Rejecting the argument that the policyholder did not bargain for the Cash

Consideration, the court explained:

> "In all likelihood neither party appreciated that a windfall could occur as a result of the MLMIC sale, because, quite simply, they did not appreciate the meaning and the value of an ownership stake prior to the demutualization plan. It cannot therefore be said that this cash contribution was negotiated or bargained for, but is simply rather an operation of law, and therefore no one's interest in the actual contract was compromised. This cash contribution, by law, is not a return to the hospital of any insurance premiums it paid on behalf of the defendant, it represents the policyholder's share in MLMIC." *Id.*, ¶ 5 (citations omitted).

Moreover, the *Columbia Mem'l Hosp.* court acknowledged *Schaffer* and the doctrine of stare decisis, but held that *Schaffer* was distinguishable based on the specific facts stipulated to therein. The court emphasized that, "it is equally well established that courts are free to correct prior erroneous interpretations of the law," such as *Schaffer*. 2019 NY Slip Op 51508(U), ¶¶5-6 (citing *In re Charles A. Field Delivery Serv.*, 66 N.Y.2d 516, 518-19 [1985]).

Finally, in *Shoback v. Broome Obstetrics and Gynecology, P.C.* (Index No. EFCA2018003334, at 4 [Sup. Ct. Broome Cty. 2019]) (see Addendum A hereto), the court confirmed that "[t]he language of the Plan is clear and unambiguous, and as such must be accorded the plain meaning of its terms"—namely that "plaintiff is entitled to the money." In short, the *Shoback* court held that "Defendant's argument - that it paid the premiums and as such is entitled to the funds, is unpersuasive," explaining:

> "Here, the defendant paid the premiums as part of its obligation

> under the Employment Agreement with plaintiff. She provided services and in return defendant was confident that she was covered (and hence it was covered) in terms of malpractice insurance. This arrangement benefitted both parties. … The bottom line is that the cash consideration that is generated as a result of demutualization is a 'windfall', or 'a pot of money no one expected or even envisioned.' Here, it was a result of a restructuring of a mutual insurance company into a stock company. However, negative connotations aside, the fact that this is a 'windfall' does not, per se, render it illicit or unjust. The court is certainly inclined to agree with the plain language of the Plan and the Insurance Law that in this case, plaintiff, the policyholder should be entitled to receive it." *Shoback*, at 4-5.[23]

Although the *Maple-Gate*, *Columbia Mem'l Hosp.* and *Shoback* decisions, like *Schaffer*, are not binding on this Court, they support the Court's reversal of the lower court's Decision, and grant of declaratory judgment in Defendant's favor.

IV. THE COURT BELOW ERRED IN DIRECTING MLMIC TO TURN OVER THE CASH CONSIDERATION TO PLAINTIFF; THIS COURT SHOULD DIRECT PLAINTIFF TO TURN THE FUNDS OVER TO DEFENDANT.

Pursuant to the escrow procedure set forth in MLMIC's Plan of Conversion—which was twice approved by the DFS (in its September 6, 2018 Decision and January 14, 2019 Order—MLMIC or its escrow agent was required to hold the Cash Consideration in escrow pending receipt of (a) "joint written instructions from the Eligible Policyholder and the Policy Administrator … as to how the allocation is to be distributed," or (b) "a *non-appealable* order of an arbitration panel or court with

[23] Ultimately, the *Shoback* court held that as a trial court, it was bound to "a higher court's existing precedent 'even though [it] may disagree.'" Shoback, at 5.

proper jurisdiction ordering payment of the allocation to the Policy Administrator … or the Eligible Policyholder." [R. 184; R. 383] (emphasis added). In furtherance of the Plan's escrow procedures, the parties expressly agreed by Stipulation dated May 6, 2019, that "MLMIC shall hold the funds in escrow pending a further stipulation of the parties or a final non-appealable order or judgment of the Court" (R. 375).

Notwithstanding the foregoing, the lower court's Decision directed MLMIC to release from escrow and pay to Plaintiff the Defendant's share of the Cash Consideration "in the amount of $128,148.92 plus interest, if any, … within fifteen (15) days of the service of this Order, with Notice of Entry, upon the Escrow Agent" (R. 11). By letter dated July 11, 2019, counsel for Defendant notified the court below of Defendant's intent to appeal the Decision and requested that the court modify its Decision to correspond with the established escrow procedure. The court below took no action, and MLMIC subsequently disbursed the Cash Consideration (plus accrued interest) to Plaintiff.

In short, the Decision was appealable; thus, the court below improperly disregarded the Plan's escrow provisions by ordering MLMIC to remit the Cash Consideration to Plaintiff. Defendant respectfully requests that this Court correct the lower court's error and direct Plaintiff to pay over to Defendant all amounts it received from MLMIC or its escrow agent, including accrued interest.

CONCLUSION

Based upon the foregoing, and on the Record herein, Defendant-Appellant respectfully requests that this Court reverse the Decision of the Court below in its entirety, deny Plaintiff's Cross-Motion for summary judgment, and grant Defendant's motion for summary judgment in his favor.

Dated: December 3, 2019
Albany, New York

NOLAN HELLER KAUFFMAN LLP

By: ______________________
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ADDENDUM "A"

COPY OF SEPTEMBER 12, 2019 UNREPORTED DECISION AND ORDER OF THE BROOME COUNTY SUPREME COURT (HON. MOLLY REYNOLDS FITZGERALD J.S.C.) IN THE MATTER OF
JENNIFER SCHOBACK, CNM, f/k/a JENNIFER M. DAVIDSON, CNM v. BROOME OBSTETRICS AND GYNECOLOGY, P.C.

At a Motion Term of the Supreme Court of the State of New York, held in and for the Sixth Judicial District, at the Broome County Courthouse, Binghamton, New York on the 28th day of June, 2019.

PRESENT: HON. MOLLY REYNOLDS FITZGERALD
JUSTICE PRESIDING

STATE OF NEW YORK
SUPREME COURT : COUNTY OF BROOME

JENNIFER M. SHOBACK, CNM, f/k/a JENNIFER M. DAVIDSON, CNM,

Plaintiff,

-against-

BROOME OBSTETRICS AND GYNECOLOGY, P.C,

Defendant.

DECISION AND ORDER

Index No.: EFCA2018003334

This declaratory action asks the court to answer the question: When a mutual liability insurance company demutualizes, who is entitled to the distribution payment - the employer, who has paid the premiums, or the employee who is the policyholder?

FACTS

Plaintiff, Jennifer Shoback, was employed by defendant, Broome Obstetrics, as a certified nurse midwife from July, 2015 - August, 2017. Her employment was pursuant to an Employment Agreement which provided the employer would maintain, at its expense, a policy of liability insurance on plaintiff's behalf.

Defendant provided a policy through Medical Liability Mutual Insurance Company, then a mutual insurance company. Plaintiff was the policyholder and, so as to enable it to make the premium payments, named defendant as her policy administrator. There is no dispute that defendant made all premium payments.

In 2016 MLMIC applied to the New York State Department of Financial Services to file a Plan to convert from a mutual insurance company, a company owned by the policy holders, to a stock insurance company. Such a conversion must comply with the mandates of Insurance Law § 7307, which provides at the time of demutualization, the eligible policyholders of said company shall receive either a cash consideration and/or stock in exchange for the extinguishment of their equitable share of the company.

In this case, the mandates of § 7307 were assimilated into MLMIC's "Conversion Plan". Under New York Insurance Law, such a conversion is allowable only if the policy holders receive consideration for their equitable share. Here, MLMIC chose cash as the consideration. The total amount paid to MLMIC policy holders for the extinguishment of their membership interests would total $2.502 billion. In the case at bar, the disputed cash consideration is $49,273.59.

Plaintiff contends that the policy was provided to plaintiff as compensation for her services and that the cash consideration in question is a result of the extinguishment of a membership interest in the company. As the owner of the policy, and thus the membership interest, the cash consideration should come to her. Defendant argues that since it paid all the premiums on the policy, equity demands it receive the money and that plaintiff will be unjustly enriched if the funds go to her.

Plaintiff has moved for summary judgment, seeking an order from the court declaring that she is entitled to the demutualization distribution funds. In support of her

INDEX NO. EFCA2018003334
RECEIVED NYSCEF: 09/12/2019

motion, plaintiff has submitted an attorney's affidavit with attachments, plaintiff's affidavit with attachments, including, inter alia, her employment agreement with defendant, and a memorandum of law in support of her motion. Defendant opposes the motion arguing that it is premature, and that plaintiff has failed to make a prima facie showing of entitlement to summary judgment. In support of its opposition, defendant has filed an attorney's affidavit with attachments including the affidavit of Marybeth Vanderpoole, Practice Manager of Broome Obstetrics and Gynecology, P.C., and a memorandum of law.

LEGAL ANALYSIS

The rights to the proceeds of a demutualization of a mutual insurance company are defined by the company's "Conversion Plan", *Bank of New York v Janowick*, 470 F3d 264, 274 (2012). The Plan in this case was approved by the New York State Department of Financial Services on September 6, 2018 and approved by the policyholders on September 14, 2018. It provided that the policyholders "or their designees" would receive cash for the extinguishment of their membership interests. The plan defines Policyholder as "the Person(s) identified on the declarations page of such Policy as the insured", and Eligible Policyholders as those *policyholders* that had a policy in effect between July 15, 2013 through July 14, 2016. It defines Policy Administrator as the person designated on the declarations page to administer the policy on behalf of the policyholder, and Designees as those 'Policy Administrators...*to the extent designated by the Eligible Policyholders* to receive the portion of the Cash Consideration allocated to such Eligible Policyholder'(emphasis added).

It is undisputed that plaintiff was the insured named on the declarations page, and as such the policyholder; and defendant was the policy administrator. To date, despite repeated requests from defendant, plaintiff has not named defendant her designee.

The language of the Plan is clear and unambiguous, and as such must be accorded the plain meaning of its terms, *Goldman v Emerald Green Prop. Owner's Assn., Inc.*, 116 AD3d 1279 , 1280 (2014). According to those terms, plaintiff is entitled to the money.

Defendant's argument - that it paid the premiums and as such is entitled to the funds, is unpersuasive. Policyholders in a mutual insurance company acquire two separate types of rights - contractual rights and membership rights. The contractual rights are paid for by the premiums, and pay for the cost of the insurance itself. "The premiums paid covered the rights under the insurance contract, not any membership rights...premium payments go toward the actual cost of the insurance benefits provided", *Dorrance v U. S.*, 809 F3d 479, 485[1].

Here, the defendant paid the premiums as part of its obligation under the Employment Agreement with plaintiff. She provided services and in return defendant was confident that she was covered (and hence it was covered) in terms of malpractice insurance. This arrangement benefitted both parties.

The membership rights are acquired at "no cost", and are in fact, a benefit of being the policyholder, *Dorrance v United States*, at 485. They do not arise as a result of paying the premiums, but are intrinsic to the owner of the policy, the policyholder.

The bottom line is that the cash consideration that is generated as a result of demutualization is a "windfall", or "a pot of money no one expected or even envisioned", *Dorrance* at 486. Here, it was a result of a restructuring of a mutual insurance company

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[1] Defendant argues that Dorrance is not relevant as it is a tax case. While the facts may differ from the case at bar, the legal import of the case lies in its analysis of the demutualization process.

into a stock company. However, negative connotations aside, the fact that this is a "windfall" does not, per se, render it illicit or unjust. The court is certainly inclined to agree with the plain language of the Plan and the Insurance Law that in this case, plaintiff, the policyholder should be entitled to receive it.

However, all of the foregoing is academic in light of *Matter of Schaffer, Schonholz & Drossman, LLP v Title,* 171 AD3d 465, an April, 2019 decision out of the 1st Department. The case involved the very issue before this court (in fact involving the same demutualization of MLMIC), who is entitled to the cash consideration. The Appellate Division found that the medical practice - the entity that had paid the premiums - was entitled to receive the funds and that any other result would unjustly enrich the individual practitioner. Despite a thorough search, the court has not discovered any third department cases that have ruled on this issue. "Where the issue has not been addressed within the Department, Supreme Court is bound by the doctrine of stare decisis to apply precedent established in another Department, either until a contrary rule is established by the Appellate Division in its own Department or by the Court of Appeals", *D'Alessandro v. Carro,* 123 AD3d 1, 6 (2014); *Tzolis v. Wolff*, 39 AD3d 138, 142 (2007); *Mountain View Coach Lines v Storms,* 102 AD2d 663, 664 (1984).

State trial courts must follow a higher court's existing precedent "even though they may disagree", *People v Rivera,* 5 NY3d 61 (2005).

Thus plaintiff's motion for summary judgment is denied. This constitutes the Decision and Order of the Court

Dated: September 10, 2019

HON. MOLLY REYNOLDS FITZGERALD
SUPREME COURT JUSTICE

cc: Justin A. Heller, Esq.
Jared R. Mack, Esq.
Judith E. Osburn, Broome County Chief Court Clerk

ADDENDUM "B"

COPY OF APPELLANT'S STATEMENT PURSUANT TO C.P.L.R. 5531

Supreme Court of the State of New York
Appellate Division – Second Department

MAPLE MEDICAL LLP,

Plaintiff-Respondent,

– against –

JOSEPH SCOTT, M.D.,

Defendant-Appellant,

– and –

MEDICAL LIABILITY MUTUAL INSURANCE COMPANY,

Defendant.

STATEMENT PURSUANT TO CPLR 5531

1. The Index Number of the case in the Court below is Westchester County Index No. 51103-2019.

2. The full names of all the original parties in this action are set forth in the caption above. There has been no change in the parties.

3. This action was commenced in the New York State Supreme Court, Westchester County.

4. This action was commenced by filing a Summons and Complaint in the Westchester County Clerk's Office on January 17, 2019. Defendant-Appellant Scott was served on January 30, 2019.

5. This action sought to resolve a dispute between the parties as to who was entitled to a share of cash consideration from the extinguishment of Defendant-Appellant's membership interest in the Medical Liability Mutual Insurance Company when it converted to a stock insurance company.

6. The appeal is from the Decision and Order of the Hon. Lawrence H. Ecker, Justice of the Supreme Court, dated July 5, 2019 and entered in the Westchester County Clerk's Office on July 9, 2019, denying Defendant-Appellant Scott's motion for summary judgment against Plaintiff-Respondent.

7. The method of appeal being used is a reproduced full record.

A & A Assocs. v. Olympic Plumbing & Heating Corp.

Supreme Court of New York, Appellate Division, Second Department

May 15, 2003, Argued ; June 9, 2003, Decided

2002-05380

Reporter

306 A.D.2d 296 *; 760 N.Y.S.2d 652 **; 2003 N.Y. App. Div. LEXIS 6460 ***

A & A Associates, Inc., Appellant, v. Olympic Plumbing & Heating Corp. et al., Respondents, et al., Defendant. (Index No. 20275/98)

Subsequent History: **[***1]**

Appeal denied by *A & A Assocs. v. Olympic Plumbing & Heating Corp., 1 N.Y.3d 503, 2003 N.Y. LEXIS 4097 (N.Y., Dec. 18, 2003)*

Counsel: Agovino & Asselta, LLP, Mineola, N.Y. (Steven R. Miller, Joseph P. Asselta, and Eric Su of counsel), for appellant.

Sonnenschein Nath & Rosenthal, New York, N.Y. (Allen G. Reiter and Stephen L. Brodsky of counsel), for respondents Olympic Plumbing & Heating Corp. and Albert Rocco.

Dewey, Pegno & Kramarsky, LLP, New York, N.Y. (David S. Pegno of counsel), for respondents A. J. Pegno Construction Corp. and Timothy S. Rexon.

Judges: FRED T. SANTUCCI, J.P., GLORIA GOLDSTEIN, HOWARD MILLER, ROBERT W. SCHMIDT, JJ. SANTUCCI, J.P., GOLDSTEIN, H. MILLER and SCHMIDT, JJ., concur.

Opinion

[*296] **[**652]** In an action, inter alia, to recover damages for unfair competition, the plaintiff appeals from an order of the Supreme Court, Queens County (Weiss, J.), dated May 3, 2002, which granted the motion of the defendants Olympic Plumbing & Heating Corp. and Albert Rocco, and the separate motion of **[*297]** the defendants A. J. Pegno Construction Corp. and Timothy S. Rexon, for summary judgment dismissing the amended complaint insofar as asserted against them.

Ordered that the order is affirmed, **[***2]** with one bill of costs.

The respondents demonstrated their prima facie entitlement to judgment as a matter of law. In opposition, the plaintiff failed to raise a triable issue of fact relating to its cause of action alleging unfair competition (*see* *Allied Maintenance Corp. v Allied Mech. Trades, 42 N.Y.2d 538, 399 N.Y.S.2d 628, 369 N.E.2d 1162 [1977]*; **[**653]** *Camelot Assoc. Corp. v Camelot Design & Dev., 298 A.D.2d 799, 750 N.Y.S.2d 155 [2002]*). In addition, no issue of fact was raised as to whether the respondents derived a benefit that belonged to the plaintiff, which is necessary to sustain a cause of action based upon unjust enrichment (*see* *Smith v Chase Manhattan Bank, USA, 293 A.D.2d 598, 741 N.Y.S.2d 100 [2002]*; *Fandy Corp. v Chang, 272 A.D.2d 369, 707 N.Y.S.2d 361 [2000]*; *Bugarsky v Marcantonio, 254 A.D.2d 384, 678 N.Y.S.2d 737 [1998]*). Moreover, the plaintiff failed to establish the existence of a triable issue of fact with respect to whether the respondents made misrepresentations which deprived the plaintiff of payment for a service which it performed, which was necessary to sustain the plaintiff's cause of action alleging fraud (*see Cohen v Houseconnect Realty Corp., 289 A.D.2d 277, 734 N.Y.S.2d 205 [2001]*; **[***3]** *Buxton Mfg. Co. v Valiant Moving & Stor., 239 A.D.2d 452, 657 N.Y.S.2d 450 [1997]*; *Garelick v Carmel, 141 A.D.2d 501, 529 N.Y.S.2d 126 [1988]*). Accordingly, the Supreme Court properly granted the respondents' motions to dismiss the amended complaint.

The plaintiff's remaining contention is without merit.

Santucci, J.P., Goldstein, H. Miller and Schmidt, JJ., concur.

Bank of N.Y. v. Janowick

United States Court of Appeals for the Sixth Circuit

September 18, 2006, Argued ; November 22, 2006, Decided ; November 22, 2006, Filed

File Name: 06a0433p.06

Nos. 05-6390/6456

Reporter

470 F.3d 264 *; 2006 U.S. App. LEXIS 28940 **; 2006 FED App. 0433P (6th Cir.) ***; 39 Employee Benefits Cas. (BNA) 1631

BANK OF NEW YORK, as former Trustee for National-Southwire Company Pension Plan, Plaintiff, SOUTHWIRE COMPANY, Defendant-Appellee, v. JOHN STEPHEN JANOWICK, GARY ERWIN, and MERL KANNAPEL, on behalf of themselves and as the representatives of a class of current and deferred annuitants of Prudential Group Annuity Contracts GA 5543 and GA 5542, Defendants-Appellants (05-6390), CENTURY ALUMINUM COMPANY, Defendant-Appellant (05-6456).

Subsequent History: US Supreme Court certiorari denied by *Southwire Co. v. Janowick, 128 S. Ct. 195, 169 L. Ed. 2d 36, 2007 U.S. LEXIS 9276 (U.S., Oct. 1, 2007)*

Prior History: [1]** Appeal from the United States District Court for the Western District of Kentucky at Owensboro. No. 03-00020--Joseph H. McKinley, Jr., District Judge.

Bank of N.Y. v. Janowick, 2005 U.S. Dist. LEXIS 16728 (W.D. Ky., Aug. 10, 2005)

Counsel: ARGUED: Michael C. Merrick, DINSMORE & SHOHL, Louisville, Kentucky, for Appellants.

Mark S. Riddle, GREENEBAUM, DOLL & McDONALD, Louisville, Kentucky, for Appellee.

ON BRIEF: Michael C. Merrick, Frank P. Doheny, Jr., DINSMORE & SHOHL, Louisville, Kentucky, Leon Dayan, Lisa M. Powell, BREDHOFF & KAISER, Washington, D.C., for Appellants.

Mark S. Riddle, Melissa Norman Bork, Benjamin J. Evans, GREENEBAUM, DOLL & McDONALD, Louisville, Kentucky, for Appellee.

Judges: Before: BATCHELDER and MOORE, Circuit Judges; COHN, District Judge. * MOORE, J., delivered the opinion of the court, in which COHN, D. J., joined. BATCHELDER, J. (p. 10), delivered a separate dissenting opinion.

Opinion by: KAREN NELSON MOORE

Opinion

[*2] [*266]** KAREN NELSON MOORE, Circuit Judge. When an insurance company's reorganization yields a pot of money that no one expected or even envisioned, who receives the proceeds? In short, that is the issue this case **[**2]** requires the court to resolve.

Bank of New York ("BNY") filed this interpleader action to resolve conflicting claims to stock it received from Prudential Insurance Company of America's demutualization, i.e., its reorganization from a mutual insurance company to a stock company. BNY received the stock as successor-in-interest to the former trustee of the National-Southwire Aluminum Company ("NSA") Pension Plan ("NSA Plan" or "Plan"). The Plan terminated in 1986, and the trustee used the Plan's assets to purchase two group annuity contracts, which satisfied the Plan's ERISA obligations to the employees.

The claimants to the stock are a class of employees ("Employees") of the now-defunct NSA (represented by Defendants-Appellants Janowick, Erwin, and Kannapel), Defendant-Appellee Southwire Company ("Southwire") (the parent company of the former NSA), and Defendant-Appellant Century Aluminum Company ("Century") (the purchaser of the former NSA's assets). The district court addressed the claims in two phases, first concluding via summary judgment that Southwire's claims were superior to those of the Employees, and

* The Honorable Avern Cohn, United States District Judge for the Eastern District of Michigan, sitting by designation.

next concluding that Southwire's claims trumped Century's. The Employees **[**3]** and Century both appeal.

Regarding the Employees' appeal, we **REVERSE** the district court's grant of summary judgment to Southwire, as we conclude that both Kentucky law and the nature of demutualization compel the conclusion that the Employees are entitled to the proceeds, and **REMAND** for further proceedings consistent with this opinion. As to Century's appeal, we **VACATE** the district court's judgment and **DISMISS** Century's appeal as moot, as we conclude that Century could not have purchased from Southwire that which Southwire never owned.

I. BACKGROUND

A. The Pension Plan

In 1970, NSA created the Plan as a defined-benefit pension plan for the Employees, **[*267]** who worked at an aluminum smelting plant NSA operated in Hawesville, Kentucky. Under a defined-benefit plan, "the benefits to be received by employees are fixed and the employer's contribution is adjusted to whatever level is necessary to provide those benefits." *Ala. Power Co. v. Davis, 431 U.S. 581, 593 n.18, 97 S. Ct. 2002, 52 L. Ed. 2d 595 (1977)*. Thus, NSA paid contributions to the Plan through a funding agent, and the Plan held in trust and managed these funds on behalf of the Employees.

[4]** The Plan became governed by ERISA upon ERISA's enactment in 1974. In December 1986, NSA terminated the Plan. At that time, Irving Trust Company ("Irving") was the designated Plan trustee. Consistent with ERISA's requirements, *see* *29 U.S.C. § 1341(b)*, Irving purchased two group annuity contracts (nos. GA-5542 and GA-5543) from the Prudential Insurance Company of America ("Prudential") for the benefit of the Employees. These annuity contracts constitute an **[***3]** "irrevocable commitment[on behalf of Prudential] to provide all benefit liabilities under the plan." *29 U.S.C. § 1341(b)(3)(A)(i)*. *See also* *29 C.F.R. §§ 4001.2*, *4041.28(c)(1)*, *4041.28(d)(1)*.

After Irving bought the annuity contracts (which cost approximately $ 7 million) from Prudential, some funds remained in the trust. Consistent with ERISA, the governing documents of the NSA Plan provided that such surplus funds could revert to NSA once the trustee fully satisfied the plan's obligations to its beneficiaries. *See* *29 U.S.C. § 1344(d)(1)*; Joint Appendix ("J.A.") at 157-58 (NSA **[**5]** Plan § 9.2). NSA received approximately $ 11.5 million under this provision. After all of the Plan's assets were distributed, Irving's status as trustee terminated sometime in 1987. At that point, the Plan was defunct.

B. Subsequent Transactions

Starting in the early 1990s, NSA underwent a series of corporate transactions with other companies under the umbrella of NSA's parent corporation, Southwire. In August 2000, Century agreed to purchase from Southwire the Hawesville plant and assets associated with its business.

C. Prudential's Demutualization

At the time Irving purchased the annuity contracts, Prudential was organized as a mutual insurance company under the laws of New Jersey. "A mutual insurance company has no shareholders and is instead owned by its policyholders." James A. Smallenberger, *Restructuring Mutual Life Insurance Companies: A Practical Guide Through the Process*, *49 DRAKE L. REV. 513, 516 (2001)*. Those who purchase policies from mutual insurance companies receive both membership interests (e.g., the right to elect directors and the right to receive a proportionate share of the company if it liquidates) and contract rights **[**6]** (i.e., the obligations of the insurance company under the policy). *Id.* at n.4.

Prior to 1998, New Jersey did not allow insurance companies to organize as stock companies. J.A. at 476 (NJ Dep't of Banking & Ins. Order No. A01-153 § I.). New Jersey law changed in 1998, and in December 2000, Prudential's board of directors adopted a plan to demutualize, that is, to reorganize from a mutual insurance company to a stock company. The demutualization plan was approved by policyholders in July 2001, and within three months, the New Jersey Insurance Commissioner approved the plan. *Id.* Prudential's demutualization plan required the new company, Prudential Financial, Inc. ("PFI"), to issue stock to eligible policyholders **[*268]** as consideration for their membership interests in the old company.

In early 2002, PFI issued 35,119 shares of stock to BNY as the successor-in-interest to Irving. The stock was intended to compensate Irving for the loss of membership interests that it held as the contract-holder of the group annuities purchased to terminate the NSA plan. However, BNY denied both that it was the contract-holder and that it was entitled to the stock. Soon, BNY began receiving conflicting **[**7]** demands for the demutualization proceeds when Southwire, the Employees, and Century all asserted entitlement to the stock. To settle these claims, BNY filed its interpleader complaint on February 3, 2003, naming Southwire, the Employees, and Century all as defendants. The district court had jurisdiction under the minimal diversity requirement of the federal interpleader statute because two of the claimants are diverse, as the Employees are Kentucky residents and Southwire is organized as a Delaware corporation. *28 U.S.C. § 1335(a)*; *State Farm Fire & Cas. Co. v. Tashire, 386 U.S. 523, 530-31, 87 S. Ct. 1199, 18 L. Ed. 2d 270 (1967)*.

[***4] D. Procedural History

The district court certified a defendant class consisting of the Employees and dismissed BNY from the case, leaving the three claimants as parties to the litigation. It also granted BNY permission to sell the stock and ordered it to deposit the proceeds with the court. Accordingly, BNY deposited approximately $ 1.3 million with the district court.

The district court proceeded in two phases to settle the claimants' dispute. First, it pitted Southwire against the Employees to determine which of those **[**8]** two parties had the better claim to the demutualization proceeds. On September 29, 2004, it granted summary judgment to Southwire and denied summary judgment to the Employees.

Next, the district court decided whether Century's claim to the proceeds was superior to Southwire's. On August 10, 2005, it granted summary judgment to Southwire and denied summary judgment to Century.

Both the Employees and Century appealed, and their appeals were consolidated for briefing and submission. We have jurisdiction over the Employees' and Century's appeals from the district court's final judgment under *28 U.S.C. § 1291*.

II. STANDARD OF REVIEW

We review de novo a district court's order granting summary judgment, *DiCarlo v. Potter, 358 F.3d 408, 414 (6th Cir. 2004)*, and will affirm a grant of summary judgment "[i]f the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." *Fed. R. Civ. P. 56(c)*. In reviewing the district **[**9]** court's decision to grant summary judgment, we must view all evidence in the light most favorable to the nonmoving party. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 587, 106 S. Ct. 1348, 89 L. Ed. 2d 538 (1986)*.

III. ANALYSIS

The Employees argue that Southwire never had a right to the demutualization proceeds, and Century argues that it purchased the right to the proceeds when it bought the Hawesville plant from Southwire in 2000. Because we conclude that the Employees are correct, Southwire never could have transferred the interest in the demutualization proceeds to Century.

[*269] Ultimately, we conclude that the Employees are entitled to the demutualization proceeds for three separate reasons. First, we conclude that the terms of the annuity contract compel the conclusion that the Employees are now the contract-holders, and thus entitled to the demutualization proceeds. Second, we conclude that under relevant contract principles, we would supply a term to the annuity contracts under *Restatement (Second) of Contracts § 204* entitling the Employees to unforeseen demutualization proceeds. Finally, we consider the nature **[**10]** of demutualization and conclude that Southwire could not have had any claim to the demutualization proceeds because it never held any ownership interest in Prudential.

A. Terms of the Annuity Contract

Prudential's demutualization plan entitles "Eligible Policyholders"--i.e., the "owners" of eligible policies and annuity contracts, J.A. at 297 (Reorganization Plan § 1)--to demutualization compensation. J.A. at 318 (Reorganization Plan § 7.1(b)). For group annuity contracts, it defines the designated contract-holders as "owners." J.A. at 312 (Reorganization Plan § 5.3). Here, the annuity contracts designate Irving as the contract-holder "as trustee for [the] National-Southwire Aluminum Company Pension Plan." J.A. at 190, 235. Irving's successor (BNY) claims that Irving's **[***5]** status as contract-holder ceased, presumably when its status as trustee of the NSA Plan terminated in 1988. The demutualization plan does not indicate how shares should be distributed when a policy lacks an owner. [1]

[11]** Because the demutualization plan does not resolve the dispute, we turn elsewhere. The Department of Labor ("DOL") has concluded that, in disputes over demutualization proceeds born from an annuity contract purchased to terminate an ERISA plan, [2] the terms of the relevant annuity contracts and state law govern. Dep't of Labor, Office of Pension and Welfare Benefit Programs Op. No. 2003-05A, 2003 WL 1901900 (Apr. 10, 2003). Although the DOL's advisory opinion is not binding on us, it is worthy of "some deference." Christensen v. Harris County, 529 U.S. 576, 587, 120 S. Ct. 1655, 146 L. Ed. 2d 621 (2000) (quoting Reno v. Koray, 515 U.S. 50, 61, 115 S. Ct. 2021, 132 L. Ed. 2d 46 (1995)). Interpretive guidance from administrative agencies that is not the product of formal, notice-and-comment rulemaking is entitled to respect "to the extent that th[e] interpretations have the 'power to persuade.'" *Id*. (quoting Skidmore v. Swift & Co., 323 U.S. 134, 140, 65 S. Ct. 161, 89 L. Ed. 124 (1944)). The Fifth Circuit applied this standard and deferred to similar guidance from the DOL in Bussian v. RJR Nabisco, Inc., 223 F.3d 286, 296 (5th Cir. 2000). We conclude **[**12]** that the DOL guidance is persuasive because a membership interest in a mutual insurance company is a precondition to any right to demutualization proceeds, and the annuity contract creates such interests. Regardless of whether the annuity contract contemplates **[*270]** the right to demutualization proceeds, previous documents (e.g., the NSA Plan documents) *could not have contemplated* such a right, as they neither created nor encompassed membership interests in Prudential.

We conclude that the terms of the annuity contracts entitle **[**13]** the Employees to the demutualization proceeds. The parties do not press this argument in their briefs, but they have provided copies of the annuity contracts in the Joint Appendix. We address the parties' primary argument, whether we should apply *Restatement (Second) of Contracts § 204* to supply a missing term to the annuity contracts, *infra* in Part III.B.

As noted above, Prudential's demutualization plan provides that contract-holders, as "owners" of the contracts, are to receive consideration in the form of stock. The annuity contracts dub Irving the contract-holder, but this provision is of no help because, as noted above, Irving's successor claims that it is no longer the contract-holder. The contracts further provide:

> The Contract-Holder at any time may, with the consent of the Prudential, appoint a successor Contract-Holder. . . . [H]owever, . . . if the Contract-Holder notifies the Prudential that it will cease to exist or cease to perform the duties of the Contract-Holder hereunder and no successor Contract-Holder is appointed, this contract shall nevertheless remain in full force and effect . . . .

J.A. at **[**14]** 195 (Annuity Contract No. 5543 at § 1.10), 242 (Annuity Contract No. 5542 at § 3.7). The record contains no indication that Irving appointed a successor contract-holder or notified Prudential prior to 2002 that it would no longer perform the duties of contract-holder. Notably, the contracts are silent regarding who becomes the successor contract-holder in this situation.

[*6]** "The primary object in construing a contract . . . is to effectuate the intentions of the parties." Cantrell Supply, Inc. v. Liberty Mut. Ins. Co., 94 S.W.3d 381, 384 (Ky. Ct. App. 2002). Kentucky courts [3] have long held

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[1] Although no party so argues, the demutualization plan hints that Prudential should have resolved this dispute by invoking its "Resolution Procedures" once BNY disclaimed entitlement to the demutualization consideration. J.A. at 314 (Reorganization Plan § 5.9). The record contains no indication that Prudential did so.

[2] The "final distribution" of a terminating ERISA plan's assets occurs when the administrator "purchase[s] irrevocable commitments from an insurer to provide all benefit liabilities under the plan, or . . . otherwise fully provide[s] all benefit liabilities under the plan." 29 U.S.C. § 1341(b)(3); 29 C.F.R. § 4041.28(c). Annuities are an example of such "irrevocable commitments." *See* 29 C.F.R. § 4001.2.

[3] The annuity contracts contain choice-of-law provisions selecting New York law. J.A. at 196 (Annuity Contract No. GA-5543 § 1.13), 243 (Annuity Contract No. GA-5542 § 3.11). Notwithstanding these provisions, we believe that, for the following reasons, Kentucky law governs interpretation of the annuity contracts.

As explained above, federal jurisdiction arises under the federal interpleader statute's minimal diversity requirement. *See supra* Part I.C. Accordingly, we apply the choice-of-law provisions of the forum state -- here, Kentucky. Republican Nat'l Comm. v. Taylor, 353 U.S. App. D.C. 236, 299 F.3d 887, 890 (D.C. Cir. 2002). *See also* Andersons, Inc. v. Consol, Inc., 348 F.3d 496, 501 (6th Cir. 2003) (forum state's choice-of-law provisions apply when federal district court has diversity jurisdiction under 28 U.S.C. § 1332).

that in so **[*271]** doing, it is proper to consider "the circumstances surrounding the parties, and the object" of the contract, in addition to the contract's language. *Owens v. Ga. Life Ins. Co., 165 Ky. 507, 177 S.W. 294, 298 (Ky. 1915)* (quoting *Mitchell v. S. Ry. Co., 124 Ky. 146, 74 S.W. 216, 217, 24 Ky. L. Rptr. 2388 (Ky. 1903))*. "Whe[n] a contract is . . . silent on a vital matter," it is especially appropriate for courts to consider each of these factors, as well as "the subject matter of the contract." *Cantrell Supply, 94 S.W.3d at 385*.

[15]** Here, these factors strongly indicate that the parties to the annuity contracts intended for the Employees to step into Irving's shoes as the contract-holders after Irving withdrew. The purpose of the annuity contracts was to provide pension benefits to which the Employees were entitled under the defunct NSA Plan. Accordingly, the Employees are third-party creditor beneficiaries of the contracts. *See Presnell Constr. Managers, Inc. v. EH Const., LLC, 134 S.W.3d 575, 579 n.12 (Ky. 2004)* (quoting *Sexton v. Taylor County, 692 S.W.2d 808, 810 (Ky. Ct. App. 1985))*. Other than Prudential, which is not a party to this case, only the Employees have a direct interest in the annuity contracts. By contrast, Southwire is neither a party to, nor a beneficiary of, the contracts. For these reasons, we conclude that the parties' intent in entering the contract was that the Employees would become the contract-holders if Irving were to step down. [4]

[16] B. *Restatement (Second) of Contracts***

Aside from our analysis of the contract's existing terms, we conclude that the Employees are entitled to the demutualization proceeds under *Restatement (Second) of Contracts § 204*. The annuity contracts say nothing regarding demutualization, which is not surprising as demutualization was not legal in New Jersey (where Prudential was located) when Irving purchased the annuity contracts from Prudential on the Employees' behalf. Because the annuity contracts do not contain a term regarding entitlement to demutualization proceeds, the Employees urge the court to apply *Restatement of Contracts (Second) § 204* to supply the annuity contracts with a missing term. *Section 204* states: "When the parties to a . . . contract have not agreed with respect to a term which **[***7]** is essential to a determination of their rights and duties, a term which is reasonable in the circumstances is supplied by the court."

Southwire objects, claiming that Kentucky courts have not endorsed *§ 204*. Although no reported case in Kentucky has applied this provision of the *Restatement* **[**17]** , the Kentucky Supreme Court has applied various other sections of the *Restatement*, which demonstrates that the *Restatement* is generally valid authority in Kentucky. *See, e.g.*, *Hargis v. Baize, 168 S.W.3d 36, 47 (Ky. 2005)* (applying *§ 195(2)*); *Nucor Corp. v. Gen. Elec. Co., 812 S.W.2d 136, 144 (Ky. 1991)* (*§ 354*); *id. at 145 n.2* (*§ 350*); *Stevens v. Stevens, 798 S.W.2d 136, 139 (Ky. 1990)* (*§ 305*). Further, Kentucky courts have recognized the principle that "if a contract is silent on a certain point, the law will imply an obligation to carry out the purpose for which the contract was made" -- exactly the substance of *§ 204*. *Old Republic Ins. Co. v. Ashley, 722 S.W.2d 55, 58 (Ky. Ct. App. 1986)* (citing *Warfield Nat. Gas Co. v. Allen, 248 Ky. 646, 59 S.W.2d 534 (Ky. 1933))*. *Cf. Richardson v. Eastland, Inc., 660 S.W.2d 7, 8 (Ky. 1983)* ("Where the contract is silent we must interpret the intent of the **[*272]** parties."). [5] Sitting in diversity,

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We have previously determined that under Kentucky law, *§ 187 of the Restatement (Second) of Conflict of Laws* governs contractual choice-of-law provisions. *Wallace Hardware Co. v. Abrams, 223 F.3d 382, 397 (6th Cir. 2000)*. *Section 187* applies the law of the chosen state unless "the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice." *RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2)(a)*, *quoted in Wallace Hardware, 223 F.3d at 393 n.9*.

The present dispute does not involve any parties domiciled in New York, nor any business conducted in New York. Even the purchase of the annuity contracts, in which the trustee to the pension plan of a Delaware corporation purchased annuity contracts from a New Jersey-based insurer for the corporation's Kentucky employees, involves no substantial relationship to New York. The only basis for the parties' choice is that Irving, which is no longer the contract-holder, was based in New York. For these reasons, under *§ 187(2)(a)*, Kentucky law applies. Further, both parties' briefs apply Kentucky law, which indicates that the parties agree that Kentucky law should govern our interpretation of the annuity contracts.

[4] If we were to analyze this issue as supplying a missing term rather than interpreting existing terms, we would reach the same conclusion, employing the same analysis under ***Restatement (Second) of Contracts § 204*** as employed in Part III.B.

[5] Southwire argues that Kentucky courts are reluctant to add terms to contracts. The cases it cites, however, are readily distinguishable, as they concern courts refusing to *alter the existing terms* of the contracts in question. *See, e.g.*, *O.P. Link*

our duty is to apply the law of the forum state as announced by its highest court. West Bay Exploration Co. v. AIG Specialty Agencies of Tex., Inc., 915 F.2d 1030, 1034 (6th Cir. 1990). **[**18]** Where the relevant state supreme court has not spoken on an issue, we apply the rule that we believe the state supreme court would apply if it were to decide the case. Himmel v. Ford Motor Co., 342 F.3d 593, 598 (6th Cir. 2003). Under these circumstances, we believe the Kentucky Supreme Court would employ *Restatement § 204*. Accordingly, so do we.

[19]** *Section 204's comment d* instructs courts to apply "community standards of fairness" to determine a term that is reasonable in the circumstances. Here, it is clear that none of the parties expected to receive the demutualization proceeds, which will constitute a windfall to whoever receives them. It is also clear that NSA's decision to terminate the Plan in 1986 relieved it of any risk associated with the Plan--namely, the responsibility to provide whatever level of funding is necessary to yield the fixed level of benefits promised. *See* Hughes Aircraft Co. v. Jacobson, 525 U.S. 432, 439, 119 S. Ct. 755, 142 L. Ed. 2d 881 (1999) (noting that under an ongoing defined benefit plan, "the employer typically bears the entire investment risk and--short of the consequences of plan termination--must cover any underfunding as the result of a shortfall that may occur from the plan's investments"). [6]

[20]** At the same time, the termination of the NSA Plan shifted risk *onto* the Employees. On paper, at least, the Employees are entitled to exactly the same level of benefits under the annuity contracts as they were under the NSA Plan, but crucially, their benefits are no longer guaranteed. Under ERISA, ongoing pension plans are guaranteed by the Pension Benefit Guarantee Corporation(PBGC). *See* 29 C.F.R. §§ 4022.1 et seq. Not so for the annuity contracts. If Prudential were to become insolvent and default on its obligations under the annuity contracts, the Employees would be unable to recover the full value of the benefits. Accordingly, the NSA Plan's termination--the very event that necessitated purchase of the annuity contracts--stuck the Employees with a new (and unbargained-for) risk. Applying community standards of fairness, the inserted term should not entitle a party absolved of risk, such as Southwire, to unforeseen demutualization proceeds in **[***8]** preference to the party burdened with additional risk. Accordingly, we supply a term to the annuity contracts entitling the Employees to the demutualization proceeds. [7]

[**21] [*273] C. The Nature of Demutualization

Finally, the nature of demutualization compels the conclusion that Southwire never could have had any right to the demutualization proceeds. As noted above, by definition demutualization "involves a conversion of the mutual policyholders' ownership interest in the old [mutual] company into ownership interest in the form of stock in the new [stock] company." UNUM Corp. v. United States, 130 F.3d 501, 502 (1st Cir. 1997), *cert. denied*, *525 U.S. 810, 119 S. Ct. 42, 142 L. Ed. 2d 32 (1998)*. Here, no ownership interests materialized until April 1988, when Irving purchased the annuity contracts for the Employees' benefit. [8] NSA did not purchase any annuities from Prudential, and was not the contract-holder. The same is true of Southwire, NSA's parent company. Accordingly Southwire did not hold, and could not have held, any membership interest in Prudential, and thus could not have held any claim to the demutualization proceeds.

Handle Co. v. Wright, 429 S.W.2d 842, 847 (Ky. 1968) (declining "to change the obligations of a contract"); State Farm Mut. Auto. Ins. Co. v. Hobbs, 268 S.W.2d 420, 422 (Ky. 1954) (stating that the court cannot "make a contract for the parties or revise the agreement while professing to construe it" and refusing to alter the contract's express termination date).

[6] Contrary to the dissent's conclusion, *Jacobson* in no way forecloses the Employees' claim to the demutualization proceeds. The dissent apparently fails to appreciate the key distinction between the two cases: Jacobson involved an *ongoing* retirement plan, whereas the Plan at issue here has been defunct since 1987. Consequently, as explained in Part III.C., the funds at issue could not have belonged to the Plan, and thus could never have been "plan surplus." For this reason, *Jacobson* is not controlling.

[7] Were we to attempt to discern the term to which the parties to the annuity contracts would have agreed (the less-favored mode of analysis under ***§ 204's comment d***), we would reach the same conclusion. As noted above, NSA's decision to terminate the Plan burdened the Employees with a risk for which they did not bargain. Accordingly, we conclude that under the "hypothetical model of bargaining" approach, Irving as the trustee would have demanded that any unanticipated proceeds from an unforeseen insurance company demutualization inure to the Employees to compensate them for this additional risk. Prudential would not have been in a position to favor either the Employees or Southwire, and would not have objected to this term.

[8] The signature pages reflect that the contracts were signed in April 1988, but were effective November 1, 1986.

[22]** Similarly, the ownership interests in Prudential never inured to the NSA Plan. The Plan's trustee (Irving) purchased group annuity contracts from Prudential to effectuate the "final distribution" of the Plan's assets under *29 U.S.C. § 1341(b)(3)*. This purchase represents the "closeout" of the Plan under *29 C.F.R. § 4041.28*. Only then, after the NSA Plan terminated, did any entity (Irving) receive an ownership interest in Prudential. Thus, like Southwire, the NSA Plan could not have held a right to demutualization proceeds. Southwire apparently recognizes as much, as it states that the right to demutualization proceeds does not constitute a "plan asset[]." Southwire Br. at 26. [9] In sum, because neither Southwire nor the NSA Plan ever held an ownership interest in Prudential--a precondition for entitlement to demutualization proceeds--neither could have been entitled to the money at issue.

[23] [*274]** Southwire disagrees, arguing that the right to demutualization proceeds reverted to NSA along with the $ 11.5 million in surplus trust funds. Flaws in this argument abound. First, Southwire overlooks that neither NSA nor the NSA Plan ever held any ownership interest in Prudential, as explained above.

[*9]** Second, Southwire's argument tortures the language of the Plan documents, which provide that only "funds remaining after the satisfaction of all liabilities" revert to Southwire. J.A. at 463 (NSA Pension Plan P 9.2). Southwire provides no reason for us to accept the counterintuitive proposition that an asserted right to proceeds from an unforeseen, and at the time unlawful, future demutualization of an insurance company was a *fund* remaining in the NSA Plan after Irving purchased the group annuity contracts.

Finally, Southwire's argument misdefines the right at issue. Southwire's position assumes the existence of some abstract right to demutualization proceeds, a right that apparently existed not only at a time predating the demutualization plan, but even when demutualization was not even legal and thus hardly foreseeable. This assumption is infinitely dubious, as the stack of documents **[**24]** regarding the Plan termination, purchase of annuity contracts, and reversion of remaining funds contains nary a word regarding such a right.

In reality, rights to proceeds from a demutualization arise only when a mutual insurance company demutualizes, and in such a situation, the mutual company's demutualization plan defines those rights. With a proper understanding of the right at issue, it is apparent that no right to the Prudential demutualization proceeds could have arisen prior to December 2000, when Prudential announced its plan to demutualize. By that time, the NSA Plan--the only vessel through which Southwire could receive any right to demutualization proceeds--had been defunct for over a dozen years.

In short, Southwire's position is incompatible with the definition of demutualization. This problem does not, however, apply to the Employees' position, which is perfectly consistent with the understanding that no rights to demutualization proceeds arise until the demutualization is announced, absent a clear earlier agreement.

D. Century's Appeal

Century argues that it received the right to the demutualization proceeds from Southwire when it purchased from Southwire **[**25]** the Hawesville plant and associated assets in 2000. We have already concluded that Southwire never had any right to the demutualization proceeds. Accordingly, Century could never have received from Southwire any right to or interest in the funds here at issue, as they were not

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[9] The Northern District of Illinois concluded in an unpublished opinion that the rights to an unforeseen demutualization may constitute "plan assets." *See* *Chi. Truck Drivers, Helpers & Warehouse Workers Union (Indep.) Health & Welfare Fund v. Local 710, Int'l Bhd. of Teamsters, No. 02 C 3115, 2005 U.S. Dist. LEXIS 42877, 2005 WL 525427 (N.D. Ill. March 4, 2005)* (unpublished opinion). Although the case involved a pension plan that had terminated decades ago, the court based its conclusion on two interpretive letters from the Department of Labor that both addressed situations involving ongoing ERISA-covered plans. *See* U.S. Dep't of Labor, Employee Benefits Security Admin. Advisory Op. 2001-02A (Feb. 15, 2001); U.S. Dep't of Labor, Pension & Welfare Benefits Office of Regulations & Interpretations Advisory Op. 92-02A (Jan. 17, 1992).

The court did not address the critical distinction between ongoing and defunct plans and did not provide any explanation of how demutualization proceeds can become an asset of a plan that is defunct and has no assets. Consequently, it appears doubtful that the case was correctly decided.

We reject the Northern District of Illinois's analysis, and instead follow the 2003 DOL opinion, which addresses how to treat demutualization proceeds purchased with the funds of a defunct pension plan. *See* Dep't of Labor, Office of Pension and Welfare Benefit Programs Op. No. 2003-05A, 2003 WL 1901900 (Apr. 10, 2003).

Southwire's to sell.

IV. CONCLUSION

For all of the foregoing reasons, we **REVERSE** the district court's order granting summary judgment to Southwire and denying the Employees' motion for summary judgment, and **REMAND** this case for further proceedings consistent with this opinion. Additionally, we **VACATE** the district court's order granting judgment to Southwire and denying Century's motion for summary judgment, and **DISMISS** Century's appeal as moot.

Dissent by: ALICE M. BATCHELDER

Dissent

[*10]** ALICE M. BATCHELDER, Circuit Judge, dissenting. I respectfully dissent, as I disagree with the reasoning and the outcome of the majority opinion. I believe this case is foreclosed by *Hughes Aircraft Co. v. Jacobson, **[*275]** 525 U.S. 432, 440-41, 119 S. Ct. 755, 142 L. Ed. 2d 881 (1999)* (holding that plan participants in a defined benefit pension plan have no claim to the plan's surplus assets). This case involves a **[**26]** defined benefit plan. There is no dispute that the annuities were properly calculated and funded to ensure that the employees will receive all of the benefits promised under the plan. The $ 1.3 million is surplus; it did not evolve over time into an additional defined benefit or become part of the annuity payments.

The majority provides multiple theories for gifting this money to the employees. None of these theories, however, changes the basic, irrefutable fact that these employees are only entitled to the benefits defined under the plan, and correspondingly, secured by the annuities. There is no evidence in the record and we have no basis to assume that these employees will not receive from Prudential all of the benefits to which they are entitled. I would affirm the decision of the district court and hold that this money represents surplus assets of a defined benefit plan, which was paid into the trust by the employer and must be returned to the employer as trust settlor.

Burns v Burns

Supreme Court of New York, Appellate Division, Fourth Department

July 25, 2018, Decided ; July 25, 2018, Entered

399 CA 17-01854

Reporter
163 A.D.3d 210 *; 81 N.Y.S.3d 846 **; 2018 N.Y. App. Div. LEXIS 5399 ***; 2018 NY Slip Op 05411 ****; 2018 WL 3569023

[**1]** Eleanor McQuilkin Burns, Appellant, v Andrew McIntosh Burns, Respondent.

Prior History: Appeal from an order of the Supreme Court, Monroe County (Richard A. Dollinger, A.J.), entered June 13, 2017. The order, among other things, denied plaintiff's motion to hold defendant in contempt.

Burns v Burns, 56 Misc 3d 864, 57 NYS3d 651, 2017 NY Misc LEXIS 2088 (May 26, 2017), affirmed.

Counsel: **[***1]** *Barney & Affronti, LLP*, Rochester (*Francis C. Affronti* of counsel), for appellant.

Burns & Schultz LLP, Pittsford (*Andrew M. Burns* of counsel), for respondent.

Judges: PRESENT: CENTRA, J.P., NEMOYER, CURRAN, AND TROUTMAN, JJ.

Opinion

[*211] **[**847]** NeMoyer, J.

According to the Domestic Relations Law and its common-law antecedents, the concept of spousal maintenance is limited to payments made to an unmarried ex-spouse. If divorcing spouses wish to vary this definition and provide for post-remarriage maintenance, they must do so clearly and unambiguously. In this case, nothing in the parties' agreement reflects an intent to depart from the statutory definition of maintenance with the clarity required by the governing case law. Consequently, as Supreme Court properly determined, defendant husband's maintenance obligation ended when plaintiff wife remarried.

[848]** Facts

The parties were married in June 1992. **[***2]** In September 2004, the husband vacated the marital residence; shortly thereafter, the wife sued for divorce. The parties subsequently executed a divorce settlement agreement pursuant to *Domestic Relations Law § 236 (B) (3)*. In the agreement, the parties specified that "[a]ll matters affecting . . . interpretation of this [a]greement and the rights of the parties [t]hereto shall be governed by the laws of the State of New York."

The agreement obligated the husband to pay "rehabilitative maintenance" to the wife pursuant to the following schedule:

> **[*212]** "(a) From December 1, 2007 - November 30, 2012: $5,500.00 Per Month = $66,000.00 Rehabilitative Maintenance Per Annum
>
> "(b) From December 1, 2012 - November 30, 2014: $2,916.00 Per Month = $34,992.00 Rehabilitative Maintenance Per Annum
>
> "(c) From December 1, 2014 - November 30, 2015: $2,500.00 Per Month = $30,000.00 Rehabilitative Maintenance Per Annum
>
> "(d) From December 1, 2015 - November 30, 2020: $2,200.00 Per Month = $26,400.00 Rehabilitative Maintenance Per Annum."

The foregoing constitutes the entirety of the agreement's maintenance provision. Critically, the agreement is silent regarding the effect, if any, of the wife's remarriage upon the husband's maintenance obligation. The agreement **[***3]** was subsequently incorporated, but not merged, into a judgment of divorce rendered by Supreme Court (Doyle, J.) in July 2008. The judgment includes a verbatim reproduction of the agreement's maintenance provision.

The wife remarried in December 2015. In April 2016, the husband emailed the wife to inform her that he would stop paying maintenance as a result of her remarriage. The husband's last maintenance payment was made that month.

The wife then moved to, inter alia, recover a monetary judgment for the amount outstanding and hold the husband in contempt for ending the maintenance payments. According to the wife, "a plain reading of . . . the agreement[ ] leads to only one conclusion: [the husband's] rehabilitative maintenance obligation survives [her] remarriage." That was so, the wife continued, because

> "[o]ther than November 30, 2020, no termination events are identified in the agreement. Since none can be implied and the Court cannot rewrite the parties' agreement, this Court must conclude [that the husband's] obligation to pay maintenance survives not only the wife's remarriage, but also her death and his death. The maintenance obligation ends on November 30, 2020 and no other time." **[***4]**

The husband opposed the wife's motion. Noting that the agreement contains no provision entitling the wife to continued maintenance payments upon her remarriage, the husband **[*213]** argued that the "fact that the parties did not expressly provide in the Agreement that maintenance payments would continue if [the wife] remarried establishes that the parties intended that [the husband's] obligation to pay [the wife] maintenance terminated upon her remarriage."

Supreme Court (Dollinger, A.J.) denied the wife's motion in its entirety. In a well-reasoned and thorough decision, the court held that, in light of the agreement's silence on the subject, the wife's remarriage ended the husband's obligation to pay maintenance. The wife now appeals.

Discussion

The friction point here is easily stated: the wife says that the husband's **[**849]** maintenance obligations are unaffected by her remarriage; the husband says that his maintenance obligations do not extend beyond the wife's remarriage. For the reasons that follow, we agree with the husband.

I

A divorce settlement agreement is a contract, subject to standard principles of contract interpretation (*see* Rainbow v Swisher, 72 NY2d 106, 109, 527 NE2d 258, 531 NYS2d 775 [1988]; Gurbacki v Gurbacki, 270 AD2d 807, 807-808, 708 NYS2d 761 [4th Dept 2000]). The agreement at issue does not explicitly define the term "maintenance," **[***5]** and it is silent regarding the effect of the wife's remarriage upon the husband's maintenance obligation. Thus, the plain text of the agreement—which the Court of Appeals says is the best source of the parties' intent (*see* Goldman v White Plains Ctr. for Nursing Care, LLC, 11 NY3d 173, 176, 896 NE2d 662, 867 NYS2d 27 [2008])—is not conclusive of the question on appeal.

> "Nevertheless, it is basic that, unless a contract provides otherwise, the law in force at the time the agreement is entered into becomes as much a part of the agreement as though it were expressed or referred to therein, for it is presumed that the parties had such law in contemplation when the contract was made and the contract will be construed in the light of such law" (Dolman v United States Trust Co. of N.Y., 2 NY2d 110, 116, 138 NE2d 784, 157 NYS2d 537 [1956]; *see* Ronnen v Ajax Elec. Motor Corp., 88 NY2d 582, 589, 671 NE2d 534, 648 NYS2d 422 [1996] [applying *Dolman*]).

[*214] The *Dolman* rule is of longstanding vintage, and the "principle embraces alike those [laws in force at the time of a contract's execution] which affect its validity, *construction*, discharge, and enforcement" (Von Hoffman v City of Quincy, 4 Wall [71 US] 535, 550, 18 L Ed 403 [1867] [emphasis added]). By virtue of the *Dolman* rule, when **[****2]** parties enter into an agreement authorized by or related to a particular statutory scheme, the courts will presume—absent something to the contrary—that the terms of the agreement are to be interpreted consistently with the corresponding statutory scheme (*see* ***[***6]*** *e.g.* Mayo v Royal Ins. Co. of Am., 242 AD2d 944, 945, 662 NYS2d 654 [4th Dept 1997], *lv dismissed* 91 NY2d 887, 691 NE2d 636, 668 NYS2d 564 [1998]; Matter of Andy Floors, Inc. [Tyler Constr. Corp.], 202 AD2d 938, 938-939, 609 NYS2d 692 [3d Dept 1994]).

The statutory scheme corresponding to the agreement in this case is *Domestic Relations Law § 236*, which authorizes divorce settlement agreements and directs that such agreements specify the "amount and duration of maintenance," if any (*§ 236 [B] [3] [3]*). The term " 'maintenance' " is defined within this statutory scheme as "payments provided for in a valid agreement between the parties or awarded by the court . . . , to be paid at fixed intervals for a definite or indefinite period of time" (*§ 236 [B] [1] [a]*). Critically, the statutory definition includes the following caveat: any maintenance award "shall terminate upon the death of either party or upon the payee's valid or invalid marriage" (*id.*). As thus defined, the concept of maintenance is unequivocally limited to payments made to an *unmarried* ex-spouse (*see Matter of Howard v Janowski, 226 AD2d 1087, 1088, 641 NYS2d 940 [4th Dept 1996]*). And unless the parties contract otherwise, the *Dolman* rule incorporates this statutory limitation directly into a divorce settlement agreement "as though it were expressed or referred to therein" (2 NY2d at 116; **[**850]** *see United States Trust Co. of N. Y. v New Jersey, 431 US 1, 19, 97 S Ct 1505, 52 L Ed 2d 92 n 17 [1977]*, *reh denied 431 US 975, 97 S Ct 2942, 53 L Ed 2d 1073 [1977]*).

Thus, we categorically reject the wife's argument that the statutory definition of maintenance embodied in *Domestic Relations Law § 236 (B) (1) (a)* is irrelevant simply because the parties chose to settle the **[***7]** terms of their divorce in a written agreement. To the contrary, the statutory definition of maintenance supplies the interpretive context necessary to understanding the agreement as an integrated whole, and it provides the benchmark against which those contractual provisions are to be construed. In short, the statutory definition shines a **[*215]** beacon light of clarity unto a term that might otherwise be subject to varying interpretations.[1]

II

The default rule of construction supplied **[***8]** by the statutory definition of maintenance is merely that, however—a default rule. There are many reported instances in which parties to a divorce settlement agreement have varied the statutory definition of maintenance so that payments would continue beyond the remarriage of the payee (*see e.g. Burn v Burn, 101 AD3d 488, 489, 956 NYS2d 19 [1st Dept 2012]*; *Matter of DeAngelis v DeAngelis, 285 AD2d 593, 593-594, 727 NYS2d 481 [2d Dept 2001]*; *Quaranta v Quaranta, 212 AD2d 683, 684, 622 NYS2d 778 [2d Dept 1995]*; *Jung v Jung, 171 AD2d 993, 994, 567 NYS2d 934 [3d Dept 1991]*; *Fredeen v Fredeen, 154 AD2d 908, 908, 546 NYS2d 60 [4th Dept 1989]*). In so doing, such parties effectively rebutted the presumption, embodied in the *Dolman* rule, that they intended to incorporate the corresponding statutory definitions into their agreement.

As the wife's appellate brief spills much ink in demonstrating, such a variance does not offend public policy (*see Fredeen, 154 AD2d at 908*). But the courts will not lightly infer the parties' intent to depart from the statutory definition of maintenance (*see Scibetta v Scibetta-Galluzzo, 134 AD2d 823, 824, 521 NYS2d 584 [4th Dept 1987]*), and it is well established that mere silence will not do (*see Quaranta, 212 AD2d at 684*; *Scibetta, 134 AD2d at 824*; *Jacobs v Patterson, 112 AD2d 402, 403, 492 NYS2d 59 [2d Dept 1985]*). Far from it—the parties' "intent to vary the statutory and precedential preference of an end to maintenance payments upon [remarriage] of **[****3]** the pay[ee] *must be expressed clearly*" (*Matter of Riconda, 90 NY2d 733, 737, 688 NE2d 248, 665 NYS2d 392 [1997]* [emphasis added]), for compelling a person to support a remarried ex-spouse, "absent an agreement to the contrary," most assuredly does violate the **[*216]** public policy of this State (*Jacobs v Patterson, 143 AD2d 397, 398, 532 NYS2d 429 [2d Dept 1988]*; *see Scibetta, 134 AD2d at 824*).[2]

[851]** The requisite degree of "clarity" in an agreement can be gleaned from the cases in which the parties successfully varied the statutory definition of maintenance. In *Burn*, for example, the First Department held that the wife's "waiver of a share of assets worth millions of dollars . . . evinces the intent of the parties that the maintenance payments would continue until [her] death or the death of [the husband], regardless of [her] marital status" (*101 AD3d at 489*).

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[1] In point I of her brief, the wife also argues that the summary maintenance-terminating procedure of *Domestic Relations Law § 248* "do[es] not apply when the parties settle maintenance with a[n] opting out agreement." Perhaps so, but we need not definitively resolve that issue because the husband did not move to terminate maintenance under *section 248*, and the court did not direct such relief. To the contrary, as the wife recognizes elsewhere in her brief, this is a contract-interpretation case that requires us to construe the term "maintenance" in the agreement. Thus, although the substantive provisions of *section 248* are arguably relevant to the public policy considerations of our interpretive inquiry, the summary procedure provided therein is not in play here.

[2] Although *Riconda* involved the other enumerated **[***9]** component of the definition of maintenance set forth in ***Domestic Relations Law § 236 (B) (1) (a)***—namely, that payments continue only so long as both payor and payee are living—that distinct prong of the definition is equally variable by the parties upon the same "clear" expression of intent. Thus, as the Third Department has recognized, the cases that explicate the degree of clarity necessary to vary the still-living prong of the statutory definition of maintenance are equally instructive when determining whether or not the parties effectively varied the remarriage prong of the definition (*see Sacks v Sacks, 168 AD2d 733, 734-735, 563 NYS2d 884 [3d Dept 1990]*).

Quaranta is similar to *Burn*. There, the Second Department held that "the parties intended that the [wife] receive lifetime maintenance payments" because she "gave up her right to a distributive **[***10]** share of [certain valuable] property in exchange for maintenance payments[, which] the [husband] could deduct . . . for income tax purposes" (*Quaranta, 212 AD2d at 684*).

In *DeAngelis*, the divorce settlement agreement specified, "in detail," multiple events that would terminate the husband's maintenance obligations, but it did not include the wife's remarriage among them (*285 AD2d at 593*). Such an agreement, the Second Department held, established that the husband had "implicitly agreed to pay post-remarriage maintenance" (*id. at 594*).

In *Jung*, the Third Department held that the divorce settlement agreement "clearly evinces the intent of the parties that [the husband's] maintenance obligation would continue for a five-year period unconditioned on [the wife's] marital status," given the parties' multiple affirmative statements on the record that the agreement's maintenance-terminating events, which did not include remarriage, were exclusive and unconditional (*171 AD2d at 994* [internal quotation marks and brackets omitted]).

And in *Fredeen*, we held that "the agreement clearly evinces the intent of the parties that [the husband's] maintenance **[*217]** obligation would continue until February 1991 . . . unconditioned on [the wife's] marital status," given the language **[***11]** in the agreement that such payments would continue past February 1991 unless, inter alia, the wife had remarried in the interim (*154 AD2d at 908*).

The wife points to nothing in this record that establishes the parties' intent to vary the statutory definition of maintenance with the clarity required by *Riconda* and demonstrated in *Burn*, *DeAngelis*, *Quaranta*, *Jung*, and *Fredeen*. The wife did not waive her right to any particular property distribution in exchange for a sum certain of maintenance (as the wife did in *Burn* and *Quaranta*); the agreement does not indicate that the wife's remarriage would preclude further maintenance payments after a certain date or under certain circumstances (as it did in *Fredeen*); the agreement does not set forth, in detail, various termination events while omitting remarriage from the list (as it did in *DeAngelis*); and there is no extrinsic evidence **[**852]** indicating that a remarriage clause was purposefully omitted from the agreement (as there was in *Jung*).[3]

III

Rather than attempting to establish, based on the unique facts of this case, that the parties intended to vary the statutory definition of maintenance, the wife contends that by setting the *duration* of maintenance, the parties necessarily varied the *definition* of maintenance to include payments after remarriage. We reject that contention.[4]

The concept of "maintenance," as noted above, is explicitly limited by statute to payments made to an unmarried payee (*see Domestic Relations Law § 236 [B] [1] [a]*; *Howard, 226 AD2d at 1088*), and the legislature explicitly invited parties to **[*218]** a divorce settlement agreement to fix the duration of "maintenance" *as defined within the operative statutory universe*, i.e., **[***13]** as payments that "shall terminate" upon the remarriage of the payee (*§ 236 [B] [3] [3]*; *see generally* McKinney's Cons Laws of NY, Book 1, Statutes § 236).[5] It follows that, by setting the duration of "maintenance" in an agreement pursuant to *Domestic Relations Law § 236*, the parties are necessarily fixing the length of an obligation that continues in force only so long as the payee remains unmarried. If the parties wish

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[3] The other cases upon which the wife relies—*Matter of Benny v Benny (199 AD2d 384, 605 NYS2d 311 [2d Dept 1993])* and ***Gush v Gush (9 AD2d 815, 192 NYS2d 678 [3d Dept 1959])***—are simply inapposite. The agreement in *Benny* was governed by California law (*see 199 AD2d at 386-387*), and the agreement in *Gush*—which was executed before the advent of equitable distribution **[***12]** —stated that the husband's alimony obligation was to be " 'absolute, unconditional and irrevocable' " (***9 AD2d at 815***).

[4] Given the many statutory and policy differences between maintenance and child support, the agreement's child support provisions do not logically inform the proper interpretation of the maintenance provisions, nor do the child support provisions assist in answering the discrete question posed by this appeal, i.e., whether the parties clearly varied the statutory definition of maintenance by providing for continued payments after the wife's remarriage.

[5] Statutes ***§ 236***, as distinct from ***Domestic Relations Law § 236***, provides that, "[i]n the absence of anything in the statute indicating an intention to the contrary, where the same word [here, 'maintenance,'] is used in different parts of a statute, it will be presumed to be used in the same sense throughout." Thus, the term "maintenance" means the same thing in ***Domestic Relations Law § 236 (B) (3) (3)*** as it does in ***Domestic Relations Law § 236 (B) (1) (a)***.

to depart from that statutory definition, they must do so "clearly" (Riconda, 90 NY2d at 737), not simply by following the statutory directive to set the "duration" of a thing already defined. Any other construction would impermissibly frustrate the legislative definition of "maintenance." To the extent that our decision in Hancher v Hancher (31 AD3d 1152, 818 NYS2d 384 [4th Dept 2006]) suggests a contrary rule, it should no longer be followed.

Indeed, the wife's proposed rule would mean that the legislature initially defined the term "maintenance," yet then proceeded, **[***14]** within the same section of the Domestic Relations Law, to direct contracting parties to take an act—i.e., set the "duration" of "maintenance" in a settlement agreement—that would necessarily and fundamentally change the very definition that the legislature had just adopted. In short, according to the wife, the legislature simultaneously defined a term and set up a procedure that invariably negates a core feature of that definition in each and **[**853]** every case. Such a statutory scheme would be at war with itself, and we cannot countenance such a result.

The wife's argument overlooks the fact that, in practice, virtually every divorce settlement agreement will fix the duration of a maintenance award. Consequently, in the mine-run of matrimonial dissolutions, the wife's proposed holding would effectively flip the statutory presumption: maintenance payments would presumptively survive the payee's remarriage, and **[****4]** the parties would need to take affirmative steps in the agreement to provide otherwise. But that is precisely the opposite of the legislature's decree, and it is not for the courts to legislate in **[*219]** the guise of construction (*see generally* Matter of Tormey v LaGuardia, 278 NY 450, 451, 17 NE2d 126 [1938]).[6]

Conclusion

Unless the parties clearly provide otherwise in a divorce settlement agreement, the payor's obligation to pay maintenance ends upon the remarriage of the payee. Here, the relevant agreement is silent as to whether the husband's maintenance obligation survives the wife's remarriage. As a result, the husband's maintenance obligation terminated upon the wife's remarriage. Supreme Court therefore properly denied the wife's motion to, inter alia, hold the husband in contempt and recover the unpaid maintenance. Accordingly, the order appealed from should be affirmed.

CENTRA, J.P., CURRAN and TROUTMAN, JJ., concur.

It is hereby ordered that the order so appealed from is unanimously affirmed without costs.

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[6] It is true, as the wife argues at great length, **[***15]** that parties to a divorce settlement agreement need not *explicitly* modify the statutory definition of maintenance in order to do so *effectively*. No one suggests otherwise. But the mere fact that the statutory definition of maintenance could be varied *implicitly* does not, as the wife argues, relieve contracting parties of the obligation to express that variance *clearly*.

Castellotti v Free

Supreme Court of New York, Appellate Division, First Department

March 8, 2016; March 8, 2016, Entered

158162/12, 16143

Reporter

138 A.D.3d 198 *; 27 N.Y.S.3d 507 **; 2016 N.Y. App. Div. LEXIS 1614 ***; 2016 NY Slip Op 01625 ****

[**1]** Peter Castellotti, Appellant, v Lisa Free, Respondent.

Subsequent History: Decision reached on appeal by, in part, Appeal dismissed by, in part *Castellotti v. Free, 165 A.D.3d 535, 86 N.Y.S.3d 50, 2018 N.Y. App. Div. LEXIS 6999 (N.Y. App. Div. 1st Dep't, Oct. 23, 2018)*

Prior History: Appeal from an order of the Supreme Court, New York County (Eileen A. Rakower, J.), entered July 11, 2014, as amended by an order of that court, entered August 5, 2014. The amended order granted defendant's motion to dismiss the complaint.

Castellotti v. Free, 2014 N.Y. Misc. LEXIS 6131 (N.Y. Sup. Ct., Aug. 5, 2014)
Castellotti v. Free, 2014 N.Y. Misc. LEXIS 3084 (N.Y. Sup. Ct., July 10, 2014)

Counsel: **[***1]** *Schwartz, Levine & Kaplan, PLLC*, New York City (*Chad T. Harlan* and *Jeffrey A. Kaplan* of counsel), for appellant.

Fox Rothschild LLP, New York City (*James M. Lemonedes* and *Zev Singer* of counsel), for respondent.

Judges: Peter Tom, J.P., David B. Saxe, Rosalyn H. Richter, Judith J. Gische, JJ. Opinion by Richter, J. All concur.

Opinion by: Rosalyn H. Richter

Opinion

[*200] **[**510]** Richter, J.

This action involves a family dispute between plaintiff Peter Castellotti and his sister, defendant Lisa Free.[1] Before her death, the parties' late mother, Madeline Castellotti, removed Peter from her will, leaving Lisa as sole beneficiary. Madeline made this change because Peter was going through a divorce, and Madeline wanted to prevent Peter's then-wife from benefiting from any of Madeline's assets. At about the same time, Peter and Lisa allegedly entered into an oral agreement whereby Lisa agreed, inter alia, to give Peter half **[**511]** of the inheritance when his divorce became final, in return for Peter's paying **[***2]** Madeline's estate taxes. After Peter paid the taxes, Lisa allegedly reneged on the deal, and this action ensued. We conclude that the complaint **[****2]** states viable claims for both promissory estoppel and unjust enrichment, even though the parties' oral agreement is barred by the statute of frauds. Further, under the circumstances presented here, Peter's claims need not be dismissed on public policy grounds merely because he entered into the alleged oral agreement for the purpose of delaying the receipt of assets that he never owned in the first place.

Madeline was the sole shareholder of Whole Pies, Inc., a business that owns John's Pizzeria in midtown Manhattan. In February 2003, prior to Madeline's death, Peter brought a divorce action against his then-wife, Rea Castellotti. After the divorce action was commenced, Madeline, who was seriously ill, decided to change her will to remove Peter as 50% beneficiary **[*201]** and instead make his sister Lisa the sole beneficiary. Madeline made the change because she disliked Rea, and wanted to ensure that Rea would not benefit in the divorce action from **[***3]** any of Madeline's assets.

In June 2004, Madeline passed away and, pursuant to her will, Lisa received all of Madeline's assets, including 100% of Whole Pies, 51% of PMPL, LTD (the general partner of a real estate partnership), Madeline's

[1] The facts set forth are taken from the complaint and are accepted as true for purposes of this appeal.

residence on Staten Island, and funds contained in various bank accounts (collectively the assets). In 2004, both before and again after Madeline's death, Peter and Lisa allegedly entered into an oral agreement whereby Peter agreed to pay Madeline's estate taxes with his share of Madeline's life insurance proceeds. In return, Lisa agreed to give Peter 50% of the assets upon the finality of his divorce, and 50% of the income and proceeds generated from the assets before the divorce was final. Lisa also agreed to name Peter as sole beneficiary of a life insurance policy valued at no less than $5 million, and to maintain that policy until the assets were physically transferred to Peter.

In February 2005, pursuant to the oral agreement, Peter allegedly paid Madeline's estate taxes with his share of the life insurance proceeds. After Peter's divorce became final in November 2008, Lisa failed to transfer 50% of the assets to Peter. Lisa did maintain an account **[***4]** in her name at Wachovia Bank, to which Peter was given access, and told Peter that she was depositing his 50% of the net proceeds from Whole Pies into the account. Lisa, however, did not deposit the agreed-upon 50%, but only made sporadic deposits; in May 2011, Lisa denied Peter access to the account. Lisa also procured, at Peter's expense, a $5 million insurance policy naming Peter as sole beneficiary. Lisa maintained this policy from February 2005 until May 2012, when she refused to sign the renewal documents and let the policy lapse.

Peter commenced this action, asserting claims against Lisa for breach of contract, unjust enrichment, breach of fiduciary duty, an accounting, fraud, breach of the covenant of good faith and fair dealing, and conversion.[2] Lisa answered, and asserted **[**512]** affirmative defenses, including that Peter's claims were barred **[*202]** by the statute of frauds. Lisa thereafter moved, pursuant to *CPLR 3211*, to dismiss the complaint. In a decision entered July 11, 2014, the motion court granted Lisa's motion and dismissed the **[****3]** complaint in its entirety *(2014 NY Slip Op 31798[U] [2014])*.[3] This appeal ensued.

[1] The complaint contains two causes of action for breach of contract. In the first, Peter alleges that although he fully complied with the oral agreement by paying Madeline's estate taxes, Lisa breached the contract by failing to transfer any of the assets to Peter or provide him with 50% of the income and proceeds generated from the assets. The second cause of action alleges that Lisa breached the agreement by failing to renew the $5 million life insurance policy. The motion court properly dismissed these claims as barred by the statute of frauds. *General Obligations Law § 5-701 (a) (9)* provides that an agreement must be in writing if it is "a promise . . . to name a beneficiary of [a life insurance] policy." As alleged in the complaint, the oral **[***6]** agreement here included a promise by Lisa to name Peter as sole beneficiary of a life insurance policy. Thus, that provision falls squarely within the statute of frauds, rendering the entire agreement void (*see* *Apostolos v R.D.T. Brokerage Corp., 159 AD2d 62, 65, 559 NYS2d 295 [1st Dept 1990]* ["As a general rule, if part of an entire contract is void under the Statute of Frauds, the whole contract is void"]).[4]

Peter argues that even if the life insurance provision falls within the statute of frauds, that provision is severable and does not void the remainder of the agreement.

> "[W]here an oral agreement is a severable one, i.e., susceptible of division and apportionment, having two or more parts not necessarily dependent upon each other, that part which, if standing alone, is not required to be in writing, may be enforced, provided such apportionment of the agreement may be accomplished without doing violence to its terms or making a new contract for the parties" (*id.*).

[*203] Under the oral agreement alleged **[***7]** here, Peter promised to pay Madeline's estate taxes and, in exchange, Lisa agreed to give Peter 50% of the assets upon his divorce being final, and 50% of the income and proceeds generated by the assets prior to the finality of the divorce. Lisa also promised to name Peter as the

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[2] In June 2013, Peter's ex-wife Rea moved to intervene in this action to bring claims against Peter and Lisa for falsely **[***5]** representing during the divorce action that Peter had no ownership interest in Whole Pies. The lower court granted Rea's motion, but that order was reversed on appeal *(118 AD3d 631, 990 NYS2d 168 [1st Dept 2014])*. This Court concluded that the proper remedy for any possible fraud committed during the divorce action was to move to vacate the divorce judgment, and not to collaterally attack that judgment in this action (*118 AD3d at 631-632*).

[3] On August 5, 2014, an amended order was entered correcting the original order by adding decretal language.

[4] There is no merit to Peter's claim that Lisa failed to meet her burden to affirmatively disprove the existence of a written contract. Because the complaint explicitly states that the parties entered into an oral agreement, there was no need for Lisa to show that no writing existed.

sole beneficiary on a life insurance policy that would be in existence up until the date of the physical transfer of the assets. Thus, the life insurance provision is intertwined with and dependent on the provision involving transfer of the assets, and cannot be apportioned without doing violence to the terms of the agreement (*see e.g. Jordache Ltd. v Oved, 40 AD3d 400, 400, 836 NYS2d 136 [1st Dept 2007]*; *Whitman Heffernan Rhein & Co. v Griffin Co., 163 AD2d 86, 87, 557 NYS2d 342 [1st Dept 1990]*, *lv denied 76 NY2d 715, 565 NE2d 1269, 564 NYS2d 718 [1990]*). Indeed, in his appellate brief, Peter concedes that the life insurance provision serves as "collateral" to ensure satisfaction of the other provisions. Further, the life insurance provision and the remaining provisions **[**513]** of the agreement are both supported by the same consideration, namely, Peter's payment of Madeline's estate taxes (*see Sheresky v Sheresky Aronson Mayefsky & Sloan, LLP, 35 Misc 3d 1201[A], 950 NYS2d 611, 2011 NY Slip Op 52504[U], *11 [Sup Ct, NY County 2011]* [portions of oral agreement not severable where the plaintiff alleged the same consideration for both promises]).

The motion court properly rejected Peter's claim that the alleged partial performance of the agreement removes it **[***8]** from the statute of frauds. Although *General Obligations Law § 5-703* requires certain contracts concerning real property to be in writing, *section 5-703 (4)* permits a court, acting in equity, to compel the specific performance of agreements that have been partially **[****4]** performed. This Court has held, however, that the partial performance exception applies only to the statute of frauds provision in *section 5-703*, and has not been extended to *section 5-701* (*Gural v Drasner, 114 AD3d 25, 32, 977 NYS2d 218 [1st Dept 2013]* ["the law simply does not provide for or permit a part performance exception for oral contracts other than those to which *General Obligations Law § 5-703* applies"], *lv dismissed 24 NY3d 935, 993 NYS2d 546, 17 NE3d 1144 [2014]*). Here, Lisa asserted a statute of frauds defense under *General Obligations Law § 5-701*, not *section 5-703*. Thus, the partial performance doctrine is inapplicable (*see Rose v Spa Realty Assoc., 42 NY2d 338, 343, 366 NE2d 1279, 397 NYS2d 922 [1977]* ["Although the General Obligations Law (*§ 5-703, subd 2*) subjects the sale of real property to the Statute of Frauds, it was not pleaded by defendants and is therefore not involved in this case"]).

[*204] Peter argues that the partial performance doctrine is properly invoked here because the oral agreement involves conveyances of real property. Specifically, Peter points to Lisa's promise to transfer 50% of PMPL, and 50% of Madeline's Staten Island residence. First, PMPL is not real property, but rather, only an entity that is a general partner in another entity **[***9]** that owns real property. Second, even if the promised conveyance of PMPL and the Staten Island home could be saved by the partial performance doctrine contained in *General Obligations Law § 5-703*, those provisions of the contract are not severable from the larger agreement, the whole of which is barred by *General Obligations Law § 5-701*.

Although the breach of contract causes of action cannot stand, the complaint sufficiently states a claim under the doctrine of promissory estoppel.[5] The elements of a promissory estoppel claim are: (i) a sufficiently clear and unambiguous promise; (ii) reasonable reliance on the promise; and (iii) injury caused by the reliance (*see MatlinPatterson ATA Holdings LLC v Federal Express Corp., 87 AD3d 836, 841-842, 929 NYS2d 571 [1st Dept 2011]*, *lv denied 21 NY3d 853 [2013]*; *Agress v Clarkstown Cent. School Dist., 69 AD3d 769, 771, 895 NYS2d 432 [2d Dept 2010]*; *Fleet Bank v Pine Knoll Corp., 290 AD2d 792, 797, 736 NYS2d 737 [3d Dept 2002]*; *Chemical Bank v City of Jamestown, 122 AD2d 530, 531, 504 NYS2d 908 [4th Dept 1986]*, *lv denied 68 NY2d 608, 500 NE2d 874, 508 NYS2d 1025 [1986]*). If a contract is barred by the statute of frauds, a promissory estoppel claim is viable in the limited set of circumstances where unconscionable **[**514]** injury results from the reliance placed on the alleged promise (*see Fleet Bank, 290 AD2d at 796-797*; *Melwani v Jain, 281 AD2d 276, 277, 722 NYS2d 145 [1st Dept 2001]*; *Steele v Delverde S.R.L., 242 AD2d 414, 415, 662 NYS2d 30 [1st Dept 1997]*; *WE Transp. v Suffolk Transp. Serv., 192 AD2d 601, 602, 596 NYS2d 166 [2d Dept 1993]*, *lv denied 82 NY2d 656, 622 NE2d 306, 602 NYS2d 805 [1993]*; *Buddman Distribs. v Labatt Importers, 91 AD2d 838, 839, 458 NYS2d 395 [4th Dept 1982]*).

[2] Here, the allegations of the complaint show an unambiguous promise by Lisa to provide Peter with half of the income generated by the assets during **[***10]** the pendency of Peter's divorce, to transfer half of the assets upon the finality of the divorce, and to name

[5] Although a cause of action for promissory estoppel is not expressly asserted in the complaint, the factual allegations therein sufficiently "fit within" a promissory estoppel claim (*Leon v Martinez, 84 NY2d 83, 87-88, 638 NE2d 511, 614 NYS2d 972 [1994]*).

Peter as sole beneficiary of a life insurance policy of at least $5 million. The complaint's allegations also show **[*205]** that Peter detrimentally relied on those promises by paying a substantial amount in taxes for Madeline's estate, and suffered resulting monetary damages (*see* *Forman v Guardian Life Ins. Co. of Am., 76 AD3d 886, 888-889, 908 NYS2d 27 [1st Dept 2010]* [reading the complaint in a light most favorable to the plaintiffs, the pleadings sufficiently allege a clear and unambiguous promise, reliance on the promise and damages]).[6]

Further, triable issues of fact exist as to whether Peter has suffered the requisite unconscionable injury (*see* *Ackerman v Landes, 112 AD2d 1081, 1083-1084, 493 NYS2d 59 [2d Dept 1985])*. At a minimum, Peter, who received nothing under Madeline's will, allegedly paid $2 **[***11]** million in estate taxes, expecting that he would later receive his share of the inheritance. To dismiss this claim as a matter of law would permit Lisa to keep all of the assets, which include a successful New York restaurant business, despite Peter's alleged substantial payment of the estate taxes (*see Buddman Distribs. v Labatt Importers, 91 AD2d 838, 839, 458 NYS2d 395 [4th Dept 1982]* [whether circumstances rise to the level of unconscionable injury should not be determined on the pleadings]).

Lisa does not dispute that a promissory estoppel claim may lie even where an underlying contract is barred by the statute of frauds. Instead, she argues that public policy should bar Peter from any recovery because he entered into the alleged oral agreement for the purpose of delaying the receipt of the prospective assets until after the conclusion of the divorce action. Although "illegal contracts, or those contrary to public policy, are unenforceable" (*Szerdahelyi v Harris, 67 NY2d 42, 48, 490 NE2d 517, 499 NYS2d 650 [1986]*), there is nothing illegal about the parties' agreement here. Madeline was free to leave her property to whomever she pleased, and the siblings were free to enter into an agreement to redistribute that inheritance.

Lisa does not identify any statute, rule or regulation that was violated by Peter and Lisa's entry into the agreement. **[***12]** Nor is there any claim that Peter concealed or transferred any property actually owned by him or titled in his name, either **[*206]** before or during the divorce action. Indeed, the purported assets alleged to have been undisclosed, i.e., the shares in Whole Pies, were never within Peter's possession. At **[**515]** most, there is a claim that Peter attempted to delay the receipt of these shares, which he was never legally entitled to in the first place, and did not disclose this potential revenue source to his then-wife. While the failure to disclose Peter's right to receive the assets in the future may impact the financial issues in the matrimonial action, that factor alone does not require wholesale dismissal of Peter's claims on public policy grounds.

This case stands in contrast to the cases cited by Lisa, where courts invoked public policy principles to deny recovery where illegality was manifest (*see e.g.* *McConnell v Commonwealth Pictures Corp., 7 NY2d 465, 470, 166 NE2d 494, 199 NYS2d 483 [1960]* [money the plaintiff sued for was the fruit of admitted crime]; *Anonymous v Anonymous, 293 AD2d 406, 407, 740 NYS2d 341 [1st Dept 2002]* ["an agreement for financial support in exchange for illicit sexual relations is violative of public policy and thus unenforceable"]; *Abright v Shapiro, 214 AD2d 496, 626 NYS2d 73 [1st Dept 1995]* [denying recovery where the parties were engaged in a scheme in violation of rent stabilization **[***13]** laws and zoning regulations]; *United Calendar Mfg. Corp. v Huang, 94 AD2d 176, 180, 463 NYS2d 497 [2d Dept 1983]* [fee-splitting arrangement was, on its face, violative of the Education Law]; *Braunstein v Jason Tarantella, Inc., 87 AD2d 203, 450 NYS2d 862 [2d Dept 1982]* [dismissing claims with respect to distribution of a film that was produced in violation of obscenity statutes]).[7]

In invoking public policy, Lisa purports to be protecting Peter's ex-wife Rea from a fraud allegedly committed in the divorce action. To deny Peter recovery here, however, would do nothing to protect Rea, the alleged victim of the fraudulent scheme. Instead, Lisa, who

[6] On appeal, Peter asserts this figure is $2 million. Although the complaint does not explicitly set forth the $2 million figure, it does refer to a "significant financial expenditure." We note that an affidavit submitted in opposition to Lisa's dismissal motion characterizes the amount as "over a million dollars," and during oral argument before the motion court, Peter's counsel stated that the estate taxes paid by Peter amounted to $2 million.

[7] Lisa's reliance on *Reid v McLeary (271 AD2d 668, 706 NYS2d 179 [2d Dept 2000])* and *Gould v Gould (261 App Div 733, 27 NYS2d 54 [1st Dept 1941]*, *lv denied 262 App Div 833, 29 NYS2d 503 [1st Dept 1941])* is misplaced. In those cases, courts found agreements to be against public policy where the main objective was to dissolve a marriage and to facilitate the obtaining of a divorce. Here, the parties' alleged agreement does neither.

allegedly participated in the fraud, would obtain a windfall by inheriting all of the assets, despite Peter's having allegedly paid $2 million in estate taxes. Such a perverse outcome would not serve any important public policy goals. If we were to accept Lisa's public policy argument, we **[*207]** would be rewarding families who seek to secrete prospective assets from a soon-to-be ex-spouse, something we decline to do.

In reaching this decision, **[***14]** we do not condone parties in matrimonial actions being less than candid with their spouses about their assets. Peter's alleged fraudulent behavior, however, should be explored in the matrimonial action, but should not preclude him from moving forward with at least some of his claims here. In our earlier decision denying Rea leave to intervene in this action, we concluded that her remedy for any fraud committed during the course of the matrimonial proceeding was to move to vacate the divorce judgment (*118 AD3d at 631-632*). We note that the record here does not allow us to determine whether Peter intentionally concealed the alleged oral agreement from Rea, or what the legal significance of that would be. Nor can we make any determination whether or not Peter made any false statements during the divorce proceeding about his assets, including in his net worth statement.

Further, allowing Peter to recover in this action may provide Rea with the **[**516]** opportunity to reopen the divorce action to explore the circumstances surrounding Peter and Lisa's alleged oral contract. We recognize that an inheritance is generally considered to be separate property (*see Domestic Relations Law § 236 [B] [1] [d] [1]*; *Tatum v Simmons, 133 AD3d 550, 550, 21 NYS3d 208 [1st Dept 2015]*). However, in her intervenor complaint, Rea stated that if **[***15]** she had known that Peter would later receive half of the inheritance, she would have sought more when she settled her equitable distribution claims. Rea also maintained that the matrimonial court's awards of maintenance and child support would have been greater if the court had known of the alleged oral agreement.

[3] The factual allegations of the complaint sufficiently state a cause of action for unjust enrichment with respect to Peter's payment of Madeline's estate taxes and Lisa's life insurance premiums. To establish unjust enrichment, the plaintiff must show that the defendant was enriched, at the plaintiff's expense, and that it is against equity and good conscience to permit the defendant to retain what is sought to be recovered (*Georgia Malone & Co., Inc. v Rieder, 19 NY3d 511, 516, 973 NE2d 743, 950 NYS2d 333 [2012]*). Here, the complaint's allegations show that Lisa was enriched at Peter's expense because Peter paid the estate taxes and insurance premiums, despite Lisa's being the sole beneficiary **[*208]** of the will, and that it would be against equity and good conscience to allow Lisa to retain that windfall.[8]

This theory of unjust enrichment is not precluded by the statute of frauds because it is not an attempt to enforce the oral contract but instead seeks to recover the amount by which Lisa was enriched at Peter's expense (*see Grimes v Kaplin, 305 AD2d 1024, 1024, 758 NYS2d 591 [4th Dept 2003]* [statute of frauds does not bar unjust enrichment cause of action where it does not seek to enforce a promise but rather seeks to recover the reasonable value of property or services rendered in reliance on the promise]; *Kearns v Mino, 83 AD2d 606, 606, 441 NYS2d 297 [2d Dept 1981]* [upholding unjust enrichment claim despite dismissal of contract claim on statute of frauds grounds]; *see also Farash v Sykes Datatronics, 59 NY2d 500, 503, 452 NE2d 1245, 465 NYS2d 917 [1983]* [quasi contract claim may proceed where it did not attempt to enforce an oral agreement, but merely sought to recover expenditures made by the plaintiff in reliance upon statements made by and at the request of the defendant]).

For the reasons previously discussed, there is no merit to Lisa's contention that the unjust enrichment claim should be dismissed on public policy grounds. Peter's recovery **[***17]** on this claim, however, cannot extend to the benefits he was allegedly due under the oral agreement (*see Komolov v Segal, 117 AD3d 557, 557, 985 NYS2d 411 [1st Dept 2014]* [precluding unjust enrichment claim because it sought same relief that was barred by the statute of frauds]; *Andrews v Cerberus Partners, 271 AD2d 348, 348, 707 NYS2d 85 [1st Dept 2000]* [dismissing claim for unjust enrichment that was indistinguishable from breach of contract claim barred by statute of frauds]). To the **[**517]** extent the complaint alleges unjust enrichment based on Lisa's misuse of corporate monies, any such claim belongs to

[8] Although the unjust enrichment cause of action in the complaint does not expressly advance this theory, it does "repeat[ ] and reallege[ ]" all allegations set forth previously, **[***16]** including those showing that Peter made the tax payment even though he was not a beneficiary of the will. Given the liberal pleading standards and standard of review on a *CPLR 3211* motion (*see Leon, 84 NY2d at 87-88*), Peter should be permitted to pursue this cause of action.

the companies, not Peter individually (*see Dragon Inv. Co. II LLC v Shanahan, 49 AD3d 403, 404-405, 854 NYS2d 115 [1st Dept 2008]*).

The complaint alleges that Lisa owed Peter a fiduciary duty of care and loyalty, and that Lisa breached that duty in two **[*209]** ways: by using the funds of Whole Pies for her own personal purposes, and by committing a host of improper acts, including failing to pay the company's sales and payroll taxes, filing a false insurance application, and operating John's Pizzeria in violation of numerous administrative regulations. To state a claim for breach of fiduciary duty, a plaintiff must allege the existence of a fiduciary relationship, misconduct by the other party, and damages directly caused by that party's misconduct (*see Pokoik v Pokoik, 115 AD3d 428, 429, 982 NYS2d 67 [1st Dept 2014]*).

[4] The motion court properly dismissed the fiduciary duty claims because **[***18]** the complaint fails to allege that a fiduciary relationship existed between Peter and Lisa. Although Peter argues that he is owed a fiduciary duty as a "rightful" shareholder of Whole Pies, it is undisputed that he has no ownership interest in the company. Nor has he ever had any such interest in the past. Rather, the complaint states that 100% of the shares in Whole Pies were transferred to Lisa upon Madeline's death. Indeed, the complaint acknowledges that Peter entered into an agreement with Lisa specifically to forestall his becoming a shareholder.

Peter nevertheless argues that he would become a shareholder of Whole Pies if he were to prevail in this action. But the complaint seeks only monetary damages and contains no request for declaratory relief as to Peter's shareholder status. Nor did the now-dismissed breach of contract claims seek specific performance of Lisa's alleged promise to transfer the shares. In any event, even if Peter could somehow obtain shareholder status as a result of this lawsuit, that would not retroactively make him a shareholder for the time period when the alleged breaches of fiduciary duty took place.

Although not alleged in the complaint, on appeal, **[***19]** Peter contends that a fiduciary relationship exists based on his familial relationship as Lisa's sibling, along with unspecified prior business dealings. The mere fact that the parties are siblings, standing alone, is insufficient to support a fiduciary relationship (*see Chasanoff v Perlberg, 19 AD3d 635, 635-636, 798 NYS2d 116 [2d Dept 2005]* [no fiduciary relationship between plaintiff sister and defendant brother]). Although family members in a co-owned business venture can owe each other fiduciary duties (*see Braddock v Braddock, 60 AD3d 84, 88, 871 NYS2d 68 [1st Dept 2009]*), **[*210]** the complaint contains no facts to **[****5]** suggest that Peter and Lisa had any business dealings.[9]

Even if a fiduciary relationship did exist, the claims that Lisa misappropriated Whole Pie's funds and failed to operate the company in compliance with the law belong to the company, not to Peter individually (*see Abrams v Donati, 66 NY2d 951, 953, 489* ***[**518]*** *NE2d 751, 498 NYS2d 782 [1985]*). Although not pleaded in the complaint, **[***20]** in his appellate brief, Peter argues that Lisa also breached her fiduciary duty by failing to transfer to him his purported interest in Whole Pies. These allegations merely duplicate one of the contract claims dismissed on statute of frauds grounds, and the requirement of a writing cannot be circumvented by recasting the claim as one sounding in tort (*see Pollak v Moore, 85 AD3d 578, 579, 926 NYS2d 434 [1st Dept 2011]; Kaminer v Wexler, 40 AD3d 405, 405, 836 NYS2d 139 [1st Dept 2007], lv dismissed in part and denied in part 9 NY3d 955, 877 NE2d 298, 846 NYS2d 79 [2007]*).

The complaint contains two causes of action for an accounting, one for Whole Pies and the other for its management company. The right to an accounting is premised upon the existence of a fiduciary relationship (*Adam v Cutner & Rathkopf, 238 AD2d 234, 242, 656 NYS2d 753 [1st Dept 1997]*). Since no fiduciary relationship is alleged, the accounting claims cannot stand (*see Royal Warwick S.A. v Hotel Representative, Inc., 106 AD3d 451, 452, 965 NYS2d 409 [1st Dept 2013]*). Nor has Peter alleged that he is a shareholder of either entity, which would give rise to the right to an accounting (*see Seretis v Fashion Vault Corp., 110 AD3d 547, 548, 973 NYS2d 176 [1st Dept 2013], lv denied 22 NY3d 861, 995 NYS2d 1, 19 NE3d 869 [2014]*).

The motion court properly dismissed the conversion claim, which alleges that Lisa used the funds of Whole Pies and its management company for her own personal purposes. "A conversion takes place when

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[9] Peter's reliance on Rea's proposed intervenor complaint is unavailing. In that pleading, Rea alleges that in 1996, Peter began working toward opening John's Pizzeria, and provided initial funding for the venture. Simply because Peter may have helped to start John's Pizzeria 20 years ago sheds no light on whether Peter and Lisa subsequently had any business relationship, let alone the nature of any such dealings.

someone, intentionally and without authority, assumes or exercises control over personal property belonging to someone else, interfering with that person's right of **[***21]** possession" (*Colavito v New York Organ Donor Network, Inc., 8 NY3d 43, 49-50, 860 NE2d 713, 827 NYS2d 96 [2006])*. The complaint fails to allege that Peter had any possessory interest in the corporate monies, and, in any event, such claim would belong to the **[*211]** companies, not Peter individually (*see Ehrlich v Hambrecht, 19 AD3d 259, 259, 797 NYS2d 471 [1st Dept 2005]*). To the extent Peter alleges that Lisa converted the funds Peter allegedly paid for Madeline's estate taxes, the complaint alleges no facts that would establish that Lisa exercised any control over such funds.

The claim for breach of the covenant of good faith and fair dealing fails, because there is no enforceable contract (*see Randall's Is. Aquatic Leisure, LLC v City of New York, 92 AD3d 463, 463, 938 NYS2d 62 [1st Dept 2012]*, *lv denied 19 NY3d 804, 969 NE2d 786, 946 NYS2d 567 [2012]*; *Guarino v North Country Mtge. Banking Corp., 79 AD3d 805, 807, 915 NYS2d 84 [2d Dept 2010]*). Finally, the fraudulent inducement claim was properly dismissed because it alleges only an insincere promise of future performance under the oral contract (*see Forty Cent. Park S., Inc. v Anza, 117 AD3d 523, 524, 985 NYS2d 543 [1st Dept 2014]*).

We have considered the parties' remaining contentions and find them unavailing.

Accordingly, the order of Supreme Court, New York County (Eileen A. Rakower, J.), entered July 11, 2014, as amended by the order of the same court and Justice, entered August 5, 2014, which granted defendant's motion to dismiss the complaint, should be modified, on the **[****6]** law, to deny the motion as to the claims for promissory estoppel, and unjust enrichment to the extent indicated herein, and otherwise affirmed, **[***22]** without costs.

Tom, J.P., Saxe and Gische, JJ., concur.

Order, Supreme Court, New York County, entered July 11, 2014, as amended by order **[**519]** , entered August 5, 2014, modified, on the law, the motion denied as to the claims for promissory estoppel, and unjust enrichment to the extent indicated, and otherwise affirmed, without costs.

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CDR Creances S.A. v. Euro-American Lodging Corp.

Supreme Court of New York, Appellate Division, First Department

May 22, 2007, Decided; May 22, 2007, Entered

8306-8306A, 8307-8308-8308A, Index 109565/03, Index 115951/03

Reporter

40 A.D.3d 421 *; 837 N.Y.S.2d 609 **; 2007 N.Y. App. Div. LEXIS 6272 ***; 2007 NY Slip Op 4338 ****

[**1]** CDR Créances S.A., as Successor to Société de Banque Occidentale, Appellant, v Euro-American Lodging Corporation, et al., Respondents, et al., Intervenor-Defendant, et al. Defendants. (Action No. 1.) CDR Créances S.A., as Successor to Société de Banque Occidentale, Respondent, v Euro-American Lodging Corporation, Appellant. (Action No. 2.)

Subsequent History: Later proceeding at *CDR Creances S.A. v. Euro-American Lodging Corp., 2007 N.Y. App. Div. LEXIS 8328 (N.Y. App. Div. 1st Dep't, July 5, 2007)*

Prior History: *CDR Creances S.A. v. Euro-American Lodging Corp., 43 A.D.3d 45, 837 N.Y.S.2d 33, 2007 N.Y. App. Div. LEXIS 6278 (N.Y. App. Div. 1st Dep't, 2007)*
CDR Creances, S.A. v. Euro-American Lodging Corp., 2007 N.Y. App. Div. LEXIS 2412 (N.Y. App. Div. 1st Dep't, Mar. 1, 2007)

Counsel: **[***1]** Kellner Herlihy Getty & Friedman, LLP, New York (Douglas A. Kellner of counsel), for CDR CrE;ances S.A., appellant/respondent.

Morvillo, Abramowitz, Grand, Iason & Silberberg, P.C., New York (Stephen M. Juris of counsel), for Euro-American Lodging Corporation, Gama Lodging LLC and Simon Elias, respondents.

Bryan Cave LLP, New York (Suzanne M. Berger of counsel), for Euro-American Lodging Corporation, appellant.

Judges: Concur--Saxe, J.P., Nardelli, Williams, Catterson, Malone, JJ.

Opinion

[*421] [610]** Judgment, Supreme Court, New York County (Debra A. James, J.), entered April 12, 2005, dismissing the complaint in the first-captioned action against defendants Euro-American Lodging, Elias and Gama Lodging, unanimously affirmed, with costs. Appeal from order, same **[****2]** court and Justice, entered March 3, 2005, unanimously dismissed, without costs. Judgments, Supreme Court, New York County (Debra A. James, J.), entered April 19 and October 19, 2005, respectively awarding plaintiff in the second-captioned action the principal sum of $ 95,837,522, and confirming a Special Referee's report awarding interest in the total sum of $ 112,159,088.41, unanimously affirmed, with costs. Appeal from order, same court and Justice, entered March **[***2]** 22, 2005, which granted plaintiff's motion for summary judgment, unanimously dismissed, without costs, as subsumed in the appeals from the judgments.

[*422] In the action for breach of a pledge agreement and related torts, the motion court properly dismissed the contract **[**611]** claim against defendants who were not parties to the agreement (*see* *Seaver v Ransom, 224 NY 233, 237, 120 NE 639 [1918]*), and properly rejected the contention that said nonsignatory defendants were bound because the agreement stated that it was binding on the pledgors' heirs and assigns; the agreement plainly meant heirs and assigns in the capacity of pledgors. The tortious interference cause of action was deficient for failure to allege the required "but for" causation and intent to induce a breach in nonconclusory fashion (*see* *Lama Holding Co. v Smith Barney, 88 NY2d 413, 424-425, 668 NE2d 1370, 646 NYS2d 76 [1996]*), and for failure to connect the entities to the alleged wrongdoing of the individuals and to each other by nonconclusory allegations regarding the claimed alter ego status and control (*see Sheridan Broadcasting Corp. v Small, 19 AD3d 331, 798 NYS2d 45 [2005]*), or to set forth how the corporate form was used as an instrument of wrongdoing (*see* *TNS Holdings v MKI Sec. Corp., 92 NY2d 335, 339, 703 NE2d 749, 680 NYS2d 891 [1998]*). **[***3]** The fraud and conversion causes of action were properly dismissed as duplicative of the contract claim (*see* *Richbell Info. Servs. v Jupiter Partners, 309 AD2d 288,* 305, 765 NYS2d 575 [2003];*Coppola v Applied Elec. Corp., 288 AD2d 41, 732 NYS2d 402 [2001])*. The unjust enrichment cause of action was properly dismissed for failure to identify any improper benefit bestowed on Euro-American Lodging, Elias or Gama Lodging *(Prospect Plaza Tenant Assn. v New York City Hous. Auth., 11 AD3d 400, 401, 783 NYS2d 563 [2004]*; *Stephen Pevner, Inc.v Ensler, 309 AD2d 722, 723, 766 NYS2d 183 [2003]*; cf. *Korff v Corbett, 18 AD3d 248, 251, 794 NYS2d 374 [2005])*. Plaintiff's argument on this issue is not based on allegations in the complaint or inferences to be fairly drawn therefrom.

The court properly recognized the judgment of the French intermediate appellate court in reasoning that a "ministerial" action pursuant to *CPLR 5303* (*see CIBC Mellon Trust Co. v Mora Hotel Corp. 100 NY2d 215, 222, 792 NE2d 155, 762 NYS2d 5 [2003]*, *cert denied 540 US 948, 124 S Ct 399, 157 L Ed 2d 279 [2003])* does not seek independent relief and does not constitute the type of "vexatious" or "duplicative" litigation that *RPAPL 1301* intends to proscribe during the pendency of a foreclosure proceeding (*see Central Trust Co. v Dann, 85 NY2d 767, 771-772, 651 NE2d 1278, 628 NYS2d 259 [1995])*; **[***4]** indeed, most of the litigation involving the underlying debt in this instance had already taken place. The report of the Special Referee regarding the interest penalty surcharge was properly confirmed as substantially supported by the record (*see Salomon v Angsten, 19 AD3d 143, 797 NYS2d 14 [2005])*, consisting of testimony that it was unlikely the French court would grant relief from the surcharge where a corporate debtor in economic distress, such as defendant borrower herein, would probably **[*423]** never be able to repay the debt. The court properly exercised its discretion in denying the requested stay pending the final outcome of the French appeal, which had been dismissed but was subject to reinstatement, and an application to a European human rights body, as there was no showing of merit to the appeal (*see 64 B Venture v American Realty Co., 179 AD2d 374, 375-376, 579 NYS2d 1 [1992]*, *lv denied 79 NY2d 757, 592 NE2d 801, 583 NYS2d 193 [1992])*. Our ruling is without prejudice to defendant borrower's application, in whatever forum appropriate, to reduce the judgment and the interest calculated thereon in light of a recent reduction of the principal amount of the French judgment **[**612]** based on a showing that a portion of it is duplicative.

[**3]** We have **[***5]** considered appellants' other contentions and find them unavailing. Concur--Saxe, J.P., Nardelli, Williams, Catterson and Malone, JJ.

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Chi. Truck Drivers, Helpers & Warehouse Workers Union (Indep.) Health & Welfare Fund v. Local 710, Int'l Bhd. of Teamsters

United States District Court for the Northern District of Illinois, Eastern Division

March 4, 2005, Decided ; March 4, 2005, Filed

02 C 3115

Reporter

2005 U.S. Dist. LEXIS 42877 *

CHICAGO TRUCK DRIVERS, HELPERS AND WAREHOUSE WORKERS UNION (INDEPENDENT) HEALTH AND WELFARE FUND, Plaintiff, v. LOCAL 710, INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHICAGO TRUCK DRIVERS, HELPER AND WAREHOUSE WORKERS UNION (INDEPENDENT) PENSION FUND, Defendants.

Prior History: *Chi. Truck Drivers, Helpers & Warehouse Union (Indep.) Health & Welfare Fund v. Local 710, Int'l Bhd. of Teamsters, 2004 U.S. Dist. LEXIS 4657 (N.D. Ill., Mar. 19, 2004)*

Counsel: **[*1]** For Chicago Truck Drivers, Helpers and Warehouse Workers Union (Independent) Health and Welfare Fund, Plaintiff: Michael Joseph Kralovec, Joseph R. Lemersal, Sara R. McClain, Nash, Lalich & Kralovec, Chicago, IL.

For Local 710 International Brotherhood of Teamsters, successor Chicago Truck Drivers, Helpers and Warehouse Workers Union, Defendant: Marvin Gittler, Stephen Jay Feinberg, Asher, Gittler, Greenfield, Cohen & D'Alba, Chicago, IL.

For Chicago Truck Drivers, Helpers and Warehouse Workers Union (Independent) Pension Fund, Defendant: David George Huffman-Gottschling, Joseph M. Burns, Sherrie E. Voyles, Jacobs, Burns, Orlove, Stanton & Hernandez, Chicago, IL.

Judges: HONORABLE RONALD A. GUZMAN, United States Judge.

Opinion by: RONALD A. GUZMAN

Opinion

MEMORANDUM OPINION AND ORDER

Judge Ronald A. Guzman

Chicago Truck Drivers, Helpers and Warehouse Workers Union (Independent) Health and Welfare Fund ("Health and Welfare Fund") seeks a declaratory judgment against Local 710, International Brotherhood of Teamsters ("Local 710") and Chicago Truck Drivers, Helpers and Warehouse Workers Union (Independent) Pension Fund ("Pension Fund") that the demutualization compensation **[*2]** for four employee-benefit plans of Principal Financial Group ("Principal") is a plan asset and should revert to the participants of the plans. Before the Court is the Health and Welfare Fund's motion for summary judgment and Local 710's motion for partial summary judgment. For the reasons provided in this Memorandum Opinion and Order, the Court grants in part and denies in part both motions.

FACTS

This controversy stems from Principal's conversion from a mutual insurance company into a public stock company, a process known as a "demutualization." Principal adopted its plan for demutualization on March 31, 2001. (Pl.'s LR 56.1(a)(3) P 27.) When a mutual insurance company undergoes a demutualization, eligible policyholders receive compensation. (*See* Local 710's LR 56.1(a)(3) P 2; Local 710's Ex. 1, Letter from Principal to Policyholders of 10/26/01.) This compensation is given because policyholders lose ownership interests in the mutual insurance company when it becomes a stock company. (Local 710's Ex. 1, Letter from Principal to Policyholders of 10/26/01.) In the instant case, the Health and Welfare Fund received compensation from Principal for four different employee **[*3]** benefit plans: an in-house pension plan, a severance plan, a life insurance plan, and a 401(k) plan. The Health and Welfare Fund now seeks a declaratory judgment as to whom is entitled to the demutualization compensation. The issues in this case are whether the demutualization compensation is an asset of the plans, and, if so, whether the compensation reverts to the participants of the plan or to the employers.

Local 710 is a local union affiliated with the International Brotherhood of Teamsters. (Pl.'s LR 56.1(a)(3) P 5.) The Chicago Truck Drivers, Helpers and Workers Union Independent (the "CTDU") merged into Local 710 on February 1, 2001. (*Id.* P 7.) The CTDU was an independent labor union representing employees in the trucking, warehousing, and related industries in and around the Chicago area. (*Id.* P 6.) After the merger, the CTDU ceased operation as a labor organization, and Local 710 is a successor to the rights and liabilities of the CTDU. (*Id.* PP 12-13.) The Health and Welfare Fund and Pension Fund were established by the CTDU for the benefit of CTDU members covered by collective bargaining agreements with participating employers. (*Id.*)

The first of the benefit **[*4]** plans at issue in this case, a retirement plan for their office employees (the "in-house pension plan"), was established by the Health and Welfare Fund, the Pension Fund, and the CTDU in 1961. (*Id.* P 14.) This plan was funded through a group annuity contract with Bankers Life and Casualty and later Principal. (*Id.*) It was funded by contributions from the Health and Welfare Fund, the Pension Fund, and the CTDU on behalf of their employees. (*Id.* P 15.) The plan was terminated in 1987. (*Id.* P 16.) When the plan was terminated, all active employees who would have been eligible for a benefit received a lump sum payment, while former employees who had retired and were receiving benefits continued to receive a defined monthly benefit through a group annuity contract with Principal. (*Id.* PP 17-18.) This contract was fully funded at the time of the discontinuation of the plan. (Pl.'s Ex. 3, Boudreau Aff. P 20.) The Health and Welfare Fund received a check from Principal in the amount of $ 1,200,280.00 as demutualization compensation in connection with the in-house pension plan. (Pl.'s LR 56.1(a)(3) P 31.)

The supplemental retirement and security plan ("severance plan") **[*5]** was established in 1969. (*Id.* P 22.) Like the in-house pension plan, the severance plan is funded by an annuity contract with Principal. (*Id.* P 23.) The severance plan is currently in effect for employees of the Health and Welfare Fund and the Pension Fund, but employees of the CTDU left the severance plan and received their benefit payments on or before the CTDU and Local 710 merged. (Pl.'s Ex. 3, Boudreau Aff. PP 26-27.) The Health and Welfare Fund received a check from Principal in the amount of $ 78,329.00 as demutualization compensation in connection with the severance plan. (Pl.'s LR 56.1(a)(3) P 30.)

The employees' savings plan ("401(k) plan") was established in July, 1983. (*Id.* P 20.) This plan is a voluntary program for employees and is funded by contributions by the employees. (*Id.* P 21.) The 401(k) plan is in effect for the employees of all three parties in this case - the Health and Welfare Fund, Pension Fund, and Local 710. (Pl.'s Ex. 3, Boudreau Aff. P 32.) The Health and Welfare Fund received a check from Principal in the amount of $ 85,766.00 as demutualization compensation in connection with the 401 (k) plan. (Pl.'s LR56.1(a)(3) P 31.)

Finally, the **[*6]** member life, accidental death, and dismemberment policy (the "life insurance plan") was established in February 1992. (*Id.* P 24; Pension Fund's Ex. F, U.S. Dep't of Labor's Pension & Welfare Benefits Admin. Office of Regs. & Interpretations Advisory Op. 94-31 A.) This plan was funded by contributions from the Health and Welfare Fund, the Pension Fund, and the CTDU on behalf of their respective employees. The benefits of this plan are paid through a group policy with Principal. (Pl.'s LR 56.1(a)(3) P 26.) Employees of the Health and Welfare Fund and the Pension Fund currently participate in the plan, but the CTDU ceased participation in the life insurance plan upon its merger with Local 710. (Pl.'s Ex. 3, Boudreau Aff. P 35.) The Health and Welfare Fund received 541 shares of Principal common stock as demutualization compensation in connection with the life insurance plan. (Pl.'s LR 56.1(a)(3) P 32.)

Local 710 argues that the compensation from the demutualization reverts to the employers -- the Health and Welfare Fund, the Pension Fund, and Local 710 as successor to the CTDU, with the exception of the 401(k) plan. (*Id.* P 34.) The Health and Welfare Fund, on the other hand, **[*7]** argues that the demutualization compensation should be used for the benefit of the participants of the various plans. (*Id.* P 35.) The Health and Welfare Fund brought suit, seeking a declaratory judgment of the rights of the parties to the demutualization compensation. (Compl. P 32.) Before the Court is the Health and Welfare Fund's motion for summary judgment seeking a declaratory judgment that the demutualization compensation is a plan asset to be used for the benefit of the participants of the plans and Local 710's motion for partial summary judgment, seeking a declaration that the demutualization compensation reverts to the employers.

DISCUSSION

Pursuant to *Federal Rule of Civil Procedure 56(c)*, the court may grant summary judgment "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." *FED. R. CIV. P. 56(c)*. When considering the evidence submitted by the parties, the court does not weigh **[*8]** it or determine the truth of asserted matters. *Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 249, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986)*. All facts must be viewed and all reasonable inferences drawn in the light most favorable to the non-moving party. *NLFC, Inc. v. Devcom Mid-America, Inc., 45 F.3d 231, 234 (7th Cir. 1995)*. "If no reasonable jury could find for the party opposing the motion, it must be granted." *Hedberg v. Ind. Bell Tel. Co., Inc., 47 F.3d 928, 931 (7th Cir. 1995)*.

Summary judgment is appropriate in this case because there are no material facts in dispute. Therefore, the movants are entitled to a judgment as a matter of law.

The first issue is whether the demutualization compensation is a plan asset of the various plans. ERISA does not define plan assets. *See Bannistor v. Ullman, 287 F.3d 394, 402 (5th Cir. 2002)*. The U.S. Department of Labor has issued advisory opinions that address the issue of whether the demutualization compensation is a plan asset. (Pension Fund's Ex. A, U.S. Dep't of Labor's Pension & Welfare Benefits Admin. Office of Regulations & Interpretations Advisory Op. 92-02A (2002); Pl.'s Ex. 5, EBSA Advisory Op. **[*9]** 2001-02A n.1 (2001).) "[I]f the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute." *Mead Corp. v. B.E. Tilley, 490 U.S. 714, 722, 109 S. Ct. 2156, 104 L. Ed. 2d 796 (1989)*. An agency's advisory opinions are not binding authority, but they are "entitled to deference, such that the interpretation will be upheld so long as it is reasonable." *Reich v. McManus, 883 F. Supp. 1144, 1153 (N.D. Ill. 1995)*. "[A] court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency." *Chevron U.S.A. v. Natural Resources Defense Council, Inc., 467 U.S. 837, 844, 104 S. Ct. 2778, 81 L. Ed. 2d 694 (1984)*.

According to the Department of Labor:

> The proceeds of the demutualization will belong to the plan if they would be deemed to be owned by the plan under ordinary notions of property rights. . . . In the case of an employee pension benefit plan, or where any type of plan or trust is the policyholder, or where the policy is paid for out of trust assets, it is the view of the department that all of the proceeds **[*10]** received by the policyholder in connection with a demutualization would constitute plan assets.

(Pl.'s Ex. 5, EBSA Advisory Op. 2001-02A n.I (2001).) Determining whether the demutualization compensation consists of a plan asset under ordinary notions of property rights requires "consideration of any contract or other legal instrument involving the plan documents. It also requires the consideration of the actions and representations of the parties involved." (Pension Fund's Ex. A, U.S. Dep't of Labor's Pension & Welfare Benefits Admin. Office of Regulations & Interpretations Advisory Op. 92-02A (2002).)

In *Ruocco v. Bateman, Eichler, Hill, Richards, Inc., 903 F.2d 1232 (9th Cir. 1990)*, the Ninth Circuit Court of Appeals considered the issue of whether stock issued as demutualization compensation for a long-term disability insurance plan could revert to an employer. This plan was wholly funded by contributions from the participants of the plan. *Id. at 1238*. The court held that allowing the compensation to revert to the employers would give the employers an undeserved windfall. *Id.* As a result, the "balancing of equities" weighed in favor **[*11]** of allowing the demutualization compensation to revert to the employees. *Id.*

Like the disability plan in *Ruocco*, the contributions to the 401(k) plan in this case were made entirely by the employees, outside of minor administrative costs. Therefore, the demutualization compensation should revert to the employees. This conclusion was undisputed and is now stipulated by the parties. (*See* Pension Fund's Resp. Pl.'s Mot. Summ. J. at 11-12; Local 710 Mem. Opp'n Pl.'s Mot. Summ. J. at 14; Joint Mot. Partial Dismissal & Release of Funds P 4.) Moreover, like the plan in *Ruocco*, the 401(k) plan in this case is an employee pension benefit plan wholly funded by the participants of the plan. Because the plan was fully funded by the employees, they are entitled to the compensation as a result of their loss of ownership in Principal. As in *Ruocco*, awarding this compensation to the employers would give them an undeserved windfall -- they would be receiving money as a result of the investment of the participants of the plans, not their own efforts. Accordingly, the demutualization compensation attributable to the 401(k) plan reverts to the employees.

Determining whether the demutualization **[*12]** compensation is a plan asset for the remaining plans is a closer issue. Following the guidelines of the EBSA, this Court will follow ordinary notions of property rights and look to the plan documents and representations by the parties to determine whether the demutualization compensation is a plan asset. There is no evidence that the parties made any representations other than in the plan documents as to whether or not the demutualization compensation is a plan asset. Therefore, this Court will focus on the language of the plans to determine this issue.

After examining the plan documents, this Court holds that the demutualization compensation is a plan asset for the in-house pension plan and the severance plan, but not for the insurance plan. At first blush, the compensation would appear not to be a plan asset for any of the remaining plans because it is undisputed that these plans were funded by the employers. Determining that the compensation reverts to the plans and not the employers could therefore result in an undeserved windfall to the plans. However, both the in-house pension plan and severance plan are "employee pension benefit plans." As a result, the compensation would be **[*13]** presumed to be a plan asset under the EBSA Advisory Opinion unless language in the plan documentation suggests otherwise.

In interpreting the language of a contract, a court's primary purpose is to discern the intent of the parties. *See* *Volt Information Sciences v. Board of Trustees, 489 U.S. 468, 488, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989)*. In this case, however, neither the in-house pension plan nor the severance plan specifically addresses the issue of demutualization compensation. The demutualization compensation would therefore be presumed to be a plan asset under the EBSA Advisory Opinion 2001-02A quoted above. The plans do address the issue of whether any dividends awarded under the plans would revert to the employers or become plan assets. Both plans declare that "[d]ividends declared under the Group Contract and forfeitures shall be applied to reduce future Employer Contributions." (Pl.'s Ex. B, Health & Welfare Fund & Pension Fund Employees Retirement Plan at 21, Pl.'s Ex. D, Health & Welfare Fund & Pension Fund Employees Restated Supplemental Retirement & Security Plan at 22.) This language suggests that the dividends would become plan assets used to pay for the **[*14]** plans, rather than simply reverting to the employers to be used however they wish. Like dividends, the demutualization compensation at issue in this case comes from Principal. The language in the plans regarding dividends shows that the parties intended future compensation from Principal to become a plan asset. Although the language of the plans with regard to the disposition of dividends alone is not determinative, coupled with the EBSA's view that demutualization compensation ordinarily becomes a plan asset for an employee pension plan, it is sufficient to convince the Court that the demutualization compensation is a plan asset for the in-house pension plan and the severance plan.

Local 710 argues that the language in the plans regarding dividends should not affect the outcome of this case because demutualization compensation is not a dividend. (Local 710's Mem. Opp'n Pl.'s Mot. Summ. J. at 10.) It is true that the demutualization compensation is not a dividend, but it is awarded to policyholders in exchange for loss of ownership interests in the company. Dividends are payments by a company to its stockholders. RICHARD A. BREALEY & STEWART C. MYERS, PRINCIPALS OF CORPORATE FINANCE **[*15]** 64 (5th ed. 1996). When a mutual insurance company demutualizes, it compensates policyholders for the loss of their ownership interests, which therefore includes their ability to receive dividends. *See id.* at 417-38.

Local 710 points out that Principal "will continue to pay policy dividends as declared." (Pl.'s Ex. K, Plan of Conversion of Principal Mut. Holding Co. at A-3.) However, this language only means that Principal will continue to pay *declared* dividends. It does not mean that Principal can award new dividends in the future. In addition, there is no evidence that Principal has awarded dividends for any of the plans at issue in this case. Therefore, the fact that demutualization compensation is not a dividend is insufficient to overcome the strong presumption that it is a plan asset given the specific facts of this case.

Although the demutualization compensation is a plan asset for the in-house pension plan and severance plan, this does not necessarily mean that it reverts to the participants of the plans. The plans state: "No part of the plan assets shall be paid to the Employer at any time, except that, after the satisfaction of all liabilities under the Plan, any **[*16]** assets remaining will be paid to the Employer. The payment may not be made if it would contravene any provision of law." (Pl.'s Ex. B, Health &

Welfare Fund & Pension Fund Employees Retirement Plan at 47; Pl.'s Ex. D, Health & Welfare Fund & Pension Fund Employees Restated Supplemental Retirement & Security Plan at 56.) Under the terms of the plans, therefore, the demutualization compensation, as a plan asset, may be distributed to the employers if the plan has satisfied all of its liabilities.

Because the in-house pension plan has been terminated, it has satisfied all of its liabilities to the participants and their beneficiaries. The Pension Fund argues that since former employees are continuing to receive benefits under this plan, the plan has not satisfied all of its liabilities. (Pension Fund's Resp. Mot. Summ. J. at 13;) However, it is undisputed that these participants are receiving their benefits under a plan that was fully funded at the time of the termination of the in-house pension plan. Therefore, the in-house pension plan has no "liabilities" and the demutualization compensation reverts to the contributing employers -- the Health and Welfare Fund, the Pension Fund, **[*17]** and Local 710 as successor to the CTDU.

The plan provides that residual assets may be distributed to an employer so long as no provision of law is violated. ERISA addresses the issue of whether residual assets may be distributed to an employer:

(d) Distribution of residual assets. . . .

> (1) Subject to paragraph (3), any residual assets of a single-employer plan may be distributed to the employer if-
>
> > (A) all liabilities of the plan to participants and their beneficiaries have been satisfied,
> >
> > (B) the distribution does not contravene any provision of law, and
> >
> > (C) the plan provides for such a distribution in these circumstances.
>
> (3)(A) Before any distribution from a plan pursuant to paragraph (1), if any assets of the plan attributable to employee contributions remain after satisfaction of all liabilities . . . such remaining assets shall be equitably distributed to the participants who made such contributions or their beneficiaries.

29 U.S.C. § 1344 (2003). The in-house pension plan satisfies all of these requirements. As noted above, all liabilities of the plan have been satisfied and the plan provides for a distribution of **[*18]** the assets to the employers. In addition, no provision of law has been violated, and the Health and Welfare Fund does not cite to any law that would be violated by distributing the compensation to the employers. Finally, it is undisputed that the employers were responsible for the contributions to the plans, not the employees. Therefore, no equitable distribution to the participants need be made.

The Health and Welfare Fund argues that the compensation cannot be distributed to three employers, *i.e.*, the Health and Welfare Fund, the Pension Fund, and Local 710, because the language of the statute is in the singular. The statute provides "any residual assets of a single-plan may be distributed to *the* employer. . . ." 29 U.S.C. § 1344(d) (emphasis added). The Court is not persuaded that this language prevents the compensation from being distributed to three employers when all three employers have made contributions to the plan. This is especially true because, as the Health and Welfare Fund points out, the plans at issue in this case are single-employer plans despite the fact that multiple employers fund the plans. (*See* Mem. Supp. Mot. Summ. J. at **[*19]** 7.) The Court therefore holds that the demutualization compensation for the in-house pension plan reverts to the three employers that are parties in this case -- the Health and Welfare Fund, the Pension Fund, and Local 710.

Unlike the in-house pension plan, the severance plan has not been terminated and is currently in full force and effect for employees of the Health and Welfare Fund and the Pension Fund. Because the plan provides that the assets of the plan shall not be distributed to the employers until after satisfaction of all liabilities of the plan, the demutualization compensation does not revert to the employers. The compensation should be used to reduce future contributions by the two remaining employers in the case - the Health and Welfare Fund and the Pension Fund. If at some point the Health and Welfare Fund and the Pension Fund satisfy all of their liabilities under the plan, Local 710 would then be entitled to a share of the demutualization compensation, using the same reasoning as applied to the in-house pension plan.

Unlike the in-house pension plan and the severance plan, the life insurance plan is not an employee pension plan. A "pension plan" is defined by ERISA **[*20]** as:

> any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program --
>
> (i) provides retirement income to employees, or

> (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond. . . .

29 U.S.C. § 1002(2)(A). Unlike a pension plan, the life insurance plan fits under the ERISA definition of "an employee welfare benefit plan" because it provides "benefits in the event of . . . death. . . ." *29 U.S.C. § 1002(1)(A)*. The EBSA discussed the disposition of demutualization compensation for an employee welfare benefit plan in the Advisory Opinion 2001-02A, which states:

> [I]n the case of an employee welfare benefit plan . . . the appropriate plan fiduciary must treat as plan assets the portion of the demutualization proceeds attributable to participant contributions. . . . [and] the plan fiduciary should give appropriate consideration to those facts and circumstances **[*21]** that the fiduciary knows or should know are relevant to the determination, including the documents and instruments governing the plan. . . .

(Pl.'s Ex. 5, EBSA Advisory Op. 2001-02A at n.2.)

In this case, it is undisputed that the employers made all of the contributions to the plans. Therefore, there is no reason to treat any portion of the demutualization compensation as a plan asset. In addition, there is nothing in the language of the plan to suggest that the parties intended demutualization compensation to become a plan asset. Unlike the in-house pension plan and the severance plan, there is no language in the life insurance plan regarding dividends. The plan is silent with respect to possible assets such as dividends or demutualization compensation. *As* a result, the employers have made no representations suggesting that demutualization compensation would be a plan asset in the language of the plans. Therefore, the Court holds that the demutualization compensation is not a plan asset for the life insurance plan and that it reverts to the Health and Welfare Fund, the Pension Fund, and Local 710.

The Pension Fund argues that Local 710 is not entitled to any of the demutualization **[*22]** compensation for the life insurance plan because Local 710 has not contributed to the plan. (Pension Fund's Resp. Pl.'s Mot Summ. J. at 11.) It is undisputed that the CTDU made contributions to the life insurance plan, however, and it is also undisputed that Local 710 is a successor to all the rights and liabilities of the CTDU. Therefore, Local 710 is entitled to a share of the demutualization compensation attributable to the contributions made by the CTDU.

CONCLUSION

For the reasons provided in this Memorandum, the Court grants in part and denies in part the Health and Welfare Fund's Motion for Summary Judgment [doc. no. 12-1] and Local 710's Motion for Partial Summary Judgment [doc. no. 19-1]. The Court enters a declaratory judgment that: (1) the demutualization compensation attributable to the 401(k) plan reverts to the participants of the plan as stipulated in the Joint Motion for Partial Dismissal and Release of Funds; (2) the demutualization compensation attributable to the severance plan must be used to offset future employer contributions; and (3) the demutualization compensation attributable to the in-house pension plan and life insurance plan reverts to the **[*23]** employers. This case is hereby terminated.

SO ORDERED

ENTERED: March 4, 2005

HON. RONALD A. GUZMAN

United States Judge

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Clark v. Daby

Supreme Court of New York, Appellate Division, Third Department

December 5, 2002, Decided ; December 5, 2002, Entered

92121

Reporter

300 A.D.2d 732 *; 751 N.Y.S.2d 622 **; 2002 N.Y. App. Div. LEXIS 11598 ***

REGINALD CLARK et al., Appellants, v KIMBALL W. DABY, Respondent.

Subsequent History: [*1]**

Appeal denied by Clark v. Daby, 2003 N.Y. LEXIS 1286 (N.Y., May 13, 2003)

Prior History: Clark v. Daby, 225 A.D.2d 974, 639 N.Y.S.2d 549, 1996 N.Y. App. Div. LEXIS 2773 (N.Y. App. Div. 3d Dep't, 1996)

Disposition: Order affirmed, with costs.

Counsel: Dennin & Dennin, Lake Placid (Gregory M. Dennin of counsel), for appellants.

James M. Brooks, Lake Placid, for respondent.

Judges: Before: Cardona, P.J., Mercure, Spain, Lahtinen and Kane, JJ. Cardona, P.J., Spain, Lahtinen and Kane, JJ., concur.

Opinion by: Mercure

Opinion

[*732] [623]** MEMORANDUM AND ORDER

Mercure, J.

Appeal from an order of the Supreme Court (Dawson, J.), entered September 28, 2001 in Essex County, which, inter alia, granted defendant's motion for summary judgment dismissing the complaint.

In 1980, defendant executed in favor of plaintiffs his bond and mortgage securing real property located in the Village of Lake Placid, Essex County. Plaintiffs subsequently brought an action to foreclose the mortgage, defendant successfully interposed the defense of usury, and Supreme Court (Viscardi, J.) entered an order in favor of defendant determining that the bond and mortgage were null and void and canceling and discharging the mortgage of record. On appeal, this Court affirmed (Clark v Daby, 225 A.D.2d 974, 639 N.Y.S.2d 549, **[***2]** *lv denied 88 N.Y.2d 816, 651 N.Y.S.2d 406, 674 N.E.2d 336*). During the pendency of plaintiffs' subsequent applications to this Court and the Court of Appeals for leave to appeal to the Court of Appeals, they elected to pay $ 10,786.77 in order to redeem the property from an impending tax sale by the Essex County Treasurer. Following the denial of plaintiffs' applications for leave to appeal, plaintiffs brought the present action seeking to recover the moneys paid to the County Treasurer on a theory of unjust enrichment. Following joinder of issue, plaintiffs moved and defendant cross-moved for, as here relevant, summary judgment. Supreme Court granted summary judgment in favor of defendant and dismissed the complaint. Plaintiffs appeal.

We affirm. "To prevail on a claim of unjust enrichment, [a] plaintiff must show that (1) defendant was enriched (2) at plaintiff's expense, and (3) that 'it is against equity and good conscience to permit * * * defendant to retain what is sought to be recovered'" (*Lake Minnewaska Mtn. Houses v Rekis, 259 A.D.2d 797, 798, 686 N.Y.S.2d 186*, quoting Paramount Film Distrib. Corp. v State of New York, 30 N.Y.2d 415, 421, 334 N.Y.S.2d 388, 285 N.E.2d 695, **[***3]** *cert denied 414 U.S. 829, 38 L. Ed. 2d 64, 94 S. Ct. 57*). Notably, it is the plaintiff's burden to "demonstrate that services were performed *for the defendant* resulting in [the latter's] unjust enrichment" (Kagan v K-Tel Entertainment, 172 A.D.2d 375, 376, 568 N.Y.S.2d 756 [emphasis in original]), and the mere fact that the plaintiff's activities bestowed a benefit on the defendant is insufficient to establish a cause of action for unjust enrichment (*see id.*; *see also* Wiener v Lazard Freres & Co., 241 A.D.2d 114, 120, 672 N.Y.S.2d 8). "Generally, courts will look to see if a benefit has been conferred on the defendant under mistake of fact or **[**624]** law, if the benefit still remains with the defendant, if there has been otherwise a change of position by the defendant, and whether the defendant's conduct was tortious or fraudulent" (

*Paramount **[*733]** Film Distrib. Corp. v State of New York, supra at 421* [citation omitted]).

Although there can be no question that plaintiffs' payment of real property taxes on the property worked to defendant's benefit by relieving him of that burden, it is equally clear that plaintiffs **[***4]** operated under no mistake of fact or law but, rather, their sole motivation in making the payment was to protect their own interests. As stated in an affidavit of plaintiffs' attorney:

> "If the taxes had not been paid, the County would have taken title to the property cutting off plaintiffs' interest in the property. Plaintiffs had to pay the taxes to protect themselves in the event of a reversal on appeal. There is no other logical reason for plaintiffs paying the taxes."

The fact that plaintiffs' calculated risk failed makes their conduct no less voluntary, and there is no evidence or claim that defendant's conduct with regard to this matter was in any way tortious or fraudulent. Under all the circumstances, we agree with Supreme Court's conclusion that any benefit to defendant was purely incidental, thereby defeating plaintiffs' claim of unjust enrichment. The parties' additional contentions have been considered and found to be unavailing.

Cardona, P.J., Spain, Lahtinen and Kane, JJ., concur.

ORDERED that the order is affirmed, with costs.

Cleghorn v. Blue Shield

United States Court of Appeals for the Ninth Circuit

February 10, 2005, Argued and Submitted, Pasadena, California ; May 23, 2005, Filed

No. 03-55528

Reporter

408 F.3d 1222 *; 2005 U.S. App. LEXIS 9348 **; 34 Employee Benefits Cas. (BNA) 2898

DOUGLAS D. CLEGHORN, individually, on behalf of other similarly-situated persons and on behalf of the public, Plaintiff-Appellant, v. BLUE SHIELD OF CALIFORNIA, dba CareAmerica, Defendant-Appellee.

Prior History: [1]** Appeal from the United States District Court for the Central District of California. D.C. No. CV-02-00852-DOC. David O. Carter, District Judge, Presiding.

Cleghorn v. Blue Shield of Cal., 2003 U.S. Dist. LEXIS 26861 (C.D. Cal., Feb. 18, 2003)

Disposition: AFFIRMED.

Counsel: Sharon J. Arkin, Robinson, Calcagnie & Robinson, Newport Beach, California, for the plaintiff-appellant.

Gregory N. Pimstone, Terri D. Keville, Manatt, Phelps & Phillips, LLP, Los Angeles, California, for the defendant-appellee.

Judges: Before: Harry Pregerson, William C. Canby, Jr., and Richard C. Tallman, Circuit Judges. Opinion by Judge Canby.

Opinion by: William C. Canby, Jr.

Opinion

[*1223] CANBY, Circuit Judge:

We are presented once again with a question concerning the degree to which the federal Employee Retirement Income Security Act ("ERISA") preempts state law. Douglas D. Cleghorn is a participant in his employer's ERISA health plan offered by Blue Shield of California (doing business as Care-America) ("Blue Shield"). On one occasion he sought and received emergency medical services and Blue Shield denied reimbursement. Cleghorn sued Blue Shield in California state court, asserting state-law causes of action and alleging that Blue Shield had violated an emergency care provision in section 1371.4(c) of the California Health and Safety Code **[**2]** .

[*1224] Blue Shield removed the case to federal court and the district court held that Cleghorn's claims were preempted by ERISA. When Cleghorn declined to amend his complaint to allege an ERISA claim, the district court dismissed his complaint for failure to state a claim. We affirm the judgment of the district court.

I. Background

Through his employer, Cleghorn became a member of a Blue Shield health plan. [1] He subsequently sought and received emergency medical care for an episode of dizziness, imminent loss of consciousness, weakness, muscle fatigue, and nausea. Cleghorn submitted a reimbursement claim to Blue Shield for the emergency care he received.

Blue **[**3]** Shield denied Cleghorn's claim on two grounds based on the terms of the plan: (1) Cleghorn's condition did not meet the criteria for emergency care; [2] and (2) the emergency treatment was not approved by Cleghorn's primary care physician or by the health plan. [3] Cleghorn filed state law claims in Orange County

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[1] In reviewing the district court's dismissal of the complaint pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure, we accept for purposes of appeal the facts as alleged in Cleghorn's complaint. *See* Johnson v. California, 207 F.3d 650, 653 (9th Cir. 2000).

[2] Blue Shield's coverage plan provides that: "Emergency services . . . are covered only in a medical emergency . . . If emergency room or urgent care services are used for a condition which is not an emergency, the services are not covered and you will be liable for all charges."

[3] Blue Shield's plan provides that emergency care is covered "only if approved in advance by a [Blue Shield] physician."

Superior Court on behalf of himself, all others similarly situated, and the general public. The claims were brought under the Unfair Competition Law ("UCL"), CAL. BUS. & PROF. CODE § 17200, et seq., and the Consumer Legal Remedies Act ("CLRA"), CAL. CIV. CODE § 1750, et seq. Cleghorn requested general damages, injunctive relief, disgorgement of illegally-gained profits, and punitive damages.

[4]** All of the claims were based on Cleghorn's allegation that Blue Shield's emergency care policy violated section 1371.4(c) of the California Health and Safety Code:

> [A] health care service plan may deny reimbursement to a provider for a medical screening examination in cases when the plan enrollee did not require emergency services and care and the enrollee reasonably should have known that an emergency did not exist. A health care service plan may require prior authorization as a prerequisite for payment for necessary medical care following stabilization of an emergency medical condition.

Cleghorn asserted that this statute required Blue Shield to cover emergency treatment whenever the insured "reasonably believes that an emergency exists" and that a requirement of pre-authorization in such cases is forbidden. [4]

Blue Shield **[**5]** removed the action to federal court on the ground that Cleghorn's state-law causes of action were completely preempted by ERISA. *See* Aetna Health Inc. v. Davila, 542 U.S. 200, 124 S. Ct. 2488, 2494-96, 159 L. Ed. 2d 312 (2004) (upholding ERISA preemption as a ground for removal). Cleghorn then amended his complaint to delete his individual claims for damages under CLRA and filed a motion to remand. The district court denied Cleghorn's motion to remand, concluding that Cleghorn's claims were preempted. Cleghorn declined the opportunity to **[*1225]** amend his complaint to include claims under ERISA's civil enforcement scheme. The district court thereupon dismissed the complaint pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure for failure to state a cognizable cause of action.

II. Standard of Review

We review de novo a dismissal pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure. Madison v. Graham, 316 F.3d 867, 869 (9th Cir. 2002). We also determine de novo whether ERISA preempts state law causes of action. Winterrowd v. Am. Gen. Annuity Ins. Co., 321 F.3d 933, 937 (9th Cir. 2003). **[**6]**

III. Discussion

There are two strands to ERISA's powerful preemptive force. First, ERISA section 514(a) expressly preempts all state laws "insofar as they may now or hereafter relate to any employee benefit plan[,]" 29 U.S.C. § 1144(a), but state "law[s] . . . which regulate insurance, banking, or securities" are saved from this preemption. 29 U.S.C. § 1144(b)(2)(A).

Second, ERISA section 502(a) contains a comprehensive scheme of civil remedies to enforce ERISA's provisions. *See* 29 U.S.C. § 1132(a). A state cause of action that would fall within the scope of this scheme of remedies is preempted as conflicting with the intended exclusivity of the ERISA remedial scheme, even if those causes of action would not necessarily be preempted by section 514(a). *See* Davila, 124 S. Ct. at 2498 n.4. It is this second strand of ERISA's preemptive force that precludes Cleghorn's action.

Section 502(a) of ERISA provides, among other things, that "[a] civil action may be brought . . . by a participant or beneficiary . . . to recover benefits due to him under the terms of his plan. . . ." 29 U.S.C. § 1132(a) **[**7]** . When Cleghorn sought benefits under the plan and did not receive them, he did not pursue his ERISA remedy but instead brought the present state-law claims. These are precisely the kind of claims that the Supreme Court in *Davila* held to be preempted. In *Davila*, the plaintiffs were denied coverage or reimbursement for certain medical services by their ERISA plan administrators. They similarly declined to pursue their ERISA remedies and instead brought state tort claims to enforce duties of care imposed by state statutes. *See* Davila, 124 S. Ct. at 2499. The Supreme Court held that the state causes of action were pre-empted even though: (1) they were tort claims (unlike ERISA claims), (2) they were based on an external state statutory duty, and (3) they did not duplicate ERISA remedies. *See* id. at 2498-99. As the Court summarized: "Congress' intent to make the ERISA civil enforcement mechanism exclusive would be undermined if state causes of action that supplement the ERISA § 502(a) remedies were permitted, even if

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[4] Blue Shield contests Cleghorn's interpretation of section 1371.4(c), but our disposition of the preemption issue makes it unnecessary for us to resolve that dispute.

the elements of the state cause of action did not precisely duplicate the elements of an ERISA claim." *Id. at 2499-2500*; *see also* *Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41, 54, 95 L. Ed. 2d 39, 107 S. Ct. 1549 (1987)* **[**8]** (noting that the "policy choices reflected in the inclusion of certain remedies and the exclusion of others under the federal scheme would be completely undermined if ERISA-plan participants and beneficiaries were free to obtain remedies under state law that Congress rejected in ERISA."); *Elliot v. Fortis Benefits Ins. Co., 337 F.3d 1138, 1147 (9th Cir. 2003)* (holding that an action "which seeks non-ERISA damages for what are essentially claim processing causes of action[] clearly falls under the *§ 1132* preemption exemplified by *Pilot Life*."); *Dishman v. UNUM Life Ins. Co., 269 F.3d 974, 983 (9th Cir. 2001)* (ruling that "claimants simply cannot obtain relief by dressing up an ERISA benefits claim in the garb of a state law tort.").

[*1226] Cleghorn argues that his claims no longer implicate ERISA because he amended his complaint to delete his individual claim. Artful pleading does not alter the potential for this suit to frustrate the objectives of ERISA. The only factual basis for relief pleaded in Cleghorn's complaint is the refusal of Blue Shield to reimburse him for the emergency medical care he received. Any duty or liability that Blue Shield **[**9]** had to reimburse him "would exist here only because of [Blue Shield's] administration of ERISA-regulated benefit plans." *Davila, 124 S. Ct. at 2498*. Even the class claim does not aid Cleghorn, for he is a participant in an ERISA plan and brings his action on behalf of others similarly situated. Cleghorn's claim therefore cannot be regarded as independent of ERISA.

The argument most forcefully urged by Cleghorn on appeal is that his suit is, at least in part, a pure citizen's action to enforce *section 1371.4(c) of the California Health and Safety Code*, which may apply across the board to all health providers, not just ERISA plans. Cleghorn contends that such a claim is not subject to preemption under our decision in *Washington Physicians Service Ass'n v. Gregoire, 147 F.3d 1039 (9th Cir. 1998)*. We reject both the argument and the applicability of *Washington Physicians Service.*

We have to deal with the complaint as it was when the district court dismissed it, not as it may be affected by concessions presented on appeal. As we have said, the factual basis of the complaint, even for the public claims, was the denial of reimbursement of plan benefits **[**10]** to Cleghorn. The relief sought on the claims most strongly argued to survive preemption included restitutionary relief, disgorgement of profits, injunctive and other equitable relief, and attorneys' fees. [5] On this record, the district court did not err in concluding that applying these remedies to Blue Shield conflicted with ERISA's exclusive enforcement scheme and that the state-law claims were therefore preempted.

Washington Physicians Service was a very different case from this one. There we dealt with a statute that required every health *carrier* to provide, in any plans it delivered or renewed, that services covered by the plan could be provided by every category of health care providers within their areas of competence (thus permitting coverage for services of "alternative" medical providers). *See* *id. at 1042*. A group of health maintenance organizations and health care service contractors sued to prevent application of the statute on the **[**11]** ground that it was preempted under the explicit preemption provision of *ERISA, section 514(a)*. We held that the statute did not "operate directly on" ERISA plans, but merely regulated "one of many products that an employee benefit plan might choose to buy." *Id. at 1044-45*. We therefore concluded that the statute did not "relate to" an ERISA plan within the meaning of *section 514(a)*. *Id. at 1045*.

We need not address whether California's different statute, as applicable to ERISA plans, operates directly on such plans and therefore "relates to" them, because we are not relying for our decision on preemption under *section 514(a)*. [6] **[*1227]** Whether or not *section 1371.4(c) of the California Health and Safety Code* may be applicable to ERISA plans, it may not be enforced against an ERISA plan by way of this lawsuit asserting state-law causes of action against Blue Shield because of its denial of ERISA plan benefits. Congress's exclusive and comprehensive civil enforcement scheme of *section 502* preempts any such state-law causes of action. *Washington Physicians Service* does not affect

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[5] A third claim sought punitive damages.

[6] For the same reason, we need not decide whether California's *section 1371.4(c)* is excepted from preemption under *section 514(b)(2)(A)* as a state regulation of insurance. *See* *Ky. Ass'n of Health Plans, Inc. v. Miller, 538 U.S. 329, 334, 155 L. Ed. 2d 468, 123 S. Ct. 1471 (2003)*. Preemption under *ERISA section 502(a)* is not affected by that exception. "Under ordinary principles of conflict preemption . . . even a state law that can arguably be characterized as 'regulating insurance' will be pre-empted if it provides a separate vehicle to assert a claim for benefits outside of, or in addition to, ERISA's remedial scheme." *Davila, 124 S. Ct. at 2500*.

this conclusion, because it did not involve an attempt to enforce state-law **[**12]** causes of action against ERISA plans or their administrators or fiduciaries. *Washington Physicians Service* accordingly did not deal with *section 502(a)* preemption at all.

IV. Conclusion

Cleghorn's state-law causes of action against Blue Shield, arising from Blue Shield's denial of benefits under an ERISA plan, conflict with the exclusive **[**13]** civil enforcement scheme established by Congress in *section 502(a) of ERISA.* The state law claims are preempted for that reason. We accordingly affirm the judgment of the district court dismissing Cleghorn's complaint.

AFFIRMED.

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Clifford R. Gray, Inc. v. LeChase Constr. Servs., LLC

Supreme Court of New York, Appellate Division, Third Department

July 20, 2006, Decided; July 20, 2006, Entered

500048, 500049

Reporter

31 A.D.3d 983 *; 819 N.Y.S.2d 182 **; 2006 N.Y. App. Div. LEXIS 9478 ***; 2006 NY Slip Op 5850 ****

[**1]** Clifford R. Gray, Inc., Respondent-Appellant, v LeChase Construction Services, LLC, et al., Appellants-Respondents.

Subsequent History: **[***1]**

Subsequent appeal at *Clifford R. Gray, Inc. v. LeChase Constr. Services, 2008 N.Y. App. Div. LEXIS 4021 (N.Y. App. Div. 3d Dep't, May 8, 2008)*

Counsel: Davidson, Fink, Cook, Kelly & Galbraith, L.L.P., Rochester (Fernando Santiago of counsel), for appellants-respondents.

McNamee, Lochner, Titus & Williams, P.C., Albany (Christopher Massaroni of counsel), for respondent-appellant.

Judges: Before: Crew III, J.P., Peters, Spain, Lahtinen and Kane, JJ. Crew III, J.P., Peters, Lahtinen and Kane, JJ., concur.

Opinion by: Spain

Opinion

[*983] **[**183]** Spain, J. Cross appeals (1) from an order of the Supreme Court (Kramer, J.), entered October 24, 2005 in Schenectady County which, inter alia, partially denied defendants' motion to compel disclosure, and (2) from an order of said court, entered January 26, 2006 in Schenectady County, which, inter alia, denied defendants' motion for summary judgment dismissing the complaint.

Plaintiff is an electrical and communications contractor that has provided services to the Knolls Atomic Power Laboratory (hereinafter KAPL) for more than 40 years. Defendants are affiliated business entities **[***2]** from the City of Rochester, Monroe County, that were seeking to win a **[**184]** contract for the design and **[*984]** construction of a building in the Town of Niskayuna, Schenectady County (hereinafter the project). After attending a meeting about the project, defendants learned of plaintiff's relationship with KAPL and the parties began to discuss plaintiff's potential involvement in the project. Plaintiff alleges that in September 2001, the parties reached an agreement, which plaintiff denominates an "exclusivity agreement." Pursuant thereto, plaintiff agreed to the following three conditions: (1) to refrain from participating with any other general contractors who were seeking the KAPL contract; (2) to refrain from sharing with any third party **[****2]** any documentation or drawings provided by defendants to plaintiff in connection with defendants' proposal; and (3) if defendants were not awarded the project, plaintiff would not deal in any manner with the successful contractor. Plaintiff alleges that in exchange for its agreement to these conditions, defendants promised to use plaintiff as the exclusive subcontractor for all electrical and teledata work if defendants were awarded the prime contract. **[***3]** The exclusivity agreement was never reduced to writing, nor did the parties execute a subcontract. Although plaintiff asserts that they agreed upon a contract form, it concedes that the parties never fully agreed on the details of a subcontract and agreed only that the outstanding details of the subcontract would be discussed if defendants were ultimately awarded the KAPL contract.

Plaintiff's estimators traveled from Schenectady County to Rochester to meet with defendants' design team in September 2001. During and subsequent to this meeting, information about the project and KAPL flowed mutually between the parties. Over the next few months, plaintiff submitted various bid proposals to defendants, who were ultimately awarded the contract. Notwithstanding the parties' alleged oral agreement to use plaintiff as the exclusive subcontractor for the electrical and teledata portions of the contract, defendants put those aspects of the contract out to competitive bidding, and plaintiff was not awarded the subcontract that it claims was due under the exclusivity agreement. Plaintiff thereafter commenced this action, seeking damages for lost profits and other revenues it would have earned **[***4]** if it had been given the subcontract. Defendants moved for summary judgment dismissing the complaint and plaintiff cross-moved for summary judgment on liability. Following oral argument, Supreme Court denied both **[*985]** motions. Defendants and plaintiff cross appeal from that order [*] and both parties cross appeal from a separate order that partially granted a motion by defendants to compel plaintiff to respond to certain interrogatories.

The complaint in this action asserts five causes of action, sounding in **[***5]** breach of contract, promissory estoppel, unjust enrichment, equitable estoppel and fraud. For the reasons that follow, we conclude that only the second cause of action, asserting promissory estoppel, survives defendant's motion for summary judgment.

Defendant contends that the exclusivity agreement is unenforceable as a matter of law, and we agree. "It is well **[**185]** settled that a contract must be definite in its material terms in order to be enforceable" (*Spectrum Research Corp. v Interscience, Inc., 242 AD2d 810, 811, 661 NYS2d 871 [1997]*; *see* *Cobble Hill Nursing Home v Henry & Warren Corp., 74 NY2d 475, 482, 548 NE2d 203, 548 NYS2d 920 [1989]*, *cert denied 498 US 816, 112 L Ed 2d 33 [1990]*; *Marraccini v Bertelsmann Music Group, 221 AD2d 95, 97, 644 NYS2d 875 [1996]*, *lv denied 89 NY2d 809, 678 NE2d 502, 655 NYS2d 889 [1997])*. Thus, an "agreement to agree, in which a material term is left for future negotiations, is unenforceable" (*see* *Joseph Martin, Jr., Delicatessen v Schumacher, 52 NY2d 105, 109, 417 NE2d 541, 436 NYS2d 247 **[****3]** [1981]*; *Spectrum Research Corp. v Interscience, Inc., supra*; *Marraccini v Bertelsmann Music Group, supra*; *Bower v Atlis Sys., 182 AD2d 951, 952-953, 582 NYS2d 542 **[***6]** [1992]*, *lv denied 80 NY2d 758, 602 NE2d 1125, 589 NYS2d 309 [1992])*. Viewing the exclusivity agreement as defined by plaintiff, the parties agreed that if plaintiff refrained from having contact with any other contractor that was seeking the project, and if defendant was awarded the prime contract, the parties would enter into a subcontract for the electrical and teledata work on the project. This is merely an agreement to later agree upon the "precise nature of the work to be subcontracted, price and manner of payment and time of performance" (*Spectrum Research Corp. v Interscience, Inc., supra at 811*).

Plaintiff's contention that the pricing information for the subcontract is ascertainable by reference to the proposals that plaintiff submitted to defendant does not satisfy the requirement that the material terms of the agreement be definite. While it is true that application of the definiteness doctrine is **[*986]** not absolutely rigid (*see* *Matter of 166 Mamaroneck Ave. Corp. v 151 E. Post Rd. Corp., 78 NY2d 88, 91, 575 NE2d 104, 571 NYS2d 686 [1991]*; *Cobble Hill Nursing Home v Henry & Warren Corp., supra at 482-483*), there must be "an objective method for supplying a missing **[***7]** term" (*Matter of 166 Mamaroneck Ave. Corp. v 151 E. Post Rd. Corp., supra at 91*). Here, although the exclusivity agreement contemplates the parties' execution of a subcontract, that implicit provision cannot be viewed as a binding formula for supplying a missing term (*see* *Joseph Martin, Jr., Delicatessen v Schumacher, supra at 110-111*), nor does it "invite[] recourse to an objective extrinsic event, condition or standard" (*id. at 110*; *see* *Matter of 166 Mamaroneck Ave. Corp. v 151 E. Post Rd. Corp., supra* [agreement provided for arbitration]; *Cobble Hill Nursing Home v Henry & Warren Corp., supra* [agreement provided that price was to be determined by the Department of Health in accordance with applicable statutes, rules and regulations]). Rather, it requires further expressions by the parties and therefore fails to "reduc[e] uncertainty to certainty" (*Cobble Hill Nursing Home v Henry & Warren Corp., supra at 483*). To the extent that the bid proposals are utilized to determine pricing as a matter of commercial practice (*see* *Henri Assoc. v Saxony Carpet Co., 249 AD2d 63, 66, 671 NYS2d 46 [1998]),* **[***8]** the record is wholly devoid of evidence that defendant agreed to the prices proposed by plaintiff (*compare id.*; *see T. Moriarty & Son v Case Contr., 287 AD2d 390, 731 NYS2d 618 [2001])*. In sum, the exclusivity agreement that is the basis for plaintiff's first cause of action for breach of contract is unenforceable as a matter of law, and defendant's motion for summary judgment **[**186]** dismissing that cause of action should have been granted.

Plaintiff correctly contends that it is possible to state a cause of action for fraud in the inducement separate and apart from a claim for breach of the contract (*see*

[*] Defendants contend that defendant LeChase Data/Telecom Services, LLC and defendant LeChase Construction Corporation were uninvolved in the events giving rise to this action, and they sought summary judgment dismissing the complaint against them. Plaintiff did not oppose that request before Supreme Court, and does not oppose it upon appeal. Accordingly, it will be granted. Therefore, further references to defendant in this decision shall pertain to the remaining defendant, LeChase Construction Services, LLC.

Deerfield Communications Corp. v Chesebrough-Ponds, Inc., 68 NY2d 954, 956, 502 NE2d 1003, 510 NYS2d 88 [1986]; Sabo v Delman, 3 NY2d 155, 162, 143 NE2d 906, 164 NYS2d 714 [1957]). To the extent, however, that plaintiff's fifth cause of action may be construed as such, it must also be dismissed because there can be no viable claim for fraudulent inducement to enter an unenforceable contract (*see* Held v Kaufman, 91 NY2d 425, 431-432, 694 NE2d 430, 671 NYS2d 429 [1998]).

Plaintiff's second cause of action asserts a claim sounding in promissory estoppel. A party relying upon promissory estoppel must demonstrate **[***9]** that there was a clear and unambiguous promise upon which it reasonably and detrimentally relied (*see* Bunkoff Gen. Contrs. v Dunham Elec., 300 AD2d 976, 978, 753 NYS2d 156 [2002]; Fourth Branch Assoc. Mechanicville v Niagara Mohawk Power Corp., 235 AD2d 962, 964, 653 NYS2d 412 [1997]; Freedman & Son v A.I. **[*987]** Credit Corp., 226 AD2d 1002, 1003, 641 NYS2d 429 [1996]). Plaintiff has submitted evidence in admissible form that defendants promised to give plaintiff the project subcontract, and that plaintiff refrained from working with other general contractors who were seeking the project in reliance on that alleged but ultimately unfulfilled promise. Defendants submit evidence that they never promised plaintiff the **[****4]** subcontract, and that plaintiff did, in fact, seek to work with another general contractor who was pursuing the project. Clearly, the parties' submissions create issues of material fact regarding whether defendant made the alleged promise and whether plaintiff reasonably relied thereon, and Supreme Court properly denied the motions for summary judgment on the promissory estoppel cause of action.

Plaintiff's fourth cause of action sounds in equitable **[***10]** estoppel. In support of the cause of action, plaintiff alleges facts similar to those underlying its promissory estoppel claim, along with allegations of the scienter that is an element to be established by a party seeking equitable estoppel (*see Michaels v Travelers Indem. Co., 257 AD2d 828, 829, 683 NYS2d 640 [1999]*; *State Bank of Albany v Fioravanti, 70 AD2d 1011, 1012-1013, 418 NYS2d 202 [1979]*, *affd* 51 NY2d 638, 417 NE2d 60, 435 NYS2d 947 [1980]). The fundamental and fatal flaw in this cause of action is plaintiff's demand for money damages upon it; equitable estoppel is invoked to prohibit a party from engaging in certain conduct (*see e.g.* *Matter of Hession v New York State & Local Employees' Retirement Sys., 24 AD3d 1008, 1010, 806 NYS2d 281 [2005]* [the petitioner sought to equitably estop the respondent from denying tier 1 retirement status]; *Doe v Holy See [State of Vatican City], 17 AD3d 793, 794-795, 793 NYS2d 565 [2005]*, *lv denied 6 NY3d 707, 845 NE2d 1274, 812 NYS2d 443 [2006]* [the plaintiffs sought to estop the defendants from asserting statute of limitations defense]; *Matter of Sarah S. v James T., 299 AD2d 785, 751 NYS2d 61 [2002]* [equitable estoppel **[***11]** invoked to prevent denial of paternity]; *McKay v Healthcare Underwriters Mut. Ins. Co., 295 AD2d 686, 688, 743 NYS2d 593 [2002]*, *lv denied 99 NY2d 503, 783 NE2d 896, 753 NYS2d 806 [2002]* [equitable estoppel sought to prevent denial of insurance coverage]). Here, because plaintiff does not seek the type of remedy that would be available upon a successful **[**187]** invocation of equitable estoppel, the fourth cause of action should have been dismissed. To the extent that equity may provide plaintiff with a remedy in damages in this particular case, plaintiff's avenue of recovery rests on its promissory estoppel claim (*see* Bunkoff Gen. Contrs. v Dunham Elec., supra at 976-977).

Plaintiff's third cause of action generally alleges that defendant was unjustly enriched by plaintiff's experience with KAPL as well as plaintiff's direct contributions to defendant's successful proposal for the prime contract. A cause of action for unjust **[*988]** enrichment requires a showing that (1) the defendant was enriched, (2) at the expense of the plaintiff, and (3) that it would be inequitable to permit the defendant to retain that which is claimed by the plaintiff (*see* **[***12]** *Cruz v McAneney, 29 AD3d 512, 512, 813 NYS2d 671 [2006]*; *Mente v Wenzel, 178 AD2d 705, 706, 577 NYS2d 167 [1991]*). The essence of such a cause of action is that one party is in possession of money or property that rightly belongs to another (*see* *Paramount Film Distrib. Corp. v State of New York, 30 NY2d 415, 421, 285 NE2d 695, 334 NYS2d 388 [1972]*, *cert denied 414 US 829, 38 L Ed 2d 64 [1973]*; *Town of Butternuts v National Grange of Patrons of Husbandry, 20 AD3d 637, 798 NYS2d 773 [2005]*; *George S. May Intl. Co. v Thirsty Moose, Inc., 19 A.D.3d 721, 796 NYS2d 196 [2005]*; *Anesthesia Group of Albany v State of New York, 309 AD2d 1130, 1131-1132, 766 NYS2d 448 [2003]*; Mente v Wenzel, supra). Here, plaintiff's submissions on the parties' competing motions for summary judgment make only conclusory allegations that defendant benefitted from plaintiff's involvement in the bid formulation process, and plaintiff asserts no facts suggesting that defendant is in possession of money or property belonging to plaintiff. Thus, there is no issue of fact requiring a trial on this cause of action (*see* Hamlin Beach Camping, Catering, & Concessions Corp. v State *of New York, 303 AD2d 849, 853, 756 NYS2d 354* ***[***13]*** *[2003]*; *Absher Constr. Corp. v Colin, 233 AD2d 279, 280, 649 NYS2d 174 [1996])*, and defendant's motion for summary judgment dismissing plaintiff's cause of action for unjust enrichment should have been granted.

Turning to defendant's appeal and plaintiff's cross appeal from Supreme Court's order addressed to defendant's discovery motion, it is well settled that the trial court has broad **[****5]** discretion in supervising discovery (*see* *Bohlke v General Elec. Co., 27 AD3d 924, 810 NYS2d 583 [2006]*; *Mora v RGB, Inc., 17 AD3d 849, 851, 794 NYS2d 134 [2005]*; *Di Mascio v General Elec. Co., 307 AD2d 600, 601, 762 NYS2d 696 [2003])*. Upon our review of the record and supplemental record, we find that the order directing and conditioning plaintiff's disclosure of certain allegedly confidential information upon the execution of a court-approved confidentiality agreement and denying other aspects of defendant's motion to compel disclosure was rendered well within the bounds of Supreme Court's discretion. Further, in the context of this protracted and contentious discovery dispute, we find no merit in defendant's contention that plaintiff waived its objections to defendant's **[***14]** demands for interrogatories.

Crew III, J.P., Peters, Lahtinen and Kane, JJ., concur. Ordered that the order entered October 24, 2005 is affirmed, without costs. Ordered that the order entered January 26, 2006 is modified, on the law, without costs, by reversing so much thereof as **[*989]** denied defendants' motion for summary judgment (1) dismissing the complaint against defendants LeChase Data/Telecom Services, LLC and LeChase **[**188]** Construction Corporation and (2) dismissing the first, third, fourth and fifth causes of action against defendant LeChase Construction Services, LLC; motion granted to that extent, summary judgment awarded to defendants and all causes of action dismissed except the second cause of action which remains against LeChase Construction Services, LLC only; and, as so modified, affirmed.

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Columbia Mem. Hosp. v Hinds

Supreme Court of New York, Columbia County

September 3, 2019, Decided

14064-19

Reporter

2019 N.Y. Misc. LEXIS 5072 *; 2019 NY Slip Op 51508(U) **; 65 Misc. 3d 1205(A); 2019 WL 4620674

[1]** The Columbia Memorial Hospital, Plaintiff, against Marcel E. Hinds, M.D., Defendant.

Notice: THIS OPINION IS UNCORRECTED AND WILL NOT BE PUBLISHED IN THE PRINTED OFFICIAL REPORTS.

Counsel: **[*1]** For Plaintiff: Anthony Prinzivalli, Esq., of counsel, Kevin G. Donoghue, Esq., of counsel, Garfunkel Wild, P.C., Great neck, New York.

For Defendant: Seth A. Nadel, Esq., of counsel, Weiss Zarett Brofman Sonnenklar & Levy, P.C., New Hyde Park, New York.

Judges: Henry F. Zwack, Acting Supreme Court Justice.

Opinion by: Henry F. Zwack

Opinion

Henry F. Zwack, J.

Pending before the Court is a motion to dismiss the complaint in this action filed by defendant Marcel E. Hinds, M.D., and for declaratory judgment. The defendant alleges that dismissal is required pursuant to CPLR 3211(a)(1) and CPLR 3211(a)(7); and an order pursuant to CPLR 3001 declaring that he is legally entitled to cash consideration in the amount of $412,418.93 arising from the demutualization of Medical Liability Mutual Insurance Company ("MLMIC"). The plaintiff opposes.

The dispute arises out of the sale and demutualization of MLMIC, a mutual insurance company formed and existing under New York Law, which plan was approved by the Department of Financial Services ("DFS") on September 6, 2018. The DFS Decision confirmed, on pages 4, 23 (affirmation of Seth Nadel, Exhibit "A") that it is in the Insurance Law 7307 (e)(3) which explicitly defines those policyholders who are **[**2]** eligible to receive the purchase price consideration." **[*2]**

In connection with the demutualization, certain sums of money were to be paid to the policyholders (physicians) who were the mutual owners of MLMIC during the statutory eligibility period prior to the sale. An objection procedure was put in place (and later extended) by MLMIC where certain employers of eligible physician policyholders were given the right to object to the cash distribution, to the extent the employer believed that it, and not the physician, was entitled to the funds. The plaintiff is the former employer of the defendant, and submitted an objection and commenced this action seeking a determination of its right to the cash contribution presently held in escrow.

According to the complaint, the $412,418.93 in dispute represents what the plaintiff paid to MLMIC for professional liability insurance on behalf of the defendant from July 15, 2013 to July 15, 2016. The complaint sets out four causes of action: declaratory judgment, unjust enrichment, money had and received, and breach of implied covenant of good faith and fair dealing. The plaintiff alleges that it is entitled to the MLMIC funds, currently being held in escrow, because it alone paid for the policies, administered **[*3]** and controlled them as the designated Policy Administrator, was always the beneficiary of any dividends, rebates or refunds under the policies, and because the defendant has no rights to receive any additional monies following his separation from the plaintiff hospital. The defendant has refused to sign the Assignment Agreement, requested by the plaintiff in order for the escrow funds to be turned over to it. The plaintiff argues that allowing the defendant to receive and retain the MLMIC funds would result in his unjust enrichment. The complaint alleges that the defendant has already received all that he is entitled to under his employment agreement.

In lieu of an answer, the defendant has moved to dismiss the complaint on the grounds that the complaint fails to state a cause of action, and on the basis that the claims fail due to documentary evidence.

The defendant argues he is entitled to the cash proceeds under the authority which governs the demutualization, the Plan of Conversion of Medical Liability Mutual Insurance Company adopted on May 31, 201, and *Insurance Law 7307*. The Plan provided that policyholders, or their designees would be provided with cash consideration for their membership interest **[*4]** according to the premiums timely paid under their eligible policies. The Plan further provided that the cash consideration was to go directly to the policyholder unless they had affirmatively **[**3]** designated a policy administrator to receive the benefit—the affirmative designation is the only instance in which the policy administrator could receive the cash consideration payable to the policyholder. The defendant asserts that he is the policyholder (as demonstrated on the policy declarations page supplied by defendant); he did not sign an Assignment Agreement (although asked to do so on at several occasions); and the plaintiff is not entitled to receive any of the cash consideration. The defendant explains that according to his Employment Agreement, at Section 3 (b) — which is attached as an Exhibit to his affidavit — he actually paid the premiums, as the plaintiff deducted the amounts it paid for his malpractice insurance from his incentive compensation. The policy administrator designation served only to appoint the plaintiff as the defendant's agent for the purposes of managing the policy, and to receive dividends to offset the cost of the policy. The defendant argues that the cash consideration **[*5]** is not a dividend or return premium as 1099 forms were sent to policyholders that confirm the proceeds arose from the sale of stock.

In opposition, the plaintiff argues that the defendant's dismissal motion is improper, by utilizing affidavits to establish "facts" rather than just to introduce documentary evidence. According to the plaintiff, there is a bona fide dispute which must be determined by the court. The plaintiff argues that the complaint should not be dismissed because there is a binding decision from the Appellate Division on point in this case. In *Shaeffer, Schonholtz & Drossman, LLP v Title, 171 AD3d 465, 465, 96 N.Y.S.3d 526 [1st Dept 2019]* the Court found that despite respondent being named as the policyholder, appellant had paid all the premiums and all the costs related to the policy and there was no record of bargaining for the benefit of the demutualization proceeds, so "awarding respondent with the cash proceeds of the MLMIC's demutualization would result in unjust enrichment." The plaintiff argues that this is the situation here — Dr. Hinds did not pay any of the premiums for the insurance, and awarding him the funds from the demutualization results in unjust enrichment. The plaintiff also argues that stare decisis applies, and this Court must follow the **[*6]** determination made by the First Department. Stare decisis provides that once a court has resolved a legal issue, it should not be re-examined each and every time it is presented *(Battle v State, 257 AD2d 745, 682 N.Y.S.2d 726 [3d Dept 1999])*.

For the reasons that follow the Court grants the defendant's motion to dismiss the plaintiff's complaint.

Here, the Court is mindful, on a motion to dismiss pursuant to **[**4]** *CPLR 3211*, it must "accept the facts as alleged in the complaint as true, according the plaintiffs the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory" (*Leon v Martinez, 84 NY2d 83, 87-88, 638 N.E.2d 511, 614 N.Y.S.2d 972 [1994]*). "[A]llegations consisting of bare legal conclusions as well as factual claims flatly contradicted by documentary evidence are not entitled to consideration" (*Mass v Cornell University, 94 NY2d 87,91, 721 N.E.2d 966, 699 N.Y.S.2d 716 [1999]*).

Insurance Law 7307 governs the process by which MLMIC was converted from a mutual insurance company into a stock insurance company. *Insurance Law 7307 (e) (3)* provides in pertinent part that "each person who had a policy of insurance in effect at any time during the three year period immediately proceeding the date of the adoption of the resolution shall be entitled to receive in exchange for such equitable share, without additional payment, consideration payable in voting shares of the insurer or other **[*7]** consideration, or both." The statute repeatedly refers to those eligible for cash consideration as the "policyholder." It is important to note that "[n]o distinction is made between a policyholder who pays the premium out of his own pocket versus a policyholder whose employer pays the premium as part of an employee compensation package. *Insurance Law 7307* does not confer an ownership interest...on anyone other than the policyholder" (*Maple-Gate Anesthesiologists, P.C. v Nasrin, 63 Misc 3d 703, 709, 96 N.Y.S.3d 837 [Sup Ct, Erie County, 2019]*).

Here, the defendant is clearly the policyholder, and the plaintiff the policy administrator. The documentary evidence — the Employment Agreement — establishes that the insurance premiums were deducted before the defendant received any incentive pay. That is, the defendant was to receive incentive pay, 65% of the amount by which his revenue exceeded the expenses paid by the hospital, and one the expenses being his medical malpractice insurance. Stated differently, the defendant would not receive incentive pay until the revenue generated by his services exceeded the amount of his medical malpractice insurance. Further, under the plain language of the Insurance Law, the cash consideration cannot be given to the plaintiff unless the defendant signs the agreement to do so. **[*8]** Here, the defendant has not signed such an agreement, and given the circumstances of this case — the Employment Agreement which required him to pay the cost of his malpractice premiums by way of his salary incentives — does not have to agree to do so.

The plaintiff's entire argument, as framed by the complaint, **[**5]** focuses on the bare and incorrect assertion that the hospital paid the policy premiums and that equity, not ownership, dictates that it should be the recipient of the cash contribution. However viewed, this assertion is belied by the terms of the Employment Agreement, whereby the defendant's incentive compensation is reduced by the policy premiums. On this record, equity does not dictate that the plaintiff should be compensated.

Nor has the plaintiff demonstrated that the defendant has been unjustly enriched. Unjust enrichment, also known as an action for money had or received, or implied contract (*Federal Ins. Co. v Groveland State Bank, 37 NY2d 252, 258, 333 N.E.2d 334, 372 N.Y.S.2d 18 [1975]*), arises when a plaintiff demonstrates "that (1) the other party was enriched, (2) at (the plaintiff's) expense, and (3) that it is against equity and good conscience to permit the other party to retain what is sought be recovered" (*New York State Worker's Compensation Bd. v Program Risk Mgt, Inc., 150 AD3d 1589, 1594, 55 N.Y.S.3d 790 [3d Dept 2017]*). Given that the plaintiff received the defendant's **[*9]** services in exchange for compensation — which was reduced by the cost of the premium payments made on the defendant's behalf by the plaintiff — there is simply no merit to the plaintiff's claim of unjust enrichment.

"The implied covenant of good faith and fair dealing between parties to a contract embraces a pledge that neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract" (*Moran v Erk, 11 NY3d 452, 456, 901 N.E.2d 187, 872 N.Y.S.2d 696 [2008]*, internal citations and quotations omitted). In all likelihood neither party appreciated that a windfall could occur as a result of the MLMIC sale, because, quite simply, they did not appreciate the meaning and the value of an ownership stake prior to the demutualization plan (*Urgent Medical Care PLLC v Amedure, 64 Misc 3d 1216[A], 2019 NY Slip Op 51188[U] [Sup Ct, Greene County 2019]*) . It cannot therefore be said that this cash contribution was negotiated or bargained for, but is simply rather an operation of law, and therefore no one's interest in the actual contract was compromised. This cash contribution, by law, is not a return to the hospital of any insurance premiums it paid on behalf of the defendant, it represents the policyholder's share in MLMIC.

Contrary to plaintiff's arguments **[*10]** that *Shaeffer, Schonholtz & Drossman, LLP v Title, 171 AD3d 465, 465, 96 N.Y.S.3d 526 [1st Dept 2019]* controls, this case is not entitled to stare decisis treatment. The doctrine of stare decisis clearly exists to provide guidance and consistent results in cases that share essentially the same facts (*Matter of Howard Johnson Co. v State Tax Commn., 65 NY2d 726, 727, 481 N.E.2d 551, 492 N.Y.S.2d 11[1985]*). It does not apply where, as here, the facts are not the same. Here, like the defendant Nasrin in *Maple-Gate Anesthesiologists (63 Misc 3d 703, 96 N.Y.S.3d 837*) the defendant's insurance premiums were paid in lieu of compensation (Nasrin received her **[**6]** malpractice insurance as part of her employee compensation plan, and the Court awarded the cash contribution to her). That being said, it is equally well established that courts are free to correct prior erroneous interpretations of the law (*Matter of Charles A. Field Delivery Serv. (Roberts), 66 NY2d 516, 488 N.E.2d 1223, 498 N.Y.S.2d 111 [1985]*).

Finally, the plaintiff's complaint itself is some what of a 'ticking time-bomb." Paragraph 10 affirmatively provides the following: "The Hospital compensated Defendant for his services with a 'Base Salary' plus ***incentive compensation***, on call compensation, and afforded him the ***full panoply of benefits, including payment of premiums for medical malpractice insurance***..." There is no other way to read this than for it to mean that the defendant's medical malpractice insurance premiums were a part of his employee compensation plan. As to the Employee Agreement **[*11]** itself, at Article 9 it reads that the hospital "shall maintain an individual occurrence -based medical malpractice policy in the minimum amounts required....and provide you with evidence of same upon request." Following the determination in *Maple-Gate Anesthesiologists* (63Misc 3d 703), the Court dismisses the plaintiff's complaint.

Accordingly, it is

ORDERED, the defendant Marcel Hinds M.D.'s motion to dismiss is granted, and the plaintiff's complaint is dismissed, and it is further

ORDERED, that the defendant Hinds is entitled to the $412,418.93 arising from the sale and demutualization of Medical Liability Mutual Insurance Company, and the funds are to be dispersed accordingly.

This constitutes the Decision and Order of the Court. This original Decision and Order is returned to the attorneys for the defendant. All other papers are delivered to the Supreme Court Clerk for transmission to the County Clerk. The signing of this Decision and Order shall not constitute entry or filing under CPLR 2220. Counsel is not relieved from the applicable provisions of this rule with regard to filing, entry and Notice of Entry.

Dated: September 3, 2019

Troy, New York

Henry F. Zwack

Acting Supreme Court Justice

Commonwealth of the N. Mariana Is. v. Canadian Imperial Bank of Commerce

Court of Appeals of New York

March 18, 2013, Argued; April 30, 2013, Decided

No. 58

Reporter

21 N.Y.3d 55 *; 990 N.E.2d 114 **; 967 N.Y.S.2d 876 ***; 2013 N.Y. LEXIS 839 ****; 2013 NY Slip Op 3018; 2013 WL 1798585

[1] Commonwealth of the Northern Mariana Islands, Appellant, v Canadian Imperial Bank of Commerce, Respondent, William H. Millard, Defendant, The Millard Foundation, Intervenor.

Prior History: Proceeding, pursuant to NY Constitution, article VI, § 3 (b) (9) and Rules of the Court of Appeals *(22 NYCRR) § 500.27*, to review a question certified to the New York State Court of Appeals by the United States Court of Appeals for the Second Circuit. The following questions were certified by the United States Court of Appeals and accepted by the New York State Court of Appeals: "1. May a court issue a turnover order pursuant to N.Y. C.P.L.R. § 5225 (b) to an entity that does not have actual possession or custody of a debtor's assets, but whose subsidiary might have possession or custody of such assets? 2. If the answer to the above question is in the affirmative, what factual considerations should a court take into account in determining whether the issuance of such an order is permissible?"

Commonwealth of the N. Mariana Islands v Canadian Imperial Bank of Commerce, 693 F3d 274, 2012 U.S. App. LEXIS 18682 (2d Cir. N.Y., 2012)

Disposition: **[****1]** Following certification of questions by the United States Court of Appeals for the Second Circuit and acceptance of the questions by this Court pursuant to section 500.27 of the Rules of Practice of the New York State Court of Appeals, and after hearing argument by counsel for the parties and consideration of the briefs and the record submitted, certified question no. 1 answered in the negative and certified question no. 2 not answered as academic.

Counsel: *Kobre & Kim LLP*, New York City (*Michael S. Kim* and *Melanie L. Oxhorn* of counsel), for appellant. I. CPLR 5225 (b)'s postjudgment enforcement remedy may be applied under circumstances where assets are held by a garnishee's subsidiary but the garnishee is determined to have the actual, practical ability to direct or control their disposition. (Koehler v Bank of Bermuda Ltd., 12 NY3d 533, 911 NE2d 825, 883 NYS2d 763; Merkling v Ford Motor Co., 251 App Div 89, 296 NYS 393; United States v First Nat. City Bank, 379 US 378, 85 S Ct 528, 13 L Ed 2d 365; *Allied Mar., Inc. v Descatrade SA, 620 F3d 70*; *JW Oilfield Equip., LLC v Commerzbank, AG, 764 F Supp 2d 587*.) II. A court considering whether to issue a turnover order to a garnishee whose subsidiary has actual possession or custody of assets should determine whether the garnishee has the actual, practical ability to control the subsidiary's disposition of them. (Bellomo v Pennsylvania Life Co., 488 F Supp 744; Frummer v Hilton Hotels Intl., 19 NY2d 533, 227 NE2d 851, 281 NYS2d 41; In re Citric Acid Litig., 191 F3d 1090; First Natl. City Bank of N.Y. v Internal Revenue Serv. of U.S. Treasury Dept., 271 F2d 616; Koehler v Bank of Bermuda Ltd., 12 NY3d 533, 911 NE2d 825, 883 NYS2d 763.)

Skadden, Arps, Slate, Meagher & Flom LLP, New York City (*Scott D. Musoff, Timothy G. Nelson* and *Gregory A. Litt* of counsel), for respondent. I. A bank that holds no property or accounts of the relevant debtor should not be compelled to turn over money or assets deposited at its foreign subsidiary banks. (Sundail Constr. Co. v Liberty Bank, 277 NY 137, 13 NE2d 745; In re Delaney, 256 NY 315, 176 N.E. 407; Greenberg, Trager & Herbst, LLP v HSBC Bank USA, 17 NY3d 565, 958 NE2d 77, 934 NYS2d 43; Brigham v McCabe, 20 NY2d 525, 232 NE2d 327, 285 NYS2d 294; Solicitor for Affairs of His Majesty's Treasury v Bankers Trust Co., 304 NY 282, 107 NE2d 448; Cruz v TD Bank, N.A., 855 F Supp 2d 157; Grain Traders, Inc. v Citibank, N.A., 960 F Supp 784; *Bradford v Chase Natl. Bank of City of N.Y., 24 F Supp 28*; Middle E. Banking Co. v State St. Bank Intl., 821 F2d 897; Geler v National Westminster Bank USA, 770 F Supp 210.) II. The turnover statutes could validly be applied to corporate affiliates only if veil-piercing were established. (*Moreau v RPM, Inc., 20*

AD3d 456, 799 NYS2d 113; *Insurance Co. of N. Am. v EMCOR Group, Inc., 9 AD3d 319, 781 NYS2d 4*; *Frummer v Hilton Hotels Intl., 19 NY2d 533, 227 NE2d 851, 281 NYS2d 41*; *Bellomo v Pennsylvania Life Co., 488 F Supp 744*; *Comprehensive Sports Planning v Pleasant Val. Country Club, 73 Misc 2d 477, 341 NYS2d 914*; *IRB-Brasil Resseguros, S.A. v Inepar Invs., S.A., 20 NY3d 310, 982 NE2d 609, 958 NYS2d 689*; *Tri City Roofers v Northeastern Indus. Park, 61 NY2d 779, 461 NE2d 298, 473 NYS2d 161*; *Western Union Telegraph Co. v Pennsylvania, 368 US 71, 82 S Ct 199, 7 L Ed 2d 139*; *JPMorgan Chase Bank, N.A. v Motorola, Inc., 47 AD3d 293, 846 NYS2d 171*; *Harris v Balk, 198 US 215, 25 S Ct 625, 49 L Ed 1023*.)

Judges: RIVERA, J. Opinion by Judge Rivera. Chief Judge Lippman and Judges Graffeo, Read, Smith and Pigott concur.

Opinion by: RIVERA

Opinion

[*877]** **[*57]** **[**115]** Rivera, J.

Two questions certified to us by the United States Court of Appeals for the Second Circuit raise issues as to whether a judgment creditor can obtain a CPLR article 52 turnover order against a bank to garnish assets held by the bank's foreign subsidiary. We hold that for a court to issue a postjudgment turnover order pursuant to *CPLR 5225 (b)* against a banking entity, that entity itself must have actual, not merely constructive, possession or custody of the assets sought. That is, it is not enough **[*58]** that the banking entity's **[2]** subsidiary might have possession **[****2]** or custody of a judgment debtor's assets.

In 1994, plaintiff, the Commonwealth of the Northern Mariana Islands (the Commonwealth), obtained two separate tax judgments in the United States District Court for the Northern Mariana Islands against William and Patricia Millard (the Millards) for unpaid taxes in the respective amounts of $18,317,980.80 and $18,318,113.41. The Millards, who had previously resided in the Commonwealth since 1987, relocated before the Commonwealth was able to obtain the judgments.[1]

In March and April 2011, the Commonwealth registered the tax judgments in the United States District Court for the Southern District of New York[2] and commenced proceedings as a judgment creditor, pursuant **[***878]** **[**116]** to *Federal Rules of Civil Procedure rule 69 (a) (1)* and *CPLR 5225 (b)*, seeking a turnover order against garnishees holding assets of the Millards. As relevant here, the Commonwealth named Canadian Imperial Bank of Commerce (CIBC), a Canadian bank headquartered in Toronto, with a branch in New York, as a garnishee under the theory that the Millards maintained **[****3]** accounts in subsidiaries of CIBC, namely, CIBC FirstCaribbean International Bank Limited (CFIB) or CFIB's affiliates in the Cayman Islands. According to the Commonwealth, CFIB is a 92% owned-and-controlled direct subsidiary of CIBC.

The Commonwealth moved, by order to show cause, for a turnover order against CIBC and a preliminary injunction, on the ground that "CIBC has the control, power, authority and practical ability to order [CFIB] to turn over funds on deposit in the name of the Millards." In support, the Commonwealth referred to the 92% ownership of CFIB, and other indicia of control, asserting that CIBC imposed a governance structure upon CFIB that "affords the parent company full oversight of the risk and control framework of all [of CFIB's] operations." The Commonwealth further argued that the overlap in significant personnel, and CIBC's oversight of CFIB's compliance with various legal requirements, such as the Sarbanes-Oxley Act, demonstrated CIBC's ability to exert actual, practical control over CFIB's operations. In opposition, CIBC contended **[****4]** that CFIB is a "legally separate and independent entit[y]" and that, **[*59]** absent an information sharing agreement, "CIBC is unable to access accounts or account information held by [CFIB] or its subsidiaries."

The District Court denied the motion and maintained a previously issued restraining order that precluded CIBC from engaging in certain activity related to the Millards' **[3]** accounts. While the District Court found the Commonwealth's "practical ability to control" argument colorable, it observed that the scope of the phrase "possession or custody," contained in *CPLR 5225 (b)*, was an issue suited for this Court's consideration.

Upon appeal, the Second Circuit determined that for the

[1] In 2010, the Commonwealth learned that the Millards had renounced their United States citizenship and resided in the Cayman Islands.

[2] The Commonwealth also registered the judgments in the United States District Court for the Southern District of Florida.

reasons set forth in the District Court's opinion, the resolution of the case turned on unresolved issues of New York law, and certified the following questions to this Court:

> "1. May a court issue a turnover order pursuant to N.Y. C.P.L.R. § 5225(b) to an entity that does not have actual possession or custody of a debtor's assets, but whose subsidiary might have possession or custody of such assets?
>
> "2. If the answer to the above question is in the affirmative, what factual considerations should a court take into **[****5]** account in determining whether the issuance of such an order is permissible?" (693 F3d 274, 275 [2d Cir 2012]).

We accepted the certified questions and now answer the first in the negative, and as a consequence refrain from answering the second as academic.[3]

Under CPLR article 52, a special proceeding for a turnover order is the procedural mechanism devised by the legislature to enforce a judgment against an asset of a judgment debtor, held in the **[***879] [**117]** "possession or custody" of a third party. Section 5225 (b) provides, in pertinent part:

> "Upon a special proceeding commenced by the judgment creditor, *against a person in possession or custody of money or other personal property in which the judgment debtor has an interest*, or against a **[*60]** person who is a transferee **[****6]** of money or other personal property from the judgment debtor, where it is shown that the judgment debtor is entitled to the possession of such property or that the judgment creditor's rights to the property are superior to those of the transferee, the court shall require such person to pay the money, or so much of it as is sufficient to satisfy the judgment, to the judgment creditor and, if the amount to be so paid is insufficient to satisfy the judgment, to deliver any other personal property, or so much of it as is of sufficient value to satisfy the judgment, to a designated sheriff."

[1] The Commonwealth contends that the phrase "possession or custody" inherently encompasses the concept of control, and, therefore, section 5225 (b) is applicable to garnishees **[4]** with constructive possession of a judgment debtor's assets. As such, the Commonwealth proposes that an actual, practical control test—i.e., whether the bank could practically order its subsidiary to turn over the assets of the judgment debtor—should be adopted by this Court as the appropriate standard. We find the Commonwealth's interpretation of section 5225 (b) unpersuasive for the reasons that follow.

In determining the expanse **[****7]** of section 5225 (b) our "starting point" is "the language itself, giving effect to the plain meaning thereof" (Majewski v Broadalbin-Perth Cent. School Dist., 91 NY2d 577, 583, 696 NE2d 978, 673 NYS2d 966 [1998]). "[W]here the statutory language is clear and unambiguous, the court should construe it so as to give effect to the plain meaning of the words used" (Patrolmen's Benevolent Assn. of City of N.Y. v City of New York, 41 NY2d 205, 208, 359 NE2d 1338, 391 NYS2d 544 [1976], citing Bender v Jamaica Hosp., 40 NY2d 560, 356 NE2d 1228, 388 NYS2d 269 [1976]). Moreover, "[i]t is fundamental that a court, in interpreting a statute, should attempt to effectuate the intent of the Legislature" (Majewski, 91 NY2d at 583, citing Patrolmen's Benevolent Assn., 41 NY2d at 208).

The plain language of section 5225 (b) refers only to "possession or custody," excluding any reference to "control." The absence of this word is meaningful and intentional as we have previously observed that the failure of the legislature to include a term in a statute is a significant indication that its exclusion was intended (*see* People v Finnegan, 85 NY2d 53, 58, 647 NE2d 758, 623 NYS2d 546 [1995] ["We have firmly held that the failure of the Legislature to include a substantive, significant prescription in a statute is a **[*61]** strong indication **[****8]** that its exclusion was intended"]; Pajak v Pajak, 56 NY2d 394, 397, 437 NE2d 1138, 452 NYS2d 381 [1982] ["The failure of the Legislature to provide that mental illness is a valid defense in an action for divorce based upon the ground of cruel and inhuman treatment must be viewed as a matter of legislative design. Any other construction of the statute would amount to judicial legislation"]; *see also* McKinney's Cons Laws of NY, Book 1, Statutes § 74). Accordingly, we interpret the omission of "control" from section 5225 (b) as an indication that "possession or custody"

[3] On appeal CIBC contends that the Commonwealth incorrectly moved pursuant to CPLR 5225 (b) rather than CPLR 5227, arguing that the latter is the applicable section to turnover orders involving bank deposits as the "debt" owed by the bank to the customer. We have no cause to address the applicability of section 5227, and limit our analysis to the issues concerning CPLR 5225 (b) presented by the Second Circuit's certification to this Court.

requires actual possession.

[*880] [**118]** The language of the predecessor statute to *section 5225 (b)* and the legislation enacting the CPLR lend additional support to the view that "possession or custody" does not include constructive possession. Prior to the 1962 legislation enacting the CPLR, the relevant turnover statutes referred to "possession" and "control" and made no mention of custody (*see* Civil Practice Act §§ 793, 796). Civil Practice Act § 796, the predecessor statute to *section 5225 (b)*, provided in relevant part that

> "[w]here it appears from the examination or testimony taken in a special proceeding authorized by this article that the judgment debtor has **[****9]** in his possession or under his control money or other personal property belonging to him, or that money or one or more articles of personal property capable of delivery, his right to the possession whereof is not substantially disputed, are in the possession or under the control of another person, the court in its discretion and upon such a notice given to such persons as it deems just, or without notice, may make an order directing the **[5]** judgment debtor or other person immediately to pay the money or deliver the articles of personal property to a sheriff designated in the order."

Section 5225 (b) and other related provisions were enacted to include the "possession or custody" language, thus making a clear distinction between the prior references to "possession" and "control." It is a well settled tenet of statutory construction that "[t]he Legislature, by enacting an amendment of a statute changing the language thereof, is deemed to have intended a material change in the law" (McKinney's Cons Laws of NY, Book 1, Statutes § 193). The exclusion of the word "control" signaled a purposeful legislative modification of the **[*62]** applicable scope of turnover statutes. The Commonwealth would have **[****10]** us construe *section 5225 (b)* to include that term, but "[a] court cannot by implication supply in a statute a provision which it is reasonable to suppose the Legislature intended intentionally to omit" because "the failure of the Legislature to include a matter within the scope of an act may be construed as an indication that its exclusion was intended" (McKinney's Cons Laws of NY, Book 1, Statutes § 74). In other words, we cannot read into the statute that which was specifically omitted by the legislature.

The Commonwealth argues that the legislature simply substituted "custody" as the functional equivalent of "control." However, we read the statute both based on its plain meaning and in context, and it is clear that the legislature did not pen one word anticipating that another would be "read into" the CPLR. When the legislature has sought to encompass the concept of "control" it has done so explicitly, evincing a legislative intent to exclude consideration of "control" from those sections from which it is omitted. For example, *CPLR 3111*, which concerns the production of discovery materials, provides that "books, papers and other things in the possession, custody or control of the **[****11]** person to be examined" should be produced. *CPLR 3119 (a) (4) (ii)* similarly provides that a subpoena may be used to order a person to produce discovery "in the possession, custody or control of the person" (*see also* *CPLR 2701*, *3120*, *3122-a*, *5224*). We are led to the conclusion that the legislature considered "control" and "custody" to refer to distinct concepts (*see* *People v Elmer, 19 NY3d 501, 507, 973 NE2d 172, 950 NYS2d 77 [2012]* [observing that the legislature is presumed to know the distinction between terms used in legislation]; *Easley v New York State Thruway Auth., 1 NY2d 374, 379, 135 NE2d 572, 153 NYS2d 28 [1956]* ["Legislatures are presumed **[***881] [**119]** to know what statutes are on the books and what is intended by constitutional amendments approved by the Legislature itself"]; McKinney's Cons Laws of NY, Book 1, Statutes § 222).

As these sections of the CPLR indicate, in a documentary discovery context, with expansive rules of disclosure, it is reasonable to conclude that the legislature would employ a broader "possession, custody or control" standard. Indeed, various courts have interpreted "possession, custody or control" to allow for discovery from parties that had practical ability to request from, or influence, another party with the desired **[****12]** discovery documents. As such, courts **[6]** have interpreted "possession, custody or control" to mean constructive possession (*see* **[*63]** *Bank of New York v Meridien BIAO Bank Tanzania Ltd., 171 FRD 135, 146 [SD NY 1997]* [" '(C)ontrol' does not require that the party have legal ownership or actual physical possession of the documents at issue; rather, documents are considered to be under a party's control when that party has the right, authority, or practical ability to obtain the documents from a non-party to the action"]; *see also* *In re NASDAQ Market-Makers Antitrust Litig., 169 FRD 493, 530 [SD NY 1996]*).

Consequently, because "possession, custody or control" has been construed to encompass constructive possession, then, by contrast, legislative use of the phrase "possession or custody" contemplates actual possession. Notably, sections of the CPLR pertaining to the disposition of property utilize the narrower "possession or custody" standard. For example, CPLR 1320, which concerns the attachment or levy of personal property, is limited to property "in the defendant's possession or custody." CPLR 6214 and 6215 similarly limit the levy of personal property to items within the "possession or custody" **[****13]** of the defendant (*see also* CPLR 1321, 1325, 2701, 5222, 5225, 5232, 5250, 6219). This distinction supports the view that the legislature has applied a higher standard to insure the proper disposition of property (*see* CPLR 5209; JPMorgan Chase Bank, N.A. v Motorola, Inc., 47 AD3d 293, 846 NYS2d 171 [1st Dept 2007]).

The Commonwealth argues that this distinction is of no moment, speculating that the legislature blindly duplicated the standards of the Federal Rules of Evidence when enacting the CPLR. However, "[w]hen different terms are used in various parts of a statute or rule, it is reasonable to assume that a distinction between them is intended" (Matter of Albano v Kirby, 36 NY2d 526, 530, 330 NE2d 615, 369 NYS2d 655 [1975]). Consequently, the distinction cannot be simply disregarded, and this Court is required to construe the entire CPLR in a manner that harmonizes these variations (*see* McKinney's Cons Laws of NY, Book 1, Statutes §§ 97, 98). In light of these differences, the most reasonable way to interpret these provisions is to conclude that "possession, custody or control" contemplates constructive possession, whereas "possession or custody," by its omission of the term "control," refers to actual possession. Accordingly, **[****14]** a section 5225 (b) turnover order cannot be issued against a garnishee lacking actual possession or custody of a judgment debtor's assets or property.

[2] Finally, our decision in Koehler v Bank of Bermuda Ltd. (12 NY3d 533, 911 NE2d 825, 883 NYS2d 763 [2009]) does not require a different reading of **[*64]** section 5225 (b). In that case, we addressed whether, under CPLR article 52, a New York court could order a bank over which it had personal jurisdiction to deliver out-of-state stock certificates to a judgment creditor. The Court noted that unlike prejudgment attachment, which requires jurisdiction **[***882]** **[**120]** over property, "postjudgment enforcement requires only jurisdiction over persons" (12 NY3d at 537). As such, "CPLR 5225 (b) applies when the property is not in the judgment debtor's possession" and "contemplate[s] an order, directed at a defendant who is amenable to the personal jurisdiction of the court, requiring **[7]** him to pay money or deliver property" (id. at 541). Accordingly, "a New York court with personal jurisdiction over a defendant may order him [or her] to turn over out-of-state property regardless of whether the defendant is a judgment debtor or a garnishee" (*id.*).

Notably, Koehler does not interpret the meaning of **[****15]** the phrase "possession or custody," and is only significant in holding that personal jurisdiction is the linchpin of authority under section 5225 (b) (*see also* Hotel 71 Mezz Lender LLC v Falor, 14 NY3d 303, 312, 926 NE2d 1202, 900 NYS2d 698 [2010]). Indeed, many cases have held that a turnover order is given effect through a court's exercise of personal jurisdiction over a party. Thus, in *Starbare II Partners v Sloan (216 AD2d 238, 629 NYS2d 23 [1st Dept 1995])*, albeit a section 5225 (a) case, the New York court had the authority to order a judgment debtor to turn over paintings he owned, but stored in New Jersey. In Miller v Doniger (28 AD3d 405, 814 NYS2d 141 [1st Dept 2006]), the judgment debtor, who was in New York, was directed to turn over his out-of-state Wachovia bank accounts to the judgment creditor. Similarly, in Gryphon Dom. VI, LLC v APP Intl. Fin. Co., B.V. (41 AD3d 25, 836 NYS2d 4 [1st Dept 2007]), the Appellate Division observed that "a turnover order merely directs a defendant, over whom the New York court has jurisdiction, to bring its own property into New York" (41 AD3d at 31). Thus, "[h]aving acquired jurisdiction of the person, the court [ ] can compel observance of its decrees by proceedings *in personam* against the owner within **[****16]** the jurisdiction" (Koehler, 12 NY3d at 539). However, in these cases, the garnishee was directed to deliver assets already within its possession. No case supports the Commonwealth's attempt to broadly construe Koehler and require that a garnishee be compelled to direct another entity, which is not subject to this state's personal jurisdiction, to deliver assets held in a foreign jurisdiction. Such an expansion is inconsistent with the plain language and scope of section 5225 (b).

[*65] Accordingly, certified question No. 1 should be answered in the negative and certified question No. 2 not answered as academic.

Chief Judge Lippman and Judges Graffeo, Read, Smith and Pigott concur.

Following certification of questions by the United States Court of Appeals for the Second Circuit and acceptance of the questions by this Court pursuant to section

500.27 of the Rules of Practice of the New York State Court of Appeals (*22 NYCRR 500.27*), and after hearing argument by counsel for the parties and consideration of the briefs and the record submitted, certified question No. 1 answered in the negative and certified question No. 2 not answered as academic.

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Dolman v. United States Trust Co.

Court of Appeals of New York

October 2, 1956, Argued ; November 15, 1956, Decided

No Number in Original

Reporter

2 N.Y.2d 110 *; 138 N.E.2d 784 **; 157 N.Y.S.2d 537 ***; 1956 N.Y. LEXIS 649 ****

Robert Dolman, Respondent, v. United States Trust Company of New York, as Trustee under the Will of Eugene Higgins, Deceased, Appellant

Prior History: **[****1]** Dolman v. United States Trust Co. of N. Y., 1 A D 2d 809, reversed.

Appeal from a judgment of the Appellate Division of the Supreme Court in the first judicial department, entered March 2, 1956, affirming, by a divided court, a judgment of the Supreme Court in favor of plaintiff, entered in New York County upon a decision of the court at a Trial Term (S. Samuel Di Falco, J.), without a jury.

Disposition: Judgments reversed, etc.

Counsel: *Williams S. Gaud* and *John P. Allee* for appellant. **[****4]** Defendant has breached no duty it owed plaintiff. (*Matter of City of New York* [*Ely Ave*.], 217 N. Y. 45; Bacon v. Miller, 247 N. Y. 311; Mawhinney v. Millbrook Woolen Mills, 231 N. Y. 290; Kip v. New York & Harlem R. R. Co., 67 N. Y. 227; Goodyear Shoe Mach. Co. v. Boston Term. Co., 176 Mass. 115.)

Milton M. Bergerman and *Joseph Calderon* for respondent. I. The finding that defendant induced and co-operated in the condemnation for the purpose of ending plaintiff's possessory rights has been affirmed by the Appellate Division and may not be reviewed in this court, and accords with the evidence. II. Defendant breached its covenant granting plaintiff quiet enjoyment of the leased premises. (Mack v. Patchin, 42 N. Y. 167; Ganz v. Clark, 252 N. Y. 92; Snow v. Pulitzer, 142 N. Y. 263; Williams v. Getman, 114 App. Div. 282; Lindwall v. May, 111 App. Div. 457; Edesheimer v. Quackenbush, 68 Hun 427; *Matter of City of New York* [*191 E. Houston St. Realty Corp*.], 194 Misc. 124; *Al's 334 9th Ave. Corp. v. Herbener, 275 App. Div. 904*; Matter of O'Donnell, 240 N. Y. 99; Fifth **[****5]** Ave. Bldg. Co. v. Kernochan, 221 N. Y. 370; Times Square Improvement Co. v. Fleischmann Vienna Model Bakery, 173 App. Div. 633.)

Judges: Dye, Froessel and Burke, JJ., concur with Conway, Ch. J.; Fuld, J., concurs in result; Desmond, J., dissents in an opinion in which Van Voorhis, J., concurs.

Opinion by: CONWAY

Opinion

[*112] **[**784]** **[***538]** This action was brought to recover damages for an alleged breach of the covenant of quiet enjoyment contained in the lease **[**785]** between the defendant as landlord and the plaintiff as tenant. It is claimed that the landlord breached the covenant by its inducement of and co-operation in the condemnation of the leased premises by the City of New York, resulting in the eviction of the plaintiff at the end of two years of the five-year term of the lease. Trial Term awarded plaintiff damages and the Appellate Division affirmed, two Justices dissenting.

Plaintiff first took possession of the land in question in 1941 from the then owner, Eugene Higgins. In 1947 the premises began to be used as a parking lot, plaintiff subletting the property to one Kane. Higgins died in 1948 and defendant, as testamentary trustee, took title **[****6]** to the property. After the expiration of plaintiff's lease on May 1, 1949, defendant began negotiations for the sale of the property with the City of New York, the Board of Education having notified the Board of Estimate that the property was desired for a public school playground. That communication of the Board of Education was on the Board of Estimate's calendar of December 8, 1949, and the matter was then referred to the City Planning Commission, the director of real estate, and the director of the budget for report. Desultory negotiations then followed with nothing being accomplished. On or about January 22, 1952, the defendant trustee had discussions concerning the status of the property with members of its own organization and its attorneys. At that time it was pointed out in the discussion that it might be a year or two before the city would acquire it, and that, therefore, rather than operate the property at a substantial **[***539]** loss, the defendant, as trustee, was obligated to secure the best price by waiting and, in the meantime, to enter into a lease with the tenant which would pay real estate taxes and insurance. The result was that on March 6, 1952 defendant **[****7]** notified the city that it intended to enter into a lease and inquired as to the city's interest. Negotiations then broke off. Thereafter, on April 29, 1952, plaintiff, with knowledge of the foregoing negotiations, and defendant entered into a lease, which contained, among others, the following two clauses:

"Sixth: Should the hereby demised premises or any part thereof be condemned for public use, then and in that event, **[*113]** upon the condemnation of the same for such public use, this lease shall at the option of the Landlord become null and void and the term cease with the same force as if the term herein had fully expired on the date when possession shall be required, anything herein contained to the contrary notwithstanding. The Tenant shall not be entitled to any part of the award or to any apportionment thereof."

"Twelfth: The said Landlord doth covenant that the said Tenant on paying the said rent and performing the covenants aforesaid, shall and may peaceably and quietly have, hold and enjoy the said demised premises for the term aforesaid."

On January 20, 1953, the city contacted the defendant to inquire whether it would be willing to sell the property. This resumption **[****8]** of negotiations was commenced by the city as a result of the pressure brought by various civic groups to acquire the property for playground purposes in conjunction with Public School 75. The defendant, in view of the continuing operating loss, obtained an appraisal of the property, which was $ 132,000. In February of 1953, the city offered $ 135,000, which the defendant accepted and on March 16, 1953 defendant sent the city a copy of the proposed contract of sale along with a copy of the outstanding lease to the plaintiff. On March 18th, the city rejected the contract as drawn and returned the copy of the lease, stating that inasmuch as the property was to be used for a playground it must be free and clear of any incumbrances. The city then introduced the defendant, for the first time, to an agreement whereby the **[**786]** city would be given an option to purchase any condemnation award to which the defendant would be entitled upon condemnation. Such procedure is specifically authorized in section B15-30.0 of the Administrative Code of the City of New York, which section appears in title B of chapter 15 of the Administrative Code entitled "*Consolidated Condemnation Procedure* **[****9]** ". The agreement proposed by the city, which was entered into, provided that the city could purchase the assignment of the award for $ 135,000. On December 17, 1953, the Board of Estimate held a meeting and at that time unanimously resolved to authorize the corporation counsel's office to institute condemnation **[***540]** proceedings and exercised the option to purchase the award in condemnation. The minutes of this meeting of the Board of Estimate clearly disclose that the acquisition of the property **[*114]** was for a "much sorely-needed playground." The condemnation authorized also took in three other damage parcels adjacent to the parking lot, one of which was owned by a party other than the defendant. In April, 1954 title vested and the city applied in the Supreme Court for an order condemning the premises, and on April 30, 1954 an order granting such relief was made and entered in the New York County Clerk's office.

Plaintiff then sued defendant for breach of the covenant of quiet enjoyment contained in the lease alleging: "17. The defendant wrongfully induced the City of New York to acquire the premises by condemnation in violation of the covenant of quiet enjoyment **[****10]** contained in the lease between the plaintiff and the defendant."

In answering defendant's demand for a bill of particulars, the plaintiff stated that: "7. The defendant's acts, which induced the City of New York to acquire the premises by condemnation, were the option to sell to the city for $ 135,000 any award to which defendant would be entitled on condemnation of the premises and such other of defendant's acts relating to said option, of which the plaintiff has no personal knowledge * * *."

As we view the case, the fundamental issue presented is whether the landlord breached the covenant of quiet enjoyment by co-operating with the city to the extent of granting the city an option, pursuant to section B15-30.0 of the Administrative Code, to purchase for $ 135,000 its rights in the condemnation award in the event that the city thereafter condemned the property. We think it did not.

A covenant of quiet enjoyment is not breached by the landlord when the tenant is evicted by the sovereign's exercise of its power to take by eminent domain, inasmuch as such a covenant goes only to the lessor's title, and does not warrant against those fundamental liabilities to action on the part of **[****11]** the sovereign power which lie behind all private titles (see Goodyear Shoe Mach. Co. v. Boston Term. Co., 176 Mass. 115, per Holmes, Ch. J.). The rights of the lessee in the land owned by the lessor are held as the property of all citizens is held, subject to the exercise of the power of eminent domain by the sovereign and the exercise of that power by the sovereign does not constitute a breach of the covenant of quiet enjoyment by the landlord (see Kip v. New York & H. R. R. Co., 67 N. Y. 227, 229).

[*115] **[***541]** In the present case no one can deny that the tenant was evicted by reason only of the exercise of the sovereign power of eminent domain and not by reason of the option given to the city by the landlord. The grant by the landlord of the option to purchase its rights in the condemnation award, in the event that the city thereafter condemned the property, did not constitute an interference by the landlord with the tenant's possessory rights, did not accomplish an eviction of the tenant and did not lead necessarily or inevitably **[**787]** to an eviction of the tenant by the sovereign. The tenant's possessory rights were not interfered with or destroyed **[****12]** until the land in question was subsequently condemned. Nor did the grant of the option to the city empower or enable the city to evict the tenant. The power of eminent domain possessed by the city, and through which the tenant was evicted, was not in any wise dependent upon the city's obtaining an option from the landlord. It is true that by granting the option the landlord "cooperated" with the city, that is, the landlord assisted the city by placing it in a position to know, in advance, the cost to it of acquiring the landlord's property by eminent domain. However, before holding that that type of co-operation creates an exception, in favor of the tenant, to the rule that an eviction resulting from the exercise of the sovereign power of eminent domain does not render a landlord liable for a breach of the covenant of quiet enjoyment, we would have to find some clear expression of intention to that effect in the lease. This must be, for to hold that the giving of the option to purchase renders the landlord guilty of a breach of the covenant of quiet enjoyment would be to render ineffective the legislative action in enacting section B15-30.0 of the Administrative Code in every **[****13]** case where there is present a leasehold interest. No property owner would be willing to follow such procedure for he would be buying himself a potential lawsuit brought by his leaseholding tenants. A great portion of New York City property is under lease and to put an end to or impair this common practice of the city, which serves the useful function of enabling the city to ascertain, with a reasonable degree of certainty, the amount of money which will have to be expended in order to obtain the parcels of land which it seeks, would be to cause great harm to the city.

We find no such clear expression of intention to that effect in the lease before us.

[*116] In paragraph "SIXTH" of the lease the parties expressly agreed that in the event of condemnation the "lease shall at the option of the Landlord become null and void and the term cease with the same force as if the term * * * had fully expired on the date when possession shall be required, anything herein contained to the contrary notwithstanding." The lease itself does not define what is meant by condemnation. Nevertheless, it is basic that, unless a contract provides otherwise, the law **[***542]** in force at the time **[****14]** the agreement is entered into becomes as much a part of the agreement as though it were expressed or referred to therein, for it is presumed that the parties had such law in contemplation when the contract was made and the contract will be construed in the light of such law (see 17 C. J. S., Contracts, § 330). Applying that rule of construction to the facts of this case, if the procedure followed by the defendant in our present case is considered to be condemnation or a mode of condemnation, which the city is authorized to follow by the Administrative Code of the City of New York, then the plaintiff in agreeing to the lease must be presumed to have agreed to lose any leasehold interest which he possessed when the provided-for statutory methods of condemnation were employed. As we stated earlier, the procedure followed by the city and the defendant, i.e., the purchase of the award, is specifically set forth in section B15-30.0 of the Administrative Code, which section appears in title B of chapter 15 of the Administrative Code entitled "*Consolidated Condemnation Procedure*", and clearly must be considered to be a mode of the procedure of condemnation. Therefore, the city in arranging **[****15]** for the purchase of the award was actually following a mode of condemnation.

The tenant specifically agreed *in unambiguous terms* that in the event of condemnation the lease should become null and void at the option of the landlord and that he, the tenant, would not be entitled **[**788]** to any part of the condemnation award. Condemnation took place and the lease was terminated. By the present action the tenant seeks to avoid the effect of his agreement that he would not be entitled to any part of the condemnation award. In answer to that attempt, we can only repeat that the tenant's eviction was the result of the sovereign's exercise of its power to take by eminent domain and that a covenant of quiet enjoyment is not breached by the landlord **[*117]** when the tenant is evicted by such exercise. There is no forfeiture by the tenant of any interest save that to which he has agreed and to which he must be held.

For the foregoing reasons, we conclude that the defendant did not breach the covenant of quiet enjoyment and that the complaint should be dismissed.

The judgment of the Appellate Division and that of Trial Term should be reversed and the complaint dismissed, with **[****16]** costs to appellant in all courts.

Dissent by: DESMOND

Dissent

Desmond, J. (dissenting). Plaintiff's judgment for damages is based on a Trial Term finding, affirmed by the Appellate Division, that the appellant breached a covenant of quiet enjoyment contained in a lease by defendant to plaintiff of vacant land in New York City used by plaintiff as a parking lot. The **[***543]** lease by its terms ran for five years from May 1, 1952, but on May 1, 1954 plaintiff was deprived of all rights under the lease when the City of New York acquired the premises in condemnation proceedings. The facts hereinafter set forth in more detail justified the trial court's finding that defendant itself had induced and brought about the condemnation proceeding. It can hardly be doubted that a landlord who leases land for a term of years and then turns around and makes an arrangement such as is hereinafter described and whereby the tenant is ousted, violates both the letter and the spirit of the quiet enjoyment covenant. That covenant in the lease under consideration read as follows: "The said Landlord doth covenant that the said Tenant on paying the said rent and performing the covenants aforesaid, shall and **[****17]** may peaceably and quietly have, hold and enjoy the said demised premises for the term aforesaid."

Plaintiff's occupancy of this land began in 1941. In 1947 he took from the then owner, one Higgins, a two-year lease. Higgins died in 1948 and defendant as a testamentary trustee took title to the premises. During the term of that earlier or 1947 lease New York City officials had shown some interest in the possible purchase of the land for use as a playground appurtenant to an adjoining public school. Defendant trustee, after it took title, had some inconclusive negotiations with the city authorities looking to such a sale but, when these did not come to a head, defendant, as of May 1, 1952, made the lease above referred to with plaintiff who had remained in possession **[*118]** without a lease from 1949 to 1952. In January, 1953, 9 or 10 months after the making of the second lease containing the quiet enjoyment covenant, the city inquired from defendant whether the property was for sale and, when defendant replied that it was, the city in March, 1953 made an offer to purchase it for $ 135,000, a little more than the amount of an appraisal which had been made for defendant. Defendant **[****18]** indicated agreement, sent to the city a proposed contract of sale at that price, and notified the city that the sale would be subject to plaintiff's lease. The city replied that it could not sign the contract unless and until defendant obtained a release of the rights of this plaintiff as tenant. Defendant did nothing toward getting such a release. Next, the city notified defendant that the city would be agreeable to an arrangement whereby the city would obtain title through condemnation proceedings but would be given, by defendant, an option to purchase for **[**789]** $ 135,000 an assignment of the award that would be made to defendant in the condemnation proceedings. That arrangement was carried out completely with the result that the city acquired the property for the price of $ 135,000 as originally agreed upon. But the tenant lost all its rights to occupancy or compensation since his 1952 lease contained a provision that if the leased premises should be taken **[***544]** by condemnation, the lease should terminate as if its term had expired, and that the tenant in that event should not be entitled to any part of the condemnation award.

There is no claim here that the arrangement **[****19]** voluntarily made between defendant and the city was invalid as between those two parties (see Administrative Code of City of New York, § B15-30.0). The theory on which plaintiff has recovered is that regardless of such validity the landlord breached the lease and violated plaintiff's rights by co-operating in and agreeing to an arrangement (which the landlord did not have to make) whereby there was a sale of the property at a previously agreed price with complete destruction of the tenant's rights, even though the arrangement took the form of a condemnation proceeding with a prior agreement that the owner's award should be sold back to the city at a price agreed on in advance. "The main object of a covenant for quiet enjoyment is to protect the lessee from the lawful claims of third persons having a title paramount to the lessor; but such a covenant * * * **[*119]** provides also for the protection of the lessee against the unlawful entry of the lessor himself" (*Mayor of City of New York v. Mabie, 13 N. Y. 151, 156*; see 2 McAdam on Landlord and Tenant [5th ed.], pp. 1528, 1570, 1571). The covenant can mean no less than that the landlord will "abstain from interfering **[****20]** with the right" granted by him to the tenant (*Mabie* case, *supra, p. 157*). When the landlord despite the lease and the covenant presumes to exercise dominion over the property by his own re-entry or by granting rights to others inconsistent with the lease, the landlord breaches the covenant. Under defendant's theory, a landlord could make a lease for a long period, include therein a covenant for quiet enjoyment, permit the tenant to enter and establish himself in the property and then turn around and act toward the property as if there were no lease at all. And all this without incurring any obligation to reimburse the tenant for his loss.

The landlord's defense to this suit can be summed up in a sentence from its brief: "No tenant can recover damages from his landlord merely because a municipality condemns the property which is the subject of his lease". But this plaintiff has been awarded damages not because the municipality exercised its power of eminent domain, but because the landlord induced and made possible the bringing of condemnation proceedings by agreeing to what was, in effect, a voluntary sale. The difference is between an involuntary transfer of the property **[****21]** by the landlord and a carefully worked out bilateral agreement which, although in form a taking by condemnation, was in fact a voluntary sale of the property to the city. The taking of this property by the city was not in hostility to defendant's title but was the carrying out of a bargain. The naked fact that title passed pursuant to a condemnation decree does not invalidate the finding made here that it was the landlord's agreement which resulted **[***545]** in the ouster of plaintiff. An illustrative case is *Lindwall v. May (111 App. Div. 457)* where it was held that a tenant could recover damages for a breach of a covenant of quiet enjoyment although the building had actually been torn down by the municipal authorities as unsafe. It was the landlord's neglect that had produced the violation which in turn produced the lawful governmental act of destroying the property which was the subject of the lease. The Appellate Division held in the *Lindwall* case (*supra*) that the **[*120]** destruction of the premises and the consequent **[**790]** eviction would not have occurred had the landlord performed its duty. In the present case the landlord's duty was to protect **[****22]** the rights which it had granted to plaintiff. Instead of doing so it agreed to a method of ousting him. *Kip v. New York & H. R. R. Co. (67 N. Y. 227)* is not in point here since it deals with the right to condemn of a tenant who had the power of eminent domain. *Goodyear Shoe Mach. Co. v. Boston Term. Co. (176 Mass. 115)* is likewise without pertinence here, since the landlord in that case merely exercised its own power of condemnation.

If there is any doubt as to the meaning of this lease, that doubt "must be resolved against the landlord and in favor of the tenant" (*455 Seventh Ave. v. Hussey Realty Corp., 295 N. Y. 166, 172)*. That settled rule of lease construction should be most strongly applied when the result of a construction in favor of the landlord would be to permit the landlord to forfeit the tenant's valuable remaining term without compensation.

Affirmance of this judgment would not impair or affect the city's practice of arranging in advance an assignment of awards in condemnation proceedings. Affirmance will merely force landlords to perform their covenants.

The measure of damages here applied, that is, the value of the unexpired term less **[****23]** the rent reserved, was correct (*Mack v. Patchin, 42 N. Y. 167*).

The judgment should be affirmed, with costs.

End of Document

Dorrance v. United States

United States Court of Appeals for the Ninth Circuit

April 9, 2015, Argued and Submitted, Pasadena, California; December 30, 2015, Amended

Nos. 13-16548, 13-16635

Reporter
809 F.3d 479 *; 2015 U.S. App. LEXIS 22820 **; 116 A.F.T.R.2d (RIA) 2015-6992

BENNETT DORRANCE; JACQUELYNN DORRANCE, Plaintiffs-Appellees/Cross-Appellants, v. UNITED STATES OF AMERICA, Defendant-Appellant/Cross-Appellee.

Prior History: **[**1]** Appeal from the United States District Court for the District of Arizona. D.C. No. 2:09-cv-01284-GMS. G. Murray Snow, District Judge, Presiding.

Dorrance v. United States, 807 F.3d 1210, 2015 U.S. App. LEXIS 21287 (9th Cir. Ariz., Dec. 9, 2015)
Dorrance v. United States, 877 F. Supp. 2d 827, 2012 U.S. Dist. LEXIS 94107 (D. Ariz., 2012)

Disposition: REVERSED.

Summary:

SUMMARY*

Tax

The panel reversed the district court's denial of the government's motion for summary judgment in a tax refund action involving the calculation of the cost basis of stock received through demutualization.

Taxpayers received and then sold stock derived from the demutualization of five mutual insurance companies from which they had purchased life insurance policies. Taxpayers initially asserted a zero cost basis in the stock and paid tax on the gain, but later claimed a full refund. The district court held that taxpayers had a calculable basis in the stock and were therefore entitled to a partial refund.

The panel held that the Internal Revenue Service properly denied the refund claim and that the district court had erred in its cost basis calculation because taxpayers had not met their burden of showing that they had in some way paid for the stock.

The panel explained that under the life insurance **[**2]** policies, taxpayers were entitled to certain contractual rights such as a death benefit, the right to surrender the policy for cash value, and annual dividends. After demutualization, taxpayers retained their contractual interests and continued to pay the same premiums. Taxpayers as policyholders also had certain membership rights for which they received nothing upon demutualization. The stock they received was due to the legal requirement that the insurance companies produce a "fair and equitable" allocation of each company's surplus at the time of demutualization, but evidence showed that this was not based on some premium value that taxpayers had paid in the past.

Judge M. Smith dissented. He agreed with the district court's cost basis calculation, and disagreed with the majority's view that taxpayers paid nothing for their membership rights.

Counsel: M. Todd Welty (argued) and Laura L. Gavioli, McDermott Will & Emery LLP, Dallas, Texas, for Plaintiffs-Appellees/Cross-Appellants.

Kathryn Keneally, Assistant Attorney General; Tamara W. Ashford, Principal Deputy Assistant Attorney General; Gilbert S. Rothenberg, Jonathan S. Cohen, and Judith A. Hagley (argued), Attorneys, United States Department **[**3]** of Justice, Tax Division, Washington, D.C., for Defendant-Appellant/Cross-Appellee.

Judges: Before: Stephen Reinhardt, M. Margaret McKeown, and Milan D. Smith, Jr. Circuit Judges. Opinion by Judge McKeown. Dissent by Judge Milan D. Smith, Jr.

Opinion by: M. Margaret McKeown

Opinion

* This summary constitutes no part of the opinion of the court. It has been prepared by court staff for the convenience of the reader.

[*481] AMENDED OPINION

McKEOWN, Circuit Judge:

This appeal requires us to "return to the very basics of tax law" and consider whether taxpayers had a cost basis in assets that they later sold, but for which they paid nothing. *Washington Mut. Inc. v. United States, 636 F.3d 1207, 1217 (9th Cir. 2011)*. The specific question we address is whether a life insurance policyholder has any basis in a mutual life insurance company's membership rights. This issue, one of first impression in our circuit, arises out of a trend in the late 1990s and early 2000s towards the "demutualization" of mutual life insurance companies. As many mutual insurance companies transformed into stock companies, the surplus resulting from the sale of shares in the company was divided among current policy holders, often in the form of stock.

Bennett and Jacquelyn Dorrance received and then sold stock derived from the demutualization of five mutual life insurance companies from which they had purchased policies. The Dorrances initially asserted a zero **[**4]** cost basis in the stock and paid tax on the gain. They later claimed a full refund on the taxes they paid upon on the sale of the stock, either because the stock represented a return of previously paid policy premiums or because their mutual rights were not capable of valuation and, therefore, the entire cost of their insurance premiums should have been counted toward their basis in the stock. The government takes the position that the Dorrances are not entitled to any refund; since they paid nothing for their membership rights, their basis was zero. The district court held that the Dorrances had a calculable basis in the stock, albeit not at the level the taxpayers claimed, and thus they were entitled to a partial refund from the Internal Revenue Service ("IRS"). We disagree. Taxpayers who sold stock obtained through demutualization cannot claim a basis in that stock for tax purposes because they had a zero basis in the mutual rights that were extinguished during the demutualization.

BACKGROUND

A. MUTUAL INSURANCE COMPANIES

The first life insurance company in America was a mutual company called the Presbyterian Minister's Fund, organized in 1759 in Philadelphia.[1] For centuries, mutual **[**5]** insurance companies have provided a structure for collecting policyholder premiums and spreading risk and surplus among policyholders, while maintaining policyholder ownership of the company. Mutual insurance companies are distinct from stock companies in that they are owned by the policyholders, not by stockholders. *See* Edward X. Clinton, *The Rights of Policyholders in an Insurance Demutualization*, 41 Drake L. Rev. 657, 659 (1992). To ensure that they can pay all of the contractual benefits, these mutual insurance companies generally charge slightly higher rates than other life insurance providers. Surplus is returned to the policyholders in dividends. For decades (and even more than a century for some mutual companies) policyholders joined, became members, and terminated their policies without getting anything back for membership rights.

Starting in the middle of the twentieth century and increasing through **[**6]** the 1980s, **[*482]** the mutual model became less economically advantageous when compared to stock companies. *Id. See also* Paul Galindo, *Revisiting the 'Open Transaction' Doctrine: Exploring Gain Potential and the Importance of Categorizing Amounts Realized*, 63 Tax L. 221, 226 (2009). The economic advantage of stock companies comes, in large part, from the fact that they can raise capital by selling shares, whereas mutual companies are able to raise capital only by increasing the number of policies sold or by reducing costs. Additionally, stock companies have a greater capacity to diversify, which provides an additional layer of financial stability. *See* Clinton, *supra*, at 667.

In response to the challenges faced by mutual insurance companies, in the mid-to-late 1990s many states changed their insurance laws to permit "demutualization" of mutual insurance companies. Demutualization entails the legal transformation of a mutual company into a stock company. *See* Jeffrey A. Koeppel, The State of Demutualization, at v (2d ed. 1996). As a consequence, by the late 1990s and early

[1] Even earlier, in 1752, Benjamin Franklin, who had likely become aware of similar innovations in England, formed the Philadelphia Contribution for the Insurance of Houses From Loss by Fire, often characterized as the first mutual insurance company. *See* The Philadelphia Contributionship, *Company History* (2015), http://www.contributionship.com/history/index.html.

2000s, many mutual insurance companies had transformed into stock companies.

The rapid shift toward demutualization was made possible only by this **[**7]** widespread change in state insurance law. Clinton, *supra*, at 674. Although state laws vary, including in the scope of regulatory oversight, the demutualization process occurred under operation of law and was monitored by external insurance regulators. *Id.* at 665. Because policyholders exert only weak influence over the mutual company's governance (each policyholder has only one vote, out of possible thousands, regardless of the size of the policy), external regulators focused on ensuring a fair and equitable legal transformation of the insurance companies. *Id.* at 678.

B. The Dorrances' Mutual Life Insurance Policies

Bennett Dorrance is the grandson of the founder of the Campbell Soup Company. At the time the Dorrances purchased life insurance policies from five mutual insurance companies[2] in 1996[3], their net worth was approximately $1.5 billion. They bought the policies to cover estate tax for their heirs. Over time, the Dorrances paid premiums totaling $15,265,608. While that sum is definitely substantial, the face value of the policies totaled just under $88 million, such that they would have received a huge contractual payout upon death.

The Dorrances' contractual rights under the policies entitled them to (1) a death benefit; (2) the right to surrender the policy for "cash value"; and (3) annual policyholder dividends representing the policyholder's portion of the company's "divisible surplus." As policyholders, they also had certain membership rights. Specifically, they were entitled to a portion of any surplus in the event of a solvent liquidation and to certain voting rights. The Dorrances' membership rights in the mutual **[*483]** insurance companies were not transferable or separable from the insurance policy. If the policies **[**9]** terminated, so too would the membership rights, without any rebate or additional compensation. Voting and other membership rights were governed by state law and company charter.

In 2000 and 2001, each of the insurance companies from which the Dorrances bought policies demutualized. Post-demutualization, the Dorrances no longer held any mutual membership rights, but they retained their contractual interests under the insurance policies and continued to pay the same premiums.

Government regulators (both in the United States and Canada) required the insurance companies to produce a "fair and equitable" allocation of the company's surplus at the time of demutualization. Mutual insurance companies complied with this requirement in a variety of ways, but the companies in question here opted to issue stock to their policyholders.

When determining how many shares of stock to distribute to each policyholder, the insurance companies calculated (1) a fixed component for the loss of voting rights, as every policyholder was entitled to a single vote regardless of policy size, and (2) a variable component for the loss of other membership rights, which was calculated based on the policyholder's past **[**10]** and projected future contributions to the company's surplus. As the government's expert report explained, each company used a different allocation calculation to arrive at a distribution that was "fair and equitable" to policyholders. MetLife, for example, "aimed for around 20%" for the fixed portion, but stated this was a "general target." Sun Life did not consider policyholders' contribution to surplus in its allocation calculation, but rather looked at the cash value and annual premiums of eligible policies.

Prior to demutualization, the insurance companies each obtained a ruling from the IRS that the stock ownership company resulting from the demutualization qualified as a tax-free organization under Internal Revenue Code, I.R.C. § 368.

Upon demutualization, the Dorrances received 58,455 shares in Prudential, 3,209 shares in Sun Life, 1,601 shares in Phoenix, 5,039 shares in Principal, and 2,721 shares in MetLife. At the time of receipt, the market value of the stock derived from these policies totaled $1,794,771. As the government's expert report explained: "Some may think that the cash paid out in

[2] The companies are: Prudential Insurance Company; Sun Life Assurance Company; Phoenix Home **[**8]** Life Mutual Insurance Company; Principal Life Insurance Company; and Metropolitan Life Insurance Company ("MetLife").

[3] By 1996, many states already allowed demutualization or were in the process of changing their laws. Demutualization was permitted under New York and Iowa law (governing MetLife, Phoenix, and Principal). *See* NY Ins. Law § 7312 (McKinney 2011); Iowa Code § 508B.1 et seq. The New Jersey demutualization statute (governing Prudential) became effective in July 1998. N.J. Stat. Ann. 17:17C-1. In 1999, Canadian regulations (governing Sun Life) were revised to allow for demutualization. Mutual Company (Life Insurance) Conversion Regulations SOR/99-128 s.14 (Can.).

demutualization comes from the distribution of positive surplus of the mutual company; however, **[**11]** such is not the case. The cash actually comes from new stockholders which subscribe to the IPO [initial public offering] . . . ."

In 2003, the Dorrances sold all of the stock for $2,248,806. On their 2003 tax return, in compliance with IRS policy, the Dorrances listed their basis in the stock as zero, reported the $2,248,806 as capital gain, and paid the tax due on that gain. *See* Rev. Rul. 71-233, 1971-1 C.B. 113; Rev. Rul. 74-277, 1974-1 C.B. 88.

C. Prior Proceedings

By 2007, the Dorrances had a change of heart. They filed a tax refund claim with the IRS, in which they argued that they owed no taxes on the stock sale because it represented a return on previously-paid insurance policy premiums. The IRS did not issue a final determination on the 2007 claim, so the Dorrances filed a complaint in district court. The IRS argued that the Dorrances had a zero basis in their stock because the life insurance premiums that they paid were not in exchange for membership rights in the life insurance policies. The district court denied the cross-motions **[*484]** for summary judgment, ruling that there was a calculable basis in the stock, and set the case for trial to determine how the basis should be calculated.

The district court held a two-day bench trial, which featured **[**12]** expert testimony from both sides regarding the basis calculation. The court rejected the Dorrances' argument that the "open transaction" doctrine, espoused by the Court of Federal Claims, applied to their refund request.[4] It also rejected the government's zero basis argument. Instead, the district court ruled that the Dorrances had "paid something for the [membership] rights because they paid premiums for policies that included both policy rights and mutual rights" and that their basis was calculable.

The district court calculated the Dorrances' basis in the stock using the following formula: (1) the initial public offering ("IPO") value of the fixed shares allocated to the Dorrances in 2003, plus (2) 60% of the IPO value of the variable shares. Applying this formula, the court found **[**13]** that the Dorrances were required to pay taxes on $1,170,678, rather than on the full $2,248,806 value of the stock. Because in 2003 the Dorrances had paid taxes based on a zero basis calculation in the stock, the district court found that they were entitled to a refund.

Both parties appeal the adverse portions of the judgment.

Analysis

The crux of this case is how to calculate the basis of stock received through demutualization. The question of basis in the stock is a mixed question of law and fact that "require[s] consideration of legal concepts and involve[s] the exercise about the values underlying legal principles [and is] reviewable de novo." *Smith v. Comm'r, 300 F.3d 1023, 1028 (9th Cir. 2002)* (citing *Mayors v. Comm'r, 785 F.2d 757, 759 (9th Cir. 1986))*. The parties do not dispute the district court's factual findings. Instead, their divergence of views stems from the legal conclusions that follow.

As the taxpayers, the Dorrances bear the burden of establishing basis, and "[t]he fact that basis may be difficult to establish does not relieve [them] from [t]his burden." *Coloman v. Comm'r, 540 F.2d 427, 430 (9th Cir. 1976)*. Because they failed to establish that they had a basis in the membership rights, we afford the basis utilized by the IRS a presumption of correctness—even where, as here, that figure is zero. *Id.* The Supreme Court explained long ago in a similar **[**14]** context that "[t]he impossibility of proving a material fact upon which the right to relief depends simply leaves the claimant upon whom the burden rests with an unenforceable claim, a misfortune to be borne by him, as it must be borne in other cases, as the result of a failure of proof." *Burnet v. Houston, 283 U.S. 223, 228, 51 S. Ct. 413, 75 L. Ed. 991 (1931)*.

A. The Structure of Mutual Insurance Policies

In analyzing the insurance policies, it pays to bear in mind that, "[a]s an overarching principle, absent specific provisions, the tax consequences of any particular transaction must reflect the economic **[*485]** reality."

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[4] The district court declined to follow the Court of Federal Claims' approach that "the value of the ownership rights [in mutual rights are] not discernible" and that, therefore, the full basis of the policy should apply under the rarely-used "open transaction" doctrine. *Fisher v. United States, 82 Fed. Cl. 780, 799 (2008)* *aff'd*, ***333 F. App'x 572 (Fed. Cir. 2009)***. In light of our decision, it is unnecessary to address whether the "open transaction" doctrine is applicable to this situation.

Washington Mut. Inc., 636 F.3d at 1217 (citing Kraft, Inc. v. United States, 30 Fed. Cl. 739, 766 (Fed. Cl. 1994); United States v. Winstar Corp., 518 U.S. 839, 863, 116 S. Ct. 2432, 135 L. Ed. 2d 964 (1996)). The reality here is that the Dorrances acquired the membership rights at no cost, but rather as an incident of the structure of mutual insurance policies.

The logic of this conclusion is simple—when the Dorrances purchased their mutual insurance policies in 1996, the premiums they paid related to their rights under the insurance contracts, not to collateral membership benefits such as voting. Under the insurance contract, policyholders paid premiums for the following "contract rights": (1) a death benefit; (2) the right to surrender the policy for a "cash value"; and (3) annual policyholder dividends representing the policyholder's portion **[**15]** of the company's "divisible surplus."

Separate from the contract rights, through operation of law and the company charter, each policyholder had a right to vote on certain matters, such as the election of the board of directors. That vote was restricted to one vote per policyholder, regardless of the size or face value of the policy. In addition, in the very unlikely event of a liquidation, the policyholder was entitled to any surplus from that liquidation.[5] At trial, the government expert stated that he did not know of a single mutual insurance company that had ever had a solvent liquidation, a point echoed by the MetLife representative. This bundle of rights—derived from operation of law—is referred to as "mutual rights" or "membership rights."[6] These rights are not transferable and upon termination of a policy, the policyholder receives nothing for any membership rights.

The difference between contract rights and membership rights is critical to resolution of this case. The premiums paid covered the rights under the insurance contract, not any membership rights. Notably, the policies themselves generally make no reference to any such membership rights. In other words, premium payments go toward the actual cost of the life insurance benefits provided. The mutual companies did not count membership rights as having a cost (apart from minimal administrative costs, if there is a policyholder vote), so they did not charge policyholders for such rights.

The government's expert, American Academy of Actuaries member Ralph Sayre, testified that mutual companies calculate premiums based solely on the expected cost of providing contractual insurance benefits. This calculation process is "very precise in actuarial circles" and "there just is no portion of the premium or charge for membership rights." He linked this analysis to the obvious: "[U]sually you don't pay [for] something if . . . you aren't charged for it." This explanation is consistent with the Supreme Court's description of what the premium pays for: "It **[**17]** is of the essence of mutual insurance that the excess in the premium over the actual cost as later ascertained shall be returned to the policy holder." Penn Mut. Life Ins. Co. v. Lederer, 252 U.S. 523, 525, 40 S. Ct. 397, 64 L. Ed. 698, T.D. 3046 (1920).

In referencing "ownership rights," by which he meant membership rights, the **[*486]** description by the Dorrances' expert was essentially in line with Sayre's conclusion: "The ownership rights were not separate from the policy rights and could not be sold. The cost associated with acquiring ownership rights cannot be established exclusively through premium payments."

Consistent with the general practice for mutual insurances companies, the companies involved in this case did not charge the Dorrances for their membership rights. This point was underscored by Mr. Dorrance's testimony that, at the time he bought the policies, he actually understood that he would pay *less* for a policy from a mutual insurance company than he would for one from a stock company. *See* S. Bancorporation, Inc. v. United States, 732 F.2d 374, 377 (4th Cir. 1984) (rejecting refund claim where the taxpayer "introduced no evidence to prove that it intended to pay an enhanced value for the [asset] *at the time of sale*") (emphasis in original). It was no surprise then, that in 2003, when the Dorrances filed their tax returns following the sale of the **[**18]** stock derived from demutualization, they listed their basis as zero.

B. The Effect of Demutualization

The membership rights were assigned a monetary value at the time of the exchange only as a consequence of

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[5] Prior to demutualization, solvent liquidation in a mutual insurance company was unlikely because mutual insurance companies are highly regulated entities that operate conservatively to remain as a "going concern" for their policyholders.

[6] The moniker "mutual rights" more accurately describes what is at issue, though we **[**16]** adopt the term "membership rights" as used by the parties.

the demutualization process. The error of the Dorrances and the district court was to assume that the value received upon demutualization was linked with some premium value paid by the policyholders in the past. But the stock the Dorrances received in exchange for the membership rights cannot be understood as a partial return on their past premium payments and it is well understood that policyholders do not contribute capital to the companies.

By the time of the demutualization, the lion's share of the surplus that fed valuation of the newly issued stock could not be traced to payments made by current policyholders. Nearly all of the surplus held by the companies at that time was attributable to former policyholders, not current policyholders like the Dorrances. For example, at the time of demutualization, less than 10% of the Sun Life surplus was attributable to current policyholders; premiums paid by former policyholders accounted for over 90% of the surplus. Thus, the value at **[**19]** demutualization was not derived from something paid for by the Dorrances.

Sayre explained the situation as follows:

> The demutualization is not a result of [] current policyholders having done something different from the other previous millions of policyholders, but is a result of outside influences, such as tax policy, economic conditions or competitive pressures. The current policyholders are fortunate to be policyholders at the time of demutualization but their value received is a result of the new stockholders who are willing to pay them in order to receive their membership benefits for the purpose of what they can do with them in the future.

This anomaly prompted one insurance company official involved in this case to refer to the receipt of stock as a "windfall" for current policyholders. This characterization was echoed by the Sixth Circuit, which referred to demutualization proceeds as "a pot of money that no one expected or even envisioned." Bank of New York v. Janowick, 470 F.3d 264, 266 (6th Cir. 2006); *see also* Douglas P. Faucette & Timothy S. Farber, *National Insurance Act of 2007 & Demutualization of Insurers: The Devil is in the Details*, 58 Fed'n Def. & Corp. Couns. Q. 109, 127 (2007) (noting that policyholders "receive payouts that **[**20]** they had not expected, consciously bargained for, or purchased. Simply **[*487]** put, distribution of the surplus amounts to 'a windfall resulting from the increase in the value of that policy arising from its unforseen restructuring.'" (citation omitted)).

Following the transfer of stock, it was business as usual in terms of the contract rights. After demutualization, the Dorrances' insurance premiums remained level—reinforcing the fact that they had not been paying a "premium" for any membership rights in the first place. For example, the premium history for Principal Financial Group shows that the Dorrances' premium was $124,450 both before and after the 1999 demutualization. This transition occurred under the oversight of regulators who were charged with ensuring that policyholders were treated fairly during the demutualization process and who did not require a reduction in the premiums to sync with the loss of the now-claimed rights. The Dorrances continued to pay the same premiums and receive the same coverage. The stock exchange, for which they paid nothing, was the only aspect of the transaction related to membership rights.

The demutualizations themselves were structured as tax-free, **[**21]** meaning that the initial transaction by which the Dorrances received the stock did not trigger any taxable gain for the policyholders. As an exchange under I.R.C. § 354[7], the deal would not have been tax free if there was a gain upon the exchange. I.R.C. § 358(a)(1) (providing that the basis of property received under a § 354 exchange "shall be the same as that of the property exchanged"). In other words, the stock was a direct exchange for the lost membership rights.

Put another way, the basis in the new stock was the same as the basis in what was being exchanged—the membership rights. Hence, the companies told policyholders that the tax basis on the stock was "zero." For example, with regard to the receipt of stock, Phoenix explained in its Q&A document:

> If you receive common stock, you will not be taxed when you receive it. However, if you sell or otherwise dispose of your common stock, you will be taxed on the full amount of the proceeds you **[**22]** receive for the common stock. (Your tax basis in the common stock will be zero.)

The other companies alerted policyholders to the same thing: Sun Life advised that the "cost basis of these

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[7] I.R.C. § 354(a)(1) provides:

> No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

shares for tax purposes will be zero" and, after saying that the tax cost would be "zero," Principal Mutual stated that "if you later sell or otherwise dispose of your Common Stock, you will generally be taxed on the full amount of the proceeds of that sale or other disposition."

The insurance companies' advice to their policyholders comports with IRS rulings dating back to the 1970s. Those rulings stated that the policyholder's basis in mutual rights is zero. *See* Rev. Rul. 71-233, 1971-1 C.B. 113; Rev. Rul. 74-277, 1974-1 C.B. 88. Revenue Ruling 71-233 addresses the tax consequences to policyholders when they exchange their proprietary interests for preferred stock. Consistent with our explanation above—distinguishing between contract rights and membership rights (which are also referred to as proprietary rights), the IRS advised:

> Payment by each policyholder of the premiums called for by the insurance **[*488]** contracts issued by X represents payment for the cost of insurance and an investment in his contract but not an investment in the assets of X. His proprietary interest in the assets of **[**23]** X arises solely by virtue of the fact that he is a policyholder of X. Therefore, the basis of each policyholder's proprietary interest in X is zero.

Id.

Within the tax code, the transaction exchanging mutual rights for stock does not operate in a vacuum. Treating the premiums as payment for membership rights would be inconsistent with the Code's provisions related to insurance premiums. For example, gross premiums paid to purchase a policy are allocated as income to the insurance company; no portion is carved out as a capital contribution. *See* I.R.C. §§ 803(a)(1), 118. On the flip side, the policyholder is allowed to deduct the "aggregate amount of premiums" paid upon receipt of a dividend or cash-surrender value. I.R.C. § 72(e). No amount is carved out as an investment in membership rights. The taxpayer can't have it both ways—a tax-free exchange with zero basis and then an increased basis upon sale of the stock.

The district court skipped a critical step by examining the *value* of the mutual rights without evidence of whether the Dorrances paid anything to first acquire them. The basis inquiry is concerned with the latter question. The district court also erred when it estimated basis by using the stock price at the time **[**24]** of demutualization rather than calculating basis at the time the policies were acquired. The stock value post-demutualization is not the same as the cost at purchase.

We have previously explained that basis[8] "refers to a taxpayer's capital stake in an asset for tax purposes." Washington Mut. Inc., 636 F.3d at 1217 (citing In re Lilly, 76 F.3d 568, 572 (4th Cir. 1996)). "The taxpayer must prove what, if anything, he actually was required to pay . . . not what he would have been willing to pay or even what the market value . . . was." Better Beverages, Inc. v. United States, 619 F.2d 424, 428 (5th Cir. 1980). Here the Dorrances failed to do so.

Conclusion

This analysis brings us back to the Dorrances' burden and the economic realities of this case. Because the Dorrances offer nothing to show payment for their stake in the membership rights, as opposed to premium payments for the underlying insurance coverage, the IRS properly rejected their refund claim. The district court erred when it found after the bench trial that the **[**25]** Dorrances had shown they paid something for the membership rights. It should have found their basis to be zero.

REVERSED.

Dissent by: M. SMITH

Dissent

M. SMITH, Circuit Judge, dissenting:

For thousands of years, philosophers, theologians, and now physicists, have debated whether the earth was created *ex nihilo*, i.e., out of nothing. Whatever the answer to that question, there is little doubt that my colleagues in the majority have performed a notable miracle of their own in this case, by creating nothing out of something, i.e., *nihil ex aliquo*. Let us consider how this miracle was wrought by endeavoring to follow the

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[8] The Code provides that "[t]he basis of property shall be the cost of such property, except as otherwise provided in this subchapter and subchapters C (relating to corporate distributions and adjustments), K (relating to partners and partnerships), and P (relating to capital gains and losses)." I.R.C. § 1012(a). None of these exceptions apply here.

money.

[*489] I. The Government's Conditions to Demutualization

For what precisely did the Dorrances pay when they purchased policies from the mutual life insurance companies involved in this case? The majority contends that they paid only for a death benefit, the right to surrender the policy for a "cash value," and annual policyholder dividends representing their share of the company's "divisible surplus."

But if, as the majority contends, the Dorrances paid nothing for their membership rights, and did not contribute capital, then why did the several governmental regulators involved require, as a condition **[**26]** of demutualization of each of those insurance companies, that they issue stock to their policyholders to compensate them for the loss of those rights?

Since those who acquired shares in the newly publicly traded insurance companies during the IPO process paid cash for their interests, if the policyholders when the insurance companies were structured as mutual insurance companies had not paid for the surplus they later received in stock, then the value of the distributed shares ought to have remained as the insurance companies' working capital, and not been gratuitously gifted to policyholders. Neither the regulators nor the IPO investors would have tolerated such a gratuity.

But the stock distribution to the Dorrances, even if not specifically contemplated at the time they purchased the policies, was no gift. While insurance companies may be powerful, they do not have the power of creation *ex nihilo*. To the contrary, by the very nature of a mutual insurance company, all of its accumulated value comes from premiums paid by its owners, and the investment of those premiums. That is why, when allocating shares during the demutualization process, the insurance companies relied on a calculation **[**27]** of a fixed component based on the loss of voting rights and a variable component related to past and projected future contributions to surplus.

The majority relies on a statement by a government's expert: "Some may think that the cash paid out in demutualization comes from the distribution of positive surplus of the mutual company; however, such is not the case. The cash actually comes from new stockholders which subscribe to the IPO . . . ." Here, the Dorrances received stock, not cash. Of course, when they sold the stock, the cash that they obtained from the sale came from the buyers of the stock, and not from the insurance companies' bank accounts. But that is always true in a stock sale. Of course, that does not mean that all stock sales have a zero basis. Thus, the cited government expert's testimony is merely a truism. It provides no support for the majority's conclusion.

II. Accrued Surplus or Not?

Some context is in order. The majority mentions the IPO value of the Dorrances' stock: $1,794,771. The majority also unworthily mentions the Dorrances' net worth, which is not relevant to any issue before us. While the majority concedes that the premiums the Dorrances had paid to the **[**28]** insurance companies, which totaled $15,265,608, were "substantial," the majority is unimpressed by that figure because the face value of the policies was substantially larger than the premium. Of course, that is always the case in insurance. The relevance of the premiums paid to the question before us is that the distributed stock represents only 11.7% of the money the Dorrances had paid the insurance companies. That may not be far from the usual dividends paid on mutual insurance **[*490]** policies.[1]

However, the majority is quick to call that return of a small proportion of funds expended a "windfall." But while the majority asserts that one insurance company official so characterized the stock distribution, he actually took **[**29]** care to state that "windfall" was the company's characterization, not his. Moreover, the majority ignores the fact that every other insurance company representative deposed in this case either expressly rejected that characterization, or in one instance, did not know how to answer the question.

The majority credits testimony by the government's expert that the insurance companies charged the

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[1] The parties did not identify the dividend rates the policies at issue provided. Data for the Massachusetts Mutual Life Insurance Company, not one of the companies at issue, is publicly available. *See* Historical Dividend Studies from Massachusetts Mutual Life Insurance Company (2015), *available at* https://fieldnet.massmutual.com/public/life/pdfs/li7954.pdf (last visited Nov. 18, 2015). That data shows that a policy purchased after March of 1996 yielded a yearly dividend interest rate of between 8.4% and 7.9% between 1996 and 2003.

Dorrances premiums that were based solely on the expected costs of providing insurance benefits, using calculations that were "very precise in actuarial circles," such that "there is just no portion of the premium or charge for membership rights." That asserted precision is disproved by the existence of a surplus accrued within the insurance company. In fact, the majority elsewhere relies on testimony that, at the time of demutualization, "less than 10% of the SunLife surplus was attributable to current policyholders; premiums paid by former policyholders accounted for over 90% of the surplus."

In other words, despite their asserted actuarial precision, the insurance companies had not been returning via dividend all of the premium surplus. Instead, the surplus accumulated within the companies, where **[**30]** it served the role that any accumulation of capital does. Therefore, the majority errs by stating that "it is well understood that policyholders do not contribute capital to the companies."[2] If not from the policyholders, from whence did that accumulated capital come?

Certainly, the cited testimony raises the question of how much the Dorrances contributed to the surplus. **[**31]** That question was addressed during the demutualization. To determine the number of shares of stock to issue to each member, the insurance companies applied a formula approved by the government regulators, which included a fixed component and a variable component. According to that formula, 14-25% of each company's shares were allocated on a fixed basis to shareholders. The variable shares were allocated based on the "contribution-to-surplus" method, which allocated the total shares based on a policyholder's contribution.

Thus, even if we were to accept the majority's conclusion that the Dorrances had no basis in the voting aspect of the **[*491]** membership rights—remembering that the fixed shares granted solely on that basis were worth $3,164, a minuscule portion of the $1,794,771 of IPO stock at issue—the calculations expressly accounted for their actual contribution to the surplus.

III. "Tax Free Exchange" Is Not a Synonym for "Zero Basis"

The majority also misapplies the concept of a tax-free exchange in stating that "[t]he taxpayer can't have it both ways—a tax-free exchange with zero basis and then an increased basis upon sale of the stock."

It is unclear how the Dorrances are trying to "have it **[**32]** both ways." All that is required for the exchange to be tax-free is for the value received in stock to be the same as the value of the property exchanged. *See* 26 U.S.C. § 358(a)(1). In this case, the IRS, citing its own interpretations, opined that the basis should be zero. Whether that interpretation squares with the facts is the very question at issue in this case. By relying in part on the IRS's interpretation to answer the question, the majority assumes the conclusion.

IV. The District Court's Sound Calculations

After hearing all of the evidence at trial, the district court determined the Dorrances' cost basis by deducting the expected future premium contribution from the IPO value of the stock, yielding a cost basis of $1,078,128. This was the sum of: (1) the IPO value of the fixed shares allocated to the Dorrances ($3,164) and (2) 60% of the IPO value of the variable shares ($1,074,964). The 60% proportion reflected an expert estimate of past contributions by the Dorrances to the life insurance policies; the remaining 40% was an estimate of the policyholders' future contributions to the policies. Applying this formula, the court found that the Dorrances were required to pay taxes on $1,170,678, which **[**33]** was their sale proceeds of $2,248,806 less their basis of $1,078,128.

Thus, the district court quite sensibly reduced the basis by an expert's estimate of the future contribution component of the IPO value, ensuring that the Dorrances would not underpay the taxes owed. This was a careful analysis using reasonable methodology based on the evidence presented at trial. By contrast, the majority's contrary conclusions do not follow from the facts. A portion of the assets of the insurance companies clearly came from the premiums paid by the

[2] The majority misconstrues government witness Ralph Sayre's testimony in this regard. Sayre testified that, from the view of a mutual insurance company, "because we don't have shareholders who have contributed to surplus or contributed capital to withstand [the demand for benefit payments], we're going to have to charge [the policyholder] a little bit more of that up front. But keep in mind that we will also give it back to you. As our experience unfolds and we realize earnings from that extra charge, or from the use of that extra money, we will return it back to you." Thus, policyholders do contribute capital—but they are eventually supposed to get it back. The majority believes that it comes back with a basis of zero, which complements the majority's belief that the insurance companies created something out of nothing.

Dorrances, and they had a substantial basis in the stock distributed to them. By contending to the contrary, my colleagues in the majority have created nothing out of something. It's a miracle!

I respectfully dissent.

End of Document

E.J. Brooks Co. v Cambridge Sec. Seals

Court of Appeals of New York

February 8, 2018, Argued ; May 3, 2018, Decided

No. 26

Reporter

31 N.Y.3d 441 *; 105 N.E.3d 301 **; 80 N.Y.S.3d 162 ***; 2018 N.Y. LEXIS 1080 ****; 2018 NY Slip Op 03171; 168 Lab. Cas. (CCH) P61,860; 2018 WL 2048724

[1] E.J. Brooks Company, Doing Business as TydenBrooks, Appellant-Respondent, v. Cambridge Security Seals, Respondent-Appellant.

Prior History: Proceeding, pursuant to NY Constitution, article VI, § 3 (b) (9) and Rules of the Court of Appeals (*22 NYCRR) § 500.27*, to review two questions certified to the New York State Court of Appeals by the United States Court of Appeals for the Second Circuit. The following questions were certified by the United States Court of Appeals and accepted by the New York State Court of Appeals: "1. Whether, under New York law, a plaintiff asserting claims of misappropriation of a trade secret, unfair competition, and unjust enrichment can recover damages that are measured by the costs the defendant avoided due to its unlawful activity. 2. If the answer to the first question is 'yes,' whether prejudgment interest under New York Civil Practice Law and Rules § 5001(a) is mandatory where a plaintiff recovers damages as measured by the defendant's avoided costs."

E.J. Brooks Co. v Cambridge Sec. Seals, 858 F3d 744, 2017 U.S. App. LEXIS 9885 (2d Cir., June 5, 2017)

Counsel: [**1]** *Kramer Levin Naftalis & Frankel LLP*, New York City (*Daniel B. Goldman, Kerri Ann Law, Claudia Pak* and *Sam Koch* of counsel), for appellant-respondent. I. A defendant's avoided costs is a proper measure of damages in a case for theft of trade secrets. (Jacobus v Colgate, 217 NY 235, 111 NE 837; General Rubber Co. v Benedict, 215 NY 18, 109 NE 96; Ruckelshaus v Monsanto Co., 467 US 986, 104 S Ct 2862, 81 L Ed 2d 815; Story Parchment Co. v Paterson Parchment Paper Co., 282 US 555, 51 S Ct 248, 75 L Ed 544; MAR Oil Co. v Korpan, 973 F Supp 2d 775; Duane Jones Co. v Burke, 306 NY 172, 117 NE2d 237; Thyroff v Nationwide Mut. Ins. Co., 8 NY3d 283, 864 NE2d 1272, 832 NYS2d 873; Paramount Film Distrib. Corp. v State of New York, 30 NY2d 415, 285 NE2d 695, 334 NYS2d 388; Mandarin Trading Ltd. v Wildenstein, 16 NY3d 173, 944 NE2d 1104, 919 NYS2d 465.) II. New York law mandates an award of prejudgment interest where damages are calculated based on a defendant's avoided costs. (De Long Corp. v Morrison-Knudsen Co., 14 NY2d 346, 200 NE2d 557, 251 NYS2d 657; Boule v Hutton, 320 F Supp 2d 132; M.D. Mark, Inc. v Kerr-McGee Corp., 565 F3d 753; Johns-Manville Corp. v Guardian Indus. Corp., 718 F Supp 1310, *925 F2d 1480*.)

Kasowitz Benson Torres LLP, New York City (*Daniel J. Fetterman, Howard W. Schub, Amber T. Wallace* and *Fria R. Kermani* of counsel), for respondent-appellant. I. New York law does not permit non-compensatory "avoided costs" damages for misappropriation of trade secrets or unfair competition. (Preston Co. v Funkhouser, 261 NY 140, 184 NE 737; Sharapata v Town of Islip, 56 NY2d 332, 437 NE2d 1104, 452 NYS2d 347; Ross v Louise Wise Servs., Inc., 8 NY3d 478, 868 NE2d 189, 836 NYS2d 509; Gressman v Morning Journal Assn., 197 NY 474, 90 NE 1131; Michel Cosmetics, Inc. v Tsirkas, 282 NY 195, 26 NE2d 16; Hyde Park Prods. Corp. v Lerner Corp., 65 NY2d 316, 480 NE2d 1084, 491 NYS2d 302; Duane Jones Co. v Burke, 306 NY 172, 117 NE2d 237; Underhill v Schenck, 238 NY 7, 143 N.E. 773; Straus v Notaseme Hosiery Co., 240 US 179, 36 S Ct 288, 60 L Ed 590, 1916 Dec. Comm'r Pat. 288; Ronson Art Metal Works v Gibson Lighter Mfg. Co., 3 AD2d 227, 159 NYS2d 606.) II. Prejudgment interest is not available on avoided costs damages. (Kassis v Teachers' Ins. &Annuity Assn., 13 AD3d 165, 786 NYS2d 473; Bamira v Greenberg, 295 AD2d 206, 744 NYS2d 367; *Mosesson v 288/98 W. End Tenants Corp., 294 AD2d 283, 743 NYS2d 269*; Langer v Miller, 305 AD2d 270, 762 NYS2d 346; *Men's World Outlet v Estate of Steinberg, 101 AD2d 854, 476 NYS2d 171*; Lesjac Realty Corp. v Mulhauser, 43 Misc 2d 439, 251 NYS2d 62; Trademark Research Corp. v Maxwell Online, Inc., 995 F2d 326;

23/23 Communications Corp. v General Motors Corp., 257 AD2d 367, 683 NYS2d 43; Weeks v Angelone, 528 US 225, 120 S Ct 727, 145 L Ed 2d 727; Bethmann v Widewaters Group, 306 AD2d 923, 762 NYS2d 319.)

Judges: FEINMAN, J. WILSON, J. (dissenting).

Opinion by: FEINMAN

Opinion

[304]** **[***165]** **[*444]** Feinman, J.

The United States Court of Appeals for the Second Circuit has asked us to decide "[w]hether, under New York law, a plaintiff asserting claims of misappropriation of a trade secret, unfair competition, and unjust enrichment can recover damages that are measured by the costs the defendant avoided due to its unlawful activity" (E.J. Brooks Co. v Cambridge Sec. Seals, 858 F3d 744, 752 [2d Cir 2017]). Under our common law, compensatory damages must return the plaintiff, as nearly as possible, to the position it would have been in had the wrongdoing not occurred—but do no more. Accordingly, we answer this question in the negative.[1]

[2] I.

E.J. Brooks Company d/b/a TydenBrooks is the largest manufacturer of plastic indicative security seals in the United States. TydenBrooks acquired Stoffel Seals Corporation, and thereafter came into possession of Stoffel's fully-automated process for manufacturing plastic indicative security seals. According to TydenBrooks, several Stoffel/TydenBrooks employees defected to a rival manufacturer, Cambridge Security Seals (CSS), bringing the confidential Stoffel **[****2]** process with them. In 2012, TydenBrooks brought an action in the United States District Court for the Southern District of New York against CSS and those former employees, asserting causes of action based on, inter alia, common-law misappropriation of trade **[*445]** secrets, unfair competition and unjust enrichment.[2] Following a jury trial, CSS **[***166]** **[**305]** was found liable under all three of these theories.

On the issue of damages, TydenBrooks sought to measure its injury by the costs CSS avoided as a result of its unlawful activity. Under this "avoided costs" theory, TydenBrooks sought monetary relief in an amount equal to the difference between the costs CSS actually incurred in developing and using the TydenBrooks' manufacturing process and the costs that CSS would have incurred had it not misappropriated TydenBrooks' process. At trial, TydenBrooks' damages expert testified that CSS would have had to incur an additional $6.1 million to $12.2 million, at a minimum, to develop the manufacturing process for its first-generation machines without making use of its knowledge of TydenBrooks' information.[3]

TydenBrooks did not present any evidence, or otherwise argue, that CSS's avoided costs could be a proxy **[****3]** for its own losses (such as its investment losses). Instead, CSS's avoided costs were presented exclusively as a measure of the benefit CSS derived from the misappropriation, which TydenBrooks asserted was its per se measure of damages. Specifically, TydenBrooks' expert testified that, among the three theories of damages he was familiar with—"lost profits," "disgorgement of unjust gains" and "reasonable royalty damages"—his avoided cost calculation was a "type of disgorgement," which he explained was a measure of how much a company "gain[ed] by taking and using information that didn't belong to them." TydenBrooks consistently took the position, both before and during trial, that its own financial losses were irrelevant to its "avoided costs" theory of damages. For instance, TydenBrooks brought motions in limine to, among other things, exclude evidence that any customers it lost to CSS were due to factors other than CSS's misappropriation. The court granted the motions, holding that such evidence was irrelevant because "TydenBrooks is not claiming damages from the loss of customers," but rather, "based on the idea that, by

[1] We also accepted the following certified question from the Second Circuit: "If the answer to the first question is 'yes,' whether prejudgment interest under New York Civil Practice Law and Rules § 5001(a) is mandatory where a plaintiff recovers damages as measured by the defendant's avoided costs" (id. at 752). We do not reach the second question because we answer the first question in the negative.

[2] TydenBrooks also asserted claims under the federal "Lanham Act," 15 USC § 1125 (a), and the District Court exercised supplemental jurisdiction over the New York common-law claims pursuant to 28 USC § 1367. TydenBrooks' Lanham Act claims are not at issue here.

[3] TydenBrooks' damages expert further testified that this figure would be $7.8 to $16.6 million if "fully burdened costs," i.e., retirement and health benefits, are taken into account.

stealing Tyden Brooks' **[*446]** trade secrets, CSS was able to avoid development **[****4]** costs . . . ."

At the close of trial, the court charged the jury on damages based solely on an avoided costs theory:

> "In evaluating cost savings, you are to use the standard of comparison method. Under this method, you are to compare actual costs incurred by the defendant you are considering with the costs it would have incurred to produce the same products without the use and knowledge of TydenBrooks' manufacturing process. . . . The difference between the costs actually incurred by the defendant you are considering and the amount he would have incurred in the absence of the misappropriation and/or unfair use is the amount of damages that you should award to TydenBrooks."

The court reminded the jury that it "may award compensatory damages only for injuries that TydenBrooks prove[d] were proximately caused by a defendant's allegedly wrongful conduct" and "only for those injuries that TydenBrooks has **[3]** actually suffered or which it is reasonably likely to suffer in the near future." However, the **[***167]** **[**306]** court did not explain how the jury could make the inference that *CSS's* avoided costs approximated the losses that *TydenBrooks* "actually suffered" or was reasonably likely to suffer in the near future. **[****5]** Separately, the court instructed the jury that if it found CSS liable for compensatory damages, it may award punitive damages, "[t]he purpose of [which] is not to compensate a plaintiff but to punish a defendant for wanton and reckless or malicious acts and thereby to discourage the defendant and other people or companies from acting in a similar way in the future."

The jury returned a verdict finding CSS liable for trade secret misappropriation, unfair competition and unjust enrichment. It assessed $1.3 million against CSS in "compensatory damages" on each claim, for a total of $3.9 million against CSS in compensatory damages. The jury did not award punitive damages.

Both parties filed postjudgment motions. First, TydenBrooks moved to amend the judgment to include prejudgment interest under CPLR 5001 (a), which the court denied (*see* *E.J. Brooks Co. v Cambridge Sec. Seals, 2015 WL 9694522 , 2015 US Dist LEXIS 174444* ***[*447]*** *[SD NY, Dec. 22, 2015, No. 12-CV-2937 (LAP)])*.[4] Second, CSS moved for judgment as a matter of law or a new trial or, in the alternative, to alter or amend the judgment, on the grounds that, among other things, avoided costs was an improper measure of damages. The court denied CSS's motion, holding that "the amount of damages recoverable in an action for misappropriation of trade secrets may be measured either by **[****6]** the plaintiff's losses . . . or by the profits unjustly received by the defendant" (*E.J. Brooks Co. v Cambridge Sec. Seals, 2015 WL 9704079, at *4, 2015 US Dist LEXIS 174447, *12 [SD NY, Dec. 23, 2015, No. 12-CV-2937 (LAP)]* [citations and internal quotation marks omitted]). The court held that avoided costs could be awarded as damages under either measure; that is, avoided costs could either measure the defendant's gains or, alternatively, the plaintiff's losses (*see* *2015 WL 9704079, *4-6, 2015 US Dist LEXIS 174447, *11-18*).

The parties cross-appealed the District Court's denial of their respective motions to the Second Circuit. With respect to the avoided costs issue raised in CSS's motion, the Second Circuit noted that "neither [the Second Circuit] nor the New York courts appear to have approved the specific type of award in this case" (*E.J. Brooks, 858 F3d at 750*). On the one hand, the court acknowledged that the Restatement (Third) of Unfair Competition and Second Circuit precedent "commend[ ] using the amount of avoided costs as a measure of damages in unfair competition cases" (*id. at 749*; *see* *Matarese v Moore-McCormack Lines, 158 F2d 631 [2d Cir 1946]*; *Restatement [Third] of Unfair Competition § 45, Comments d*, *f*). On the other hand, the court noted that "New York courts have suggested that the measure of damages in trade secret cases, even when measured by reference to a defendant's profits, should correspond to a plaintiff's losses as a means of compensation" (*E.J. Brooks, 858 F3d at 750*; **[****7]** *see Suburban Graphics Supply Corp. v Nagle, 5 AD3d 663, 666, 774 NYS2d 160 [2d Dept 2004]*; *Hertz Corp. v Avis, Inc., 106 AD2d 246, 485 NYS2d 51 [1st Dept 1985])*, a proposition that the court deemed "contrary" to "the specific type of award in this case" (*E.J. Brooks, 858 F3d at 750*). "Assuming New York requires that trade secret damages bear some connection to the plaintiff's losses," **[*448]** the Second Circuit

[4] Section 5001 (a) provides that "[i]nterest shall be recovered upon a sum awarded . . . because of an act or omission depriving or otherwise interfering with title to, or possession or enjoyment of, property, except that in an action of an equitable nature, interest and the rate and date from which it shall be computed shall be in the court's discretion."

conceded **[***168] [**307]** that "it is not apparent . . . that assessing damages based on the defendant's avoided costs satisfies the requirement" (*id.*). With respect to the prejudgment interest issue, the Second Circuit likewise stated that New York law was inconclusive as to whether prejudgment interest would be "mandatory" on the damages award in this case (*id. at 750-751*).

Accordingly, the Second Circuit certified the following questions:

> "1. Whether, under New York law, a plaintiff asserting claims of misappropriation of a trade secret, unfair competition, and unjust enrichment can recover damages that are measured by the costs the defendant avoided due to its unlawful activity.
>
> "2. If the answer to the first question is 'yes,' whether prejudgment interest under [CPLR] 5001(a) is mandatory where a plaintiff recovers damages as measured by the defendant's avoided costs." (*Id. at 752*)

The Court accepted these questions on June 27, 2017 (*see 29 NY3d 1045, 56 NYS3d 506, 78 NE3d 1191 [2017]*).

II.

We turn first to the question of whether avoided costs are awardable as **[****8]** compensatory damages in an action based on a theory of unfair competition.

The "fundamental purpose" of compensatory damages is to have the wrongdoer "make the victim whole" (*Sharapata v Town of Islip, 56 NY2d 332, 335, 437 NE2d 1104, 452 NYS2d 347 [1982]*; *see Ross v Louise Wise Servs., Inc., 8 NY3d 478, 489, 868 NE2d 189, 836 NYS2d 509 [2007]*; *Matter of Rothko, 43 NY2d 305, 322, 372 NE2d 291, 401 NYS2d 449 [1977]*). "Put another way, these measure fair and just compensation, commensurate with the loss or injury sustained from the wrongful act" (*Sharapata, 56 NY2d at 335* [citations and internal quotation marks omitted]; *see also Steitz v Gifford, 280 NY 15, 20, 19 NE2d 661 [1939]* ["The damages must be compensatory only" and must result "directly from and as a natural consequence of the wrongful act"]). "The goal is to restore the injured party, to the extent possible, to the position that would have been occupied had the wrong not occurred" (*McDougald v Garber, 73 NY2d 246, 254, 536 NE2d 372, 538 NYS2d 937 [1989]*). "The damages cannot be remote, contingent or speculative. They need not be immediate, but need to be so near to the cause only that they may be **[*449]** reasonably traced to the event . . . ." (*Steitz, 280 NY at 20*.) The standard is not one of "mathematical certainty" but only "reasonable certainty" (*id.*).

[1] Such is the rule in unfair competition cases. Damages must correspond to "the amount which the plaintiff would have made except for the defendant's wrong . . . , not the profits or revenues actually received or earned" by the defendant (*McRoberts Protective Agency v Lansdell Protective Agency, 61 AD2d 652, 655, 403 NYS2d 511 [1st Dept 1978]* [citations and internal quotation marks omitted]; **[****9]** *see David Fox & Sons v King Poultry Co., 30 AD2d 789, 790-791, 292 NYS2d 21 [1st Dept 1968*, Eager, J., dissenting], *mod on dissenting op below 23 NY2d 914, 246 NE2d 166, 298 NYS2d 314 [1969]*, *rearg denied 24 NY2d 896, 249 NE2d 476, 301 NYS2d 634 [1969]*; *Santa's Workshop v Sterling, 2 AD2d 262, 267, 153 NYS2d 839 [3d Dept 1956]*, *affd 3 NY2d 757, 143 NE2d 529, 163 NYS2d 986 [1957])*. Another way of stating this rule is that damages in unfair competition cases should correspond to "plaintiff's losses [that] were a proximate result of defendants' **[***169] [**308]** conduct" (*Duane Jones Co. v Burke, 306 NY 172, 191, 117 NE2d 237 [1954])*.

Here, CSS was found liable to TydenBrooks under a "misappropriation theory" of unfair competition. Under the "misappropriation theory" of unfair competition, a party is liable if they unfairly exploit "the skill, expenditures and labors" of a competitor (*ITC Ltd. v Punchgini, Inc., 9 NY3d 467, 476-477, 880 NE2d 852, 850 NYS2d 366 [2007]*; *Electrolux Corp. v Val-Worth, Inc., 6 NY2d 556, 567-568, 161 NE2d 197, 190 NYS2d 977 [1959])*. The essence of the misappropriation theory is not just that the defendant has "reap[ed] where it has not sown," but that it has done so in an unethical way and thereby unfairly neutralized a commercial advantage that the plaintiff achieved through "honest labor" (*International News Service v Associated Press, 248 US 215, 236, 239-240, 39 S Ct 68, 63 L Ed 211 [1918])*.[5] Damages, therefore, must be measured by the

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[5] Indeed, the law could not categorically prevent businesses from "reaping where they have not sown" in the absence of inherently perfidious conduct and actual injury to a competitor. Virtually every form of technological and creative progress stands on ideas and information taken from others (*see Harper & Row, Publishers, Inc. v Nation Enterprises, 471 US 539, 582, 105 S Ct 2218, 85 L Ed 2d 588 [1985*, Brennan, J.,

loss of the *plaintiff's* commercial advantage, which may not correspond to what the defendant has wrongfully gained (*see* Electrolux, 6 NY2d at 571-572; Victor G. Reiling Assoc. v Fisher-Price, Inc., 2006 WL 1102754, 2006 US Dist. LEXIS 22813 [D Conn, Apr. 25, 2006, No. 3:03CV222(JBA)] [applying New York law], *reconsideration denied* 463 F Supp 2d 117 [D Conn 2006]). "What is true of all **[*450]** actions, [and] is especially true in a suit for unfair competition[, is that] disposition of each case peculiarly depends upon the precise state of **[4]** facts disclosed" (Electrolux, 6 NY2d at 571 [citations and **[****10]** internal quotation marks omitted]), particularly since proof of damages for unfair competition is "especially complicated" where the injury only affects intangible values (6 Callmann on Unfair Competition, Trademarks & Monopolies § 23:66 [4th ed]). However, the principle that a plaintiff's losses may be measured practically and flexibly does not remove the requirement that damages be measured by the plaintiff's actual losses (*see* Electrolux, 6 NY2d at 572).

To be sure, courts may award a defendant's unjust gains as a proxy for compensatory damages in an unfair competition case (*see* Underhill v Schenck, 238 NY 7, 17, 143 NE 773 [1924]; Epstein Eng'g, P.C. v Cataldo, 124 AD3d 420, 421, 1 NYS3d 38 [1st Dept 2015]). However, "[t]he accounting for profits under such circumstances is not *in lieu of* . . . damages, but is *a method of computing* damages" (Ronson Art Metal Works v Gibson Lighter Mfg. Co., 3 AD2d 227, 230, 159 NYS2d 606 [1st Dept 1957] [emphasis added], *rearg denied 3 AD2d 833, 161 NYS2d 830 [1st Dept 1957], mot to cancel and discharge undertaking denied 7 AD2d 897, 181 NYS2d 869 [1st Dept 1959]*, quoting Biltmore Publ. Co., Inc. v Grayson Publ. Corp., 272 App Div 504, 507, 71 NYS2d 337 [1st Dept 1947]). Such a computation of damages may be appropriate where a plaintiff's actual losses cannot "be traced with even approximate precision," but even in those cases it must first be shown that there is "some approximate relation of correspondence, a causal relation not wholly unsubstantial and imaginary, between the gains of the aggressor and those diverted from his [or her] victim" (Underhill, 238 NY at 17-18; *accord* Harry R. Defler ***[***170] [**309]*** Corp., 19 AD2d 396, 403, 243 NYS2d 930 [4th Dept 1963]). Without evidence of that correspondence, **[****11]** "[t]here is no presumption of law or of fact" that what a defendant has gained will competently measure what the plaintiff has lost (Michel Cosmetics, Inc. v Tsirkas, 282 NY 195, 202, 26 NE2d 16 [1940], quoting Dickinson v O. & W. Thum Co., 8 F2d 570, 575 [6th Cir 1925]). Furthermore, if a plaintiff seeks to establish an inference that its compensable losses are linked to the value of the defendant's gains, then the defendant must be afforded an opportunity to challenge the link with its own rebuttal evidence (*see* Hyde Park Prods. Corp. v Lerner Corp., 65 NY2d 316, 322, 480 NE2d 1084, 491 NYS2d 302 [1985]).

In Michel Cosmetics (282 NY 195, 26 NE2d 16), the defendants stole the plaintiff's manufacturing process for making lipsticks and **[*451]** packaged and sold the products in the same containers that the plaintiff used, "with the object of deceiving buyers into the belief that they were buying the product of the plaintiff" (*see* id. at 197-198). The trial court ordered the defendants to pay plaintiffs "all profits . . . on the lipsticks manufactured and sold by defendants . . . *[as] if said lipsticks had been manufactured and sold by plaintiff*" (id. at 198 [emphasis added]).[6] This Court held that the measure of damages was overbroad. The Court stated that

> "[t]he wrong inflicted upon the plaintiff is analogous to the wrong suffered by an owner through infringement of his patent or trade-mark, and the rule of damages is similar. An infringer must compensate the owner of a trade-mark, **[****12]** a patent, a process or a formula for the profits which the owner would have acquired in [the owner's] business except for such infringement" (id. at 200).

The Court acknowledged that, "if the plaintiff would otherwise have made the sales of lipsticks which in fact the defendants made by the use of plaintiff's formulas," then the plaintiff would be "entitled to recover from the defendants [such] amount of the profits" (*id.*). However, the Court observed that there was insufficient evidence that the defendant's customers actually overlapped with the plaintiff's, noting in particular that the defendants distributed the products in countries where the plaintiff

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dissenting]).

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[6] The Court noted that

"[a] wrongdoer who has imitated the containers of the plaintiff and has used the secret formulas and processes belonging to the plaintiff might be compelled to 'yield up his gains to the true owner, upon a principle analogous to that which charges a trustee with the profits acquired by wrongful use of the property of the *cestui que trust*' " (id. at 199, quoting Hamilton-Brown Shoe Co. v Wolf Brothers & Co., 240 US 251, 259, 36 S Ct 269, 60 L Ed 629, 1916 Dec. Comm'r Pat. 281 [1916]).

However, as the defendant did not actually make any profits, no such constructive trust was imposed (id. at 198).

was not even marketing them (*see* id. at 200-201). When a plaintiff "seeks to recover damages," the Court held that "the burden is on him to prove by competent and sufficient evidence his lost sales, or that he was compelled to reduce prices as the result of his competitor's wrongful conduct" (id. at 202). Because the evidence in *Michel Cosmetics* was "insufficient to justify an inference that the plaintiff would have made all the sales actually made by the defendants," the Court remitted for a new trial on damages (id. at 204).

In *Hyde* ***[*452]*** *Park (65 NY2d 316, 480 NE2d 1084, 491 NYS2d 302)*, the defendant who wrongfully **[****13]** solicited customers away from the plaintiff was found liable for **[***171] [**310]** unfair competition. The trial court awarded damages equal to the profits that the defendant made by selling to the plaintiff's customers (*see* id. at 320). We held that this was error and that the defendants should have been permitted to introduce evidence that, among other things, the defendant's customers were no longer customers of the plaintiff at the time the defendant made its sales, or that they were bulk buyers whose orders could not entirely have been fulfilled by the plaintiff (*see* id. at 322). Sales to such customers, we held, should have been excluded from the damages award, since they did not rationally relate to any "lost opportunity for profit" caused by the solicitation (*id.*).

Michel Cosmetics and *Hyde Park* establish that, while a defendant's gains may be evidence of a plaintiff's losses, they will not be presumed to be the actual measure of a plaintiff's losses. Otherwise, damages would "cease[ ] to serve the compensatory goals of tort recovery" (McDougald, 73 NY2d at 254). The dissent notes, correctly, that neither Michel Cosmetics nor Hyde Park were about avoided costs. However, these cases signify more broadly that the measure of damages in a trade **[****14]** secret action must be designed, as nearly as possible, to restore the plaintiff to the position it would have been in but for the infringement. Whether those losses are measured by the defendant's profits, revenues, cost savings or any other measure of unjust gain, there is "no presumption of law or of fact" that such a figure will adequately approximate the losses incurred by the plaintiff (Michel Cosmetics, 282 NY at 202; *see* Electrolux, 6 NY2d at 571-572). A plaintiff therefore may not elect to measure its damages by the defendant's avoided costs in lieu of its own losses.

III.

We next turn to whether avoided costs are awardable as damages in trade secret actions. "A plaintiff claiming misappropriation of a trade secret must prove: (1) it possessed a trade secret, and (2) defendant is using that trade secret in breach of an agreement, confidence, or duty, or as a result of discovery by improper means" (*Shaw Creations Inc. v Galleria Enters., Inc., 29 Misc 3d 1213[A], 918 NYS2d 400, 2010 NY Slip Op 51813[U], at *6 [Sup Ct, NY County 2010]*, quoting *Integrated Cash Mgt. Servs., Inc. v Digital Transactions, Inc., 920 F2d 171, 173 [2d* ***[*453]*** *Cir 1990])*. A trade secret is "any formula, pattern, device or compilation of information which is used in one's business, and which gives [one] an opportunity to obtain an advantage over competitors who do not know or use it" (*Ashland Mgt. v Janien, 82 NY2d 395, 407, 624 NE2d 1007, 604 NYS2d 912 [1993])*. This Court has not definitively stated whether trade secret damages may be measured by avoided costs—or, for that **[****15]** matter, by any other measure of the defendant's own gains.

In *Hertz Corp. v Avis, Inc. (106 AD2d 246, 485 NYS2d 51 [1st Dept 1985])*, the Appellate Division held that trade secret damages may not be measured by a defendant's increased profits, except to the extent that those profits are evidence of the plaintiff's own losses. There, the plaintiff alleged that a departing employee retained confidential documents and trade secrets (*see* id. at 247). Using these materials, the defendant was able to "reverse substantial business losses" and "correct operational deficiencies" (*id.*). The plaintiff abandoned any allegation that the use of its trade secrets had caused *it* **[***172] [**311]** any harm; instead, the plaintiff sought to measure "damages" exclusively by the defendant's profits (*id. at 248-250*). The trial court granted the plaintiff's discovery request for the defendant's financial statements, and the Appellate Division reversed. Because the plaintiff conceded that it suffered no harm, the defendant's financials were "irrelevant to [its] claim for damages" (*id. at 249*). Relying largely on unfair competition cases, where recovery is limited to a plaintiff's own losses (*see* Part II, *supra*), the Court stated that the plaintiff was only "entitled to recover as damages the amount of loss sustained by it, including opportunities **[****16]** for profit on the accounts diverted from it through defendants' conduct" (*id. at 251*, quoting *Duane Jones Co., 306 NY at 192*).

Trade secret cases following Hertz have generally adhered to this holding (*see Equity Now, Inc. v Wall St. Mtge. Bankers, Ltd., 98 AD3d 909, 950 NYS2d 904 [1st Dept 2012]* ["Plaintiff was entitled to damages for the profits it lost as a result of defendant's conduct"], *lv denied 21 NY3d 854 [2013]*; *Suburban Graphics Supply Corp. v Nagle, 5 AD3d 663, 666, 774 NYS2d 160 [2d Dept 2004]* ["The measure of damages for 'unfair competition and the misappropriation and exploitation of confidential information is the loss of profits sustained by reason of the improper conduct' "]; *Allan Dampf, P.C. v Bloom, 127 AD2d 719, 720, 512 NYS2d 116 [2d Dept 1987]* [same]; *Feinberg v Poznek, 12 Misc 3d 1185[A], 824 NYS2d 762, 2006 NY Slip Op 51456[U], *4, 2006 NY Slip Op 51456[U], at *4 [Sup Ct, NY County 2006]*; *Robert Plan Corp.* ***[*454]*** *v. Onebeacon Ins., 10 Misc 3d 1053[A], 809 NYS2d 483, 2005 NY Slip Op 51940[U] [Sup Ct, Nassau County 2005]*; *Hair Say, Ltd. v Salon Opus, Inc., 6 Misc 3d 1041[A], 800 NYS2d 347, 2005 NY Slip Op 50382[U], *9 [Sup Ct, Nassau County 2005])*.

[2] We agree that damages in trade secret actions must be measured by the losses incurred by the plaintiff, and that damages may not be based on the infringer's avoided development costs. Authorities embracing the avoided cost method of damages almost universally consider them a measure of the *defendant's* unjust gains, rather than the plaintiff's losses (*see e.g. GlobeRanger Corp. v Software AG United States of Am., Inc., 836 F3d 477, 499 [5th Cir 2016]*; *G.S. Rasmussen & Assoc., Inc. v Kalitta Flying Serv., Inc., 132 F3d 39 [9th Cir, Dec. 11, 1997]* [table; text at *1997 WL 774869, *2, 1997 US App LEXIS 34884, *4-6 (1997)*]; *Litton Sys., Inc. v Ssangyong Cement Indus. Co., Ltd., 107 F3d 30* [Fed Cir, Feb. 13, 1997] [table; text at *1997 WL 59360, *8, 1997 US App LEXIS 2386, *21-23 (1997)]*; *Salsbury Labs., Inc. v Merieux Labs., Inc., 908 F2d 706, 714-715 [11th Cir 1990])*. This calculation of damages, however, does not consider the effect of the misappropriation on the *plaintiff*. Because this figure is tied to the defendant's gains rather than the plaintiff's losses, it is not a permissible measure of damages.

It is true that, in trade secret cases, "loss" is broadly defined and must account for the fact that trade **[****17]** secrets inherently derive their value from their confidentiality. The plaintiff's injury in trade secret misappropriation cases includes the loss of "competitive advantage over others . . . by virtue of its exclusive access" to the secret (*Ruckelshaus v Monsanto Co., 467 US 986, 1012, 104 S Ct 2862, 81 L Ed 2d 815 [1984]*). Where disclosure of a trade secret has "destroy[ed] that competitive edge" (*id.*), the plaintiff's costs of developing the product may be the best evidence of the (now-depleted) value that the plaintiff placed on the secret (*see W.L. Gore & Associates, Inc. v GI Dynamics, Inc., 872 F Supp 2d 883, 892 [D Ariz 2012]*; *In re Cross, 2006 WL 2337177, at *6, 2006 U.S. Dist. LEXIS 56112, *15-18 [SD NY, Aug. 11, 2006, No. 06 Civ. 4228(MBM)]*; *LinkCo, Inc. v Fujitsu Ltd., 232 F Supp 2d 182, 185* ***[***173] [**312]*** *[SD NY 2002])*. However, it is neither automatically nor presumptively the case that the costs avoided by the *defendant* will be an adequate approximation of the *plaintiff's* investment losses, any more than it can be presumed that the defendant's sales would approximate those of the plaintiff (*see Michel Cosmetics, 282 NY at 202*). Indeed, the **[*455]** cases cited by TydenBrooks show the opposite: that the *plaintiff's actual* development costs will commonly be used as a proxy for the *defendant's saved* development costs (under a damages regime that permits recovery of unjust gains) (*see e.g. GlobeRanger, 836 F3d at 499-500*; *University Computing Co. v Lykes-Youngstown Corp., 504 F2d 518, 538 [5th Cir 1974])*. This is only logical; the plaintiff's actual development costs have actually been incurred and are known, whereas the defendant's avoided costs, by definition, are hypothetical. **[****18]** Flipping this formula—measuring the *plaintiff's* actual expenditures, a known quantity, by the *defendant's* projected expenditures, an unknown one—is precisely the kind of "wholly unsubstantial and imaginary" nexus that Judge Cardozo warned of in *Underhill* (*238 NY at 17-18*).

IV.

Finally, the certified question asks us whether avoided costs may be awarded as compensatory damages in an unjust enrichment action. We have stated that, in order to sustain an unjust enrichment claim, "[a] plaintiff must show that (1) the other party was enriched, (2) at [the plaintiff's] expense, and (3) that it is against equity and good conscience to permit [the other party] to retain what is sought to be recovered" (*Mandarin Trading Ltd. v Wildenstein, 16 NY3d 173, 182, 944 NE2d 1104, 919 NYS2d 465 [2011]* [internal quotation marks omitted]). However, this doctrine is a narrow one; it is "not a catchall cause of action to be used when others fail" (*Corsello v Verizon N.Y., Inc., 18 NY3d 777, 790, 967 NE2d 1177, 944 NYS2d 732 [2012])*. Unjust enrichment, or an action in quasi contract,

> "is available only in unusual situations when, though the defendant has not breached a contract nor committed a recognized tort, circumstances create an equitable obligation running from the

> defendant to the plaintiff. Typical cases are those in which the defendant, though guilty of no wrongdoing, has received money to which he or she is not entitled" **[****19]** (*id.*).

In such circumstances, equity merely intervenes to deem the parties privy to each other (*see* Miller v Schloss, 218 NY 400, 113 NE 337 [1916]). "The contract is a mere fiction, a form imposed in order to adapt the case to a given remedy . . . . . The law creates it, regardless of the intention of the parties, to assure a just and equitable result" (Clark-Fitzpatrick, Inc. v Long Is. R.R. Co., **[*456]** 70 NY2d 382, 388-389, 516 NE2d 190, 521 NYS2d 653 [1987], quoting Bradkin v Leverton, 26 NY2d 192, 196, 257 NE2d 643, 309 NYS2d 192 [1970]).[7]

IDT Corp. v Morgan Stanley Dean Witter & Co. (12 NY3d 132, 142, 907 NE2d 268, 879 NYS2d 355 [2009]) is **[5]** instructive. There, the plaintiff, IDT, brought an unjust enrichment action (among other causes of action) against its former advisor, Morgan Stanley, alleging that Morgan Stanley used its intimate knowledge of IDT's confidential business and financial information in order to induce a third party, Telefonica, to breach a contract with IDT (*see* id. at 136-139). Under the contract in question, IDT would have acquired a 10% stake in the operations of SAm-1, a large undersea fiber-optic cable, as the anchor tenant of the cable network (*see* Morgan Stanley v IDT Corp., 2006 N.Y. Misc. LEXIS 9640, 2006 WL 4682158 [Sup Ct, NY County, Apr. 10, 2006], *affd* 45 AD3d 419, 846 NYS2d 116 [1st Dept 2007], *revd* 12 NY3d 132, 907 NE2d 268, 879 NYS2d 355 [2009]). IDT alleged that Morgan Stanley misappropriated its confidential information and induced the breach so that it could earn substantial investment banking fees replacing IDT as anchor tenant (*see id.*). We held that the unjust enrichment claim could not "support the disgorgement of any profits Morgan Stanley obtained from Telefonica **[****20]** or other companies, in connection with SAm-1" (IDT, 12 NY3d at 142). "In seeking Morgan Stanley's profits from SAm-1, IDT [did] not, and [could] not, allege that Morgan Stanley [had] been unjustly enriched *at IDT's expense*, because IDT did not pay the alleged fees" (*id.* [emphasis added]). Though Morgan Stanley may have been enriched, and though IDT may have been injured in other ways, recovery of the third-party fees was denied because there was no impairment of any preexisting right to the fees.

[3] Similarly, where a defendant saves, through its unlawful activities, costs and expenses that otherwise would have been payable to third parties, those avoided third-party payments do not constitute funds held by the defendant "at the expense of" the plaintiff. Therefore, a plaintiff bringing an unjust enrichment action may not recover as compensatory damages the costs that the defendant avoided due to its unlawful activity in lieu of the plaintiff's own losses.

V.

Accordingly, the first certified question should be answered in the negative and the second certified question not answered as unnecessary.

Dissent by: WILSON

Dissent

Wilson, J. (dissenting). This case was brought and tried in federal court, on three distinct theories of trade secret theft, unfair competition and unjust enrichment. The jury returned judgment for TydenBrooks, specifically finding that TydenBrooks "possessed a trade secret, identifiable with reasonable particularity, which was unlawfully misappropriated by [Cambridge Security Seals]"; that Cambridge Security Seals stole those secrets and used them for its own benefit, injuring TydenBrooks by that theft; that Cambridge Security Seals "engaged in unfair competition" with TydenBrooks; and that Cambridge Security Seals was "unjustly enriched, that is, that [Cambridge Security Seals] received a benefit at [TydenBrooks'] expense that, in equity and good conscience, [Cambridge Security Seals] should not

[7] The term "unjust enrichment" (or "restitution") can refer to a number of distinct concepts, and courts employing these terms have meant different things in different contexts (*see generally* Doug Rendleman, *Measurement of Restitution: Coordinating Restitution with Compensatory Damages and Punitive Damages*, 68 Wash & Lee L Rev 973, 976 [2011] [describing multiple concepts that have historically been referred to as "restitution" and noting that "(o)ur court-made common law jurisprudence has not developed fences around the doctrines to define exact boundaries"]). As a *remedy*, unjust enrichment, in contrast to damages, is designed to avoid wrongful gains rather than compensate the plaintiff for its losses (*see Dobbs Law of Remedies: Damages, Equity, Restitution* § 4.1 [1] [2d ed 1993]). As a **[***174]** **[**313]** *cause of action,* however, unjust enrichment simply refers to liability imposed on a defendant who has been enriched apart from a breach of an independent legal duty (*see* Corsello, 18 NY3d at 790-791)

retain." The United States Court of Appeals for the Second Circuit has asked us, and we have **[***175] [**314]** agreed to resolve, three questions of New York's law relating to damages: "Whether, under New York law, a plaintiff asserting claims of [1] misappropriation of a trade secret, [2] unfair competition, and [3] unjust **[****21]** enrichment can recover damages that are measured by the costs the defendant avoided due to its unlawful activity" (*E.J. Brooks Co. v Cambridge Sec. Seals, 858 F3d 744, 752 [2d Cir 2017]*).[1] Those certified questions do not ask whether this plaintiff may recover, but whether, as a matter of law, any plaintiff may recover a defendant's avoided costs on one or another of these three theories of liability. The majority answers the questions through a misguided bottoms-up attempt to decide this plaintiff's case rather than a top-down **[*458]** approach announcing the principles of law. Not only does that approach produce an incorrect answer here, but it also forsakes New York's historic role at the vanguard. Where we should lead, we now refuse even to follow.

As to the Second Circuit's first question—whether avoided costs may form the basis of a damage award for trade secret misappropriation—the majority admits a vacuum in our decisional law. Instead of engaging with the unique nature of trade secret theft and the policy concerns at issue, the majority relies on several inapposite Appellate Division cases that discuss whether a plaintiff can be awarded defendant's profits as a measurement of damages; in none of the cited cases did plaintiffs seek avoided costs as damages. **[****22]** As to the second question, the majority misinterprets our prior case law to adopt an unnecessarily narrow interpretation of damages. In particular, the majority ignores our case law expressly allowing flexible recovery in equity. As to the third question, the majority tacitly concedes the absence of authority, again pointing to inapposite decisions.

The Second Circuit recognized not just the paucity of New York law on the questions it certified, but also the historically established common-law role of our court, when framing the issue as an "unresolved policy decision," that our court is "better situated" to make (*858 F3d at 750*). Our charge is to answer the question from the top down, looking to several basic principles. *First*, "the principle that there is no wrong without a remedy" (*General Rubber Co. v Benedict, 215 NY 18, 23, 109 NE 96 [1915,* Cardozo, J.]). *Second*, a successful plaintiff cannot be held to proof of damages with mathematical certainty; damages cannot be speculative, but must bear some reasonable relation to the injury (*see* *Steitz v Gifford, 280 NY 15, 20, 19 NE2d 661 [1939]* ["The fact that (damages) cannot be measured with absolute mathematical certainty does not bar substantial recovery if they may be approximately fixed"]; *Duane Jones Co. v Burke, 306 NY 172, 192, 117 NE2d 237 [1954]* ["when from the nature of the case the amount of the damages cannot **[****23]** be estimated **[6]** with certainty, or only a part of them can be so estimated, no objection is perceived to placing before the jury all the facts and circumstances of the case having any tendency to show damages or their probable amount, so as to enable them to make the most intelligible and accurate estimate which the nature of the case will permit"]). *Third*, protectible intellectual property in whatever form, be it trade secret, patent, copyright, trademark or **[***176] [**315]** other, has a value **[*459]** greater than merely its development cost, and innovation depends on the ability of inventors to protect that property from theft (*see* *Kewanee Oil Co. v Bicron Corp., 416 US 470, 482, 94 S Ct 1879, 40 L Ed 2d 315 [1974]* [noting the "importance of trade secret protection to the subsidization of research and development"]; Gordon L. Doerfer, *The Limits on Trade Secret Law Imposed by Federal Patent and Antitrust Supremacy*, 80 Harv L Rev 1432, 1454 [1967] ["(trade secret law) protects independent innovators who will be encouraged to invent knowing that their work, if successful, will not be appropriated by others to their disadvantage"]).

Avoided costs are widely recognized as an available measure of damages in trade secret cases. They comport with each of the principles above. In both unfair competition actions and unjust enrichment **[****24]** actions, avoided-cost damages deprive the wrongdoer of its gain. As a policy matter, avoided-cost damages would often undercompensate plaintiffs, because no rational economic actor would spend $X to recover profits of merely $X (*see* *LinkCo, Inc. v Fujitsu Ltd., 232 F Supp 2d 182, 186 [SD NY 2002]* [opting for reasonable royalty where "losses measured solely by (plaintiff's) development costs would not adequately compensate the company for its loss of the potentially valuable trade secret"]; *see also* Christopher Rebel J. Pace, *The Case for A Federal Trade Secrets Act, 8 Harv JL & Tech 427, 439 [1995]* ["a business invest(s) in

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[1] The first certified question is really three separate questions, one each for trade secret theft, unfair competition and unjust enrichment. The Second Circuit certified an additional question concerning prejudgment interest, to be answered if any of the other questions was answered in the affirmative. Because the majority has not answered that question, I also do not.

innovations that it can maintain in secrecy while exploiting the innovations to recover its expenses and, it is hoped, turn a profit"]). However, the calculation of avoided-cost damages is generally much simpler than, and less subject to challenge than, lost-profit damages, which makes them an attractive alternative for plaintiffs who are willing to forego a potentially larger recovery in favor of a smaller, more certain one. I do not suggest that avoided-cost damages will always be the best measure of damages. Rather, it is one of several measures of damages, subject to election by the plaintiff, challenge by the defendant, and acceptance by the trier of fact. Trade secret cases in particular require **[****25]** "a flexible and imaginative approach to the problem of damages" (*University Computing Co. v Lykes-Youngstown Corp., 504 F2d 518, 538-539 [5th Cir 1974])*. Such flexibility and imagination have been, and should remain, a hallmark of our jurisprudence.

By focusing on and misconstruing the underlying proceeding and by relying on inapposite case law, the majority also fails to discern the greater point of the Second Circuit's questions. The **[*460]** majority ignores crucial precedent: under New York law, a defendant's ill-gotten gains are available as an *equitable* remedy, particularly in trade secret and unfair competition cases. Instead, the majority treats the certified questions as if they asked whether avoided-cost damages are available at law, regardless of their availability in equity. Long ago, the federal courts merged law and equity, and thus the answer to the certified question must consider the availability of avoided costs as equitable damages. The majority also disregards the widespread use of avoided-cost damages under the Restatement (Third) of Unfair Competition and the laws of other states. Such willful blindness leads the majority to provide a half-answer to the Second Circuit, "avoided-cost damages have not been historically recoverable at law," instead of a full **[****26]** answer: equity allows flexibility in damage awards, unrestricted to the plaintiff's lost profits.

I.

Answering the first certified question requires an examination of trade secret **[***177] [**316]** law. A trade secret, by definition, must have economic value and provide a competitive advantage to its owner due to the exclusive use of a product or technique (*see Ashland Mgt. v Janien, 82 NY2d 395, 407, 624 NE2d 1007, 604 NYS2d 912 [1993]*; *Restatement [First] of Torts § 757, Comment b* [defining a trade secret as "any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it"]; Michael Risch, *Why Do We Have Trade Secrets*?, *11 Marq Intell Prop L Rev 1, 38 [2007]* ["economic value is a signal to the court that the special rules associated with trade secrets are warranted"]). The factors in a trade secret claim include, among others, the value of the information to the business and its competitors, the amount of effort or money expended by the business in developing the information, and the difficulty with which the information could be properly acquired or duplicated by others (*see Ashland at 407*). As the majority recognizes, the loss in trade secret cases will not necessarily be comparable to that in other unfair **[****27]** competition cases because "trade secrets inherently derive their value from their confidentiality" (majority op at 454). Damages in trade secret cases "are not, unlike in **[7]** other commercial tort cases, confined to a single incident of loss of use and depreciation" (Felix Prandl, *Damages for Misappropriation of Trade Secret*, **[*461]** *22 Tort & Ins LJ 447, 447 [1987]*; *see also FMC Corp. v Taiwan Tainan Giant Indus. Co., Ltd., 730 F2d 61, 63 [2d Cir 1984]* ["A trade secret once lost is, of course, lost forever"]).

When a trade secret is stolen, the injury encompasses many things, including the lost profits plaintiff might have made without the theft, the loss in potential exclusive licensing opportunities, the loss in the value of the secret once exposed and, perhaps most importantly, the lost incentive for others to expend their time and efforts on innovation. In simple terms, "there is no secret any longer"; but "the standard rules of damages are, however, not tailored to take this extra loss into account" (Prandl, 22 Tort & Ins LJ at 448). Thus, when the theft can be nipped in the bud, courts routinely grant injunctions, because money damages are deemed insufficient to capture the true loss suffered by a plaintiff (*see e.g. Basicomputer Corp. v Scott, 973 F2d 507, 511 [6th Cir 1992]* [affirming injunction because "an injury is not fully compensable by money damages if the nature of **[****28]** the plaintiff's loss would make damages difficult to calculate"]; *Norbrook Labs. Ltd. v G.C. Hanford Mfg. Co., 126 Fed Appx 507, 509 [2d Cir 2005]*; *North Atl. Instruments, Inc. v Haber, 188 F3d 38, 49 [2d Cir 1999]*; *Computer Assoc. Int'l, Inc. v Bryan, 784 F Supp 982, 986 [EDNY 1992]*; *Invesco Institutional (N.A.), Inc. v Deutsche Inv. Mgmt. Americas, Inc., 74 AD3d 696, 697, 904 NYS2d 46 [1st Dept 2010]*; *Ingenuit, Ltd. v Harriff, 33 AD3d 589, 590, 822 NYS2d 301 [2d Dept 2006])*.

The majority claims that "damages in trade secret actions must be measured by the losses incurred by the plaintiff" (majority op at 454). By "losses incurred by the plaintiff," the majority means "plaintiff's lost profits," or perhaps "plaintiff's development costs." That narrow interpretation flouts the above basic principles and fails to engage meaningfully with the unique nature of trade secrets, as well as the differences between profits and development costs. In a trade secret case, the plaintiff's loss is the loss in value of the trade secret; that loss can be *measured* in **[***178] [**317]** several ways, but all correspond to the plaintiff's loss, even though they may differ in amount, just as a damage award based on royalties predicated on a hypothetical license may not yield the same—or even a similar—amount as damages based on the plaintiff's lost profits. Of course, plaintiffs will often want to prove lost profits as a measurement of damages, but that may be difficult or impossible to do, because factors exogenous to the theft (*e.g.*, changes in demand, changes in costs, other competition, leak of the trade secret **[****29]** by **[*462]** the defendant to others) make the estimation of lost profits difficult or unreliable. Plaintiffs may be constrained, for practical or legal reasons, to a hypothesized royalty when, for example, there is a history of the licensing of that or other secrets by the plaintiff, evidencing the plaintiff's practice of monetizing secrets and providing yardsticks for estimating a royalty. But a plaintiff's costs of development or the costs a defendant avoided by stealing the secret are also appropriate measures, because those are reasonably related to the value of the trade secret (*see* *University Computing Co. at 535-538*; *W.L. Gore & Assoc., Inc. v GI Dynamics, Inc., 872 F Supp 2d 883, 892 [D Ariz 2012]*; *In re Cross Media Mktg. Corp., 2006 WL 2337177, at *5-6, 2006 US Dist. LEXIS 56112, *12-18 [SD NY, Aug. 11, 2006, No. 06 Civ. 4228(MBM)]*). It is of no moment that they may not be the same dollar number as a lost-profits analysis might show: as anyone who has ever retained an expert to determine lost profits knows, no two experts are likely to arrive at the same figure. Again, the law does not require such exactitude in recompensing a wrong.

The majority recognizes that "[w]here disclosure of a trade secret has 'destroy[ed] that competitive edge,' the *plaintiff's* costs of developing the product may be the best evidence of the (now-depleted) value that the plaintiff placed on the secret" (majority op at 454 [citations omitted and emphasis added]). **[****30]** The majority suggests, though, that it is "neither automatically nor presumptively the case that the [defendant's cost-savings] will be an adequate approximation of the plaintiff's investment losses" (*id.* [emphasis omitted]).[2] That conclusion misses the point; **[***179] [**318]** the issue is not whether **[8]** defendant's avoided costs **[*463]** adequately approximate plaintiff's *investment* losses, but whether they adequately measure the plaintiff's losses caused by the misappropriation. Certainly, a plaintiff may claim that the value of the secret it lost should be measured by the cost it took to develop the product or technique. A trade secret might be worth more or less than the plaintiff claims, and, in that case, the defendant may adduce evidence to challenge the plaintiff's damage claim by, for example, showing that the defendant could have developed the secret (or its equivalent) more cheaply because technology has advanced, inputs have cheapened, a license was available from a third party, etc. But a plaintiff may also present the loss in terms of the costs avoided by the defendant, which might better represent the value of the secret; that is, a secret's value can be measured by what it would cost someone else to develop it—or **[****31]** a good substitute for it—

[2] The majority's objection that we cannot measure "plaintiff's actual expenditures, a known quantity, by the defendant's projected expenditures, an unknown one," is a challenge suitably made by defense counsel in attacking a plaintiff's damage model, but not a basis to deny recovery as a matter of law (majority op at 455 [emphasis omitted]). Avoided-cost damages do not attempt to measure plaintiff's actual expenditures; they measure plaintiff's loss—the loss of the exclusive use of the trade secret—by providing an approximation of its value: what would it cost the defendant to have developed the secret on its own? Here, TydenBrooks' damage model consisted of two components: capital costs for construction of the machines incorporating the trade secrets, and labor costs associated with the development of the trade secrets and incorporation into the first-generation machines. The $1,886,395 of capital costs included in the damage estimate was—without any adjustment—the capital cost TydenBrooks itself incurred. So, when the majority says, "TydenBrooks did not present any evidence, or otherwise argue, that CSS' avoided costs could be a proxy for its own losses (such as its investment losses)," that is flatly incorrect, at least as to the $1,886,395 of capital costs (majority op at 445.

The labor cost component was based on a high and a low estimate of the number of hours TydenBrooks spent developing the trade secrets, allocated by the type of work involved to specific persons (or types of persons) actually employed by Cambridge Security Seals, and multiplied by the monthly cost of each of those employees. That is, instead of claiming that Cambridge Security Seals could have hired the relevant employees at the wages paid by TydenBrooks, TydenBrooks used Cambridge Security Seals' actual rate of pay, multiplied by an estimate of the actual hours it needed to because no one would pay more for a secret than that amount (accounting, as well, for economic cost in terms of the difference in timing between immediate theft and protracted independent development). As the majority admits, a trade secret's value to the plaintiff is in its confidentiality and exclusive use (majority op at 454); but the use is exclusive only so long as competitors are unwilling to fund the costs to develop the product independently. That is precisely what the defendant has avoided by stealing it, and what the plaintiff has lost due to **[9]** the theft. The defendant, of course, can provide its own estimate to challenge the calculation of avoided costs,[3] **[*464]** or demonstrate that avoided costs are inappropriate given the peculiar facts of a case.[4]

In other words, if the defendant could have independently developed the trade secrets at a cost of $X in a period of Y years, and the plaintiff recovers $X plus the profits lost during the Y years due to the defendant's early entry made possible by the theft, the plaintiff will be put exactly into the position it would have been in had the defendant not stolen the secrets—which satisfies the majority's "fundamental **[****32]** purpose" to "make the victim whole" (majority op at 448, quoting *Sharapata v Town of Islip, 56 NY2d 332, 335, 437 NE2d 1104, 452 NYS2d 347 [1982])*. The majority restricts plaintiffs to profits lost during Y years, which plainly does not restore the plaintiff to the position it would have been in had the theft not occurred, because the defendant spends nothing to obtain use of the secrets. The majority's rule fails to adhere to the proposition it touts, that damages "must be measured by the loss of the *plaintiff's* commercial advantage" (majority op at 449). Here, TydenBrooks seeks only $X, which most likely undercompensates it unless its lost profits during Y were $0, in which case **[***180]** **[**319]** $X perfectly compensates TydenBrooks (subject to adjustment for the time value of money).

develop the trade secrets. There is nothing "unsubstantial [or] imaginary" about that method (majority op at 455). If the hourly rates or estimated hours are overstated, it is up to a defendant to challenge them by contrary evidence, including expert opinion.

[3] Indeed, defendant here attempted that proof; from what we can tell based on the verdict, the jury here credited Cambridge Security Seals' attack on the avoided-cost damages proffered by TydenBrooks, awarding $3.9 million in damages instead of the $7.8-16.6 million claimed by TydenBrooks' expert.

[4] For example, if an injunction issued before a defendant had made any use or disclosure of the trade secrets, avoided costs would most likely not be an appropriate measure of damage.

The majority insists that damages for trade secret misappropriation cannot include defendant's avoided costs, relying on Appellate Division cases where the measure of damages was lost profits. However, those cases do not stand for the proposition that plaintiff's losses must be measured *exclusively* by plaintiff's lost profits. In *Hertz Corp. v Avis, Inc. (106 AD2d 246, 250, 485 NYS2d 51 [1st Dept 1985])*, the issue decided was whether Avis would be required to disclose hundreds of thousands of pages of sensitive documents; Hertz expressly stated that it **[****33]** had lost no profits, and the court, in passing, referred to the "basic" rule of unfair competition damages—not an exclusive rule. In fact, the portion of *Hertz* cited by the majority demonstrates that lost profits are considered one of many ways to measure loss (majority op at 453, quoting *Hertz at 251* [plaintiff was "entitled to recover as damages the amount of loss sustained by it, *including* opportunities for profit on the accounts diverted from it" (emphasis added)]). The cited Appellate Division cases that followed *Hertz* all involved claims of active solicitation of **[*465]** plaintiffs' customers, not claims that misappropriation of a trade secret devalued the secret or gave the defendant a competitive advantage by avoiding costs (*see Equity Now, Inc. v Wall St. Mtge. Bankers, Ltd., 98 AD3d 909, 950 NYS2d 904 [1st Dept 2012]* [plaintiff claimed defendant stole and used confidential customer list]; *Suburban Graphics Supply Corp. v Nagle, 5 AD3d 663, 665, 774 NYS2d 160 [2d Dept 2004]* [plaintiff's claim involved defendant's "actively soliciting the plaintiff's customers"]; *Allan Dampf, P. C. v Bloom, 127 AD2d 719, 512 NYS2d 116 [2d Dept 1987]* [plaintiff alleged that defendant used confidential information and records to divert plaintiff's patients]). In that type of case, plaintiff's lost profits as a damages award makes sense, because the nature of the claim is that plaintiff's own customers were misdirected. However, those cases say nothing **[****34]** about recovery of development costs, whether direct or avoided, and certainly do not state that plaintiff's lost profits are the *only* measure of damages in unfair competition cases.

Nor is an examination of cases involving lost profits particularly helpful in determining the rule for avoided costs, because lost profits differ from avoided costs in important ways. Lost profits cases generally involve products or services sold to third parties, where the profits from those sales would have been realized by the plaintiff, had it not been for the defendant's misconduct. The analysis must involve a consideration of whether plaintiff would have made those sales, because the nature of the claim means that either the plaintiff or defendant would have made those sales, but not both (*see infra* at 467-468).

Anything else would award plaintiff a windfall. Avoided costs, however, are an entirely different measure of damages. Plaintiff's own investment costs, which the majority concedes would be an appropriate measure of loss, do not depend at all on third-party sales, nor do they have any relation to a particular defendant. Rather, plaintiff's investment costs serve as "evidence of the (now-depleted) value" of **[****35]** the trade secret **[10]** (majority op at 454). So, too, would defendant's avoided costs. Unlike lost profits, there is no concern that plaintiff will receive more than it would have had it not been for the theft, and plaintiff's investment costs and defendant's avoided costs need not be the same. **[***181] [**320]** Those considerations are simply irrelevant because investment costs (direct or avoided) measure the inherent value of the trade secret, rather than actual profits gained or lost.

[*466] II.

The majority's answer to the Second Circuit's second question—whether avoided costs are available as a measure of damages for unfair competition—is similarly flawed. The majority claims that damages in unfair competition cases "must correspond to 'the amount which the plaintiff would have made except for the defendant's wrong' . . . not the profits or revenues actually . . . earned,' " relying on cases in which no claim for avoided-cost damages was made (majority op at 449).[5] At the same time, the majority admits that "proof of damages for unfair competition [may be] 'especially complicated' where the injury only affects intangible values" and approvingly quotes Electrolux Corp. v Val-Worth, Inc. (6 NY2d 556, 571, 161 NE2d 197, 190 NYS2d 977 [1959]) for the proposition that "especially true in a suit for unfair competition **[****36]** [, is that] disposition of each case peculiarly depends upon the precise state of facts disclosed" (majority op at 450). The majority also expressly cites Underhill v Schenck (238 NY 7, 17, 143 NE 773 [1924, Cardozo, J.]) for the long-standing rule that "courts may award a defendant's unjust gains as a proxy for *compensatory damages* in an unfair competition case" (majority op at 450 [emphasis added]), and then cites several Appellate Division cases for the proposition that such an award "is not *in lieu of*, damages but is *a . . . method of computing* damages" (*id.*). That is precisely the point: a defendant's unjust gains (here, the avoided costs) may be the method of computing plaintiff's compensatory damages. In *Underhill*, we recognized that "[d]amages whether resulting from infringement in the strict sense or from unfair competition can seldom be traced with even approximate precision" and courts "have **[*467]** thus been led to award alternative relief" (*Underhill* at 17).[6] Yet the majority's ultimate conclusion voids its recitation of those propositions; although acknowledging that "plaintiff's losses may be measured practically and **[11]** flexibly" (majority op at 450), the majority insists that "damages" (meaning recovery in a cause of action at law) **[****37]** must be measured by plaintiff's lost profits.

[321] [***182]** The majority reaches its conclusion by misinterpreting the holdings of Michel Cosmetics, Inc. v Tsirkas (282 NY 195, 26 NE2d 16 [1940]) and Hyde Park Prods. Corp. v Lerner Corp. (65 NY2d 316, 480 NE2d 1084, 491 NYS2d 302 [1985]). Those cases stand for a very different proposition: that the plaintiffs in those cases had not demonstrated an entitlement to recover as damages the entirety of the *defendants' profits* from products produced by purloined trade secrets. In *Michel Cosmetics*, the plaintiff sought an injunction and an accounting "for all sales and contracts made by [defendant], for the sale of lipsticks made by the secret formulae or secret processes owned by the plaintiff" (282 NY at 198). We held that the damages were inappropriate because, although the plaintiff was entitled to recover its losses, "there [was] no evidence in this case which would support a finding that plaintiff would

[5] The claim in Santa's Workshop v Sterling (3 NY2d 757, 143 NE2d 529, 163 NYS2d 986 [1957], *affg* 2 AD2d 262, 153 NYS2d 839 [3d Dept 1956]) was that defendant diverted plaintiff's customers by unlawfully imitating plaintiff's advertising and publicity materials. David Fox & Sons v King Poultry Co. (23 NY2d 914, 246 NE2d 166, 298 NYS2d 314 [1969], *modfg on dissenting op 30 AD2d 789, 292 NYS2d 21 [1st Dept 1968])* and McRoberts Protective Agency v Lansdell Protective Agency (61 AD2d 652, 403 NYS2d 511 [1st Dept 1978]) turned on even narrower grounds involving specific deductions and net-vs.-gross profits. Under the specific facts of those cases, in which no plaintiff sought development costs or avoided costs as damages, plaintiff's profits may often have been the best measure of damages, but not always so (*see* Epstein Eng'g, P.C. v Cataldo, 124 AD3d 420, 421, 1 NYS3d 38 [1st Dept 2015] ["Plaintiff may elect to measure its damages in this unfair competition action by reference to the profits made by *defendants* from clients or business opportunities diverted from plaintiff" (emphasis added)]).

[6] It is noteworthy that the "unjust gains" in *Underhill* referred to the defendant's *profits*, not the tamer, more directly-related amount of avoided costs.

have sold those lipsticks except for the defendant's wrong" (id. at 201). We clarified that "the evidence may be sufficient to permit the inference that the defendants have caused some loss of profits to the plaintiff, but is certainly insufficient to justify an inference that the plaintiff would have made *all the sales* actually made by the defendants if the defendants **[****38]** had not competed with it" (id. at 204 [emphasis added]). In *Hyde Park*, we held that the plaintiff could not receive all of the defendants' profits from sales made to improperly solicited customers. Rather, the defendant could show that specific sales did not result from solicitation, that plaintiff could not have fulfilled those customers' orders, or that the customers were no longer plaintiff's customers at the time of the sale (65 NY2d at 320).

Michel Cosmetics and *Hyde Park* have nothing to do with a defendant's avoided costs, or even a plaintiff's cost of development in trade secret cases. Those cases disallowed wholesale recovery of the *defendant's profits* as a measure of plaintiff's **[*468]** loss, and for good reason: the profit from a product depends not just on the trade secrets stolen, but also on many other components that may be necessary to create the product, the cost at which the defendant is able to purchase the necessary inputs, the defendant's skill in marketing, the defendant's sales efforts, the defendant's advertising expenditures, the defendant's reputation and goodwill, and a host of other factors as to which the plaintiffs in those cases had adduced no evidence.[7]

If *Michel Cosmetics* and *Hyde Park* ***[****39]*** tell us anything about avoided costs as trade-secret damages, it is that defendants should be allowed to challenge the amount of damages claimed; for example, by showing that the defendant could have developed the same or an equivalent method through cheaper, legitimate means (thus challenging the claimed value of the secret) or that plaintiff retained some value in the secret that should be deducted from the claimed damage amount (*e.g.*, when a court issues an injunction after defendant has made substantial sales). Those cases provide no basis whatsoever to announce **[***183] [**322]** that, as a matter of New York law, a plaintiff may *never* "recover damages that are measured by the costs the defendant avoided due to its unlawful activity." Rather, the answer to the second question asked by the Second Circuit must be yes—as one acceptable measure of damages for unfair competition, a plaintiff may *sometimes* recover defendant's avoided costs as damages for its lost trade secret, because such avoided costs can be a reasonable approximation of the injury to the plaintiff, subject, of course, to evidentiary challenge by the defendant and acceptance by the trier of fact.

The majority's answer is wrong for **[****40]** a second reason: common-law unfair competition "is an action in equity and not one at law" (Warren, Inc. v Turner's Gowns, Ltd., 285 NY 62, 67, 32 NE2d 793 [1941], citing Westcott Chuck Co. v Oneida Natl. Chuck Co., 199 NY 247, 251, 92 NE 639 [1910]). In *Warren*, we explained: "It is possible that in an action at law for damages proof of actual damage suffered by a plaintiff would be necessary to justify more than a **[*469]** nominal recovery" (id. at 68). We held that in contrast, in an action for unfair competition, "equity will treat the wrongdoer as a trustee for the plaintiff so far as the former has realized profits from its acts. . . . Inability to prove damages would not preclude plaintiffs from recovering, on an accounting, profits realized from sales unlawfully made, together with interest thereon from the time of the commencement of the action" (*id.*). Even in *Michel Cosmetics* we noted that

> "[a] wrongdoer who has imitated the containers of the plaintiff and has used the secret formulas and processes belonging to the plaintiff might be compelled to '*yield up his gains* to the true owner, upon a principle analogous to that which charges a trustee with the profits acquired by wrongful use of the property of the *cestui que trust*'" (282 NY at 199 [emphasis added], quoting Hamilton-Brown Shoe Co. v Wolf Brothers & Co., 240 US 251, 259, 36 S Ct 269, 60 L Ed 629, 1916 Dec. Comm'r Pat. 281 [1916])

Thus, inasmuch as the majority relies on *Michel Cosmetics* and *Hyde Park* for **[****41]** the proposition that, because the entirety of a defendant's profits cannot be recovered in an action at law for unfair competition based on a theft of trade secrets, and therefore (although this remains quite a leap) avoided costs also cannot be recovered, the same is not true in equity. We

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[7] If the only form of damages available were the entirety of a defendant's profits, the results would sometimes be unjustified; for example, a valve manufacturer stealing my trade secret relating to valve manufacture would pay all its profits to me, as would an automobile manufacturer who stole my valve trade secret and used it in the tires of cars it sold—including all the profits on the cars. A trade secret thief who broadly published but made no commercial use of my trade secrets would owe me nothing; one who, through great skill and effort, successfully commercialized them beyond anything I ever could have accomplished would owe me everything.

should, therefore, answer the Second Circuit's second question affirmatively: as a matter of law, avoided-cost damages are available in a common-law claim of unfair competition.

III.

The majority fares no better in attempting to answer the Second Circuit's third question: whether avoided-cost damages are an available remedy for unjust enrichment. Instead, the majority answers an entirely different question—whether TydenBrooks can state a claim for unjust enrichment at all. We lack the power to decide that question, which the federal district court has already decided.

The cases cited by the majority, supposedly related to whether a plaintiff bringing an unjust enrichment action may recover costs that the defendant avoided, stand for no such proposition (majority op at 455-456). *Corsello v Verizon N.Y., Inc. (18 NY3d 777, 791, 967 NE2d 1177, 944 NYS2d 732 [2012])* and *Clark-Fitzpatrick, Inc. v Long Is. R.R. Co. (70 NY2d 382, 388, 516 NE2d 190, 521 NYS2d 653 [1987])* hold that a claim for unjust enrichment *cannot be brought at all* if it is duplicative of a **[*470]** *contractual* claim. **[***184] [**323]** *State of New* ***[****42]*** *York v Barclays Bank of N.Y.* involved an unjust enrichment action "framed as one for money had and received" *(76 NY2d 533, 536 n 2, 563 NE2d 11, 561 NYS2d 697 [1990]*; *see also* Glen Banks, New York Contract Law § 4:27 [2d ed 28 West's NY Prac Series]). There, we held that the claim was not viable where the checks at issue were never actually or constructively delivered to the plaintiff (*76 NY2d at 540*). Those cases say nothing about avoided costs as damages, or anything about damages whatsoever, for that matter.[8]

Relying on *IDT Corp. v Morgan Stanley Dean Witter & Co. (12 NY3d 132, 907 NE2d 268, 879 NYS2d 355 [2009])*, the majority asserts that where a defendant avoids costs that would have been paid to third parties, the defendant is not enriched "at the expense of" the plaintiff (majority op at 457). That assertion suggests that TydenBrooks cannot bring its claim for unjust enrichment *at all*, because one of the elements of the claim is not satisfied—not that avoided costs are unavailable as damages to a plaintiff who has proved its claim. Indeed, in *IDT*, we held that the claim for unjust enrichment should be dismissed (*id. at 142*); we cannot hold that here. Furthermore, Morgan Stanley was not enriched "at IDT's expense" because IDT did not pay the investment banking fee Morgan Stanley allegedly received, nor was IDT deprived of any investment banking fee by Morgan Stanley's alleged **[****43]** misuse of IDT's confidential information, because IDT was not in the investment banking business (it was a telecommunications company) and was never going to be retained as an investment banker and receive investment banking fees. Certainly, an element of the claim of unjust enrichment is that the defendant must have been enriched at the plaintiff's expense; but it can hardly be said that pilfered commercially valuable trade secrets are not stolen "at the plaintiff's expense." Here, it **[12]** would be impossible to say so, in view of the jury's express finding in TydenBrooks' favor as to each of those elements, contained in black and white on the verdict sheet, which we may not disturb.

Even were it within our power to decide whether a cause of action for unjust enrichment lies here, and were one to read the majority opinion to say that it does not, that would be **[*471]** grave error, inconsistent with our precedents. Like the common-law action for unfair competition (*see supra at 468*), an action for unjust enrichment is an action in equity, not at law (*see Georgia Malone & Co., Inc. v Rieder, 19 NY3d 511, 516, 973 NE2d 743, 950 NYS2d 333 [2012]*; *Paramount Film Distrib. Corp. v State of New York, 30 NY2d 415, 421, 285 NE2d 695, 334 NYS2d 388 [1972])*. That TydenBrooks may have a remedy at law, restricted to its lost profits as the majority here announces, would not disable it from recovering in equity **[****44]** through unjust enrichment. Thus, in *Falk v Hoffman (233 NY 199, 201-202, 135 NE 243 [1922,* Cardozo, J.]), we held that although a shareholder suing at law could either rescind and recover the value of his shares, or affirm and recover the value of his shares less what he had been (fraudulently) **[***185] [**324]** paid for them, he could sue in equity to recover more:

> "[E]quity will intervene to declare the wrongdoers trustees. Some remedy at law there is. It is not so complete or effective as the remedy in equity. Suing at law, the plaintiff would be restricted to the value of his shares, if he rescinded, or to the difference between the value and par . . . , if he affirmed. Suing in equity, he may reach the proceeds of the resale, securities and cash, though the price upon resale is found to be greater than the value. . . . Equity will not be overnice in balancing the efficacy

[8] If cited to show that trade secret plaintiffs may not ever bring a claim for unjust enrichment, *Corsello* and *Clark-Fitzpatrick* hold nothing of the kind (because trade secret thieves do not usually steal by contract), and, as mentioned above, any such holding is far beyond the scope of the certified question.

of one remedy against the efficacy of another when action will baffle, and inaction may confirm, the purpose of the wrongdoer" (citations omitted).

We have consistently upheld the principle that a common-law cause of action for unjust enrichment prevents a defendant from retaining any benefit wrongly received. Unjust enrichment is "undoubtedly equitable and depends upon broad considerations of equity and **[****45]** justice" (*Paramount Film Distrib. Corp. at 421*; *see also Saunders v Kline, 55 AD2d 887, 888, 391 NYS2d 1 [1st Dept 1977]* ["it is not a necessary element of a cause of action for unjust enrichment to show that plaintiff suffered a loss corresponding to the gain received by the defendant"]).[9] Cambridge Security Seals was unjustly enriched by stealing to avoid **[*472]** development costs, which injured TydenBrooks. It would be against equity to allow the defendant to retain the value it received (*see Mandarin Trading Ltd. v Wildenstein, 16 NY3d 173, 182, 944 NE2d 1104, 919 NYS2d 465 [2011]*).

The answer to the question certified by the Second Circuit is obvious merely from stating the question: recovery of the benefit obtained by the defendant is the definition of an action for unjust enrichment: "The essential inquiry in any action for unjust enrichment . . . is whether it is against equity and good conscience to permit the defendant to *retain* what is sought to be *recovered*" (*Mandarin Trading at 182* [emphasis added], quoting *Paramount Film Distrib. Corp. at 421* **[13]**). Especially when defendant's enrichment has come about by wrongdoing, plaintiff's recovery may even include defendant's gains (*see* Restatement [Third] of Restitution and Unjust Enrichment § 51).

IV.

The most curious feature of the majority's opinion is that, by completely neglecting the availability of avoided costs as a measure of equitable damages, it answers the question in a way that renders the **[****46]** proffered answer irrelevant to the Second Circuit. We have recognized—and the majority does not dispute—that disgorgement of defendant's ill-gotten gains is available as an *equitable* remedy, including in cases involving intellectual property (*see* **[***186]** **[**325]** *Warren, Inc. v Turner's Gowns, 285 NY 62, 68, 32 NE2d 793 [1941]* [in unfair competition case based on trade name infringement, "equity will treat the wrongdoer as a trustee for the plaintiff so far as the former has realized profits from its acts. . . . Inability to prove damages would not preclude plaintiffs from recovering, on an accounting, profits realized from sales unlawfully made, together with interest thereon from the time of the commencement of the action"]; *Michel Cosmetics, Inc. v Tsirkas, 282 NY 195, 199, 26 NE2d 16 [1940]*; *New York Bank Note Co. v Hamilton Bank Note Engraving & Print. Co., 180 NY 280, 295-297, 73 NE 48 [1905]*; *Falk v Hoffman, 233 NY 199, 201, 135 NE 243 [1922]*).

[*473] To avoid our ancient, settled law that equity permits disgorgement of a defendant's ill-gotten gains, the majority tacitly interprets the word "damages" to mean damages historically recoverable at law, not in equity. The majority offers no reason for doing so, and does not even attempt to account for our decisions in *Warren, New York Bank Note*, or *Hoffman*. Interpreting the Second Circuit's questions as restricted to damages at law is in fundamental conflict with the manner in which federal courts have operated for the past **[****47]** 80 years, since their merger of law and equity in 1938. *Federal Rules of Civil Procedure rule 54 (c)* provides that, other than for default judgments, "[e]very . . . final judgment should grant the relief to which each party is entitled, even if the party has not demanded that relief in its pleadings." The Advisory Committee note explains that this portion of *rule 54 (c)* "makes clear that a judgment should give the relief to which a party is entitled, regardless of whether it is legal or equitable or both."[10]

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[9] The availability of unjust enrichment in trade secret actions is particularly equitable (***see*** Risch, *11 Marq Intell Prop L Rev at 59* ["Because the economic justification of trade secrets differs from the justification for patents and copyrights, disgorging unjust enrichment is important. If the competitor values the secret in an amount more than the owner will lose or if the court undervalues the amount of the owner's loss, then the competitor will have an incentive to spend more on appropriation. In turn, this will cause the owner to spend more on protection than it otherwise might need to if it had the remedy, leading to the same 'arms race' without a commensurate gain in expected social value. Thus, the law disgorges the additional benefit in order to reduce the competitor's incentive to focus more resources on appropriation"]).

[10] Wright and Miller's Federal Practice and Procedure § 2662 provides a full explanation:

"Perhaps most significantly *subdivision (c)* is designed to implement the merger of law and equity mandated by *Rule 2* by allowing relief to be given that is consistent with what is shown to be necessary to compensate the parties or remedy the situation without regard to the constraints of the antiquated and rigid forms of action. At common law it was held that

Federal courts, governed by rule 54 (c), award damages without regard to whether they arise from a legal or an equitable cause of action (*see e.g., In re Fasano/Harriss Pie Co., 848 F2d 190* ***[*474]*** *[6th Cir 1988]* [table; text at 1988 WL 44738, *2 (1988)] ["FMA next argues that it should not have been held liable under the equitable doctrine of unjust enrichment because the theory was not pleaded by plaintiffs. Rather, plaintiffs brought an action at law alleging that FMA had breached an express contract. Rule 54(c), however, supports **[***187]** **[**326]** the granting of equitable relief in such circumstances"]; *Kaszuk v Bakery & Confectionery Union & Indus. Intl. Pension Fund, 791 F2d 548, 559 [7th Cir 1986]* ["Rule 54(c) 'has been liberally construed, leaving no question that it is the court's duty to grant whatever relief is appropriate in the case on the facts proved.' This includes injunctive relief when appropriate, and even when not specifically **[****48]** requested" (citations omitted)], quoting *United States v Marin, 651 F2d 24, 31 [1st Cir 1981]*; *Travis v Gary Community Mental Health Ctr., Inc., 921 F2d 108, 112 [7th Cir 1990]* ["Fed.R.Civ.P. 54(c) requires courts to award the relief to which the prevailing party is entitled, even if that party did not request the relief or relied on the wrong statute"]).

Thus, the Second Circuit did not ask us whether avoided costs may be an appropriate measure at law but not in equity. Upon the jury's finding of liability, the federal courts are indifferent to under which of those branches the relief is available. The majority's opinion does not dispute the availability of a defendant's avoided costs as damages in equity. Indeed, the majority goes so far as to say that a defendant's gain may be used as "the method of computing damages" (majority op at 450 [emphasis omitted]). Thus, the majority's ostensible "no" is a practical "yes," unless we turn the clock back to 1937.

V.

Suppose, for a moment, that the majority is entirely right: although the answer is not dictated by our precedents, they suggest that plaintiffs cannot recover defendant's avoided costs as a measure of compensatory damages. The approach provided by nearly all other jurisdictions and the Restatement (Third) of Unfair Competition explicitly allows plaintiffs in trade secret cases to recover the plaintiff's cost of development or **[****49]** the defendant's avoided costs. That is of no moment to the majority. The suggestion that our court—the court that, in Judge Cardozo's time and thereafter, led the nation in advancing the laws that govern civil wrongs in contract, tort and equity—should turn a blind eye and disregard our duty "to bring the law into accordance with present day standards of wisdom and **[*475]** justice" (*Woods v Lancet, 303 NY 349, 355, 102 NE2d 691 [1951]*, quoting *Funk v United States, 290 US 371, 382, 54 S Ct 212, 78 L Ed 369 [1933]*), is most perplexing.

Underlying the majority's hidebound view that a plaintiff's lost profits must always be the remedy for theft of commercially valuable information of any type is a failure to comprehend the difference between private goods and public goods,[18] and therefore the reasons that some types of public goods, if they are to exist, require a damage remedy that, though not punitive, is not cabined to the plaintiff's lost profits. That is, the appropriate calculus for thefts of private goods should not constrain the calculus for thefts of public goods (*see e.g.* Roger D. Blair & Thomas F. Cotter, *An Economic Analysis of Damages Rules in Intellectual Property Law*, 39 Wm & Mary L Rev 1585, 1590 [1998] ["the optimal

plaintiff could not recover anything other than the relief specifically requested in the ad damnum clause of the complaint. In equity, however, the general practice was for plaintiff to demand whatever special relief desired and then to add a prayer for general relief. If the court decided that the evidence did not justify the specific remedy requested, it could rely on the general prayer for relief for the purpose of granting the relief to which plaintiff actually was entitled. Rule 54(c) adopts the more liberal approach used by the equity courts for all civil actions, whether they formerly would be brought at law or in equity, as long as defendant has not defaulted. In this way the rule effectuates one of the objectives of the federal rules—the development of a uniform procedure for all civil actions" (*See also* 10 Moore's Federal Practice—Civil § 54.70).

In any event, TydenBrooks expressly sought equitable relief in its complaint: "That the Defendants be adjudged to have been unjustly enriched . . . and that Defendants be required to disgorge the profits gained as a result of their conduct and actions and any other appropriate equitable remedy including that the Defendants be enjoined from such unlawful act or practice."

[18] Private goods are, in the Economics parlance, rivalrous and excludable. That is, if I consume my $5 sandwich, you cannot ("rivalrous"), and I can readily prevent you from consuming it ("excludable"). If I create a secret recipe for the sauce used on my sandwiches, your using the recipe does not stop me from using it too ("nonrivalrous"), and—absent legal protection—I cannot easily prevent you from using the recipe once you learn it ("nonexcludable").

set of damages rules should preserve both the incentive structure of intellectual property law and the property- **[***188]** **[**327]** like character of intellectual property rights . . . in the absence of enforcement, **[****50]** information, and other transaction costs, these goals require at a minimum an award that renders the infringer no better off as a result of the infringement"]; Mark A. Lemley, *The Surprising Virtues of Treating Trade Secrets as IP Rights*, *61 Stan L Rev 311, 329-330 [2008]* ["Trade secrets are best understood not as applications or extensions of existing common law principles (warranted or unwarranted), but as IP rights. . . . A right to exclude does not have to be absolute to be effective in rewarding and therefore encouraging innovation. It need merely provide sufficient advantage in terms of lead time or relative costs to minimize or eliminate the public goods problem"]).

The majority also abandons our role in crafting the common law to fulfill the policy goals of this State. The Supreme Court of the United States has identified the general policies behind trade secret law as the "maintenance of standards of commercial ethics and the encouragement of invention" (*Kewanee, 416 US at 481*). The legal protections against theft of advancements in the sciences, arts and industry—not to punish, but to spur innovation—is embodied in the United States Constitution **[*476]** (*US Const, art I, § 8, cl 8*). "Trade secret law will encourage invention in areas where patent law does not **[****51]** reach, and will prompt the independent innovator to proceed with the discovery and exploitation of his invention" (*Kewanee, 416 US at 485*; *see also* *Rockwell Graphic Sys., Inc. v DEV Indus., Inc., 925 F2d 174, 180 [7th Cir 1991]* ["trade secret protection is an important part of intellectual property, a form of property that is of growing importance to the competitiveness of American industry. . . . The future of the nation depends in no small part on the efficiency of industry, and the efficiency of industry depends in no small part on the protection of intellectual property"]).

New York, as the nation's commercial center and a hub of innovation, embodies those goals by fostering inventors and innovation; those are unmistakable goals of our legislative and executive branches (*see e.g.* Press Release, *Governor Cuomo Announces Highlights of the FY 2019 Budget* [Mar. 30, 2018] [announcing budget includes "$600 million to support construction of a world-class, state-of-the-art life sciences public health laboratory in the Capital District that will promote collaborative public/private research and development partnerships"]; Governor Andrew Cuomo, State of the State Address to 2015 New York Legislature [announcing "new innovation hotspots . . . (to) provide one-stop funding and services—legal **[****52]** services, accounting services, all the services (inventors) need to grow their business"]).

What commercial ethics or invention is encouraged by the majority's decision? What does that decision bode for our role in molding the common law to changing times? By rejecting the predominant rule accepted by most states and the Restatement, the majority undermines the policy goals of this State and casts off our mantle. Under the majority's rule, I am encouraged to steal your trade secrets. If I can make better use of them than you, because I am a better salesperson, better funded or a cheaper purchaser of inputs, even if I lose when you sue me, I can make a net profit, repaying you only what you can prove you lost in sales. If I am not better suited to exploit your trade secrets, I **[14]** may nevertheless profit if you are unable to prove your lost sales, which, because of the messiness of the real world, is often difficult or impossible to do. At worst, I may be subjected to an injunction, but at that point, the secret has begun to leak out, and you will be hard-pressed to prove **[***189]** **[**328]** that some third, fourth or fifth party derived its identical **[*477]** process from your secret. The incentive for others to innovate **[****53]** will be replaced by the incentive to steal. Punitive damages, of course, remain as a deterrent, but because many trade secrets are allegedly stolen by employees moving from one company to another (which, quite correctly, the law does not restrain per se), the theft is difficult enough to prove, and punitive damages in those situations are uncommon, as this case itself demonstrates. Likewise, although you may have purposefully refrained from licensing your secret to anyone, you may be forced to accept a "reasonable royalty" from the defendant as damages, based on a conjectural price at which you might have licensed your secret—a sort of eminent domain power for thieves.

Cases such as this, "where a decision one way or the other, will count for the future, will advance or retard, sometimes much, sometimes little, the development of the law . . . are the cases where the creative element in the judicial process finds its opportunity and power" (Benjamin Cardozo, *The Nature of the Judicial Process* 165 [Yale University Press 1921]). Judge Cardozo set that course for us a century ago; I am saddened we shirk from it; doubly so when the Second Circuit has steered us to it.

Chief Judge DiFiore and Judges Stein and Garcia concur; Judge Wilson dissents in an opinion in which Judges Rivera and Fahey concur.

Following certification of questions **[****54]** by the United States Court of Appeals for the Second Circuit and acceptance of the questions by this Court pursuant to section 500.27 of the Rules of Practice of the Court of Appeals *(22 NYCRR 500.27)*, and after hearing argument by counsel for the parties and consideration of the briefs and record submitted, first certified question answered in the negative and second certified question not answered as unnecessary.

Fruchthandler v. Green

Supreme Court of New York, Appellate Division, First Department

November 19, 1996, Decided ; November 19, 1996, ENTERED

59103

Reporter

233 A.D.2d 214 *; 649 N.Y.S.2d 694 **; 1996 N.Y. App. Div. LEXIS 11790 ***

Abraham H. Fruchthandler, Individually and as General Partner on Behalf of FBE, Ltd., Formerly Known as Fruchthandler Brothers Enterprises, Appellant, v. Israel Green, Respondent.

Counsel: **[***1]** For Plaintiff-Appellant: Jonathan David Bachrach.

For Defendant-Respondent: Sheldon Eisenberger.

Judges: Concur--Sullivan, J. P., Ellerin, Nardelli, Tom and Andrias, JJ.

Opinion

[*214] **[**695]** Order, Supreme Court, New York County (Ira Gammerman, J.), entered on or about July 7, 1995, which, *inter alia,* granted defendant's motion to dismiss the amended complaint for failure to state a cause of action, unanimously affirmed, with costs.

Deeming the allegations in the amended complaint to be true and affording plaintiff the benefit of all favorable inferences and implications that may be drawn from the amended complaint (*Underpinning & Found. Constructors v Chase Manhattan Bank, 46 NY2d 459*), it was properly dismissed for failure to state a cause of action since the release plaintiff executed relieved defendant from liability under two promissory notes, and the allegations that such release was procured through economic duress were insufficient (*cf., Bloss v Va'ad Harabonim, 203 AD2d 36*; *Wilf v Halpern, 194 AD2d 508*, *lv dismissed 82 NY2d 846*). To succeed on a duress theory, plaintiff would have to show he was compelled to agree to the terms of the release **[***2]** by means of a wrongful threat which precluded the exercise of his free will (*Muller Constr. Co. v New York Tel. Co., 40 NY2d 955*). On its face, however, the record reveals that the release resulted from vigorous bargaining tactics which do not amount to economic duress (*Laub & Co. v* ***[*215]*** *Domansky, 172 AD2d 289*), notwithstanding financial considerations which may have induced plaintiff to enter into the agreement (*Bethlehem Steel Corp. v Solow, 63 AD2d 611*; **[**696]** *Walbern Press v C.V. Communications, 212 AD2d 460*). Moreover, at the time the release was entered into, defendant surrendered his partnership interest in certain properties to plaintiff. Having accepted the benefits of the agreement before commencing this action, plaintiff, in effect, ratified the release and is therefore barred from alleging economic duress in its execution (*Goldstein Prods. v Fish, 198 AD2d 137, 138)*. The claim of economic duress was also waived in light of the inordinate length of time which passed between the alleged duress and the assertion of the claim (*Joseph F. Egan, Inc. v City of New York, 17 NY2d 90, 98*; *Bethlehem Steel Corp. v Solow, supra,* ***[***3]*** *at 612*).

The cause of action for unjust enrichment was also properly dismissed since defendant provided consideration for the release and thus plaintiff's conclusory allegations that it would be against equity and good conscience to permit defendant to retain what was sought to be recovered are insufficient (*see, Paramount Film Distrib. Corp. v State of New York, 30 NY2d 415, 421*, *mot to amend remittitur granted 31 NY2d 678*, *cert denied 414 US 829*).

We have considered plaintiff's remaining contentions and find them to be without merit.

Concur--Sullivan, J. P., Ellerin, Nardelli, Tom and Andrias, JJ.

End of Document

Goddard v. Martino

Supreme Court of New York, Dutchess County

June 24, 2013, Decided

556/2012

Reporter
40 Misc. 3d 1050 *; 970 N.Y.S.2d 382 **; 2013 N.Y. Misc. LEXIS 2996 ***; 2013 NY Slip Op 23240 ****; 2013 WL 3742580

[**1]** Donald J. Goddard, Plaintiff, v Thomas J. Martino et al., Defendants.

Counsel: **[***1]** *Drake Loeb Heller Kennedy Gogerty Gaba & Rodd PLLC*, New Windsor (*Stephen J. Gaba* of counsel), for defendants. *Jonathan Lovett*, White Plains, for plaintiff.

Judges: Hon. Peter M. Forman, Acting Supreme Court Justice.

Opinion by: Peter M. Forman

Opinion

[*1051] **[**383]** Peter M. Forman, J.

[**2]** Plaintiff is a former member of the Town of Hyde Park Police Department. The individually named defendants are a former Town Supervisor and three former **[**384]** Town Councilmen (collectively, the Town Board). This action seeks compensatory and punitive damages on the grounds that defendants obstructed or defeated plaintiff's civil service rights in violation of *Civil Service Law § 106*.

Defendants now move for an order dismissing the complaint pursuant to *CPLR 3212*. That motion is granted for the reasons stated herein.

Background

In 1986, plaintiff was hired to work as a police officer in the Town of Hyde Park Police Department. He was promoted to Sergeant in 1988, and was promoted to Lieutenant in 2004. Plaintiff held each of these positions on a permanent competitive civil service basis.

On or about November 1, 2009, **[***2]** plaintiff was named the provisional Chief of Police. This appointment was made on a provisional basis because plaintiff had not yet taken or passed the civil service examination necessary to qualify for a permanent **[*1052]** appointment as Chief of Police. The Lieutenant position was not filled after plaintiff was appointed provisional Chief of Police.

Plaintiff alleges that a promotional exam was scheduled for March of 2010, and that it was "understood and agreed" at the time that he was provisionally appointed that he would be promoted to Chief of Police on a permanent basis if he passed that examination. Plaintiff also alleges that it was "understood and agreed" that the examination would be conducted on a promotional basis, making plaintiff the only person eligible to take the examination. Plaintiff also alleges that it was also understood and agreed that plaintiff would continue to serve as the provisional Chief of Police if he failed the promotional examination.

The individually named defendants were elected on November 4, 2009, and took office for the first time on January 1, 2010. Ten days later, the newly-elected Town Board decided that the Chief of Police civil service examination would **[***3]** be conducted on an open and competitive basis, rather than on a promotional basis.

Plaintiff and defendants have made numerous allegations against each other relating to the events that transpired during the relatively short period of time that plaintiff served as the Town's provisional Chief of Police. While there are significant discrepancies in the competing factual accounts that have been provided by the parties on this motion, it is evident that the relationship between plaintiff and the newly-elected Town Board quickly became toxic.

On March 10, 2010, plaintiff submitted a letter expressing his intent to retire from the **[****3]** Town of Hyde Park Police Department effective April 10, 2010. That letter cited his concerns about the direction the Town Board was taking the police department, and the "almost total lack of communication" between plaintiff and the Town Board.

Plaintiff alleges that he submitted this retirement letter because: (1) he had become aware that the Town Board was contemplating abolishing the position of Lieutenant, and (2) he was advised by a member of the Town Board that he would never be appointed as the permanent Chief of Police, regardless of his performance on the **[***4]** civil service examination. Plaintiff alleges that under these circumstances, he felt compelled to retire in order to preserve his health benefits, which would be forfeited if his employment ended due to termination rather than retirement.

[*1053] On March 22, 2010, the Town Board adopted a Resolution abolishing the Lieutenant position. The March 22, 2010 Resolution did not expressly identify the date **[**385]** that this abolition would become effective, but authorized the Town Supervisor to execute any documents that were necessary to effectuate that abolition.

On June 16, 2010, the Town Board adopted a second Resolution purporting to "clarify" the March 22, 2010 Resolution. Specifically, the June 16, 2010 Resolution states that the Lieutenant position was abolished effective April 14, 2010.

Plaintiff alleges that the Town Board abolished the Lieutenant position in order to prevent him from being reinstated to that position once the permanent Chief of Police position was filled. Although the Town Board asserted that the Lieutenant position was being abolished for financial reasons, plaintiff alleges that this financial justification was a pretext, and that the Town Board was manipulating the civil service **[***5]** system in order to prevent plaintiff from being reinstated as Lieutenant.

In support of this pretext argument, plaintiff alleges that the Town Board learned after the March 22, 2010 Resolution was adopted that plaintiff would be placed on a preferred eligibility list if the Lieutenant position had been abolished prior to his April 10, 2010 retirement. Upon being placed on a preferred eligibility list, plaintiff would be entitled to reappointment if the Lieutenant position was reinstated. Plaintiff alleges that the April 14, 2010 abolition date identified in the June 16, 2010 Resolution was selected for the sole purpose of preventing plaintiff from being placed on that preferred eligibility list.

Plaintiff also argues that the financial justification advanced by the Town Board was a pretext because the Town did not realize any savings as a result of the temporary abolition of this office. Specifically, plaintiff asserts that the Lieutenant position was unfunded at the time that it was abolished, that the Town Board reinstated the Lieutenant position on January 1, 2011, and that the Town Board filled that position on January 10, 2011. Therefore, plaintiff argues that the Town did not realize **[***6]** any immediate or long-term savings as a result of the temporary abolition of the Lieutenant position, and that preventing plaintiff from being reinstated as Lieutenant was the only objective actually achieved by the Resolutions.

Plaintiff also alleges that the Town presented him with a proposed letter in December of 2010, by which plaintiff would waive and relinquish any claim that he might have to reinstatement **[*1054]** as a Lieutenant in the Town Police Department. Plaintiff refused to sign that letter.

Plaintiff did not commence a CPLR article 78 proceeding challenging the March 22, 2010 and June 16, 2010 Resolutions abolishing the Lieutenant position, the January 1, 2011 Resolution reinstating and funding the Lieutenant position, or the January 10, 2011 appointment filling the **[****4]** Lieutenant position. Instead, plaintiff filed a notice of claim with the Town on March 11, 2011. The notice of claim alleged that defendants obstructed or defeated his civil service rights in violation of *Civil Service Law § 106*. After a hearing was conducted on that notice of claim pursuant to *General Municipal Law § 50-h*, plaintiff commenced this litigation asserting a private cause of action based upon defendants' alleged **[***7]** violation of *Civil Service Law § 106*.

Defendants have moved for summary judgment dismissing the complaint on the grounds, inter alia, that no private cause of action is available under *Civil Service Law § 106*. Defendants also argue that even if a cause of action was available under *Civil Service Law § 106*, plaintiff still would have been required to commence an article 78 proceeding successfully **[**386]** challenging the Resolutions before commencing this action. Defendants also argue that any cause of action that plaintiff may have under the Civil Service Law is barred by a one-year statute of limitations, and that the factual record demonstrates that defendants did not violate *Civil Service Law § 106* as a matter of law. Defendants also argue that plaintiff is barred from seeking punitive damages against the Town of Hyde Park as a matter of law.

Discussion

Civil Service Law § 106 makes it a misdemeanor to defeat, deceive or obstruct the civil service rights of any person who seeks appointment, promotion, or reinstatement to a covered civil service position. Civil Service Law § 106 also makes it a misdemeanor to make false representations about a person for purposes of improving or injuring their **[***8]** chances of obtaining appointment, promotion, or reinstatement to a covered civil service position. Civil Service Law § 106 does not expressly make a private cause of action available to individuals who believe that their civil service rights have been violated.

While Civil Service Law § 106 clearly prohibits interference with an individual's civil service rights, that statutory proscription "does not necessarily carry with it a right of private enforcement by means of tort litigation." (***Uhr v East Greenbush*** ***[*1055]*** ***Cent. School Dist.****, 94 NY2d 32, 38, 720 NE2d 886, 698 NYS2d 609 [1999*, Rosenblatt, J.].) "Where a penal statute does not expressly confer a private right of action on individuals pursuing civil relief, recovery under such a statute 'may be had only if a private right of action may be fairly implied.' " (***Hammer v American Kennel Club****, 1 NY3d 294, 299, 803 NE2d 766, 771 NYS2d 493 [2003]*, quoting ***Sheehy v Big Flats Community Day****, 73 NY2d 629, 633, 541 NE2d 18, 543 NYS2d 18 [1989]*.) In assessing whether a private right of action can be implied, the Court of Appeals has emphasized that "the Legislature has both the right and the authority to select the methods to be used in effectuating its goals, as well as to choose the goals themselves." (***Id****. at 299*, quoting **[***9]** ***Sheehy*** *at 634*.)

When assessing whether a statute provides an implied right to a private cause of action,

> "the essential factors to be considered are: (1) whether the plaintiff is one of the class for whose particular benefit the statute was enacted; (2) whether recognition of a private right of action would promote the legislative purpose; and (3) whether creation of such a right would be consistent with the legislative scheme." (***Sheehy v Big Flats Community Day****, 73 NY2d at 633*.)

The first factor is the one that is most easily satisfied (***id****. at 634*). When a statute seeks to deter certain conduct, the second factor will be satisfied upon a determination that a private **[****5]** cause of action for injuries arising from this prohibited conduct would further the statute's deterrent goal (***id****. at 634*).

Plaintiff clearly falls within the class of people for whose benefit Civil Service Law § 106 was enacted. Recognizing a private cause of action under Civil Service Law § 106 would also clearly advance the statute's deterrent goal. Therefore, the first two *Sheehy* prongs have been satisfied.

The third factor—i.e., whether a private right of action is consistent with the legislative scheme— **[***10]** is generally recognized as the most important factor (***id****. at 634* **[**387]** *see also* ***Carrier v Salvation Army****, 88 NY2d 298, 302, 667 NE2d 328, 644 NYS2d 678 [1996]*; ***Brian Hoxie's Painting Co. v Cato-Meridian Cent. School Dist.****, 76 NY2d 207, 212, 556 NE2d 1087, 557 NYS2d 280 [1990]*). "It is not always easy to distinguish this 'consistency' prong from the second *Sheehy* prong, which centers on 'promotion' of the legislative goal." (***Uhr v East Greenbush Cent. School Dist.****, 94 NY2d at 40*.) Even where a private cause of action would promote the goals of a statute, the existence of a private cause of action and a government enforcement mechanism "may disserve **[*1056]** the goal of consistency—like having two drivers at the wheel. Both may ultimately, at least in theory, promote statutory compliance, but they are born of different motivations and may produce a different allocation of benefits owing to differences in approach." (***Id****. at 40*.) When an implied private cause of action would subject a municipality to potential financial liability, this third factor will not be satisfied unless there is "clear evidence of the Legislature's willingness to expose the governmental entity to liability that it might not otherwise incur." (***Id****. at 42*.)

Civil Service Law § 6 **[***11]** requires the state civil service commission to develop suitable rules and regulations implementing the requirements of the Civil Service Law and article V, § 6 of the State Constitution. That comprehensive regulatory framework has been adopted as chapter 4 of the Official Compilation of Codes, Rules and Regulations of the State of New York. Civil Service Law § 20 also requires each municipal civil service commission to develop a set of civil service rules and regulations. The Dutchess County Department of Personnel, which is the municipal civil service commission for all towns in this county (Civil Service Law § 17 [1]), has promulgated a comprehensive set of civil service rules pursuant to its statutory mandate.

Article V of the Civil Service Law, and the rules and regulations promulgated thereunder, establish a complex statutory and regulatory framework defining the applicable civil service rights when a covered position is abolished. These rights include the right to reinstatement if the position is restored, and the right to placement on a preferred eligibility list pending such restoration. Civil Service Law § 106 prohibits unlawful interference with these civil service rights. Civil Service Law § 102 (3) **[***12]** authorizes a state or municipal civil service commission to commence an action in the New York State Supreme Court to enjoin any alleged violation of the Civil Service Law and rules, and to seek such incidental relief as may be necessary. However, Civil Service Law § 102 does not extend a corresponding right to commence a private cause of action to enjoin, or seek monetary damages arising from, such violations.

There is no clear evidence that the legislature intended to expose municipalities to the risk of financial liability for a violation of Civil Service Law § 106. Rather, Civil Service Law § 102 (3) squarely places the authority for enforcement of Civil Service Law § 106 on the appropriate municipal civil service commission. Read in combination, these sections demonstrate that **[*1057]** the legislature intended to limit enforcement of Civil Service Law § 106 to criminal **[****6]** proceedings (to punish past violations), and to actions by the appropriate municipal civil service commission seeking injunctive relief (to prevent continued violations). (*See* ***McLean v City of New York***, 12 NY3d 194, 200-201, 905 NE2d 1167, 878 NYS2d 238 [2009]; ***Hammer v American Kennel Club***, 1 NY3d at 299.) **[**388]** Recognizing an implied private cause **[***13]** of action under these circumstances would run contrary to that legislative intent, and would essentially place "two drivers at the wheel" who are possessed "of different motivations and may produce a different allocation of benefits owing to differences in approach." (***Uhr v East Greenbush Cent. School Dist.***, 94 NY2d at 40.) Therefore, the complaint must be dismissed as a matter of law because Civil Service Law § 106 "does not make an express provision for civil damages, and a private right of action cannot fairly be implied for the plaintiff under these circumstances." (***Kenneth H. Brown & Co., Inc. v Dutchess Works One-Stop Empl. & Training Ctr., Inc***., 73 AD3d 984, 986, 904 NYS2d 75 [2d Dept 2010].)

Plaintiff argues that the Third Department has already determined that a private cause of action is available under Civil Service Law § 106 (***Matter of Leisner v Bahou***, 97 AD2d 860, 469 NYS2d 255 [3d Dept 1983]), and that this court is bound by that determination in the absence of contrary appellate authority. However, plaintiff's reliance on Leisner is misplaced.

This court is certainly obligated to follow precedent established by the Third Department when there is no conflicting appellate authority **[***14]** in the other departments of the Appellate Division. However, "a case 'is precedent only as to those questions presented, considered and squarely decided.' " (***Wellbilt Equip. Corp. v Fireman***, 275 AD2d 162, 719 NYS2d 213 [1st Dept 2000], quoting ***People v Bourne***, 139 AD2d 210, 216, 531 NYS2d 899 [1st Dept 1988].) "Principles are not established by what was said, but by what was decided, and what was said is not evidence of what was decided, unless it relates directly to the question presented for decision." (***Robinson Motor Xpress, Inc. v HSBC Bank, USA***, 37 AD3d 117, 123-124, 826 NYS2d 350 [2d Dept 2006], quoting ***People ex rel. Metropolitan St. Ry. Co. v State Bd. of Tax Commrs.***, 174 NY 417, 447, 67 NE 69 [1903], *affd* 199 US 1, 25 S Ct 705, 50 L Ed 65 [1905].)

In *Leisner*, the petitioner brought an article 78 proceeding challenging the termination of his employment by the Department of Social Services. The petitioner also asserted claims seeking monetary damages for alleged violations of his civil rights under 42 USC § 1985, and alleged violations of his civil **[*1058]** service rights under Civil Service Law § 106. The Third Department concluded that these monetary damages claims should not have been joined with the petitioner's **[***15]** article 78 proceeding. The Third Department also concluded that the allegations contained in the pleadings failed to sufficiently particularize petitioner's claims for purposes of his section 1985 claim but that, giving him the benefit of every inference, these allegations sufficiently stated a claim under Civil Service Law § 106.

The ***Leisner*** Court did not find that a private cause of action can be fairly implied from Civil Service Law § 106 and the relevant statutory and regulatory framework. There is no indication that this issue was ever presented to or considered by the Third Department, and it was certainly never squarely decided. Rather, the *Leisner* Court merely presupposed that a private cause of action was available under the statute, and then assessed the adequacy of petitioner's allegations under that presumed cause of action. Therefore, ***Leisner*** does not have binding precedential value for purposes of determining whether a private cause of action can be fairly implied from Civil Service Law § 106. **[****7]**

[389]** Even if a private cause of action was available under Civil Service Law § 106, the complaint would still be subject to dismissal as a matter of law because a successful article 78 proceeding **[***16]** is a prerequisite to a claim for monetary damages arising out of defendants' alleged manipulation of the civil service system. (*See* ***Austin v Board of Higher Educ. of City of N.Y.****, 5 NY2d 430, 443-444, 158 NE2d 681, 186 NYS2d 1 [1959]*; ***Meyers v City of New York****, 208 AD2d 258, 265, 622 NYS2d 529 [2d Dept 1995]*; ***Feraca v Town of Esopus****, 63 AD2d 771, 404 NYS2d 753 [3d Dept 1978]*.) Specifically, "[a] public employer may abolish civil service positions for the purpose of economy or efficiency, as long as the position is not abolished as a subterfuge to avoid statutory protection afforded civil servants before they are discharged." (***Matter of Chandler v Village of Spring Val.****, 104 AD3d 847, 962 NYS2d 297 [2d Dept 2013]*, quoting ***Matter of Civil Serv. Empls. Assn., Inc., Local 1000, AFSCME, AFL-CIO v Rockland County Bd. of Coop. Educ. Servs.****, 39 AD3d 641, 642, 834 NYS2d 263 [2d Dept 2007]*.) When a public employer has abolished a civil service position for improper reasons not related to economy or efficiency, a person whose civil service rights have been infringed by that misconduct has standing to bring an article 78 proceeding, either in the nature of mandamus or certiorari to review. (*See Matter of Arnold v Erie County Med. Ctr. Corp., 59 AD3d 1074, 1077, 873 NYS2d 789 [4th Dept 2009]*; **[***17]** *Matter of Triana v Board of Educ. of City School* ***[*1059]*** *Dist. of City of N.Y., 47 AD3d 554, 557-558, 849 NYS2d 569 [1st Dept 2008]*; ***Matter of Terrible v County of Rockland****, 81 AD2d 837, 438 NYS2d 840 [2d Dept 1981]*.)

Plaintiff asserts that an article 78 proceeding should not be a prerequisite to his *Civil Service Law § 106* claim because he does not have standing to bring such a proceeding against defendants. This argument is without merit. Plaintiff alleges that he was forced to submit his March 10, 2010 retirement letter to preserve his health insurance benefits before the Town Board adopted the March 22, 2010 Resolution abolishing the Lieutenant position, and that this Resolution was motivated by an improper desire to deprive plaintiff of his statutory right to return to that position. Therefore, plaintiff had standing to commence an article 78 proceeding challenging the March 22, 2010 Resolution on the grounds that he was forced to retire because the Lieutenant position was being abolished, not for the purpose of economy or efficiency, but as a subterfuge to deprive plaintiff of his civil service rights.

Similarly, plaintiff alleges that the Town Board did not adopt the June 16, 2010 Resolution to clarify the March 22, 2010 **[***18]** Resolution, but rather to manipulate its effective date to prevent plaintiff from being placed on the preferred eligibility list. Therefore, plaintiff also had standing to commence an article 78 proceeding challenging the June 16, 2010 Resolution, on the grounds that the effective date of abolition was retroactively adopted for the strategic purpose of preventing plaintiff from being placed on a preferred eligibility list for that position.

Plaintiff also argues that an article 78 proceeding should not be a prerequisite to his *Civil Service Law § 106* claim because he does not seek reinstatement and back pay. Specifically, plaintiff asserts that he only

> "seeks damages for the deliberate impairment/defeat, by reason of the manipulation of the effective date of abolition of the Lieutenant position, of his otherwise entitlement to have his name on a preferred eligible list which would have insured his reinstatement to the Lieutenant position when it was re-established and **[**390]** funded in 2011." (Plaintiff's mem of law at 11 n 3.)

Whether plaintiff chooses to characterize his monetary damages claim as back pay is not controlling. It is clear that plaintiff's alleged damages are directly **[***19]** related to his claim that the **[****8]** Town Board manipulated the civil service system to prevent **[*1060]** plaintiff from being reinstated as a Lieutenant in the Town Police Department.

In any event, the obligation to bring an article 78 proceeding as a prerequisite to an action for monetary damages is not limited to an action seeking reinstatement or back pay. That obligation applies equally to an action in which a former public employee seeks damages as a principal form of relief, after having resigned in anticipation of an impending termination. (***Finley v Giacobbe****, 79 F3d 1285 [2d Cir 1996]*.) Therefore, even if a private cause of action was available under *Civil Service Law § 106*, the complaint would still be subject to dismissal as a matter of law because plaintiff failed to first commence a successful article 78 proceeding.

Defendants also moved for summary judgment on several alternative grounds in the event that this court found both that a private cause of action exists under *Civil Service Law § 106*, and that plaintiff was not obliged to bring a successful article 78 proceeding as a prerequisite to commencing this action. Although defendants' motion for summary judgment has been granted **[***20]** for the reasons stated above, the court will address those remaining alternative arguments briefly.

Defendants moved for summary judgment dismissing the complaint on the grounds that any cause of action that plaintiff may have under the Civil Service Law is barred by a one-year statute of limitations. The applicable limitations period for a private cause of action enforcing a penalty created by statute is one year. (*CPLR 215 [4]*.) This action was commenced on January 30, 2012, which is more than one year after the Lieutenant position was abolished, restored and filled. Therefore, defendants' motion for summary judgment based on this alternative statute of limitations defense is granted.

Defendants also moved for summary judgment dismissing the complaint on the grounds that the defendants did not violate *Civil Service Law § 106* as a matter of law. However, there are significant, material discrepancies in the competing factual accounts that have been provided by the parties on this motion. Defendants' motion for summary judgment on the merits of any *Civil Service Law § 106* claim that may exist is denied because there are material issues of fact on that substantive claim.

Finally, defendants **[***21]** have moved for partial summary judgment on the grounds that plaintiff is barred from seeking punitive damages against the Town of Hyde Park as a matter of law. Punitive damages are not available against a town. (***Sharapata [*1061] v Town of Islip***, *56 NY2d 332, 339, 437 NE2d 1104, 452 NYS2d 347 [1982]*; *see also* ***Volunteer Fire Assn. of Tappan, Inc. v County of Rockland***, *101 AD3d 853, 857, 956 NYS2d 102 [2d Dept 2012]*; ***Matter of Gillen v Giordano***, *297 AD2d 678, 679, 747 NYS2d 186 [2d Dept 2002]*; ***M. C. D. Carbone, Inc. v Town of Bedford***, *98 AD2d 714, 714, 469 NYS2d 117 [2d Dept 1983]*.)

Therefore, defendants' alternate motion for partial summary judgment dismissing the punitive damages claim as against the Town of Hyde Park is granted. It is therefore ordered, that defendants' motion for summary judgment dismissing the **[**391]** complaint pursuant to *CPLR 3212* is granted for the reasons stated herein.

End of Document

Goel v. Ramachandran

Supreme Court of New York, Appellate Division, Second Department

November 20, 2013, Decided

2012-04022

Reporter

111 A.D.3d 783 *; 975 N.Y.S.2d 428 **; 2013 N.Y. App. Div. LEXIS 7655 ***; 2013 NY Slip Op 7708 ****; 2013 WL 6083436

[**1]** Vikas Goel et al., Respondents, v Anush Ramachandran, Defendant, and Bunge Ltd. et al., Appellants. (Index No. 50017/10)

Subsequent History: Related proceeding at, Motion granted by, Dismissed by, in part, Dismissed without prejudice by, in part *Goel v. Am. Digital Univ., Inc., 2015 U.S. Dist. LEXIS 103612 (S.D.N.Y., Aug. 6, 2015)*

Prior History: *Goel v. Ramachandran, 2012 N.Y. Misc. LEXIS 6764 (N.Y. Sup. Ct., Apr. 4, 2012)*

Counsel: **[***1]** Reed Smith, LLP, New York, N.Y. (Wendy H. Schwartz and Jennifer L. Achilles of counsel), for appellants.

Nixon Peabody, LLP, New York, N.Y. (Robert C. Sentner, Nicole F. Mastropieri, and Cassandra R. Hamar of counsel), for respondents.

Judges: PETER B. SKELOS, J.P., RUTH C. BALKIN, JEFFREY A. COHEN, ROBERT J. MILLER, JJ. SKELOS, J.P., BALKIN, COHEN and MILLER, JJ., concur.

Opinion

[*783] [431]** In an action, inter alia, to recover damages for unjust enrichment, aiding and abetting a fraud, and money had and received, the defendants Bunge Ltd. and Bunge S.A. appeal, as limited by their brief, from so much of an order of the Supreme Court, Westchester County (Scheinkman, J.), dated April 4, 2012, as denied those branches of their motion pursuant to *CPLR 3211 (a)* which were to dismiss the first, second, and fifth causes of action insofar as asserted against them.

Ordered that the order is reversed insofar as appealed from, on the law, with costs, and those branches of the motion of the defendants Bunge Ltd. and Bunge S.A. pursuant to *CPLR 3211 (a)* which were to dismiss the first, second, and fifth causes of action insofar as asserted against them are granted.

The plaintiffs, Vikas Goel and Rainforest Trading, **[***2]** Ltd. (hereinafter Rainforest), commenced this action against the defendants, Anush Ramachandran, Bunge Ltd., and Bunge S.A. The plaintiffs alleged that they lost approximately $100 million as a result of a fraudulent scheme orchestrated by the defendants.

The amended complaint (hereinafter the complaint) alleged that Goel, a resident of Dubai, owned 99.99% of eSys Technologies Pte Ltd. (hereinafter eSys), a company incorporated under the laws of Singapore. In 2006, Goel was contacted by a representative **[*784]** of Teledata Informatics (hereinafter Teledata), a company organized under the laws of the British Virgin Islands. The representative informed Goel that Teledata was interested in acquiring shares of eSys.

By agreement dated November 29, 2006 (hereinafter the Share Subscription Agreement), Teledata agreed to purchase 51% of the shares of eSys. The complaint alleged that the purchase price was originally $105 million, then subsequently increased to $120 million. The transaction was to be accomplished through the creation of Rainforest, which was to serve as a holding company. Pursuant to the Share Subscription Agreement, Goel transferred all of his shares of eSys to Rainforest. The complaint **[***3]** alleged that in return, Rainforest issued 65 million shares to **[****2]** Goel and 55 million shares to Teledata. Goel then transferred 6.5 million of his shares in Rainforest to Teledata, which, in turn, **[**432]** pledged those shares to the State Bank of India as collateral for an $80 million loan.

The complaint alleged that Teledata was to invest $25 million of its own funds along with the $80 million loan from the State Bank of India. A bank account was established for Rainforest to enable Teledata to transfer the purchase funds pursuant to the Share Subscription Agreement. The complaint alleged that, since Teledata obtained the controlling interest in Rainforest after the distribution of the Rainforest shares, it "assumed the managerial role[ ] of the majority shareholder" and had "control over disbursements from [Rainforest's] bank account."

The complaint alleged that "Teledata did not intend to, and did not, invest the $25 million into Rainforest that it had agreed to." The complaint alleged that Teledata "ultimately transferred only a small fraction of the money, a substantial part of which was re-routed back to Teledata." The complaint specified that instead of transferring the $25 million into **[***4]** Rainforest's account, Teledata transferred "much smaller sums" into the Rainforest account, then caused those sums to be transferred out of Rainforest's account to the defendant Bunge S.A. and to separate, unidentified entities that were allegedly controlled by Ramachandran. The complaint further alleged that Bunge S.A. claimed that it was entitled to the money it received from the Rainforest account pursuant to contracts it had with Teledata, pursuant to which Teledata owed it money.

The complaint alleged that "all of the funds that were transferred out of the Rainforest Account were transferred either directly or indirectly through Ramachandran-controlled companies, into Bunge accounts" and that these funds were, in turn, "transferred to Teledata, or Teledata-controlled companies **[*785]** to be 're-invested' into Rainforest." The plaintiffs asserted that "[b]y doing this, Teledata, ultimately had records showing that it had invested $25 million into Rainforest, while in truth, it had not done so. Rather, it had wired much smaller amounts into Rainforest, but by the circular pattern described above, wired such amounts over and over again, so that it appeared it had invested much more."

The complaint **[***5]** asserted five causes of action against the defendants. As relevant here, four causes of action were asserted against Bunge Ltd. and Bunge S.A. (hereinafter together the Bunge defendants): the first cause of action was for money had and received, the second cause of action alleged unjust enrichment, the third cause of action alleged tortious interference with contract, and the fifth cause of action alleged aiding and abetting fraud. These four causes of action were asserted directly against Bunge S.A. for its allegedly tortious conduct. With respect to Bunge Ltd., the complaint alleged that Bunge S.A. was its alter ego, and the four causes of action described above were asserted against Bunge Ltd. under a theory of piercing the corporate veil.

The Bunge defendants thereafter moved to dismiss the complaint insofar as asserted against them pursuant to *CPLR 3211 (a) (7)* and insofar as asserted against Bunge S.A. pursuant to *CPLR 3211 (a) (8)*. The Bunge defendants contended, inter alia, that the Supreme Court lacked personal jurisdiction over Bunge S.A., a corporation located and incorporated in Switzerland. The Bunge defendants further contended that the complaint failed to state a cause of **[***6]** action for money had and received, unjust enrichment, or aiding and abetting fraud, and that the complaint was insufficient to state a cause of action against Bunge Ltd. under a theory of piercing the corporate veil. The Bunge defendants also argued that the complaint **[**433]** failed to state a cause of action to recover damages for tortious interference with contract and that, in any event, any such cause of action was time-barred.

The plaintiffs opposed the motion of the Bunge defendants. The plaintiffs contended, among other things, that the Supreme Court had personal jurisdiction over Bunge S.A. under the "mere department" and agency tests for personal jurisdiction by virtue of its relationship with Bunge Ltd., a corporation with its principal place of business in New York. The plaintiffs further contended that they had made a "sufficient start" in demonstrating that facts "may exist" which would establish personal jurisdiction over Bunge S.A. such that they should be granted jurisdictional discovery pursuant to *CPLR 3211 (d)*. **[*786]** The plaintiffs also opposed those branches of the motion of the Bunge **[****3]** defendants which were pursuant to *CPLR 3211 (a) (7)*.

The Supreme Court denied that branch of the **[***7]** motion of the Bunge defendants which was to dismiss the complaint insofar as asserted against Bunge S.A. pursuant to *CPLR 3211 (a) (8)* for lack of personal jurisdiction. The Supreme Court concluded that the plaintiffs had made a sufficient start in demonstrating that facts may exist so as to support the exercise of jurisdiction pursuant to *CPLR 301*. In this regard, the court concluded that, "because the evidence [was] sufficient to support the exercise of jurisdiction on the mere department theory, the Court will deny the Bunge Defendants' motion to dismiss on jurisdictional grounds, without prejudice to the assertion of such a jurisdictional defense at trial, should these Defendants be so advised."

The Supreme Court also denied those branches of the Bunge defendants' motion which were to dismiss the first, second, and fifth causes of action insofar as asserted against them pursuant to *CPLR 3211 (a) (7)*.

However, the court granted that branch of their motion which was to dismiss as time-barred the third cause of action, which alleged tortious interference with contract.

On appeal, the Bunge defendants contend that the Supreme Court erred in denying that branch of their motion which was to **[***8]** dismiss the complaint insofar as asserted against Bunge S.A. pursuant to CPLR 3211 (a) (8) for lack of personal jurisdiction. They further contend that the Supreme Court erred in denying those branches of their motion which were to dismiss the first, second, and fifth causes of action pursuant to CPLR 3211 (a) (7).

We first address the Bunge defendants' contention regarding personal jurisdiction over Bunge S.A. However, we note that, in light of our determination granting those branches of the Bunge defendants' motion which were to dismiss the only remaining causes of action asserted against these defendants for failure to state a cause of action, it will not be necessary for the Supreme Court to resolve the issue of whether it has personal jurisdiction over Bunge S.A.

"A foreign corporation is amenable to suit in New York courts under CPLR 301 if it has engaged in such a continuous and systematic course of 'doing business' here that a finding of its 'presence' in this jurisdiction is warranted" (*Landoil Resources Corp. v Alexander & Alexander Servs., 77 NY2d 28, 33, 565 NE2d 488, 563 NYS2d 739 [1990]*, quoting *Laufer v Ostrow, 55 NY2d 305, 309-310, 434 NE2d 692, 449 NYS2d 456 [1982]*, and *Frummer v Hilton Hotels Intl., 19 NY2d 533, 536, 227 NE2d 851, 281 NYS2d 41 [1967]*, and *Simonson v International Bank, 14 NY2d 281, 285, 200 NE2d 427, 251 NYS2d 433 [1964]*). **[***9]** The **[*787]** test is whether "the aggregate of the corporation's activities in **[**434]** the State [are] such that it may be said to be 'present' in the State 'not occasionally or casually, but with a fair measure of permanence and continuity' " (*Laufer v Ostrow, 55 NY2d at 310*, quoting *Tauza v Susquehanna Coal Co., 220 NY 259, 267, 115 NE 915 [1917]*). Any exercise of jurisdiction over a foreign corporation on the basis of state law must comport with the due process requirement that there be sufficient "minimum contacts" between the foreign corporation and the forum State such that the forum State's assertion of jurisdiction will not offend " 'traditional notions of fair play and substantial justice' " (*International Shoe Co. v Washington, 326 US 310, 316, 66 S Ct 154, 90 L Ed 95 [1945]*, quoting *Milliken v Meyer, 311 US 457, 463, 61 S Ct 339, 85 L Ed 278 [1940]*).

Here, the Supreme Court concluded that the plaintiffs failed to sustain their burden of demonstrating that Bunge S.A., a Swiss corporation, had directly engaged in activities sufficient to establish its presence in New York within the meaning of CPLR 301. However, it determined that facts may exist which would permit it to impute the in-state activities of Bunge Ltd. to Bunge S.A., such that Bunge S.A. may be deemed to be vicariously **[***10]** present in New York pursuant to CPLR 301.

In its limited jurisprudence concerning the mere department doctrine, the primary focus of the Court of Appeals has been on the degree of control exercised by the domestic corporation over the foreign corporation (*see* *Delagi v Volkswagenwerk AG of Wolfsburg, Germany, 29 NY2d 426, 431-432, 278 NE2d 895, 328 NYS2d 653 [1972]*; *Public Adm'r of County of N.Y. v Royal Bank of Can., 19 NY2d 127, 131-132, 224 NE2d 877, 278 NYS2d 378 [1967]*). Such control may be manifested in numerous ways and, thus, the method by which such control may be demonstrated will necessarily depend on the attendant facts (*see* *Delagi v Volkswagenwerk AG of Wolfsburg, Germany, 29 NY2d at 431-432*; *Public Adm'r of County of N.Y. v Royal Bank of Can., 19 NY2d at 131-132*; *compare* *Matter of Morris v New York State Dept. of Taxation & Fin., 82 NY2d 135, 141, 623 NE2d 1157, 603 NYS2d 807 [1993]*). Although the Court of Appeals has noted that it "has never **[****4]** held a foreign corporation present on the basis of control, unless there was in existence at least a parent-subsidiary relationship," it has nevertheless indicated that this factor is not dispositive (*Delagi v Volkswagenwerk AG of Wolfsburg, Germany, 29 NY2d at 432*). "The control over [a] subsidiary's activities . . . must be so complete that **[***11]** the subsidiary is, in fact, merely a department of the parent" (*id.*). It is only when the two corporations are "in fact, if not in name . . . one and the same corporation, [that] there is realistically no basis for distinguishing between them" for jurisdictional purposes (*Public Adm'r of County of N.Y. v Royal Bank of Can., 19 NY2d at 132*).

[*788] Here, the plaintiffs, as the parties seeking to assert personal jurisdiction, bear the ultimate burden of proof as to whether Bunge S.A. is a mere department of Bunge Ltd. (*see* *Daniel B. Katz & Assoc. Corp. v Midland Rushmore, LLC, 90 AD3d 977, 978, 937 NYS2d 236 [2011]*). In opposition to the Bunge defendants' motion to dismiss the complaint insofar as asserted against Bunge S.A. pursuant to CPLR 3211 (a) (8) on the ground of lack of personal jurisdiction, the plaintiffs "need only make a prima facie showing" that such jurisdiction exists (Cornely v Dynamic HVAC Supply, LLC, 44 AD3d 986, 986, 845 NYS2d 797 [2007]).

[**435] However, where, as here, plaintiffs oppose a motion to dismiss the complaint pursuant to CPLR 3211 (a) (8) on the ground that discovery on the issue of personal jurisdiction is necessary, plaintiffs need not make a prima facie showing of jurisdiction, but instead "need only demonstrate [***12] that facts 'may exist' to exercise personal jurisdiction over the defendant" (Ying Jun Chen v Lei Shi, 19 AD3d 407, 407-408, 796 NYS2d 126 [2005], quoting Peterson v Spartan Indus., 33 NY2d 463, 467, 310 NE2d 513, 354 NYS2d 905 [1974]). If "it appear[s] from affidavits submitted in opposition to [the] motion . . . that facts essential to justify opposition may exist but cannot then be stated," a court may, in the exercise of its discretion, postpone resolution of the issue of personal jurisdiction (CPLR 3211 [d]).

Here, it is undisputed that Bunge S.A. is a wholly-owned subsidiary of Bunge Ltd. The plaintiffs submitted evidence indicating a degree of financial interdependency between Bunge Ltd. and its various wholly-owned subsidiaries, although funding appeared to be formalized as loan agreements. In addition, the plaintiffs adduced evidence indicating an overlap of executive personnel between Bunge Ltd. and a regional business grouping of Bunge subsidiaries identified as "Bunge Europe," and, in turn, an overlap of executive personnel between Bunge Europe and Bunge S.A. The plaintiffs also submitted evidence indicating that Bunge Ltd. had represented Bunge S.A. as the "headquarters of Bunge's European activities and the main trading office [***13] Bunge worldwide."

Although there was evidence of a close parent-subsidiary connection between Bunge Ltd. and Bunge S.A., the Supreme Court correctly concluded that the plaintiffs' submissions failed to establish, prima facie, that the control exerted by Bunge Ltd. over Bunge S.A. was "so complete that the subsidiary is, in fact, merely a department of the parent" (Delagi v Volkswagenwerk AG of Wolfsburg, Germany, 29 NY2d at 432; *see* Public Adm'r of County of N.Y. v Royal Bank of Can., 19 NY2d at 132). Nevertheless, the plaintiffs' submissions did indicate that Bunge Ltd. exerted some degree of control over its subsidiaries through [*789] internal business groupings which were comprised of employees of its various subsidiaries and organized to achieve common purposes under its direction. Since the plaintiffs demonstrated that facts "may exist" which would permit the exercise of personal jurisdiction over Bunge S.A., but that such facts remain in the exclusive control of the Bunge defendants, the Supreme Court providently exercised its discretion in denying that branch of the Bunge defendants' motion which was to dismiss the complaint insofar as asserted against Bunge S.A. pursuant to CPLR 3211 (a) (8) [***14] for lack of personal jurisdiction (CPLR 3211 [d]; *see* Peterson v Spartan Indus., 33 NY2d at 467).

However, the Supreme Court improvidently exercised its discretion to the extent that it denied that branch of the Bunge defendants' motion which was to dismiss the complaint insofar as asserted against Bunge S.A. pursuant to CPLR 3211 (a) (8) "without prejudice to the assertion of such a jurisdictional defense at trial." "Liability may be considered only after it is decided . . . that the defendant is subject to the in personam jurisdiction of our courts" (Kreutter v McFadden Oil Corp., 71 NY2d 460, 470, 522 NE2d 40, 527 NYS2d [**436] 195 [1988]). By permitting the case to move forward in such a manner, the Supreme Court exposed Bunge S.A. to the full panoply of burdens inherent in defending this case, despite the fact that the court may not have jurisdiction over it. Under the circumstances of this case, the [****5] Supreme Court should have denied that branch of the Bunge defendants' motion without prejudice to renewal upon the completion of limited discovery confined to the issue of whether Bunge S.A. was a mere department of Bunge Ltd. (*see Expert Sewer & Drain, LLC v New England Mun. Equip. Co., Inc., 106 AD3d 775, 776, 964 NYS2d 597 [2013]*; Marist Coll. v Brady, 84 AD3d 1322, 1322, 924 NYS2d 529 [2011]).

We [***15] now turn to the merits of that branch of the motion of the Bunge defendants which was to dismiss the first, second, and fifth causes of action insofar as asserted against them pursuant to CPLR 3211 (a) (7) for failure to state a cause of action. "On a motion to dismiss the complaint pursuant to CPLR 3211 (a) (7) for failure to state a cause of action, the court must afford the pleading a liberal construction, accept all facts as alleged in the pleading to be true, accord the plaintiff the benefit of every possible inference, and determine only whether the facts as alleged fit within any cognizable legal theory" (Breytman v Olinville Realty, LLC, 54 AD3d 703, 703-704, 864 NYS2d 70 [2008]; *see* Leon v Martinez, 84 NY2d 83, 87-88, 638 NE2d 511, 614 NYS2d 972 [1994]).

The first cause of action asserted against the Bunge defendants was for money had and received. "A cause of action for money had and received is one of quasi-contract or of contract **[*790]** implied-in-law" (*Board of Educ. of Cold Spring Harbor Cent. School Dist. v Rettaliata, 78 NY2d 128, 138, 576 NE2d 716, 572 NYS2d 885 [1991]*; *see Parsa v State of New York, 64 NY2d 143, 148, 474 NE2d 235, 485 NYS2d 27 [1984]*). "Having money that rightfully belongs to another, creates a debt; and wherever a debt exists without an express promise to pay, the law implies a promise" **[***16]** (*Byxbie v Wood, 24 NY 607, 610 [1862]*).

The essential elements of a cause of action for money had and received are (1) the defendant received money belonging to the plaintiff, (2) the defendant benefitted from receipt of the money, and (3) under principles of equity and good conscience, the defendant should not be permitted to keep the money (*see Matter of Witbeck, 245 AD2d 848, 850, 666 NYS2d 315 [1997]*; *see also Rocks & Jeans v Lakeview Auto Sales & Serv., 184 AD2d 502, 502, 584 NYS2d 169 [1992]*; *see generally 22A NY Jur 2d Contracts § 533* [2013]). "The action depends upon equitable principles in the sense that broad considerations of right, justice and morality apply to it" (*Parsa v State of New York, 64 NY2d at 148*; *see People ex rel. Dusenbury v Speir, 77 NY 144, 150, 57 How. Pr. 274 [1879]*).

Here, the complaint alleged that, after the distribution of the Rainforest shares, Teledata obtained the controlling interest in Rainforest, it assumed the managerial role of the majority shareholder, and it was in a position of control over disbursements from Rainforest's bank account. The complaint alleged that Teledata, in its role as majority shareholder of Rainforest, transferred certain funds "out of the Rainforest Account . . . either directly or indirectly **[***17]** through Ramachandran-controlled companies, into Bunge accounts" **[**437]** and that these funds were, in turn, "transferred to Teledata, or Teledata-controlled companies to be 're-invested' into Rainforest."

The complaint does not allege that the transfers were made to Bunge S.A. for no legitimate purpose. In addition, the complaint does not allege that the transfers were the result of a mistake, or were unlawful or unauthorized. Indeed, the complaint itself alleges that the transfers were precipitated by Teledata, which, as alleged, was the majority shareholder of Rainforest with the legal authority to control Rainforest's bank accounts and transfer money therefrom. The only theory articulated in the complaint as to why the money transferred rightfully belongs to Rainforest is that the transfer constituted a breach of the Share Subscription Agreement by Teledata. This allegation, that Teledata breached the Share Subscription Agreement by failing to adequately capitalize Rainforest, does not render the money transferred to Bunge S.A. the rightful property of Rainforest. Accordingly, the factual allegations are insufficient to state a cause of action for money had and received, **[*791]** since the complaint **[***18]** failed to adequately allege that Bunge S.A. received money that "rightfully belongs" to Rainforest (*Byxbie v Wood, 24 NY at 610*; *see McCulloch v Town of Milan, 74 AD3d 1034, 1036, 907 NYS2d 19 [2010]*; *Amanat v Bank Leumi Trust Co. of N.Y., 243 AD2d 257, 257, 662 NYS2d 501 [1997]*; *Stephans v Apostol, 17 AD2d 982, 983, 234 NYS2d 337 [1962]*).

The second cause of action asserted against the Bunge defendants was to recover damages for unjust enrichment. "To prevail on a claim of unjust enrichment, a party must show that (1) the other party was enriched, (2) at that party's expense, and (3) that it is against equity and good conscience to permit [the other party] to retain what is sought to be recovered" (**[****6]** *Citibank, N.A. v Walker, 12 AD3d 480, 481, 787 NYS2d 48 [2004]* [internal quotation marks omitted]; *see Robertson v Wells, 95 AD3d 862, 864, 944 NYS2d 194 [2012]*; *Levin v Kitsis, 82 AD3d 1051, 1053, 920 NYS2d 131 [2011]*; *Anesthesia Assoc. of Mount Kisco, LLP v Northern Westchester Hosp. Ctr., 59 AD3d 473, 481, 873 NYS2d 679 [2009]*).

"The essential inquiry in any action for unjust enrichment or restitution is whether it is against equity and good conscience to permit the defendant to retain what is sought to be recovered" (*Paramount Film Distrib. Corp. v State of New York, 30 NY2d 415, 421, 285 NE2d 695, 334 NYS2d 388 [1972]*). "Such a claim is undoubtedly equitable and depends **[***19]** upon broad considerations of equity and justice" (*id.*). "Generally, courts will look to see if a benefit has been conferred on the defendant under mistake of fact or law, if the benefit still remains with the defendant, if there has been otherwise a change of position by the defendant, and whether the defendant's conduct was tortious or fraudulent" (*id.*).

"[A] plaintiff's allegation that the [defendant] received benefits, standing alone, is insufficient to establish a cause of action to recover damages for unjust enrichment" (*Old Republic Natl. Tit. Ins. Co. v Cardinal Abstract Corp., 14 AD3d 678, 680, 790 NYS2d 143 [2005]*; *see McGrath v Hilding, 41 NY2d 625, 629, 363 NE2d 328, 394 NYS2d 603 [1977]*; *Erlitz v Segal, Liling & Erlitz, 142 AD2d 710, 712, 530 NYS2d 848 [1988]*). "Critical is that under the circumstances and as between the two parties to the transaction the enrichment be **[**438]** unjust" (McGrath v Hilding, 41 NY2d at 629, citing *Restatement of Restitution § 1, Comment a*).

Here, the amended complaint merely asserted, in a conclusory fashion, that Bunge S.A. received funds from which it benefitted and that "[e]quity and good conscience require restitution." However, on a motion to dismiss pursuant to CPLR 3211 (a) (7), "bare legal conclusions are not presumed to be **[***20]** true" (*Khan v MMCA Lease, Ltd., 100 AD3d 833, 833, 954 NYS2d 595 [2012]*; *see* *Felix v Thomas R. Stachecki Gen. Contr., LLC, 107 AD3d 664, 667, 966 NYS2d 494 [2013]*). **[*792]** Accordingly, the bare legal conclusion that it is against equity and good conscience to permit Bunge S.A. to retain this unidentified benefit is insufficient to adequately allege that the asserted enrichment was unjust (*see* *Felix v Thomas R. Stachecki Gen. Contr., LLC, 107 AD3d at 667*; *Khan v MMCA Lease, Ltd., 100 AD3d at 833*).

In addition, the general factual assertions contained in the complaint do not satisfy the pleading requirements of unjust enrichment. As previously noted, the complaint did not allege that Bunge S.A. received the transfers through some mistake or deception practiced upon Rainforest by Bunge S.A. The complaint alleged that the transfers were duly authorized by Teledata, which was in control of Rainforest's bank account through its role as the majority shareholder. The fact that Teledata may have breached the Share Subscription Agreement or some other legal duty owed to the plaintiffs when it made the transfers does not render the transfers "unjust" with respect to Bunge S.A. (*McGrath v Hilding, 41 NY2d 625, 629, 363 NE2d 328, 394 NYS2d 603 [1977]*; *see* *Citibank, N.A. v Walker, 12 AD3d at 481*). **[***21]** Accepting the facts alleged in the complaint as true, and according the plaintiff the benefit of every favorable inference (*see* *Leon v Martinez, 84 NY2d at 87-88*), the complaint fails to state a cause of action to recover damages for unjust enrichment (*see* *Robertson v Wells, 95 AD3d at 864*; *Levin v Kitsis, 82 AD3d at 1053*; *Spector v Wendy, 63 AD3d 820, 822, 881 NYS2d 465 [2009]*).

The fifth cause of action asserted in the complaint alleged aiding and abetting fraud. "A plaintiff alleging an aiding-and-abetting fraud claim must allege the existence of the underlying fraud, actual knowledge, and substantial assistance" (*Oster v Kirschner, 77 AD3d 51, 55, 905 NYS2d 69 [2010]*; *see* *High Tides, LLC v DeMichele, 88 AD3d 954, 960, 931 NYS2d 377 [2011]*). Aiding and abetting fraud "is not made out simply by allegations which would be sufficient to state a claim against the principal participants in the fraud" combined with conclusory allegations that the aider and abettor had actual knowledge of such fraud (*National Westminster Bank v Weksel, 124 AD2d 144, 149, 511 NYS2d 626 [1987]*; *see CDR Creances S.A.S. v First Hotels & Resorts Invs., Inc., 101 AD3d 485, 486-487, 956 NYS2d 16 [2012]*). "Aiding and abetting fraud must be pleaded with the specificity sufficient to satisfy CPLR 3016 (b)" (*High Tides, LLC v DeMichele, 88 AD3d at 960*; **[***22]** *see* *Jones v OTN Enter., Inc., 84 AD3d 1027, 1028, 922 NYS2d 810 [2011]*; *Rizel v Bodner, 225 AD2d 410, 640 NYS2d 19 [1996]*; *Shearson Lehman Bros. v Bagley, 205 AD2d 467, 614 NYS2d 5 [1994]*; *National Westminster Bank v Weksel, 124 AD2d at 149*). **[**439]** The heightened pleading requirements of CPLR 3016 (b) may be met when the material facts alleged in the complaint, in **[*793]** light of the surrounding circumstances, "are sufficient to permit a reasonable inference of the alleged conduct" including the adverse party's knowledge of, or participation in, the fraudulent scheme (*Pludeman v Northern Leasing Sys., Inc., 10 NY3d 486, 492, 890 NE2d 184, 860 NYS2d 422 [2008]*; *see* *Eurycleia Partners, LP v Seward & Kissel, LLP, 12 NY3d 553, 559, 910 NE2d 976, 883 NYS2d 147 [2009]*; **[****7]** *Polonetsky v Better Homes Depot, 97 NY2d 46, 55, 760 NE2d 1274, 735 NYS2d 479 [2001]*; *High Tides, LLC v DeMichele, 88 AD3d at 960*).

Here, the complaint consists of conclusory allegations regarding the Bunge defendants' knowledge that Teledata entered into the Share Subscription Agreement with the intent to defraud Goel. Furthermore, the facts alleged in the complaint are insufficient to permit a reasonable inference as to the Bunge defendants' knowledge of this fraud and their substantial assistance in the achievement of the fraud (*see CDR Creances S.A.S. v First Hotels & Resorts Invs., Inc., 101 AD3d 485, 486-487, 956 NYS2d 16 [2012]*; **[***23]** *High Tides, LLC v DeMichele, 88 AD3d at 960*; *National Westminster Bank v Weksel, 124 AD2d at 149*). Accordingly, the complaint fails to state a cause of action alleging aiding and abetting fraud.

The complaint also alleged that Bunge Ltd. is liable under a theory of piercing the corporate veil with respect to the first, second, and fifth causes of action. Since the complaint fails to adequately set forth these underlying causes of action against Bunge S.A., those causes of action must be dismissed as against Bunge Ltd., since "an attempt of a third party to pierce the corporate veil does not constitute a cause of action independent of that against the corporation; rather it is an assertion of facts and circumstances which will persuade the court to impose the corporate obligation on its [parent]" (*Matter of Morris v New York State Dept. of Taxation & Fin., 82 NY2d 135, 141, 623 NE2d 1157, 603 NYS2d 807 [1993]*).

The Bunge defendants' contention that the mere department test is unconstitutional (*see* *Goodyear Dunlop Tires Operations, S.A. v Brown, 564 US ___, 131 S Ct 2846, 180 L Ed 2d 796 [2011]*; *see also* Lea Brilmayer and Kathleen Paisley, *Personal Jurisdiction and Substantive Legal Relations: Corporations, Conspiracies, and Agency*, **[***24]** *74 Cal L Rev 1, 27 [1986]*), is raised for the first time on appeal and, thus, is not properly before this Court.

In light of the foregoing, we need not address the parties' remaining contentions.

Accordingly, we reverse the order insofar as appealed from, and grant those branches of the Bunge defendants' motion pursuant to *CPLR 3211 (a)* which were to dismiss the first, second, and fifth causes of action insofar as asserted against them. Skelos, J.P., Balkin, Cohen and Miller, JJ., concur.

End of Document

[IDT Corp. v. Morgan Stanley Dean Witter & Co.]

Court of Appeals of New York

February 10, 2009, Argued; March 26, 2009, Decided

No. 27

Reporter

12 N.Y.3d 132 *; 907 N.E.2d 268 **; 879 N.Y.S.2d 355 ***; 2009 N.Y. LEXIS 42 ****; 2009 NY Slip Op 2262; 47 Comm. Reg. (P & F) 747

[1] IDT CORPORATION, Respondent, v MORGAN STANLEY DEAN WITTER & CO. et al., Appellants.

Subsequent History: Reargument denied by *IDT Corp. v. Morgan Stanley Dean Witter & Co., 12 N.Y.3d 889, 911 N.E.2d 855, 2009 N.Y. LEXIS 2496, 883 N.Y.S.2d 793 (2009)*

Prior History: Appeal, by permission of the Appellate Division of the Supreme Court in the First Judicial Department, from an order of that Court, entered November 20, 2007. The Appellate Division affirmed an order of the Supreme Court, New York County (Herman Cahn, J.; op 2006 NY Slip Op 30076[U]), which, to the extent appealed from, had denied defendants' motion to dismiss the first, second, fourth and fifth causes of action in the complaint. The following question was certified by the Appellate Division: "Was the order of this Court, which affirmed the order of the Supreme Court, properly made?"

IDT Corp. v. Morgan Stanley Dean Witter & Co., 45 A.D.3d 419, 846 N.Y.S.2d 116, 2007 N.Y. App. Div. LEXIS 11936 (N.Y. App. Div. 1st Dep't, 2007)

Disposition: [**1]** Order reversed, with costs, defendants' motion to dismiss the remaining causes of action granted, complaint dismissed in the entirety, and certified question answered in the negative.

Counsel: *Davis Polk & Wardwell,* New York City (*Guy Miller Struve, Benjamin S. Kaminetzky* and Rebecca Winters of counsel), for appellants. I. IDT Corporation's attempt to relitigate the issue of damages is impermissible under the well-settled doctrine of collateral estoppel. (*Buechel v Bain, 97 NY2d 295, 766 NE2d 914, 740 NYS2d 252*; *D'Arata v New York Cent. Mut. Fire Ins. Co., 76 NY2d 659, 564 NE2d 634, 563 NYS2d 24*; *Kaufman v Eli Lilly & Co., 65 NY2d 449, 482 NE2d 63, 492 NYS2d 584*; *Schwartz v Public Adm'r of County of Bronx, 24 NY2d 65, 246 NE2d 725, 298 NYS2d 955*; *Ryan v New York Tel. Co., 62 NY2d 494, 467 NE2d 487, 478 NYS2d 823*; *Matter of American Ins. Co. [Messinger--Aetna Cas. & Sur. Co.], 43 NY2d 184, 371 NE2d 798, 401 NYS2d 36*; *Rembrandt Indus. v Hodges Intl., 38 NY2d 502, 344 NE2d 383, 381 NYS2d 451*; *New York Lumber & Wood Working Co. v Schneider, 119 NY 475, 24 NE 4*; *Guard-Life Corp. v Parker Hardware Mfg. Corp., 50 NY2d 183, 406 NE2d 445, 428 NYS2d 628*; *Stuzin v Pizza Hut, 241 AD2d 647, 659 NYS2d 573*.) II. IDT Corporation's claims are untimely. (*Kronos, Inc. v AVX Corp., 81 NY2d 90, 612 NE2d 289, 595 NYS2d 931*; *Ackerman v Price Waterhouse, 84 NY2d 535, 644 NE2d 1009, 620 NYS2d 318*; *Snyder v Town Insulation, 81 NY2d 429, 615 NE2d 999, 599 NYS2d 515*; *Spinap Corp. v Cafagno, 302 AD2d 588, 756 NYS2d 86*; *Matter of Martin v C. A. Prods. Co., 8 NY2d 226, 168 NE2d 666, 203 NYS2d 845*; *Norris v Grosvenor Mktg. Ltd., 803 F2d 1281*; *Schwartz v Heyden Newport Chem. Corp., 12 NY2d 212, 188 NE2d 142, 237 NYS2d 714*; *New York Univ. v Continental Ins. Co., 87 NY2d 308, 662 NE2d 763, 639 NYS2d 283*; *Kvetnaya v Tylo, 49 AD3d 608, 854 NYS2d 425*; *Shivers v Siegel, 11 AD3d 447, 782 NYS2d 752*.) III. IDT Corporation's unjust enrichment cause of action fails as a matter of law. (*Clark-Fitzpatrick, Inc. v Long Is. R.R. Co., 70 NY2d 382, 516 NE2d 190, 521 NYS2d 653*; *Rosenberg, Minc & Armstrong v Mallilo & Grossman, 39 AD3d 335, 833 NYS2d 485*; *Hutton v Klabal, 726 F Supp 67*; *Miller v Schloss, 218 NY 400, 113 NE 337*; *Young v Farwell, 165 NY 341, 59 NE 143*; *805 Third Ave. Co. v M.W. Realty Assoc., 58 NY2d 447, 448 NE2d 445, 461 NYS2d 778*; *Wujin Nanxiashu Secant Factory v Ti-Well Intl. Corp., 14 AD3d 352, 788 NYS2d 78*; *Matter of Guttenplan, 222 AD2d 255, 634 NYS2d 702*; *Matter of Moncrief, 235 NY 390, 139 NE 550*; *Morad v Morad, 27 AD3d 626, 812 NYS2d 126*.)

Patterson Belknap Webb & Tyler LLP, New York City (*Stephen P. Younger* of counsel), *Grayson & Kubli, P.C.,* Vienna, Virginia (Alan M. Grayson, of the Virginia bar, admitted pro hac vice, and Victor A. Kubli of counsel), and *Bracewell & Giuliani, LLP,* Houston, Texas, and New York City (*Glenn A. Ballard, Jr., Jeffrey L. Oldham* and Michael D. Hess of counsel), for respondent. I. The courts below correctly held that IDT Corporation's claims against Morgan Stanley Dean Witter & Co. are not affected by the doctrine of collateral estoppel. (*D'Arata v New York Cent. Mut. Fire Ins. Co., 76 NY2d 659, 564 NE2d 634, 563 NYS2d 24*; *Amarant v D'Antonio, 197 AD2d 432, 602 NYS2d 837*; *PenneCom B.V. v Merrill Lynch & Co., Inc., 372 F3d 488*; *Inchaustegui v 666 5th Ave. Ltd. Partnership, 268 AD2d 121, 706 NYS2d 396*, *96 NY2d 111, 749 NE2d 196, 725 NYS2d 627*; *Guard-Life Corp. v Parker Hardware Mfg. Corp., 50 NY2d 183, 406 NE2d 445, 428 NYS2d 628*; *International Mins. & Resources, S.A. v Pappas, 96 F3d 586*; *Matter of American Ins. Co. [Messinger--Aetna Cas. & Sur. Co.], 43 NY2d 184, 371 NE2d 798, 401 NYS2d 36*; *R.S.J. Leasing Corp. v Michelin Tire Corp., 92 AD2d 914, 460 NYS2d 129*; *Matter of Kellogg, 138 AD2d 799, 525 NYS2d 443*; *Gramatan Home Invs. Corp. v Lopez, 46 NY2d 481, 386 NE2d 1328, 414 NYS2d 308*.) II. The lower courts correctly held the IDT Corporation's claims are timely because they were filed within the applicable limitations periods after IDT learned of Morgan Stanley Dean Witter & Co.'s misconduct, which Morgan Stanley fraudulently concealed. (*Marine Midland Bank v Worldwide Indus. Corp., 307 AD2d 221, 763 NYS2d 27*; *Maric Piping v Maric, 271 AD2d 507, 705 NYS2d 684*; *Green v Albert, 199 AD2d 465, 605 NYS2d 395*; *Zumpano v Quinn, 6 NY3d 666, 849 NE2d 926, 816 NYS2d 703*; *Hetelekides v Ford Motor Co., 299 AD2d 868, 750 NYS2d 404*; *Powers Mercantile Corp. v Feinberg, 109 AD2d 117, 490 NYS2d 190*; *Matter of Steyer, 70 NY2d 990, 521 NE2d 429, 526 NYS2d 422*; *Simcuski v Saeli, 44 NY2d 442, 377 NE2d 713, 406 NYS2d 259*; *General Stencils v Chiappa, 18 NY2d 125, 219 NE2d 169, 272 NYS2d 337*; *Vigliotti v North Shore Univ. Hosp., 24 AD3d 752, 810 NYS2d 82*.) III. The lower courts correctly held that IDT Corporation stated a claim for unjust enrichment. (*Clark-Fitzpatrick, Inc. v Long Is. R.R. Co., 70 NY2d 382, 516 NE2d 190, 521 NYS2d 653*; *Sosnoff v Carter, 165 AD2d 486, 568 NYS2d 43*; *Sergeants Benevolent Assn. Annuity Fund v Renck, 19 AD3d 107, 796 NYS2d 77*; *Duane Reade v Cardinal Health, Inc., 12 AD3d 224, 784 NYS2d 534*; *Wiener v Lazard Freres & Co., 241 AD2d 114, 672 NYS2d 8*.) IV. This Court may properly consider the new allegations in IDT Corporation's amended complaint. (*Hummingbird Assoc. v Dix Auto Serv., 273 AD2d 58, 709 NYS2d 51*; *Halmar Distribs. v Approved Mfg. Corp., 49 AD2d 841, 373 NYS2d 599*; *Millard v Delaware, Lackawanna & W. R.R. Co., 204 App Div 80, 197 NYS 747*; *Wahrhaftig v Space Design Group, 28 AD2d 940, 281 NYS2d 500*; *Anthony J. Demarco, Jr., P.C. v Bay Ridge Car World, 169 AD2d 808, 565 NYS2d 176*; *Vanderwoude v Post/Rockland Assoc., 130 AD2d 739, 515 NYS2d 838*; *Watson v Sony Music Entertainment, 282 AD2d 222, 722 NYS2d 385*.)

Judges: Opinion by Judge Pigott. Judges Ciparick, Graffeo, Read, Smith and Jones concur. Chief Judge Lippman took no part.

Opinion by: Pigott

Opinion

[*357] [**270] [*136]** PIGOTT, J.

IDT Corporation and Telefonica Internacional, S.A., both telecommunications companies, executed a Memorandum of Understanding (MOU) in August 1999 concerning SAm-1, a vast underwater fiber-optic cable network Telefonica was building. Pursuant to the MOU, IDT was to buy from Telefonica a 10% equity share in NewCo, a corporation that would "construct, establish, operate and maintain . . . and . . . sell capacity on" SAm-1. A **[2]** separate entity was to be created to market products associated with the network. IDT would have the right to buy capacity in the network, at a favorable rate, during its operational life.

In June 2000, Telefonica informed IDT that it intended to modify the MOU, replacing NewCo with a larger entity, Emergia, in which Telefonica offered IDT a five percent share. According to IDT, **[****2]** Morgan Stanley Dean Witter & Co. (Morgan Stanley), Telefonica's investment banker, advised IDT in the summer of 2000 that the value of a five percent interest in Emergia was far greater than that of a 10% interest in NewCo. Nevertheless, IDT, unpersuaded, broke off negotiations with Telefonica in October 2000.

Although Morgan Stanley acted as Telefonica's investment banker in relation to SAm-1, it had previously acted on IDT's **[*137]** behalf in 1999, in negotiations concerning a different proposed fiber-optic cable network, and in subsequent matters. IDT engaged Morgan Stanley as its financial adviser in regard to shares in Net2Phone, Inc. that it sold in the summer of 2000 for about $ 1 billion. According to IDT, in 1999-2000, Morgan Stanley requested and received confidential business and financial information concerning IDT, had access to IDT's records, and enjoyed wide-ranging communications with its executives.

IDT commenced an arbitration proceeding on May 25, 2001, against Telefonica, alleging that Telefonica had breached the MOU, in particular its provisions entitling IDT to an equity share in NewCo and giving it the right to buy capacity in SAm-1. IDT sought an award in an **[****3]** amount no less than $ 3.15 billion. IDT made no allegations against Morgan Stanley. No representative of Morgan Stanley testified, but a valuation memorandum concerning NewCo and Emergia that Morgan Stanley had presented to IDT in 2000 was subpoenaed and submitted to the arbitration panel.

Following a lengthy hearing, the panel concluded that Telefonica had breached both the "capacity purchase" and "equity purchase" provisions of the MOU. It calculated IDT's aggregate damages for Telefonica's capacity purchase breach to be $ 16,883,817. However, noting the weakness of the telecommunications market in the second half of 2000, the panel calculated that the present value of IDT's interest in NewCo was negative, and concluded that IDT had suffered no damages as a result of Telefonica's breach of the equity purchase provisions. [1] Telefonica paid IDT **[**271]** **[***358]** $ 21.6 million, representing damages and interest. **[3]**

On November 5, 2004, IDT commenced this action against Morgan Stanley, alleging that it had provided Telefonica with confidential information about IDT, induced Telefonica to **[*138]** breach the MOU and, moreover, presented false and misleading evidence to the arbitration panel, affecting the panel's assessment of IDT's damages. Its complaint contains five causes of action: (1) breach of fiduciary duty, (2) intentional interference with existing contract, (3) intentional interference with prospective business relations, (4) misappropriation of confidential and proprietary business information, and (5) unjust enrichment. IDT seeks compensatory damages, disgorgement of profits obtained by Morgan Stanley in connection with SAm-1, **[****5]** punitive damages, and the return of a $ 10,000,000 fee that IDT paid Morgan Stanley in relation to the Net2Phone, Inc. transaction, plus interest and fees.

Morgan Stanley moved to dismiss the complaint under *CPLR 3211*, arguing, among other things, that IDT's claims were barred by collateral estoppel and the statute of limitations. Supreme Court dismissed IDT's intentional interference with prospective business relations claim, but otherwise denied the motion (2006 NY Slip Op 30076[U]). On appeal, the Appellate Division affirmed, with one Justice dissenting, holding that IDT's remaining claims were not barred by collateral estoppel, because IDT had not "had an opportunity to conduct discovery on the extent of the damages it suffered due to Morgan Stanley's alleged tortious conduct" *(45 AD3d 419, 419, 846 NYS2d 116 [1st Dept 2007])*. The majority also concluded that the claims stated valid causes of action and were not time-barred. The Appellate Division granted Morgan Stanley leave to appeal to this Court, certifying the question whether its order was properly made. We answer that question in the negative and reverse. [2]

[1] Although the issue of whether IDT is collaterally estopped from relitigating the amount of its compensatory damages divided the Appellate Division in this case, we need not **[4]** address it, because all of IDT's claims are either time-barred or fail to state a cause of action. We conclude that IDT's breach of fiduciary duty, tortious interference with contract, and misappropriation of confidential and proprietary business information **[*139]** claims are untimely and its unjust enrichment claim fails to state a cause of action.

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[1] The panel rejected IDT's contention that NewCo and Emergia were one and the same. Rather, it found, NewCo was envisaged as a company holding the infrastructure assets of SAm-1, and did not encompass the marketing function and revenues of the enterprise. In reaching this conclusion, the arbitration **[****4]** panel relied on, among other things, minutes of a July 2000 IDT board meeting, indicating that IDT recognized that Emergia was a larger enterprise, with greater growth potential, than NewCo. The arbitration panel expressed skepticism about Morgan Stanley's summer 2000 valuation of NewCo and Emergia, noting that its projections were "prepared by Telefonica and Morgan Stanley be presented to IDT as part of the process of negotiating IDT's ownership percentage in Emergia."

[2] After Supreme Court denied the motion to dismiss, the parties proceeded to discovery and Morgan Stanley produced **[****6]** documents that, according to IDT, reveal further wrongdoing by Morgan Stanley during the arbitration proceeding. IDT filed an amended complaint. Supreme Court granted Morgan Stanley's motion to dismiss the new claims. That decision is under appeal.

In June 2008, IDT moved to dismiss the present appeal as moot, on the ground that the original complaint had been significantly amended. We denied the mootness motion on September 4, 2008 (***11 NY3d 750, 894 NE2d 1187, 864 NYS2d 798 [2008]***).

We address the causes of action in the sequence they appear in the complaint.

IDT's first cause of action alleges that Morgan Stanley breached fiduciary duties it owed to IDT, by "provid[ing] Telefonica with IDT's confidential and **[****7]** proprietary **[***359]** **[**272]** business and financial information without IDT's knowledge or consent," thus inducing Telefonica to renege on the MOU, and by "devis[ing] a fraudulent scheme to dupe both IDT and the Arbitration Panel as to the 'distinction' between NewCo and Emergia and the valuation of these companies." IDT alleges that the arbitration panel was misled into minimizing the amount of damages Telefonica owed to IDT. It seeks full compensatory damages--in an amount it describes at the outset of its complaint as "hundreds of millions of dollars"--as well as disgorgement of profits and punitive damages.

IDT submits that its breach of fiduciary duty claim is governed by a six-year statute of limitations and is therefore timely. Morgan Stanley asserts that a three-year limitations period applies.

New York law does not provide a single statute of limitations for breach of fiduciary duty claims. Rather, the choice of the applicable limitations period depends on the substantive remedy that the plaintiff seeks (*Loengard v Santa Fe Indus., 70 NY2d 262, 266, 514 NE2d 113, 519 NYS2d 801 [1987]*). Where the remedy sought is purely monetary in nature, courts construe the suit as alleging "injury to property" within the **[****8]** meaning of *CPLR 214 (4)*, which has a three-year limitations period (*see e.g.* *Yatter v Morris Agency, 256 AD2d 260, 261, 682 NYS2d 198 [1st Dept 1998]*). Where, however, the relief sought is equitable in nature, the six-year limitations period of *CPLR 213 (1)* applies (*Loengard, 70 NY2d at 266-267*). Moreover, where an allegation of fraud is essential to a breach of fiduciary duty claim, courts have applied a six-year statute of limitations under *CPLR 213 (8)* (*Kaufman v Cohen, 307 AD2d 113, 119, 760 NYS2d 157 [1st Dept 2003]*).

[2] Here, IDT primarily seeks damages--in the amount of "hundreds of millions of dollars"--and the equitable relief it seeks, including the disgorgement of profits, is incidental to that relief. This is not an action in which it can reasonably be asserted that "the relief demanded in the complaint . . . is equitable in nature and that a legal remedy would not be adequate" (*Loengard, 70 NY2d at 267*). Thus, looking to the **[*140]** reality, rather than the form, of this action (*see* *Matter of Paver & Wildfoerster [Catholic High School Assn.], 38 NY2d 669, 674, 345 NE2d 565, 382 NYS2d 22 [1976]*), we conclude that IDT seeks a monetary remedy.

Moreover, we are not persuaded by IDT's argument that its breach of fiduciary duty claim is essentially **[****9]** a fraud action and therefore governed by a six-year statute of limitations. The fiduciary relationship alleged by IDT exists between Morgan Stanley and IDT, not between **[5]** Morgan Stanley and the arbitration panel. For us to conclude that IDT's breach of fiduciary duty cause of action is a sufficiently pleaded fraud action, we would have to discern a claim that IDT acted in "justifiable reliance" (*Lama Holding Co. v Smith Barney, 88 NY2d 413, 421, 668 NE2d 1370, 646 NYS2d 76 [1996]*) on Morgan Stanley's alleged misrepresentation or material omission. Although IDT asserts that Morgan Stanley attempted to deceive it in 2000, with regard to the relative values of Emergia and NewCo, IDT does not claim that it was actually duped. In fact, IDT refused to accept a modified MOU, contrary to Morgan Stanley's recommendations. Consequently, we conclude that this is not a fraud allegation, and that the three-year limitations period of *CPLR 214 (4)* applies.

[3] We now turn to the question of when IDT's breach of fiduciary duty claim **[***360]** **[**273]** accrued. A tort claim accrues as soon as "the claim becomes enforceable, i.e., when all elements of the tort can be truthfully alleged in a complaint" (*Kronos, Inc. v AVX Corp., 81 NY2d 90, 94, 612 NE2d 289, 595 NYS2d 931 [1993]*). **[****10]** As with other torts in which damage is an essential element, the claim "is not enforceable until damages are sustained" (*id. at 94*). To determine timeliness, we consider whether plaintiff's complaint must, as a matter of law, be read to allege damages suffered so early as to render the claim time-barred (*id. at 94-97*). Here, the only reasonable inference to be drawn from IDT's allegations is that it first suffered loss, as a result of Morgan Stanley's alleged breach of fiduciary duty, after Telefonica refused to comply with the MOU. The exact date of the injury is not alleged but must have been before May 25, 2001, when IDT commenced the arbitration against Telefonica, alleging that it had sustained a loss of some $ 3.15 billion as a result of Telefonica's breach of their binding agreement. More than three years passed, therefore, **[*141]** before IDT commenced this action, rendering IDT's breach of fiduciary duty claim time-barred. [3]

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[3] Morgan Stanley contends that the breach of fiduciary duty claim fails on the merits, because there was no fiduciary relationship between IDT and Morgan Stanley on the

[4] Turning to IDT's second and fourth causes of action [4] -- intentional interference with existing contract and misappropriation of confidential and proprietary business information, respectively--the statute of limitations in each case is three years, under CPLR 214 (4), which the parties do not dispute. As with IDT's first cause of action, the claims were not enforceable until IDT first suffered damages. The damages are those resulting from Telefonica's refusal to comply with the MOU--intransigence that was allegedly induced by Morgan Stanley by means **[6]** of the disclosure of confidential IDT business information. Again, we must conclude from IDT's complaint that it first suffered loss--as a result of Morgan Stanley's alleged interference with contractual relations and misappropriation of confidential business information--when Telefonica refused to comply with the MOU. And again, although the exact date of the injury is not alleged, it must have been before May 25, 2001, rendering the claims time-barred.

[5] IDT argues that Morgan Stanley's statute of limitations defenses should be barred by equitable **[****12]** estoppel. However, IDT fails to demonstrate that any action or inaction by Morgan Stanley caused IDT's delay in bringing this action (*see* Zumpano v Quinn, 6 NY3d 666, 673-676, 849 NE2d 926, 816 NYS2d 703 [2006]). According to its complaint, IDT learned in 2000 that Morgan Stanley was denigrating it in discussions with Telefonica. IDT, given its awareness that Telefonica's financial adviser had disparaged it, should have made further inquiry before the statute of limitations expired (*see* Putter v North Shore Univ. Hosp., 7 NY3d 548, 553-554, 858 NE2d 1140, 825 NYS2d 435 [2006]).

[6] Finally, IDT alleges that Morgan Stanley was unduly enriched by the investment banking fees it obtained from IDT and from Telefonica "and any other fees Morgan Stanley received for its 'search' for a replacement anchor tenant, as well as any other fees of any kind that Morgan Stanley has earned for additional, presently-unknown **[***361]** **[**274]** misappropriations and misuses of IDT's confidential business and financial information." On appeal, Morgan Stanley does not argue that the unjust **[*142]** enrichment claim is time-barred. Instead it contends that IDT's fifth claim fails to state a cause of action. We agree.

"The theory of unjust enrichment lies as a quasi-contract claim" (Goldman v Metropolitan Life Ins. Co., 5 NY3d 561, 572, 841 NE2d 742, 807 NYS2d 583 [2005]). **[****13]** It is an obligation imposed by equity to prevent injustice, in the absence of an actual agreement between the parties concerned. Where the parties executed a valid and enforceable written contract governing a particular subject matter, recovery on a theory of unjust enrichment for events arising out of that subject matter is ordinarily precluded (Clark-Fitzpatrick, Inc. v Long Is. R.R. Co., 70 NY2d 382, 388, 516 NE2d 190, 521 NYS2d 653 [1987]).

It follows that the unjust enrichment claim cannot form the basis of IDT's demand that Morgan Stanley return the $ 10,000,000 fee paid in relation to the Net2Phone, Inc. transaction, because that fee arose from services governed by an engagement letter signed by IDT on July 26, 2000. [5] Nor can the unjust enrichment claim support the disgorgement of any profits Morgan Stanley obtained from Telefonica or other companies, in connection with SAm-1. An unjust enrichment claim "rests upon the equitable principle that a person shall not be allowed to enrich himself unjustly at the expense of another" (Miller v Schloss, 218 NY 400, 407, 113 NE 337 [1916]; **[7]** *see also Restatement [First] of Restitution § 1*). In seeking Morgan Stanley's profits from SAm-1, IDT does not, and cannot, allege that Morgan **[****14]** Stanley has been unjustly enriched at IDT's expense, because IDT did not pay the alleged fees.

Accordingly, the order of the Appellate Division should be reversed, with costs, defendants' motion to dismiss the remaining causes of action granted, the complaint dismissed in the entirety, and the certified question answered in the negative.

Judges CIPARICK, GRAFFEO, READ, SMITH and JONES concur; Chief Judge LIPPMAN taking no part.

Order reversed, etc.

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transaction in suit, but this too is a question we need not reach because the claim, even if **[****11]** meritorious, is time-barred.

[4] IDT did not appeal Supreme Court's dismissal of its third claim.

[5] IDT's argument that it engaged Morgan Stanley under duress is unpersuasive, in that the coercion by Morgan Stanley that IDT alleged in its complaint occurred after IDT refused to pay the fee, not before the fee was agreed on.

In re Charles A. Field Delivery Serv.

Court of Appeals of New York

December 19, 1985, Decided

No Number in Original

Reporter

66 N.Y.2d 516 *; 488 N.E.2d 1223 **; 498 N.Y.S.2d 111 ***; 1985 N.Y. LEXIS 17937 ****

In the Matter of Charles A. Field Delivery Service, Inc., Respondent. Lillian Roberts, as Commissioner of Labor, Appellant

Prior History: **[****1]** Appeal from an order of the Appellate Division of the Supreme Court in the Third Judicial Department, entered July 24, 1985, which, by a divided court, affirmed a decision of the Unemployment Insurance Appeal Board that respondent's delivery persons are independent contractors for whom respondent need make no unemployment insurance contributions.

Matter of Field Delivery Serv. (Roberts), 112 AD2d 505.

Disposition: On review of submissions pursuant to section 500.4 of the Rules of the Court of Appeals (*22 NYCRR 500.4*), order reversed, without costs, and matter remitted to the Appellate Division, Third Department, with directions to remand to the Unemployment Insurance Appeal Board for further proceedings in accordance with the opinion herein.

Counsel: *Robert Abrams, Attorney-General (Richard S. Lo Primo* of counsel), for appellant.

Michael R. Suprunowicz for respondent.

Judges: Meyer, J. Chief Judge Wachtler and Judges Jasen, Simons, Kaye, Alexander and Titone concur.

Opinion by: MEYER

Opinion

[*516] [1225] [***113] OPINION OF THE [****3] COURT**

A decision of an administrative agency which neither adheres **[*517]** to its own prior precedent nor indicates its reason for reaching a different result on essentially the same facts is arbitrary and capricious. The order of the Appellate Division confirming the determination of the Unemployment Insurance Appeal Board that respondent's delivery persons are independent contractors for whom respondent need make no unemployment insurance contribution should, therefore, be reversed and the matter remitted to the Board for further proceedings in accordance with this opinion.

I

Respondent operates a delivery service pursuant to a contract with a medical laboratory. Respondent's drivers are called directly by the laboratory and on the basis of those calls pick up specimens from the offices of physicians who use the laboratory's services. The driver takes them to Albany County Airport for transportation to the laboratory. Upon completion of the laboratory's testing and analysis the results are delivered to a collection center, from which they are picked up by respondent's drivers and delivered to the forwarding physician. The drivers collect no money from the physicians **[****4]** and channel any complaints received directly to the laboratory without informing respondent.

The drivers have no written contract with respondent and are terminable at will. They use their own vehicles and pay for their own gas, tolls, insurance and other expenses. They are free to determine the order in which calls will be made and to make pickups or deliveries for others, for which respondent receives no part of the compensation, so long as all pickups and deliveries under respondent's contract with the laboratory are completed on the day received. A driver who is unable to work on a particular day is responsible for finding a replacement driver for that day.

Drivers are not required to complete time sheets or other records or forms for respondent, except an itemized invoice covering a two-week period and stating the names, addresses and dates of pickups and deliveries made during that period. Each driver is compensated by respondent on the basis of the number and type of the jobs completed by him during the period, the amount paid for any given delivery being computed by respondent's president on the basis of the distance traveled and the time expended in completing it. No **[****5]** taxes are withheld from a driver's compensation, nor is workers' compensation insurance provided.

[*518] The Commissioner of Labor determined that respondent's drivers were employees rather than independent contractors and assessed a deficiency of $ 2,834.40 against respondent under the Unemployment Insurance Law (*Labor Law § 570*). Respondent having requested a hearing, the administrative judge agreed that the drivers were employees, but on respondent's appeal to the Unemployment Insurance Appeal Board, that body reversed, concluding that respondent "did not have the right to exercise significant control over the method or manner by which the drivers chose to complete performance of their delivery services" [1] and on reconsideration, adhered to that decision. In neither its original decision nor its decision on reconsideration **[***114]** did the Board cite any precedent for its determination.

[**6]** On the Commissioner's appeal to the Appellate Division that court affirmed, without **[**1226]** opinion, two Justices dissenting. The dissenters, finding that the facts of the case were "indistinguishable, in any significant respect" from two earlier Board decisions which had been confirmed by both the Appellate Division and the Court of Appeals *(Matter of Di Martino [Buffalo Courier Express Co. -- Ross], 59 NY2d 638, affg 89 AD2d 829*; *Matter of Wells [Utica Observer-Dispatch & Utica Daily Press -- Roberts], 59 NY2d 638, affg 87 AD2d 960*) and concluding that "it is incumbent on the Board to decide like cases the same way or explain the departure [citations omitted]", voted to reverse. (*112 AD2d, at p 507*.) We agree that, absent an explanation by the agency, an administrative agency decision which, on essentially the same facts as underlaid a prior agency determination, reaches a conclusion contrary to the prior determination is arbitrary and capricious. And we conclude, as did the dissenters below, that the present case involves facts indistinguishable from those of the *Di Martino* and *Wells* cases. We, therefore, reverse and remit to the Board for **[****7]** further proceedings.

II

Stare decisis is no more an inexorable command for administrative agencies than it is for courts *(see*, Wachtler, *Stare Decisis and a Changing New York Court of Appeals*, 59 St **[*519]** John's L Rev 445, 452). [2] They are, therefore, free, like courts, to correct a prior erroneous interpretation of the law *(Matter of Pascual v State Bd. of Law Examiners, 79 AD2d 1054, 1055*, *lv denied 54 NY2d 601*; *Matter of Leap v Levitt, 57 AD2d 1021*, *lv denied 42 NY2d 807*) by modifying or overruling a past decision *(see*, Davis, Administrative Law §§ 20:10-20:11 [2d ed]; Jaffe, Judicial Control of Administrative Action, at 587-588). They are, likewise, free, like courts, to determine how disputed facts are to be decided, judging credibility and drawing such inference as they find reasonable in order to resolve contested questions of fact *(Matter of McSweeney v Hammerlund Mfg. Co., 275 App Div 447, 450*; *see, Matter of Dresher [Lubin], 286 App Div 591*; Gabrielli and Nonna, *Judicial Review of Administrative Action in New York: An Overview and a Survey*, 52 St John's L Rev 361, 363; Jaffe, *Judicial Review: Questions of Law*, 69 Harv **[****8]** L Rev 239, 241), and it is not within the power of the courts to impose factual consistency.

The policy reasons for consistent results, given essentially similar facts, are, however, largely the same whether the proceeding be administrative or judicial -- to provide guidance for those governed by the determination made *(Matter of Howard Johnson Co. v State Tax Commn., 65 NY2d 726, 727)*; to deal impartially with litigants; promote stability in the law; allow for efficient use of the adjudicatory process; and to maintain **[****9]** the appearance of justice (Davis, *Doctrine of Precedent as Applied to Administrative Decisions*, 59 W Va L Rev 111, 128-136). The underlying precept is that in administrative, as in judicial, proceedings "justice demands that cases with like antecedents should breed like consequences" *(id.*, at 117; *accord*, Koslow, *Standardless Administrative Adjudication*, 22 Admin L Rev 407, 424; **[***115]** Kramer, *Place and Function of Judicial Review in the*

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[1] The facts stated in the preceding three paragraphs of this opinion are the facts on which the Board based its determination.

[2] Indeed, it is often suggested that such an agency "has somewhat greater freedom than a common-law court" *(Matter of Dresher [Lubin], 286 App Div 591, 594*; *see, Food Mktg. Inst. v Interstate Commerce Commn., 587 F2d 1285, 1290*; Davis, *Administrative Findings, Reasons and Stare Decisis*, 38 Cal L Rev 218; Davis, *Doctrine of Precedent As Applied To Administrative Decisions*, 59 W Va L Rev 111, 124; Ann., ***79 ALR2d 1126, 1131-1132***; 2 NY Jur 2d, Administrative Law, § 146, at 230).

Administrative Process, 28 Fordham L Rev 1, 8). Legislative awareness of the policy considerations involved is evident from Labor Law § 534, the third unnumbered paragraph of which requires **[**1227]** that the Board "maintain a current index, by topic, of the principles of law established by **[*520]** the decisions rendered by the board and the courts concerning matters arising under [the Unemployment Insurance Law]" and make copies of the index available for public inspection and examination at all locations where unemployment insurance hearings are conducted. [3]

[**10]** From the policy considerations embodied in administrative law, it follows that when an agency determines to alter its prior stated course it must set forth its reasons for doing so. Unless such an explanation is furnished, a reviewing court will be unable to determine whether the agency has changed its prior interpretation of the law for valid reasons, or has simply overlooked or ignored its prior decision (Kramer, *op. cit.*, at 68-70). Absent such an explanation, failure to conform to agency precedent will, therefore, require reversal on the law as arbitrary, even though there is in the record substantial evidence to support the determination made *(* Matter of Howard Johnson Co. v State Tax Commn., 65 NY2d, at p 727, *supra;* Matter of New York Tel. Co. v Public Serv. Commn., 62 NY2d 57, 62; Matter of Dresher [Lubin], 286 App Div, at p 594, *supra;* Matter of Fitzgerald v State Div. of Dept. of Public Serv., 262 App Div 393, 397; *see,* Atchison, Topeka & Santa Fe Ry. Co. v Wichita Bd. of Trade, 412 U.S. 800, 807-808 [plurality opn]; Greater Boston Tel. Corp. v Federal Communications Commn., 444 F2d 841, 852, *cert denied 403 U.S. 923*; 4 Davis, Administrative **[****11]** Law § 20:11, at 37 [2d ed]; Kaufman, *Judicial Review of Agency Action: A Judge's Unburdening*, 45 NYU L Rev 201, 204, 209).

III

Examined against that background, it is clear that there must be a reversal. The question before the Board, not uncommon in Unemployment Insurance Law cases, was whether the drivers working for respondent were its employees for whom respondent was required to make contributions to the unemployment insurance fund (*Labor Law § 511*) or independent contractors for whom no such contribution need be made. **[*521]** Whether an employer-employee relationship exists is a question of fact, to be decided on the basis of evidence from which it can be found that the alleged employer "exercises control over the results produced * * * or the means used to achieve the results" *(* Matter of 12 Cornelia St. v Ross, 56 NY2d 895, 897). No one factor is determinative, but control over means is the more important factor to be considered *(* Matter of Ted Is Back Corp. [Roberts], 64 NY2d 725, 726). The Board's determination of the issue, if supported by substantial evidence on the record as a whole, is beyond judicial review even though the evidence would have **[****12]** supported a contrary conclusion *(* Matter of Concourse Ophthalmology Assoc. [Roberts], 60 NY2d 734, 736; Matter of Di Martino [Buffalo Courier Express Co. -- Ross], 59 NY2d 638, 641, *supra)*.

The problem in the present case is that in the *Di Martino* and *Wells* cases *(supra)*, the Board determined that the relationship was that of employer-employee, **[***116]** determinations which were confirmed by us, on the record before the Board, as supported by substantial evidence. In *Di Martino*, each of the delivery persons for a newspaper company signed an "independent contractor" agreement. The delivery **[**1228]** persons were provided with a list of customers and were required to make all deliveries by a specified time. All subscription fees were collected by the newspaper itself. The delivery persons used their own vehicles but received a mileage allowance. The newspaper bore the risk of loss for damaged papers, and the newspaper took all complaints from subscribers directly. In *Wells*, the delivery persons also signed an "independent contractor" agreement and used their own vehicles to deliver newspapers to retailers. They were not reimbursed for **[****13]** gas or mileage. Remuneration was on a per-delivery basis, with no sequence prescribed for the drop-offs. The delivery persons were allowed to subcontract their deliveries. The ultimate responsibility for each delivery person was to finish all deliveries by a stated time. Delivery persons were paid without any deductions, and there were no employment rules or regulations to follow. Comparison of the facts on the basis of which *Di Martino* and *Wells* were decided with the facts of the instant case recited above makes evident, if not the impossibility of distinguishing this case from *Di Martino* and *Wells*, at least the existence of sufficient factual similarity between those

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[3] Although the Unemployment Insurance Appeal Board is not covered by the State Administrative Procedure Act (§ 102 [1]), that act likewise requires that each agency governed by the act "maintain an index by name and subject of all written final decisions, determinations and orders rendered by the agency in adjudicatory proceedings", make the index and the text of any such decision available for public inspection and copying, and index each decision within 60 days after it is rendered (State Administrative Procedure Act § 307 [3] [a]).

cases and this to require explanation by the Board of why it reached a different result in this case.

For the foregoing reasons, the order of the Appellate Division **[*522]** should be reversed, without costs, and the matter remitted to the Board for further proceedings in accordance with this opinion.

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ISS Action, Inc. v Tutor Perini Corp.

Supreme Court of New York, Appellate Division, Second Department

March 6, 2019, Decided

2016-05400

Reporter

170 A.D.3d 686 *; 95 N.Y.S.3d 298 **; 2019 N.Y. App. Div. LEXIS 1551 ***; 2019 NY Slip Op 01577 ****; 2019 WL 1051554

[**1]** ISS Action, Inc., Appellant, v Tutor Perini Corporation, Respondent. (Index No. 53046/14)

Counsel: **[***1]** Coti & Sugrue, New City, NY (Stephen R. Sugrue of counsel), for appellant.

Kaufman Dolowich Voluck LLP, Woodbury, NY (Andrew L. Richards and Megan E. Yllanes of counsel), for respondent.

Judges: RUTH C. BALKIN, J.P., CHERYL E. CHAMBERS, JEFFREY A. COHEN, ROBERT J. MILLER, JJ. BALKIN, J.P., CHAMBERS, COHEN and MILLER, JJ., concur.

Opinion

[*686] **[**300]** In an action, inter alia, to recover damages for fraudulent misrepresentation and unjust enrichment and for declaratory relief, the plaintiff appeals from an order of the Supreme Court, Westchester County (Linda S. Jamieson, J.), dated April 15, 2016. The order denied the plaintiff's motion for summary judgment on its first, third, and fourth causes of action and granted the defendant's cross motion for summary judgment dismissing the complaint.

Ordered that the order is affirmed, with costs, and the matter is remitted to the Supreme Court, Westchester County, for the entry of a judgment, inter alia, making an appropriate declaration in accordance herewith.

The plaintiff alleged that the defendant entered into an agreement with the Port Authority of New York and New Jersey to make certain improvements to a runway at John F. Kennedy International Airport. **[***2]** The plaintiff further alleged that on July 31, 2009, it entered into an agreement (hereinafter the 2009 Agreement) with the defendant, pursuant to which the plaintiff was to provide security services at the job site. The 2009 Agreement set forth the various rates of compensation that the plaintiff was to receive in exchange for the security services. It also stated that those rates were "subject to New York State Sales Tax." The 2009 Agreement stated that "[t]he parties agree that as soon as they are able they will execute a completed contract subject to [the defendant's] terms and conditions."

The plaintiff alleged that it commenced performance in accordance with the 2009 Agreement and, in its first invoice to the defendant, it "included a charge for sales tax." The plaintiff alleged that the defendant paid the full amount of the first invoice, including the charge for sales tax. However, the plaintiff alleged that "one or more representatives" of the defendant informed the plaintiff that the security services it provided "were, as a matter of fact and law, exempt from New York State and local sales and use taxes."

[*687] The plaintiff alleged that the defendant subsequently provided the plaintiff **[***3]** with a New York State and Local Sales and Use Tax Contractor Exempt Purchase Certificate dated August 3, 2009 (hereinafter the Tax Exemption Certificate). The Tax Exemption Certificate, which was **[****2]** signed by an employee of the defendant, stated that "[t]he tangible personal property or service[s] being purchased" by the defendant were "exempt from sales and use tax because," and then listed a number of possible exemptions. The exemption which was marked on the Tax Exemption Certificate stated that "[t]he tangible personal property **[**301]** will be used . . . to improve real property . . . owned by an organization exempt under *section 1116 (a) of the Tax Law*."

The plaintiff alleged that after it received the completed Tax Exemption Certificate, it refunded the sales tax paid by the defendant in connection with the first invoice and did not charge the defendant any further sales tax. A more formal subcontract between the two parties was executed on February 12, 2010 (hereinafter the 2010 Agreement). As relevant here, the 2010 Agreement provided that the plaintiff would be responsible for "all payments of taxes," including "sales and use taxes." The 2010 Agreement recited that it was "the entire agreement between the parties **[***4]** relating to the work covered hereby." The complaint alleged that "[i]n light of the representations made by [the defendant] . . . that the services being performed by [the plaintiff] on the runway [p]roject were exempt from sales and use taxes," the plaintiff signed the 2010 Agreement.

The plaintiff alleged that it continued to provide services to the defendant in connection with the runway project, and that the runway project was completed on November 1, 2011. A document titled "Final Release and Waiver of Lien" was executed by the plaintiff's representative on January 12, 2012, which "release[d] and forever discharge[d]" the defendant from "any and all claims, demands, liens and claims of lien whatsoever arising out of [the 2010 Agreement] and/or [the described] work."

In March of 2013, the plaintiff was audited by the New York State Department of Taxation and Finance, which determined that the plaintiff owed approximately $125,000 in back taxes plus interest with respect to the work it performed for the defendant. After the defendant refused the plaintiff's demands to pay the back taxes, the plaintiff commenced this action.

The plaintiff asserted four causes of action against the defendant. **[***5]** The first cause of action sought a declaration that the defendant was legally obligated to pay all sales tax, including **[*688]** interest and penalties, if any, owed as a result of the plaintiff's provision of services to the defendant. The second, third, and fourth causes of action sought to recover damages for breach of contract, unjust enrichment, and fraudulent misrepresentation, respectively.

The plaintiff subsequently moved for summary judgment on the first, third, and fourth causes of action. The defendant cross-moved for summary judgment dismissing the complaint. In the order appealed from, the Supreme Court denied the plaintiff's motion and granted the defendant's cross motion. The plaintiff appeals.

"In order to prevail in an action based upon fraudulent representations, whether for rescission of a contract or in tort for damages, the plaintiff must establish a misrepresentation of a material fact, which was false and known to be false by the defendant, made for the purpose of inducing the other party to rely upon it, justifiable reliance of the other party, and injury" (*Sitar v Sitar, 61 AD3d 739, 741, 878 NYS2d 377 [2009]*; *see* *Lama Holding Co. v Smith Barney, 88 NY2d 413, 421, 668 NE2d 1370, 646 NYS2d 76 [1996]*; *Hecker v Paschke, 133 AD3d 713, 716, 19 NYS3d 568 [2015])*.

A cause of action alleging fraudulent misrepresentation requires that reliance be reasonable (*see* *Epifani v Johnson, 65 AD3d 224, 230, 882 NYS2d 234 [2009])*. "[I]f **[***6]** the facts represented are not matters peculiarly within the party's knowledge, and the other party has the means available to him [or her] of knowing, by the exercise of ordinary intelligence, the truth or the real quality of the subject of the **[**302]** representation, he [or she] must make use of those means, or he [or she] will not be heard to complain that he [or she] was induced to enter into the transaction by misrepresentations" (*Schumaker v Mather, 133 NY 590, 596, 30 NE 755, 4 Silv A 224 [1892]*; *see* *ACA Fin. Guar. Corp. v Goldman, Sachs & Co., 25 NY3d 1043, 1044, 10 NYS3d 486, 32 NE3d 921 [2015]*; *DDJ Mgt., LLC v Rhone Group L.L.C., 15 NY3d 147, 154, 931 NE2d 87, 905 NYS2d 118 [2010])*.

Moreover, " '[w]hen the party to whom a misrepresentation is made has hints of its falsity, a heightened degree of diligence is required of it' " (*Centro Empresarial Cempresa S.A. v América Móvil, S.A.B. de C.V., 17 NY3d 269, 279, 952 NE2d 995, 929 NYS2d 3 [2011]* **[****3]** , quoting *Global Mins. & Metals Corp. v Holme, 35 AD3d 93, 100, 824 NYS2d 210 [2006])*. Under such circumstances, the party " 'cannot reasonably rely on such representations without making additional inquiry to determine their accuracy' " (*Centro Empresarial Cempresa S.A. v América Móvil, S.A.B. de C.V., 17 NY3d at 279*, quoting *Global Mins. & Metals Corp. v Holme, 35 AD3d at 100*).

Here, the fourth cause of action sought to recover damages **[*689]** for fraudulent misrepresentation. The complaint alleged that the defendant's erroneous representations as to the tax-exempt status of the plaintiff's services induced the plaintiff to enter into the 2010 Agreement and forgo the collection of taxes from the defendant in connection with the runway project. However, the defendant established, prima **[***7]** facie, that any such reliance was unreasonable as a matter of law. The plaintiff does not allege that the defendant was in the exclusive possession of any facts which bore upon the tax-exempt status of the plaintiff's work. To the contrary, the plaintiff was aware of the nature of the services it was providing to the defendant. As such, the only representation upon which the plaintiff could have relied was the defendant's legal opinion as to the taxable status of the plaintiff's work. In that regard, the plaintiff was in an equal position to discover the applicable law. Furthermore, the Tax Exemption

Certificate issued by the defendant was, on its face, inapplicable to the plaintiff's work given that the plaintiff was providing security services to the defendant, rather than "tangible personal property." Under such circumstances, a " 'heightened degree of diligence is required' " (*Centro Empresarial Cempresa S.A. v América Móvil, S.A.B. de C.V., 17 NY3d at 279*, quoting *Global Mins. & Metals Corp. v Holme, 35 AD3d at 100*), and yet the plaintiff failed to utilize the means it had to determine the truth of the defendant's legal representations (*see Hecker v Paschke, 133 AD3d at 716-717*; *Sitar v Sitar, 61 AD3d at 742*; *Friedler v Palyompis, 44 AD3d 611, 611-612, 845 NYS2d 347 [2007]*; *Orlando v Kukielka, 40 AD3d 829, 831-832, 836 NYS2d 252* **[**303]** *[2007]*; *Curran, Cooney, Penney v Young & Koomans, 183 AD2d 742, 743-744, 583 NYS2d 478 [1992]*).

In opposition to the defendant's prima facie showing, the plaintiff failed to raise a triable issue of fact as to whether its reliance upon the alleged misrepresentations **[***8]** was justified under the circumstances. Accordingly, we agree with the Supreme Court's grant of that branch of the defendant's cross motion which was for summary judgment dismissing the fourth cause of action (*see Hecker v Paschke, 133 AD3d at 716-717*; *Sitar v Sitar, 61 AD3d at 742*; *Friedler v Palyompis, 44 AD3d at 611-612*; *Orlando v Kukielka, 40 AD3d at 831-832*; *Curran, Cooney, Penney v Young & Koomans, 183 AD2d at 743-744*). For the same reasons, we agree with the court's denial of that branch of the plaintiff's motion which was for summary judgment on that cause of action.

The third cause of action asserted in the complaint alleged unjust enrichment. The doctrine of unjust enrichment invokes an "obligation imposed by equity to prevent injustice, in the **[*690]** absence of an actual agreement between the parties concerned" (*IDT Corp. v Morgan Stanley Dean Witter & Co., 12 NY3d 132, 142, 907 NE2d 268, 879 NYS2d 355 [2009]*; *see Pappas v Tzolis, 20 NY3d 228, 234, 982 NE2d 576, 958 NYS2d 656 [2012]*). Accordingly, "a party may not recover in quantum meruit or unjust enrichment where the parties have entered into a contract that governs the subject matter" (*Cox v NAP Constr. Co., Inc., 10 NY3d 592, 607, 891 NE2d 271, 861 NYS2d 238 [2008]*; *see Pappas v Tzolis, 20 NY3d at 234*).

Here, the defendant established, prima facie, that the payment of applicable taxes was expressly provided for in the parties' agreements (*see CSI Group, LLP v Harper, 153 AD3d 1314, 61 NYS3d 592 [2017]*; *Rayham v Multiplan, Inc., 153 AD3d 865, 868-869, 61 NYS3d 90 [2017]*). Indeed, the plaintiff's complaint alleges as much. In opposition, the plaintiff failed to raise a triable issue of fact. Accordingly, we agree with the Supreme Court's grant of that branch of the defendant's cross motion which was for summary judgment dismissing **[***9]** the third cause of action (*see CSI Group, LLP v Harper, 153 AD3d 1314, 61 NYS3d 592 [2017]*; *Rayham v Multiplan, Inc., 153 AD3d at 868-869*). For the same reasons, we agree with the court's denial of that branch of the plaintiff's motion which was for summary judgment on that cause of action.

The second cause of action sought to recover damages for breach of contract. The complaint alleged that the defendant breached the 2009 Agreement by failing to pay applicable sales tax for services rendered pursuant to that agreement, and that the plaintiff was damaged in the amount of back taxes, and interest imposed thereon, which the New York State Department of **[****4]** Taxation and Finance sought to recover from the plaintiff after the audit.

The defendant established that the unpaid taxes which New York State sought to recover from the plaintiff accrued on invoices which were dated *after* the 2010 Agreement was executed by the parties. The 2010 Agreement required the plaintiff to pay all applicable taxes. Accordingly, the defendant established, prima facie, its entitlement to summary judgment dismissing the second cause of action. In opposition, the plaintiff failed to raise a triable issue of fact as to whether any of the back taxes accrued for work that was performed prior to the execution of the 2010 **[***10]** Agreement such that the terms of the 2009 Agreement would control. Accordingly, we agree with the Supreme Court's grant of that branch of the defendant's cross motion which was for summary judgment dismissing the second cause of action (*see Alvarez v Prospect Hosp., 68 NY2d 320, 324, 501 NE2d 572, 508 NYS2d 923 [1986]*).

Finally, inasmuch as the defendant established, as a matter **[*691]** of law, that it was not required to pay the disputed taxes under any theory advanced by the plaintiff, we agree with the Supreme Court's denial of that branch of the plaintiff's motion which was for summary judgment on the first cause of action, and grant of that branch of the defendant's cross motion which was for summary judgment dismissing **[**304]** the first cause of action. Since this is, in part, a declaratory judgment action, we remit the matter to the Supreme Court, Westchester County, for the entry of a judgment, inter alia, declaring that the defendant is not legally obligated to pay all sales tax, including interest and penalties, if any, owed as a result of the plaintiff's provision of services to the defendant (*see* *Lanza v Wagner, 11 NY2d 317, 183 NE2d 670, 229 NYS2d 380 [1962]*). Balkin, J.P., Chambers, Cohen and Miller, JJ., concur.

End of Document

Kasen v. Morrell

Supreme Court of New York, Appellate Division, Second Department

June 16, 1958 - Decided

No Number in Original

Reporter

6 A.D.2d 816 *; 175 N.Y.S.2d 315 **; 1958 N.Y. App. Div. LEXIS 5562 ***

DAVID KASEN, Respondent, v. CHARLOTTE S. MORRELL et al., Appellants, et al., Defendants.

Opinion

[*1]** **[*816]** **[**316]** Appeal from so much of an order as denied a motion, pursuant to subdivision 4 of rule 106 of the Rules of Civil Practice, to dismiss the first cause of action in the complaint (which was pleaded solely against appellant Charlotte S. Morrell) and the third and fourth causes of action in the complaint (which were pleaded solely against appellant Samuel Morrell). Order affirmed, with $10 costs and disbursements. The first cause of action is based on the alleged breach of a written contract between respondent and appellant Charlotte S. Morrell, the owner of a licensed retail liquor store, pursuant to which respondent agreed to purchase, and said appellant agreed to sell, a one-half interest in the liquor store and to become partners in the business, conditioned on the approval of the State Liquor Authority of the application for the retail liquor store license necessary for the sale of the one-half interest and the creation of the partnership.It was agreed therein that application to the State Liquor Authority for approval would be made within a reasonable time and that, in the event the State Liquor Authority did not approve the purchase within four months **[***2]** from the date of the contract, the sale would become of no effect and all money paid to said appellant should be returned to respondent within 60 days thereafter. The contract provided that, subject to the provisions therein contained, respondent and said appellant would become partners in the business. It was also provided therein that "Upon the approval by the State Liquor Authority, as hereinafter provided, the parties hereto, at the closing, will enter into a partnership agreement to effectuate the purposes of this agreement." **[**317]** The complaint was verified about 19 months after the contract was executed. In the first cause of action, it is alleged that respondent loaned $10,000 to said appellant and paid $5,000 on account of the purchase price, pursuant to the terms of the contract, and that respondent is willing to abide by the agreement and to perform. It is also alleged that said appellant failed and refused to make the application to the State Liquor Authority for the approval and sale of the one-half interest in the business and the creation of the partnership. Appellants contend that since the contract provided that, on approval by the State Liquor Authority **[***3]** the parties would enter into a partnership agreement to effectuate the purposes of the agreement, the first contract was nothing more than an agreement to agree and therefore unenforcible. They refer to the fact that there are no provisions in the contract for the duration of the partnership, the drawings of the partners, how the business should be managed and what should happen on the death of a partner or the dissolution of the partnership. The contract was not a mere brief memorandum. It had many provisions which need not now be described. From the contract itself, it is evident that it was executed with consideration of the restrictions imposed by the Alcoholic Beverage Control Law and the Rules of the State Liquor Authority on the issuance and transfer of licenses, and with consideration of the approval required of persons who have, or seek to acquire, interests in licensed premises. It is evident that the contract was executed with the realization that a license is a valuable asset of the owner of licensed premises (see, e.g., *Monclova v. Arnett, 3 N Y 2d 33*). A contract is to be interpreted in accordance with the intention of the contracting parties. Custom **[***4]** or usage, when the parties know or have reason to know of the custom or usage, when the custom or usage is reasonable, uniform, well **[*817]** settled, not in opposition to fixed rules of law and not in contradiction of the express terms of the agreement, is deemed to form a part of the contract and to enter into the intention of the parties. The parties are presumed to contract in reference to the law of this State *(Frye v. State of New York, 192 Misc. 260, 264-265)*. Unless "a contract provides otherwise, the law in force at the time the agreement is entered into becomes as much a part of the agreement as though it were expressed or referred to therein, for it is presumed that the parties had such law in contemplation when the contract was made and the contract will be construed in the light of such law" *(Dolman v. United States Trust Co., 2 N Y 2d 110, 116)*. In our opinion the allegations in the first cause of action do not require a determination that an agreement on material elements had not been made and that the contract was unenforcible *(Spiritusfabriek Astra of Amsterdam, Holland v. Sugar Prods. Co., 176 App. Div. 829*, **[**318]** affd. **[***5]** *221 N. Y. 581*; cf. *Ansorge v. Kane, 244 N. Y. 395*). The "purposes of this agreement" could have been effectuated by the application of the Partnership Law (see, e.g., *Spiritusfabriek Astra of Amsterdam, Holland v. Sugar Prods. Co., supra).* Even if the contract were unenforcible, it would not be proper to dismiss the cause as insufficient since it states a cause of action at least for the return of the money paid by respondent pursuant to the contract *(Nisofsky v. Simon, 280 App. Div. 874*; see, e.g., *Healy v. Hourigan, 276 App. Div. 1085*). So far as the causes of action against appellant Samuel Morrell are before us for review, they cannot be dismissed as insufficient even if the contract between respondent and Charlotte S. Morrell were unenforcible. They state at least causes of action to recover damages for breach of a contract signed by appellant Samuel Morrell, the husband of the other appellant, on the same date that the other contract was executed, guaranteeing, in part, performance by the wife of her contract. Wenzel, Acting P.J., Beldock, Murphy, Hallinan and **[***6]** Kleinfeld, JJ., concur. [*10 Misc 2d 176*.]

Maple-Gate Anesthsiologists, P.C. v. Nasrin

Supreme Court of New York, Erie County

March 22, 2019, Decided

818104/2018

Reporter

63 Misc. 3d 703 *; 96 N.Y.S.3d 837 **; 2019 N.Y. Misc. LEXIS 1173 ***; 2019 NY Slip Op 29075 ****

[**1]** Maple-Gate Anesthsiologists, P.C., Plaintiff against Deixry Nasrin and DOUGLAS BRUNDIN, Defendants

Counsel: **[***1]** For Plaintiff: Robert J. Portin and Michael E. Ferdman, of Counsel, HURWITZ & FINE, P.C.

For Defendant: Amber Storr and Andrea Schillaci, of Counsel.

Judges: HON. FRANK A. SEDITA, III, J.S.C.

Opinion by: FRANK A. SEDITA, III

Opinion

[*704] **[**838]** Frank A. Sedita III, J.

The plaintiff is suing the defendants for unjust enrichment and conversion. Before the court is the defendants' pre-Answer motion to dismiss the lawsuit.

The plaintiff is a medical practice. It provides anesthesia services to hospitals and ambulatory surgical centers in Western New York. These facilities require the plaintiff's physicians and Certified Registered Nurse Anesthetists to maintain professional liability insurance.

The defendants are Certified Registered Nurse Anesthetists. Defendant Deixry Nasrin was employed by the plaintiff from March 13, 2012 to April 28, 2017. Defendant Douglas Brundin was employed by the plaintiff from January 1, 2010 to January 6, 2016. Article 3 (c)(ii) of their employment agreements provided that the plaintiff would pay professional liability **[****2]** insurance premiums as an "employment benefit for and on behalf of" the employee. That insurance was secured through the Medical Liability Mutual Insurance Company (MLMIC). The defendants **[***2]** were named as the insured under their individual MLMIC policies. They consequently became policyholders and members of MLMIC.

MLMIC and the defendants entered into a "MLMIC Policy Administrator — Designation & /or Change" agreement, by which the defendants designated the plaintiff as their agent and policy administrator. According its terms, "The Policy Administrator is the agent of all Insureds herein for the paying of premium, requesting changes in the policy, including cancellation thereof and for receiving dividends and any return premiums when due."

Neither the employment agreement nor the MLMIC Policy Administrator — Designation & /or Change agreement contained language indicating that the defendants **[**839]** waived, transferred or assigned their ownership interest in the policy to someone else.

The MLMIC Board of Directors approved a proposed transaction by which MLMIC would demutualize, convert to a stock **[*705]** insurance company, and be acquired by the National Indemnity Company (NICO) for $2.502 billion. The MLMIC Board later adopted a plan of conversion, whereby cash consideration would be paid to policyholders/members in exchange for the extinguishment of the policyholder membership interests. **[***3]** Pursuant to §8.2(a) of the Plan of Conversion (the Plan), "Each Eligible Policyholder (or it's designee) shall receive a cash payment in an amount equal to the applicable conversion." Pursuant to §2.1 of the Plan, an "eligible policyholder" was the person designated as the insured, while a "designee" meant employers or policy administrators, "designated by Eligible Policyholders to receive the portion of the Cash Consideration allocated to such Eligible Policyholders." The Plan did not provide for the policy administrator to receive cash consideration absent such a designation from the policyholder/member.

The New York Superintendent of Financial Services held a public hearing and approved the Plan. In her September 6, 2018 decision (DFS Decision), the Superintendent wrote: "MLMIC's eligible policyholders will receive cash consideration. Insurance Law §7307(e)(3) expressly defines those persons who are entitled to receive the proceeds of the Demutualization as each person who had a policy in effect during the three-year period preceding the MLMIC Board's adoption of the resolution (the 'Eligible Policyholders') and explicitly provides that each Eligible Policyholder's equitable share of the purchase price shall be determined **[***4]** based on the amount of the net premiums paid on eligible policies" (DFS Decision, p.4).

The DFS Decision also acknowledged testimony and written comments from medical groups. Nearly identical to the plaintiff's contentions in this case, the medical groups had argued that the cash consideration belonged to them because they had paid the premiums on behalf of the policyholders and/or had acted as the policy administrators. Addressing these arguments, the Superintendent of Financial Services wrote: "Insurance Law §7307(e)(3) defines the policyholders eligible to be paid their proportional shares of the purchase price, but also recognizes that such policyholders may have assigned such legal right to other persons. Therefore, the plan appropriately **[*706]** includes an objection and escrow procedure for the resolution of disputes for those persons who dispute whether the policyholder is entitled to the payment in a given case." Such a claim would be, "decided either by agreement of the parties or by an arbitrator [which must be voluntary] or court" (DFS Decision, p.25).

The plaintiff did not make a claim, or otherwise avail itself of the objection and escrow procedure. MLMIC paid $18,532.60 to defendant Nasrim and $15,546.95 **[***5]** to defendant Brundin **[****3]** on October 4, 2018. Plaintiff's counsel corresponded to both defendants on the very same day. He threatened the defendants with legal action and demanded that they, "execute an [enclosed] Assignment Agreement transferring your right to the cash consideration to the practice."

Much of the foregoing detail is alleged in the plaintiff's complaint. It additionally alleges, inter alia, that the money received by the defendants is "unwarranted" and "rightly belongs to Maple-Gate" (¶29-32); that "it is against equity and good conscience" for defendants to have kept these **[**840]** benefits because the plaintiff paid the premiums (¶40); that the defendants were "unjustly enriched" (¶41); that the, "cash consideration that Defendants received is Maple-Gate's property" (¶45); and, that "by failing and refusing to remit the Benefit that each Defendant received, each Defendant has converted Maple-Gate's property" (¶48).

The defendants filed their motion to dismiss, in lieu of an Answer, on January 6, 2019. Pursuant to CPLR 3211(a)(7), the defendants allege that the complaint fails to state a cause of action. Pursuant to CPLR 3211(a)(1), the defendants also allege that the documentary evidence conclusively establishes **[***6]** that the plaintiff does not have a cause of action. The plaintiff's opposition papers were filed on February 8, 2019. Oral arguments were heard by the court on February 20, 2019.

In support of their motion to dismiss, the defendants principally contend that they were the lawful policyholders and thus possessed an actual and exclusive ownership interest in the cash consideration.

In opposition, the plaintiff principally contends that it is entitled to the cash consideration because it had a virtual ownership interest in the cash consideration; i.e. being designated as the policy administrator, paying the premiums and using any refunds to reduce overall business costs, "vested **[*707]** the Practice w/ virtually all incidents of ownership in the policies" (Plaintiff's Memorandum of Law, p.5). The plaintiff also contends that the Plan and the DFS Decision, "control everything in the case and take precedence over everything in the case" and that, "both expressly recognize the practice's claims to the proceeds and expressly or implicitly, at least, refute the claim that the defendants have to those proceeds as a matter of law" (Transcript of Motions Argument, p.11).

CPLR 3211 authorizes the summary dismissal **[***7]** of a complaint. The court, when considering such a motion, must accept the facts as alleged in the complaint as true, accord the plaintiff the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory. Leon v. Martinez, 84 NY2d 83, 88, 638 N.E.2d 511, 614 N.Y.S.2d 972; Murmane Building Contractors, LLC v. Cameron Hill Construction, LLC, 159 AD3d 1602, 1603, 73 N.Y.S.3d 848. A cause of action cannot, however, be predicated on mere conclusory statements unsupported by factual allegations. *Bratge v. Simons, 167 AD3d 1458, 91 N.Y.S.3d 630*; *Miller v. Allstate Indemnity Co., 132 AD3d 1306, 17 N.Y.S.3d 240*. Allegations consisting of bare legal conclusions, as well as claims flatly contradicted by documentary evidence, are not entitled to consideration. *Maas v. Cornell University, 94 NY2d 87, 91, 721 N.E.2d 966, 699 N.Y.S.2d 716*; *Attallah v. Milbank, Hadley, and McCoy, LLP 168 AD3d 1026, 93 N.Y.S.3d 353*. Such a complaint should be dismissed when the documentary evidence conclusively refutes its allegations. *Dominski v. Frank Williams & Son, LLC, 46 AD3d 1443, 848 N.Y.S.2d 791* (*also see, Liberty Affordable Housing Inc. v. Maple Court Apartments, 125 AD3d 85, 998 N.Y.S.2d 543*).

The complaint's allegations are made in support of two causes of action, namely, conversion and unjust enrichment. An actionable conversion takes place when someone, intentionally and without authority, assumes or exercises control over personal property belonging to someone else, interfering with that person's right of possession. *Reeves v. Gianotta, **[****4]** 130 AD3d 1444, 12 N.Y.S.3d 736*. The key elements of conversion are (1) the plaintiff's possessory right or interest in the property and (2) **[**841]** the defendants dominion over the property or interference with **[***8]** it, in derogation of the plaintiff's rights. *Palermo v. Taccone, 79 AD3d 1616, 1619-1620, 913 N.Y.S.2d 859*.

Like conversion, an unjust enrichment claim presupposes that the plaintiff has an ownership interest in the property or benefit it seeks to recover from the defendants (*see, 28 NY Practice, **[*708]** Contract Law* § 4:14; *Roslyn Union Free School Dist. v. Barkan, 71 A.D.3d 660, 661, 896 N.Y.S.2d 406)*. The key elements of unjust enrichment are (1) that the defendants were enriched (2) at the plaintiff's expense and (3) that it is against equity and good conscience to permit the defendants to retain what is sought to be recovered. The doctrine is a narrow one and is not a catchall cause of action to be used when others fail. *E.J. Brooks Company v. Cambridge Security Seals, 31 NY3d 441, 455, 80 N.Y.S.3d 162, 105 N.E.3d 301*. Mere enrichment is not enough to warrant liability and an allegation that the defendants received benefits, standing alone, is insufficient to establish the cause of action. Critical is that the enrichment be unjust (*see, Goel v. Ramachandran, 111 AD3d 783, 791, 975 N.Y.S.2d 428)*.

It is undisputed that the plaintiff received refunds, like returned dividends and premiums, while it was the policy administrator and MLMIC was the insurer. The benefit at issue in this matter is the cash consideration. Unlike a refund, the cash consideration was clearly intended to be in exchange for the extinguishment of the defendants' membership interest in MLMIC.

It is important to note **[***9]** that MLMIC was a mutual insurance company. Generally speaking, a mutual insurance company is a cooperative enterprise in which the policyholders constitute the members for whose benefit the company is organized, maintained, and operated (*68 NY Jur. 2d Insurance § 179*). In this regard, *Insurance Law § 1211(a)*, provides in part, that: "Every domestic mutual insurance corporation shall be organized, maintained and operated for the benefit of its members as a non-stock corporation. Every policyholder shall be a member of such corporation." Thus, when the defendants, at the plaintiff's behest, signed up for professional liability policies issued by MLMIC, they acquired certain rights and benefits, including membership in MLMIC.

It is also important to take note of the demutualization process by which MLMIC was converted from a mutual insurance company into a stock insurance company acquired by NICO. *§7307 of the Insurance Law* governs this process. *Insurance Law §7307(e)(3)*, in relevant part, provides that, "each person who had a policy of insurance in effect at any time during the three year period immediately preceding the date of adoption of the resolution shall be entitled to receive in exchange for such equitable share, without additional payment, **[*709]** consideration payable in voting common **[***10]** shares of the insurer or other consideration, or both." The statute goes on to repeatedly refer to the eligible recipient as the policyholder and sets forth a formula regarding how to calculate the amount of consideration the policyholder would receive as a result of demutualization. The formula takes-into-account the amount of premiums paid. No distinction is made between a policyholder who pays the premium out of his own pocket versus a policyholder whose employer pays the premium as part of an employee compensation package. *Insurance Law §7307* does not confer an ownership interest in the stock or to the to the cash consideration to anyone other than the policyholder.

Being designated as the policy administrator did not make the plaintiff a policyholder, did not make the plaintiff a member **[**842]** of MLMIC and did not entitle the plaintiff to the cash consideration. More was required. Under the Plan, the policyholder was required to designate someone as being entitled to the cash consideration before that person or entity was entitled to that benefit. The DFS Decision reiterated that it was the policyholder who was entitled to the **[****5]** cash consideration; recognized that such policyholders "may have assigned such **[***11]** legal right to other persons" (DFS Decision, p.25); and, tied eligibility for the objection and escrow process to when the policyholder had, in fact, assigned the right to cash consideration to another person or entity. It appears certain that such a designation or assignment never took place in this case. More to the point, the plaintiff does not allege that such a designation or assignment ever took place. This alone is fatal to the plaintiff's claim that it is entitled to the cash consideration.

As it appears the defendants never had designated the plaintiff to receive the cash consideration, it is no wonder that the plaintiff did not avail itself of the objection and escrow process. The plaintiffs instead demanded that the defendants, "execute an assignment agreement transferring your right to the cash consideration to the Practice." Such an explicit recognition of the defendant's *right* to the cash consideration undermines the claim that the they unlawfully converted it to themselves or that they were unjustly enriched. The transfer demand is also an implicit acknowledgement that the defendants had never designated the plaintiff to receive the cash consideration.

The controlling **[***12]** statutes and the documentary evidence conclusively demonstrate that the defendants had an actual **[*710]** and exclusive ownership interest in the cash consideration. Allegations to the effect that the plaintiff had a legally cognizable ownership interest in the cash consideration is flatly contradicted by the same statutes and evidence. Allegations to the effect that the defendants windfall was unwarranted, or that the defendants converted to themselves that which rightly belonged to the plaintiff, or that the defendants were unjustly enriched, or that it is against equity and good conscience for the defendants to keep their money, are nothing more than bare legal conclusions. Accordingly, the defendants' motion to dismiss the Complaint, pursuant to *CPLR 3211(a)(1)* and *CPLR 3211(a)(7)*, is GRANTED.

The foregoing shall constitute the decision and order of this court.

Dated: March 22, 2019

HON. FRANK A. SEDITA, III, J.S.C.

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF WESTCHESTER

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MAPLE MEDICAL LLP, RICHARD FRIMER, M.D., ANDREW GOLDSTEIN, M.D., JOANNE TAMBURRI, M.D., AND WILLIAM ZAROWITZ, M.D.,

Petitioner,

-against-

NEW YORK STATE DEPARTMENT OF FINANCIAL SERVICES, MARIA T. VULLO, SUPERINTENDENT OF THE DEPARTMENT OF FINANCIAL SERVICES,

Respondents,

For a judgment, pursuant to Article 78 of the Civil Practice Law and Rules.

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DECISION, ORDER & JUDGMENT

Index No. 65929/2018

SCHWARTZ, J.

Petitioners commenced this hybrid CPLR Article 78 proceeding and declaratory judgment action seeking an order and judgment (1) reversing, annulling, vacating and setting aside the Decision of the Superintendent of the Department of Financial Services dated September 6, 2018, and/or (2) declaring that the parties that paid the premiums on the polices of insurance for the identified period are the policy holders of the policies issued by Medical Liability Insurance Company, and/or (3) declaring that the parties that paid the premiums on these policies are the parties entitled to receive any payment due upon demutualization. The respondents oppose.

The Court has considered the following papers: the e-filed documents numbered 1-23, 31-48, and 51-57.

Upon the foregoing papers, the petition is disposed of as follows:

Petitioner MAPLE MEDICAL LLP is a multispecialty medical practice in White Plains, New York. As gleaned from the papers, on or about July 15, 2016, Medical Liability Mutual Insurance Company ("MLMIC") announced that it would seek to convert from a domestic mutual property/casual insurance company into a domestic stock property/casualty insurance company and, pursuant to Insurance Law § 7307, filed an application with the respondents for permission to convert. Pursuant to the conversion plan and an acquisition agreement, MLMIC would convert, and, in exchange, the eligible policyholders would receive cash consideration for their interest in MLMIC, rather than stock, which would instead be sold to National Indemnity Company. Policyholders' cash payments would be calculated based upon the pro-rata share of net premiums paid on eligible policies. The conversion plan defines a policyholder as a person or persons identified on the declaration page of the policy as the insured.

Respondents ordered an examination of MLMIC pursuant to Insurance Law § 7307(b)(3) and after a duly-noticed public hearing, amendments to the acquisition agreement and examination report, the Department approved the conversion plan provided the plan was submitted to a vote by the record date policyholders and, upon approval, the acquisition closed by September 30, 2018, or any agreed upon extended date (*see* Decision, Doc No. 23). On September 13, 2018, the record date policyholders approved the plan and the acquisition by National Indemnity Company's of MLMIC's shares closed on October 1, 2018. As of October 30, 2018, over $2.3 billion has been paid out to eligible policyholders.

On September 28, 2018, the petitioner commenced the instant proceeding and action. Petitioners do not argue that the determination approving demutualization and sale of MLMIC was arbitrary and capricious, irrational, or in violation of proper procedure. Rather, the petitioners argue that the definition of a policyholder in the conversion plan is erroneous because it is contrary to the Insurance Law's definition of a policy holder. Petitioners contend that, in effect, Insurance Law § 7307 requires policyholders be defined under the conversion plan as the parties who actually paid the premiums and not the doctors who are insured under the policies. Since Petitioners paid for and procured medical liability insurance from MLMIC for employees of their practice, Petitioners argue they, not the doctors they paid to insure, should have been deemed the policyholders and thus recipients of cash payments under the conversion plan.

Respondents argue as affirmative defenses that, *inter alia*, the petition must be dismissed as moot and the petitioners failed to name necessary parties. Respondents also contend that, nevertheless, the determination was not contrary to the Insurance Law, arbitrary and capricious, nor irrational, and should be upheld.

Relevant Law

An administrative determination "must be upheld if it has support in the record, a reasonable basis in law, and is not arbitrary or capricious" (*Paloma Homes, Inc. v Petrone*, 10 AD3d 612, 613 [2d Dept 2004]).

"As the power of a court to declare the law only arises out of, and is limited to, determining the rights of persons which are actually controverted in a particular case, courts generally may not pass on academic, hypothetical, moot, or otherwise abstract questions…Thus, courts ordinarily may not consider questions that have become moot by passage of time or change in circumstances…When a determination would have no practical effect on the parties, the matter is moot and the court generally has no jurisdiction to decide the matter" (*Berger v Prospect Park Residence, LLC*, 166 AD3d 937 [2d Dept 2018] [internal citations omitted]; *see also State Farm Mut. Auto. Ins. Co. v TIG Ins. Co.*, 62 AD3d 859, 860 [2d Dept 2009]).

"A party whose interest may be adversely effected by a potential judgment must be made a party in a CPLR article 78 proceeding" (*Karmel v White Plains Common Council*, 284 AD2d 464, 465 [2d Dept 2001]; *see also Feder v Town of Islip Zoning Bd. of Appeals*, 114 AD3d 782 [2nd Dept 2014] and CPLR 1001[a]). Where a necessary party has not been timely joined and does not voluntarily appear or participate in the proceeding, the Supreme Court must deny the petition and dismiss the proceeding. (*see Karmel v White Plains Common Council*, 284 AD2d 464, 465 [2d Dept 2001; *Artrip v Inc. Vil. of Piermont*, 267 AD2d 457, 457 [2d Dept 1999]).

<u>Discussion</u>

Since the filling of the petition, it is not disputed that demutualization has occurred and that over $2.3 billion in cash payments have been distributed to policyholders pursuant to the determination of the Department and the conversion plan. In light of the foregoing and petitioners' failure to seek injunctive relief from this Court to preserve the status quo before demutualization and distribution of cash payments, I find the petition is moot and must be dismissed (*see Berger* at 937; *see also Weeks Woodlands Ass'n, Inc. v Dormitory Auth. of State, 95 AD3d 747 [1st Dept 2012], affd, 20 NY3d 919 [2012]*).

If the petition were not moot, it would still be dismissed for failure to name necessary parties. The policyholders who received cash payments were not made parties to this proceeding, and it cannot be disputed they would be adversely effected by a potential judgment declaring them not entitled to those payments in whole or in part (*see Karmel* at 465). Moreover, of those policyholders who are entitled to receive cash payments under the plan, it is not in dispute some of them are doctors employed by the petitioners' very own medical practice (*see* Doc. No. 4). Yet, the petitioners did not join those doctors in this proceeding and action.

Even if the Court were to reach the merits of the petition, the Court would not annul the respondents' determination. The Court's review of the parties' submissions, including the record, reveals that the respondents properly considered and weighed the relevant criteria and that the determination had a rational basis. Furthermore, the record does not reveal that the respondents acted illegally or arbitrarily and capriciously. Given these circumstances, the Court would not disturb the respondents' determination. Accordingly, it is

ORDERED and ADJUGED that the petition is dismissed in its entirety.

This decision constitutes the order and judgment of the Court.

Dated: White Plains, New York
December 28, 2018

HON. LARRY J. SCHWARTZ, A.J.S.C.

January 2nd 2019

TO: All parties by e-filing.

Matter of Schaffer, Schonholz & Drossman, LLP v Title

Supreme Court of New York, Appellate Division, First Department

April 4, 2019, Decided; April 4, 2019, Entered

8892, 1602015/18

Reporter
171 A.D.3d 465 *; 96 N.Y.S.3d 526 **; 2019 N.Y. App. Div. LEXIS 2630 ***; 2019 NY Slip Op 02617 ****; 2019 WL 1473748

[**1]** In the Matter of Schaffer, Schonholz & Drossman, LLP, Petitioner, v Rachel S. Title, M.D., Respondent.

Counsel: **[***1]** Hughes Hubbard & Reed LLP, New York (Amina Hassan of counsel), for petitioner.

Richard A. Klass, Brooklyn, for respondent.

Judges: Concur—Sweeny, J.P., Manzanet-Daniels, Kern, Oing, Singh, JJ.

Opinion

[*465] **[**526]** Upon facts submitted to this Court pursuant to CPLR 3222 (b) (3), it is declared that petitioner is entitled to the cash proceeds resulting from the demutualization of nonparty Medical Liability Mutual Insurance Company (MLMIC). The Clerk of Supreme Court, New York County is directed to enter judgment awarding petitioner said cash proceeds, including interest accrued while the proceeds were in escrow.

Although respondent was named as the insured on the relevant MLMIC professional liability insurance policy, petitioner purchased the policy and paid all the premiums on it. Respondent does not deny that she did not pay any of the annual premiums or any of the other costs related to the policy. Nor did she bargain for the benefit of the demutualization proceeds. Awarding respondent the cash proceeds of MLMIC's demutualization would result in her unjust enrichment (*see* *Ruocco v Bateman, Eichler, Hill, Richards, Inc., 903 F2d 1232, 1238 [9th Cir 1990]*, *cert denied 498 US 899, 111 S Ct 254, 112 L Ed 2d 212 [1990]*; *Chicago Truck Drivers, Helpers & Warehouse Workers Union [Ind.] Health & Welfare Fund v Local 710, Intl. Bhd. of Teamsters, Chicago Truck Drivers, Helper & Warehouse Workers Union [Ind.] Pension Fund, 2005 U.S. Dist. LEXIS 42877, *10-11, *21-22, 2005 WL 525427, *4, *8 [ND Ill, Mar. 4, 2005, No. 02 C 3115]*). **[***2]** Concur—Sweeny, J.P., Manzanet-Daniels, Kern, Oing, Singh, JJ.

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Menin v. New York Life Ins. Co.

Supreme Court of New York, Special Term, New York County

June 19, 1941

No Number in Original

Reporter

188 Misc. 870 *; 69 N.Y.S.2d 523 **; 1941 N.Y. Misc. LEXIS 1367 ***

Abraham I. Menin, as Trustee in bankruptcy of American Art Association-Anderson Galleries, Inc., Plaintiff, v. New York Life Insurance Company et al., Defendants *

Subsequent History: **[***1]** * See, also, Fenster v. New York Life Ins. Co., 188 Misc. 909, affd. without opinion *272 A.D. 879*.

Prior History: Action on policy of life insurance.

Counsel: *Gerson C. Young* and *Everett M. Seixas, Jr.,* for plaintiff.

John M. Harlan, Leslie H. Arps and *Ferdinand H. Pease* for New York Life Insurance Company, defendant.

Judges: Steuer, J.

Opinion by: STEUER

Opinion

[*871] [524]** The object of the suit is to realize on a policy of life insurance on the life of Robert M. Mitchill, Jr. In the year 1939, the policy was eight years old and the premium on it was being paid in quarterly installments. The third quarterly installment became payable on September 18th. It was not paid. The grace period expired. Defendant insurance company then declared the cash value to be as fixed in the policy for one in existence eight and three-quarters years. Deducting from this sum an outstanding loan, a small remainder was left. This remainder purchased paid-up term insurance expiring November 20, 1939. The insured committed suicide on November 27, 1939.

The contention of the plaintiff beneficiary is that, had three quarters of the annual dividend which would have become payable on the policy on the anniversary date, December 18th, been credited at the time of the default, that sum could **[***4]** have been used to buy term insurance. Had this been done, the term insurance bought concededly would have been in effect at the time of the insured's death. The question therefore presented is whether defendant was under a duty to make the fractional part of the dividend available at that time.

[525]** It is now well recognized that the so-called dividend payable upon a mutual life insurance contract bears no relation to a dividend upon stock of a stock corporation (Rhine v. New York Life Ins. Co., 273 N.Y. 1, 6 N.E.2d 74). The distribution of available surplus, which is the life insurance dividend, must be made by the company and its manner of apportionment is determined by the contract and the Insurance Law. The law in effect at the time of the making of the contract in suit (Insurance Law of 1909, § 83, as amd. by L. 1927, ch. 467) provides that such distribution is to be made "annually and not otherwise." In the case of ordinary life policies no specific date for a distribution is fixed. (Cf. Wells v. Metropolitan Life Insurance Co., 171 Misc. 878, 13 N.Y.S.2d 22, affd. *258 A.D. 986, 18 N.Y.S.2d 170*.) Subsequent clarification of the statute (Insurance Law **[***5]** of 1939, § 216; L. 1939, ch. 882, § 216) and a long history of practice approved by the administrative authorities leaves no doubt that the anniversary date of the policy is a proper date for distributing. Providing this practice was uniform, and it was, no complaint against it could be made.

The question therefore becomes whether, despite the fact that distribution could not be made prior to the anniversary date, in the event of a lapse must a credit be given to the policy of the dividend or a fraction of it. No such specific direction is to be found either in the contract or the statute. If any obligation exists it comes into being from the very nature of the dividend.

[*872] It is quite true that in its essentials this dividend represents a return of the excess in cost of the insurance which conservative management has exacted to provide for unforeseen contingencies in the shape of disasters or investment upsets, which contingencies have not in fact materialized. However, it is equally true that the entire fabric of insurance is built upon mathematical principles of experience adhering to the average if a sufficient number of instances are involved. In a policy where the **[***6]** premium is payable in installments instead of annually in advance (the only instance where the problem presented can arise) the factor of lapse is always present. This factor finds reflection in the calculation of the premium especially as affected by the dividend. An interpretation of the statute which would require the dividend or a portion of it to be applied to the purchase of term insurance at a time prior to the time when the dividend was payable by the terms of the statute cannot be said to reflect the intention of the Legislature unless it be assumed that the Legislature was ignorant of this factor or disapproved of it. When the statute of 1939 containing the presently effective section 216 is considered, the opposite conclusion must be reached. In this section companies are given the authority (not the direction) to write policies providing for more frequent distributions, but only under certain conditions as regards the available surplus. As installment premium contracts are the only ones in which such more frequent distributions would **[**526]** be feasible and a threatened lapse the only occasion where the distribution would have real significance, it would seem to follow **[***7]** that provision for such a contract belied the contention that the duty to apply the dividend before its due date existed in any other form of contract.

Plaintiff has other theories upon which the term insurance purchasable was extended to a date subsequent to the death of the insured. They all depend on the dividend or a portion of it being used. In the light of the above, no discussion thereof is required.

Submit findings accordingly.

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Mountain View Coach Lines, Inc. v. Storms

Supreme Court of New York, Appellate Division, Second Department

June 18, 1984

No Number in Original

Reporter

102 A.D.2d 663 *; 476 N.Y.S.2d 918 **; 1984 N.Y. App. Div. LEXIS 18836 ***

Mountain View Coach Lines, Inc., Appellant, v. Betty Storms, Respondent

Prior History: **[***1]** Appeal from so much of a judgment of the Supreme Court (Vincent Gurahian, J.), entered July 12, 1983 in Dutchess County, as dismissed plaintiff's claim for loss of use.

Disposition: Judgment of the Supreme Court, Dutchess County, entered July 12, 1983, reversed insofar as appealed from, on the law, with costs, and matter remitted to the Supreme Court, Dutchess County, for entry of an appropriate judgment in the principal sum of $ 3,200.

Counsel: *George A. Roland* for appellant.

Owen & Grogan (*Thomas N. O'Hara* of counsel), for respondent.

Judges: Titone, J. Mollen, P. J., Weinstein and Rubin, JJ., concur.

Opinion by: TITONE

Opinion

[*663] OPINION OF THE COURT

[919]** Plaintiff appeals from so much of a judgment of the Supreme Court, Dutchess County, as dismissed its claim for damages for loss of use of a bus placed out of service as a result of defendant's negligence. The core issue is whether damages for loss of use are interdicted because plaintiff did not hire a substitute bus, utilizing one it maintained in reserve instead. We hold that loss of use damages are recoverable in such circumstances and decline to follow two Third Department cases to the contrary **[***3]** (*Mountain View Coach Lines v Gehr, 80 AD2d 949*; *Mountain View* ***[*664]*** *Coach Lines v Hartnett*, 99 Misc 2d affd *69 AD2d 1020*, as amd *70 AD2d 977*, mot for lv to app den *47 NY2d 710*).

On October 28, 1980, a collision occurred between a bus owned by the plaintiff and a motor vehicle owned by the defendant. The parties stipulated that the defendant was negligent, that the cost of repairs was $ 983.23, that the damages sustained for loss of use were $ 3,200, and that the facts supporting the claim for loss of use were the same as those in the two Third Department cases (*Mountain View Coach Lines v Gehr, supra; Mountain View Coach Lines v Hartnett, supra*) i.e., that no substitute was hired by the plaintiff during the period of repairs, plaintiff having substituted one of its own buses for the damaged bus. The loss of use claim was thus submitted to the Supreme Court as an issue of law, and was dismissed solely on constraint of the Third Department cases. We reverse the judgment insofar as appealed from and remit the case to the Supreme Court, Dutchess County, for entry of a judgment awarding plaintiff damages for loss of use.

At the outset, we note that if the Third Department **[***4]** cases were, in fact, the only New York authorities on point, the trial court followed the correct procedural course in holding those cases to be binding authority at the nisi prius level. The Appellate Division is a single State-wide court divided into departments for administrative convenience (see *Waldo v Schmidt, 200 NY 199, 202*; Project, The **[**920]** Appellate Division of the Supreme Court of New York: An Empirical Study of its Powers and Functions as an Intermediate State Court, 47 Ford L Rev 929, 941) and, therefore, the doctine of *stare decisis* requires trial courts in this department to follow precedents set by the Appellate Division of another department until the Court of Appeals or this court pronounces a contrary rule (see, e.g., *Kirby v Rouselle Corp., 108 Misc 2d 291, 296*; *Matter of Bonesteel, 38 Misc 2d 219, 222*, affd *16 AD2d 324*; 1 Carmody-Wait 2d, NY Prac, § 2:63, p 75). This is a general principle of appellate procedure (see, e.g., *Auto Equity Sales v Superior Ct. of Santa Clara County, 57 Cal 2d 450, 455*; *Chapman v Pinellas County, 423 So 2d 578, 580* [Fla App]; *People v Foote, 104 Ill App*

3d 581), necessary to maintain uniformity **[***5]** and consistency (see *Lee v Consolidated Edison Co.,* ***[*665]*** *98 Misc 2d 304, 306)*, and, consequently, any cases holding to the contrary (see, e.g., *People v Waterman, 122 Misc 2d 489, 495, n 2*) are disapproved.

Such considerations do not pertain to this court. While we should accept the decisions of sister departments as persuasive (see, e.g., *Sheridan v Tucker, 145 App Div 145, 147*; 1 Carmody-Wait 2d, NY Prac, § 2:62; cf. *Matter of Ruth H., 26 Cal App 3d 77, 86)*, we are free to reach a contrary result (see, e.g., *Matter of Johnson, 93 AD2d 1, 16*, revd on other grounds *59 NY2d 461*; *State v Hayes, 333 So 2d 51, 53* [Fla App]; *Glasco Elec. Co. v Department of Revenue, 87 Ill App 3d 1070*, affd 86 I11 2d 346). Denial of leave to appeal by the Court of Appeals is, of course, without precedential value (*Giblin v Nassau County Med. Center, 61 NY2d 67, 76*, n). We find the Third Department decisions little more than a "conclusory assertion of result", in conflict with settled principles, and decline to follow them (*People v Hobson, 39 NY2d 479, 490)*.

It is beyond dispute that where a motor vehicle is harmed as a result of a tortious act, the plaintiff **[***6]** is entitled to damages for loss of use during the time reasonably required to make repairs (*Johnson v Scholz, 276 App Div 163*; *Restatement, Torts 2d, § 928*; 10 Fuchsberg, Encyclopedia NY Law, Damages, § 875). While some early lower court cases held that recovery for loss of use was barred unless a substitute was actually hired (e.g., *Murphy v New York City Ry. Co., 58 Misc 237*), the Appellate Term, Second Department, later noted that these holdings were at variance with the rule generally prevailing in this State and elsewhere (*Dettmar v Burns Bros., 111 Misc 189*; see, also, Recovery for Loss of Use of Motor Vehicle Damaged or Destroyed, Ann., *18 ALR3d 497, 528)*. *Dettmar* states the correct rule and is in accord with subsequent New York authority (*Nicholas v Mellon Constr. Co., 241 App Div 771*; *Denehy v Pasarella, 230 App Div 707*; *Sellari v Palermo, 188 Misc 1057*; *Pittari v Madison Ave. Coach Co., 188 Misc 614*; 10 Fuchsberg, *op. cit.*, § 878).

There is no logical or practical reason why a distinction should be drawn between cases in which a substitute vehicle is actually hired and those in which the plaintiff utilizes a spare. The point is well **[***7]** illustrated by then **[*666]** Justice Cardozo's opinion in *Brooklyn Eastern Term. v United States* (287 U.S. 170, 176-177), explaining the so-called "spare boat" doctrine applied in admiralty: "Shipowners at times maintain an extra or spare boat which is kept in reserve for the purpose of being utilized as a substitute in the contingency of damage to other vessels of the fleet. There are decisions to the effect that in such conditions the value of the use of a boat thus **[**921]** specially reserved may be part of the demurrage * * * If no such boat had been maintained, another might have been hired, and the hire charged as an expense. The result is all one whether the substitute is acquired before the event or after." [1]

[*8]** This reasoning is persuasive and is fully applicable to the case before us. The rule has the support of the Restatement of Torts, Second (§ 931, Comment *c*) and numerous commentators (11 Blashfield, Automobile Law & Practice [rev 3d ed], § 429.2; Dobbs, Remedies, § 5.11, pp 387-389; 10 Fuchsberg, *op. cit.*, § 878; McCormick, Damages, § 124, pp 470-476; 1 Sedgwick, Damages [9th ed], §§ 195, 243b). Moreover, it has been consistently followed in this department (see *Nicholas v Mellon Constr. Co., supra; Denehy v Pasarella, supra; Dettmar v Burns Bros., 111 Misc 189*, *supra*), in the United States Court of Appeals for the Second Circuit applying New York law (*Koninklijke Luchtvaart Maatschaapij, N.V. v United Technologies Corp., 610 F2d 1052*), [2] and is in accord with the overwhelming weight of authority elsewhere (*Malinson v Black*, 83 Cal Appn 2d 375; *Hillaman v Bray Lines, 41 Col App 493*, affd *Col , 625 P2d 364*; *Graf v Rasmussen Co.*, 399 Ore App 311; *Holmes v Raffo, 60 Wn 2d 421*; **[*667]** Recovery for Loss of Use of Motor Vehicle Damaged or Destroyed, Ann., *18 ALR3d 497*, § 13).

[*9]** For these reasons, the judgment should be reversed insofar as appealed from, with costs, and the

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[1] It is true that the Supreme Court declined to extend the "spare boat" doctrine to a boat acquired and maintained for the general uses of the business, limiting recoverable damages to "the additional wear and tear on the over-worked vessels"(Dobbs, Remedies, § 5.11, p 389). While that result has been criticized (Note, 39 Hary L Rev 760), that portion of the holding is irrelevant to the case now before us as plaintiffs utilized a spare bus and the parties have stipulated the amount of damages incurred as a result of the loss of use.

[2] After this opinion was filed we became aware of ***CIT Int. v Lloyds Underwriters (735 F2d 679***) in which the Second Circuit retreated from this decision on constraint of ***Mountain View Coach Lines v Gehr (80 AD2d 949***), and *Mountain View Coach Lines v Harnett* (999 Misc 2d 271, affd ***69 AD2d 1020***, as amd ***70 AD2d 977***, mot for lv to app den *47 NY2d 710*). As we have previously explained, these decisions are contrary to settled New York authority.

matter remitted to the Supreme Court, Dutchess County, for entry of an appropriate judgment awarding damages for loss of use in accordance with the stipulation.

New York Cent. Mut. Fire Ins. Co. v. 563 Grand Med., P.C.

Supreme Court of New York, Otsego County

August 23, 2004, Decided

9744-03

Reporter

4 Misc. 3d 1020(A) *; 798 N.Y.S.2d 345 **; 2004 N.Y. Misc. LEXIS 1478 ***; 2004 NY Slip Op 50979(U) ****

[**1]** NEW YORK CENTRAL MUTUAL FIRE INSURANCE COMPANY, Plaintiff, v. 563 GRAND MEDICAL, P.C., et al., Defendants.

Notice: [*1]** THIS OPINION IS UNCORRECTED AND WILL NOT BE PUBLISHED IN THE PRINTED OFFICIAL REPORTS.

PUBLISHED IN TABLE FORMAT IN THE NEW YORK SUPPLEMENT.

Disposition: Defendants' motions to dismiss granted and complaint dismissed as against all defendants; Plaintiff's motion for summary judgment seeking dismissal of defendant Eastern Comprehensive Medical Services granted and counterclaim dismissed.

Judges: Hon. William F. O'Brien, III, Justice, Supreme Court.

Opinion by: William F. O'Brien

Opinion

William F. O'Brien, J.

Several motions were presented at the Court's May 14, 2004, motion term for resolution in this dispute between a no-fault insurance provider and ninety-nine (99) professional medical corporations. A number of defendants move pursuant to *CPLR 3211* to dismiss the Complaint for failure to state a cause of action, while other defendants cross-move pursuant to *CPLR 3212* for summary judgment dismissing the Complaint. Plaintiff opposes these motions and filed a cross-motion seeking dismissal of defendant Eastern Comprehensive Medical, P.C.'s counterclaim. June 1, 2004, was set as the date for final submissions by the parties on the motions.

FACTUAL BACKGROUND

Plaintiff is a provider of no-fault automobile liability insurance policies in New York State and defendants are professional corporations (hereinafter "PCs") **[***2]** which were owned and operated by medical doctors. According to the pleadings, from 1998 until mid-2001, defendants rendered treatment to persons covered under no-fault policies issued by plaintiff. The covered insured patients were treated by licensed acupuncturists who were employees of defendant medical corporations. The covered insured patients executed facially-valid assignments of their no-fault benefits to defendant corporations. Defendant corporations submitted bills for the treatment provided by these licensed acupuncturists to plaintiff. Plaintiff paid the bills submitted by defendant corporations.

Plaintiff filed this action on July 10, 2003, alleging that defendants had improperly employed acupuncturists and that, based upon this organizational flaw, were operating illegally and were not entitled to the payments that plaintiffs made during the time period cited in the Complaint. The Complaint demands that defendant corporations refund all payments made by plaintiff for services provided by the licensed acupuncturists. Plaintiffs allege that these payments amount to a total of $ 1,367,272.00. Defendant Eastern Comprehensive Medical Services, P.C., filed a counterclaim with **[***3]** its Answer alleging that it is owed an additional $ 10, 581.50.

RELEVANT LAW/ANALYSIS

This case presents two questions which are currently unsettled in New York law: (1) Whether a medical corporation owned and operated by doctors who do not possess a certificate **[****2]** to practice acupuncture may lawfully employ an acupuncturist and (2) whether a medical corporation which illegally employs a licensed acupuncturist is entitled to reimbursement by insurers for medical services provided to covered persons pursuant to no-fault policies issued by the insurer? There is no precedent directly addressing the first question and, while several lower courts have addressed the second issue, the results are diverging and in need of clarification. [1]

[*4]** Analysis of these motions begins by examining the claims stated in the Complaint, which lists two causes of action against each named defendant: (1) fraud, alleging that defendants knowingly made false representations to plaintiff to induce plaintiff to pay bills for services which defendants were not authorized to provide; and (2) unjust enrichment, alleging that defendants accepted payments from plaintiff that they knew were illegal and yet still retained the proceeds of said payments. The parties agree that there are no disputed facts present in this case and that the issues here may be settled as matters of law.

Corporate Structure Violations

Before analyzing the causes of action stated in the Complaint it is necessary to review the statutory basis for plaintiff's theory of recovery. *Section 1503(a) of the Business Corporation Law* provides that "one or more individuals duly authorized to render the same professional service within the state may organize, or cause to be organized, a professional service corporation for pecuniary profit under this article for the purpose of rendering the same professional service." Under this statute, **[***5]** only professionals licensed to render the same professional services may organize as a corporation and multidisciplinary professional practices are disallowed.

Plaintiff contends that defendant PCs have violated this prohibition against multidisciplinary practices by employing acupuncturists. All of the defendant PCs are organized for the practice of medicine. Acupuncture, according to plaintiff, is a separate discipline that is not subsumed within the practice of medicine. Thus, according to plaintiff, unless at least one shareholder/owner of each of the defendant PCs was certified to practice acupuncture along with being a licensed medical doctor, the defendant PCs could not properly employ an acupuncturist because acupuncture was beyond the scope of the corporation's expertise.

Plaintiff's Cause of Action for Fraud

In order to establish a cause of action for fraud, a plaintiff must allege (1) a misrepresentation of a material fact, (2) falsity, (3) scienter (knowledge of the falsity), (4) reliance upon the false statement and (5) injury. *See Small v. Lorillard Tobacco Co., 94 N.Y.2d 43, 56, 720 N.E.2d 892, 698 N.Y.S.2d 615 (1999)*. In addition, the Complaint must state with specificity **[***6]** the acts which constituted the fraud. *See Kovach v. Hinchey, 276 A.D.2d 942, 714 N.Y.S.2d 791 (3d Dept. 2000)*; *CPLR § 3016(b)*.

Defendants contend that the Complaint here does not plead the fraud cause of action with sufficient specificity. The Complaint states that "defendants intentionally and knowingly made false and fraudulent statements of material facts to (plaintiff), namely that each was lawfully **[****3]** entitled to payment from (plaintiff) for the acupuncture services provided to each said eligible injured person." It goes on to allege that these "fraudulent and false statements" were made "to induce (plaintiff) to pay for the acupuncture services they were not entitled to claim or receive." The Complaint recites that defendants "knowingly concealed material facts from (plaintiff), namely that each defendant wrongfully and illegally employed an acupuncturist . . . in order to bill and receive payment for acupuncture services to which they were not entitled." Finally, the Complaint states that plaintiff justifiably relied upon the misrepresentations of defendant PCs in rendering payment for the acupuncture services performed.

Such allegations contain sufficient **[***7]** detail to place defendants on notice of the acts which are alleged to have constituted the fraud. *See Black v. Chittenden, 69 N.Y.2d 665, 503 N.E.2d 1370, 511 N.Y.S.2d 833 (1986)*. Even without further elaboration, defendant PCs would know from these pleadings that plaintiff is alleging that defendant PCs knowingly misled plaintiff to believe they were entitled to be paid for acupuncture services when such payments were, according to plaintiff, illegal and wrongful. Keeping in mind that the statute is not to be interpreted so strictly as to defeat what might otherwise be a valid claim where some knowledge might be

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[1] The recent decision of the Second Circuit Court of Appeals in *State Farm Insurance v. Mallela, 372 F.3d 500 (2nd Cir. June 18, 2004)* certified the following question to the Court of Appeals: "Is a medical corporation that was fraudulently incorporated under *N.Y. Business Corporation Law §§ 1507*, *1508*, and *N.Y. Education Law § 6507(4)(c)* entitled to be reimbursed by insurers, under *New York Insurance Law § 5101 et seq.* and its implementing regulations, for medical services rendered by licensed medical practitioners?"

peculiarly within the knowledge of the defendant PCs, the present claim is stated in sufficient detail to satisfy CPLR § 3016(b)'s specificity requirement. *See Oxford Health Plans (N.Y.), Inc. V. Bettercare Health Care Pain Management & Rehab PC, 305 A.D.2d 223, 762 N.Y.S.2d 344 (1st Dept. 2003)*.

The theory underlying plaintiff's fraud claim relies upon the premise that defendants were violating BCL § 1503 by employing acupuncturists. Assuming without deciding that plaintiff is correct in this assertion, plaintiff's claim further asserts **[***8]** that it may recover the payments made to defendant PCs based upon this violation of the *Business Corporation Law*. Such a right of recovery is not explicit in the statute and defendants contend that no private right of action exists for any purported violation of *BCL § 1503(a)*. Several reported and unreported decisions support this position. *Allstate Insurance Co. v. Belt Parkway Imaging, P.C.*, Sup. Ct. New York County, March 19, 2004, Moskowitz, J., Index No. 600509/2003; *Oxford Health Plans (N.Y.) Inc. v. Bettercare Health Care Pain Management & Rehab, P.C., supra*; *State Farm Mut. Auto Insurance Co. v. Mallela, 175 F. Supp. 2d 401 (E.D.N.Y. 2001)*, *issue certified to Ct. Of Appeals, 372 F.3d 500 (2nd Cir. 2004)*; *Universal Acupuncture Pain Services, P.C. v. State Farm Mut. Auto Insurance Co., 196 F. Supp. 2d 378, (S.D.N.Y. 2002)*.

Plaintiffs, meanwhile, rely upon several unpublished New York State Supreme Court decisions in asserting that a private right of action does exist. *See, e.g. State Farm Insurance Co. v. North Bronx Medical, P.C.*, Sup. Ct. New York County, January 17, 2002, Wetzel, **[***9]** J., Index No. 117539/01; *Fordham Med. Pain & Treatment. P.C. v. State Farm*, Sup. Ct. New York County, January 4, 2001, Shafer, J., Index No. 600403; *Advanced Care of New York, Inc. v. Friscia*, Sup. Ct. Kings County, Feb. 22, 2002, Hall, J., Index No. 32528/99; *GEICO v. Southern Medical Services, Inc.*, Sup. Ct. New York County Nov. 5, 1993, Ciparick, J., Index No. 118101/93; *Queens Spinal Testing v. GEICO*, Civ. Ct., Queens County, April 4, 1997, Gazzara, J., Index No. 5378/95. [2]

[*10]** **[****4]** These decisions, to the extent that they address the issue at hand, are neither controlling nor particularly persuasive. They contain minimal analysis of the issue and, most importantly, are factually distinguishable from the present case. For example, *State Farm v. North Bronx Medical* involved an insurance company which sought to deny payments for no-fault treatments rendered by a medical PC which was owned by a pathologist and purported to offer physical therapy treatment. That court stated that it chose not to follow *Malella*, making the uncited assertion that *Malella* was "in conflict with the established law in New York State Courts". In *Fordham Med. Pain & Treatment, P.C. v. State Farm*, the plaintiff sought to receive payment from a no-fault insurer for treatment provided. The insurance company denied the payments, alleging it did not have to pay because plaintiff was violating BCL § 1503 because plaintiff's putative owner/sole shareholder was not actually involved in the management of the corporation. The decision stated that the plaintiff's reliance upon the principle that a party may not use a regulatory violation such as a violation **[***11]** of BCL § 1502 as a sword to be misplaced, but then failed to explain why the rule should not be applied.

By contrast, the *Universal Acupuncture* court made substantial analysis of New York law in concluding that the insurer in that case could not recover under a theory of common law fraud for a violation of BCL § 1503 because the statute provides no private right of action for a violation thereof and because the insurer alleged no substantive injury apart from the statutory violation. *Universal Acupuncture Pain Services, P.C. v. State Farm, supra at 387*. It is noteworthy that the charges in *Universal Acupuncture* were more malevolent than those levied in the present case; the PC in that case was owned in name only by an acupuncturist who was all the while splitting fees with a physician who was billing the no-fault insurer for acupuncture services provided. Here, the only dishonesty alleged is plaintiff's contention that defendants knew that a medical corporation could not lawfully employ an acupuncturist unless one of its principals held a certificate in acupuncture, an allegation of dubious merit **[***12]** as discussed below. As such, the lack of a substantive injury to plaintiff directly - not to the covered insured

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[2] Plaintiff also cites several arbitration decisions in support of this position, including *Medical Office of Stony Brook & State Farm Insurance Co.*, AAA Case No. 17-970-22848-98 (June 2001) and *Kew Forest Medical, P.C. & Allstate Insurance Co.*, AAA Case No. 17-991-1553-1 (March 1, 2002). These decisions have no precedential value as they are not determinations of law, *Banc of America Securities v. Knight, 4 Misc.3d 756, 781 N.Y.S.2d 829 (Sup. Ct. New York County, May 19, 2004)*, and because an arbitrator is not bound by substantive law or rules of evidence. *Silverman v. Benmor Coats, Inc., 61 N.Y.2d 299, 461 N.E.2d 1261, 473 N.Y.S.2d 774 (1984)*.

persons or to the public at large - compels adoption of the Universal Acupuncture analysis.

The *Malella* court engaged in an equally lengthy discussion of New York law on the subject. That case dealt with allegations of shell ownership of medical corporations and insurance companies seeking reimbursement for payments that they purported to be illegal based upon improper licensing of the defendant PCs. The court noted that the insurer in that case had "done no more than pay claims it was required to pay by law" and determined that a private right of action was not available to the insurance companies because they were not intended beneficiaries of BCL § 1503 and that a private right of action would not promote the legislative intent of the statute. State Farm Mut. Auto Insurance Co. v. Mallela, supra at 416-17.

The analyses set forth in *Universal Acupuncture* and *Malella* were recently adopted by the Supreme Court of New York County in *Allstate v. Belt Parkway Imaging, P.C.*, *supra*. In that case, insurers sought to **[***13]** recover fees paid to medical PC defendants based upon purported **[****5]** violations of BCL § 1503 involving physicians named as owners of corporations which were, in fact, owned by a layperson without a medical license who owned a medical management company. That court extensively analyzed many of the aforementioned decisions and held the plaintiff insurance companies were not among the class of intended beneficiaries of BCL § 1503 and could not use a purported violation of the statute offensively in seeking to recover for payments already made.

Such analysis is directly applicable to the facts of the present case. Here, plaintiff seeks to recoup payments made to the defendant PCs based solely upon a purported violation of the BCL. It is noteworthy that while the Complaint infers that defendant PCs "knew" that hiring acupuncturists without having a physician certified to practice acupuncture as a corporate shareholder constituted a violation of the Education Law and BCL, plaintiff cannot point to any controlling authority that decisively states such a rule. In fact, the only violation alleged against defendants here is a potentially **[***14]** open question of law that is best resolved by the regulatory agencies which govern this area but have yet to speak definitively on the issue. There are no allegations of deceptive corporate structure as set forth in nearly every other case dealing with this issue. Plaintiff further concedes that the services for which they were billed were actually performed and that they were performed by licensed acupuncturists. Plaintiff's sole basis for relief is to use the alleged violation of BCL § 1503 as a sword, which goes against settled New York decisional law. As noted by the *Malella* court, "the violation at issue here is not evil in itself and plaintiff plainly seeks to use the . . . violations as a sword for personal gain in order to recoup payments that it would, but for the alleged violations of the Business Corporations Law, indisputably have been required to pay." Id. at 419-420.

Since no private right of action exists to recover for a violation of BCL § 1503(a), plaintiff's fraud claim fails to state a cause of action upon which relief may be granted and the cause of action must be dismissed.

Plaintiff's unjust enrichment **[***15]** claim is similarly unavailing. In order to recover under an unjust enrichment theory, a party must prove (1) the defendants were enriched, (2) at plaintiff's expense, and (3) that "it is against equity and good conscience to permit . . . defendant(s) to retain what is sought to be recovered". *Lake Minnewaska Mountain Houses, Inc. v. Rekis, 259 A.D.2d 797, 686 N.Y.S.2d 186 (3d Dept. 1999)*. While plaintiff's submissions likely satisfy the first two elements of the claim, it fails to establish how equity and good conscience require the return of fees paid for services rendered by defendants. Plaintiff advances its public policy concerns in support of this claim as well, but they are no more convincing in the equitable forum. The facts remain that defendants rendered services, billed for those services and were paid for the services rendered. Plaintiff does not allege that the bills submitted did not accurately reflect the services provided, they do not allege that the services provided were substandard or insufficient to meet the needs of the covered insured persons and they do not allege that the amounts sought in the bills were inappropriate for the work performed. Plaintiffs received **[***16]** exactly what they paid for - medical services provided by licensed acupuncturists. Allowing plaintiff to disgorge the fees paid for these services would arguably unjustly enrich plaintiff and, despite plaintiff's stated concern for the public health problems associated with the alleged improper practice of medical doctors employing acupuncturists, public policy mitigates most strongly in favor of proper compensation for services rendered. Furthermore, the practice of forfeiture of payments already rendered is **[****6]** disfavored by New York courts "particularly where a . . . party seeks to raise illegality as a sword for personal gain rather than a shield for public good." State Farm Mut. Auto Insurance Co. v. Mallela, supra at 419, *quoting* Lloyd Capital Corp. v. Pat Henchar, Inc., 80 N.Y.2d 124, 128, 603 N.E.2d

246, 589 N.Y.S.2d 396 (1992). Thus, plaintiff has failed to establish the viability of its unjust enrichment cause of action and that claim must also be dismissed.

Plaintiff's motion for summary judgment dismissing the counterclaim of defendant Eastern Comprehensive Medical Services must be granted. The counterclaim lacks the required specificity to place the Court and parties on notice of **[***17]** the exact nature of the claim. *Willis v. Kepner, 109 A.D.2d 950, 486 N.Y.S.2d 440 (3d Dept. 1985)*. The counterclaim set forth in defendant Eastern Comprehensive Medical's Answer states only that acupuncture services were provided to persons who were covered insureds of plaintiff and that "there remains owing and unpaid for the Services the amount of Ten Thousand Five Hundred Eighty-One Dollars and fifty cents ($ 10,581.50) which is due and owing from Plaintiff to Defendant". These allegations are not sufficient to sustain any cause of action as they fail to specify, among other things, the time period in which these services were provided, whether plaintiff was ever billed for said services and the alleged reasonable value of the services.

Accordingly, for the reasons set forth, both the motions of the defendants seeking dismissal of the Complaint for failure to state a claim and the motions of the defendants seeking summary judgment dismissing the Complaint are granted, and the Complaint is dismissed as against all defendants. Plaintiff's motion for summary judgment seeking dismissal of defendant Eastern Comprehensive Medical Services is granted and the counterclaim is dismissed.

[*18]** This decision shall also constitute the Order of this Court.

Wampsville, N.Y.

Hon. William F. O'Brien, III

Justice, Supreme Court

PAPERS FILED WITH THE OTSEGO COUNTY CLERK:

1. Decision (August ___, 2004) 2. Memorandum of Law of Defendant 563 Grand Medical, P.C. (May 27, 2004) 3. Letter of Ralph A. Erbaio, Jr., Esq. (May 27, 2004) 4. Affirmation of Ralph A. Erbaio, Jr., Esq. (May 11, 2004) 5. Reply Memorandum of Law (May 7, 2004) 6. Reply Affirmation of Brian C. Clark, Esq. (May 7, 2004) 7. Reply Memorandum of Law (March 30, 2004) 8. Affirmation in Opposition of Brian C. Clark, Esq. (March 26, 2004) 9. Reply Memorandum of Law (March 15, 2004) 10. Memorandum of Law (March 12, 2004) 11. Notice of Cross-Motion (March 12, 2004) 12. **[****7]** Affirmation of Brian C. Clark, Esq., in Opposition to Cross-Motion of Queens Medical Services (March 12, 2004) 13. Affirmation of Brian C. Clark, Esq., in Opposition to Cross-Motion of Ocean Spine & Joint Medical, P.C. (March 12, 2004) 14. Affirmation of Brian C. Clark, Esq., in Opposition to Cross-Motion of Hampton Medical (March 12, 2004) 15. Affirmation of Brian C. Clark, Esq., in Opposition to Cross-Motion of Highland Park Medical Care, P.C. (March 12, 2004) 16. Notice of Motion (March 2, 2004) 17. Notice **[***19]** of Cross-Motion (February 27, 2004) 18. Memorandum of Law (February 24, 2004) 19. Notice of Motion (February 23, 2004) 20. Notice of Cross-Motion (February 19, 2004) 21. Notice of Cross-Motion (January 23, 2004) 22. Notice of Motion (January 23, 2004) 23. Memorandum of Law (January 23, 2004) 24. Notice of Cross-Motion (January 21, 2004) 25. Memorandum of Law (December 3, 2003) 26. Affirmation of Roy A. Mura, Esq. (December 2, 2003) 27. Memorandum of Law (November 25, 2003) 28. Notice of Motion (November 25, 2003) 29. Notice of Motion (November 10, 2003) 30. Memorandum of Law (November 10, 2003) 31. Notice of Motion (October 15, 2003) 32. Affirmation of Rudolph C. Gabriel, Esq. (October 15, 2003) 33. 34. **[****8]** 35.

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People v. Gonzales

Supreme Court of New York, Appellate Division, Second Department

August 8, 1983

No Number in Original

Reporter

96 A.D.2d 847 *; 465 N.Y.S.2d 694 **; 1983 N.Y. App. Div. LEXIS 19437 ***

The People of the State of New York, Respondent, v. Heriberto Gonzales, Also Known as Alberto Gonzales, Appellant

Judges: **[***1]** Gibbons, Weinstein and Rubin, JJ., concur. Titone, J. P., dissents and votes to deny the motion for reargument.

Opinion

[*847] **[**694]** Motion by defendant for leave to reargue the appeal resulting in an order of this court dated March 7, 1983 (*92 AD2d 873*), which reversed a judgment of the Supreme Court, Kings County (Bernstein, J.), rendered August 30, 1979, convicting him of manslaughter in the first degree and criminal possession of a weapon in the second degree, upon a jury verdict, and ordered a new trial. Motion granted and, upon reargument, the decretal paragraph of our decision and order both dated March 7, 1983 is deleted and the following is substituted therefor: "Judgment reversed, on the law and as a matter of discretion in the interest of justice, and new trial ordered on the present indictment solely with respect to the count of criminal possession of a weapon in the second degree, and indictment otherwise dismissed without prejudice **[**695]** to the People to re-present any appropriate charges to another Grand Jury (see *People v Beslanovics, 57 NY2d 726*)."

Dissent by: TITONE

Dissent

Titone, J.P., dissents and votes to deny the motion for reargument, with the **[***2]** following memorandum:

Defendant was charged in a multicount indictment with, *inter alia*, murder in the second degree and criminal possession of a weapon in the second degree. At trial, he was convicted of manslaughter in the first degree, which was submitted to the jurors as a lesser included offense of the murder count (CPL 300.50, subd 1), and criminal possession of a weapon in the second degree. By decision and order of this court, both dated March 7, 1983 (*92 AD2d 873*) the judgment was reversed and a new trial ordered. On this motion, defendant contends that, because he was convicted of a lesser included offense not contained in the original indictment, he may not be retried for manslaughter under the present accusatory instrument. I disagree. Defendant's conviction was reversed as a result of what this court perceived to be error occurring during the course of his trial. Pursuant to CPL 470.20 (subd 1), in such circumstances, this court "*must* * * * order a new trial of the accusatory instrument and remit the case to the criminal court for such action" (emphasis supplied; see People v Allen, 39 NY2d 916). Upon such retrial, the accusatory instrument contains **[***3]** all of its original counts and charges *except* those on which the defendant "was acquitted or deemed to have been acquitted" (CPL 470.55, subd 1). [1] By operation of law, the count of the indictment charging murder in the second degree is considered to encompass every lesser included offense as well (People ex rel. Colcloughley v Montanye, 49 AD2d 1034, 1035; **[*848]** see, e.g., People v Pawley, 71 AD2d 307, 312; People v Leichtweis, 59 AD2d 383, 387). Inasmuch as the jury verdict convicting the defendant of the lesser included offense of manslaughter in the first degree is regarded as an implied acquittal of the greater count of murder (CPL 300.40, subd 3, par [b]; see People v Ressler, 17 NY2d 174), the indictment by virtue of CPL 470.55, is deemed to now contain only the manslaughter charge on that count (People v Moorehead, 82 Misc 2d 1064,

[1] This is a stark contrast to CPL 310.60 (subd 2), construed in People v Mayo (48 NY2d 245, 248, n 1), which provides that a defendant may be retried following the declaration of a mistrial with *all* counts contained in the indictment reinstated, including those dismissed during trial for evidentiary insufficiency. In other words, that section lacks an excising provision like CPL 470.55.

1071). There is no need to dismiss the present accusatory instrument and require the People to recommence Grand Jury proceedings from scratch (see People v Graham, 36 NY2d 633; People v Moorehead, supra). Prior to retrial, the People may apply to amend the indictment, pursuant to CPL 200.70, to delete the **[***4]** charge of murder in the second degree and substitute a charge of manslaughter in the first degree. Indeed, an amendment is a ministerial act (People v Moorehead, supra) as, by definition, the submission of a lesser included offense must be consistent with the theory of the People's case as presented to the Grand Jury (see People v Glover, 57 NY2d 61, 64). This standard procedure has been followed by the trial courts (People v Moorehead, supra) and has received the implicit approval of the Court of Appeals in *People v Graham* (*supra*). Surely, there is no constitutional proscription against it (see People ex rel. Prince v Brophy, 273 NY 90, 98-99; Mildwoff v Cunningham, 432 F Supp 814, 817; see, generally, Indictment-Amendment-Circumstances, Ann., 17 ALR3d 1285). Appellate courts have been recently admonished to take into account the concerns of victims and witnesses prior to directing further judicial proceedings in **[**696]** criminal cases (*United States v Hasting*, 461 U.S. , 33 Crim L Rptr 3091, 3093; *Morris v Slappy*, 461 U.S. , 75 L ed 2d 610, 621-622). A second presentment to the Grand Jury will require an additional appearance **[***5]** of witnesses for no substantive purpose. The time, expenditure and effort placed on these individuals, as well as on the judicial system itself, is not counterbalanced by any meaningful protection to the accused. I do not view *People v Beslanovics (57 NY2d 726*), a brief memorandum decision made on review of submissions pursuant to rule 500.2 (b) of the Rules of the Court of Appeals (*22 NYCRR 500.2 [g]*) as overriding the corrective action dictated by the express provisions of the CPL. *Beslanovics* (*supra*) offered no explanation for the radical departure from established New York law (see Pitler, NY Criminal Practice Under the CPL, §§ 14.46, 14.48). [2] As the Court of Appeals itself has observed, cases in which the corrective action undertaken deviates from that specified by the CPL do not constitute a precedent for such a procedural disposition in the future if the applicable CPL provisions are neither cited nor discussed and no "supporting rationale for the unusual result" is offered (People v Allen, 39 NY2d 916, 918, *supra*; see, also, People v Rickert, 58 NY2d 122, 133, n 4; cf. People v Hobson, 39 NY2d 479, 490 ["a precedent is less binding if it is **[***6]** little more than an ipse dixit, a conclusory assertion of result, perhaps supported by no more than generalized platitudes"]). At best, *Beslanovics* (*supra*) is an "errant footprint barely hardened overnight" which we are cautious not to treat "as an inescapable mold for future travel" (People v Hobson, supra, p 488). Thus, unless CPL 470.25 (subd 1) is unconstitutional -- and I perceive no basis to conclude that it is -- we are obligated to follow its mandate. In any **[*849]** event, as an intermediate appellate court we have an obligation to bring this question to the attention of the Court of Appeals so that it can clarify, or correct, a perceived error (see Hopkins, The Role of Intermediate Appellate Court, 41 Brooklyn L Rev 459). Therefore, as in People v Santiago (51 AD2d 1, 7, revd *40 NY2d 990*, cert den *sub nom. New York v Luis J., 431 U.S. 908*), I invite the People to make an application for permission to appeal to the Court of Appeals. Although our reversal is not predicated on the law alone, an appeal to the Court of Appeals could still be taken by the People on the ground that the corrective action we have directed is illegal (CPL 450.90, subd 2, **[***7]** par [b]; see People v Mackell, 40 NY2d 59, 61-62; People v Crimmins, 36 NY2d 230, 236).

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[2] People v Villani (59 NY2d 781) was decided in the same procedural manner as ***People v Beslanovics (57 NY2d 726***) again without explanation. On the other hand, in People v Zaborski (59 NY2d 863), a new trial on the lesser included charge was directed.

To the extent that this court may have followed an inconsistent course in decisions in which I have concurred, I find myself in the same circumstances as Justice Jackson in McGrath v Kristensen (340 U.S. 162, 178 [Jackson, J., concurring]) and invoke all the "ways of gracefully and good-naturedly surrendering former views to a better considered position".

People v. Hobson

Court of Appeals of New York

February 20, 1976, Argued ; May 4, 1976, Decided

No Number in Original

Reporter

39 N.Y.2d 479 *; 348 N.E.2d 894 **; 384 N.Y.S.2d 419 ***; 1976 N.Y. LEXIS 2673 ****

The People of the State of New York, Respondent, v. Henry Cornelius Hobson, Appellant

Prior History: [**1]** *People v Hobson, 47 AD2d 716.*

Appeal, by permission of an Associate Judge of the Court of Appeals, from an order of the Appellate Division of the Supreme Court in the Second Judicial Department, entered February 24, 1975, which affirmed a judgment of the Suffolk County Court (Ernest L. Signorelli, J.), convicting defendant, upon his plea of guilty, of robbery in the third degree.

Disposition: Order reversed, etc.

Counsel: *Gerald J. Callahan, John F. Middlemiss, Jr.*, and *Leon J. Kesner* for appellant. I. The People violated the constitutional rights of appellant in questioning him without his attorney being present. *(People v Arthur, 22 NY2d 325*; **[****4]** *People v Vella, 21 NY2d 249*; *People v Donovan, 13 NY2d 148*.) II. The trial court had insufficient evidence presented to determine that appellant waived his constitutional rights. *(Blyden v Hogan, 320 F Supp 513*; *Inmates of Attica Correctional Facility v Rockefeller, 453 F2d 12*; *People v Horowitz, 21 NY2d 55*; *People v Custis, 32 AD2d 966*.)

Henry F. O'Brien, District Attorney (Charles M. Newell of counsel), for respondent. I. Appellant's confession was not rendered inadmissible by the fact that it was made in the absence of his attorney. *(People v Huntley, 15 NY2d 72*; *People v Valerius, 31 NY2d 51*; *People v Leonti, 18 NY2d 384, 19 NY2d 922, 389 U.S. 1007*; *Blackburn v Alabama, 361 U.S. 199*; *People v Stephen J. B., 23 NY2d 611*; *People v Chaffee, 42 AD2d 172*; *People v Paulin, 25 NY2d 445*; *People v Arthur, 22 NY2d 325*; *People v Gunner, 15 NY2d 226*; *People v McIntyre, 31 AD2d 964, 41 AD2d 776, 36 NY2d 10*.) II. The record contains ample evidence that appellant freely and knowingly waived his constitutional rights and made a voluntary confession. *(Blyden v Hogan, 320 F Supp 513*; *Miranda v Arizona, 384 U.S. 436*; **[****5]** *People v Cerrato, 24 NY2d 1, 397 U.S. 940*; *People v Huntley, 15 NY2d 72*; *People v Fairley, 32 AD2d 976*; *Johnson v Zerbst, 304 U.S. 458*; *People v Jennings, 40 AD2d 357, 33 NY2d 880*; *United States ex rel. Stephen J. B. v Shelly, 430 F2d 215*; *People v Tanner, 30 NY2d 102*; *People v Anthony, 24 NY2d 696*.)

Judges: Judges Jones, Wachtler, Fuchsberg and Cooke concur with Chief Judge Breitel; Judge Jasen concurs in a separate opinion; Judge Gabrielli concurs in result in another separate opinion.

Opinion by: BREITEL

Opinion

[*481] [896] [***420]** Defendant, following denial of a motion to suppress his incriminating statements, was convicted, after a guilty plea, of third degree robbery (*Penal Law, § 160.05*). He was sentenced to seven years' imprisonment. His conviction was affirmed, and he appeals.

The issue is whether a defendant in custody, represented by a lawyer in connection with criminal charges under investigation, may validly, in the absence of the lawyer, waive his right to counsel.

There should be a reversal. Once a lawyer has entered a criminal proceeding representing a defendant in connection with criminal charges under investigation, the **[****6]** defendant in custody may not waive his right to counsel in the absence of the lawyer *(People v Arthur, 22 NY2d 325, 329)*. Any statements elicited by an agent of the State, however subtly, after a purported "waiver" obtained without the presence or assistance of counsel, are inadmissible. Since the purported "waiver" of defendant's right to counsel was obtained in the absence of his lawyer, who had represented him at a just-completed lineup in connection with the criminal charges, his **[*482]** statements were inadmissible and should have been suppressed.

The facts are undisputed. On February 7, 1973, at approximately 8:30 p.m., defendant entered a delicatessen in Central Islip in Suffolk County. After asking for directions from the owner, George Gundlach, defendant drew a gun and demanded all the cash in the register. After he had received the cash and a number of packages of cigarettes, defendant left.

When the police arrived shortly thereafter, Mr. Gundlach described the robber to Suffolk County Detective Dolan. He then accompanied the detective to the police station, where he eventually identified photographs of defendant as those of the culprit. Mr. Gundlach did state, **[****7]** however, that to be **[***421]** positive he would have to see defendant in person.

Nine months later, on September 26, 1973, defendant was being held in the Suffolk County Jail on charges unrelated to the delicatessen robbery. He was not under arrest for the robbery at that time, although he was a photograph-identified suspect. Defendant was placed in a five-man lineup. Because defendant had requested counsel, Samuel McElroy, a Legal Aid lawyer, was assigned and present to represent him. Mr. Gundlach identified defendant as the robber. Mr. McElroy then left.

After Mr. McElroy left, a Sheriff's deputy asked Detective Dolan if he desired to speak to defendant. Despite his admitted knowledge that defendant was now represented by counsel on the robbery charge, Dolan replied that he would. The detective had not told Mr. McElroy that he was going to speak to defendant, nor did he make any effort to reach counsel before seeing defendant. At the deputy's request, defendant signed an undescribed form of "waiver" (which Dolan testified he had never seen) and agreed to speak to Dolan. Defendant was then brought to an "interview" room in the jailhouse.

Detective Dolan read to defendant **[****8]** the standard preinterrogation warnings and asked him if he understood. Defendant said that he did. The detective then asked defendant "Do you wish to contact a **[**897]** lawyer?" Defendant shook his head, indicating "No". The detective then asked "Having these rights in mind, do you wish to talk to me now without a lawyer?" Defendant replied "Yes".

Defendant then inquired of Dolan whether he had been identified by Mr. Gundlach, and the detective told him that he **[*483]** had. Expressing a desire to "clear up everything", defendant in effect confessed to the robbery.

In *People v Arthur (22 NY2d 325, 329*, *supra)*, the court held: "Once an attorney enters the proceeding, the police may not question the defendant in the absence of counsel unless there is an affirmative waiver, in the presence of the attorney, of the defendant's right to counsel *(* People v. Vella, 21 N Y 2d 249). There is no requirement that the attorney or the defendant request the police to respect this right of the defendant." The rule of the *Arthur* case has been restated many times (see People v Hetherington, 27 NY2d 242, 244-245; People v Paulin, 25 NY2d 445, 450; People v McKie **[****9]** , 25 NY2d 19, 26; People v Miles, 23 NY2d 527, 542, cert den *395 U.S. 948*; cf. *People v Stephen J. B., 23 NY2d 611, 616)*.

This unequivocal and reiterated statement of the law in this State is no mere "dogmatic claim" or "theoretical statement of the rule" (see, contra, People v Robles, 27 NY2d 155, 158, cert den *401 U.S. 945*, thus characterizing the rule). It is, instead, a rule grounded in this State's constitutional and statutory guarantees of the privilege against self incrimination, the right to the assistance of counsel, and due process of law (see People v Arthur, 22 NY2d 325, 328, *supra;* People v Failla, 14 NY2d 178, 180; People v Donovan, 13 NY2d 148, 151; Richardson, Evidence [10th ed], § 545, at p 546). Indeed, the rule resisted narrow classification of defendants entitled to its protection; it is applicable to a defendant when taken into custody, whether as an "accused", a "suspect", or a "witness" (cf. *People v Sanchez, 15 NY2d 387, 389)*.

Of course, as with all verbalizations of constitutional principles, the rule of **[***422]** the *Arthur* case *(supra)* is not an absolute. Thus, the fact that a defendant is represented by counsel **[****10]** in a proceeding unrelated to the charges under investigation is not sufficient to invoke the rule (see People v Hetherington, 27 NY2d 242, 245, *supra;* *People v Taylor, 27 NY2d 327, 331-332)*. The rule applies only to a defendant who is in custody; it does not apply to noncustodial interrogation *(* People v McKie, 25 NY2d 19, 28, *supra)*. Moreover, the rule of the *Arthur* case *(supra)* does not render inadmissible a defendant's spontaneously volunteered statement *(* People v Kaye, 25 NY2d 139, 144; cf. People v Robles, 27 NY2d 155, 159, cert den *401 U.S. 945*, *supra)*.

The *Donovan* and *Arthur* cases *(supra)* extended constitutional protections of a defendant under the State Constitution **[*484]** beyond those afforded by the Federal Constitution (compare People v Arthur, 22 NY2d 325, 329, *supra*; and People v Donovan, 13 NY2d

148, 151, *supra*; with *Miranda [**898] v Arizona, 384 U.S. 436, 475*; and *Escobedo v Illinois, 378 U.S. 478, 486-487*; see Richardson, Evidence [10th ed], *op. cit*., at pp 548-549; but cf., e.g., *Massiah v United States, 377 U.S. 201, 205-206*; *United States v Thomas, 474 F2d 110, 112*, **[****11]** cert den *412 U.S. 932*; *United States ex rel. Lopez v Zelker, 344 F Supp 1050, 1054*, affd *465 F2d 1405*, cert den *409 U.S. 1049*, dealing with the right to counsel after the commencement of adversary judicial proceedings).

Notwithstanding that warnings alone might suffice to protect the privilege against self incrimination, the presence of counsel is a more effective safeguard against an involuntary waiver of counsel than a mere written or oral warning in the absence of counsel (see *United States v Massimo, 432 F2d 324, 327* [Friendly, J., dissenting], cert den *400 U.S. 1022*; compare ALI, Model Code of Pre-Arraignment Procedure [Tent Draft No. 6, 1974], § 140.8, subd [2]; *Miranda v Arizona, 384 U.S. 436, 475*, *supra)*. The rule that once a lawyer has entered the proceedings in connection with the charges under investigation, a person in custody may validly waive the assistance of counsel only in the presence of a lawyer breathes life into the requirement that a waiver of a constitutional right must be competent, intelligent and voluntary (see *People v Witenski, 15 NY2d 392, 395*; *Matter of Bojinoff v People, 299 NY 145, 151-152*; *Johnson v Zerbst, 304 [****12] U.S. 458, 464)*. Indeed, it may be said that a right too easily waived is no right at all.

Moreover, an attempt to secure a waiver of the right of counsel in a criminal proceeding in the absence of a lawyer, already retained or assigned, would constitute a breach of professional ethics, as it would be in the least-consequential civil matter (see ABA Code of Professional Responsibility, DR7-104, subd [A], par [1]; *People v Robles, 27 NY2d 155, 162* [Fuld, Ch. J., dissenting], cert den *401 U.S. 945*, *supra; United States v Thomas, 474 F2d 110, 111-112*, cert den *412 U.S. 932*, *supra; United States v Springer, 460 F2d 1344, 1355* [Stevens, J., dissenting], cert den *409 U.S. 873*; *United States v Durham, 475 F2d 208, 211* [Swygert, Ch. J.]; *Coughlan v United States, 391 F2d 371, 376* [Hamley, J., dissenting], cert den *393 U.S. 870*; Drinker, Legal Ethics, p 202; Broeder, *Wong Sun v United States*: A Study in **[***423]** Faith and Hope, 42 Neb L Rev 483, 601; cf. *People v Lopez, 28 NY2d 23, 29* [dissenting opn], cert **[*485]** den *404 U.S. 840*). Since the Code of Professional Responsibility is applicable, it would be grossly incongruous for the courts to **[****13]** blink its violation in a criminal matter.

Of course, it would not be rational, logical, moral, or realistic to make any distinction between a lawyer acting for the State who violates the ethic directly and one who indirectly uses the admissions improperly obtained by a police officer, who is the badged and uniformed representative of the State. To do so would be, in the most offensive way, to permit that to be done indirectly what is not permitted directly. Indeed, in each of the cases cited above the rejected "waiver" was secured by investigators and not by lawyers.

Moreover, the principle is not so much, important as that is, to preserve the civilized decencies, but to protect the individual, often ignorant and uneducated, and always in fear, when faced with the coercive police power of the State. The right to **[**899]** the continued advice of a lawyer, already retained or assigned, is his real protection against an abuse of power by the organized State. It is more important than the preinterrogation warnings given to defendants in custody. These warnings often provide only a feeble opportunity to obtain a lawyer, because the suspect or accused is required to determine his **[****14]** need, unadvised by anyone who has his interests at heart. The danger is not only the risk of unwise waivers of the privilege against self incrimination and of the right to counsel, but the more significant risk of inaccurate, sometimes false, and inevitably incomplete descriptions of the events described. Surely, the need for and right to a lawyer at an identification lineup is insignificant compared to the need in an ensuing interrogation. If Dick the Butcher said, "The first thing we do, let's kill all the lawyers", the more zealous policeman in the station or jailhouse may well say, "The first thing we do, let's get rid of all the lawyers" (Shakespeare, Henry VI, pt II, act IV, sc ii).

The rule to be applied in this case would be evident, unquestionably evident, on the basis of what has been discussed thus far, but for one significant circumstance. Between September, 1970 and September, 1972 three cases were decided in this court which departed from the evident rule. The reasons for the departure were never made explicit, but nice distinctions were used, if the fact of departure was mentioned at all. On the other hand, the line of cases out of which the *Arthur* case **[****15]** *(supra)* arose, as well as the *Arthur* case itself, was an elaborated legal development, consciously evolved as **[*486]** such, stretching back at least to 1960 (see *People v Di Biasi, 7 NY2d 544*; and *People v Spano, 4 NY2d 256, 264-267* [Desmond J., dissenting], revd *360 U.S. 315*). It was not a string of happenstances (see *People v Lopez, 28 NY2d 23, 26-28* [dissenting opn], cert den *404 U.S. 840*, *supra*, for a detailed analysis of the development of the right to counsel in this State; but see, in contrast, *People v Robles, 27 NY2d 155, 158-160*, cert den *401 U.S. 945*, *supra)*. The three cases were *People v Robles (supra)*; *People v Lopez (28 NY2d 23*, cert den *404 U.S. 840*, *supra)*, and *People v Wooden (31 NY2d 753*). The *Wooden* case simply relied on the *Lopez* case, without opinion, three Judges concurring on constraint of the *Lopez* case. The *Robles* case involved an egregiously brutal and unnatural double murder. The *Lopez* case also involved a murder. That is perhaps the best that one can speculate about what moved the court, reminiscent of the adage about the influence of "hard cases".

[*424]** In the *Robles* **[****16]** case (p 158), the *Arthur* rule was discussed as "merely a theoretical statement" and it was said that "this dogmatic claim is not the New York law" citing *People v Kaye (25 NY2d 139*, *supra)* and *People v McKie (25 NY2d 19*, *supra)*, cases which applied as exceptions to the right to counsel doctrine spontaneous statements and noncustodial interrogation. There was further discussion of cases quite beside the issue, turning on coercion, trickery, and the like, as conditions which would require exclusion of interrogations of uncounseled defendants.

Actually the stability of these odd cases has already been undermined, albeit collaterally. The hapless Lopez, defeated in the State courts, went to the Federal courts. There the District Court in an extensive opinion by Judge Marvin Frankel granted habeas corpus relief, adopting the reasoning of the dissenters in the State court as **[**900]** a statement of Federal constitutional principles *(United States ex rel. Lopez v Zelker, 344 F Supp 1050, 1054*, *supra)*. The Court of Appeals for the Second Circuit affirmed unanimously from the Bench, without opinion (*465 F2d 1405*, cert den *409 U.S. 1049*). (See, also, *People* ***[****17]*** *v Santos, 85 Misc 2d 602, 608* [NYLJ, March 24, 1976, at p 8, col 6], declining to follow the *Lopez* case, *supra.)* As for the *Robles* case *(supra)*, the Richardson treatise is unsure of its effect on the *Arthur* line of cases (Richardson, Evidence [10th ed], *op. cit.*, at pp 547-548, listing five unanswered questions). Nor were the distinguished Justices in the Appellate Division for the Fourth Department able to agree (see *People v Pellicano,* ***[*487]*** *40 AD2d 169* [opn by Mr. Justice Del Vecchio and dissenting opn by Mr. Justice Cardamone]).

The problem this departure from a deliberately elaborated line of cases raises is: What is required of a stable court in applying the eminently desirable and essential doctrine of *stare decisis*. Which is the *stare decisis*: The odd cases or the line of development never fully criticized or rejected?

Frankfurter, a stalwart for stability and systemic values in a jurisprudence, and no evanescent impulsive innovator, answered the question rather succinctly. In *Helvering v Hallock (309 U.S. 106, 119)* he said: "We recognize that *stare decisis* embodies an important social policy. It represents an **[****18]** element of continuity in law, and is rooted in the psychologic need to satisfy reasonable expectations. But *stare decisis* is a principle of policy and not a mechanical formula of adherence to the latest decision, however recent and questionable, when such adherence involves collision with a prior doctrine more embracing in its scope, intrinsically sounder, and verified by experience."

The *Di Biasi-Arthur* line of cases, stretching over almost two decades, represents "a prior doctrine more embracing in its scope, intrinsically sounder, and verified by experience". The three odd cases of uncertain root, present recency in time, but surely are in collision with the "prior doctrine", and in each instance decided by the closest possible margin in the court. They do not merit application of "a mechanical formula of adherence", just because of their recency.

Stare decisis, if it is to be more than shibboleth, requires more subtle analysis. Indeed, the true doctrine by its own vitality should not, perversely, give to its violation strength and stability. That would be like the parricide receiving mercy because he is an orphan. The odd cases rode roughshod over *stare decisis* **[****19]** and now would be accorded *stare decisis* as their legitimate right, whether or not they express sound, good, or acceptable doctrine.

There are many thinkers in the law whose comments on *stare decisis* bear directly on the problem in this case. Invariably, the concern is with the exercise of restraint in overturning established well-developed doctrine and, on the other hand, the justifiable rejection of archaic and obsolete **[***425]** doctrine which has lost its touch with reality (see, e.g., *Heyert v Orange & Rockland Utilities, 17 NY2d 352, 360-361* [Van Voorhis, J.], and cases and materials cited). But one comment **[*488]** by Mr. Justice Von Moschzisker, as long ago as 1924, is especially useful. He said: "From the very nature of law and its function in society, the elements of certainty, stability, equality, and knowability are necessary to its success, but reason and the power to advance justice must always be its chief essentials; and the principal cause for standing by precedent is not to be found in the inherent probable virtue of a judicial decision, it 'is to be drawn from a consideration of the nature and object of law itself, considered as a system or **[****20]** a science'." (Von Moschzisker, Stare Decisis in Courts of Last Resort, 37 Harv L Rev 409, 414.)

[901]** The nub of the matter is that *stare decisis* does not spring full-grown from a "precedent" but from precedents which reflect principle and doctrine rationally evolved. Of course, it would be foolhardy not to recognize that there is potential for jurisprudential scandal in a court which decides one way one day and another way the next; but it is just as scandalous to treat every errant footprint barely hardened overnight as an inescapable mold for future travel.

While this case involves a narrow issue of the right to counsel in a criminal matter, it necessarily turns on what appears to be binding precedent, and hence, the doctrine of *stare decisis*. It is not sufficient to limit the discussion of the doctrine to its application to this case. There is the danger, otherwise, of a misunderstanding of the doctrine's role in the larger perspective in which this case is but an isolated instance. Indeed, this case is another example in which a treatment of the particular requires treatment of the universal under which it falls.

Distinctions in the application and withholding **[****21]** of *stare decisis* require a nice delicacy and judicial self-restraint. At the root of the techniques must be a humbling assumption, often true, that no particular court as it is then constituted possesses a wisdom surpassing that of its predecessors. Without this assumption there is jurisprudential anarchy. There are standards for the application or withholding of *stare decisis*, the ignoring of which may produce just that anarchy.

For one, in this case the court deals with constitutional limitations contained in the Bill of Rights. Legislative correction is confined. Although the limitations are designed to protect the individual against the encroachments of a transitory majority, the principle is well established that in cases interpreting the Constitution courts will, nevertheless, if convinced **[*489]** of prior error, correct the error (see, e.g., Glidden Co. v Zdanok, 370 U.S. 530, 543; Smith v Allwright, 321 U.S. 649, 665-666; Burnet v Coronado Oil & Gas Co., 285 U.S. 393, 406-407 [Brandeis, J., dissenting]; Von Moschzisker, 37 Harv L Rev 407, 420-421). But the conviction of error must be imperative.

Tort cases, but especially personal injury cases, **[****22]** offer another example where courts will, if necessary, more readily re-examine established precedent to achieve the ends of justice in a more modern context (see, e.g., Victorson v Bock Laundry Mach. Co., 37 NY2d 395; Goldberg v Kollsman Instrument Corp., 12 NY2d 432; Bing v Thunig, 2 NY2d 656; Woods v Lancet, 303 NY 349). Significantly, in these cases the line of precedent, although well established, was found to be analytically unacceptable, and, more important, out of step with the times and the reasonable expectations of members of society.

Always critical to justifying adherence to precedent is the requirement that those who engage in transactions based on the **[***426]** prevailing law be able to rely on its stability. This is especially true in cases involving property rights, contractual rights, and property dispositions, whether by grant or testament (see, e.g., United States v Title Ins. Co., 265 U.S. 472, 486-487; Heyert v Orange & Rockland Utilities, 17 NY2d 352, 360, 362-363, *supra* [property rights]; United States v Flannery, 268 U.S. 98, 105 [commercial transactions]; Matter of Eckart, 39 NY2d 493, decided herewith; Douglas, **[****23]** Stare Decisis, 49 Col L Rev 735-736 [wills]; cf. Endresz v Friedberg, 24 NY2d 478, 488-489 [wrongful death **[**902]** action under EPTL 5-4.1]; Matter of Brown, 362 Mich 47, 52 [statute pertaining to the descent and distribution of property]). The absence of such factors, on the other hand, makes easier the reassessment of aberrational departures from precedents and accepted principles.

Precedents involving statutory interpretation are entitled to great stability (Matter of Schinasi, 277 NY 252, 265-266; see 20 Am Jur 2d, Courts, § 198). After all, in such cases courts are interpreting legislative intention and a sequential contradiction is a grossly aggrogated legislative power. Moreover, if the precedent or precedents have "misinterpreted" the legislative intention, the Legislature's competency to correct the "misinterpretation" is readily at hand. (See, e.g., People v Butts, 32 NY2d 946, 947; People v Cicale, 35 NY2d 661, 662, concurred in on constraint and decided on authority of People v Carter, 31 NY2d 964.)

There is a more rarely recognized principle, a sort of exception **[*490]** to the general rule about the interpretation of statutes **[****24]** by courts. There are statutes drawn in such general terms that it is evident that the legislative intention is that the courts, by their interpretation, indeed construction, fill in, by a case-by-case approach, the skeletal outlines. Those are statutes which apply general and therefore flexible standards. The classic example is that of the antitrust statutes, Federal and State, which apply "rules of reason". In such cases the degree of flexibility in handling statutory precedents is that much the greater, but still not unlimited. (See Breitel, The Lawmakers, 65 Col L Rev 749, 761.)

There are obviously other principles that do not now come to mind but most likely would share the rationale of those already discussed. Throughout, however, a precedent is less binding if it is little more than an ipse dixit, a conclusory assertion of result, perhaps supported by no more than generalized platitudes. On the contrary, a precedent is entitled to initial respect, however wrong it may seem to the present viewer, if it is the result of a reasoned and painstaking analysis. Indeed, that constitutes one of the bases for treating the *Robles* and *Lopez* cases as overruled in principle, **[****25]** just because they did not satisfy the rational test when compared to the line of reasoned and consciously developed cases which a bare majority in the *Lopez* and *Robles* cases found unsatisfactory.

The closeness of a vote in a precedential case is hardly determinative *(* *Semanchuck v Fifth Ave. & 37th St. Corp., 290 NY 412, 420*; see 21 CJS, Courts, § 189, at p 307). It certainly should not be. Otherwise, every precedent decided by a bare majority is a nonprecedent -- one to be followed if a later court likes it, and not to be followed if it does not like it. In the *Semanchuck* case, Chief Judge Lehman stated the rule precisely: "Three judges, including the writer of this opinion, dissented from the decision in the earlier case, insofar as it held that the general contractor was not, under the contract, entitled to indemnity from the subcontractor. The controversy over the applicable rule to be followed in the construction of **[***427]** the indemnity agreement has been resolved by that decision. The authoritative force of a decision as a precedent in succeeding cases is not determined by the unanimity or division in the court. The controversy settled by a decision **[****26]** in which a majority concur should not be renewed without sound reasons, not existing here. All the judges of the court accept the **[*491]** decision in the *Walters* case *[Walters v Rao Elec. Equip. Co., 289 NY 57]* and the rules which form the basis for that decision as guides in analogous cases."

[903]** Similarly, the accident of a change of personalities in the Judges of a court is a shallow basis for jurisprudential evolution *(Simpson v Loehmann, 21 NY2d 305, 314* [concurring opn]; see *Minichiello v Rosenberg, 410 F2d 106, 109* [Friendly, J.], cert den *396 U.S. 844*). In the *Simpson* case, the troublesome precedent was all but mint-new; its symmetrical conformance to prior law was facially absent. Nevertheless, the precedent was followed just because it would have been scandalous for a court to shift within less than two years because of the replacement of one of the majority in the old court by one who now intellectually would have preferred to have voted with the old minority and the new one.

The ultimate principle is that a court is an institution and not merely a collection of individuals; just as a higher court commands superiority over a lower **[****27]** not because it is wiser or better but because it is institutionally higher. This is what is meant, in part, as the rule of law and not of men.

Accordingly, the order of the Appellate Division should be reversed, the plea vacated, and the statements of defendant suppressed.

Concur by: JASEN; GABRIELLI

Concur

Jasen, J. (concurring). Convinced as I am that the reasoning which prompted the holdings in the *Robles* and *Lopez* cases has failed to produce a stable and recognized rule, I concur in the majority opinion and particularly for the respect it accords to the doctrine of *stare decisis* and the limited exceptions which it would allow.

Gabrielli, J. (concurring). I concur in the result reached by the majority. In doing so, however, I am unable to join in overruling *People v Lopez (28 NY2d 23)*. I would adhere to the established view that, until counsel is assigned or retained by a defendant in a criminal action, he is perfectly free, after suitable and proper admonitions, to waive his right to the presence and assistance of counsel and make voluntary statements *(* *People v Bodie, 16 NY2d 275*; cf. *People v Meyer, 11 NY2d 162, 165)*. It is always the task of the courts, **[****28]** of course, to assure that such a waiver is knowingly and intelligently made and that statements following a waiver are voluntarily given.

We succinctly stated in *People v Bodie* (*supra, p 279*) that **[*492]** "since the right to counsel also imports the right to refuse counsel, we hold that a defendant may effectively waive his right to an attorney." This holding is qualified, of course, in the situation where counsel has been assigned or retained in which case we have held that a defendant may not be interrogated without the presence or consent of counsel *(* People v Arthur, 22 NY2d 325; People v Vella, 21 NY2d 249; People v Donovan, 13 NY2d 148). Under the circumstances of the instant case, it is this rule which is applicable as the majority ably demonstrates. To reach the result in the case before us, it is unnecessary to consider People v Lopez (supra). As noted in the majority opinion, defendant Hobson was represented by counsel at the time of the interrogation, while, in *Lopez*, the defendant decided to forego representation by counsel.

[*428]** While the rule in the Federal courts may be unsettled, several of them have recognized the admissibility **[****29]** of postindictment statements made after a waiver of right to counsel. Thus, in United States ex rel. O'Connor v State of New Jersey (405 F2d 632, 636) the Third Circuit Court of Appeals, focusing on the quality of the waiver, stated that "only a clear, explicit, and **[**904]** intelligent waiver may legitimate interrogation without counsel following indictment" (see, also, United States v Crisp, 435 F2d 354, 358-359. And, in United States v Garcia (377 F2d 321, 324, cert den *389 U.S. 991*), the Second Circuit indicated that"*Massiah [v* United States, 377 U.S. 201] does not immunize a defendant from normal investigation techniques after indictment".

In the landmark decision of Massiah v United States (377 U.S. 201, 206, *supra)*, the United States Supreme Court held that the defendant "was denied the basic protections of that guarantee [Sixth Amendment right to counsel] when there was used against him at his trial evidence of his own incriminating words, which federal agents had deliberately elicited from him after he had been indicted and in the absence of his counsel." In *Massiah*, the defendant had retained counsel before the statements were elicited **[****30]** from him and, significantly, the court noted that "it was entirely proper to continue an investigation of the suspected criminal activities of the defendant * * * even though the defendant had already been indicted" *(*supra, p 207).

I do not view the Federal District Court decision in United States ex rel. Lopez v Zelker (344 F Supp 1050, affd 465 F2d ***[*493]*** 1405) as requiring a contrary result. The essence of Judge Frankel's decision in the *Lopez* habeas corpus proceeding was that defendant's waiver of the right to counsel was not knowingly and intelligently rendered because he was not aware of the outstanding indictment against him for the crime of murder. The decision, therefore, is predicated upon a view of the facts which is divergent from the facts as developed in the proceedings against Lopez in our State courts. The majority of this court in *Lopez* observed that "[defendant] does not dispute either the waiver or the sufficiency of the evidence to find that it was intelligently and understandingly made" *(*supra, p 25). The trial court in *Lopez*, affirmed by an unanimous Appellate Division, found, following a suppression hearing, that "the People **[****31]** have proven beyond a reasonable doubt that the defendant intelligently understood the warnings and knowingly expressed his waiver of Constitutional rights," and we held that there was evidence in the record to sustain such a finding (p 25). Thus, three New York courts found that Lopez made voluntary statements following a knowing and intelligent waiver of the right to counsel.

I would only add that adopting the position proposed by the majority would bar the admissibility of any statements which a defendant might wish to tender in response to any police inquiry, no matter how knowingly and intelligently made, following the commencement of any criminal action by the filing of an accusatory instrument even so minor as a simplified traffic information. [*]

End of Document

[*] CPL 1.20 (subd [1]) defines an accusatory instrument as "an indictment, an information, a simplified traffic information, a prosecutor's information, a misdemeanor complaint or a felony complaint."

Rayham v Multiplan, Inc.

Supreme Court of New York, Appellate Division, Second Department

August 23, 2017, Decided

2015-04427

Reporter

153 A.D.3d 865 *; 61 N.Y.S.3d 90 **; 2017 N.Y. App. Div. LEXIS 6277 ***; 2017 NY Slip Op 06306 ****; 2017 WL 3611693

[**1]** Roman Rayham, M.D., et al., Appellants, v Multiplan, Inc., et al., Respondents. (Index No. 503315/13)

Counsel: **[***1]** Kenneth L. Kutner, New York, NY, for appellants.

James Edward Gross, Albany, NY, and Baker Donelson, Bearman, Caldwell & Berkowitz, P.C., Baton Rouge, Louisiana (Errol J. King, pro hac vice, and Robert Blankenship, pro hac vice, of counsel), for respondents (one brief filed).

Judges: CHERYL E. CHAMBERS, J.P., ROBERT J. MILLER, BETSY BARROS, FRANCESCA E. CONNOLLY, JJ. CHAMBERS, J.P., MILLER, BARROS and CONNOLLY, JJ., concur.

Opinion

[91]** **[*865]** Appeal from an order of the Supreme Court, Kings County (Carolyn E. Demarest, J.), dated February 23, 2015. The order denied the plaintiffs' motion for summary judgment on the complaint, and granted the defendants' cross motion for summary judgment dismissing the complaint.

Ordered that the order is affirmed, with costs.

The plaintiff Roman Rayham is a plastic surgeon, and the plaintiff RR Plastic Surgery P.C. (hereinafter RR Office) is his private practice. Rayham also works as an attending physician at various New York City hospitals, including New York Methodist Hospital (hereinafter Methodist). Nonparty Park Slope Physician Services P.C. (hereinafter PSPS) handles all of Methodist's billing, including the billing for services Rayham provides at Methodist.

[92]** **[***2]** In 2009, in connection with his practice at Methodist, Rayham executed a limited power of attorney authorizing nonparty Allegiance Billing & Consulting, LLC (hereinafter Allegiance), to contract on his behalf with network providers and health insurance companies for services performed at Methodist.

In 2010, Allegiance executed an agreement (hereinafter the Beech Street Agreement) on Rayham's behalf with the defendant **[*866]** Beech Street Corporation (hereinafter Beech Street), a preferred provider organization. The Beech Street Agreement provided that its terms may be amended upon "30 days prior written notice from Beech to [Rayham]" and that the "amendment shall be effective at the conclusion of such 30 day notice period unless [Rayham] objects to the amendment and notifies Beech in writing of [Rayham's] intent to terminate prior to the conclusion of such notice period." The address to which the Beech Street Agreement required the written notice to be sent was the address for the office of PSPS. The Beech Street Agreement further provided that Beech Street may assign its rights under the contract to a "Beech Affiliate," which was defined as any "entity" that is "controlled by or is under common **[***3]** control of Beech [Street]."

In 2010, the defendant Multiplan, Inc. (hereinafter Multiplan), another preferred **[****2]** provider organization, acquired Beech Street's parent company. In March 2011, Multiplan sent two letters to Rayham at PSPS's address. Both letters advised that Multiplan had acquired Beech Street and that, effective July 15, 2011, the Beech Street and Multiplan networks would integrate and claims would be processed under Multiplan's fee schedule. The second letter, dated March 28, 2011, advised that the Beech Street Agreement would be amended so as to include the claims for services Rayham provided at Methodist in the Multiplan network. Rayham claims he never received these letters.

In November 2011, the plaintiffs faxed Beech Street a letter on their letterhead requesting that the RR Office be added "to our profile," with a retroactive date of July 1, 2011. The letter provided the RR Office's address and tax-identification number, and a W-9 form was attached.

Upon receiving the fax, the defendants retroactively enrolled the RR Office in their networks and processed the RR Office's claims according to Multiplan's fee schedule. A few months later, after realizing that the RR **[***4]** Office was receiving lower reimbursements than were once provided by Beech Street, Rayham learned that Multiplan had acquired Beech Street and that claims were being processed pursuant to Multiplan's fee schedule. Rayham requested the RR Office's removal from the defendants' networks. This request was granted, but the request for the reprocessing of the RR Office's claims was denied.

The plaintiffs commenced this action, asserting causes of action sounding in breach of contract, breach of the implied covenant of good faith and fair dealing, unjust enrichment, and quantum meruit. The plaintiffs alleged that the defendants **[*867]** unilaterally altered the terms of the Beech Street Agreement by placing the RR Office in the Multiplan network and repricing its claims under the Multiplan fee schedule without affording the plaintiffs with notice or an opportunity to object as required under the Beech Street Agreement. Following joinder of issue and the completion of discovery, the plaintiffs moved for summary judgment on the complaint, and the defendants cross-moved for summary judgment dismissing the complaint. The Supreme Court denied the plaintiffs' motion and granted the defendants' cross motion. **[***5]** The plaintiffs appeal.

[93]** The Supreme Court properly granted that branch of the defendants' motion which was for summary judgment dismissing the breach of contract cause of action. The elements of a cause of action to recover damages for breach of contract are the existence of a contract, the plaintiff's performance pursuant to the contract, the defendant's breach of its contractual obligations, and damages resulting from the breach (*see* Tudor Ins. Co. v Unithree Inv. Corp., 137 AD3d 1259, 1260, 27 NYS3d 399 [2016]; PFM Packaging Mach. Corp. v ZMY Food Packing, Inc., 131 AD3d 1029, 1030, 16 NYS3d 298 [2015]). "[A] contract is to be construed in accordance with the parties' intent, which is generally discerned from the four corners of the document itself. Consequently, 'a written agreement that is complete, clear and unambiguous on its face must be enforced according to the plain meaning of its terms' " (Legum v Russo, 133 AD3d 638, 639, 20 NYS3d 124 [2015], quoting MHR Capital Partners LP v Presstek, Inc., 12 NY3d 640, 645, 912 NE2d 43, 884 NYS2d 211 [2009]).

Here, the defendants established, prima facie, that they did not breach the Beech Street Agreement by placing the RR Office in the Multiplan network and repricing its claims. Contrary to the plaintiffs' contentions, the defendants afforded the plaintiffs the contractually-required notice and opportunity to object. The defendants complied with the Beech Street Agreement by sending the March 2011 letters, which advised Rayham that Multiplan had acquired **[***6]** Beech Street and that claims would be processed under the Multiplan fee schedule, to the address expressly required by the contract for such written notices (*see* Global Events LLC v Manhattan Ctr. Studios, Inc., 123 AD3d 449, 449, 998 NYS2d 336 [2014]; *Foley Prods. v Singer Corp., 133 AD2d 531, 531, 519 NYS2d 902 [1987]*; *see also* FG Harriman Commons, LLC v FBG Owners, LLC, 75 AD3d 527, 528, 906 NYS2d 62 [2010]). Contrary to the plaintiffs' contention, it was not improper for Multiplan, as opposed to Beech Street, to send the March 2011 letters, as it met the definition of a "Beech affiliate" under the Beech Street Agreement. To the extent the plaintiffs argue that the defendants did not present evidence conclusively establishing the **[*868]** date, destination, and method for sending the letters, this argument, raised for the first time on appeal, is not properly before this Court (*see* Yong U Lee v Huan Wen Zhang, 133 AD3d 651, 652, 18 NYS3d 871 [2015]). Since the defendants provided Rayham with proper notice that the Beech Street Agreement would be amended so as to subject claims to the Multiplan fee schedule, and Rayham failed to object in writing within the 30-day notice period, the amendment took effect, as stated in the letters, on July **[****3]** 15, 2011.

The defendants further established, prima facie, that the RR Office's subsequent enrollment in their networks was pursuant to the plaintiffs' voluntary request. The defendants established, prima facie, that they did not breach the Beech Street Agreement **[***7]** by enrolling the RR Office in their networks and processing their claims under the Multiplan fee schedule by submitting the letter that the plaintiffs faxed to Beech Street in November 2011 requesting that the RR Office be added "to our profile" (*see* Countrywide Home Loans, Inc. v United Gen. Tit. Ins. Co., 109 AD3d 953, 953-954, 972 NYS2d 296 [2013]; Bradco Homes v Gellert, 223 AD2d 857, 859, 636 NYS2d 202 [1996]). In opposition, the plaintiffs failed to raise a triable issue of fact (*see* Zuckerman v City of New York, 49 NY2d 557, 562, 404 NE2d 718, 427 NYS2d 595 [1980]).

[94]** The Supreme Court also properly granted that branch of the defendants' motion which was for summary judgment dismissing the cause of action alleging a breach of the implied covenant of good faith and fair dealing. Implicit in every contract is a covenant of good faith and fair dealing, which encompasses any promise that a reasonable promisee would understand to be included (*see* New York Univ. v Continental Ins. Co., 87 NY2d 308, 318, 662 NE2d 763, 639 NYS2d 283 [1995]; Staffenberg v Fairfield Pagma Assoc., L.P., 95 AD3d 873, 875, 944 NYS2d 568 [2012]). "The covenant is breached 'where one party to a contract seeks to prevent its performance by, or to withhold its benefits from, the other' " (Michaan v Gazebo Hort., Inc., 117 AD3d 692, 693, 985 NYS2d 601 [2014], quoting Collard v Incorporated Vil. of Flower Hill, 75 AD2d 631, 632, 427 NYS2d 301 [1980], *affd* 52 NY2d 594, 421 NE2d 818, 439 NYS2d 326 [1981]). The defendants' submissions established, prima facie, that they did not withhold the benefits of, or seek to prevent the performance of, the Beech Street Agreement either in its original form, or as amended (*see generally* 1357 Tarrytown Rd. Auto, LLC v Granite Props., LLC, 142 AD3d 976, 977, 37 NYS3d 341 [2016]; Staffenberg v Fairfield Pagma Assoc., L.P., 95 AD3d at 875; 767 Third Ave. LLC v Greble & Finger, LLP, 8 AD3d 75, 75, 778 NYS2d 157 [2004]). In opposition, the plaintiffs failed to raise a triable issue of fact (*see* Zuckerman v City of New York, 49 NY2d at 562).

The Supreme Court properly **[***8]** granted those branches of the **[*869]** defendants' motion which sought summary judgment dismissing the causes of action sounding in unjust enrichment and quantum meruit. Those causes of action cannot be maintained if there is a valid, enforceable contract governing the same subject matter underlying the action (*see* Cox v NAP Constr. Co., Inc., 10 NY3d 592, 607, 891 NE2d 271, 861 NYS2d 238 [2008]; Goldman & Assoc., LLP v Golden, 115 AD3d 911, 913, 982 NYS2d 519 [2014];*Scott v Fields, 92 AD3d 666, 669, 938 NYS2d 575 [2012]*). Here, the defendants established, prima facie, that the Beech Street Agreement governs the subject matter underlying the action (*see* Goldman & Assoc., LLP v Golden, 115 AD3d at 913; *Scott v Fields, 92 AD3d at 669*). In opposition, the plaintiffs failed to raise a triable issue of fact (*see* Zuckerman v City of New York, 49 NY2d at 562).

Accordingly, the Supreme Court properly denied the plaintiffs' motion for summary judgment on the complaint and properly granted the defendants' cross motion for summary judgment dismissing the complaint. Chambers, J.P., Miller, Barros and Connolly, JJ., concur.

End of Document

RLJCS Enters. v. Prof'l Benefit Trust, Inc.

United States District Court for the Northern District of Illinois, Eastern Division

June 15, 2006, Decided ; June 15, 2006, Filed

No. 03 C 6080

Reporter

438 F. Supp. 2d 903 *; 2006 U.S. Dist. LEXIS 44131 **; 38 Employee Benefits Cas. (BNA) 1368

RLJCS ENTERPRISES, INC., et al., Plaintiffs, v. PROFESSIONAL BENEFIT TRUST, INC., et al., Defendants.

Subsequent History: Affirmed by Rljcs Enters. v. Prof'l Benefit Trust Multiple Emplr. Welfare Benefit Plan & Trust Multiple Emplr. Welfare Ben. Plan & Trust, 2007 U.S. App. LEXIS 10125 (7th Cir. Ill., May 2, 2007)

Prior History: RLJCS Enters. v. Prof'l Benefit Trust, Inc., 2005 U.S. Dist. LEXIS 27250 (N.D. Ill., Nov. 8, 2005)

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For Professional Benefit Trust, Inc, Defendant: Douglas Spears Robson, Handler, Thayer, & Duggan LLC, Chicago, IL;

For Professional Benefit Trust Multiple Employer Welfare Benefit Trust Plan and Trust, Defendant: Columbus R. Gangemi, Jr., Romy Elisabeth Carr, Timothy John Rooney, Winston & Strawn, Chicago, IL.

For 1st Fidelity Trust Co., Ltd, Defendant Professional Benefit Trust, Ltd., Defendant: Richard D Hart, Handler, Thayer, & Duggan LLC, Chicago, IL; Columbus R. Gangemi, Jr., Cheryl Tama Oblander, Romy Elisabeth Carr, Timothy John Rooney, Winston & Strawn, Chicago, IL.

For Sunderlage Resource Group, Inc., Professional Benefit Trust, Administration, LLC, Tracy L Sunderlage, Carey L Sunderlage, Defendant: Richard D Hart, Douglas Spears Robson, Handler, Thayer, & Duggan LLC, Chicago, IL.

For Canada Life Financial Corporation, Canada Life Assurance Corporation, Defendant: David Joseph Novotny, Chittenden, Michael Brian Galibois, Murday & Novotny, LLC, Chicago, IL; Stephen James Jorden, Jorden Burt, **[**3]** LLP., Washington, DC.

For Sun Life Financial Services of Canada Inc, Sun Life Assurance Company of Canada, Defendant: Mark E Schmidtke, Robert L. Clark, Schmidtke Hoeppner Consultants LLP, Valparaiso, IN; F Joseph Jaskowiak, Hoeppner Wagner & Evans, Valparaiso, IN.

For Professional Benefit Trust, Ltd., Counter Claimant: Richard D Hart, Handler, Thayer, & Duggan LLC, Chicago, IL; Columbus R. Gangemi, Jr., Cheryl Tama Oblander, Timothy John Rooney, Winston & Strawn, Chicago, IL.

For Professional Benefit Trust Multiple Employer Welfare Benefit Trust Plan and Trust, Counter Claimant: Columbus R. Gangemi, Jr., Cheryl Tama Oblander, Timothy John Rooney, Winston & Strawn, Chicago, IL.

For RLJCS Enterprises, Inc., R Leldon Sweet, Mitchell A. Toups PC, Mitchell A Toups, Gail C. Jenkins PC, Gail C Jenkins, Gilbert I. Low Ltd, Gilbert I Low, R. Lyn Stevens, P.C., R Lyn Stevens, Hubert Oxford III PC, Hubert Oxford, III, David A Bosse MD PA, M.D. David A Bosse, SG/SW Bourque Management, Inc., Stephen G

Bourque, Stacy Bourque, Script Care Management, Inc., James F Brown, Stephen N Cherewaty, M.D. Stephen N Cherewaty, Christopher's Copy Service, Inc., Monty Christopher, Larry **[**4]** P Ducharme Inc, Larry P Ducharme, Joseph M. Finley & Associates, M.D., P.A., MD Joseph M Finley, Mehmet Gurgun MD PA, MD Mehmet Gurgun, Cleveland Management, Inc., Claude Cleveland, E. Linn Heartfield M.D., P.A., MD E Linn Heartfield, JLH Enterprises, Inc, MD J Leonard Hilliard, Michael G. Keller D.O. P.A., DO Michael G Keller, B A King Jr MD PA, MD B A King, Jr, Brent L. Mainwaring M.D. P.A., MD Brent L Mainwaring, Wayne S. Margolis M.D. P.A., MD Wayne S Margolis, PWM Enterprises, Inc., Phil W Meaux, Vida K. Riston, R.N. C.N.M. P.C., Vida K Riston, Daniel R. Roubein, M.D. P.A., MD Daniel R Roubein, Rodney D. Anderson, M.D. P.A., MD Rodney D Anderson, Miguel Castellanos MD PA, MD Miguel Castellanos, Mark A Wilson MD PA, MD Mark A Wilson, Counter Defendant: Paul Ethan Slater, Sperling & Slater, Chicago, IL; Richard Lyle Coffman, Richard L. Coffman, P.C., Beaumont, TX.

Judges: John E. Grady, United States District Judge.

Opinion by: John E. Grady

Opinion

[*904] **MEMORANDUM OPINION**

Before the court are the parties' cross-motions for summary judgment on the issue of stock ownership and plaintiffs' motion to strike certain of defendants' statements of material fact and supporting affidavits and documents. **[**5]** For the reasons explained below, the motions are treated as motions for partial summary judgment; defendants' motion is granted, and plaintiffs' motion is denied. Plaintiffs' motion to strike is denied.

BACKGROUND

We will repeat here a brief summary of the facts of this case from an earlier opinion:

> Plaintiffs are former employer and employee participants in a multiple-employer benefits trust ("the Trust"). The employers participated in the Trust for the sole purpose of providing death benefits for their participating employees. These death benefits were funded by life insurance policies that were purchased by the Trust with contributions made by the employers. The Trust was designed to be a qualifying trust under *section 419A(f)(6) of the Internal Revenue Code*, which allows employers to realize a tax deduction for contributions made to certain employee benefit plans. See *I.R.C. § 419A(f) (6)*.
>
> At the heart of this dispute are life insurance policies purchased by the Trust from Canada Life and Sun Life on behalf of participating employees. When these policies were issued, Canada Life and Sun Life were both mutual **[**6]** insurance companies, or, "insurer[s] whose policyholders are its owners, as opposed to a stock insurance company owned by outside shareholders." BLACK'S LAW DICTIONARY 1041 (7th ed. 1999). However, Canada Life and Sun Life, in 1999 and 2000 respectively, "demutualized," which is "[t]he process of converting a mutual insurance company (which is owned by its policyholders) to a stock insurance company (which is owned by outside shareholders). . . ." Id. at 445.
>
> As a result of these demutualizations, the Trust received shares of Canada Life and Sun Life stock (together, "the Demutualized Stock"). Then, in or around September 2000, the trustee of the Trust liquidated the Demutualized Stock for approximately $ 5,000,000, which the Trust has retained. Effective December 31, 2002, plaintiffs terminated their participation in the Trust. Upon their withdrawal, the Trust distributed to the participating employees their respective Canada Life and Sun Life insurance policies and their *pro rata* share of other related Trust assets. The distribution, however, did not include any of the sales proceeds from the Demutualized Stock.
>
> This action followed. Plaintiffs have brought a 73-page, **[**7]** sixteen-count complaint alleging violations of civil RICO, *18 U.S.C. §§ 1961, et seq.*, and ERISA, *29 U.S.C. §§ 1001, et seq.*, as well as various common law breach of contract, fiduciary duty and fraud-based claims. The crux of the complaint is that the participating employees had an ownership interest in the Demutualized Stock and that defendants -- the Trust and several related entities and individuals -- unlawfully **[*905]** deprived the employees of that interest when their *pro rata* shares of the sales proceeds were not included in their distributions.

RLJCS Enters., Inc. v. Professional Benefit Trust, Inc., 2004 U.S. Dist. LEXIS 17769, No. 03 C 6080, 2004 WL 2033067, at *1 (N.D. Ill. Sept. 2, 2004) (footnote omitted). [1]

In our opinion of September 2, 2004, we indicated that much of the complaint **[**8]** hinges on the narrow question of ownership of the Demutualized Stock and therefore put that question on the front burner. Shortly thereafter, we instructed the parties to conduct discovery on the question of stock ownership, with a view to preparing dispositive motions on the issue. We later set a briefing schedule on cross-motions for summary judgment. After the parties filed their initial briefs, defendants filed a motion to strike plaintiffs' expert reports, and we stayed briefing on the summary judgment motions pending a ruling on the motion to strike. After we granted the motion to strike in most respects, briefing on the summary judgment motions resumed. Those motions have been fully briefed for some time now, but at a late stage of the briefing, plaintiffs filed a motion to strike various of defendants' documents and statements. We decided to take that motion along with the summary judgment motions, and the motion to strike was then briefed. All the motions are now fully briefed.

A few initial observations are in order. The first is that the summary judgment briefs and exhibits are ridiculously voluminous. Upon reviewing the briefs, we are unable to understand why each side **[**9]** wanted to file its own summary judgment motion instead of briefing a single motion. After seeing the huge stack of papers devoted to these motions, one would be surprised to learn that the issue is simple: who is entitled to this windfall of Demutualized Stock? Each side merely had to set forth its supporting arguments for the contention that it is entitled to the proceeds. Instead, the parties, particularly plaintiffs, have briefed many other issues that are somewhat factually related, but ultimately of very little use in determining the legal issue of ownership.

We also are compelled to remark that the briefs, chiefly those of plaintiffs, are marked by pettiness and a lack of civility. [2] The same sort of incivility creeps into defendants' briefs at points. Our colleague, Judge Kennelly, confronted the problem of incivility and prudently remarked:

> It goes without saying that the parties on both sides of high-stakes civil cases often find their veracity, integrity, competence, and reputation under attack, not to mention their economic well-being. It is understandable that the parties in such cases sometimes take it personally and react negatively. But taking **[*906]** it personally **[**10]** is not the role of counsel. The lawyer's office does not include acting as the channeler of the client's anger and frustration. To put it another way, a lawyer is not, contrary to the colloquialism, a "mouthpiece" for his client. A lawyer representing a client can and must represent the client zealously. Sometimes, to be sure, this involves striking hard blows. But the punches must be thrown fairly. And personal attacks of the type made by the attorneys who filed the papers quoted above are rarely, if ever, justified. Our system of justice does not work, or at least does not work well, if lawyers act like professional wrestlers hyping the next match rather than as members of. the honorable profession to which they belong.

Daniels v. Bursey, 2004 U.S. Dist. LEXIS 9665, No. 03 C 1550, 2004 WL 1144046, at *2 (N.D. Ill. May 19, 2004). Counsel are advised to refrain from using inflammatory language in future filings.

[11]** The parties' unreasonable contentiousness is also displayed in their multiple motions and requests to strike various documents or statements. The briefing on the summary judgment motions was delayed by the filing of the first such motion by defendants. The motion was granted in large part. Plaintiffs then sent the court a letter calling our attention to their own request, which had been included within their response to defendants'

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[1] It appears that plaintiffs are seeking both stock proceeds and stock that was not sold. We will simply refer to the proceeds and the stock as the "stock" for convenience.

[2] In their reply brief regarding their motion for summary judgment, plaintiffs characterize defendants as (1) "danc[ing] a little sidestep" (curiously quoting from the movie "The Best Little Whorehouse in Texas," and providing a footnote to that effect, as if plaintiff's counsel is proud of the flippant remark); (2) "say[ing] what they need to say when they need to say it in order to make a point;" (3) "employing the fine art of shading and wordsmithing;" (4) "hid[ing] behind" the Plan documents. (Plaintiffs' Reply in Support of Summary Judgment Motion at 2, 5.) In their reply in support of their motion to strike, plaintiffs provide another abrasive quotation -- "Those who know the least know it the loudest" -- and accuse defendants of "ignor[ing] the cold hard facts, ignor[ing] the law and say[ing] what they have to say." (Plaintiffs' Reply in Support of Motion to Strike at 1.) These are just a few examples of the general snide tone that pervades many of plaintiffs' briefs.

motion to strike, to strike the legal opinions and testimony of one of defendants' witnesses, Thomas J. Handler. Thereafter, we issued a minute order stating in relevant part:

> Defendants state that the "memoranda and documents authored by Handier and/or the Handler law firm are offered exclusively as *transactional* documents, issued *to the PBT Plan and its participants at the time of and as part of the transactions at issue*. These documents establish the very history of the facts of the case and are relevant as facts in the case." (Reply at 10.) Accordingly, these materials will not be stricken because they may assist the court on factual issues. Of course, to the extent that they do not bear on the *facts* of the case and contain legal **[**12]** analysis and conclusions that would usurp the province of the court, the legal analyses will be disregarded. At this juncture, though, it would be a waste of time to sift through each exhibit identified by plaintiffs to assess which portions are fact and which portions are legal opinion. Plaintiffs can rest assured that, when ruling on the motions for summary judgment, the court will disregard legal analysis and conclusions whether those analyses and conclusions are offered by plaintiffs or by defendants.

(Minute Order of December 1, 2005.) It is puzzling to us how this order could be construed as an invitation or suggestion to file another motion to strike, but a week after we issued the order, plaintiffs did just that. Plaintiffs move to strike (1) the affidavit of Tracy L. Sunderlage, one of the defendants; (2) the affidavit of Thomas J. Handler (whose testimony was the very subject of the minute order); and (3) certain excerpts of Sunderlage and Handler's deposition testimony; and (4) over 150 of defendants' Rule 56.1 statements of material fact. Plaintiffs have even submitted a proposed order seeking individual rulings on each and every paragraph in the affidavits to which **[**13]** they object, and on each and every fact statement. The same day plaintiffs filed their motion to strike, defendants filed a response to plaintiffs' Rule 56.1 Statement arguing that the entire Statement should be stricken.

Motions to strike are generally disfavored except when they serve to expedite. See *Heller Fin., Inc. v. Midwhey Powder Co., 883 F.2d 1286, 1294 (7th Cir. 1989)*. These motions and requests to **[*907]** strike do not serve to expedite or streamline matters here; rather, the motions are unnecessary clutter and have only delayed briefing on the substantive motions. We need not and will not wade through the Sunderlage and Handler affidavits, or through their deposition testimony, to provide a detailed analysis of why each paragraph or statement is or is not improper legal opinion, or conclusory, or based on hearsay. We have found it unnecessary to even consider the statements in the affidavits and the deposition testimony to which plaintiffs object because they are not material to our ruling today. Similarly, we need not and will not provide individual rulings on over 150 of defendants' statements of fact for relevance or hearsay objections, or dozens of plaintiffs' **[**14]** statements of fact. We will say as a general matter that many of plaintiffs' statements of "fact" do appear to contain inappropriate legal argument, and that plaintiffs' relevancy objections to many of defendants' statements of fact are unfounded.

Perhaps individualized rulings on some of the evidence or statements would have been necessary were the issue here not so simple. But the only question before us at this point is ownership of the stock, and the relevant undisputed facts -- which are far fewer than the facts that the parties have deemed relevant -- will be set forth in our discussion infra. It will be clear from our discussion and analysis which facts are relevant to the issues. Plaintiffs' motion to strike and defendants' request to strike will be denied. [3]

DISCUSSION

Summary judgment "shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, **[**15]** and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." *Fed. R. Civ. P. 56(c)*. In considering such a motion, the court construes the evidence and all inferences that reasonably can be drawn therefrom in the light most favorable to the nonmoving party. See *Pitasi v. Gartner Group, Inc., 184 F.3d 709, 714 (7th Cir. 1999)*. "Summary judgment should be denied if the dispute is 'genuine': 'if the evidence is such that a reasonable jury could return a verdict for the nonmoving party.'" *Talanda v. KFC Nat'l Mgmt. Co., 140 F.3d 1090, 1095 (7th Cir. 1998)* (quoting *Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986))*. The court will

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[3] One wonders what amounts of needless attorneys' fees have been generated by the creation of this mound of paper.

enter summary judgment against a party who does not "come forward with evidence that would reasonably permit the finder of fact to find in [its] favor on a material question." McGrath v. Gillis, 44 F.3d 567, 569 (7th Cir. 1995).

A. **Additional Material Facts**

Defendant Professional Benefit Trust Multiple **[**16]** Employer Welfare Benefit Plan and Trust (the "Trust") was established in 1989. It has provided specified employee welfare benefits for sixteen years and currently provides benefits for over 2500 employee participants in 300 employer groups. The Trust is governed by the Professional Benefit Trust ("PBT") Multiple Employer Welfare Benefit Plan and Trust document, which has been amended from time to time. Defendant Professional Benefit Trust, Ltd. ("PBTL") is the entity that is the Managing Trustee of the Trust, and defendant Tracy Sunderlage is CEO and Chairman of PBTL. [4]

Plaintiffs began participating in the Trust during the mid-1990s for the sole **[*908]** purpose of securing death benefits, but not severance, long-term care, or medical benefits. In late 1997, the Trust amended the governing Trust document by issuing the PBT Third Amended and Restated Multiple Employer Welfare Benefit Plan and Trust ("the Third Amended Document"). The employer plaintiffs **[**17]** were provided copies of the Third Amended Document, a Summary Plan Description, and a 47-page legal opinion prepared by counsel for the Trust that addressed the operation of and participation in the Trust and the federal income tax and estate tax consequences. Each employer plaintiff executed an Adoption Agreement formally agreeing to the Third Amended Document.

The Trust was designed to operate as follows. Covered employees, those whose employers participated in the Trust, would be entitled to a death benefit in an amount (relative to the employee's compensation) that was selected by the employer in the Adoption Agreement. The Trust funded these benefits primarily through the purchase of investment-grade insurance policies on the lives of the employees. The employers contributed to the Trust by paying the premiums on these life insurance policies; the Trust then paid the premiums to the life insurance companies.

The language of the Third Amended Document indicates that the Trust was intended to comply with § 419A(f) (6) of the Internal Revenue Code, 26 U.S.C. § 419A(f)(6), which would allow the employers to claim federal income tax **[**18]** deductions for their contributions. In a § 419A(f) (6) plan, the Trust must be the owner of the insurance policies, even though the policies are written on the employee participants' lives. Moreover, § 419A(f)(6) requires that there be a single plan, not an aggregation of individual plans, and that all plan assets be available for all employee participants instead of allocated to specific employers.

Most of the life insurance policies were purchased from The Canada Life Assurance Company ("Canada Life"), and one policy was purchased from Sun Life Assurance Company of Canada ("Sun Life"). In 1999 and 2000, respectively, Canada Life and Sun Life demutualized. The Trust had never experienced a demutualization, and evidently Sunderlage and his advisors were initially unsure about how to treat the stock windfall. There is no dispute that at the time of the demutualizations, the Third Amended Document was the governing Trust document. The Third Amended Document does not contain the words "demutualized stock" or include any provisions pertaining to the treatment of demutualized stock specifically. Plaintiffs' position was that they alone were entitled to the stock, and there were extensive **[**19]** discussions between plaintiffs' representatives and the Trust. The parties also obtained legal opinions concerning treatment of the stock. Eventually, the stock proceeds were deposited in the "Surplus Account" of the Trust, [5] and plaintiffs did not **[*909]** receive the stock or stock proceeds. The Trust

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[4] There are other related defendants whom we need not discuss.

[5] Pursuant to the terms of the Third Amended Document, the "Surplus Account" receives "all experience gains" of the Trust. The Third Amended Document does not define the term "experience gain." It does refer, however, to some occurrences that are treated as experiences gains. It provides that after certain triggering events, if an employee or the beneficiary of the employee's death benefit does not purchase the insurance policy, the proceeds of the sale or surrender of the policy "shall be treated as an experience gain" and shall be governed by § 11.4 of the Document, which provides that experience gains are to be deposited in the Surplus Account. (App. to Defendants' Rule 56.1 Statement, Vol. I, Ex. 4, Third Amended Document, § 5.4.) The Third Amended Document also provides that unclaimed benefits become a part of the Surplus Account, and that excess assets remaining in the Trust after certain conditions are satisfied following an employer's withdrawal shall be treated as experience gains and credited to the Surplus Account. (Id., §§ 12.2, 12.3(b).)

reasoned that the stock was an "experience gain" that must be retained by the Trust in keeping with the Third Amended Document and § 419A(f)(6).

[20]** Beginning in late 2002, the employer plaintiffs began to request to withdraw from the Trust; all but two of the employer plaintiffs withdrew effective December 31, 2002. [6] According to the Third Amended Document, when an employer withdrew from the Trust, the participant employees were entitled to receive their pro rata share of Trust assets, exclusive of the Surplus Account. Upon withdrawal, plaintiffs elected to keep their life insurance policies and "roll them over" to another account, and so the policies were distributed to the employee plaintiffs, along with excess funds that had been deposited in the Trust that temporarily had been invested in tax-free municipal bonds. Because this distribution was largely in-kind (consisting of the life insurance policies) instead of in cash, plaintiffs claim that the Trust did not actually make a calculation of their pro rata shares. In plaintiffs' view, the Trust did not comply with § 419A(f) (6) because it did not divvy up the Trust assets on a pro rata basis based on mathematical calculations. Defendants admit that they did not perform actuarial calculations when plaintiffs withdrew from the Trust, but state that the relevant calculations **[**21]** of the cash surrender values had already been made by the insurance companies that issued the policies. Defendants contend that when plaintiffs received the insurance policies, plaintiffs had actually"purchased" them by having their pro rata shares reduced by the cash surrender values of the policies.

B. Demutualized Stock Ownership

The parties' briefs, voluminous as they are, fail to provide a framework for deciding the question of entitlement to the Demutualized Stock. Instead, the parties plunge directly into their reasons why they believe they are entitled to the stock, without indicating why these factors matter in the overall equation. Defendants contend that (1) the Trust was created and intended to comply with § 419A(f) (6), which requires that the value of the stock be held by the Trust for all ongoing participants; (2) defendants were authorized by the terms of the governing **[**22]** Trust documents to deposit the proceeds of the Demutualized Stock in the Surplus Account for the benefit of all Trust participants; and (3) plaintiffs are estopped from claiming any right to the stock because they accepted the Trust's welfare benefits and tax benefits and expressly agreed to the terms of the Trust documents. Plaintiffs, on the other hand, argue that they are entitled to the stock because (1) Sunderlage "repeatedly promised" to distribute it to plaintiffs when they terminated their participation in the Trust; (2) the Trust is a collection of individual welfare benefit plans instead of a single Trust of pooled assets that complies with § 419A(f)(6); and (3) the stock is not an "experience gain" that the Trust was required to allocate to its Surplus Account under the terms of the trust documents or the law.

The proper framework for our analysis is provided in an opinion cited in plaintiffs' reply brief in support of their motion, *Chicago Truck Drivers, Helpers & Warehouse Workers Union (Independent) Health & Welfare Fund v. Local 710, International Brotherhood of Teamsters, No. 02 C 3115, 2005 U.S. Dist. LEXIS 42877, 2005 WL 525427 (N.D. Ill.* ***[*910]*** *Mar. 4, 2005)* (Guzman, J.). Chicago **[**23]** Truck Drivers involved four employee-benefit plans that held insurance policies purchased from companies that demutualized. The issues were whether the demutualization proceeds were plan assets, and if so, whether the compensation reverted to the employees or to the employers. The court noted that ERISA does not define "plan assets," but that the Department of Labor [7] has issued advisory opinions concerning the treatment of demutualization compensation by benefit plans. An agency's advisory opinions are not binding authority, but they are entitled to deference if reasonable. See *2005 U.S. Dist. LEXIS 42877, [WL] at *3*.

A side note before plunging into our analysis. The instant case is unusual because the former employer and employee Trust participants are not adversaries; **[**24]** they have aligned themselves on the same side because the employer plaintiffs are the wholly-owned professional corporations of the employee plaintiffs. In the typical scenario, as in Chicago Truck Drivers, the question would be whether the demutualized stock reverts to the employers or to the employees. Here, plaintiffs -- both employers and employees -- claim that the stock is not a plan asset and that they are entitled to the stock to the exclusion of the other participants in the

[6] As for the remaining two employers, one withdrew on December 31, 2001, and the other withdrew on December 31, 2003.

[7] "The Department of Labor shares enforcement responsibility for ERISA with the Department of the Treasury." *John Hancock Mut. Life Ins. Co. v. Harris Trust & Sav. Bank, 510 U.S. 86, 107 n.14, 114 S. Ct. 517, 126 L. Ed. 2d 524 (1993)* (citing *29 U.S.C. § 1204(a)*).

Trust. [8]

According to the Department of Labor, "the assets of a plan generally are to be identified on the basis of ordinary notions of property rights under non-ERISA law. This identification process includes consideration of any contract or other legal instrument involving the plan, including the plan documents. It also requires the consideration **[**25]** of the actions and representations of the parties involved." Dep't of Labor Advisory Op. 92-02A, at 2 (Jan. 17, 1992). A more recent advisory opinion stated: "The proceeds of the demutualization will belong to the plan if they would [sic] deemed to be owned by the plan under ordinary notions of property rights. . . . In the case of an employee pension benefit plan, or where any type of plan or trust is the policyholder, or where the policy is paid for out of trust assets, it is the view of the department that all of the proceeds received by the policyholder in connection with a demutualization would constitute plan assets." Dep't of Labor Advisory Op. 2001-02A, at 5-6 n.2 (Feb. 15, 2001) (emphasis added).

In Chicago Truck Drivers, the court analyzed, among other plans, a life insurance plan that met ERISA's definition of an employee welfare benefit plan. [9] The court found that because the employers made all of the contributions to the plan and because **[*911]** there was nothing in the language of the plan to suggest that demutualization compensation was intended to be a plan asset, the demutualization compensation was not a plan asset and reverted to the employers. *2005 U.S. Dist. LEXIS 42877, 2005 WL 525427, **[**26]** at *8*.

Plaintiffs maintain that under **[**27]** the analysis of Chicago Truck Drivers, they are entitled to the Demutualized Stock because the employers made the contributions to the Trust and because the Third Amended Document does not mention demutualized stock. We disagree. The life insurance plan in *Chicago Truck Drivers* is distinguishable in two very important ways. First, the policy at issue in that case was a group policy owned by the employers. Here, the policies were owned by the Trust pursuant to the express language of the Third Amended Document:

> Each application for a policy, and the policies themselves, shall designate the Trustee as sole owner, with the right reserved to the Trustee to exercise any right or option contained in the policies, subject to the terms and provisions of this Agreement. The Trustee shall be the named beneficiary.
>
> Subject to the right of a Participant Employee to make a Beneficiary [10] designation (and change such designation from time to time) the Trustee shall have full and complete control over any insurance policy as set forth in Section 14.4(k) hereof.
>
> [T]he Trustee is authorized and empowered . . . [t]o apply for and own any life insurance policy of the Insurer **[**28]** held as an asset of the Trust Fund, and to exercise any option, privilege or benefit in connection therewith, including, without limitation, the right to collect and receive the cash surrender value proceeds and all dividends or other distributions thereof. . . .

(Third Amended Document, §§ 3.1, 5.2(a), 14.4(m).) In compliance with the language of the Third Amended Document, the policies on the employee plaintiffs' lives were titled to the Trust and named the Trust as beneficiary. The Adoption Agreements that the employer plaintiffs executed (in which they formally agreed to the Third Amended Document) stated: "All insurance policies and bond funds will be titled (owned) by TTEE, Independent Trust Company FBO

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[8] Plaintiffs do not seek to recover any share of demutualized stock that may have been issued with respect to life insurance policies insuring the lives of other Trust participants.

[9] There is no genuine dispute that the Trust is an "employee welfare benefit plan" under ERISA, *29 U.S.C. § 1002(1) (A)*, because it provides benefits in the event of death. The Trust documents contemplate a single plan, not a collection of plans. But plaintiffs argue, without authority, that the Trust is a collection of hundreds of individual employee welfare benefit plans instead of a single employee welfare benefit plan. This position is relevant to their contention that the Trust did not operate in compliance with *§ 419A(f)(6) of the Internal Revenue Code*. However, for our purposes, the characterization "employee welfare benefit plan" is an ERISA determination that is independent of the Trust's status for tax purposes. Indeed, plaintiffs themselves argue that the employee welfare benefit plan at issue in Chicago Truck Drivers is analogous to the Trust. (Plaintiffs' Reply in Support of Summary Judgment Motion at 6.)

[10] "Beneficiary" is defined by the Third Amended Document as "the person or persons or entity designated by a Participant Employee to receive the Death Benefit, if any, payable under the Plan." (Third Amended Document, § 1.1(d).) So, the Third Amended Document uses the term "beneficiary" in two different ways: uncapitalized, it refers to the named beneficiary of the life insurance contract, which was the Trust; capitalized, the term refers to the person or entity who was designated to receive the death benefit from the Trust pursuant to the terms of the Third Amended Document.

Professional Benefit Trust." (App. to Defendants' Rule 56.1 Statement, Vol. II, Ex. 16, Sample Adoption Agreement, art. XVI.)

[29]** A second distinguishing factor is that in *Chicago Truck Drivers*, there was nothing in the language of the plan at issue to suggest how to treat demutualization compensation. The plan document was silent in regard to possible assets such as dividends. In this case, however, there are indicia in the language of the Third Amended Document that demutualization compensation should be treated as assets of the Trust for the benefit of all Trust participants, not just plaintiffs. Because "ordinary notions of property rights" govern, first and foremost is the above-quoted language stating that the Trust owned the policies and had full and complete control over the policies. In contrast to Chicago Truck Drivers, the Third Amended Document **[*912]** contains a provision concerning dividends; the Trustee has "the right to collect and receive the cash surrender value proceeds and all dividends or other distributions thereof." (Third Amended Document, § 14.4(m).) Moreover, the following additional provisions giving the Trustee broad ownership and control, and disclaiming any ownership or control by employers or employees, support the treatment of the Demutualized Stock as an asset of the Trust:

. **[**30]** Upon termination of employment, the participant employees do not have the right to purchase the insurance policies; rather, the Trustee "may permit" them to purchase the policies for their cash surrender value. (§ 5.4)
. "The Employer shall have no right, title or interest in and to the contributions made by it to the Trust; and, no part of the Trust property, or res, nor any income attributable thereto, ever shall revert to the Employer or be used for, or be diverted to, purposes other than for the exclusive benefit of the Participant Employees or for the payment of taxes and expenses of administration of the Trust. No Participant Employee shall have any right, title or interest in and to any contributions to the Trust by the Employer, any portion of the Trust res, nor any portion of any income attributable to the Trust, except as may otherwise be provided herein. (§ 8.3)
."[N]o Participant Employee shall have any right, title or interest in any specific assets of the Trust Fund." (§ 10.3(i))

. "[T]he Trustee is authorized and empowered" to manage, convey, and "otherwise deal with all property" "on such terms and conditions as the Trustee shall decide," in **[**31]** addition to other broad rights. (§ 14.4)

Because the Trust owned the policies, it follows that the Trust owned the Demutualized Stock that flowed from the policies.

Plaintiffs argue in the alternative that even if the plaintiff employers are not entitled to the Demutualized Stock under a Chicago Truck Drivers analysis, the plaintiff employees are entitled to the stock pursuant to *Ruocco v. Bateman, Eichler, Hill, Richards, Inc., 903 F.2d 1232 (9th Cir. 1990)*. In Ruocco, the Ninth Circuit affirmed the district court's holding that demutualized stock reverted to the employee participants in a long-term disability insurance plan under a "balancing of the equities" test. The court found that allowing the compensation to revert to the employers would give the employers an undeserved windfall because the plan contributions had been made by the employees.

We see no reason to apply *Ruocco* here. Like Chicago Truck Drivers, Ruocco involved a group policy evidently owned by the employer. Furthermore, we decline to "balance the equities" because in the instant case, there was a contract that governed the administration of the Trust, and that contract **[**32]** stated that the Trust, not the plaintiffs, owned the policies. Plaintiffs decided to become participants in the Trust and agreed to its terms, knowing from the outset that they would not own the policies, and indeed why they would not own the policies. The Trust had to be structured in that way so that it would comply with *§ 419A(f)(6)*, and so the employers would therefore receive tax benefits.

Given that the benchmark of our analysis is "ordinary notions of property rights" (pursuant to Chicago Truck Drivers, a case cited by plaintiffs themselves), plaintiffs' contentions -- that defendants are "hiding behind" the Third Amended Document and that we should disregard the **[*913]** language of that document -- are absurd. In our view, the language of the Third Amended Document is clear and controlling. Plaintiffs make much of their experts' legal opinions and of a private letter ruling by the IRS to the effect that in practice, the Trust did not actually comply with all of the requirements of *§ 419A(f)(6)* at certain points in time. Defendants strenuously argue that it did, and the parties devote much of their briefs to the ins and outs of pooled assets, experience gains, and other esoteric **[**33]** characteristics of *§ 419A(f)(6)* plans.

We do not believe that the plan's compliance with *§*

419A(f)(6) bears on the issue of ownership. Whether the Trust was required to treat the Demutualized Stock as an "experience gain" is also beside the point; whether the Trust could do so because it owned the Stock is the relevant issue. We look to what the parties intended at the outset, and that intent is evidenced in the governing Trust document. The plaintiffs contracted for death benefits; they did not contract for ownership of the life insurance policies or other assets. Plaintiffs cite no authority whatsoever to support their argument that we should ignore the language of the Third Amended Document and focus instead on the Trust's compliance with tax regulations.

Plaintiffs also assert that they are entitled to the stock because Sunderlage "repeatedly promised" to distribute the stock to them when they terminated their participation in the Trust. (It is disputed whether Sunderlage actually made any "promise," but we will assume for purposes of this discussion that he did.) The argument, however, stops at "he promised"; plaintiffs fail to explain what the legal effect of such **[**34]** a "promise" was. And as with their arguments concerning tax compliance, plaintiffs fail to cite any authority at all to support their position. Again, what is relevant is what the parties intended regarding ownership of the policies at when they agreed to the terms of the governing documents, not what occurred years later when the Demutualized Stock was distributed.

Under ordinary notions of property rights, the Trust owned the policies. And it is not as if ownership by the Trust was some sort of decision made by a coin flip. Because they contemplated receiving (and did in fact receive) tax benefits, plaintiffs agreed to a welfare benefit plan structure in which the Trust was the policyholder. Because the Trust owned the policies, we hold that the Trust also owned the Demutualized Stock that was issued in relation to those policies.

A final note regarding the nature of our ruling. The parties have titled their cross-motions as simple motions for summary judgment. They are really motions for "partial" summary judgment on the issue of ownership because the parties have not identified which claims or counterclaims are affected by our ruling. It appears that our ruling today will dispose **[**35]** of most, if not all, of the case, but it is unclear exactly what is left of the claims and counterclaims. Therefore, the parties are directed to file cross-memoranda by June 23, 2006 and cross-responses by July 7, 2006, stating their views as to the effect of today's ruling on the claims and counterclaims in the case.

CONCLUSION

For the foregoing reasons, the cross-motions of the parties are treated as motions for "partial" summary judgment on the question of ownership of the Demutualized Stock. Defendants' motion for partial summary judgment is granted, and plaintiffs' motion for partial summary judgment is denied. Plaintiffs' motion to strike certain of defendants' statements of **[*914]** material fact and supporting affidavits and documents is denied.

DATE: June 15, 2006

ENTER:

John E. Grady, United States District Judge

Carlos Rodriguez, Appellant, v City of New York, Respondent.

Court of Appeals of New York

February 14, 2018, Argued ; April 3, 2018, Decided

No. 32

Reporter

31 N.Y.3d 312 *; 101 N.E.3d 366 **; 76 N.Y.S.3d 898 ***; 2018 N.Y. LEXIS 793 ****; 2018 NY Slip Op 02287; 2018 WL 1595658

[1] Carlos Rodriguez, Appellant, v City of New York, Respondent.

Subsequent History: On remand at, Judgment entered by Rodriguez v. City of New York, 161 A.D.3d 575, 77 N.Y.S.3d 46, 2018 N.Y. App. Div. LEXIS 3599, 2018 NY Slip Op 3634 (May 22, 2018)

Prior History: Appeal, by permission of the Appellate Division of the Supreme Court in the First Judicial Department, from an order of that Court, entered September 1, 2016. The Appellate Division order, insofar as appealed from, affirmed, to the extent appealed from by plaintiff, so much of an order of the Supreme Court, New York County (Kathryn E. Freed, J.; op 2014 NY Slip Op 33650[U] [2014]), as had denied plaintiff's motion for partial summary judgment on the issue of liability. The following question was certified by the Appellate Division: "Was the order of Supreme Court, as affirmed by this Court, properly made?"

Carlos Rodriguez v. City of New York., 2016 N.Y. App. Div. LEXIS 8958 (N.Y. App. Div. 1st Dep't, Dec. 15, 2016)
Rodriguez v. City of New York, 142 A.D.3d 778, 37 N.Y.S.3d 93, 2016 N.Y. App. Div. LEXIS 5821 (Sept. 1, 2016)

Disposition: Order, insofar as appealed from, reversed, with costs, case remitted to the Appellate Division, First Department, for consideration of issues raised but not determined on the appeal to that court and certified question answered in the negative.

Counsel: **[****1]** *Kelner & Kelner, Esqs*., New York City (*Joshua D. Kelner* of counsel), for appellant. I. A plaintiff makes out a prima facie showing of entitlement to relief by demonstrating that the defendant's negligence proximately caused his or her injuries, and can obtain summary judgment as to a defendant's liability even if there is an issue of fact as to comparative fault. (*Roman v A1 Limousine, Inc., 76 AD3d 552, 907 NYS2d 251*; *Tselebis v Ryder Truck Rental, Inc., 72 AD3d 198, 895 NYS2d 389*; *Gonzalez v ARC Interior Constr., 83 AD3d 418, 921 NYS2d 33*; *Calcano v Rodriguez, 91 AD3d 468, 936 NYS2d 185*; *Maniscalco v New York City Tr. Auth., 95 AD3d 510, 943 NYS2d 486*; *Capuano v Tishman Constr. Corp., 98 AD3d 848, 950 NYS2d 517*; *Simoneit v Mark Cerrone, Inc., 122 AD3d 1246, 996 NYS2d 810*; *Pries-Jones v Time Warner Cable, Inc., 93 AD3d 1299, 941 NYS2d 410*; *Doody v Gottshall, 67 AD3d 1347, 891 NYS2d 216*.) II. Plaintiff should have been granted summary judgment on the issue of liability, as defendant was negligent, and its negligence proximately caused his accident. (*Coutrier v Haraden Motorcar Corp., 237 AD2d 774, 655 NYS2d 660*; *Sarosy v Scheina, 225 AD2d 493, 639 NYS2d 817*; *Pfaffenbach v White Plains Express Corp., 17 NY2d 132, 216 NE2d 324, 269 NYS2d 115*; *Dudley v Ford Credit Titling Trust, 307 AD2d 911, 762 NYS2d 905*; *Canfield v Giles, 182 AD2d 1075, 585 NYS2d 242, 182 AD2d 1075, 585 NYS2d 322*; *LaMasa v Bachman, 56 AD3d 340, 869 NYS2d 17*; *Mitchell v Gonzalez, 269 AD2d 250, 703 NYS2d 124*; *Long v Niagara Frontier Transp. Auth., 81 AD3d 1391, 917 NYS2d 463*; *Sheila C. v Povich, 11 AD3d 120, 781 NYS2d 342*; *Garcia v Verizon N.Y., Inc., 10 AD3d 339, 781 NYS2d 93*.)

Zachary W. Carter, Corporation Counsel, New York City (*Richard Dearing, Tahirih M. Sadrieh* and *Claude S. Platton* of counsel), for respondent. I. Issues of fact as to the City of New York's negligence defeat partial summary judgment on liability. (*Vega v Restani Constr. Corp., 18 NY3d 499, 965 NE2d 240, 942 NYS2d 13*; *Bruni v City of New York, 2 NY3d 319, 811 NE2d 19, 778 NYS2d 757*; *Ugarriza v Schmieder, 46 NY2d 471, 386 NE2d 1324, 414 NYS2d 304*; *Kowalsky v Conreco Co., 264 NY 125, 190 N.E. 206*; *Black v Wallace Church Assoc., 147 AD3d 668, 46 NYS3d 891*; *Consalvo v City of New York, 53 AD3d 521, 861 NYS2d 404*; *Wolfe v Teele, 223 AD2d 854, 636 NYS2d 198*; *Brugnano v Merrill Lynch & Co., 216 AD2d 18, 627 NYS2d 635*; *McKenna v Reale, 137 AD3d 1533, 29 NYS3d 596*;

Desio v Cerebral Palsy Transp., Inc., 121 AD3d 1033, 994 NYS2d 681.) II. Alternatively, issues of fact as to comparative fault also preclude summary judgment. (Schmidt v Flickinger Co., 88 AD2d 1068, 452 NYS2d 767; Thoma v Ronai, 189 AD2d 635, 592 NYS2d 333, *82 NY2d 736, 621 NE2d 690, 602 NYS2d 323*; Barker v Savage, 45 NY 191; Hersh v New York City Tr. Auth., 297 AD2d 556, 747 NYS2d 153; Cohen v Simmons, 240 AD2d 191, 658 NYS2d 29; Sammis v Nassau/Suffolk Football League, 95 NY2d 809, 732 NE2d 941, 710 NYS2d 834; Castiglione v Kruse, 130 AD3d 957, 15 NYS3d 360, 27 NY3d 1018, 32 NYS3d 579, 52 NE3d 243; Alvarez v Prospect Hosp., 68 NY2d 320, 501 NE2d 572, 508 NYS2d 923; Zuckerman v City of New York, 49 NY2d 557, 404 NE2d 718, 427 NYS2d 595; Ferrante v American Lung Assn., 90 NY2d 623, 687 NE2d 1308, 665 NYS2d 25.)

Andrew Zajac, Rona L. Platt, Brendan T. Fitzpatrick and *Lisa L. Gokhulsingh*, *Amicus Curiae Committee of the Defense Association of New York, Inc.*, and *Heather Wiltshire Clement, Defense Association of New York, Inc.*, for Defense Association of New York, Inc., amicus curiae. I. Summary judgment is appropriate only when no triable issues of fact remain for a jury to resolve. (Nicholas Di Menna & Sons, Inc. v City of New York, 301 NY 118, 92 NE2d 918; Fredburn Constr. Corp. v City of New York, 280 NY 402, 21 NE2d 370; Friends of Animals v Associated Fur Mfrs., 46 NY2d 1065, 390 NE2d 298, 416 NYS2d 790; Zuckerman v City of New York, 49 NY2d 557, 404 NE2d 718, 427 NYS2d 595; Andre v Pomeroy, 35 NY2d 361, 320 NE2d 853, 362 NYS2d 131; Sillman v Twentieth Century-Fox Film Corp., 3 NY2d 395, 144 NE2d 387, 165 NYS2d 498; Winegrad v New York Univ. Med. Ctr., 64 NY2d 851, 476 NE2d 642, 487 NYS2d 316; Ritt v Lenox Hill Hosp., 182 AD2d 560, 582 NYS2d 712; Friends of Thayer Lake LLC v Brown, 27 NY3d 1039, 33 NYS3d 853, 53 NE3d 730.) II. Requiring a plaintiff to demonstrate both the defendant's negligence and freedom from contributory negligence prima facie promotes fairness and conserves judicial resources. (Solomon v City of New York, 66 NY2d 1026, 489 NE2d 1294, 499 NYS2d 392; Derdiarian v Felix Contr. Corp., 51 NY2d 308, 414 NE2d 666, 434 NYS2d 166; Nallan v Helmsley-Spear, Inc., 50 NY2d 507, 407 NE2d 451, 429 NYS2d 606; Vanderhurst v Nobile, 130 AD3d 716, 13 NYS3d 231; *Koulermos v A.O. Smith Water Prods., 137 AD3d 575, 27 NYS3d 157*; Rodrigues v Lesser, 136 AD3d 1322, 24 NYS3d 816; Schillaci v Sarris, 122 AD3d 1085, 997 NYS2d 504; Jacobsen v New York City Health & Hosps. Corp., 22 NY3d 824, 988 NYS2d 86, 11 NE3d 159; Valerio v Terrific Yellow Taxi Corp., 149 AD3d 1140, 50 NYS3d 882; *Macaluso v Pilcher, 145 AD3d 1559, 43 NYS3d 658*.) III. If this Court should adopt the dissent's view, then statutory interest should not run from such an award.

Judges: FEINMAN, J. Opinion by Judge Feinman. Judges Rivera, Fahey and Wilson concur. Judge Garcia dissents in an opinion in which Chief Judge DiFiore and Judge Stein concur.

Opinion by: FEINMAN

Opinion

[*899] [**367] [*315]** Feinman, J.

This appeal requires us to answer a question that has perplexed courts for some time: Whether a plaintiff is entitled to partial summary judgment on the issue of a defendant's liability, when, as here, defendant has arguably raised an issue of fact regarding plaintiff's comparative negligence. Stated differently, to obtain partial summary judgment in a comparative negligence case, must plaintiffs establish the absence of their own comparative negligence. We hold that a plaintiff does not bear that burden.

I.

Plaintiff Carlos Rodriguez was employed by the New York City Department of Sanitation (DOS) as a garage utility worker. He was injured while "outfitting" sanitation trucks with tire chains and plows to enable them to clear the streets of snow and ice. The following facts are uncontradicted: On a snowy winter day, plaintiff and his two coworkers were tasked with outfitting sanitation trucks **[****2]** with tire chains and plows at the Manhattan 5 facility. Typically, the driver backs the truck into one of the garage bays, and the driver and other members of the team **[2]** "dress" the truck. One person acts as a guide, assisting the driver by providing directions through appropriate hand signals while standing on the passenger's side of the truck. Once the truck is safely parked in the garage, the driver, the guide, and the third member of the team (here, plaintiff) place chains on the truck's tires.

At the time of his accident, plaintiff was standing between the front of a parked Toyota Prius and a rack of tires outside of the garage bay while the driver began backing the sanitation truck into the garage. The guide, at some point, stood on the *driver's* side of the sanitation truck while directing the driver in violation of established DOS safety practices. The sanitation truck began skidding and eventually crashed into the front of the parked Toyota Prius, propelling the car into plaintiff and pinning him up against the rack of tires. Plaintiff was taken to the hospital and ultimately had to undergo spinal fusion surgery, a course of lumbar epidural steroid injections, and extensive physical **[****3] [**368] [***900]** therapy. He is permanently disabled from working.

[*316] Plaintiff commenced this negligence action against the City of New York. After discovery, he moved for partial summary judgment on the issue of defendant's liability pursuant to CPLR 3212. Defendant opposed the motion and cross-moved for summary judgment in its favor. Supreme Court denied both motions. In denying plaintiff's motion for partial summary judgment, Supreme Court held that there were triable issues of fact regarding foreseeability, causation, and plaintiff's comparative negligence.[1]

The Appellate Division, among other things, affirmed the denial of plaintiff's motion for partial summary judgment (*Rodriguez v City of New York, 142 AD3d 778, 37 NYS3d 93 [1st Dept 2016]*). The majority, relying on this Court's memorandum decision in *Thoma v Ronai (82 NY2d 736, 621 NE2d 690, 602 NYS2d 323 [1993])*, held that plaintiff was not entitled to partial summary judgment on the issue of liability, because he failed to make a prima facie showing that he was free of comparative negligence. The dissent, relying on the language and purpose of *CPLR article 14-A*, would have held that plaintiff does not bear the burden of disproving the affirmative defense of comparative negligence, and thus, plaintiff should have been granted partial summary judgment on the issue of defendant's liability (*Rodriguez, 142 AD3d at 797 [Acosta, J.*, **[****4]** dissenting]).

The Appellate Division granted plaintiff leave to appeal to this Court (*lv granted* 2016 NY Slip Op 96039[U] [1st Dept 2016]), certifying the following question: "Was the order of Supreme Court, as affirmed by this Court, properly made?"[2]

[*317] [3] II.

Whether a plaintiff must demonstrate the absence of his or her own comparative negligence to be entitled to partial summary judgment as to a defendant's **[**369] [***901]** liability is a question of statutory construction of the CPLR. The usual rules of statutory construction apply to the provisions of the CPLR (*see e.g. Chianese v Meier, 98 NY2d 270, 275, 774 NE2d 722, 746 NYS2d 657 [2002]*). "In matters of statutory interpretation, our primary consideration is to discern and give effect to the Legislature's intention" (*Matter of Albany Law School v New York State Off. of Mental Retardation & Dev. Disabilities, 19 NY3d 106, 120, 968 NE2d 967, 945 NYS2d 613 [2012]*). We look "first to the plain language of the statute[ ] as the best evidence of legislative intent" (*Matter of Malta Town Ctr. I, Ltd. v Town of Malta Bd. of Assessment Review, 3 NY3d 563, 568, 822 NE2d 331, 789 NYS2d 80 [2004]*).

CPLR 3212, which governs summary judgment motions,

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[1] Defendant moved for summary judgment on the ground that an employee cannot recover for injuries sustained while doing an assigned job, the purpose of which is to eliminate the cause of the injury. However, Supreme Court disagreed and held that defendant was not entitled to dismissal of the complaint, because contrary to defendant's assertion, "the danger of being knocked down by a skidding sanitation vehicle is not an ordinary and obvious hazard of plaintiff's employment," nor is it "inherent in the work of a sanitation worker" (*Rodriguez v City of New York, 2014 N.Y. Misc. LEXIS 6059, 2014 NY Slip Op 33650[U], *7, 2014 WL 10726797, at *2 [Sup Ct, NY County, Oct. 16, 2014, No. 109444/2011, Freed, J.]*). The propriety of this ruling is not before us as defendant did not cross-appeal Supreme Court's order.

[2] Defendant additionally argues that material issues of fact exist as to its negligence, which bar plaintiff from obtaining partial summary judgment. We do not reach this issue.

The Appellate Division began its analysis by framing the sole issue for resolution as "whether a plaintiff seeking summary judgment on the issue of liability must establish, as a matter of law, that he or she is free from comparative fault" (*Rodriguez, 142 AD3d at 778*). To be sure, Supreme Court addressed the issue of defendant's negligence and agreed with defendant that there are questions of fact as to foreseeability and causation. We do not read the Appellate Division's majority decision as reaching the merits of whether there is any question of fact as to defendant's negligence. Both the majority and dissenting opinions at the Appellate Division framed their resolution of this appeal as turning on whether plaintiff bore the burden of proving the absence of comparative negligence. Although the majority's five-page decision contains one sentence that makes a passing reference to defendant's negligence, it is utilized to distinguish a prior case on the issue of comparative negligence as a bar to summary judgment and is not offered as an evaluation of the merits of defendant's alternative argument.

provides that "[t]he motion shall be granted if . . . the cause of action . . . [is] established sufficiently to warrant the court as a matter of law in directing judgment in favor of any party" (CPLR 3212 [b]). The motion for summary judgment must also "show that there is no defense to the cause of action" (*id.*). Further, subdivision (c) of the same section sets forth the procedure for obtaining partial summary **[****5]** judgment and states that "[i]f it appears that the only triable issues of fact arising on a motion for summary judgment relate to the amount or extent of damages . . . the court may, when appropriate for the expeditious disposition of the controversy, order an immediate trial of such issues of fact raised by the motion" (CPLR 3212 [c]).

Article 14-A of the CPLR contains our State's codified comparative negligence principles. CPLR 1411 provides that

> "[i]n any action to recover damages for personal injury, injury to property, or wrongful death, the **[*318]** culpable conduct attributable to the claimant or to the decedent, including contributory negligence or assumption of risk, *shall not bar recovery*, but the amount of damages otherwise recoverable shall be diminished in the proportion which the culpable conduct attributable to the claimant or decedent bears to the culpable conduct which caused the damages." (Emphasis added.)

CPLR 1412 further states that "[c]ulpable conduct claimed in diminution of damages, in accordance with [CPLR 1411], shall be an affirmative defense to be pleaded and proved by the party asserting the defense."

Placing the burden on the plaintiff to show an absence of comparative fault is inconsistent with the plain language of CPLR 1412. In 1975, **[****6]** New York adopted a system of pure comparative negligence, and, in so doing, directed courts to consider a plaintiff's comparative fault only when considering the amount of damages a defendant owes to plaintiff. The approach urged by defendant is therefore at odds with the plain language of CPLR 1412, **[4]** because it flips the burden, requiring the plaintiff, instead of the defendant, to prove an absence of comparative fault in order to make out a prima facie case on the issue of defendant's liability.[3]

[3] Various commentators have pointed out this inconsistency. The late Professor David Siegel, a preeminent expert in New York civil practice, has referred to the approach defendant proposes as "peculiar," for it "imposes on the plaintiff the burden of establishing . . . freedom from comparative fault even though by statute that's a burden of both pleading and proof borne by the defendant under the specific terms of CPLR 1412" (Siegel, NY Prac § 280 [5th ed 2011, Jan. 2013 Update]).

Professor Patrick Connors similarly notes:

> "CPLR 1412 and the standards of summary judgment appear to require that defendant tender sufficient evidence to support the affirmative defense on the facts of the case. Requiring the plaintiff moving for partial summary judgment on liability to affirmatively establish complete freedom from comparative fault, while allowing defendant to simply contend that plaintiff has committed at least some culpable conduct, appears to tilt the scales too favorably for the defendant" (Patrick M. Connors, *Can Comparative Fault Stop the Train Known as Summary Judgment?*, NYLJ, Jan. 16, 2013 at 3, col 1, at 8, col 3).

Finally, John R. Higgitt writes in the Practice Commentaries to CPLR 3212 that the approach favored by Siegel and Connors, which he refers to as the "Siegel approach," has appeal for at least two reasons. First, he notes:

> "CPLR 1411's language suggests that a plaintiff seeking partial summary judgment on the issue of the defendant's liability should not have the burden of showing her freedom from comparative fault . . . If a plaintiff's comparative fault 'shall not bar recovery' but merely diminishes her damages award, then it would seem that the plaintiff should not be required to prove her freedom from comparative fault as a precondition to obtaining partial summary judgment on the issue of the defendant's liability" (John R. Higgitt, Supp Practice Commentaries, McKinney's Cons Laws of NY, CPLR C3212:15).

Secondly, he contends that "the Siegel approach provides for harmony between the substantive law of torts and the rules of decision on a plaintiff's motion for partial summary judgment" (*id.*). Higgitt writes:

> "A plaintiff is entitled to recover damages in a negligence action if she demonstrates that a defendant's negligence was 'a' proximate cause of the plaintiff's injuries, i.e., that the defendant's negligence was one, not necessarily the only, substantial factor in causing the injuries. Thus, a plaintiff's right of recovery arises on her showing that the defendant was negligent and that the defendant's negligence was a proximate cause of the plaintiff's injuries, and any comparative fault on the plaintiff's part will merely diminish the damages award.
>
> "Under the present rule reflected in the decisions of the First and Second Departments, a plaintiff seeking partial summary judgment on the issue of the defendant's liability is required to prove her freedom from comparative fault. That doesn't seem to jibe with the rule of

[370] [*319] [***902]** Defendant's approach also defies the plain language of CPLR 1411, and, if adopted, would permit a possible **[5]** windfall to defendants. CPLR 1411 explicitly provides that "[i]n any action to recover damages for personal injury . . . the culpable conduct attributable to the [plaintiff] . . . shall not bar recovery, but the amount of damages otherwise recoverable shall be diminished in the proportion . . . attributable to the claimant." For example, assuming in a hypothetical case a defendant's negligence could be established as a matter of law because defendant's conduct was in violation of a statute (*see* PJI 2:26) and further assuming plaintiff was denied **[****7]** partial summary judgment on the issue of defendant's negligence because plaintiff failed to establish the absence of his or her own comparative negligence, the jury would be permitted to decide the question of whether defendant was negligent and whether defendant's negligence proximately caused plaintiff's injuries. If the jury answers in the negative on the question of defendant's negligence, the plaintiff would be barred from recovery even though defendant's negligence was established as a matter of law and in contradiction to the plain language of CPLR 1411. **[*320]** Such a windfall to a defendant would violate section 1411's mandate that a plaintiff's comparative negligence "shall not bar recovery" and should only go to the diminution of damages recoverable by plaintiff. Furthermore, it is no answer to this conundrum that the trial court could set aside the verdict. The whole purpose of partial summary judgment is to streamline and focus the factfinder on the issues that need resolution, and avoid having juries make findings that are contrary to law.

[371] [***903]** Defendant's attempts to rely on CPLR 3212's plain language in support of its preferred approach are also unavailing. Specifically, defendant points to CPLR 3212 (b), which provides: **[****8]** "[a] motion for summary judgment shall . . . show that there is no defense to the cause of action." Defendant's approach would have us consider comparative fault a defense. But, comparative negligence is *not* a defense to the cause of action of negligence, because it is not a defense to any element (duty, breach, causation) of plaintiff's prima facie cause of action for negligence, and as CPLR 1411 plainly states, is not a bar to plaintiff's recovery, but rather a diminishment of the amount of damages.

The approach we adopt is also supported by the legislative history of article 14-A (*see* Matter of Tompkins County Support Collection Unit v Chamberlin, 99 NY2d 328, 335, 786 NE2d 14, 756 NYS2d 115 [2003] ["(T)he legislative history of an enactment may also be relevant and is not to be ignored, even if words be clear" (internal quotation marks and citations omitted)]). Article 14-A's enactment was proposed by the 1975 Judicial Conference of the State of New York (the Conference) in response to this Court's decision in Dole v Dow Chem. Co. (30 NY2d 143, 282 NE2d 288, 331 NYS2d 382 [1972]), which first provided for the apportionment of negligent responsibility among joint tortfeasors. In proposing the section which later became CPLR 1411, the Conference specifically noted that neither the defense of contributory negligence or assumption of risk "shall continue to serve as complete defenses" in negligence **[****9]** actions (21st Ann Rep of NY Jud Conf at 240). In proposing the section which became CPLR 1412, the Conference urged the adoption of the then-majority rule in this country, which provided that "in all negligence actions . . . the defendant claiming contributory negligence of the plaintiff has the burden of showing it" (*id.* at 245). The Conference also observed that the "burden of pleading and burden of proof are usually parallel" and that "[t]his article may be viewed as having created a partial defense, the effect of which is to mitigate damages, and **[*321]** such defenses traditionally must be pleaded affirmatively" (*id.* at 246).

When article 14-A was proposed in the legislature, the Introducer's Memorandum before the New York Assembly noted that the then-current system of traditional contributory negligence had "become an obstacle to the dispensing of substantial justice" (Assembly Introducer's Mem in Support at 1, Bill Jacket, L 1975, ch 69). The purpose of the law was to bring "New York law into conformity with the majority rule and represents the culmination of the gradual but persistent erosion of the rule that freedom from contributory negligence must be pleaded and proven by the plaintiff" (*id.*, citing Rossman v La Grega, 28 NY2d 300, 304, 270 NE2d 313, 321 NYS2d 588 [1971]). The legislative history of article **[****10]** 14-A makes clear that a plaintiff's comparative negligence is no longer a complete defense and its absence need not be pleaded and proved by the plaintiff, but rather is only relevant to the mitigation of plaintiff's damages and should be

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substantive law providing that a plaintiff is entitled to recover once she establishes that the defendant was negligent and that the defendant's negligence was a proximate cause of the plaintiff's injuries" (*id.* [citation omitted]).

pleaded and proved by the defendant.[4]

[372] [***904]** Resolution of the issue before us necessarily turns on the interpretation and interplay of these various CPLR provisions. In *Thoma v Ronai (82 NY2d 736, 621 NE2d 690, 602 NYS2d 323 [1993]*), this Court held that the plaintiff there did not meet her burden of demonstrating the absence of any material fact; "a factual question of her reasonable care" existed, and thus plaintiff was properly denied summary judgment (*id. at 737*). However, *Thoma* never addressed **[*322]** the precise question we now confront. The decision itself never considered the import of article 14-A, and a review of the briefs publicly filed in that case reveal that the plaintiff proceeded on the assumption that if a question of fact existed as to her negligence, summary judgment on the issue of liability would be denied. The plaintiff in *Thoma,* in her limited submissions to this Court, maintained that "[t]he crux of the case is the existence, as a matter of law, of any question of culpable conduct (contributory negligence) by the **[****11]** Plaintiff that would warrant the Trial Court's denial of summary judgment pursuant to *C.P.L.R. § 3212* on the issue of Defendant's liability" (brief for plaintiff-appellant in *Thoma* at 1). Thus, to the extent that the Departments of the Appellate Division have interpreted *Thoma* as explicitly holding that a plaintiff must show an absence of comparative fault in order to obtain partial summary judgment on liability, such a reading of *Thoma* is mistaken (*see Global Reins. Corp. of Am. v Century Indem. Co., 30 NY3d 508, 517, 69 NYS3d 207, 91 NE3d 1186 [2017]* ["(T)he Court's holding comprises only those 'statements of law which address issues which were presented to the (Court) for determination' "], quoting *Village of Kiryas Joel v County of Orange, 144 AD3d 895, 900, 43 NYS3d 51 [2d Dept 2016])*.[5]

[4] The dissent points to recently proposed amendments to *CPLR 1412*, explicitly pronouncing that the party asserting the defense of comparative negligence must interpose proof of such culpable conduct when asserting the defense on a motion for summary judgment, to contend that the legislature is "under the impression" that *Thoma* is the correct and currently binding rule (*see* dissenting op at 328, citing 2017 NY Senate-Assembly Bill S2057, A2776; 2016 Senate Bill S7779). However, "we have often been reluctant to ascribe persuasive significance to legislative inaction" (*Desrosiers v Perry Ellis Menswear, LLC, 30 NY3d 488, 497, 68 NYS3d 391, 90 NE3d 1262 [2017]*, quoting *Boreali v Axelrod, 71 NY2d 1, 13, 517 NE2d 1350, 523 NYS2d 464 [1987]*; *see also Pension Benefit Guaranty Corporation v LTV Corp., 496 US 633, 650, 110 S Ct 2668, 110 L Ed 2d 579 [1990]* ["Congressional inaction lacks persuasive significance because several equally tenable inferences may be drawn from such inaction, including the inference that the existing legislation already incorporated the offered change" (internal quotation marks omitted)]). While at times, we have construed legislative inaction "to be some manifestation of legislative approbation" of a lower's court's interpretation of a particular statute, that is only the case in "instances in which the legislative inactivity has continued in the face of a prevailing statutory construction" (*Desrosiers, 30 NY3d at 497*; *Brooklyn Union Gas Co. v New York State Human Rights Appeal Bd., 41 NY2d 84, 90, 359 NE2d 393, 390 NYS2d 884 [1976])*. That is not the case here, where the Appellate Division Departments have struggled to adopt a universal interpretation.

[5] The dissenters question our assessment of *Thoma* and assert that our interpretation is "undermined by later case law" (dissenting op at 326). The dissent maintains that in our memorandum decision in *Sammis v Nassau/Suffolk Football League (95 NY2d 809, 810, 732 NE2d 941, 710 NYS2d 834 [2000])*, and summary reversal in *Castiglione v Kruse (27 NY3d 1018, 1019, 32 NYS3d 579, 52 NE3d 243 [2016]*, *rearg denied* ***28 NY3d 941, 38 NYS3d 509, 60 NE3d 403 [2016])***, we reaffirmed the purported procedural rule created by *Thoma*. Notably missing from either of those decisions is any discussion or even citation to *Thoma*. In fact, it appears this Court has never cited *Thoma* for any proposition whatsoever. Neither *Sammis* nor *Castiglione* addressed whether the CPLR requires plaintiffs to show an absence of comparative fault in order to obtain partial summary judgment on the issue of liability. Further, while we reversed the Appellate Division in *Castiglione*, holding that "triable questions of fact preclud[ed] summary judgment in plaintiff's favor" (*27 NY3d at 1019*), it is not at all clear whether such questions of fact related to comparative negligence, the defendant's negligence, or some other issue related to liability. Contrary to the dissenters' view, neither *Thoma* nor these subsequent decisions created a procedural rule placing the burden on plaintiffs to show an absence of comparative fault in order to obtain partial summary judgment on the issue of defendant's liability.

It bears noting that initially courts did not even treat *Thoma* as creating a new rule requiring that plaintiffs show an absence of comparative negligence in order to obtain partial summary judgment on the issue of a defendant's liability. Indeed, at least in the First Department, a majority of the appellate decisions initially refrained from putting such a burden on plaintiffs even after *Thoma* (***see e.g. Pace v Robinson, 88 AD3d 530, 930 NYS2d 581 [1st Dept 2001]***; *Gonzalez v ARC Interior Constr., 83 AD3d 418, 921 NYS2d 33 [1st Dept 2011]*; *Strauss v Billig, 78 AD3d 415, 909 NYS2d 724 [1st Dept 2010]*; *Tselebis v Ryder Truck Rental, Inc., 72 AD3d 198, 895 NYS2d 389 [1st Dept 2010])*. These decisions reasoned, as articulated in *Tselebis*, that placing the burden on plaintiffs to show freedom from comparative negligence as a component of their prima facie showing on summary judgment "cannot be

[373]** **[*323]** **[***905]** On this appeal, plaintiff raises the issue not addressed in *Thoma*. Plaintiff contends, even assuming there is an issue of fact regarding his comparative fault, that he is entitled to partial summary judgment on the issue of defendant's liability. Defendant would have us follow the line of cases that hold that plaintiff bears the burden of disproving comparative fault as a component of establishing his prima facie entitlement to partial summary judgment on the issue of **[****12]** defendant's liability. Defendant points to various instances of plaintiff's conduct in this case and asserts that plaintiff was comparatively negligent. We agree with plaintiff that to obtain partial summary judgment on defendant's liability he does not have to demonstrate the absence of his own comparative fault.

We also reject defendant's contention that granting the plaintiff partial summary judgment on defendant's liability serves no practical purpose. A principal rationale of partial summary judgment is to narrow the number of issues presented **[*324]** to the jury (*see* Janos v Peck, 21 AD2d 529, 531, 251 NYS2d 254 [1964], *affd* 15 NY2d 509, 202 NE2d 560, 254 NYS2d 115 [1964]). In a typical comparative negligence trial, the jury is asked to answer five questions:

> 1. Was the defendant negligent?
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> 2. Was defendant's negligence a substantial factor in causing (the injury or the accident)?
>
> **[**374]** **[***906]** 3. Was plaintiff negligent?
>
> 4. Was plaintiff's negligence a substantial factor in causing (his or her) own injuries?
>
> 5. What was the percentage of fault of the defendant and what was the percentage of fault of the plaintiff?

(PJI 2:36). Where plaintiff has already established defendant's liability as a matter of law, granting plaintiff partial judgment eliminates the first two questions submitted to the jury, thereby **[****13]** serving the beneficial purpose of focusing the jury on questions and issues that are in dispute.

Nor do we agree with defendant that what it characterizes as bifurcation of the issues of defendant's liability from plaintiff's liability runs counter to the Pattern Jury Instructions. When a defendant's liability is established as a **[6]** matter of law before trial, the jury must still determine whether the plaintiff was negligent and whether such negligence was a substantial factor in causing plaintiff's injuries. If so, the comparative fault of each party is then apportioned by the jury. Therefore, the jury is still tasked with considering the plaintiff's and defendant's culpability together. As a practical matter, a trial court will instruct the jury in a modified version of Pattern Jury Instruction 1:2B that the issue of defendant's negligence, and in some cases, the related proximate cause question, have been previously determined as a matter of law. Trial courts are experienced in crafting such instructions, for example when liability has already been determined in a bifurcated trial, or when an Appellate Division upholds a liability determination and remands solely for a recalculation **[****14]** of damages, or a trial on damages has been ordered pursuant to CPLR 3212 (c).

III.

To be entitled to partial summary judgment a plaintiff does not bear the double burden of establishing a prima

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reconciled" with CPLR 1411 and 1412 "if the statute[s] [are] to be given effect" (*Tselebis, 72 AD3d at 200*).

However, in *Roman v A1 Limousine, Inc. (76 AD3d 552, 907 NYS2d 251 [2d Dept 2010])*, the Second Department parted company with the First Department. That Court explicitly read *Thoma* as creating such a procedural rule, and held that "plaintiff's motion for summary judgment on the issue of liability was properly denied where the plaintiff's submissions failed to eliminate a triable issue of fact regarding her comparative negligence" (*id. at 553*). Since *Roman*, the clear majority (but not all) of Second Department cases have relied on *Thoma* as answering this issue, and have placed the "double burden" on plaintiffs to not only prove the defendant's prima facie negligence as a matter of law, but also prove their own absence of comparative negligence as a matter of law in order to obtain partial summary judgment on the issue of liability.

After *Roman*, the First Department began to reconsider its holding in *Tselebis*, but it appears to remain sharply divided internally over the issue (*see e.g. Calcano v Rodriguez, 91 AD3d 468, 936 NYS2d 185 [1st Dept 2012, Catterson, J.*, concurring]; *Maniscalco v New York City Tr. Auth., 95 AD3d 510, 943 NYS2d 486 [1st Dept 2012, DeGrasse, J.*, dissenting]; *Capuano v Tishman Constr. Corp., 98 AD3d 848, 950 NYS2d 517 [1st Dept 2012, Acosta, J.*, concurring]; *Geralds v Damiano, 128 AD3d 550, 10 NYS3d 38 [1st Dept 2015, Moskowitz, J.*, dissenting]). The Fourth Department recently held in *Simoneit v Mark Cerrone, Inc. (122 AD3d 1246, 996 NYS2d 810 [4th Dept 2014])*, that a plaintiff was entitled to partial summary judgment on the issue of defendant's liability, notwithstanding unresolved questions of fact regarding the plaintiff's comparative fault (*see id. at 1248*).

facie case of **[*325]** defendant's liability and the absence of his or her own comparative fault. Accordingly, the order of the Appellate Division, insofar as appealed from, should be reversed, with costs, and the case remitted to the Appellate Division for consideration of issues raised but not determined on the appeal to that Court and the certified question answered in the negative.

Dissent by: GARCIA

Dissent

Garcia, J. (dissenting). The majority holds that plaintiff's motion for partial summary judgment on liability was improperly denied, notwithstanding issues of fact as to plaintiff's comparative negligence. We disagree. The rule has been, and should remain, that a plaintiff must demonstrate the absence of issues of fact concerning both defendant's negligence and its own comparative fault in order to obtain summary judgment (*see Thoma v Ronai, 82 NY2d 736, 621 NE2d 690, 602 NYS2d 323 [1993])*.

Plaintiff's injury occurred while he was working in a New York City Department of Sanitation garage, as he and his colleagues outfitted sanitation trucks with tire chains and a plow in order to clear snow **[****15]** and ice from the City streets. With the storm ongoing, plaintiff's colleagues were backing a truck into the Department's garage bay when the truck slid several feet and hit a parked car, which skidded forward and hit plaintiff.

Supreme Court rejected both parties' summary judgment motions. In rejecting plaintiff's motion, the court found that there were triable issues of fact as to the City's liability, specifically with respect to causation and foreseeability, as well as plaintiff's comparative fault. The court noted that "[f]oreseeability questions are generally left for the fact finder to resolve" **[**375] [***907]** (*2014 NY Slip Op 33650[U], *7 [Sup Ct, NY County 2014]*, citing *Derdiarian v Felix Contr. Corp., 51 NY2d 308, 315, 414 NE2d 666, 434 NYS2d 166 [1980])* and that numerous issues of fact remained concerning causation. In addition, the court found that even if defendant's liability was established, "plaintiff would not be entitled to summary judgment as to liability since the question of his comparative fault must be resolved at trial" (*2014 NY Slip Op 33650[U], *8*).

The Appellate Division upheld Supreme Court's finding of triable issues concerning defendant's negligence. After reviewing the facts, the Appellate Division held that "[u]nder this factual scenario, the trier of fact could determine *that defendant was free from negligence* and that plaintiff was 100% **[****16]** at fault in causing his injuries" (*142 AD3d 778, 781 [1st Dept 2016]* [emphasis added]). The majority dismisses this aspect of **[*326]** the Appellate Division's holding as a "passing reference," and, without explanation, determines that this statement "is not offered as an evaluation of the merits of defendant's alternative argument" (majority op at 317 n 2). Here, where the holding of two lower courts calls into question plaintiff's demonstration of defendant's liability as a matter of law, the majority's summary dismissal of this **[7]** issue is inadequate.[1] In any event, as discussed below, the fact that the City was found to have created an issue of fact as to any liability on its part highlights the unreasonableness of the majority's approach.

Even assuming plaintiff demonstrated the City's liability as a matter of law, our case law requires, as the Appellate Division majority held, that plaintiff's motion for summary judgment be denied. In *Thoma v Ronai*, the Appellate Division denied summary judgment to plaintiff, a pedestrian struck by a car while "lawfully in [a] crosswalk," finding that although plaintiff's "comparative negligence may be found by a jury to be minimal, or even zero . . . the record does not support our finding **[****17]** a total absence of comparative negligence as a matter of law" *(189 AD2d 635, 635-636, 592 NYS2d 333 [1st Dept 1993])*. This Court affirmed, holding that plaintiff was not entitled to summary judgment because "[she] did not satisfy her burden of demonstrating the absence of any material issue of fact," namely the "factual question of her reasonable care" *(82 NY2d 736, 737, 621 NE2d 690, 602 NYS2d 323 [1993])*. The majority rejects *Thoma*'s holding

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[1] The majority "do[es] not reach" the issue of whether plaintiff demonstrated defendant's negligence as a matter of law (majority op at 316 n 2). In fact, this question is a preserved issue of law. The majority asserts that the Appellate Division "fram[ed as] the sole issue for resolution" the question "whether a plaintiff seeking summary judgment on the issue of liability must establish, as a matter of law, that he or she is free from comparative fault" (*id.* at 316-317 n 2). This is not correct. The Appellate Division certified the question "[w]as the order of Supreme Court, as affirmed by this Court, properly made?" (*2016 NY Slip Op 96039[U] [1st Dept 2016]*.) Accordingly, Supreme Court's ruling that plaintiff did not demonstrate defendant's negligence as a matter of law, and the Appellate Division's affirmance on that issue, is properly before us.

because it does not explicitly "address[ ] [the relevant] CPLR provisions" and presumes that it "never considered the import of article 14-A" (majority op at 321-322). But this questionable assessment of the *Thoma* holding is undermined by later case law. In *Sammis v Nassau/Suffolk Football League*, we reiterated the *Thoma* rule, denying partial summary judgment to plaintiff because "[o]n this record, there exist issues of fact as to comparative fault for a fact finder to consider pursuant to CPLR 1411" (95 NY2d 809, 810, **[*327]** 732 NE2d 941, 710 NYS2d 834 [2000]). **[**376]** **[***908]** More recently, we reviewed a decision of the Appellate Division that, in granting plaintiff's summary judgment motion, attempted to distinguish *Thoma* because "plaintiffs established that the defendant driver was negligent and that the injured plaintiff was free from comparative fault" (Castiglione v Kruse, 130 AD3d 957, 958, 15 NYS3d 360 [2d Dept 2015]). The dissent, in rejecting summary judgment, asserted that the majority "fail[ed] to correctly apply **[****18]** controlling precedent from the Court of Appeals," namely *Thoma*'s assessment of a pedestrian's comparative negligence in failing to "look to the sides" while crossing the street (id. at 960-961 [Dillon, J., dissenting]). We reversed, holding that "triable questions of fact preclude summary judgment in plaintiffs' favor" (Castiglione v Kruse, 27 NY3d 1018, 1019, 32 NYS3d 579, 52 NE3d 243 [2016]). The rule set out is clear, and speculation as to what the Court "considered"—or in other words, the suggestion that we did not mean what we said—does not mask the fact that the majority is overruling this line of cases.

Accordingly, the issue of whether a plaintiff is entitled to summary judgment without showing freedom from comparative fault is settled, and the Appellate Division Departments have, for the most part, been applying that precedent. Since *Thoma*, each Department has held that a plaintiff is precluded from obtaining summary judgment where issues of fact exist concerning comparative fault (*see e.g. Piscitello v Fortress Trucking, Ltd., 118 AD3d 1441, 988 NYS2d 784 [4th Dept 2014]*; *Calcano v Rodriguez, 91 AD3d 468, 936 NYS2d 185 [1st Dept 2012]*; *Roman v A1 Limousine, Inc., 76 AD3d 552, 907 NYS2d 251 [2d Dept 2010]*; *Rigney v Ichabod Crane Cent. School Dist., 59 AD3d 842, 874 NYS2d 280 [3d Dept 2009]*). Moreover, in other contexts, each Department has ruled that a plaintiff has the burden of demonstrating the absence of issues of fact as to affirmative defenses to obtain summary judgment (*see e.g. Morley Maples, Inc. v Dryden Mut. Ins. Co., 130 AD3d 1413, 14 NYS3d 579 [3d Dept 2015]*; *Ahmad v City of New York, 129 AD3d 443, 444, 11 NYS3d 27 [1st Dept 2015]*; *Jessabell Realty Corp. v Gonzales, 117 AD3d 908, 909, 985 NYS2d 897 [2d Dept 2014]*; *Birt v Ratka, 39 AD3d 1238, 1239, 835 NYS2d 781 [4th Dept 2007]*). Conversely, the majority's **[8]** approach, granting summary **[****19]** judgment without eliminating issues of fact concerning plaintiff's comparative fault, has only been taken by a minority of judges in the First Department (*Gonzalez v ARC Interior Constr., 83 AD3d 418, 921 NYS2d 33 [1st Dept 2011]*; *Tselebis v Ryder Truck Rental, Inc., 72 AD3d 198, 895 NYS2d 389 [1st Dept 2010]*; *Strauss v Billig, 78 AD3d 415, 909 NYS2d 724 [1st Dept 2010]*), and has been expressly **[*328]** rejected within the First Department since those cases (*see Calcano, 91 AD3d at 469* ["Although this Court departed from the *Thoma* holding in *Tselebis* . . . we respectfully decline to follow *Tselebis*"]).[2]

Similarly, the legislature is under the impression that *Thoma* is the applicable rule and has declined to change it.[3] Attempts **[**377]** **[***909]** have been made

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[2] This approach has been partially followed in the Fourth Department, with some courts granting partial summary judgment on defendant's breach of the duty of care, but leaving for the jury the question of proximate cause (*Simoneit v Mark Cerrone, Inc., 122 AD3d 1246, 1248, 996 NYS2d 810 [4th Dept 2014]*).

[3] The majority cites *Desrosiers v Perry Ellis Menswear, LLC (30 NY3d 488, 497, 68 NYS3d 391, 90 NE3d 1262 [2017])* for the principle that "we have often been reluctant to ascribe persuasive significance to legislative inaction," but more relevant language follows, distinguishing

> "instances in which the legislative inactivity has continued in the face of a prevailing statutory construction. . . . Stated another way, it is a recognized principle that where a statute has been interpreted by the courts, the continued use of the same language by the Legislature subsequent to the judicial interpretation is indicative that the legislative intent has been correctly ascertained" (*id.* [internal quotation marks and citations omitted]).

This is particularly true where " 'the Legislature, with presumed knowledge of the judicial construction of a statute, [forgoes] specific invitations and requests to amend its provisions to effect a different result' " (*id.*, quoting *Matter of Alonzo M. v New York City Dept. of Probation, 72 NY2d 662, 667, 532 NE2d 1254, 536 NYS2d 26 [1988]*). Here, the legislative history in support of these amendments specifically refers to our prior determination and provides that "this amendment would not overrule *Thoma*" (Mem in Support, 2017 NY Assembly Bill A2776).

to amend the comparative fault statute to place on a defendant opposing summary judgment "the burden of interposing proof of culpable conduct" (*see* 2017 NY Senate Bill S2057; 2016 NY Senate Bill S7779; *see also* Mem in Support, 2017 NY Assembly Bill A2776 [proposing amendment to impose on defendant at summary judgment the burden of producing enough evidence of plaintiff's comparative fault to raise a genuine issue of fact]). Such attempts at legislative reform would be unnecessary if plaintiffs were entitled to summary judgment despite the existence of issues of fact concerning comparative fault. As defendant points out, these proposed bills would still preclude **[****20]** summary judgment where "defendant presents evidence of plaintiff's comparative fault sufficient to raise a question of fact" after a plaintiff has demonstrated defendant's liability as a matter of law (*see* Mem in Support, 2017 NY Assembly Bill A2776). The majority's approach goes well beyond these proposals, enabling a plaintiff to obtain summary judgment even where, as happened here, a defendant **[*329]** has demonstrated that plaintiff's comparative fault may be significant.

The *Thoma* rule, denying summary judgment where there are triable issues concerning comparative fault, is not only the established rule, it is the fairer outcome. We have previously held that comparative fault must be **[9]** analyzed from a holistic perspective (*see* *Arbegast v Board of Educ. of S. New Berlin Cent. School, 65 NY2d 161, 168-169, 480 NE2d 365, 490 NYS2d 751 [1985]* [the comparative fault analysis requires a court to consider "the culpable conduct attributable to the (plaintiff as) compared with the total culpable conduct which caused the damages" and to "fix the relationship of each party's conduct to the injury sustained"]). Determinations of degrees of fault should be made as a whole, and assessing one party's fault with a preconceived idea of the other party's liability is inherently unfair; or, as the Appellate Division **[****21]** characterized it, a defendant would "enter[ ] the batter's box with two strikes already called" (*142 AD3d at 782*). Indeed, as the Appellate Division also noted, the Pattern Jury Instructions advise that a jury consider both parties' liability together (*see* PJI 2:36). This is because the issues of defendant's liability and plaintiff's comparative fault are intertwined. A jury cannot fairly and properly assess plaintiff's comparative fault without considering defendant's actions (*see e.g.* Siegel, Practice Commentaries, McKinney's Cons Laws of NY, CPLR C3212:24 [noting that "(n)o purpose (is) served by the granting of summary judgment" where "the proof that would go into the damages question substantially overlaps that on which liability depends"]). The facts of this case—which two courts **[**378] [***910]** have found created an issue of fact as to any liability on the part of defendant—highlight the unfairness of the majority's new rule (*see e.g.* *Ugarriza v Schmieder, 46 NY2d 471, 474-475, 386 NE2d 1324, 414 NYS2d 304 [1979]* ["Negligence cases by their very nature do not usually lend themselves to summary judgment, since often, even if all parties are in agreement as to the underlying facts, the very question of negligence is itself a question for jury determination"]).

Simultaneous consideration by the jury of both parties' level **[****22]** of culpability is also the more practical approach. Indeed, "few, if any, litigation efficiencies are achieved by the entry of partial summary judgment in this context because the defendant would still be entitled, at trial, to present an all-out case on the plaintiff's culpable conduct" (Vincent C. Alexander, Practice Commentaries, McKinney's Cons Laws of NY, Book 7B, *CPLR 1412*). In the event that plaintiff obtained partial summary **[*330]** judgment without removing issues of comparative fault, a jury would still be required to assess plaintiff's degree of liability, and then make a damages determination in a subsequent proceeding. Such an inefficient approach would dispose of any benefits to be gained in granting partial summary judgment (*see e.g.* *E.B. Metal & Rubber Indus. v County of Washington, 102 AD2d 599, 602-603, 479 NYS2d 794 [3d Dept 1984]* ["Granting plaintiffs' motions (for partial summary judgment) would be illusory and would spare neither the court's nor the litigants' time and effort. The issue of plaintiffs' comparative negligence would still need to be resolved, which resolution would require a comparison of the parties' culpable conduct"]). The majority promotes its approach by pointing to the "eliminat[ion]" of the first two questions a jury must answer in a "typical comparative **[****23]** negligence trial" (majority op at 324). But these questions would not be eliminated by a grant of partial summary judgment, as an assessment of defendant's negligence would be required in order for the jury to determine comparative fault and damages.

Nor is our approach barred by the statutory language of CPLR article 14-A. Requiring a plaintiff to show freedom from comparative fault in advance of obtaining summary judgment does not "bar recovery" in derogation of article 14-A. Before the enactment of article 14-A, a plaintiff was unable to obtain recovery of any sort where he or she was in any way culpable (*Fitzpatrick v International Ry. Co., 252 NY 127, 133-134, 169 NE 112 [1929]* ["At common law a person has no cause of action for negligence, if he himself has contributed, in the slightest degree, to bring it about"]). Article 14-A enables a plaintiff to *recover* despite comparative fault (*see* *Arbegast, 65 NY2d at 167* [article 14-A "permit(s) partial recovery in cases in which the conduct of each party is culpable"]). It does not mandate that courts grant partial summary judgment on liability to plaintiffs who are comparatively at fault, as the majority's approach would require. The comparative fault statute simply provides that a plaintiff is entitled to recover a certain amount of **[****24]** damages, to be determined by a jury, even in cases where plaintiff has engaged in some degree of culpable conduct. This requires that each party's culpability be assessed and liability determined before judgment is granted (*see* *id. at 168* ["(W)hat the statute requires comparison of is not negligence but conduct which, for whatever reason, the law deems blameworthy, in order to fix the relationship of each party's conduct to the injury sustained and the damages to be **[**379]** **[***911]** paid by the one and received by the other as recompense for that injury"]).

[*331] The majority repeatedly speaks to the "double burden" our approach would place on defendant. But there is no unfair tipping of the scales. Plaintiff in his moving papers made a blanket assertion of freedom from any comparative negligence and defendant, in response, came forward with extensive evidence of plaintiff's comparative fault. Plaintiff's burden was merely that placed on any party moving for summary judgment—to demonstrate a lack of triable issues of fact. In that, plaintiff failed.

Judges Rivera, Fahey and Wilson concur; Judge Garcia dissents in an opinion in which Chief Judge DiFiore and Judge Stein concur.

Order, insofar as appealed from, reversed, with costs, case remitted to the Appellate Division, First Department, for consideration of issues raised but not determined on **[****25]** the appeal to that Court and certified question answered in the negative.

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Ruocco v. Bateman, Eichler, Hill, Richards, Inc.

United States Court of Appeals for the Ninth Circuit

March 6, 1990, Pasadena, California, Argued and Submitted ; May 18, 1990, Filed

No. 88-6655

Reporter
903 F.2d 1232 *; 1990 U.S. App. LEXIS 7998 **; 12 Employee Benefits Cas. (BNA) 1557

John D. Ruocco, on behalf of himself and as the representative of a class of persons similarly situated, Plaintiff-Appellee, v. Bateman, Eichler, Hill, Richards, Incorporated, John R. Bolin, Theodore Prush, Defendants-Appellants

Prior History: [1]** Appeal from the United States District Court for the Central District of California; Dickran M. Tevrizian, District Judge, Presiding; D.C. No. CV-87-04173-DT.

Counsel: Craig B. Jorgensen, Jon L. Rewinski, Louis W. Karlin, Kindel & Anderson, Los Angeles, California, for the Defendants-Appellants.

J. Michael Hennigan, Richard M. Callahan, Jr., Hennigan & Mercer, Los Angeles, California, for the Plaintiff-Appellee.

Judges: David R. Thompson and Stephen S. Trott, Circuit Judges, and Malcolm F. Marsh, District Judge. * Opinion by Judge Malcolm F. Marsh.

Opinion by: MARSH

Opinion

[*1234] Marsh, District Judge

This action involves claims by John Ruocco, on behalf of himself and current and former Bateman, Eichler, Hill, Richards, Inc., et al., ("BEHR") employees who participated in BEHR's long-term disability plan between January 1, 1982 and December 30, 1984. The plaintiff class claims that BEHR violated its fiduciary duties, the Employmee Retirement Income and Security Act ("ERISA"), *29 U.S.C. §§ 1001-1461 (1982 & Supp. V 1987)*, section 8315 **[**2]** of the California Commercial Code, and the Racketeer Influenced and Corrupt Organizations Act ("RICO"), *18 U.S.C. §§ 1961-1968 (1982 & Supp. V 1987)*, when it failed to distribute to the plan participants a surplus dividend received from BEHR's disability insurance carrier. BEHR appeals the district court's grant of partial summary judgment to Ruocco on the non-RICO causes of action awarding to Ruocco $ 629,423.31 minus administrative costs, and attorney's fees. We affirm the district court's decision with respect to defendant BEHR but reverse the decision holding defendants Bolin and Prush personally liable.

I.

BEHR is a stock brokerage and financial consulting firm with its principal place of business in Los Angeles, California. At all relevant times, John R. Bolin was BEHR's president, chief executive officer and chairman of the board of directors. Theodore W. Prush was BEHR's executive vice president, chief financial officer and a member of the board of directors.

From 1968 to 1986, BEHR offered its employees group long term disability insurance through Union Mutual Insurance Company ("Union Mutual"). The Union Mutual policy was paid for by the employees **[**3]** participating in the plan. BEHR deducted premiums from the pay of participating employees and transmitted these premiums to Union Mutual. While BEHR paid premiums itself from time to time in order to prevent a lapse in coverage, the amount of premiums paid by BEHR was minimal. BEHR paid all administrative costs for the plan. Ruocco, an employee BEHR until August 1986, elected the long term disability coverage provided by Union Mutual.

The Union Mutual policy provided:

> When proof is received that an insured employee is totally disabled as a result of sickness or injury and requires the regular attendance of a legally qualified physician, the Insurance Company will pay a monthly benefit to the insured employee after completion of the elimination period.

The policy defined "employee" as "a full-time employee,

* Honorable Malcolm F. Marsh, United States District Judge for the District of Oregon, sitting by designation.

individual, proprietor, or partner who is regularly working at least 30 hours per week during the regular work week of the employer." The policy also provided that

> all insurance provided under this Policy for an insured employee will cease at 12:00 midnight on the earliest of the following occurrences: . . . (2) On the date **[*1235]** that the insured **[**4]** employee ceases to be in a class of employees eligible for insurance.

On September 24, 1986, Union Mutual notified BEHR that it intended to convert from a mutual insurance company to a wholly-owned subsidiary of a publicly-owned stock corporation called UNUM. Under Maine law, where Union Mutual was incorporated, such conversion could take place only upon distribution to each policyholder of a pro rata share of the retained surplus which the converting company had acquired while it was operating as a mutual company. Union Mutual determined the BEHR surplus by considering the premiums paid between January 1, 1982 and December 31, 1984. Union Mutual notified BEHR that the returned surplus would take the form of shares of UNUM stock and warrants to purchase additional shares of UNUM stock. The warrants had to be exercised between September 26 and October 28, 1986.

In October 1986, the Executive Committee of BEHR decided to exercise the warrants and paid $ 609,336 to buy 25,755 shares of UNUM stock. These shares were sold by BEHR in November 1986 for $ 712,249.30 thereby generating a profit of $ 104,913.30. In November 1986, BEHR also received the straight distribution of UNUM **[**5]** shares which BEHR sold on November 6, 1988 for $ 524,510.01. In total, BEHR received $ 629,423.31 from the profit on the sale of shares purchased on the warrants and the sale of the distributed shares.

On June 29, 1987, Ruocco filed this action, claiming that BEHR's decision to retain the UNUM distribution violated ERISA, California Commercial Code section 8315, and various provisions of RICO. The district court dismissed the RICO claims, but granted summary judgment to Ruocco on both the ERISA and California Commercial Code section 8315 claims. The court found that the BEHR long term disability plan was an "employee welfare benefit plan" as defined by ERISA, 29 U.S.C. § 1002(1), that defendants were "fiduciaries" of the Plan, that Ruocco was a "participant" in the plan, and that the surplus dividend constituted an "asset of the plan" pursuant to 29 U.S.C. section 1101. While the court found that defendants did not breach their fiduciary duty to the plaintiff class, the court held that defendants' decision to keep the UNUM distribution was "arbitrary and capricious." The court found that the balance of equities weighed in favor of **[**6]** the plan participants because "the premiums for the plan were paid for by the participants" and because "the funds would not inure to the benefit of the participants of the plan" if distributed to the defendants. The district court also found that the sale of the UNUM stock constituted a wrongful transfer of securities, in violation of California Commercial Code section 8315. Finally, the court ruled that plaintiffs were entitled to attorney's fees under ERISA pursuant to 29 U.S.C. section 1132(g)(1).

On September 6, 1988, BEHR petitioned this court for permission to pursue an immediate interlocutory appeal. The court granted this petition on December 2, 1988.

II.

A grant of summary judgement is reviewed de novo. Kruso v. International Tel. & Tel. Corp., 872 F.2d 1416, 1421 (9th Cir. 1989); State Farm Fire & Casualty Co. v. Martin, 872 F.2d 319, 320 (9th Cir. 1989). The appellate court's review is governed by the same standard used by the trial court under Fed.R.Civ.P. 56(c). Darring v. Kincheloe, 783 F.2d 874, 876 (9th Cir. 1986). The appellate court must determine, viewing the evidence in the light **[**7]** most favorable to the nonmoving party, whether there are any genuine issues of material facts and whether the district court correctly applied the relevant substantive law. Tzung v. State Farm Fire & Casualty Co., 873 F.2d 1338, 1339-40 (9th Cir. 1989); Judie v. Hamilton, 872 F.2d 919, 920 (9th Cir. 1989).

Issues dealing with the interpretation and application of ERISA provisions as well as preemption under ERISA are also subject to de novo review. Admiral Packing Co. v. Robert F. Kennedy Farm Workers ***[*1236]*** Medical Plan, 874 F.2d 683, 684 (9th Cir. 1989); Chase v. Trustees of W. Conf. of Teamsters Pension Trust Fund, 753 F.2d 744, 746 (9th Cir. 1985); Trustees of Amalg. Ins. Fund v. Geltman Indus., Inc., 784 F.2d 926, 929 (9th Cir.), *cert. denied*, *479 U.S. 822, 107 S. Ct. 90, 93 L. Ed. 2d 42, 55 U.S.L.W. 3232 (1986)*.

III.

BEHR asserts error on nine grounds.

1. *Lack of Jurisdiction*

BEHR argues that the district court erred because it lacked jurisdiction over plaintiff's ERISA claim. BEHR argues that Ruocco was not a "participant" of a welfare benefit **[**8]** plan as defined by ERISA because Ruocco received all the benefits he was entitled to under the disability benefit plan and was no longer employed by BEHR at the time the Union Mutual surplus was distributed.

ERISA defines participant as "any employee or former employee of an employer . . . who is or may become eligible to receive a benefit of any type from an employee benefit plan." *29 U.S.C. § 1002(7)*. The Supreme Court has interpreted ERISA's definition of participant as including both "employees in or reasonably expected to be in, currently covered employment," *Firestone Tire & Rubber Co. v. Bruch, 489 U.S. 101, 109 S. Ct. 948, 957-58, 103 L. Ed. 2d 80 (1989)* (quoting *Saladino v. ILGWU Nat'l Retirement Fund, 754 F.2d 473, 476 (2d Cir. 1985))*, or "former employees who 'have a reasonable expectation of returning to covered employment' or who have 'a colorable claim' to vested benefits." *Firestone, 109 S. Ct. at 957-58* (quoting *Kuntz v. Reese, 785 F.2d 1410, 1411* (9th Cir.), *cert. denied*, *479 U.S. 916, 93 L. Ed. 2d 291, 107 S. Ct. 318 (1986))*.

Applying the *Firestone* **[**9]** test to this case, we find that Ruocco presents "a colorable claim" of entitlement to the Union Mutual surplus based on his status as a former plan participant who contributed financially to the plan. This claim to entitlement is not altered by Ruocco's termination of employment with BEHR.

2. *California Insurance Code Section 10270.65*

BEHR argues that the district court erred because under *California Insurance Code section 10270.65*, BEHR was entitled to retain the Union Mutual surplus.

Section 10270.65 provides:

> If hereafter any dividend is paid or any premium refunded under any policy of group disability insurance heretofore or hereafter issued, the excess, if any, of the aggregate dividends or premium refunds under such policy over the aggregate expenditures for insurance under such policy made from funds contributed by the policyholder, or by an employer of such insured persons or by union or association to which insured persons belong, including expenditures made in connection with the administration of such policy, shall be applied by the policyholder for the benefit of such insured employees generally or their dependents or insured members generally or their **[**10]** dependents. For the purpose of this section and at the option of the policyholder, "policy" may include all group life and disability insurance policies of the policy holder.

Cal.Ins.Code § 10270.65 (West 1972).

The district court made three findings on this issue: first, that the code is not applicable to the facts of this case "since the UNUM distribution was neither a 'premium refund' nor 'dividend' as contemplated by the statute;" second, that because *section 10270.65* "does not contemplate the offsetting of employer costs from all benefit plans before providing the surplus to the participants of the plan," BEHR could only recoup administrative costs incurred in connection with the BEHR long term disability plan; and third, that *section 10270.65* is "preempted by ERISA, as it clearly 'relates to' an employee welfare benefit plan, as codified in *29 U.S.C. § 1144(a)* [1]."

[11] [*1237]** BEHR argues that the district court erred in its first holding because the Union Mutual distribution does constitute a "dividend" within the meaning of *section 10270.65*. BEHR argues that the court erred in its second holding because *section 10270.65* allows a policyholder to aggregate the costs incurred in connection with its group life policy. With respect to the third holding, BEHR argues that there is no ERISA preemption because *section 10270.65* deals with the regulation of insurance and therefore is covered by the insurance "saving clause" contained in *section 1144(b)(2)(A)*.

While defendants are correct that the distribution of the surplus constitutes a dividend under *section 10270.65* on which costs can be aggregated, *see* *Luksich v. Kaiser Steel Corp., 245 Cal.App.2d 373, 374-75, 53 Cal.Rptr. 875 (1966)*, we find that *section 10270.65* is preempted under ERISA because it relates to an employee benefit plan within the meaning of *29 U.S.C. section 1144(a)*.

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[1] *29 U.S.C. § 1144(a)* provides:

> Except as provided in subsection (b) of this section, the provisions of this subchapter and subchapter III of this chapter shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in section 1003(a) of this title and not exempt under section 1003(b) of this title.

The "saving clause" of § 1144(b)(2)(A) provides that "nothing in this title shall be construed to exempt or relieve any person from any law of any state which regulates **[**12]** insurance, banking, or securities." In determining whether a state's law regulates insurance and therefore is not preempted under section 1144(a), the Supreme Court set forth the following two-part test in Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41, 95 L. Ed. 2d 39, 107 S. Ct. 1549 (1987):

> In *Metropolitan Life*, we were guided by several considerations in determining whether a state law falls under the saving clause. First, we took what guidance was available from a common sense view' of the language of the saving clause itself. 471 U.S. 724, 740, 105 S. Ct. 2380, 85 L. Ed. 2d 728 (1985). Second, we made use of the case law interpreting the phrase 'business of insurance' under the McCarran-Ferguson Act, 15 U.S.C. § 1011 et seq., in interpreting the saving clause.

481 U.S. at 48. *See also* Metropolitan Life Ins. Co. v. Massachusetts, 471 U.S. 724, 85 L. Ed. 2d 728, 105 S. Ct. 2380 (1985). With respect to the second-part of this test, the Court set forth the following three criteria for determining whether a practice falls under the 'business of insurance' for purposes **[**13]** of the McCarran-Ferguson Act: [2]

> '*First*, whether the practice has the effect of transferring or spreading a policyholder's risk; *second*, whether the practice is an integral part of the policy relationship between the insurer and the insured; and *third*, whether the practice is limited to entities within the insurance industry.'

Pilot Life, 481 U.S. at 48-49 (quoting Union Labor Life Ins. Co. v. Pireno, 458 U.S. 119, 129, 73 L. Ed. 2d 647, 102 S. Ct. 3002 (1982)) (emphasis in original).

California Insurance Code section 10270.65 does not regulate insurance within the meaning of either the McCarran-Ferguson Act or ERISA, 29 U.S.C. § 1144(b)(2)(A). This **[**14]** statute fails the first part of the *Metropolitan* test because it does not transfer or spread the policyholder's risk but rather deals merely with the administration of certain policy surplus. The statute fails the second part of the test because it is not an "integral part of the policy relationship" between the insurer and the insured but rather deals with the relationship between the policyholder and the insured. While section 10270.65 is limited to entities within the insurance industry, this alone does not support a finding of insurance regulation within the meaning of section 1144(b)(2)(A). The "saving clause" to ERISA exempts from preemption state regulation of insurance companies and terms of insurance contracts not state regulation of employee benefit plans funded by the insurance industry. [3] **[*1238]** The same conclusion is reached under a "common sense view" of section 10270.65.

[15]** 3. *Asset of the Insurer*

BEHR claims the retained surplus of a group disability carrier is not an asset of a covered plan pursuant to 29 U.S.C. section 1101 and therefore ERISA does not require BEHR to distribute the Union Mutual surplus to participating employees. Section 1101(b)(2) provides that "in the case of a plan to which a guaranteed benefit policy is issued by an insurer, the assets of such plan shall be deemed to include such policy, but shall not, solely by issuance of such policy, be deemed to include any assets of the insurer."

While the premium surplus may have been held as an asset by Union Mutual, this asset was not owned by the insurance company but was part of the interest of the mutually insured in the company. *See* 18 J. Appleman, Insurance Law and Practice § 10059 (1945). As stated, Union Mutual was required to distribute this retained surplus to policyholders prior to its conversion from a mutual insurance company to a wholly-owned subsidiary of a publicly-owned stock corporation. The surplus, therefore, did not constitute an asset of the

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[2] The McCarran-Ferguson Act of 1945 provides that "no act of Congress shall be construed to invalidate, impart, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . ." 15 U.S.C. § 1012(b) (1982).

[3] In reaching this conclusion, we also draw support from the fact that "the express pre-emption provisions of ERISA are deliberately expansive, and designed to 'establish pension plan regulation as exclusively a federal concern.'" Pilot Life, 481 U.S. at 45-46 (quoting Alessi v. Raybestos-Manhattan, Inc., 451 U.S. 504, 523, 68 L. Ed. 2d 402, 101 S. Ct. 1895 (1981)); *see also* Board of Trustees v. H.F. Johnson, Inc., 830 F.2d 1009, 1016 (9th Cir. 1987)("ERISA preemption is to be construed broadly").

insurer within the meaning of 29 U.S.C. section 1101(b)(2).

[**16] 4. *Unexpected and Undeserved Windfall*

BEHR contends that the district court erred in awarding the Union Mutual surplus to former employees because the award constitutes an unexpected and undeserved windfall for the employees. In determining who was entitled to the surplus, the district court relied heavily on the Third Circuit's decision in *Chait v. Bernstein, 835 F.2d 1017 (3d Cir. 1987)*. In *Chait*, the court held that an employer could amend an ERISA plan to allow surplus assets to revert to the employer despite the plan's prohibition on amendments to the plan to allow the funds to be used for purposes other than for the exclusive benefit of the employees. The court held that the plan could be so amended because the plan contained no additional language limiting the reversion beyond the "exclusive benefit" provision and because the equities of the case favored the employer's creditors rather than the vested employees. *Id. at 1027*. In reaching this conclusion, the court emphasized the fact that the plan was a "defined benefit plan to which the employees never contributed." On this matter, the court held:

> In the context of **[**17]** a defined-benefit plan to which the employer was the sole contributor that does not contain explicit prohibitory language, we see no congressional policy that would prevent allowing the employer to amend the plan to receive excess assets after paying out all the benefits.

Id. See also Wright v. Nimmons, 641 F. Supp. 1391, 1406-07 (S.D.Tex. 1986) (noting that where a trust plan is silent as to the distribution of assets, if the employer has "exclusively funded a plan," the "unbargained for distribution of excess assets to participants represents an unintended windfall for employees").

In this case, the district court found that the balancing of equities weighed in favor of the plan participants because the premiums for the plan were paid for by the participants and because "outside of minor administrative costs, BEHR paid nothing." The court also found that if the surplus were distributed to the defendants, the fund would not inure to the benefit of the plan participants, but rather "as a result of BEHR's incentive bonus plan, would fall in large part into the hands of BEHR's Executive Committee which had voted to keep the distribution." We agree with **[**18]** the district court that the balance of equities weighs in favor of the plaintiff class.

[*1239] 5. *Resulting Trust*

Next BEHR argues that it is entitled to retain the Union Mutual surplus under the law of trust because BEHR was the creator or settlor of the plan trust. BEHR argues that, as a result of its status as settlor of the trust, when surplus assets remained in the long term disability fund after the trust's purpose had been fulfilled, a resulting trust arose for its benefit. We reject BEHR's argument. BEHR did not pay the premium costs to fund the plan and therefore was neither a 'creator' nor 'settlor' of the trust. *See, e.g., Lehman v. Commissioner of Internal Revenue, 109 F.2d 99, 100* (2d Cir.), *cert. denied*, *310 U.S. 637, 60 S. Ct. 1080, 84 L. Ed. 1406 (1940)* (defining settlor as one who furnishes the consideration for a trust).

6. *Financial Risk*

BEHR argues that the district court erred in ordering BEHR to pay its former employees the profits which it earned by exercising the UNUM warrants because BEHR risked its own money in exercising the warrants and could not have provided its former employees with sufficient **[**19]** notice to exercise these warrants given the large number of employees involved. BEHR's argument as to what would have happened had it given the plan participants notice is speculative and does not support a finding that BEHR is entitled to retain the surplus. Nor does the fact that BEHR used its own money to exercise the warrants justify BEHR's retention of the acquired profit.

7. *California Commercial Code Section 8315*

BEHR argues that the district court erred in finding that the sale of the UNUM stock by defendants constituted a wrongful transfer of securities in violation of California Commercial Code section 8315 which prohibits the wrongful transfer of securities. [4] We disagree. The

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[4] Section 8315(1) of the California Commercial Code states in pertinent part:

> Any person against whom the transfer of a security is wrongful for any reason, . . . as against any purchaser except a bona fide purchaser, may do any of the following:

district court correctly found that section 8315 is a state statute regulating securities and therefore is saved from ERISA preemption under *29 U.S.C. section 1144(b)(2)(A)*. Contrary to BEHR's contention, we find no inconsistency between the district court's finding that *California Insurance Code section 10270.65* is preempted by ERISA because it does *not* regulate insurance and the court's finding that *California Commercial Code section 8315* is not preempted **[**20]** because it *does* regulate securities.

8. *Attorney's Fees*

BEHR argues that the district court erred in awarding attorney fees *sua sponte* because it did not discuss the factors set forth in *Hummell v. S.E. Rykoff & Co., 634 F.2d 446, 452 (9th Cir. 1980)* and did not give the parties an adequate opportunity to address this matter. We disagree. The district court provided BEHR with an opportunity to address the matter when it received BEHR's opposition to the proposed statement of undisputed facts. The district **[**21]** court also considered the *Hummell* factors in determining that an award of attorney's fees was reasonable and appropriate. In *Hummell*, the court held that the following five factors must be considered in determining whether to award attorney's fees under *29 U.S.C. section 1132(g)*:

> (1) the degree of the opposing parties' culpability or bad faith; (2) the ability of the opposing parties to satisfy an award of fees; (3) whether an award of fees against the opposing parties would deter others from acting in similar circumstances; (4) whether the parties requesting fees sought to benefit all participants and solve a significant legal question regarding ERISA; and (5) the relative merits of the parties' positions.

Hummell, 634 F.2d at 453. The district court in this case applied the *Hummell* test **[*1240]** and found that defendants had the ability to satisfy an award of attorney's fees, that the awarding of fees will deter others from acting in an arbitrary and capricious manner, that Ruocco was seeking to benefit all participants of the BEHR Plan and to resolve significant legal questions concerning ERISA, and that **[**22]** Ruocco's position in this litigation was substantiated on both legal and equitable grounds.

9. *Personal Liability of Bolin and Prush*

While the district court did not err in awarding the Union Mutual surplus and attorney's fees to the plaintiff class, the district court did err in its finding that defendants Bolin and Prush were personally liable in light of its additional finding that neither defendant breached his fiduciary duty or otherwise acted in bad faith. While Bolin and Prush may have benefited by their decision to retain the UNUM surplus under BEHR's bonus incentive program for top executives, there is no evidence that Bolin or Prush did anything personally or that the decision to retain the UNUM surplus was not a corporate act. Likewise, while Bolin and Prush were members of the Executive Committee, the decisionmaking body of BEHR, there is no evidence that they controlled this Committee.

CONCLUSION

We affirm the judgment of the district court awarding the plaintiff class $ 629,423.31 minus administrative costs, and attorney's fees against defendant BEHR. We reverse the court's decision holding defendants Bolin and Prush personally liable. Plaintiff shall recover **[**23]** from defendant BEHR 80 percent of his costs on appeal.

AFFIRMED IN PART, REVERSED IN PART.

> (a) Reclaim possession of any new certificated security wrongfully transferred.
>
> (b) Obtain possession of any new certificated security representing all or part of the same rights . . .
>
> (d) Have damages.

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Smith v. Chase Manhattan Bank, USA, N.A.

Supreme Court of New York, Appellate Division, Second Department

November 1, 2001, Argued ; April 15, 2002, Decided

2000-08199

Reporter
293 A.D.2d 598 *; 741 N.Y.S.2d 100 **; 2002 N.Y. App. Div. LEXIS 3790 ***

Timothy P. Smith et al., Appellants, v. Chase Manhattan Bank, USA, N.A., et al., Respondents.

Prior History: **[***1]** In a purported class action to recover damages for a violation of *General Business Law § 349*, breach of contract, unjust enrichment, and a violation of *Civil Rights Law §§ 50* and *51*, the plaintiffs appeal from an order of the Supreme Court, Kings County (Clemente, J.), dated July 27, 2000, which granted the defendants' motion pursuant to *CPLR 3211 (a) (1)* and *(7)* to dismiss the complaint.

Counsel: Wolf Popper, LLP, New York, N.Y. (Lester L. Levy and Peter G. A. Safirstein of counsel), and Schoengold & Sporn, P.C., New York, N.Y. (Samuel P. Sporn and Jay P. Saltzman of counsel), for appellants (one brief filed).

Skadden, Arps, Slate, Meagher & Flom, LLP, New York, N.Y. (Andrew L. Sandler of counsel), for respondents.

Judges: NANCY E. SMITH, J.P., SONDRA MILLER, DANIEL F. LUCIANO, ROBERT W. SCHMIDT, JJ. SMITH, J.P., S. MILLER, LUCIANO and SCHMIDT, JJ., concur.

Opinion

[*598] **[**101]** Ordered that the order is affirmed, with costs.

The plaintiffs, who purport to represent a class of similarly-situated persons, are holders of credit cards and mortgages issued by Chase Manhattan Bank USA, **[***2]** N.A. The plaintiffs commenced this class action against the defendants, Chase Manhattan Bank USA, N.A., and its parent, Chase Manhattan Corporation (hereinafter collectively Chase), alleging five separate causes of action: (1) a violation of *General Business Law § 349 (a)* for engaging in a deceptive practice, (2) breach of contract, (3) unjust enrichment, (4) a violation of *Civil Rights Law § 50*, and *(5)* a violation of *Civil Rights Law § 51*.

The complaint alleges that Chase violated its commitment to protect customer privacy and confidentiality and not to share customer information with any unrelated third party, except, inter alia, to conduct its business or make available special offers of products and services which might be of interest to customers. This confidentiality commitment was contained in a printed document entitled "Customer Information Principles," which was distributed to the plaintiffs. Allegedly unbeknownst to the plaintiffs, without their consent and without giving the plaintiffs an opportunity to opt out, Chase sold information to nonaffiliated third-party vendors, including the plaintiffs' **[***3]** names, addresses, telephone numbers, account or loan numbers, credit card usage, and other financial data. The third-party vendors used this information and created lists of Chase customers, including the plaintiffs, who might be interested in their products or services. These lists were then provided to telemarketing and direct mail representatives to conduct solicitations. In return for the information, the third-party vendors agreed to pay Chase a commission (of up to 24% of the sale) in the event that a product or service offered were purchased.

The defendants moved to dismiss all five causes of action for **[*599]** failure to state a cause of action. The Supreme Court granted the **[**102]** defendants' motion in its entirety. We affirm.

To establish a cause of action under *General Business Law § 349*, a plaintiff must prove that the challenged act or practice was consumer oriented, that it was misleading in a material way, and that the plaintiff suffered injury as a result of the deceptive act. Whether a representation or omission, the deceptive practice **[***4]** must be likely to mislead a reasonable consumer acting reasonably under the circumstances. In addition, to recover under the statute, a plaintiff must prove actual injury, though not necessarily pecuniary harm (*see* *Stutman v Chemical Bank, 95 NY2d 24, 29*; *see also* *Small v Lorillard Tobacco Co., 94 NY2d 43*;

Oswego Laborers' Local 214 Pension Fund v Marine Midland Bank, 85 NY2d 20).

Presuming the allegations in the complaint to be true, and giving them the benefit of every favorable inference (*see Cron v Hargro Fabrics, 91 NY2d 362, 366)*, to the extent that the plaintiffs alleged that Chase sold confidential customer information to third-party vendors in violation of its document entitled "Customer Information Principles," the complaint alleges actionable deception. However, the plaintiffs have not alleged, and cannot prove, any "actual injury" as is necessary under *General Business Law § 349* (*Stutman v Chemical Bank, supra at 29*; *Small v Lorillard Tobacco Co., supra; Oswego Laborers' Local 214 Pension Fund v Marine Midland Bank, supra*). The **[***5]** complaint alleged that Chase's "deceptive acts and practices deceived the plaintiffs and other members of the class, and have directly, forseeably and proximately caused actual damages and injury to the plaintiffs and other members of the class in amounts yet to be determined." These allegations failed to allege any actual harm. Elsewhere in the complaint, the plaintiffs alleged: "the products and services offered to class members as a result of [Chase's] practices of selling class members' confidential financial information included memberships in discount shoppers' clubs, emergency road service plans, dental and legal service plans, travel clubs, home and garden supply clubs, and credit card registration and magazine subscription services."

Thus, the "harm" at the heart of this purported class action, is that class members were merely offered products and services which they were free to decline. This does not qualify as actual harm.

The complaint does not allege a single instance where a named plaintiff or any class member suffered any actual harm due to the receipt of an unwanted telephone solicitation or a **[*600]** piece of junk mail. Accordingly, the court properly **[***6]** dismissed the plaintiffs' General Business Law causes of action.

The plaintiffs seek to recover damages for unjust enrichment based on the profits Chase earned as commissions on the purchases made by members of the plaintiffs' class. "To state a cause of action for unjust enrichment, a plaintiff must allege that it conferred a benefit upon the defendant, and that the defendant will obtain such benefit without adequately compensating plaintiff therefor" (*Nakamura v Fujii, 253 AD2d 387, 390*; *see Wolf v National Council of Young Israel, 264 AD2d 416, 417)*. The plaintiffs failed to state a cause of action to recover damages for unjust enrichment since the members of the plaintiffs' class who made purchases **[**103]** of products and/or services received a benefit. There being no allegation that the benefits received were less than what these purchasers bargained for, it cannot be said that the commissions paid by the third-party vendors to Chase belong to the plaintiffs as a matter of equity (*see Wiener v Lazard Freres & Co., 241 AD2d 114, 121*; **[***7]** *Fandy Corp. v Chang, 272 AD2d 369*; *Bugarsky v Marcantonio, 254 AD2d 384*).

Similarly, the plaintiffs failed to state a cause of action to recover damages for breach of contract. The plaintiffs' allegation of contract damages consisted solely of the phrase "all to the damage of the class." Such a vague and conclusory allegation is insufficient to support a cause of action for breach of contract (*see Gordon v Dino De Laurentiis Corp., 141 AD2d 435, 436)*. Even if the complaint were construed to allege damages for the invasive and unsolicited telephone calls, no cause of action is stated, since damages for emotional distress are insufficient to state a cause of action for breach of contract (*see Wehringer v Standard Sec. Life Ins. Co., 57 NY2d 757, 759)*. In addition, the plaintiffs may not rely on Chase's profits to satisfy the damage element of their cause of action, since the plaintiffs never had any expectation of monetary compensation.

The plaintiffs have failed to state a cause of action under *Civil Rights Law §§ 50* **[***8]** and *51*. *Civil Rights Law §§ 50* and *51*, which must be narrowly construed, were never intended to address the wrongs complained of by the plaintiffs (*see Messenger v Gruner & Jahr Print. & Publ., 94 NY2d 436, 441*, *cert denied 531 US 818*; *Arrington v New York Times Co., 55 NY2d 433, 439*, *cert denied 459 US 1146*).

Smith, J.P., S. Miller, Luciano and Schmidt, JJ., concur.

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Town of N. Haven v.

Superior Court of Connecticut, Judicial District of New Haven, At New Haven

January 5, 2004, Decided ; January 5, 2004, Filed

CV030474463

Reporter
2004 Conn. Super. LEXIS 15 *

Town of North Haven et al. v. North Haven Education Association

Notice: **[*1]** THIS DECISION IS UNREPORTED AND MAY BE SUBJECT TO FURTHER APPELLATE REVIEW. COUNSEL IS CAUTIONED TO MAKE AN INDEPENDENT DETERMINATION OF THE STATUS OF THIS CASE.

Judges: Robert I. Berdon, Judge Trial Referee.

Opinion by: Robert I. Berdon

Opinion

MEMORANDUM OF DECISION

This is an action brought by the plaintiffs, Town of North Haven (Town) and the North Haven Board of Education (Board) against the North Haven Education Association (Association) seeking a declaratory judgment that the-issues raised by the shares of Anthem common stock received by the Town as a result of the demutualization of Anthem Blue Cross/Blue Shield is not arbitrable under the employment contract between the Association and the Board and the plaintiffs seek a permanent injunction to that effect.

The Board is a separate entity from the Town. The Board is the employer of the members of the Association, has its own budget, and provides certain benefits for its employees including the teachers who are represented by the Association. These benefits are paid pursuant to the provisions of the contract between the Board and Association. The specific contract at the time that Anthem was demutualized covered the period of September 1, 2000 through **[*2]** August 31, 2004. (Contract.) One of the benefits under the Contract was that the Board would provide the teachers medical coverage through Anthem. Article XXVII of the Contract specifically provides the following: "The *Board shall* provide for each teacher . . . the following medical . . . benefits. Teachers participating in the insurance coverages . . . shall contribute ten percent (10%) of the premium cost of the applicable coverage . . . [for] . . . Anthem Blue Cross/Blue Shield Century Preferred (PPO) Plan, with a $ 15.00 co-pay on the Home and Office Benefit." (Emphasis supplied.) The Board, instead of paying the premium directly to Anthem and obtaining its own policy, received this coverage through the Town's policy with Anthem.

During the period of 2001-02 Anthem was demutualized. As a result, Anthem distributed shares of stock to the Town based upon the premiums paid by the Town and Board including the premiums paid by the teachers. The Town sold the stock for the sum of $ 1,505,564. The teachers neither received their proportionate share of the $ 1,505,564 nor was that portion of the health premiums paid by the teachers reduced as a result of the Anthem stock distribution. **[*3]** Through the Association's lens, the distribution of Anthem stock was in reality a return of premiums and the members of the Association should share to the extent of the premiums paid by its members.

On February 14, 2002, the Association pursuant to the Contract filed the following grievance against the Board: "Article XXVII requires all teachers half or full time . . . to contribute ten percent (10%) of the premium cost of the applicable coverage . . . through payroll deduction. The Board/Town of North Haven is receiving a share value rebate that represents past premium contributions from Anthem Blue Cross Blue Shield and the employee share of said shares should be paid to the teacher/participants." The Superintendent of Schools and the Board denied the grievance. Thereafter, the Association filed a demand for arbitration before the American Arbitration Association in accordance with the Contract describing the nature of the dispute as follows: "The Board of Education has withheld from teachers a portion of a returned insurance premium, which results in an overpayment of premium by teachers. This violates the Agreement's Medical Insurance Benefits provision."

Although there is only **[*4]** one issue before the Court--that is, whether the issue or issues pertaining to the Anthem stock distribution as a result of its demutualization are subject to arbitration under the Contract--the Court feels compelled to comment on the fairness of the position of the Board and Town. *Fairness* dictates that the teachers should share in the proceeds received by the Town to the extent that the amount of the premiums paid by them bears to the total amount of the premiums paid by the Town upon which the total stock distribution was based. [1] The number of shares of Anthem stock received by the Town was based in part on the ten percent of the premiums paid by the teachers to the Board and eventually received by the Town. The position that the Board and Town in this case take is indefensible.

[*5] "Whether a dispute is an arbitrable one is a legal question for the court rather than for arbitrators, in the absence of a provision in the agreement giving arbitrators such jurisdiction. The parties may manifest such a purpose by an express provision or by the use of broad terms such as were employed in [International Brotherhood v. Trudon & Platt Motor Lines, Inc., 146 Conn. 17, 21, 147 A.2d 484 (1958)]. But unless they do, the determination of the question of the arbitrability of a particular dispute is the function of the court. (Citations omitted in part.) Connecticut Union of Telephone Workers, Inc. v. Southern New England Telephone Company, 148 Conn. 192, 197, 169 A.2d 646 (1961). In the present case, the parties agree that the issue of whether the dispute is arbitrable is one for the Court.

"In determining whether a party is bound to arbitrate, the courts look at the language employed in the contract. A contract is to be construed as a whole and all relevant provisions will be considered together. A court will not torture words to import ambiguity where the ordinary meaning leaves no room for ambiguity and words do not become ambiguous **[*6]** simply because lawyers or laymen contend for different meanings." (Citation omitted; internal quotations marks omitted.) Scinto v. Sosin, 51 Conn.App. 222, 239, 721 A.2d 552 (1998).

The Court, accordingly, looks to the Contract between the Association and the Board. The Board points out that it is a separate entity from the Town and it was the Town that was the policyholder of Blue Cross which enabled it to obtain the shares of Anthem stock upon the demutualization of Anthem. However, the Board unilaterally decided to fulfill its Contract obligation with the Association through the Town. The contract is clear that it was the Board's obligation to obtain the coverage with Anthem. Article 27 of the Contract provides: "the Board shall provide for such coverage with Anthem." Although the plaintiffs produced an abundance of evidence that the Board and the Town to prove that they were separate entities, there was not a scintilla of evidence that the Board was required to obtain the coverage through the policy of the Town. If the Board had fulfilled its contractual obligation for medical coverage directly, as the contact obviously contemplated, it would have received the **[*7]** shares of stock from Anthem. If that had occurred, the issue of whether the teachers should share in the proceeds would be arbitrable.

Notwithstanding that the policy was in the name of the Town and the Anthem stock was distributed to the Town this grievance filed by the Association is arbitrable under the Contract. The Contract defines grievance as follows: " 'Grievance' shall mean a claim by a teacher or group of teachers or the Association based upon an alleged violation, misinterpretation or misapplication of a specific contract provision." Article XXX, § 30.1a. The issue involves the obligation on the part of the members of the Association to pay ten percent of the premium as required by Article XXVII. It clearly is a grievance that falls within the provisions of the Contract. [2]

[*8] After providing for levels of review for a grievance filed (which was done in this case XI) the Contract provides that--the "Association shall submit such grievance to the American Arbitration Association for processing by a single arbitrator in accordance with the voluntary rules and regulations of the American Arbitration Association then in effect except as modified herein within eight (8) days of the receipt of the Board's

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[1] A *rough calculation* of the amount at issue based upon the premiums paid by the Town for the year 2002 are as follows: The Town paid total premiums to Anthem in the amount of $ 5,950,000 of which $ 3,640,000 or 61 percent was attributed to the employees of the Board; 61 percent of $ 1,505,564 the Town received as a result of the sale of Anthem stock attributed to the premiums the Board paid is $ 918,394; 10 percent paid by the employees of the board would amount to $ 91,839. The litigation costs to prosecute and defend this case could exceed $ 91,839, the approximate amount that is at issue.

[2] Indeed, the Superintendent of Schools and the Board considered the claim of the Association as a grievance. They both denied the Association's grievance when presented to them under levels two and three of formal grievance procedures. Article XXX of the Contract.

decision."

The issues in this case become confused because this action was also brought by the Town to avoid arbitration. The Town in this matter, however, is a mere interloper. The Association does not seek to arbitrate the issues with the Town. The demand for arbitration filed by the Association seeks an arbitration with the Board, to wit: "North Haven Board of Education c/o Mary Jane Sheehy, Supt." [3] Although the proceeds received from the sale of the stock may have gone into the pocket of the Town as a result of the actions of the Board, it remains a dispute which is the proper subject of an arbitration between the Association and the Board.

[*9] Any question as to the arbitrability of the issue is put to rest when the "positive assurance" test is applied. "It has . . . been clearly established that the *Warrior* 'positive assurance' test is the law in Connecticut. Under the positive assurance test, judicial inquiry . . . must be strictly confined to the question whether the reluctant party did agree to arbitrate the grievance . . . An order to arbitrate the particular grievance should not be denied unless it may be said with *positive assurance* that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute. Doubts should be resolved in favor of coverage." (Citations omitted; internal quotation marks omitted in part.) *Board of Education v. Frey, 174 Conn. 578, 582, 392 A.2d 466 (1978)*; *United Steelworkers of America v. Warrior & Gulf Navigation Co., 363 U.S. 574, 582-83, 4 L. Ed. 2d 1409, 80 S. Ct. 1347 (1960)*.

The Court concludes that the issue with respect to that portion of the proceeds realized from the sales of Anthem stock which was received as a result of the ten percent paid by the participating members of the Association is subject to the arbitration clause **[*10]** of the Contract. Accordingly, the request of the plaintiffs Town of North Haven and North Haven Board of Education for a declaratory judgment and injunction are denied [4] and the North Haven Board of Education is ordered to proceed with the arbitration in accordance with the Contract.

[*11] Robert I. Berdon

Judge Trial Referee

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[3] Application made to the American Arbitration Association, dated January 23, 2003, Exhibit E.

[4] The defendant has called to the Court's attention that there are two other trial court opinions, contrary to this opinion, which are on appeal, involving the same issue. They are: *Wallingford Board of Education v. Wallingford Education Association* (Docket No. CV03-0472527, J.D. of New Haven dated New Haven, dated May 14, 2003, DeMayo, J.), and *Region 14 Board of Education v. Nonnewaug Teachers' Association* (Docket No. CV03-0089873, J.D. of Litchfield, Pickard, J.) (35 Conn. L. Rptr. 46). If this decision is appealed, counsel should alert the Staff Attorney's Office so the three cases can be assigned to the same panel of judges. In the alternative, the Association and/or the Board may wish to move to have it decided by the Supreme Court of Connecticut calling to its attention the other pending appeals. ***Conn. Practice Book § 65-2***.

Towne Bus Corp. v. Insurance Co. of Greater N.Y.

Supreme Court of New York, New York County

January 18, 2008, Decided

120333/99

Reporter
18 Misc. 3d 1121(A) *; 856 N.Y.S.2d 503 **; 2008 N.Y. Misc. LEXIS 207 ***; 2008 NY Slip Op 50149(U) ****

[**1]** Towne Bus Corp., Plaintiff, against Insurance Company of Greater New York, Defendant.

Notice: THIS OPINION IS UNCORRECTED AND WILL NOT BE PUBLISHED IN THE PRINTED OFFICIAL REPORTS

Judges: [*1]** Emily Jane Goodman, J.

Opinion by: Emily Jane Goodman

Opinion

Emily Jane Goodman, J.

In this action, plaintiff Towne Bus Corp., an insured under a workers' compensation liability insurance policy, seeks the recovery of a policyholder dividend on a renewal policy. Defendant Insurance Company of Greater New York, the insurer, now moves, pursuant to CPLR 3212, for summary judgment dismissing the complaint. For the following reasons, the motion is granted.

BACKGROUND The underlying facts are not in dispute. Plaintiff purchased a workers' compensation and employers' liability policy (policy No. 6631003142) from defendant, with a policy period from February 1, 1996 through February 1, 1997 (the original policy) (Hess Affirm., Exh. A, Information Page). Plaintiff was the named insured. The insurance applied to claims brought under the Workers' Compensation Law of the State of New York (*id.*). At the end of that policy period, defendant renewed plaintiff's policy for another year, for a period from February 1, 1997 through February 1, 1998 (the renewal policy) (Hess Affirm., Exh. B, Information Page). [1]

Part Six of the renewal policy permitted plaintiff to cancel the policy (*id.,* Part Six-Conditions [D] [1]). The renewal policy states that the "policy period will end on the day and hour stated in the cancelation notice" (*id.,* Part Six-Conditions [D] [3]).

The policies were "audit premium" policies, where the insured pays estimated premiums, known as deposit premiums, based on estimated payroll for the coming year. After termination of the policy, the insurer audits the policy to determine the earned premium (the actual amount of premium owed to the insurer based on actual payroll information), and generally either refunds the difference to the insured or requires the insured to pay an additional amount. Specifically, Part Five of the renewal policy provides, in relevant part, that:

[**2]** The premium shown on the Information Page, schedules, and endorsements is an estimate. The final premium will be determined after this policy ends by using the actual, not the estimated, premium basis and the proper classifications and rates that lawfully apply to the business and work covered by this policy. If **[***3]** the final premium is more than the premium you paid to us, you must pay us the balance. If it is less, we will refund the balance to you. The final premium will not be less than the highest minimum premium for the classifications covered by this policy.

(*id.,* Part Five-Premium [E]). It further states that, if the insured cancelled the policy, final premium would be determined in the following way unless defendant's manuals provided otherwise: "final premium will be more than pro rata; it will be based on the time this policy was in force, and increased by our short-rate cancelation table and procedure. Final premium will not be less than the minimum premium" (*id.,* Part Five-Premium [E] [2]).

With regard to dividends, the renewal policy states, as in the original policy, that:

[1] The policies state that "[t]his policy includes . . . the Information Page and all endorsements and schedules listed **[***2]** there" (Hess Affirm., Exh. A, General Section [A]; Hess Affirm., Exh. B, General Section [A]).

Dividend: You shall participate in the earnings of the Company to such extent and upon such conditions as shall be determined by the Board of Directors of the Company in accordance with Law and as made applicable to this policy provided that you shall have complied with all of the terms of this policy with respect to the payment of premium.

(*id.,* policy jacket [emphasis in original]).

By letter dated September 15, **[***4]** 1997, plaintiff cancelled its renewal policy effective October 15, 1997, several months before the expiration of the policy. An endorsement reflects that the renewal policy was cancelled at plaintiff's request. Plaintiff replaced its coverage with another insurance carrier.

On October 1, 1997, defendant held a meeting of its Board of Directors, at which it passed a resolution concerning payment of dividends on workers' compensation policies. The minutes state that:

> [T]he Company shall pay a dividend upon Workers Compensation policies written or renewed by the Company and canceled or expiring during the period October 1, 1997, through December 31, 1997, both dates inclusive, as follows:

. . .

(B) On policies upon risks in the State of New York, a dividend plan that is identified as a Workers' Compensation Flat Percentage Dividend Plan, a dividend of 8% of the earned premium on all coverages, upon risks which develop a final annual audited earned premium of $ 50,000.00 or more;

. . .

Provided, however, that:

[**3]** . . .

(3) No dividend shall be payable on policies or renewals thereof which have been canceled prior to their full term of one year, unless such policy or renewal has been canceled after **[***5]** being in effect for six months by the Company upon its initiative for reasons other than non-payment of premium, or unless such policy or renewal has been immediately replaced by another policy written by the Company or its parent.

(Hess Affirm., Exh. C, 10/1/97 Minutes of Board of Directors of Insurance Company of Greater New York, at 2, 3, 4).

Plaintiff thereafter brought the present action. The complaint contains one cause of action for breach of contract for failure to pay dividends on the renewal policy, and seeks damages in an amount of $ 90,000. Defendant counterclaimed against plaintiff for $ 7,104 in unpaid premiums. However, defendant thereafter refunded $ 18,375.95 to plaintiff for unused premium for the renewal policy, and plaintiff does not dispute that it was paid the correct amount for the unused premium (Marksohn Aff., P 4). Thus, the only issue to be resolved is plaintiff's entitlement to a dividend on the renewal policy.

Defendant moves for summary judgment, contending that the issuance of a dividend was within its discretion under case law and under the language of the dividend provision. Thus, plaintiff did not qualify pursuant to the dividend resolution, since plaintiff **[***6]** cancelled the policy prior to the expiration of its full term. [2]

Plaintiff contends first that it expected to share in dividends on a pro rata basis. According to plaintiff, defendant's construction of the dividend provision of the policy impermissibly places plaintiff at defendant's mercy, because every contract contains an implied obligation of good faith and fair dealing. And, the dividend provision only requires that it complied with all of the terms of the policy with respect to the payment of premiums, which it undisputedly did. Second, plaintiff was never provided with a copy of the renewal policy, and thus it would be unjust to bind it to terms of **[***7]** which it was not aware. Third, the language of the policy is ambiguous in that it did not provide plaintiff with notice of the severe financial consequences of early cancellation. In addition, plaintiff requests, through its attorney's affirmation and without serving a separate notice of cross motion, that summary judgment be granted in its favor.

In reply, defendant does not dispute plaintiff's assertion that it was never provided with a copy of the renewal policy, but argues that it knew the terms because the original policy was automatically renewed by operation

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[2] Defendant also submits affidavits stating that an audit of the original policy determined that the total earned premium was $ 1,117,245, less a deposit premium of $ 1,155,251, which left a credit of $ 38,006 to plaintiff. Plaintiff's dividend in the sum of $ 167,587 for the original policy was then added to that credit, for a total credit of $ 205,593 for the original policy (Salik Aff., P 3; D'Onofrio Aff., PP 5-6). However, plaintiff's only claim is with respect to the renewal policy, not the original policy (Complaint, PP 6-8).

of Workers' Compensation Law § 54 for a one-year period on the same terms.

[**4] DISCUSSION**

An insurance "dividend" is an adjustment of the premium between the original estimate and the actual amount found to have been necessary in retrospect (Kern v John Hancock Mut. Life Ins. Co., 8 AD2d 256, 259, 186 N.Y.S.2d 992 [1st Dept 1959], *affd* 8 NY2d 833, 168 N.E.2d 532, 203 N.Y.S.2d 92 [1960]). In other words, an insurance dividend is a partial return to the policyholder of the amount it was charged for the insurance (Spencer, White & Prentis, Inc. v City of New York, 262 App Div 285, 286, 28 N.Y.S.2d 401 [1st Dept], *lv denied 262 App Div 992, 30 N.Y.S.2d 809 [1941]*; Scholem v Prudential Ins. Co., 172 Misc 664, 665, 15 N.Y.S.2d 947 [Sup Ct, NY County 1939]). **[***8]** Therefore, the distribution of an insurance dividend is not akin to a division of surplus among stockholders of record (Kern, 8 AD2d at 259). "The declaration of a dividend upon a policy reduces pro tanto the cost of insurance to the holder of the policy. That is its purpose and effect" (Rhine v New York Life Ins. Co., 273 NY 1, 13, 6 N.E.2d 74 [1936]).

Defendant contends that the courts have upheld the power of an insurer's Board of Directors to declare policyholder dividends. It is true that an insurer's directors have broad discretion as to the determination of surplus, how much of the surplus should be retained by the company, and how much of the surplus should be distributed to policyholders [3] (Rhine, 273 NY at 8; Greeff v Equitable Life Assur. Socy., 160 NY 19, 32, 54 N.E. 712 [1899]; Kern, 8 AD2d at 262; *see generally* 5 Couch on Ins. § 80:51 [3d ed 2007]). The distribution to policyholders of surplus is known as "equitable apportionment" (Rhine, 273 NY at 8 [internal quotation marks omitted]). Courts will not interfere unless there has been bad faith, willful neglect, or abuse of discretion (Greeff, 160 NY at 32). However, plaintiff is not challenging the manner in which defendant computed the dividend, **[***9]** nor is it seeking to compel defendant to declare the dividend in some other manner. Rather, plaintiff is suing defendant for breach of contract for its share of the dividends on the renewal policy (*see* Kern, 8 AD2d at 263).

Insurance Co. of Greater NY v Glen Haven Residential Health Care Facility (253 AD2d 378, 676 N.Y.S.2d 176 [1st Dept 1998]), relied upon by defendant, is not dispositive of the issues in this case. There, the Appellate Division, First Department, stated that "[w]e also agree with the IAS Court that the payment of dividends was within plaintiff's discretion, and that plaintiff was justified in refusing to pay a dividend to defendant based on defendant's failure to meet its obligation to pay the premium" (*id. at 379*). A review **[***10]** of the record on appeal reveals that the dividend provision in that case was identical to the one in this case. Here, in contrast, defendant does not dispute that plaintiff paid its premium until the date of cancellation, when the policy period ended. In fact, defendant remitted $ 18,375.95 in unused premium to plaintiff after the renewal policy was cancelled.

Thus, the court turns to the terms of the renewal policy. "Workers' compensation insurance policies are no more than contracts, and as such are governed by the ordinary rules of contractual construction" (Commissioners of State Ins. Fund v Photocircuits Corp., 20 AD3d [****5] 173, 180-181, 798 N.Y.S.2d 367 [1st Dept 2005]). Where the terms of an insurance contract are clear and unambiguous, they must be given their plain and ordinary meaning, and the interpretation of such terms is an issue of law for the court (*see* City of New York v Continental Cas. Co., 27 AD3d 28, 31, 805 N.Y.S.2d 391 [1st Dept 2005]).

An unambiguous provision is one that is not "reasonably susceptible of more than one interpretation" (McCabe v Witteveen, 34 AD3d 652, 654, 825 N.Y.S.2d 499 [2d Dept 2006] [internal quotation marks and citation omitted]; *see also* Broad St., LLC v Gulf Ins. Co., 37 AD3d 126, 131, 832 N.Y.S.2d 1 [1st Dept 2006], **[***11]** quoting Breed v Ins. Co. of N. Am., 46 NY2d 351, 355, 385 N.E.2d 1280, 413 N.Y.S.2d 352 [1978], *rearg denied 46 NY2d 940, 415 N.Y.S.2d 1027 [1979]* ["contract is unambiguous if the language has a definite and precise meaning, unattended by danger of misconception in the purport of the [agreement] itself, and concerning which there is no reasonable basis for a difference of opinion'"]). "[T]he test to determine whether an insurance contract is ambiguous focuses on the reasonable expectations of the average insured upon

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[3] The purpose of this retention of surplus' funds . . . is to cover all the insurer's risks and obligations, as well as to insure the security of its policyholders in the future as well as the present, and to cover any contingencies that may arise, or that may be fairly anticipated" (5 Couch on Ins. § 80:51 [3d ed 2007]). In determining the amount of surplus to be credited as dividends, the insurer typically considers the amount of premiums paid (*id.*, § 80:54).

reading the policy'" (*Penna v Federal Ins. Co., 28 AD3d 731, 732, 814 N.Y.S.2d 226 [2d Dept 2006]*, quoting *Matter of Mostow v State Farm Ins. Cos., 88 NY2d 321, 326-327, 668 N.E.2d 392, 645 N.Y.S.2d 421 [1996])*. But a literal construction which places one party at the mercy of the other should be avoided, if possible (*McGrail v Equitable Life Assur. Socy. of U.S., 292 NY 419, 424, 55 N.E.2d 483*, *rearg denied 293 NY 663, 56 N.E.2d 258 [1944]*; *Lowy & Donnath v City of New York, 98 AD2d 42, 45, 469 N.Y.S.2d 760 [1st Dept 1983]*, *affd 62 NY2d 746, 465 N.E.2d 369, 476 N.Y.S.2d 830 [1984]*; *Jacobowitz v Mutual Benefit Health & Acc. Assn., 10 AD2d 159, 162, 198 N.Y.S.2d 7 [1st Dept 1960])*.

If the terms of an insurance contract are ambiguous, the terms must be construed in favor of the insured and against the insurer, the drafter of the policy language (*Marshall v Tower Ins. Co. of NY, 44 AD3d 1014, 1015, 845 N.Y.S.2d 90 [2d Dept 2007]*; **[***12]** *Tower Ins. Co. of NY v Breyter, 37 AD3d 309, 830 N.Y.S.2d 122 [1st Dept 2007]*; *242-44 E. 77th St., LLC v Greater NY Mut. Ins. Co., 31 AD3d 100, 105, 815 N.Y.S.2d 507 [1st Dept 2006])*. However, the terms of an insurance contract are not ambiguous simply because the parties interpret the language differently (*Commercial Union Ins. Co. v Liberty Mut. Ins. Co., 36 AD3d 645, 645-646, 828 N.Y.S.2d 479 [2d Dept 2007])*.

In the instant case, the renewal policy states that plaintiff "shall participate in the earnings of the Company to such extent and upon such conditions as shall be determined by the Board of Directors of the Company in accordance with Law and as made applicable to this policy provided that [plaintiff] shall have complied with all of the terms of this policy with respect to the payment of premium" (Hess Affirm., Exh. B, policy jacket). The plain language of this provision is clear and unambiguous. Although the provision states that plaintiff "shall" participate in the earnings of the Company, this phrase is clearly modified by "*upon such conditions as shall be determined by the Board of Directors of the Company."* Any reasonable insured would read this provision to mean that defendant's Board of Directors had the discretion to make **[***13]** payments of any dividends, and that dividends were not guaranteed. The court is not free to rewrite the insurance contract based upon plaintiff's subjective interpretation of the policy language or notions of fairness (*see* *Broad St., LLC, 37 AD3d at 131*, quoting *Bretton v Mutual of Omaha Ins. Co., 110 AD2d 46, 49, 492 N.Y.S.2d 760 [1st Dept]*, *affd 66 NY2d 1020, 489 N.E.2d 1299, 499 N.Y.S.2d 397 [1985]* [" [a] court, no matter how well intentional, cannot create policy terms by implication or rewrite an insurance contract. Nor should a court disregard the provisions of an insurance contract which are clear and unequivocal'"]). While the covenant of good faith and fair dealing is implicit in every contract, it cannot be used to add terms to a contract between two sophisticated parties, as here (*see* *D & L Holdings v Goldman Co., 287* **[****6]** *AD2d 65, 73, 734 N.Y.S.2d 25 [1st Dept 2001]*, *lv denied 97 NY2d 611, 769 N.E.2d 351, 742 N.Y.S.2d 604 [2002])*. Moreover, plaintiff was aware of the terms of the renewal policy since the relevant terms were identical to those in the original policy, and the original policy was automatically renewed in the absence of notice of defendant's intention not to renew that policy (*see* *Workers' Compensation Law § 54 [5]*).

On October 1, 1997, the Board of Directors made **[***14]** a resolution to pay dividends on policies covering risks in New York, but not for "policies or renewals thereof which have been canceled [by the insured] prior to their full term of one year, . . . [] unless such policy or renewal has been immediately replaced by another policy written by the Company or its parent" (Hess Affirm., Exh. B, at 4). Plaintiff cancelled its policy approximately eight months into the renewal policy, and did not replace its policy with defendant, and thus, did not pay premiums for the entire one-year period of the renewal policy. Notably, plaintiff does not allege or claim here that defendant abused its discretion or made this determination in bad faith (*see* *Rhine, 273 NY at 8*). [4] Therefore, plaintiff was not entitled to a dividend.

Accordingly, it is

ORDERED that the motion by defendant Insurance Company of Greater New York for summary judgment is granted and the complaint is dismissed with costs and disbursements to defendant as taxed by the Clerk of the Court upon the submission of an appropriate bill of costs; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

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[4] Plaintiff appears to argue that defendant unfairly discriminated against it by failing to pay a dividend, relying upon *Fidelity & Cas. Co. of NY v Metropolitan Life Ins. Co. (42 Misc 2d 616, 248 N.Y.S.2d 559 [Sup Ct, NY County 1963])*. However, that case dealt with equitable apportionment of dividends (*id. at 627*). In this case, plaintiff did not receive any dividends at all, and does not claim that any insured that cancelled early did in fact receive **[***15]** any dividends.

This Constitutes the Decision and Order of the Court.

Dated: January 18, 2008

End of Document

Vidal v. Maldonado

Supreme Court of New York, Bronx County

December 8, 2008, Decided

23718/2006

Reporter

23 Misc. 3d 186 *; 873 N.Y.S.2d 842 **; 2008 N.Y. Misc. LEXIS 7200 ***; 2008 NY Slip Op 28523 ****

[**1]** Victor Vidal, Plaintiff, v Ricardo Maldonado et al., Defendants.

Counsel: **[***1]** *Law Office of Thomas K. Moore*, White Plains (*Nick Migliaccio* of counsel), for defendants. *Pena & Kahn*, Bronx (*John M. Martello* of counsel), for plaintiff.

Judges: Paul A. Victor, J.S.C.

Opinion by: Paul A. Victor.

Opinion

[*187] **[**844]** Paul A. Victor, J.

Relief Sought

Defendants Ricardo Maldonado and Zobeida Franco move for summary judgment pursuant to *CPLR 3212* and dismissal of the complaint against them, for the failure of the plaintiff Victor Vidal to prove that he has sustained a "serious injury," as that term is defined in *section 5102 of the Insurance Law*.

Another Frustrating Assembly Line "Serious Injury" Motion

The defendants' motions and plaintiffs' responses have become almost assembly line, "cookie cutter" prototypes; and attorneys for defendants (and most plaintiffs) have become expert on how to present or attack a serious injury claim.

Defendants are very adept at providing prima facie proof demonstrating that a plaintiff has not suffered a serious injury; proof at the very least sufficient to meet their "initial burden" to present competent evidence that plaintiff has no cause of action. Plaintiffs, too, have become quite conversant with the requirements to defeat a defendant's motion.

Defendant's counsel usually submits at least two (sometimes **[***2]** three) affirmations of **[****2]** so-called "independent" [1] medical experts **[**845]** (an orthopedist, a neurologist, and radiologist, usually from the same stable of defense medical experts), each of whom examine the plaintiff and/or the reports and tests submitted by plaintiff, and then by affirmation refute plaintiff's claim to have sustained a serious injury. These examinations usually take place years after the automobile accident which has been alleged to cause injury, and each of the defendant's medical experts conclude that plaintiff is no longer impaired or injured; that all tests and **[*188]** findings are normal; that if originally injured, said injuries have resolved; and that, in any event, all of plaintiff's claimed limitations or impairments have been caused, not by the accident, but by degenerative (normal aging process) changes in the cervical and lumbar regions. Except for the dates and the unique peripheral circumstances presented by each case, these medical reports and affirmations submitted by defendant's chosen medical experts, are virtually identical. Plaintiff's submissions, made in opposition to a defendant's motion, are no less boilerplate.

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[1] Although these examinations are customarily **[***3]** referred to as "independent medical examinations," this court recognizes that such is not truly the case. As aptly stated in *Bazakos v Lewis (56 AD3d 15, 18, 864 NYS2d 505 [2d Dept 2008])*,

> "the time has come to acknowledge the essential nature of the relationship inherent in the performance of a statutory medical examination, pursuant to *22 NYCRR 202.17*, by a physician retained and paid by a defendant's insurance carrier to assist in the defense of a personal injury action and the duty that flows to a party outside that relationship--in this case a personal injury plaintiff. It is beyond cavil that a statutory medical examination is an adversarial process. The examinee's attendance is compelled by rule of law (*see 22 NYCRR 202.17*), and his or her engagement and interaction with the examining physician is nonconsensual."

Following an automobile accident many of the claims made by plaintiffs seem to have the same script; and many of the medical experts also are drawn from an oft-used and known pool of plaintiffs' physicians. In addition to "treating" physicians (usually a chiropractor and/or physiatrist, and sometimes the family doctor), plaintiff's proof of serious injury is "supported" **[***4]** (as it must be in accordance with judicially imposed guidelines) by an attempt to provide the "qualitative" or "quantitative" assessment of an orthopedist or a neurologist, who, after conducting a number of range of motion (ROM) tests (which are said to be positive because of the detection of spasm), and reviewing a positive MRI and/or an EMG/NCV test, concludes that plaintiff has a herniated disc or bulges which impinge on the thecal sac and thus causing significant limitations and quality of life impairments which meet the statutory definition of serious injury.

Great Expenditure of Limited Judicial Resources

Trial courts are then presented with the "serious injury" issue on a motion made by a defendant for summary judgment; and the court must then use its "powers" to discern whether the minimum legal requirements have been met to send the case to a trial by jury. The motions **[****3]** and papers submitted by both sides are usually copious, and thus, a thorough review of the record and current appellate decisions requires a great expenditure of limited judicial time. In any event, the decision rendered is usually challenged and refuted by the losing side; and thus many (too many) of these **[***5]** cases are appealed, and many of those appeals result in nonunanimous (and sometimes acrimonious) decisions which are often difficult to reconcile with prior precedent.

Elusive Standards

The enabling legislation for the No-Fault Law itself provides little or no guidance to the bench and bar as to the scope of the terms used. For example, one should reasonably assume that the legislature sought to distinguish "*significant limitation* of **[*189]** use of a body *function or system*" from a "*consequential limitation* of use of a *body organ or member*." (*Insurance Law § 5102 [d]* [emphasis added].) However, there appears to be no practical difference. Some courts have held that "consequential" means "significant" (*see e.g. Altman v Gassman, 202 AD2d 265, 608 NYS2d 651 [1st Dept 1994]*); and there are abundant cases in which all of the above terms **[**846]** (including body function, system, organ or member) are used interchangeably. The guidelines, conditions and examples provided by the Court of Appeals in a series of decisions, including *Toure v Avis Rent A Car Sys. (98 NY2d 345, 774 NE2d 1197, 746 NYS2d 865 [2002]* [cited and discussed infra]), although very helpful, have not entirely unburdened the trial courts; and these serious injury claims continue to be the cause of incessant motion practice, and an abundant use of judicial resources at both the trial **[***6]** and appellate levels.

Issues Presented Herein

This case, like all other "serious injury" cases, presents the court with the ongoing and frustrating conundrum of deciding when a plaintiff's injury qualifies as significant within the meaning of the No-Fault Law.

As noted in a three to two decision rendered by the Appellate Division, First Department, concerning a similar "serious injury" claim: "This personal injury lawsuit . . . *once again* presents us with the sometimes *frustrating task* of deciding when evidence presented on a motion for summary judgment meets the serious injury threshold . . . , *an elusive standard that all too frequently escapes facile and final resolution*" (*Brown v Achy, 9 AD3d 30, 31, 776 NYS2d 56 [1st Dept 2004]* [internal quotation marks omitted; emphasis added]).

Factual Background

The accident underlying this case occurred on December 21, 2004 at approximately 12:45 p.m. at the intersection of E. 188th St. and Cambreleng Avenue in the Bronx, at which time and place the vehicles owned and driven by the plaintiff and defendant collided. The 33-year-old plaintiff, who did not lose consciousness, and was not bleeding, was removed from the scene of the accident by ambulance and taken to St. Barnabas Hospital. At the hospital, he **[***7]** complained of pain in his chest, neck and back, and he stated that, even though he was wearing a seatbelt, his chest hit the steering wheel. X rays were taken of the cervical spine and of the chest, both of which were determined to be negative. Thereafter, he was released the same day.

[*190] On December 30th, nine days postaccident, plaintiff came under the care of Dr. Vladimir Zlatnik, an internist. The underlying treatment records, and the empirical data contained therein, were provided and reviewed by the defendants' physicians, but were not submitted to the court. **[****4]** All of the information concerning the substance of plaintiff's care and treatment is gleaned from the affirmation of Dr. Zlatnik, dated April 21, 2008, which was submitted in opposition to defendants' motion to dismiss. In any event, on plaintiff's first visit to Dr. Zlatnik, the plaintiff reported that after the accident he had ringing in his ears and nausea; and he complained of neck pain radiating down to his shoulders with numbness; periods of dizziness when turning his head; shooting pain in his arms when turning his neck, especially on the left side; and lower back pain which gets worse on physical exertion and which **[***8]** spreads to the right buttocks, right thigh and leg, with a tingling sensation. On that occasion Dr. Zlatnik conducted a neurological and physical examination which, with the use of a goniometer, included cervical and lumbar range of motion tests and measurements; and he found that Mr. Vidal "suffered from a limited range of motion of the cervical and lumbar spines," and diagnosed the plaintiff with "traumatic nerve root injury, plexopathy due to plexus stretching of compression pain by injured muscles, referred nociceptive pain, myofascial pain syndrome with cervical and lumbar spine trigger points and a lumbosacral sprain." Despite the use of the goniometer, the numerical measurements of the limitations are not **[**847]** set forth anywhere in the plaintiff's submissions. Dr. Zlatnik does state in his affirmation, however, that they were "less than the normal range of motion."

Based on all of the above, plaintiff was started on a course of aggressive physical therapy (which continued from December 30, 2004 until May 27, 2005), and he was "sent for MRI and other diagnostic testing," including nerve conduction velocity (EMG/NCV) tests. However, only the results of the MRI, which was conducted on **[***9]** January 17, 2005, are presented to the court on this motion.

The MRI testing of plaintiff's lumbar and cervical spine was conducted by Dr. John Rigney, a radiologist, who in an affirmation dated April 15, 2008 states that the plaintiff "suffered a posterior disc herniation at L5-S1 into the epidural fat abutting the interior sac margin and anterior disc bulges into the prevertebral soft tissues at L2-3 and L4-5; [and] . . . posterior disc bulges at C3-4, C4-5 and C5-6 all of which impinge on the thecal sac."

[*191] In the MRI report, attached to the affirmation dated January 17, 2005, the following additional relevant findings are set forth: a straightening of the lumbar curvature, and a mild loss in the signal intensity of the L2-3, L4-5, and L5-S1 intervertebral discs "which reflect mild and slight loss in fluid content respectively."

On February 8, 2005, after a review of his own records together with the MRI results, Dr. Zlatnik concluded that plaintiff's cervical and lumbar injuries "were caused as a result of [plaintiff's] motor vehicle accident of December 21, 2004"; and "it was determined that the best course of treatment would be continued physical therapy," which, as noted above, lasted **[***10]** until May 16, 2005.

In May of 2005, the physical therapy sessions were discontinued because the plaintiff's "no-fault benefits were terminated" and Dr. Zlatnik determined that, in any event, "any further physical therapy would have only been palliative in nature." In his affirmation Dr. Zlatnik states: **[****5]**

> "The course of treatment was designed to decrease pain, promote healing of the affected areas and restoration to pre-injury range of motion, strength and functional capabilities. *However, Mr. Vidal made slow, poor and erratic improvement while under our care and continued to suffer with severe pain and exacerbations upon performance with his daily activities*." (Emphasis added.)

Dr. Zlatnik next and last examined the plaintiff almost three years later, on April 7, 2008, and reported in his affirmation, that "it is my *impression* that [plaintiff] continued with residual signs of right sided L5 radiculopathy and post-traumatic myofascial pain syndrome." In paragraph 13 of the affirmation, Dr. Zlatnik also states that:

> "There is objective verification of the injuries suffered by Mr. Vidal based upon my most recent examination as well as his course of physical therapy and diagnostic test results. **[***11]** My opinion as to the degree of permanence is based [on] these objective measurements as well as how his injuries affect his daily activities. In sum, because of the severity of the symptomatology as well as the persistence of the plaintiff's signs and symptoms, Mr. Vidal is limited in his daily activities and will continue to be because of the injuries he suffered to his back as a direct result of the accident on December 21, 2004. The plaintiff, as set forth in his complaints above, **[*192]** has difficulty lifting and bending. Further, since the date of his accident, he has been unable to perform his usual and customary activities as he did before the accident."

[848]** In the above-quoted statement Dr. Zlatnik appears to lump all of his examinations and findings together, and thus it is difficult to determine what, if any, objective findings were made on this last occasion to support Dr. Zlatnik's "impressions."

In any event, Dr. Zlatnik in his affirmation concludes and states (with reference to plaintiff's claimed ongoing limitations) that:

> "The lumbar and cervical spine are areas that will continue to present problems and will cause difficulties for the rest of Mr. Vidal's life. Based upon the severity **[***12]** of Mr. Vidal's symptoms, results of examinations and past experience with similar cases, the injuries that were sustained will result in a predisposition to further complications. *The trauma of the accident will cause abnormal degenerative changes at an accelerated rate. As such, he will surely sustain greater restrictions in his ranges of motion. The herniating and bulging discs produce localized pain and radicular symptoms; [and] Mr. Vidal's prognosis is guarded.* His injuries are causally related to his accident of December 21, 2004. I found him to be permanently disabled from performing heavy lifting or strenuous types of activity" (emphasis added).

At the time of the accident, the plaintiff was employed seven days a week in two different jobs. The first as a supervisor at a company called PCF, which is a publication service for the **[****6]** New York Times, in which capacity he supervises 360 delivery people. At this job he was required to drive around to make sure that the various routes were being covered. As an employee of PCF, plaintiff worked every night from 1:30 a.m. to 7:30-8:00 a.m., except Wednesday and Thursday. In his second job, plaintiff is employed as a messenger for a company **[***13]** called SDS, based in Long Island City, where he would drive to deliver medications to various dental offices. He normally worked at that job Monday through Friday from 9:30 a.m. to 5:30-6:00 p.m. As a result of the injuries sustained he was apparently unable to work for approximately one month; and has been fully employed at both jobs to date.

The Defendants' Motion

Defendants claim that the plaintiff has not sustained a "serious injury," as that term is defined in *sectopm 5102 of the Insurance Law*; **[*193]** and in support thereof they submit the affirmation of Dr. Charles Totero, an orthopedist, and the report of Dr. Stephen Mendelsohn, a radiologist.

Dr. Totero saw the plaintiff on November 14, 2007 and conducted a comprehensive orthopedic evaluation, as well as a review of all of plaintiff's prior medical records, [2] and the report submitted by defendant's radiologist, Dr. Stephen Mendelsohn. After obtaining and recording the history of the accident as well as plaintiff's work history and past medical history, the following *present complaints* were set forth: "The claimant tells me that his neck is improving little by little. He does have some pain which is intermittent. He complains primarily of back pain, particularly **[**849]** with cold weather and certain types of activities. He complains of no radiation of the pain and no paresthesis."

The comprehensive affirmation and report includes the following range of motion findings: in the lumbar spine, extension was to 20 degrees (normal 20 degrees to 30 degrees); flexion to 75 degrees (normal 70 degrees to 90 degrees); left and right tilt 30 degrees **[***15]** (normal 30 degrees to 45 degrees), the straight-leg raising test was negative bilaterally although there was a complaint of left-sided low back pain on the left at 90 degrees; in the cervical spine, extension to 30 degrees (normal 30 degrees to 45 degrees); flexion to 50 degrees (normal 40 degrees to 50 degrees); and left and right rotation 75 degrees (normal 70 degrees to 90 degrees).

Apart from all of the negative observations, Dr. Totero records, with reference to the lumbar region, that "there is a mild left lumbar tenderness," and that plaintiff "complains of **[****7]** left-sided low back pain on SLR on the left to 90°"; and with reference to the cervical region that plaintiff "does complain of pain posteriorly on limits of motion" and that "there is mild tenderness about the vertebral prominence (C7) and posteriorly." It is also noted that although all ROMs are "within the normal **[*194]** range," some of them are at the very bottom of the ROM spectrum. In any event, Dr. Totero made a diagnosis of "cervical sprain and lumbar sprain" and

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[2] Dr. Totero affirmed that he reviewed the following records: the plaintiff's bill of particulars; neurological evaluation of Dr. Zlatnik of December **[***14]** 30, 2004; the MRI of the cervical and lumbar spines of January 17, 2005; the ambulance call report of December 21, 2004; emergency room record from St. Barnabas Hospital, including reports of X rays of the cervical spine and chest X ray, as well as report of an EKG, taken on December 21, 2004; medical records from Rego Park Rehabilitation; handwritten physical therapy progress notes; electrodiagnostic studies of both the upper and lower extremities, performed by Dr. Zlatnik on January 31, 2005; MRI of the thoracic spine from January 17, 2005; and the interpretation of the cervical and lumbar MRIs, by Dr. Stephen Mendelsohn.

concluded that since there was no "objective orthopedic findings" and "claimant is undergoing no active treatment **[***16]** at this time [and] is currently working in his regular capacity without restrictions, [i]t is *my impression* that this claimant exhibits no causally-related disability *at this time* [and] requires no further treatment and/or diagnostic testing." (Emphasis added.) Dr. Totero also specifically noted that he only reviewed the MRI *report* and that "the films should be provided for my review and a supplemental will be done at that time." No supplemental report has been provided.

Dr. Stephen Mendelsohn, a radiologist, reviewed the MRI films of the plaintiff's lumbar and cervical spine and concluded that the plaintiff suffered from "moderate degenerative changes at the L2-3 and L4-5 discs," and "mild multilevel cervical degenerative changes"; and that the MRIs "reveal no evidence of focal disc herniation or any trauma related abnormality." He did, however, specifically find, with reference to C3-4, C4-5 and C5-6, "mild circumferential degenerative *bulging*; and with reference to L4-5 and L2-3 moderate desiccation and mild (or L2-3 moderate) loss of height with moderate to circumferential (L2-3) degenerative bulging"; and disagreed "with the interpretation . . . provided by Dr. John Rigney in so **[***17]** far as I find no evidence of disc herniation."

The defendants argue that since the plaintiff admitted that he was unable to work for only one month, had no complaints of pain when examined, was no longer undergoing any physical therapy or medical treatment for the claimed injuries, and had not done so for the last three years, his injuries have resolved and were neither significant nor consequential.

Plaintiff's Opposition

In opposition to defendant's motion, plaintiff submits the hospital emergency room records, his own affidavit as well as the affirmation of Dr. Zlatnik, and the affirmation of Dr. John Rigney, a radiologist, as reviewed above. As to the "gaps in treatment," it was explained by plaintiff and Dr. Zlatnik that the failure to pursue further medical treatment after June of 2005 was caused by plaintiff's inability to afford the medical expenditures after the no-fault benefits were cut off and because treatment would have only been "palliative in nature." Plaintiff states further that, although he continues to work two jobs (over a seven-day period each week), his injuries continue to affect **[*195]** his quality of **[**850]** life, including his "relationship" with his wife, and claims that, **[***18]** to date, he is also unable to lift anything heavy, grocery shop, or play soccer or volleyball.

Applicable Law

"Serious Injury"

Under the No-Fault Law, in order to maintain an action for personal injury, a plaintiff must establish that a "serious injury" has been sustained. (*Licari v Elliot, 57 NY2d 230, 441 NE2d 1088, 455 NYS2d 570 [1982]*.) The term "serious injury" is defined in *scetion 5102 of the Insurance Law* as follows:

> ""(d) 'Serious injury' means a personal injury which results in death; dismemberment; disfigurement; a fracture; loss of a fetus; *permanent loss of use of a body organ, member,* ***[****8]*** *function or system; permanent consequential limitation of use of a body organ or member; significant limitation of use of a body function or system*; or a medically determined injury or impairment of a non-permanent nature which prevents the injured person from performing substantially all of the material acts which constitute such person's usual and customary daily activities for not less than ninety days during the one hundred eighty days immediately following the occurrence of the injury or impairment." (Emphasis added.)

The proponent of a motion for summary judgment must tender sufficient evidence to show the absence of any material **[***19]** issue of fact and the right to judgment as a matter of law. (*Alvarez v Prospect Hosp., 68 NY2d 320, 508 NYS2d 923 [1986]*; *Winegrad v New York Univ. Med. Ctr., 64 NY2d 851, 487 NYS2d 316, 476 NE2d 642 [1985]*.) In the present action, the burden rests on defendant to establish, by the submission of evidentiary proof in admissible form, that plaintiff has not suffered a "serious injury." (*Lowe v Bennett, 122 AD2d 728, 511 NYS2d 603 [1st Dept 1986]*, *affd* 69 NY2d 700, 512 NYS2d 364, 504 NE2d 691 [1986].) When a defendant's motion is sufficient to raise the issue of whether a "serious injury" has been sustained, the burden shifts, and it is then incumbent upon the plaintiff to produce sufficient prima facie evidence *in admissible form* to support the claim of "serious injury." (*Licari, supra*; *Lopez v Senatore, 65 NY2d 1017, 484 NE2d 130, 494 NYS2d 101 [1985]*.)

A plaintiff cannot defeat a motion for summary judgment and successfully rebut a prima facie finding that he did not sustain a "serious injury," merely by relying solely on documented subjective complaints of pain (*Uddin v Cooper, 32 AD3d 270, 820 NYS2d 44 [1st Dept 2006]*), or by the mere submission of an MRI report **[*196]** demonstrating the existence of a bulging or herniated **[***20]** disc, absent medical proof of a significant physical limitation related thereto. (*Nelson v Amicizia, 21 AD3d 1015, 803 NYS2d 87 [2d Dept 2005]*; *Guzman v Michael Mgt., 266 AD2d 508, 698 NYS2d 719 [2d Dept 1999]*.)

The "Permanent Consequential" and "Significant Limitation" Categories

Claims of "serious injury" under the "permanent consequential limitation" category and under the "significant limitation" category are the most difficult for trial and appellate courts to assess. As noted above, these terms are not defined and many times are used interchangeably. In an effort to assist the trial courts, and to better implement the "legislative intent … to weed out frivolous claims and limit recovery to significant injuries," the Court of Appeals, in *Toure v Avis Rent A Car Sys. (98 NY2d 345, 774 NE2d 1197, 746 NYS2d 865 [2002])*, reviewed and discussed three cases in its decision, **[**851]** discussed infra (*Toure v Avis Rent A Car Sys.*; *Manzano v O'Neil*; *Nitti v Clerrico*).

In the *Toure* and *Manzano* cases, the plaintiffs claimed serious injury under the "permanent consequential" and/or "significant limitation" categories, whereas in *Nitti*, the plaintiff claimed injury under the 90/180-day category. Significantly, in its preamble paragraph for all three cases, the **[***21]** Court emphasized that in "these three cases [it] examine[d] the nature and extent of . . . *objective medical proof* necessary for a plaintiff to meet the 'serious injury' threshold under the No-Fault law." (*98 NY2d at 350* [emphasis added].) The Court cautioned that "subjective complaints *alone* are not sufficient"; and explained that an expert opinion, *if supported by objective evidence*, can be used to **[****9]** substantiate a claim of serious injury; and that, *without an objective basis*, an expert's opinion may be deemed wholly speculative, and the claim can be found to be frivolous and/or insignificant. (*Id.* [emphasis added].)

The minimum required content of an expert's opinion was also discussed by the Court of Appeals. For the "limitation" categories of serious injury, the Court stated that the expert can provide *either* a "quantitative" or a "qualitative" assessment of plaintiff's condition. In other words, in order to establish the seriousness of the plaintiff's physical limitations, a plaintiff may provide *either* "an expert's designation of a numeric percentage of a plaintiff's loss of range of motion" (i.e., a quantitative assessment); *or* an expert's evaluation which "compares the plaintiff's **[***22]** limitations to the normal function, purpose and use of the affected body organ, member, function or system" (i.e., a **[*197]** *qualitative* assessment) (*id.*). In the former assessment, the expert numerically measures and compares normal ranges of motion with plaintiff's claimed loss, *and provides* the percentage of the loss of range of motion, whereas in the latter assessment, the expert, without numerical reference, merely compares plaintiff's limitations with normal function, purpose and use of the affected body part. In each instance, the expert must causally connect the injury to the accident and must attribute said limitations to the injuries sustained and the complaints made by plaintiff. A summary of the three cases reviewed in *Toure* is instructive:

In *Toure*, plaintiff commenced an action to recover damages for neck and back injuries which allegedly resulted in a "permanent consequential limitation of a body organ or member" and/or in a "significant limitation of the use of a body function or system."

Defendants moved to dismiss each of plaintiff's claims and submitted sufficient medical affirmations and other prima facie proof, which indicated that plaintiff had recovered, and had **[***23]** not sustained a "serious injury" within the meaning of the No-Fault Law. Plaintiff in opposition submitted his own affidavit, as well as the affirmation of a neurosurgeon who had treated plaintiff for a year and a half prior to defendants' motion, *together with MRI and CT scan tests and reports*.

The Supreme Court had granted defendants' motion and dismissed the complaint, and the Appellate Division affirmed, with two Justices dissenting; the plaintiff appealed to the Court of Appeals as of right. After an examination of all the proof submitted, the Court of Appeals concluded that "[it could not] say that the alleged limitations of plaintiff's neck and back are so 'minor, mild or slight' as to be considered insignificant within the meaning of *Insurance Law § 5102 (d)*," and reversed the orders below and reinstated **[**852]** the complaint. (*98 NY2d at 353*) It is significant to note that, in doing so, the Court of Appeals expressly noted that a *quantified* measurement of plaintiff's limitations was not necessary. The Court stated that "[although plaintiff's expert's affirmation] does not ascribe a specific percentage to the loss of range of motion in plaintiff's spine, he sufficiently **[***24]** describes the 'qualitative nature' of plaintiff's limitations 'based on the normal function, purpose and use of the body part" (*id.*). It was sufficient, said the Court, that the expert "attribute[d] the limitations in plaintiff's physical activities to the nature of the injuries sustained by opining that plaintiff's **[*198]** 'difficulty in sitting, standing or walking for any extended period of time and his inability to lift heavy boxes at work are a natural and expected medical consequence of his injuries' " (*id.*). The Court of Appeals, however, also **[****10]** again emphasized that the plaintiff's expert's *qualitative assessment* was "*supported by objective medical evidence, including MRI and CT scan tests and reports, paired with his observations of muscle spasms during his physical examination of plaintiff.*" (*Id.* [emphasis added].)

In *Manzano v O'Neil*, the New York Court of Appeals granted leave to appeal from an order of the Appellate Division, Fourth Department, which had reversed a judgment of the Supreme Court, entered after a jury verdict in favor of plaintiff in an action in which plaintiff claimed to have sustained a "permanent consequential limitation of a body organ or member."

At the trial plaintiff **[***25]** and her husband had testified that after the accident she was taken to the hospital because of pain and tingling in her neck and spine, released the same day, and when pain persisted she was treated by several health care providers and received physical therapy. However, despite said treatment, she testified that she "can no longer do heavy lifting of any kind … cannot shovel the driveway like I used to . . . don't clean the house like I used to . . . can't carry the vacuum cleaner [and] can't pick up my children." (*Manzano at 354*.)

Plaintiff's expert, an orthopedic surgeon who had treated plaintiff on four occasions, testified that upon examination he found plaintiff had tenderness in her neck and low back as well as "discomfort with extremes of motion of her neck" all of which "sprains" were consistent with a rear-end collision (*id*.). Upon review of MRI films which were admitted into evidence, he concluded that plaintiff had suffered two herniated discs in her cervical spine. The Court of Appeals expressly noted that "[plaintiff's expert] opined that this injury was consistent with plaintiff's complaints regarding the physical limitations of her neck and back . . . [and] stated that plaintiff's injury was permanent, **[***26]** a conclusion founded on the plaintiff's 'history, physical examination, [and] the review of the MRI scan' " (*id.*).

The Court of Appeals again rejected the notion that only an expert's *quantitative* assessment can support an action of "serious injury," and again expressly noted that the expert's opinion and findings were sufficiently supported by a qualitative assessment and objective evidence:

> "Although th[e] medical expert did not assign a **[*199]** *quantitative* percentage to the loss of range of motion in plaintiff's neck or back, he described the *qualitative* nature of plaintiff's limitations based on the normal function, purpose and use of her body parts. *In particular, [the expert] correlated plaintiff's herniated discs with her inability* ***[**853]*** *to perform certain normal, daily tasks. These limitations are not so insignificant as to bar plaintiff's recovery*" (*id. at 355* [emphasis added]).

In *Nitti v Clerrico*, the Court of Appeals reversed an order of the Appellate Division, Fourth Department, which had affirmed the judgment of the Supreme Court entered upon a jury **[****11]** verdict in favor of plaintiff under the 90/180-day category. That "serious injury" category [3] requires the plaintiff **[***27]** to establish that he suffered "a medically determined injury or impairment of a non-permanent nature which prevented [him] from performing substantially all of the material acts which constitute [his] usual and customary daily activities for not less than ninety days during the one hundred eighty days immediately following the occurrence of the injury or impairment" (*Insurance Law § 5102 [d]*). Defendants did not contest the "substantiality" of plaintiff's limitations, and thus, the only issue presented for review was "simply whether plaintiff offered sufficient *objective* medical evidence to establish a qualifying injury or impairment" (*Nitti at 357* [emphasis added]). In that regard the reliability of the alleged corroborating evidence (back spasm and an MRI) was challenged by defendants and reviewed by the Court of Appeals.

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[3] When a claim is raised under this category of serious injury, it has been held that the plaintiff must provide proof that his or her activities were curtailed to a "great extent," rather than to a "slight" one (*Berk v Lopez, 278 AD2d 156, 157, 718 NYS2d 332 [1st Dept 2000]*; *Szabo v XYZ, Two Way Radio Taxi Assn., 267 AD2d 134, 700 NYS2d 179 [1st Dept 1999]*; ***Badger v Schinnerer, 301 AD2d 853, 754 NYS2d 399 [3d Dept 2003]***; *Dabiere v Yager, 297 AD2d 831, 748 NYS2d 38 [3d Dept 2002]*) and the proof as to the **[***28]** claimant's alleged medically determined injury or impairment must be supported by objective evidence. (*Nitti v Clerico, supra*; *Uddin v Cooper, 32 AD3d 270, 820 NYS2d 44 [1st Dept 2006]*; ***Alexander v Garcia, 40 AD3d 274, 835 NYS2d 147 [1st Dept 2007]***.) Of course, neither the statute nor the decisions define and clearly distinguish a "great" impairment from a "slight" one, and thus we have another amorphous standard.

At trial the plaintiff's expert testified that he "detected spasm" but he inexplicably did not state what test he performed to elicit that spasm, but more importantly, conceded, upon cross-examination, that his conclusion concerning plaintiff's limitations were "*subjective in nature* as they relied on plaintiff's **[*200]** complaint of pain" (*id. at 357-358*). His testimony and the trial record concerning the MRI were equally deficient. Neither the MRI, nor the MRI report, were introduced into evidence, and the expert merely "mentioned" the MRI report but did *not* even substantiate "that the underlying MRI film supported his diagnosis of an L4-5 intervertebral disk disorder" (*id. at 358* [internal quotation marks omitted]). The Court of Appeals, although acknowledging that "medical testimony concerning observations of a spasm can constitute objective evidence" and that "an expert's conclusion **[***29]** based on a review of MRI films and reports can provide objective evidence of a serious injury," held, in view of the above deficiencies, that *there was no reliable objective evidence* supporting the plaintiff's claim (*id. at 357-358*). The Court observed:

> "Although medical testimony concerning observations of a spasm can constitute objective evidence in support of a serious injury, *the spasm must be objectively ascertained*. This requirement was not satisfied by the testimony of plaintiff's expert that he detected a spasm, *where he did not, for example, indicate what test, if any, he performed to induce the spasm. Furthermore, Dr. Patriarco testified on cross-examination that the tests he administered to reach his conclusion regarding plaintiff's limitation of motion were subjective in nature as they relied on plaintiff's complaints of pain. Nor did the MRI report he mentioned constitute objective proof. Toure* and *Manzano* recognize **[**854]** that an expert's conclusion based on a review of MRI films and reports can provide objective **[****12]** evidence of a serious injury. In this case, however, the witness merely mentioned an MRI report without testifying as to the findings in the report. Moreover, *the MRI report was not **[***30]** introduced into evidence*, thus foreclosing cross-examination. Nor did Dr. Patriarco testify that the underlying MRI film supported his diagnosis of an 'L4-5 intervertebral disk disorder.' " (*Id.* [emphasis added].)

Inconsistent Application of *Toure* Guidelines

A comparison of opinions issued in the Appellate Division, First Department, after *Toure* will exemplify the frustrations and difficulty encountered by all courts when attempting to discern whether the plaintiff has proffered sufficient evidence to establish a "serious injury." (*See and compare Brown v Achy, 9 AD3d 30, 31,* ***[*201]*** *776 NYS2d 56 [1st Dept 2004]*, *with Parreno v Jumbo Trucking, 40 AD3d 520, 836 NYS2d 593 [1st Dept 2007]*.) These decisions, which were both issued in the First Department, appear to be inconsistent with each other; and the *Parreno* decision seems to impose conditions which are more harsh than those set forth by the Court of Appeals in the *Toure* series of cases. It is noted that in *Parreno* (which was decided by a different panel of jurists in the First Department than those in *Brown*), no attempt is made to distinguish or recall *Brown* or its rationale.

The *Brown* Decision

In *Brown*, the trial court granted defendant's motion for summary **[***31]** judgment and dismissed the complaint for failure to establish a serious injury. Upon appeal to the Appellate Division, First Department, in a three to two decision (with a vigorous dissent) the order was reversed and the complaint reinstated. At the trial level, in opposition to defendant's motion, the plaintiff submitted an MRI which demonstrated a cervical disc herniation at C3-4, as well as an EMG/NCV test (conducted six months later) which demonstrated abnormal findings at C5-6 and L5-S1 levels, and an expert's medical affirmation which indicated that plaintiff had a 25% loss of lateral flexion and rotation cervically, and a 25% loss of forward flexion in the lumbar spine. The doctor's findings and conclusions were based upon a recent examination which included a seated straight-leg raising test which was "positive" bilaterally at 60 degrees. It was the doctor's further conclusion that the plaintiff had a "permanent partial disability." The majority held that findings of a 25% loss of flexion in the cervical and lumbar spines, *although "in part" based upon plaintiff's subjective complaint of pain during range of motion tests*, nevertheless raised a question of fact as **[***32]** to whether or not the plaintiff sustained a "serious injury" especially because these findings were supported by "other" objective evidence (*9 AD3d at 33*). It must be noted that the *Brown* decision does not mention "spasm" as a necessary ingredient for any straight-leg raising test to be considered "positive," although the use of the words "in part" seems to infer that the other basis was spasm. The *Brown* court further observed that:

> "*Evidence of range of motion limitations is sufficient to defeat summary judgment* (*see Toure v Avis Rent A Car Sys., 98 NY2d 345, 350, 774 NE2d*

> 1197, 746 NYS2d 865 [2002]; *Eng v New Main Line Trading Corp., 249 AD2d 359, 670 NYS2d 800 [1998]*; Cassagnol v Williamsburg Plaza Taxi, 234 AD2d 208, 651 NYS2d 518 **[*202]** [1996]). **[****13]** *Furthermore, this Court has held that straight-leg raising tests are objective evidence of serious injury* (*see* Aguilar v N.Y.C. Water Works, 298 AD2d 245, 748 NYS2d 155 [2002]; **[**855]** Adetunji v U-Haul Co. of Wis., 250 AD2d 483, 672 NYS2d 869 [1998]), especially where, as here, they are coupled with positive MRI and nerve conduction velocity test results." (*Brown v Achy, 9 AD3d 30, 32, 776 NYS2d 56 [2004]* [emphasis added].)

The dissent, in a somewhat critical decision, **[***33]** highlighted every purported weakness in the majority's analysis and every sign, signal and circumstance, including an insufficiently explained three-year gap in treatment, from which they concluded that plaintiff had not sustained a serious injury in this accident. Of course, the quality of the objective evidence was also discussed. For comparison purposes to the *Toure* cases, as well as to *Parreno*, the rationale of the dissent is set forth herein in detail.

It was observed by the dissent that on the day of the accident (Dec. 25, 1997), this "overweight" plaintiff declined an offer to be taken to the hospital by ambulance, and chose instead to "walk away" from the scene of the accident, and take a subway to the emergency room of a rehabilitation center in Bayshore, Long Island where she resided; and where "she was examined, x-rayed, given Motrin and discharged [that same] evening" (*id. at 35*). Also significant to the dissent was the resumption by plaintiff of her full time employment shortly after the accident (although she claimed she was bedridden for two weeks following the accident), and that "the first professional plaintiff consulted about her alleged injuries (after her brief emergency room **[***34]** visit) was her lawyer . . . [and] it was her lawyer who referred her to . . . a chiropractor, whom plaintiff first visited 10 days after the accident" (*id. at 36*). She was seen by this chiropractor periodically for a period of six months (to July 1998) and once more in September 1998; she was not seen again by the chiropractor for three years (i.e., Sept. 2001), and then only after it was necessary to respond to defendant's motion to dismiss.

The dissent was disturbed by this three-year hiatus during which "plaintiff apparently did not receive *any treatment* for physical complaints allegedly connected to the subject accident"; and the dissent thought it noteworthy to mention that although she had been referred by the chiropractor to a neurologist, in June of 1998 she "made only one visit" to this neurologist who had "recommended various forms of follow-up care," which the **[*203]** plaintiff did not follow (*id.*). The dissent argued that the plaintiff's three-year gap in the treatment was not sufficiently explained (despite plaintiff's doctor's statement that plaintiff "had reached the point of maximal medical improvement"), and concluded that

> "[t]o the extent (if any) plaintiff's medical evidence might otherwise be deemed to have raised a **[***35]** triable issue as to the existence of a statutory serious injury . . . such evidence is negated, as a matter of law, by plaintiff's unexplained failure to obtain any treatment . . . for a period of about three years prior to the submission of her opposition to the summary judgment motion." (*9 AD3d at 38* [internal quotation marks omitted].)

The dissent also disagreed with the majority's assertion that the explanation provided by plaintiff's doctor (maximal medical improvement) complied with *Toure*'s guidelines for a "sufficient explanation," and thus concluded that this explanation given "without any substantive elaboration" was "vague and conclusory" and, thus, speculative and worthless (*id.*). **[****14]**

The dissent also was critical of the majority's reliance upon plaintiff's neurologist's "unsworn . . . report" and "the unsworn and unaffirmed MRI report" of plaintiff's radiologist dated April 17, 1998, which allegedly revealed a "[c]entral disc herniation at C3-4 [and] [n]o other focal disc herniation," noting that, in any event, this MRI report was contradicted by defendant's **[**856]** neurologist, Dr. Hudak, who in an affirmed report dated September 14, 1999, "reached a different conclusion" as to the same MRI (*id. at 36-37*). These unsworn and unofficial reports of the plaintiff's neurologist and radiologists **[***36]** were held by the majority to be properly before the court because they were referred to, and used by, the defendants' examining neurologists.

The defendant's physician, Dr. Hudak, stated in his affirmed report that a "[r]eview of [the] actual MRI of the claimant's cervical spine failed to reveal an acute herniated disc at any level and no herniated disc at the particular C3-4 level" (*id. at 37*). In addition, Dr. Hudak observed and reported, based on an examination of the plaintiff conducted in 1999, that "plaintiff's stated height was 5 feet, 3 inches, and her weight was then 290 pounds"; that all of range of motion measurements in the cervical and lumbar region, as well as in the upper and lower extremities, were normal; and that, although the report of **[*204]** plaintiff's physician (Dr. Sultan) referred to "electrophysical evidence of acute left sided L5-S1 radiculopathy," *no such complaints were made by plaintiff* at the time of the examination (*id.*). He concluded therefore that

> "[plaintiff] is not disabled as a result of that accident [of December 25, 1997] and requires no further orthopedic care or physical therapy. There are no objective findings at this time to confirm the presence of an acute herniated **[***37]** disc in the area of the cervical spine related to the accident of 12/25/97." (9 AD3d 30, 37 [2004].)

Dr. Rosenblum, defendants' neurologist, based on an examination held on March 1, 2001 reported that "[a]fter conducting a variety of tests [including a seated straight-leg raising test, which was negative], there is no neurological sequela from the trauma of 12-25-97" (*id. at 38* [internal quotation marks omitted]). In that regard, the dissent criticized the majority's reliance on the alleged positive straight-leg raising tests made by plaintiff's chiropractor because "the existing record does not establish whether the particular tests used by plaintiff's medical experts were based on subjective complaints of pain" (*id. at 40*).

In any event, despite all of the dissent's criticisms, the *Brown* majority held that plaintiff's submissions were adequate to defeat defendants' motion for summary judgment.

The *Parreno* Decision

In *Parreno*, a somewhat different panel of the First Department, set aside *a jury finding* that the plaintiff had sustained a "significant limitation of use of a body function or member." In this case, despite the existence of objective evidence (spasm and a somewhat positive MRI) which appeared much more compelling than **[***38]** that in *Manzano* and *Brown*, this panel in the First Department determined and concluded that plaintiff's "medical evidence failed to establish a prima facie case of serious injury under either a quantitative or qualitative analysis." (*Parreno, 40 AD3d 520, 523, 836 NYS2d 593 [2007]*.) **[****15]**

At the trial in *Parreno*, the plaintiff testified that he sustained injury to his neck and back when his vehicle was rear-ended by a heavy truck; that he was taken to the hospital for neck and back pain; and at the emergency room was X-rayed, given medication and released. Over the next five months he received physical therapy, including chiropractic care; treatment was eventually discontinued because "the facility was not being paid" (*id. at 521*). Because of persistent pain, plaintiff was seen **[*205]** by an orthopedist (Dr. Kaplan) who, after examination, diagnosed a herniated cervical disc, a bulging lumbar disc, cervical and lumbar straightening, radiculopathy, *and muscle spasm with trigger points*, and who administered a series of steroid injections which provided only temporary relief. He was **[**857]** treated by Dr. Kaplan on seven occasions between January 2001 and May 2003; on the initial visit the examination revealed the following findings: a "30% [**[***39]** cervical] limitation in the range of motion"; "multiple trigger points of muscular spasm in *his neck and shoulder girdle*"; "*spasm and tightness of the lower back* [with] pain in the lower back and legs during a straight leg raising test at 70 degrees, whereas the normal is 90 degrees" (*id.*). Dr. Kaplan testified that "the findings related to muscle spasm [were] objective . . . [and] beyond the control of the patient," and it was his opinion that "the return of muscle spasms was an indication of an ongoing problem with the neck and lower back, causing the limited ranges of motion" (*id.* [internal quotation marks omitted]). It was his opinion that because plaintiff was still experiencing pain and limitations five years after the accident that plaintiff's injuries were both "significant" and "permanent" and causally related to the accident.

At the trial the plaintiff testified that his pain was ongoing making it "difficult [for him] to turn his neck or bend forward or turn side to side"; that it prevents him from taking out the garbage without assistance; that he was required to reduce his work schedule as an inspector (although he only missed three or four days from work); and that his pain has caused him to develop a temper leading to marital **[***40]** problems (*id. at 521*).

At the trial, the defendants offered the testimony of two medical witnesses (Dr. Eisenstadt, a radiologist, and Dr. Gorsky, whose medical specialty was not identified in the decision).

Dr. Eisenstadt examined MRI films of the plaintiff's cervical and lumbar regions and testified with reference to the lumbar MRI, that she "found no evidence of traumatic change, no straightening of the lumbar spine and no bulging disc"; with reference to the cervical MRI she testified that the film was "blurry" but she found "no signs of trauma or disc herniation" but she did concede that this MRI showed "some straightening" and that "such straightening could be caused by a muscle spasm" but in this case she believed "it was the result of patient movement" (*id. at 522*).

Dr. Gorsky, the defendant's second medical witness, who conducted a five-minute examination, found "some limitation in **[*206]** his head and neck, but found normal results for the straight leg raising test, which [in his opinion] indicated no herniated disc" (*id*. [internal quotation marks omitted]). He concluded that "plaintiff had intermittent complaints of neck and back pain that were consistent with his age and occupation, and that there were no objective findings to suggest that the accident **[***41]** caused any impairment, permanency or disability" (*id*.).

On this record the jury returned a split verdict finding that plaintiff failed to establish "a permanent consequential limitation of the use of a body organ or member" but that plaintiff did sustain a "significant loss of use of a body function or member," and made an award for past and future pain and suffering. **[****16]**

The *Parreno* court, despite the presence of ROM limitations and objective evidence (spasm and some MRI findings indicative of spasm) supporting plaintiff's doctors' qualitative *and* quantitative analysis, ruled that, as a matter of law, plaintiff failed to establish a serious injury. The Court held that, although plaintiff's doctor found a *quantitative* 30% loss of cervical motion and a 20 degrees difference from normal in the lumbar region during straight-leg raising tests, "any fair reading of the record demonstrates that these numerical restrictions on range of motion were premised *exclusively* on plaintiff's subjective indications of pain." (*Id. at 523-524* [emphasis added].) This finding, however, appears to be contradicted by the trial record and, in any event, appears inconsistent with the *Toure* guidelines, as well as with this Department's **[***42]** prior holding **[**858]** in *Brown*. Muscle spasms detected during range of motion tests are universally recognized (medically and legally) as an objective sign supporting a claim of serious injury. Dr. Kaplan (plaintiff's orthopedist) so testified. Moreover, in compliance with the *Toure* guidelines, Dr. Kaplan provided both a "quantitative" and a "qualitative assessment" which related these findings to plaintiff's ongoing limitations and pain. Despite this evidence in the record, and the Court's obligation to view the trial evidence in a light most favorable to the plaintiff, the *Parreno* bench inexplicably concluded:

> "Although plaintiff's expert did identify some objective evidence of plaintiffs injury--a herniated disc, a bulging disc and *multiple points of muscular spasm*--this evidence alone was insufficient to establish a serious injury, in the absence of objective medical evidence showing the extent or degree of **[*207]** the limitations resulting from these specific injuries and their duration." (*Id. at 524*.)

The *Parreno* panel also stated, with reference to the qualitative assessment, that plaintiff's doctor's testimony was "[m]anifestly . . . vague" and "fail[ed] to compare plaintiff's limitations to the normal function, purpose and use **[***43]** of the cervical and the lumbar regions of his spine" (*id*.). However, the trial record (as revealed in the opinion) discloses that, in addition to the plaintiff's testimony regarding life quality changes, Dr. Kaplan corroborated same stating, among other things, that "[h]e certainly has pain with activities, acquires pain, complained of pain with activities, complained of pain with weather changes. He has muscular spasm that limits his motion, worse at times than other times. And, so, he has a limited function, certainly" (*id*.).

The Dilemma Continues

The *Parreno* standard of review seems harsh and much more stringent than that found satisfactory in *Toure* and *Brown (supra)*. The *Parreno* bench appears to require a more technical and ritualistic application of the "qualitative" and "quantitative" assessments discussed and approved in *Toure.* The *Parreno* review does not appear to have "viewed the trial evidence in a light most favorable to the plaintiff," and unlike the *Brown* panel, appears to apply a construction which would, when technical requirements are not meticulously followed, deprive a plaintiff of a common-law right. Its construction, at least to this court, appears to go far beyond **[****17]** what is necessary **[***44]** to weed out the "frivolous" and the "minor, mild and slight limitations" which are deemed insignificant by the No-Fault Law.

"Gaps In Treatment"

An unexplained gap in, or termination of, treatment, can result in a judicial determination that plaintiff's injuries have resolved and were thus not significant within the meaning of the No-Fault Law. (*See Pommells v Perez, 4 NY3d 566, 830 NE2d 278, 797 NYS2d 380 [2005]*.) In evaluating whether the plaintiff has sustained a serious injury under the categories of "permanent consequential limitation" or "significant limitation," it is appropriate for the court to look at any gaps in the plaintiff's treatment, *even if there is objective medical proof of injury*. As stated by the Court of Appeals in *Pommells:* "We conclude that, even where there is objective medical proof, when additional contributory factors interrupt the chain of causation between the accident and claimed injury--such as a gap in treatment, an intervening medical **[*208]** problem or a preexisting condition--summary dismissal of the complaint *may* be appropriate." **[**859]** (Id. at 572 [emphasis added].)

While a gap in, or cessation of, treatment is not necessarily dispositive--since the law does not require a record of needless treatment **[***45]** in order for a plaintiff's case to survive a summary judgment motion--a plaintiff who suspends therapeutic measures, while claiming a serious injury, must offer a bona fide and reasonable explanation for having done so. For example, when the plaintiff has provided evidence in admissible form from his physician that a continuation of medical therapy would have only been "palliative in nature," a subsequent gap in treatment would not necessitate the granting of summary judgment to the defendant, since the cessation of treatment was adequately explained. (Pommells v Perez, supra; Brown v Dunlap, 4 NY3d 566, 830 NE2d 278, 797 NYS2d 380 [2005].)

Another explanation deemed reasonable is a cessation or gap caused by a claimant's inability to afford continued treatment after no-fault benefits have been discontinued. (*See* Wadford v Gruz, 35 AD3d 258, 826 NYS2d 57 [2d Dept 2006]; Francovig v Senekis Cab Corp., 41 AD3d 643, 838 NYS2d 635 [2d Dept 2007].) However, inconsistent explanations for a cessation of treatment can be fatal to a claim of serious injury. (*See* Gonzalez v A.V. Managing, Inc., 37 AD3d 175, 829 NYS2d 70 [1st Dept 2007] [summary judgment granted where inconsistent explanations given by plaintiff as to reasons for cessation of treatment; his **[***46]** own doctor stated that treatment should not have been stopped, yet records showed plaintiff's range of motion findings were normal within four months of happening of accident]; *see also* DeLeon v Ross, 44 AD3d 545, 844 NYS2d 36 [1st Dept 2007] [undisputed 20-month gap not adequately explained by plaintiff's undocumented assertion that he discontinued treatment only after his no-fault benefits were cut off due to his inadvertent failure to attend a required physical examination for the carrier]; Brown v City of New York, 29 AD3d 447, 815 NYS2d 88 [1st Dept 2006] [explanation held not reasonable where plaintiff's expert was retained long after cessation of treatment, and plaintiff failed to provide contemporaneous medical records supporting the **[****18]** explanation that plaintiff had achieved maximum recovery].)

What constitutes a significant gap in treatment is still a work in progress; the amount of time which constitutes a fatal "gap" has not been definitively determined. (*See* Sung v Mihalios, 44 AD3d 500, 843 NYS2d 317 [1st Dept 2007] [unexplained gap of "one year" does not lead to grant of summary judgment]; Ning Wang v Harget Cab Corp., 47 AD3d 777, 850 NYS2d 537 [2d Dept 2008] [a 10-month gap **[*209]** was held to require an explanation]; *Phillips v Zilinsky, 39 AD3d 728, 834 NYS2d 299 [2d Dept 2007]* **[***47]** [inadequate explanation for 15-month gap in treatment warrants grant of summary judgment].)

Recent Evidence of Serious Injury

A plaintiff should not rely merely on stale medical reports and current "self serving" sworn statements that his/her limitations are ongoing. Recent cases are now looking to the duration of the limitations and thus require *current proof* (i.e., recent to the motion) that plaintiff is still impaired by said limitations. (*See* Shvartsman v Vildman, 47 AD3d 700, 849 NYS2d 600 [2d Dept 2008].) Proof of significant limitations which are merely relatively contemporaneous with the accident may not be sufficient to establish a serious injury especially if there is evidence provided by defendant's experts that plaintiff's injuries have resolved and plaintiff has recovered. In Shvartsman (at 701), it was held:

> **[**860]** "The mere existence of a herniated or bulging disc, and even a tear in a tendon, is not evidence of a serious injury in the absence of objective evidence of the extent of the alleged physical limitations resulting from the injury *and its duration* (*see* Patterson v NY Alarm Response Corp. 45 AD3d 656, 850 NYS2d 114 [2007]; Tobias v Chupenko, 41 AD3d 583, 584, 837 NYS2d 334 [2007]; Mejia v DeRose, 35 AD3d 407, 407-408, 825 NYS2d 722 [2006]." (Emphasis **[***48]** added.)

Discussion and Conclusion

Competing Statutes and Rules of Construction--"A Judicial Dilemma"

The No-Fault Law has a remedial purpose, i.e., to reduce insurance premiums by weeding out frivolous claims and limiting recovery to significant injuries (*see* Dufel v Green, 84 NY2d 795, 798, 647 NE2d 105, 622 NYS2d 900 [1995]; Montgomery v Daniels, 38 NY2d 41, 340 NE2d 444, 378 NYS2d 1 [1975]). This law *is in derogation of a common-law right* of an injured person to bring an action for injuries sustained in an automobile accident caused by the wrongful conduct of another motorist. Being remedial in nature, the No-Fault Law must be accorded a liberal interpretation and the widest application in order to carry out reforms intended. (McKinney's Cons Laws of NY, Book 1, Statutes §§ 302, 321.) However, that law, being in derogation of common-law rights, also involves the "rule of strict **[****19]** construction," which requires, therefore, an interpretation of the No-Fault Law which "makes no further innovation upon common law rights than the particular case requires." (Statutes § 301 **[*210]** [a], Comment; §§ 304, 311.) Courts are thus confronted with a conundrum caused not only by the above conflicting statutory requirements, **[***49]** but also by what often seems like an impossible task: to discern, *on motion*, the false and frivolous and to distinguish "minor, mild or slight" injuries from appropriate claims. These impairments, though unobservable, can cause genuine quality of life changes in those who really suffer same. These are usually issues which are presented to jurors at trial, who have the benefit of live testimony and can make credibility determinations. The task of deciding these issues on "papers" is, at best, extremely difficult.

<u>A Difficult and Frustrating Task</u>

There are those who harbor a flawed assumption that judges (on papers), rather than medical scientists and jurors, are more able and equipped to discern and distinguish the false, frivolous and/or insignificant claims of serious injury from those which can cause legitimate, sometimes profound and "more than frivolous" limitations, pain and quality of life impairments. This legislatively imposed task has caused more than a season of judicial discontent and frustration, it has resulted in an extremely difficult and flawed process which results too often in an inconsistent and unfair application of the law.

This court is not sufficiently prescient to **[***50]** determine whether this plaintiff *actually*, as claimed, has ongoing significant cervical and lumbar pain, limitations and quality of life impairments. Certainly these kinds of injuries and limitations can be feigned and/or exaggerated. When genuinely significant, however, cervical and lumbar injuries can be insidious and their syndrome is characterized by periods of remission and exacerbation which is not readily observable by others. Certainly if plaintiff's injuries have continued to affect his relationship with his wife and preclude him from lifting anything heavy, playing soccer or volleyball, and assisting his wife **[**861]** with ordinary chores, such as grocery shopping, then, this court would certainly *not* conclude that the claim is frivolous or that the injuries are insignificant. But since the court cannot infallibly predict what the plaintiff's future course may be, it must make its decision on this motion based upon the examples and standards (clues) promulgated by appellate authority to assist it in making its determination. This obligation, as discussed above, can be exceedingly difficult and frustrating.

<u>The Defendants' Proof</u>

The defendants have provided sufficient proof in admissible **[***51]** form to establish prima facie entitlement to the relief requested. **[*211]** Dr. Totero swore that he found no objective evidence of range of motion restrictions in either the plaintiff's cervical or lumbar regions, found no objective indication of any disability, and concluded that it was his opinion that the plaintiff had sustained strains and sprains which were not disabling and required no further treatment. **[****20]** However, it is noted that he did elicit tenderness and complaints of pain not inconsistent with plaintiff's allegations of serious injury.

Dr. Mendelsohn, a radiologist, reviewed the MRI films taken of the plaintiff's cervical and lumbar areas, and concluded that both areas demonstrated only degenerative changes, and no herniations caused by the accident, but did concede that plaintiff had bulges at multiple levels.

The conclusions reached by the defendants' medical team are corroborated by plaintiff's admission that, except for one month following the accident, he is capable of, and continues to, work at two full time jobs.

<u>The Plaintiff's Proof</u>

In the case at bar plaintiff's physician, Dr. Zlatnik, based upon his full treatment, current examination, course of physical therapy and diagnostic **[***52]** test results, found and concluded in essence that the plaintiff was permanently disabled from performing heavy lifting or any other types of strenuous activity, that his lumbar and cervical spines will continue to cause him problems for the rest of his life, that his herniated and bulging discs will produce localized pain and radicular symptoms, and that he will be predisposed to further complications.

Unfortunately, none of Dr. Zlatnik's reports of, or notes taken during the examinations have been provided on this motion, and the court is thus unable to independently ascertain what objective evidence (*apart *from the MRI*), if any, existed at that time to establish that plaintiff had suffered and is still suffering from the cervical and lumbar injuries and limitations described. Dr. Zlatnik does state that he detected cervical and lumbar spine "trigger points" (a form of spasm or tenderness within a muscle); however it is unclear whether these findings were objectively determined, or based upon subjective complaints of pain. In any event, a review of plaintiff's MRI and the course of treatment and medical assessment provided by Dr. Zlatnik is useful. Apart from the six months of aggressive **[***53]** therapy conducted under Dr. Zlatnik's supervision, the record before the court indicates that plaintiff was examined by Dr. Zlatnik on three occasions, i.e., initially on December 30, 2004, on a second **[*212]** occasion on February 8, 2005 (after a review of the MRI, dated Jan. 17, 2005), and finally, almost three years later, on April 7, 2008. This last examination, which was not for treatment, was conducted in order to provide an affirmation in opposition to defendants' motion.

During his initial examination of plaintiff, after receiving a history of complaints **[**862]** consistent with injury to the cervical and lumbar regions, Dr. Zlatnik conducted a physical and neurological examination, which included "measured" range of motion tests, using a goniometer. Although Dr. Zlatnik concluded that the ROMs were "less than normal," this court, on the record presented, is unable, on a "quantified" review to determine whether they were significant or "minor, mild or slight," since no numeric percentages have been provided; and, although Dr. Zlatnik states that he found the cervical and the lumbar spine trigger points during this examination, it is unclear from the record if these trigger points findings **[***54]** were based wholly or partially on subjective complaints. Thus, the court must rely on plaintiff's statements and complaints together with Dr. Zlatnik's "*qualitative*" assessment, *and of course, the MRI*, conducted on January 17, 2005.

It is noted that, although the plaintiff was sent by Dr. Zlatnik "for an MRI and *other **[****21]** diagnostic testing*," only the MRI results are presented for review on this motion and the court therefore must assume that the other testing was negative. [4] However, the MRI reports do contain objective proof of disc injury, i.e., a disc herniation at L5-S1 multiple cervical and lumbar bulges with impingement, a straightening of the lumbar curvature (which is consistent with a muscle spasm) and early degenerative changes, as demonstrated by a "mild loss of signal intensity" at multiple lumbar disc sites, "which reflect mild and a slight loss in the fluid content." These early degenerative changes are not inconsistent with recent trauma, and Dr. Zlatnik did opine that "the trauma of this accident will cause abnormal degenerative changes at an accelerated rate [and] as such [plaintiff] will surely sustain greater restrictions in his ranges of motion," and that "the injuries **[***55]** that were sustained [by plaintiff] will result in a predisposition to further complications."

On February 8, 2002, after a review of the above MRI reports the plaintiff was again examined and continued on an aggressive **[*213]** course of physical therapy, which continued until May 16, 2005, at which time it was discontinued because no-fault benefits were terminated and because plaintiff "made a slow, poor and erratic improvement" *and because* it was determined that "further medical therapy would be only palliative in nature." Thus, in accord with the rationale of *Pommels* and *Brown (supra)*, the plaintiff's cessation in treatment has been sufficiently explained.

On the last examination, April 7, 2008, "it was [Dr. Zlatnik's] *impression* that Victor Vidal continued with residual signs of right sided L5 radiculopathy and post-traumatic myofascial pain syndrome." However, again no report and details have been provided, but **[***56]** Dr. Zlatnik asserts in his affirmation that he obtained "objective verification of the injury suffered by [plaintiff] upon [the] most recent examination as well as his course of physical therapy and diagnostic test results."

Depending upon which of the above reviewed appellate precedents this court chooses to accept as controlling, the plaintiff here will either succeed or fail. Certainly the proof will be deemed insufficient if measured with the *Parreno* yardstick--where, despite the production of objective evidence (spasm and a positive MRI), and both a quantitative and qualitative assessment, **[**863]** plaintiff's proof was found by the Court to be lacking.

Certainly the submissions on behalf of the plaintiff are not overwhelming in their specificity; however, they do, nevertheless, reach the level where this court finds a question of fact has been raised as to whether the plaintiff sustained a serious injury as a result of the accident. In reaching this conclusion, the court rejects the *Parreno* decision and specifically relies on the rationales of, and holdings in, *Manzano v O'Neil (supra)*

[4] Since the plaintiff has chosen not to provide the court with the report of electrodiagnostic studies conducted by Dr. Zlatnik on January 31, 2005, the court has not considered the statement in defendants' doctor's report that the test was allegedly "consistent with L5-S1 radiculopathy."

and *Brown v Achy (supra)*. The ruling in *Parreno* seems questionable and out of step with the more liberal **[***57]** guidelines provided by the Court of Appeals in *Manzano*. Although *Parreno* is a First Department case and a **[****22]** precedent which ordinarily would be absolutely binding on this court (*Mountain View Coach Lines v Storms, 102 AD2d 663, 476 NYS2d 918 [2d Dept 1984]*), it conflicts with *Brown*, an equally binding First Department precedent, as well as with *Manzano*, an even more binding one. In view of these conflicting decisions, this court is free to fashion a decision which it deems to be appropriate and consistent, not only with *Manzano* and *Brown*, but also with the overall objective sought to be achieved by the No-Fault Law, and with the rule of statutory construction which "make[s] no further innovation upon common **[*214]** law rights than the particular case requires." (Statutes § 301 [a], Comment; *see* *Reyes v Sanchez Pena, 191 Misc 2d 600, 606, 742 NYS2d 513 [Sup Ct Bronx County 2002]*.)

In *Manzano* the Court of Appeals reversed a dismissal of the plaintiff's complaint by the Appellate Division since it found that a sufficient qualitative assessment (supported by MRI findings) had been presented by the plaintiff. Her expert had testified that the plaintiff's complaints were consistent with the injury, that the injury itself was permanent, and that this **[***58]** conclusion was founded on the plaintiff's history, physical examination and review of an objective test (an MRI).

In *Brown*, the First Department reinstated a complaint which had been dismissed at the trial level, because it found that the plaintiff's evidence on range of motion limitations (including straight-leg raising tests) was sufficient to defeat summary judgment since those findings, although partially based upon subjective complaints, were also supported by other objective evidence such as an MRI and nerve conduction velocity test.

Similarly, here, although the affirmation of plaintiff's doctor does not provide numerical percentages or degrees of range of motion loss, he does, however, find deficits in the ranges of motion as compared to normal, and his conclusions are supported by the existence of trigger points (a form of spasm) and another objective test (an MRI) that contains numerous positive findings consistent with, and supportive of, plaintiff's ongoing complaints. On this record, giving the plaintiff every fair inference, this court cannot conclude, as a matter of law, that plaintiff's injuries and limitations are "mild, minor or slight." **[***59]**

End of Document

Wellbilt Equip. Corp. v. Fireman

Supreme Court of New York, Appellate Division, First Department

October 12, 2000, Decided

No Number in Original

Reporter

275 A.D.2d 162 *; 719 N.Y.S.2d 213 **; 2000 N.Y. App. Div. LEXIS 14135 ***

Wellbilt Equipment Corporation, Respondent, v. Sheldon Fireman et al., Appellants, et al., Defendants.

Prior History: **[***1]** Appeal from an order of the Supreme Court (Carol Huff, J.), entered July 16, 1998 in New York County, which, to the extent appealed from, granted summary judgment to plaintiff and dismissed defendants' second, third and fourth counterclaims.

Disposition: Appeal from order, Supreme Court, New York County, entered on or about July 16, 1998, dismissed as academic, without costs.

Counsel: *Barry J. Glickman* of counsel (*Michael L. Slonim* on the brief; *Zeichner Ellman & Krause, L. L. P.,* attorneys), for respondent.

Jeffrey Turkel of counsel (*Gary M. Rosenberg, Warren A. Estis* and *Norman Flitt* on the brief; *Rosenberg & Estis, P. C.,* attorneys), for appellants.

Judges: Nardelli, J. P., Tom, Mazzarelli and Ellerin, JJ., concur.

Opinion by: Friedman

Opinion

[*163] **[**214]** Friedman, J.

On this appeal we are required to determine whether a Lien Law § 39-a claim, which seeks damages for the alleged wilful exaggeration of a lien, survives the consensual discharge of the lien. We conclude that where, as here, the lien is discharged on consent of the parties and the lienor's action to foreclose the lien is discontinued, a wilful exaggeration **[***2]** claim does not survive.

In or about September 1994, defendants hired plaintiff Wellbilt to construct the Red Eye Grill restaurant in Manhattan. * Plaintiff asserts that after construction commenced defendants repeatedly changed architects, building plans, and interior requirements. As a result, plaintiff advised defendants that construction costs would likely rise.

After construction was largely completed, the Red Eye Grill restaurant opened for business in November of 1996. About the same time, plaintiff demanded that defendants make additional payments towards the construction cost, which plaintiff asserted had risen to $ 5,000,000. In a letter dated December 2, 1996, defendants admitted to plaintiff **[***3]** that it was entitled to more than $ 2,362,000 in fees, disputing only the amount that **[*164]** plaintiff was due beyond that sum. Despite the acknowledgment that $ 2,362,000 was due, defendants paid plaintiff only $ 2,054,000, leaving a balance that, according to defendants' own calculations, exceeded $ 300,000. In view of defendants' failure to make payment beyond the $ 2,054,000, plaintiff filed a lien against the property.

The first lien, which was filed on July 22, 1997, alleged that the total cost of construction was $ 5,000,000, of which a balance of $ 2,946,000 remained unpaid. The dispute not being resolved, this action was commenced one month later.

Plaintiff's complaint asserted causes of action, *inter alia,* for breach of contract and foreclosure of the lien. Shortly after commencement of the action, however, plaintiff discovered that its lien was fatally defective because it had failed to file proof of service of the notice of lien with the County Clerk within 35 days as required by Lien Law § 11. In view of this, plaintiff refiled the lien on September 10, 1997, this time properly filing proof of service.

* There is an ongoing dispute as to which of the defendants actually hired plaintiff and is liable for the payment of plaintiff's fees. Although we refer to defendants collectively for purposes of this decision, we make no finding as to this issue as it is irrelevant to the legal issue presented.

As plaintiff's foreclosure **[***4]** action was premised on the defective lien it had previously filed, plaintiff also served a supplemental summons and complaint identical in all respects to its original summons and complaint, except that the complaint sought to foreclose the second lien, instead of the first.

In response, defendants served an amended answer, which interposed various counterclaims. As is relevant to this appeal, the second counterclaim alleged that both of the liens filed by plaintiff were wilfully exaggerated, thereby requiring the liens to be discharged. The third counterclaim attacked the allegedly duplicative nature of the liens, i.e., since both liens were for the identical work, the liens viewed together were necessarily exaggerated. The fourth counterclaim sought damages pursuant to *Lien Law § 39-a*, asserting that the liens were wilfully exaggerated whether viewed individually or jointly.

Thereafter, plaintiff moved for partial summary judgment against defendants in the amount of $ 406,000 and for an immediate trial as to the extent of plaintiff's damages beyond that amount. The motion was premised upon a concession in defendants' answer, which stated that plaintiff **[***5]** had been paid all but $ 406,000. Defendants **[**215]** cross-moved for summary judgment on their second, third, and fourth counterclaims, arguing that the two liens, when viewed together, were exaggerated since they were duplicative of each other.

Supreme Court granted plaintiff partial summary judgment, awarding it damages in the sum of $ 406,000 (a matter which is **[*165]** not the subject of this appeal), leaving for trial a determination of whether plaintiff was entitled to any sums beyond $ 406,000. The court also denied defendants' cross motion for summary judgment and granted plaintiff reverse summary judgment dismissing defendants' second, third, and fourth counterclaims.

In dismissing defendants' counterclaims, Supreme Court apparently viewed such claims as being rooted only in the alleged duplication of the liens. Since the court found that the first lien was void by operation of law, and that the second lien was filed merely because of plaintiff's failure to properly perfect the first lien, the court concluded that there was no basis for a wilful exaggeration claim. This appeal by defendants followed.

Before this appeal was perfected, however, defendants entered **[***6]** into a stipulation with plaintiff regarding the lien. Pursuant to that stipulation, plaintiff discharged the lien and discontinued its seventh cause of action, which sought to foreclose the lien. The stipulation did not resolve the issue of how much additional money plaintiff was owed. That issue was left for trial.

The principal issue presented by this appeal concerns the effect of this stipulation on defendants' counterclaims. A subsidiary issue concerns the effect of plaintiff's filing of duplicate liens. Analysis of the matter must begin with the statutory backdrop.

Section 39 of the Lien Law provides that: "In any action … to enforce a mechanic's lien … if the court shall find that a lienor has wilfully exaggerated the amount for which he claims a lien as stated in his notice of lien, his lien shall be declared to be void."

Where a lien has been discharged under this section, *Lien Law § 39-a* permits the recovery of damages. Thus, *section 39-a* provides: " **[***7]** Where in any action … to enforce a mechanic's lien … the court shall have declared said lien to be void on account of wilful exaggeration the person filing such notice of lien shall be liable in damages to the owner or contractor."

Regarding the issue of plaintiff's filing of duplicate liens, we agree with Supreme Court's conclusion that a wilful exaggeration claim premised upon this ground cannot stand. The first lien filed by plaintiff was, as a matter of law, void because of plaintiff's failure to file proof of service of the notice of lien with the County Clerk within 35 days as required by *Lien Law § 11* (*Outrigger Constr. Co. v Nostrand Ave. Dev. Corp., 217 AD2d 689*). **[*166]** In view of this, plaintiff's filing of a second lien, which it plainly did in recognition that its first lien was defective, could not support a claim of wilful exaggeration. Hence, Supreme Court was correct in finding that the second filing did not entitle defendants to summary judgment.

Defendants contend, however, that, even if Supreme Court was correct with **[***8]** regard to the duplication of the liens, the court nevertheless erred in dismissing their wilful exaggeration claims and granting plaintiff reverse summary judgment. In this regard, they point out that, setting aside the purported duplication of the lien, there remained a claim that the second lien, viewed individually, was itself wilfully exaggerated. Defendants further contend that the subsequent discharge of the lien pursuant to stipulation has no effect on the viability of their exaggeration claim. This latter contention by defendants does not bear scrutiny.

In interpreting the Lien Law, our courts have held that damages under section 39-a **[**216]** may not be awarded unless the lien has been declared void for wilful exaggeration after a trial in an action to foreclose the lien (*see,* *Joe Smith, Inc. v Otis-Charles Corp., 279 App Div 1, 4*, *affd* *304 NY 684*; *see also,* *Pyramid Champlain Co. v Brosseau & Co., 267 AD2d 539, 542*; *Stamatopoulos v Karasik, 238 AD2d 688, 691, lv dismissed and denied 92 NY2d 844*; **[***9]** *Pamco Indus. v Medical Plaza Assocs., 231 AD2d 504, 505*; *Guzman v Estate of Fluker, 226 AD2d 676, 678*; Bowmar, Mechanics' Liens in New York § 3.12 [1992]). The conclusion reached by these courts is well founded as it flows from the explicit words of the statute.

In this connection, section 39-a, by its terms, only permits a wilful exaggeration claim to be asserted in an action "to enforce a mechanic's lien," namely, a foreclosure action. Where the lien has been discharged prior to trial, the action is no longer one seeking to enforce a mechanic's lien. The action is, at that juncture, merely one in contract (*see,* *Joe Smith, Inc. v Otis-Charles Corp., supra*; *Guzman v Estate of Fluker, supra*; *see also,* Bowmar, Mechanics' Liens in New York § 3.12, at 131-132).

Additionally, section 39-a provides for damages only where "the court shall have declared [the] lien to be void on account of wilful exaggeration" pursuant to section 39 **[***10]** (*see,* *Pyramid Champlain Co. v Brosseau & Co., supra* [sections 39 and 39-a must be read in tandem]; Bowmar, Mechanics' Liens in New York, *op. cit.,* at 130). Where the lien has been discharged for reasons unrelated to its supposed exaggeration, there remains **[*167]** no lien to be declared void by the court (*see,* *Joe Smith, Inc. v Otis-Charles Corp., supra*; *Guzman v Estate of Fluker, supra*).

In this case, plaintiff's lien was discharged on consent of the parties and its foreclosure action discontinued. Hence, a wilful exaggeration claim is precluded.

Notwithstanding the foregoing, defendants assert that the discharge of a lien only eviscerates a wilful exaggeration claim if it has been discharged on procedural grounds. Based upon this conclusion, defendants assert that where, as here, the lien does not suffer from any procedural defects, its consensual discharge has no effect on a wilful exaggeration claim.

We initially observe that there is nothing in the statutory framework to support the distinction advocated by defendants. As previously noted, the statute, by its terms, requires that the wilful exaggeration claim **[***11]** be asserted in the context of a foreclosure action and that the lien be declared void by the court on account of wilful exaggeration. It is evident that, whether a lien is discharged because of some procedural ground or on consent via stipulation, the end result is the same. In either case, there is no longer a foreclosure action or a lien to be declared void.

Contrary to defendants' claim, there is also nothing in the cases interpreting the Lien Law to support the distinction for which it advocates. It is true that in many of the reported cases dismissing wilful exaggeration claims the subject liens had been discharged on procedural grounds or because the liens were otherwise defective (*see, e.g.,* *Joe Smith, Inc. v Otis-Charles Corp., 279 App Div 1, 4*, *affd* *304 NY 684*, *supra; see also,* *Pyramid Champlain Co. v Brosseau & Co., 267 AD2d 539, 542-543*, *supra; Stamatopoulos v Karasik, 238 AD2d 688, 691*, *supra; Pamco Indus. v Medical Plaza Assocs., 231 AD2d 504, 505*, *supra*). However, this factual circumstance **[***12]** had no bearing on the ratio decidendi that compelled dismissal of the claims. This analysis of the case law is borne out in the oft-cited decision of *Joe Smith, Inc. v Otis-Charles Corp.* (*supra*).

In *Smith,* the defendant (apparently the owner of the property against which the **[**217]** lien was asserted) moved to dismiss the lien at the outset of trial, asserting that the notice of lien suffered from certain deficiencies in its content. The court reserved decision and, at the conclusion of the plaintiff's case, granted the defendant's motion and discharged the lien. The action was thereafter tried and finally submitted, not as one seeking foreclosure of the lien, but as one seeking recovery on the contract between the parties.

[*168] The Court, relying on the specific language of Lien Law § 39-a, found that the defendant's wilful exaggeration claim was not cognizable because "the lien having been discharged, there remained no lien to be foreclosed or to be declared void" (*id., at 4*). The Court then stated: "The [defendant] having succeeded in obtaining a discharge of the lien at the beginning of the **[***13]** trial, the foreclosure action was thereby terminated, and thereafter the court was without authority to declare the lien void on account of wilful exaggeration" (*id., at 5*).

What emerges from *Smith* is that it was irrelevant that the lien was discharged for procedural reasons. What was relevant was only that there was neither a lien to be declared void nor a foreclosure action extant. These dual requirements, as previously noted, flow directly from the statutory language of Lien Law § 39 and 39-a.

One further observation regarding *Smith* is necessary. The *Smith* Court noted that the defendant could have preserved its wilful exaggeration claim by abandoning its procedural defense to the lien (*id., at 4*). Stated otherwise, notwithstanding that the lien may have suffered from technical deficiencies, defendant's wilful exaggeration claim would have been cognizable if it had not obtained a discharge of the lien on procedural grounds. This shows that the determinative factor in assessing the viability of a wilful exaggeration **[***14]** claim is the continued existence of the lien and the continued existence of the action to foreclose the lien.

To the extent defendants rely upon this Court's decision in *Bran Elec. v MHA, Inc. (269 AD2d 231)* in support of a contrary conclusion, such reliance is misplaced. In *Bran* we did not hold, as defendants contend, that a wilful exaggeration claim survives the discharge of a mechanic's lien. That issue was neither briefed nor presented to the Court for adjudication. Thus, as a case "is precedent only as to those questions presented, considered and squarely decided" (*People v Bourne, 139 AD2d 210, 216*, *lv denied 72 NY2d 955*), *Bran* cannot be viewed as expressing any opinion on the issue presented here.

This brings us to defendants' claim that *Lien Law § 12-a* authorizes the assertion of a wilful exaggeration claim even if the lien is discharged for reasons other than exaggeration. *Section 12-a (1)* provides as follows: " **[***15]** Within sixty days after the original filing, a lienor may amend his lien … provided that no action … to enforce … the mechanics' lien has been brought in the interim, where the purpose of the amendment is to reduce the amount of the lien, except the question of wilful exaggeration shall survive such amendment."

[*169] According to defendants, since a lienor cannot escape a wilful exaggeration claim when it unilaterally reduces its lien via a pre-action amendment, it follows that it cannot escape such a claim when it discharges its lien on consent of the parties via stipulation. The answer to defendants' *Lien Law § 12-a* argument lies in a critical observation regarding the nature of Lien Law liability.

Lien Law § 39-a, which is penal in nature, is a purely statutory offense, providing for drastic consequences in the event the statute is violated (*Joe Smith, Inc. v Otis-Charles Corp., supra, at 4*). **[**218]** As a result, there can be no liability under this provision by implication of fact or law (*id.* **[***16]**). Furthermore, the statute must be strictly construed in favor of the person upon who the penalty is sought to be imposed (*id.*).

Bearing these principles in mind, it is apparent that defendants seek to impose liability in this case not because *section 12-a* specifically provides for continued liability after the consensual discharge of a lien, but because of what defendants believe flows by implication from the statute. To accept defendants' argument would, therefore, impose liability by implication, which, as indicated, is not permitted.

In any event, even if *section 12-a* were interpreted as prohibiting a lienor from extricating itself from a wilful exaggeration claim by unilaterally discharging its lien (an issue we need not decide), plaintiff in this case did not act unilaterally. Rather, the lien was discharged on consent via stipulation. This is of critical significance. As previously indicated, where an owner succeeds in obtaining a discharge of a lien on procedural grounds by court order, the owner's wilful exaggeration claim is extinguished. It follows that, where an owner succeeds in obtaining a discharge of the lien via stipulation, a wilful exaggeration claim **[***17]** should be similarly precluded.

In the end, we acknowledge that Supreme Court seems to have misperceived defendants' wilful exaggeration claim as being rooted solely in the purported duplication of the lien. We also acknowledge that, at the time the court rendered its decision, defendants still had a viable claim premised upon the alleged exaggeration of the second lien irrespective of any duplication. While this would mean that Supreme Court prematurely dismissed defendants' counterclaims, the fact remains that, at this juncture, where a stipulation has been executed, a wilful exaggeration claim is no longer viable, as a matter of law. Thus, defendants' appeal has been rendered academic.

[*170] Accordingly, defendants' appeal from an order of the Supreme Court, New York County (Carol Huff, J.), entered on or about July 16, 1998, which, to the extent appealed from, granted plaintiff summary judgment dismissing defendants' second, third, and fourth counterclaims, should be dismissed as academic, without costs.

Nardelli, J. P., Tom, Mazzarelli and Ellerin, JJ., concur.

Appeal from order, Supreme Court, New York County, entered on or about July 16, 1998, dismissed as **[***18]** academic, without costs.

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Williams v. AGK Communications, Inc.

Supreme Court of New York, Onondaga County

May 10, 1989

No Number in Original

Reporter
143 Misc. 2d 845 *; 542 N.Y.S.2d 122 **; 1989 N.Y. Misc. LEXIS 310 ***

James K. Williams, Plaintiff, v. AGK Communications, Inc., Doing Business as WAQX Radio, Defendant

Disposition: **[***1]** Submit judgment on the verdict accordingly.

Counsel: *Lombardi, Devorsetz, Stinziano & Smith (Frank A. Bersani* of counsel), for plaintiff.

Kallusch & Raus (George M. Raus, Jr., of counsel), for defendant.

Judges: Wallace Van C. Auser, J.

Opinion by: AUSER

Opinion

[*845] **[**123]** **OPINION OF THE COURT**

The matter before the court deals with the perplexing issue of whether the terms wages and salary are synonymous. A nonjury trial was held by the court at which time testimony was taken, arguments were heard and judgment was granted to the plaintiff in the amount of $ 25,000, which represented the amount of severance pay due under the written contract of employment.

[*846] Following the court's decision, plaintiff moved under *section 198 (1-a) of the Labor Law* for the court to award reasonable attorneys' fees and an additional amount as liquidated damages equal to 25% of the verdict amount. It is this issue which is now before the court.

The plaintiff herein, James K. Williams, was hired by the defendant radio station, WAQX, in early 1987 as their station manager. The parties entered into a written employment contract which provided that he would be paid $ 50,000 **[***2]** per year. It also provided that severance pay in the amount of 3 months would be paid if the plaintiff's employment was terminated within the first 6 months and in the amount of 6 months' pay if the plaintiff's employment was terminated thereafter. There was testimony adduced at trial as to the responsibilities of the position plaintiff held. He did all of the hiring and firing of employees, as well as all other employee supervision. He was to stimulate growth of the listening market and attempt to increase the ratings. In a word, he was the "manager". He was in charge of the station in a managerial capacity.

There was no dispute at trial as to the fact that in January of 1988, the plaintiff was demoted to the position of general sales manager, but continued at the same salary and with the same terms of employment, including the provision concerning severance pay. On March 14, 1988, plaintiff's employment was terminated but he was told the defendant would honor the severance pay provision of the contract. Thereafter, defendant reneged on the severance pay issue and it was that refusal to pay which resulted in the underlying litigation.

This court found that the plaintiff **[***3]** did indeed have a written contract of employment with the defendant under the terms of which he was to receive severance pay in a specified amount should the employment be terminated. The employment was terminated and the court awarded severance pay to the plaintiff in the amount of $ 25,000.

The plaintiff now contends that since he, as the employee, was successful in his claim he is entitled to an award of reasonable attorneys' fees and liquidated damages.

The interpretation of *section 198 (1-a) of the Labor Law* is the crucial element here. The section reads as follows: "In any action instituted upon a wage claim by an employee or the commissioner in which the employee prevails, the court shall allow such employee reasonable attorney's fees and, upon a **[*847]** finding that the employer's failure to pay the wage required by this article was willful, an additional amount as liquidated damages equal to twenty-five percent of the total amount of the wages found to be due."

If the plaintiff were to prevail here, he would be entitled to the original judgment amount of $ 25,000, $ 6,250 in liquidated damages, and reasonable attorneys' fees. If the plaintiff does not prevail, he **[***4]** walks away only with his judgment amount of $ 25,000.

The plaintiff's claim under section 198 (1-a) can be sustained only if his salary, under the terms of his written contract, falls within the definition of "wages" as found in the Labor Law. Section 190 (1) of the Labor Law defines wages as follows: "'Wages' means the earnings of an employee for labor or services rendered, regardless of whether the amount of **[**124]** earnings is determined on a time, piece, commission or other basis."

There is no dispute over the fact that plaintiff was an employee as that term is generally defined. It is with the term "wages" that there is a difference of opinion and some ambiguity found in the reported decisions of the courts. Succinctly stated, our question is whether or not the severance pay due the plaintiff falls within the definition of wages as found in the Labor Law.

The courts have repeatedly held that the severance pay of a "wage earner" falls within the definition of wages. *(* Saunders v Big Bros., 115 Misc 2d 845; Gerlach v Horn & Hardart Co., 683 F Supp 342.) Even assuming that severance pay is considered as wages we are left with the nagging question of whether what **[***5]** the plaintiff earned per pay period was in fact wages or was it salary? Was the plaintiff a "wage earner"? To make this determination we must look at the nature of his employment. He was hired as the station manager and even after his demotion he was the general sales manager of the station. His duties, as mentioned above, were all managerial in nature and included hiring, firing and supervision, sales of commercial time, stimulating revenue growth and improvement of ratings. It is obvious that plaintiff held a very responsible position for which he received an appropriate salary.

As noted above in the *Gerlach* case *(supra)*, the Southern District of New York Federal Court held that severance pay was in fact wages. The decision in that case, however, makes an assumption that the salary paid to the CEO was wages. **[*848]** The actual issue of whether the salary paid was in fact wages was never actually raised by the parties or the court itself. The doctrine of stare decisis does not bind this court since the issue before us was not actually raised in the *Gerlach* case. A binding precedent is not created by a court's decision unless the subject matter is clearly **[***6]** and squarely dealt with and the principal established is well defined. *(* People v Garthaffner, 103 Misc 2d 671.) The decision in *Gerlach* was a Federal decision and as such is not binding authority upon this court since no Federal question was presented there. *(* Marsich v Eastman Kodak Co., 244 App Div 295.) The construction of State statutes is left primarily as a matter for the State courts to decide and decisions by Federal courts on such State statutes are not binding. *(* People ex rel. Weber & Heilbroner v Graves, 249 App Div 49.)

The *Gerlach* case also cited Matter of Horn & Hardart Co. v Ross (58 AD2d 518, *supra)* which held only that a "retiree" is an employee but did not deal with the manner or method of payment. Thus it seems clear that the Federal court in *Gerlach (supra)* made an unwarranted assumption which the court is not bound to follow.

The rules of construction also come into play in this matter. Section 302 of McKinney's Consolidated Laws of NY, Book 1, Statutes indicates that "the Labor Law is to be liberally construed to accomplish the beneficent purpose for which it was framed." This advisory was followed by the New York County **[***7]** Supreme Court in the matter of Klepner v Codata Corp. (139 Misc 2d 382). However, this court is not bound by the decision of the New York County Supreme Court. Courts of coequal authority are not bound to follow one another. *(* People v Kearns, 168 Misc 264.) This court adheres to the philosophy that the cited rule of construction requires that while parts of the Labor Law should be liberally construed, particularly as to such matters as worker safety, all other rules of construction indicate that punitive or penal statutes, such as Labor Law § 198, must be strictly construed, and certainly a rule of construction cannot be used to expand the plain language of a statute.

When article 6 of the Labor Law, the title of which is Payment of Wages, was enacted in 1966, the Court of Appeals had already distinguished between wages and salary. Wages is to be considered to be compensation for manual labor, a "menial job" or subordinate occupation which is **[**125]** subject to immediate supervision. Salary, on the other hand, denotes **[*849]** compensation of a higher degree of employment which implies an office or position, or a fixed compensation for more important services. **[***8]** *(* Matter of Stryker, 158 NY 526 [1899].) Thus, some 67 years later the

Legislature could easily have remedied the problem and defined wages to include salary. However, it did not do so, but rather created the definition of wages as found in *section 190 of the Labor Law*.

There is a further provision which clarifies the Legislature's intention as to salary in general and the instant case in particular. *Section 191* sets forth the frequency of payments in which every employer is bound to pay wages. Specifically listed are the following: manual worker, railroad worker, commission salesman and then finally, the catchall category in *section 191 (1)(d)*, "clerical and other worker". If the plaintiff in the instant case is not within the definition of "clerical and other worker", then it would be evident that the Legislature did not protect him in his position under the "Payment of Wages" article of the Labor Law. To determine that issue, we need to go back to *section 190*, wherein subdivision (7) contains the following definition: "'Clerical and other worker' includes all employees not included in subdivisions four, five and six of this section, except any person employed in a **[***9]** bona fide executive, administrative or professional capacity whose earnings are in excess of four hundred dollars a week." Subdivisions (4), (5) and (6) refer to manual workers, railroad workers and commission salesmen. Clearly plaintiff does not fall within this definition.

Finally, it should be noted that at no time since 1966 has *section 190* or *191* been amended to expand the definition of "clerical and other worker" to include executives such as the plaintiff in the instant case. This court assumes that the Legislature was aware of the *Stryker* distinction between wages and salary and was further aware of the judicial struggles over the matter of "salary". It would have been simply too easy for the Legislature to have done away with this distinction if it had intended to.

It is therefore this court's determination that the plaintiff in his executive capacity received his remuneration as salary and not as wages and that he is therefore not covered under article 6 of the Labor Law. Plaintiff is thus not entitled to the attorneys' fees or liquidated damages referred to in *Labor Law § 198 (1-a)*.

[*850] It is therefore determined by the court that the issue of willfulness **[***10]** on the part of the defendant in not paying the severance pay need not be reached.

The plaintiff's motion is in all respects denied.

Submit judgment on the verdict accordingly.

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Yellow Book of Ny L.P. v. Dimilia

District Court of New York, First District, Nassau County

May 31, 2001, Decided

INDEX NO. 11639/00

Reporter

188 Misc. 2d 489 *; 729 N.Y.S.2d 286 **; 2001 N.Y. Misc. LEXIS 202 ***

Yellow Book of NY L. P., Individually and as Successor in Interest to Yellow Book Co. Inc., Plaintiff, v. Mary A. Dimilia, Doing Business as The Rug Nurse, Defendant.

Counsel: **[***1]** *Jay A. Press, P. C.,* Woodbury, for plaintiff.

Mary A. Dimilia, defendant *pro se.*

Judges: Kenneth L. Gartner, J.

Opinion by: Kenneth L. Gartner

Opinion

[*489] **[**287]** Kenneth L. Gartner, J.

The instant motion presents a unique issue of first impression involving a conflict between two legal principles: the **[*490]** principle that unpublished memorandum decisions of a court are not to be given binding effect, and the principle that decisions of a court with direct appellate authority are to be given controlling (i.e., stare decisis) effect by a subordinate court.

Pursuant to *Judiciary Law § 431*, all decisions of the Court of Appeals and the four Appellate Divisions are officially published. The conflict presented by these principles is therefore unique to the New York State trial courts of limited jurisdiction (e.g., the Nassau and Suffolk County District **[***2]** Courts, the New York City Civil and Criminal Courts, the various City, Village, and Justice Courts, *et al.*). The Supreme Court, Appellate Term, reviews their decisions, but its decisions are published only selectively. Many decisions of this intermediate appellate tribunal therefore circulate in samizdat form only.

The issue is also unique because unpublished decisions may still be considered as persuasive authority. Persuasive authority is how decisions of other (even superior) trial courts, federal courts, or courts of other jurisdictions would be viewed in any event by New York State trial courts of limited jurisdiction. The fact of nonpublication does not materially alter the deference afforded them. It is only when, in the case of the Appellate Term, the decision is to be normatively given not just persuasive but binding effect, that the issue comes to a head.

In the instant case, the issue is presented by the plaintiff moving for reargument based almost entirely upon two unreported Appellate Term decisions which the plaintiff has now annexed to its moving papers.

[*3]** Under the rule of stare decisis, "decisions by the Appellate Term must be followed by courts whose appeals lie to it." (28 NY Jur 2d, Courts and Judges § 220, at 274 [1997].) However, "generally, unpublished decisions or opinions have no precedential value other than the persuasiveness of their reasoning" (Binimow, *Precedential Effect of Unpublished Opinions,* 2000 ALR5th 17; *see* *Dubai Islamic Bank v Citibank, 126 F Supp 2d 659, 669, n 14* [SD NY 2000] [applying New York law]). (Even under this principle, unpublished decisions would of course bind the parties themselves pursuant to the doctrines of law of the case, collateral estoppel, and res judicata.)

Two basic policy concerns have been advanced to support this principle. The first is that "an opinion that is not published is written primarily for the parties who are already knowledgeable **[*491]** of the facts of the particular case, and for this reason, most unpublished opinions do not contain a **[**288]** comprehensive analysis of the legal **[***4]** issues decided by the court." (Binimow, at 17.) The second policy consideration supporting the application of this principle was expressed by Weaver, *The Precedential Value of Unpublished Judicial Opinions* (39 Mercer L Rev 477, 485-486 [1988]):

"To treat unpublished opinions as precedent would probably not promote the predictability and stability of the law. Rather, unpredictability and instability would seem to follow. If the average person, even through his attorney, does not have access to a decision, he certainly cannot take it into his account in ordering his affairs. The use as precedent of an unpublished opinion, to which even the average man with counsel does not have access, would make the law capricious and unpredictable. Thus, the policies behind the doctrine of stare decisis would support the conclusion that unpublished judicial opinions are not appropriate subjects of stare decisis."

Further recognition of this latter policy concern is given in section 0.23 of the Rules Relating to the Organization of the Court, promulgated by the United States Court of Appeals for the Second Circuit. This rule prohibits the citation of unreported summary orders **[***5]** of that appellate court because, *inter alia,* such unreported memoranda "are not uniformly available to all parties." (Decisions which are at least unofficially reported--by, e.g., Commerce Clearing House, the New York Law Journal, Westlaw, LEXIS, *et al.*--will be more widely available, often through searchable electronic data bases, and thus their exclusion from stare decisis would be supported by a weaker policy argument.) [1]

[*6]** The policy concern expressed by the Second Circuit rule, as well as the Mercer Law Review article, appears in the instant case particularly apt. The plaintiff, by dint of its status as one of the most frequent collection plaintiffs in Nassau County, is **[*492]** in a unique position of access to a multitude of decisions concerning it, and--whether volitionally or due to a faulty indexing system--has in the past presented to the court only those of the multitude which were resolved in its favor, and not those resolved against it. (*See Yellow Book v O'Connor,* NYLJ, Nov. 30, 2000, at 34, col 6 [Nassau Dist Ct] [unpublished Nassau County Supreme Court decision cited as precedent, with two conflicting unofficially reported Nassau County Supreme Court decisions ignored].) Hence, if an opinion has not been at least unofficially reported, this Court, at least in this particular situation, is at a disadvantage in assessing whether it represents an accurate and complete statement of the authoring court's position. [2]

[*7]** **[**289]** In weighing these policy concerns, some courts give stare decisis effect to unpublished decisions while others do not. (*Compare,* Nationwide Gen. Ins. Co. v Thomas, 1995 WL 158599, *3-4, 1995 Del Super LEXIS 129, *10-11 [Del Super, Feb. 27, 1995], *with* Matter of Shorter, 570 A2d 760, 771 [DC 1990]; *see also,* Weaver, *supra,* 39 Mercer L Rev at 489-490 [concluding that "those courts that regard unpublished opinions as (binding) precedents are not following the best rule"].)

Informed by these policy arguments, this Court proceeds, with caution, and with the rules of stare decisis to at the very least be strictly scrutinized, to the facts of the motion at bar.

The defendant, an $ 11,000 per year house cleaner residing in section 8 housing in the Suffolk County Town of Westhampton Beach, sought to have vacated the $ 3,000 default judgment entered against her by the plaintiff, a publisher of a Yellow Pages directory. The judgment was for an admittedly unpaid fee for advertising concededly published by the plaintiff on behalf of an entity known as The Rug Nurse.

[*493] By prior decision, this **[***8]** Court deferred action on the defendant's motion pending a hearing on three specified factual issues raised by the parties'

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[1] The rule that unpublished decisions are not to be given stare decisis effect must be distinguished from the rule instituted by some jurisdictions, such as the Second Circuit, prohibiting the citation of unpublished decisions at all. While motivated by similar policy concerns, some commentators have expressed the belief that these no-citation rules are unconstitutional. (*See* Katsh and Chachkes, *Examining the Constitutionality of No-Citation Rules,* NYLJ, Apr. 2, 2001, at 1, col 1.) Such a blanket no-citation rule would in any event be unworkable and unfair if applied to New York State trial courts and the Appellate Term: in the Second Circuit, all decisions are uniformly reported unless deliberately withheld. In these New York courts, such is not the case. The fact of nonreportage is not necessarily a volitional choice.

[2] Code of Professional Responsibility DR 7-106 (b) (22 NYCRR 1200.37) requires a lawyer to cite "controlling legal authority … directly adverse to the position of the client." This has been extremely narrowly construed. (*See* Simon, New York Code of Professional Responsibility Annotated, at 562 [2001 ed].) (Ironically, denying stare decisis effect to unpublished Appellate Term decisions would bring them outside the ambit of this limited rule.) However, the Appellate Division, Second Department, apparently imposes upon counsel a broader "affirmative obligation to advise the court of authorities adverse to his position." (Matter of La Cucina Mary Ann v State Liq. Auth., 150 AD2d 450, 451 [2d Dept 1989]; Matter of Cicio v City of New York, 98 AD2d 38, 40 [2d Dept 1983].) In People v Whelan (165 AD2d 313, 324, n 3 [2d Dept], *lv denied* ***78 NY2d 927*** [1991]), this principle was applied to an attorney's failure to cite to the Appellate Division a decision by Nassau County Court, an inferior, and therefore not "controlling," trial level court.

papers.

The plaintiff now moves for reargument, asserting that defendant's motion should be denied without the necessity for a factual hearing. For the following reasons, the plaintiff's motion for reargument is granted, but on reargument the prior determination is adhered to.

In the prior decision, this Court determined that one factual issue had been raised because the defendant has disputed the service alleged by the plaintiff's process server. The process server attests that service was made upon an individual identified as the defendant's daughter, Sue Dimilia. The defendant, however, asserts that "no one in my household was *ever* served a paper regarding this matter. The paper was served to a Sue Dimilia. There is no such person at that address."

In the prior decision, this Court observed that, as held by the Appellate Division in Chase Manhattan Bank v Carlson (113 AD2d 734, 735 [2d Dept 1985]), if service were in fact improper, dismissal **[***9]** would be required whether or not a meritorious defense had been stated:

"Absent proper service of a summons, a default judgment is a nullity and once it is shown that proper service was not effected the judgment must be unconditionally vacated. The existence or lack of a meritorious defense is irrelevant to the question of whether a judgment should be vacated for lack of personal jurisdiction [citations omitted]." (*Accord, Matter of Liberty Mut. Ins. Co.* [*Markovitch--Eagle Fuel Transp.--AIV Ins. Co.*], 214 AD2d 734 [2d Dept 1995]; DeMartino v Rivera, 148 AD2d 568 [2d Dept 1989]; New York State Higher Educ. Servs. Corp. v Adams, 173 Misc 2d 283 **[**290]** [Sup Ct, Albany County 1997].)

The plaintiff, in its current papers, asserts without citing any authority that this determination was "improper" because an affidavit was filed by the plaintiff "which clearly indicates that the defendant was sufficiently served with process according to the mandates of the CPLR." This contention is without merit. In fact, the instant facts are quite similar to those presented in OCI Mtge. Corp. v Omar (232 AD2d 462 **[***10]** [2d Dept 1996]). In *OCI Mtge. Corp.,* the Appellate Division held (232 AD2d at 462-463):

"The Supreme Court erred in failing to hold a hearing on the issue of the propriety of personal service **[*494]** upon the appellant since the appellant has raised an issue of fact with respect to the service of the summons and verified complaint. The burden of proving jurisdiction is upon the party asserting it and when challenged that party must sustain that burden by a preponderance of the credible evidence [citations omitted]. An affidavit of service is not conclusive once there is a sworn denial of receipt [citations omitted]. The appellant denies that the person upon whom process was served pursuant to CPLR 308 (2) was her cousin … Thus, factual issues have been raised which require a hearing to be held [citations omitted]."

Just as a hearing was required in *OCI Mtge. Corp.* where the defendant denied that process was served upon her cousin, a hearing is required in the instant case, where the defendant has denied that process was served **[***11]** upon her daughter.

Moreover, even if proper service was established, this Court in its prior decision identified another factual issue, i.e., whether the defendant has alleged a meritorious defense.

This Court determined (and the defendant agrees) that if (as the summons and complaint in this action indicate) The Rug Nurse is not a corporation but rather a d/b/a (doing business as) of the individual defendant, individual liability will lie and the defendant, having conceded that advertising charges were incurred by The Rug Nurse and have not been paid, would have no defense, since a sole proprietor bears unlimited liability for the venture's undertakings. (*Matter of Williams v Gleason,* 1980 WL 102282 [Sup Ct, Albany County 1979]; Latham Sparrowbush Assocs. v Shaker Estates, 153 AD2d 788, 791 [3d Dept 1989].) However, this Court determined that if The Rug Nurse is in fact a corporate party, rather than a sole proprietorship, no liability would lie, since the single signature line utilized on the plaintiff's form contracts is ambiguous, and thus, **[***12]** in light of the mandate that form contracts be construed against the drafters, is insufficient to personally bind the individual signatory on behalf of a corporate party. (*Yellow Book v O'Connor, supra,* NYLJ, Nov. 30, 2000, at 34, col 6 [Nassau Dist Ct].) This is particularly the case on the instant facts where, as observed by the Supreme Court, Nassau County, in *Yellow Book Co. v Williams* (NYLJ, Sept. 26, 1994, at 31, col 2 [hereafter *Williams*]), the signatories are largely "unsophisticated, non-legal-trained individuals running small businesses." (*Accord, Yellow Book v Greene,* NYLJ, Feb. 8, 1994, at 27, col 1 [Sup Ct, Nassau County] [O'Connell, J.].) A factual issue is thus presented as to whether The Rug Nurse is indeed a sole proprietorship or some other form of entity.

[*495] The plaintiff protests that *O'Connor, Greene,* and *Williams* are all contrary to a decision in *Yellow Book Co. v Baum* (case No. 2000-786, Dec. 22, 2000 **[**291]** [App Term, 2d Dept]). However, the *Baum* decision simply stated:

"A reading of the two page agreement **[***13]** involved herein reveals that it clearly and unambiguously made the defendant individually liable thereon. Under the circumstances, the defendant's attempt to avoid personal responsibility was properly rejected [citations omitted]."

Baum is an unpublished summary decision which does not set forth the facts adjudicated even to the extent of revealing whether the contract at issue was the same as, or similar to, the contract at issue in the instant case. Neither does *Baum* reveal whether the specific grounds given for the *O'Connor, Greene,* and *Williams* decisions were presented. "The doctrine of stare decisis presupposes the existence of a well-defined precedent determinative of a point in question, and in the absence of such a precedent, the doctrine is inapplicable." (28 NY Jur 2d, Courts and Judges § 207, at 258 [1997].) As held in *Wellbilt Equip. Corp. v Fireman (275 AD2d 162, 168* [1st Dept 2000]), a case "is precedent only as to those questions presented, considered and squarely decided [citations omitted]." (*Accord, Williams v AGK Communications, 143 Misc 2d 845, 848* **[***14]** [Sup Ct, Onondaga County 1989] ["(a) binding precedent is not created by a court's decision unless the subject matter is clearly and squarely dealt with and the principle established is well defined"]; *see also, Imling v Port Auth., 184 Misc 2d 893, 895* [Sup Ct, NY County 2000] [finding that where the particular legal argument at issue had not been raised in the prior case or addressed by the court, the prior case held no precedential value on the specific legal issue].)

Moreover, in *Baum,* the Appellate Term was unaware of the "smoking gun" concession which would later be made in *Yellow Book v Davis* (index No. 378/99, Feb. 26, 2001 [Nassau Dist Ct] [Fairgrieve, J.]). During the trial in *Davis,* counsel for the instant plaintiff was questioned as to why, in light of the persistent litigation engendered by the plaintiff's anomalous attempt to have a single signature line perform the threefold function of (1) binding the principal to the agreement, (2) supporting the agency of the signatory, and (3) binding the agent as a guarantor of its principal's obligation (*see Savoy Record Co. v Cardinal Export Corp., 15 NY2d 1* [1964]), **[***15]** the plaintiff had not opted to amend the form to provide for at least two separate signature lines, one binding the principal and one **[*496]** personally guaranteeing the obligation, so that clarity could be imposed and a frequent necessity for litigation obviated:

"THE COURT: Could I ask you a question? When you made the amendment in 1995 was it considered to put in the two separate signature lines?

"COUNSEL: Yes, and we opted not to do it and I'll tell you exactly why.

"THE COURT: Why?

"COUNSEL: The reason why is from a commercial business practice. Sometimes when you ask a person to sign twice they refuse. We're in the business of selling advertising."

In *Williams* (*supra*), Nassau County Supreme Court stated (at 31, col 2):

"It would appear that the practice of the Plaintiff Yellow Book Co., Inc., to bind unsophisticated, non-legal-trained individuals running small businesses to personal liability … may be a fraud on the business public."

It is not necessary to agree with this formulation to nevertheless conclude, as did *O'Connor, Williams* and *Greene,* that **[**292]** the contract is sufficiently ambiguous to preclude the imposition of personal **[***16]** liability upon corporate officers. Since a different result would thus obtain if The Rug Nurse is a corporation as opposed to a sole proprietorship, this question must be addressed factually at a hearing in this matter.

Even if proper service were shown, and a meritorious defense found to be lacking, a third factual issue was identified in this Court's prior decision. This Court found that there superficially did not appear to be any basis for this Court to exercise jurisdiction over the Westhampton Beach resident defendant pursuant to *UDCA 404*. The signing of a contract in Westhampton Beach did not "constitute the transaction of any business within a district of a court within [Nassau] County" within the meaning of that statute. (*Marketing Showcase v Alberto-Culver Co., 445 F Supp 755, 759* [SD NY 1978].) While parties are permitted to nevertheless contractually agree on jurisdiction, the clause in the contract relied upon by the plaintiff makes no mention of consenting to jurisdiction in Nassau County. The clause simply provides that the contract is "deemed transacted **[***17]** in Nassau County." The import of this indirect formulation may be clear to a lawyer or judge familiar with the legal rules governing the bases for establishing jurisdiction. A lay reader, however, would not necessarily know the legal significance of **[*497]** the fiction to which he or she is being asked to give assent. This indirect formulation is therefore insufficient to confer jurisdiction when utilized in a form contract in a transaction with many of the indicia of "consumer transactions." (*See Yellow Book v Abbott,* NYLJ, Oct. 30, 2000, at 33, col 5 [Nassau Dist Ct].) A factual issue is raised as to whether there are additional grounds to support jurisdiction.

The plaintiff asserts that the *Abbott* decision is contrary to yet another unpublished decision of the Appellate Term, Second Department, *Yellow Book Co. v Anderson* (index No. 96-1025 N C, June 4, 1997). In that case, the Appellate Term reversed a decision of the District Court, Nassau County (Madden, J.), on the ground that the allegation in the complaint in that action (which referred to the same clause which is at issue in the instant case), "was sufficient to establish the basis for personal jurisdiction **[***18]** over defendant." However, it is once again not clear that the specific legal grounds upon which the *Abbott* decision was based were ever considered or ruled upon by the Appellate Term in *Anderson. Anderson* can therefore not be considered precedent as to these entirely different issues. (*Wellbilt Equip. Corp. v Fireman, supra, 275 AD2d at 168*.)

A hearing must therefore be held as directed in this Court's prior decision.

End of Document

29 USCS § 1103

Current through Public Law 116-68, approved November 8, 2019.

United States Code Service > TITLE 29. LABOR (Chs. 1 — 32) > CHAPTER 18. EMPLOYEE RETIREMENT INCOME SECURITY PROGRAM (§§ 1001 — 1461) > PROTECTION OF EMPLOYEE BENEFIT RIGHTS (§§ 1001 — 1191c) > REGULATORY PROVISIONS (§§ 1021 — 1191c) > Fiduciary Responsibility (§§ 1101 — 1114)

§ 1103. Establishment of trust

(a) Benefit plan assets to be held in trust; authority of trustees. Except as provided in subsection (b), all assets of an employee benefit plan shall be held in trust by one or more trustees. Such trustee or trustees shall be either named in the trust instrument or in the plan instrument described in section 402(a) [*29 USCS § 1102(a)*] or appointed by a person who is a named fiduciary, and upon acceptance of being named or appointed, the trustee or trustees shall have exclusive authority and discretion to manage and control the assets of the plan, except to the extent that—

(1)the plan expressly provides that the trustee or trustees are subject to the direction of a named fiduciary who is not a trustee, in which case the trustees shall be subject to proper directions of such fiduciary which are made in accordance with the terms of the plan and which are not contrary to this Act, or

(2)authority to manage, acquire, or dispose of assets of the plan is delegated to one or more investment managers pursuant to section 402(c)(3) [28 USCS § 1102(c)(3)].

(b) Exceptions. The requirements of subsection (a) of this section shall not apply—

(1)to any assets of a plan which consist of insurance contracts or policies issued by an insurance company qualified to do business in a State;

(2)to any assets of such an insurance company or any assets of a plan which are held by such an insurance company;

(3)to a plan—

(A)some or all of the participants of which are employees described in *section 401(c)(1) of the Internal Revenue Code of 1986* [*26 USCS § 401(c)(1)*]; or

(B)which consists of one or more individual retirement accounts described in *section 408 of the Internal Revenue Code of 1986* [*26 USCS § 408*];

to the extent that such plan's assets are held in one or more custodial accounts which qualify under section 401(f) or 408(h) of such Code [*26 USCS § 401(f)* or *408(h)*], whichever is applicable.

(4)to a plan which the Secretary exempts from the requirement of subsection (a) and which is not subject to any of the following provisions of this Act—

(A)part 2 of this subtitle [*29 USCS §§ 1051* et seq.],

(B)part 3 of this subtitle [*29 USCS §§ 1081* et seq.], or

(C)title IV of this Act; or

(5)to a contract established and maintained under *section 403(b) of the Internal Revenue Code of 1986* [*26 USCS § 403(b)*] to the extent that the assets of the contract are held in one or more custodial accounts pursuant to section 403(b)(7) of such Code [*26 USCS § 403(b)(7)*].

(6) Any plan, fund or program under which an employer, all of whose stock is directly or indirectly owned by employees, former employees or their beneficiaries, proposes through an unfunded arrangement to compensate retired employees for benefits which were forfeited by such employees under a pension plan maintained by a former employer prior to the date such pension plan became subject to this Act.

(c) Assets of plan not to inure to benefit of employer; allowable purposes of holding plan assets.

(1) Except as provided in paragraph (2), (3), or (4) or subsection (d), or under section 4042 and 4044 [29 USCS §§ 1342, 1344] (relating to termination of insured plans), or under section 420 of the Internal Revenue Code of 1986 [26 USCS § 420] (as in effect on the date of the enactment of the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015 [enacted July 30, 2015]), the assets of a plan shall never inure to the benefit of any employer and shall be held for the exclusive purposes of providing benefits to participants in the plan and their beneficiaries and defraying reasonable expenses of administering the plan.

(2)

(A) In the case of a contribution, or a payment of withdrawal liability under part 1 of subtitle E of Title IV [29 USCS §§ 1381 et seq.]—

(i)if such contribution or payment is made by an employer to a plan (other than a multiemployer plan) by a mistake of fact, paragraph (1) shall not prohibit the return of such contribution to the employer within one year after the payment of the contribution, and

(ii)if such contribution or payment is made by an employer to a multiemployer plan by a mistake of fact or law (other than a mistake relating to whether the plan is described in section 401(a) of the Internal Revenue Code of 1986 [26 USCS § 401(a)] or the trust which is part of such plan is exempt from taxation under section 501(a) of such Code [26 USCS § 501(a)]), paragraph (1) shall not prohibit the return of such contribution or payment to the employer within 6 months after the plan administrator determines that the contribution was made by such a mistake.

(B) If a contribution is conditioned on initial qualification of the plan under section 401 or 403(a) of the Internal Revenue Code of 1986 [26 USCS § 401 or 403(a)], and if the plan receives an adverse determination with respect to its initial qualification, then paragraph (1) shall not prohibit the return of such contribution to the employer within one year after such determination, but only if the application for the determination is made by the time prescribed by law for filing the employer's return for the taxable year in which such plan was adopted, or such later date as the Secretary of the Treasury may prescribe.

(C) If a contribution is conditioned upon the deductibility of the contribution under section 404 of the Internal Revenue Code of 1986 [26 USCS § 404], then, to the extent the deduction is disallowed, paragraph (1) shall not prohibit the return to the employer of such contribution (to the extent disallowed) within one year after the disallowance of the deduction.

(3) In the case of a withdrawal liability payment which has been determined to be an overpayment, paragraph (1) shall not prohibit the return of such payment to the employer within 6 months after the date of such determination.

(d) Termination of plan.

(1) Upon termination of a pension plan to which section 4021 [29 USCS § 1321] does not apply at the time of termination and to which this part [29 USCS §§ 1101 et seq.] applies (other than a plan to which no employer contributions have been made) the assets of the plan shall be allocated in accordance with the provisions of section 4044 of this Act [29 USCS § 1344], except as otherwise provided in regulations of the Secretary.

(2) The assets of a welfare plan which terminates shall be distributed in accordance with the terms of the plan, except as otherwise provided in regulations of the Secretary.

History

HISTORY:

Act Sept. 2, 1974, *P. L. 93-406*, Title I, Subtitle B, Part 4, § 403, *88 Stat. 876*; Sept. 26, 1980, *P. L. 96-364*, Title III, § 310, Title IV, §§ 402(b)(2), 410(a), 411(c), *94 Stat. 1296*, 1299, 1308; Dec. 22, 1987, *P. L. 100-203*, Title IX, Subtitle D, Part II, Subpart D, § 9343(c), *101 Stat. 1330*-372; Dec. 19, 1989, *P. L. 101-239*, Title VII, Subtitle G, Part V, Subpart C, § 7881(k), Subpart D, §§ 7891(a)(1), 7894(e)(1)(A), (3), *103 Stat. 2443*, 2445, 2450; Nov. 5, 1990, *P. L. 101-508*, Title XII, Subtitle B, § 12012(a), *104 Stat. 1388*-571; Dec. 8, 1994, *P. L. 103-465*, Title VII, Subtitle D, § 731(c)(4)(B), *108 Stat. 5004*; Dec. 17, 1999, *P. L. 106-170*, Title V, Subtitle C, Part I, § 535(a)(2)(B), *113 Stat. 1934*; April 10, 2004, *P. L. 108-218*, Title II, § 204(b)(2), *118 Stat. 609*; Oct. 22, 2004, *P. L. 108-357*, Title VII, § 709(a)(2), *118 Stat. 1551*; Aug. 17, 2006, *P. L. 109-280*, Title I, Subtitle A, § 108(a)(11) [107(a)(11)], *120 Stat. 819*; June 25, 2010, *P. L. 111-192*, Title II, Subtitle A, § 202(a), *124 Stat. 1297*; July 6, 2012, *P. L. 112-141*, Div D, Title II, Subtitle B, Part IV, § 40241(b)(1), *126 Stat. 859*; July 31, 2015, *P. L. 114-41*, Title II, § 2007(b)(1), *129 Stat. 459*.

End of Document

[29 USCS § 1132, Part 1 of 4]

Current through Public Law 116-68, approved November 8, 2019.

United States Code Service > TITLE 29. LABOR (Chs. 1 — 32) > CHAPTER 18. EMPLOYEE RETIREMENT INCOME SECURITY PROGRAM (§§ 1001 — 1461) > PROTECTION OF EMPLOYEE BENEFIT RIGHTS (§§ 1001 — 1191c) > REGULATORY PROVISIONS (§§ 1021 — 1191c) > Administration and Enforcement (§§ 1131 — 1151)

§ 1132. Civil enforcement

(a) Persons empowered to bring a civil action. A civil action may be brought—

(1)by a participant or beneficiary—

(A)for the relief provided for in subsection (c) of this section, or

(B)to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan;

(2)by the Secretary, or by a participant, beneficiary or fiduciary for appropriate relief under section 409 [*29 USCS § 1109*];

(3)by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this title or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of this title or the terms of the plan;

(4)by the Secretary, or by a participant, or beneficiary for appropriate relief in the case of a violation of 105(c) [*29 USCS § 1025(c)*];

(5)except as otherwise provided in subsection (b), by the Secretary (A) to enjoin any act or practice which violates any provision of this title, or (B) to obtain other appropriate equitable relief (i) to redress such violation or (ii) to enforce any provision of this title;

(6)by the Secretary to collect any civil penalty under paragraph (2), (4), (5), (6), (7), (8), or (9) of subsection (c) or under subsection (i) or (l);

(7)by a State to enforce compliance with a qualified medical child support order (as defined in section 609(a)(2)(A) [*29 USCS § 1169(a)(2)(A)*]);

(8)by the Secretary, or by an employer or other person referred to in section 101(f)(1) [*29 USCS § 1021(f)(1)*], (A) to enjoin any act or practice which violates subsection (f) of section 101 [*29 USCS § 1021(f)*], or (B) to obtain appropriate equitable relief (i) to redress such violation or (ii) to enforce such subsection;

(9)in the event that the purchase of an insurance contract or insurance annuity in connection with termination of an individual's status as a participant covered under a pension plan with respect to all or any portion of the participant's pension benefit under such plan constitutes a violation of part 4 of this title [subtitle] or the terms of the plan, by the Secretary, by any individual who was a participant or beneficiary at the time of the alleged violation, or by a fiduciary, to obtain appropriate relief, including the posting of security if necessary, to assure receipt by the participant or beneficiary of the amounts provided or to be provided by such insurance contract or annuity, plus reasonable prejudgment interest on such amounts;

(10)in the case of a multiemployer plan that has been certified by the actuary to be in endangered or critical status under section 305 [*29 USCS § 1085*], if the plan sponsor—

(A)has not adopted a funding improvement or rehabilitation plan under that section by the deadline established in such section, or

(B)fails to update or comply with the terms of the funding improvement or rehabilitation plan in accordance with the requirements of such section,

by an employer that has an obligation to contribute with respect to the multiemployer plan or an employee organization that represents active participants in the multiemployer plan, for an order compelling the plan sponsor to adopt a funding improvement or rehabilitation plan or to update or comply with the terms of the funding improvement or rehabilitation plan in accordance with the requirements of such section and the funding improvement or rehabilitation plan; or

(11)in the case of a multiemployer plan, by an employee representative, or any employer that has an obligation to contribute to the plan, (A) to enjoin any act or practice which violates subsection (k) of section 101 [*29 USCS § 1021*] (or, in the case of an employer, subsection (l) of such section), or (B) to obtain appropriate equitable relief (i) to redress such violation or (ii) to enforce such subsection.

(b) Plans qualified under Internal Revenue Code; maintenance of actions involving delinquent contributions.

(1) In the case of a plan which is qualified under *section 401(a)*, *403(a)*, or *405(a) of the Internal Revenue Code of 1986* (or with respect to which an application to so qualify has been filed and has not been finally determined) the Secretary may exercise his authority under subsection (a)(5) with respect to a violation of, or the enforcement of, parts 2 and 3 of this subtitle [*29 USCS §§ 1051* et seq., *§§ 1081* et seq.] (relating to participation, vesting, and funding), only if—

(A)requested by the Secretary of the Treasury, or

(B)one or more participants, beneficiaries, or fiduciaries, of such plan request in writing (in such manner as the Secretary shall prescribe by regulation) that he exercise such authority on their behalf. In the case of such a request under this paragraph he may exercise such authority only if he determines that such violation affects, or such enforcement is necessary to protect, claims of participants or beneficiaries to benefits under the plan.

(2) The Secretary shall not initiate an action to enforce section 515 [*29 USCS § 1145*].

(3) Except as provided in subsections (c)(9) and (a)(6) (with respect to collecting civil penalties under subsection (c)(9)), the Secretary is not authorized to enforce under this part any requirement of part 7 [*29 USCS §§ 1181* et seq.] against a health insurance issuer offering health insurance coverage in connection with a group health plan (as defined in section 733(a)(1) [*29 USCS § 1191b(a)(1)*]). Nothing in this paragraph shall affect the authority of the Secretary to issue regulations to carry out such part.

(c) Administrator's refusal to supply requested information; penalty for failure to provide annual report in complete form.

(1) Any administrator (A) who fails to meet the requirements of paragraph (1) or (4) of section 606, section 101(e)(1), section 101(f), or section 105(a) [*29 USCS § 1166(a)(1)* or (4), 1021(e)(1), 1021(f), or 1025(a)] with respect to a participant or beneficiary, or (B) who fails or refuses to comply with a request for any information which such administrator is required by this title to furnish to a participant or beneficiary (unless such failure or refusal results from matters reasonably beyond the control of the administrator) by mailing the material requested to the last known address of the requesting participant or beneficiary within 30 days after such request may in the court's discretion be personally liable to such participant or beneficiary in the amount of up to $100 a day from the date of such failure or refusal, and the court may in its discretion order such other relief as it deems proper. For purposes of this paragraph, each violation described in subparagraph (A) with respect to any single participant, and each violation described in subparagraph (B) with respect to any single participant or beneficiary, shall be treated as a separate violation.

(2) The Secretary may assess a civil penalty against any plan administrator of up to $1,000 a day from the date of such plan administrator's failure or refusal to file the annual report required to be filed with the Secretary under section 101(b)(1) [29 USCS § 1021(b)(1)]. For purposes of this paragraph, an annual report that has been rejected under section 104(a)(4) [29 USCS § 1024(a)(4)] for failure to provide material information shall not be treated as having been filed with the Secretary.

(3) Any employer maintaining a plan who fails to meet the notice requirement of section 101(d) [29 USCS § 1021(d)] with respect to any participant or beneficiary or who fails to meet the requirements of section 101(e)(2) [29 USCS § 1021(e)(2)] with respect to any person or who fails to meet the requirements of section 302(d)(12)(E) with respect to any person may in the court's discretion be liable to such participant or beneficiary or to such person in the amount of up to $100 a day from the date of such failure, and the court may in its discretion order such other relief as it deems proper.

(4) The Secretary may assess a civil penalty of not more than $1,000 a day for each violation by any person of subsection (j), (k), or (l) of section 101 [29 USCS § 1021] or section 514(e)(3) [29 USCS § 1144(e)(3)].

(5) The Secretary may assess a civil penalty against any person of up to $1,000 a day from the date of the person's failure or refusal to file the information required to be filed by such person with the Secretary under regulations prescribed pursuant to section 101(g) [29 USCS § 1021(g)].

(6) If, within 30 days of a request by the Secretary to a plan administrator for documents under section 104(a)(6) [29 USCS § 1024(a)(6)], the plan administrator fails to furnish the material requested to the Secretary, the Secretary may assess a civil penalty against the plan administrator of up to $100 a day from the date of such failure (but in no event in excess of $1,000 per request). No penalty shall be imposed under this paragraph for any failure resulting from matters reasonably beyond the control of the plan administrator.

(7) The Secretary may assess a civil penalty against a plan administrator of up to $100 a day from the date of the plan administrator's failure or refusal to provide notice to participants and beneficiaries in accordance with subsection (i) or (m) of section 101 [29 USCS § 1021]. For purposes of this paragraph, each violation with respect to any single participant or beneficiary shall be treated as a separate violation.

(8) The Secretary may assess against any plan sponsor of a multiemployer plan a civil penalty of not more than $1,100 per day—

> **(A)**for each violation by such sponsor of the requirement under section 305 [29 USCS § 1085] to adopt by the deadline established in that section a funding improvement plan or rehabilitation plan with respect to a multiemployer plan which is in endangered or critical status, or
>
> **(B)**in the case of a plan in endangered status which is not in seriously endangered status, for failure by the plan to meet the applicable benchmarks under section 305 [29 USCS § 1085] by the end of the funding improvement period with respect to the plan.

(9)

> **(A)**The Secretary may assess a civil penalty against any employer of up to $100 a day from the date of the employer's failure to meet the notice requirement of section 701(f)(3)(B)(i)(I) [29 USCS § 1181(f)(3)(B)(i)(I)]. For purposes of this subparagraph, each violation with respect to any single employee shall be treated as a separate violation.
>
> **(B)**The Secretary may assess a civil penalty against any plan administrator of up to $100 a day from the date of the plan administrator's failure to timely provide to any State the information required to be disclosed under section 701(f)(3)(B)(ii) [29 USCS § 1181(f)(3)(B)(ii)]. For purposes of this subparagraph, each violation with respect to any single participant or beneficiary shall be treated as a separate violation.

(10) Secretarial enforcement authority relating to use of genetic information.

(A) General rule. The Secretary may impose a penalty against any plan sponsor of a group health plan, or any health insurance issuer offering health insurance coverage in connection with the plan, for any failure by such sponsor or issuer to meet the requirements of subsection (a)(1)(F), (b)(3), (c), or (d) of section 702 [*29 USCS § 1182*] or section 701 or 702(b)(1) [*29 USCS § 1181* or *1182(b)(1)*] with respect to genetic information, in connection with the plan.

(B) Amount.

(i) In general. The amount of the penalty imposed by subparagraph (A) shall be $100 for each day in the noncompliance period with respect to each participant or beneficiary to whom such failure relates.

(ii) Noncompliance period. For purposes of this paragraph, the term "noncompliance period" means, with respect to any failure, the period—

(I)beginning on the date such failure first occurs; and

(II)ending on the date the failure is corrected.

(C) Minimum penalties where failure discovered. Notwithstanding clauses (i) and (ii) of subparagraph (D):

(i) In general. In the case of 1 or more failures with respect to a participant or beneficiary—

(I)which are not corrected before the date on which the plan receives a notice from the Secretary of such violation; and

(II)which occurred or continued during the period involved;

the amount of penalty imposed by subparagraph (A) by reason of such failures with respect to such participant or beneficiary shall not be less than $2,500.

(ii) Higher minimum penalty where violations are more than de minimis. To the extent violations for which any person is liable under this paragraph for any year are more than de minimis, clause (i) shall be applied by substituting "$15,000" for "$2,500" with respect to such person.

(D) Limitations.

(i) Penalty not to apply where failure not discovered exercising reasonable diligence. No penalty shall be imposed by subparagraph (A) on any failure during any period for which it is established to the satisfaction of the Secretary that the person otherwise liable for such penalty did not know, and exercising reasonable diligence would not have known, that such failure existed.

(ii) Penalty not to apply to failures corrected within certain periods. No penalty shall be imposed by subparagraph (A) on any failure if—

(I)such failure was due to reasonable cause and not to willful neglect; and

(II)such failure is corrected during the 30-day period beginning on the first date the person otherwise liable for such penalty knew, or exercising reasonable diligence would have known, that such failure existed.

(iii) Overall limitation for unintentional failures. In the case of failures which are due to reasonable cause and not to willful neglect, the penalty imposed by subparagraph (A) for failures shall not exceed the amount equal to the lesser of—

(I)10 percent of the aggregate amount paid or incurred by the plan sponsor (or predecessor plan sponsor) during the preceding taxable year for group health plans; or

(II)$500,000.

(E) Waiver by Secretary. In the case of a failure which is due to reasonable cause and not to willful neglect, the Secretary may waive part or all of the penalty imposed by subparagraph (A) to the extent that the payment of such penalty would be excessive relative to the failure involved.

(F) Definitions. Terms used in this paragraph which are defined in section 733 [*29 USCS § 1191b*] shall have the meanings provided such terms in such section.

(11) The Secretary and the Secretary of Health and Human Services shall maintain such ongoing consultation as may be necessary and appropriate to coordinate enforcement under this subsection with enforcement under section 1144(c)(8) of the Social Security Act [*42 USCS § 1320b-14(c)(8)*].

(12) The Secretary may assess a civil penalty against any sponsor of a CSEC plan of up to $100 a day from the date of the plan sponsor's failure to comply with the requirements of section 306(j)(3) [29 USCS § 1805a(j)(3)] to establish or update a funding restoration plan.

(d) Status of employee benefit plan as entity.

(1) An employee benefit plan may sue or be sued under this title as an entity. Service of summons, subpena, or other legal process of a court upon a trustee or an administrator of an employee benefit plan in his capacity as such shall constitute service upon the employee benefit plan. In a case where a plan has not designated in the summary plan description of the plan an individual as agent for the service of legal process, service upon the Secretary shall constitute such service. The Secretary, not later than 15 days after receipt of service under the preceding sentence, shall notify the administrator or any trustee of the plan of receipt of such service.

(2) Any money judgment under this title against an employee benefit plan shall be enforceable only against the plan as an entity and shall not be enforceable against any other person unless liability against such person is established in his individual capacity under this title.

(e) Jurisdiction.

(1) Except for actions under subsection (a)(1)(B) of this section, the district courts of the United States shall have exclusive jurisdiction of civil actions under this title brought by the Secretary or by a participant, beneficiary, fiduciary, or any person referred to in section 101(f)(1) [*29 USCS § 1021(f)(1)*]. State courts of competent jurisdiction and district courts of the United States shall have concurrent jurisdiction of actions under paragraphs (1)(B) and (7) of subsection (a) of this section.

(2) Where an action under this title is brought in a district court of the United States, it may be brought in the district where the plan is administered, where the breach took place, or where a defendant resides or may be found, and process may be served in any other district where a defendant resides or may be found.

(f) Amount in controversy; citizenship of parties. The district courts of the United States shall have jurisdiction, without respect to the amount in controversy or the citizenship of the parties, to grant the relief provided for in subsection (a) of this section in any action.

(g) Attorney's fees and costs; awards in actions involving delinquent contributions.

(1) In any action under this title (other than an action described in paragraph 2) by a participant, beneficiary, or fiduciary, the court in its discretion may allow a reasonable attorney's fee and costs of action to either party.

(2) In any action under this title by a fiduciary for or on behalf of a plan to enforce section 515 [*29 USCS § 1145*] in which a judgment in favor of the plan is awarded, the court shall award the plan—

(A)the unpaid contributions,

(B)interest on the unpaid contributions,

(C)an amount equal to the greater of—

(i)interest on the unpaid contributions, or

(ii)liquidated damages provided for under the plan in an amount not in excess of 20 percent (or such higher percentage as may be permitted under Federal or State law) of the amount determined by the court under subparagraph (A),

(D)reasonable attorney's fees and costs of the action, to be paid by the defendant, and

(E)such other legal or equitable relief as the court deems appropriate.

For purposes of this paragraph, interest on unpaid contributions shall be determined by using the rate provided under the plan, or, if none, the rate prescribed under *section 6621 of the Internal Revenue Code of 1986* [*26 USCS § 6621*].

(h) Service upon Secretary of Labor and Secretary of the Treasury. A copy of the complaint in any action under this title by a participant, beneficiary, or fiduciary (other than an action brought by one or more participants or beneficiaries under subsection (a)(1)(B) which is solely for the purpose of recovering benefits due such participants under the terms of the plan) shall be served upon the Secretary and the Secretary of the Treasury by certified mail. Either Secretary shall have the right in his discretion to intervene in any action, except that the Secretary of the Treasury may not intervene in any action under part 4 of this subtitle [*29 USCS §§ 1101* et seq.]. If the Secretary brings an action under subsection (a) on behalf of a participant or beneficiary, he shall notify the Secretary of the Treasury.

(i) Administrative assessment of civil penalty. In the case of a transaction prohibited by section 406 [*29 USCS § 1106*] by a party in interest with respect to a plan to which this part applies, the Secretary may assess a civil penalty against such party in interest. The amount of such penalty may not exceed 5 percent of the amount involved in each such transaction (as defined in *section 4975(f)(4) of the Internal Revenue Code of 1986* [*26 USCS § 4975(f)(4)*]) for each year or part thereof during which the prohibited transaction continues, except that, if the transaction is not corrected (in such manner as the Secretary shall prescribe in regulations which shall be consistent with section 4975(f)(5) of such Code [*26 USCS § 4975(f)(5)*]) within 90 days after notice from the Secretary (or such longer period as the Secretary may permit), such penalty may be in an amount not more than 100 percent of the amount involved. This subsection shall not apply to a transaction with respect to a plan described in section 4975(e)(1) of such Code [*26 USCS § 4975(e)(1)*].

(j) Direction and control of litigation by Attorney General. In all civil actions under this title, attorneys appointed by the Secretary may represent the Secretary (except as provided in *section 518(a) of title 28, United States Code*), but all such litigation shall be subject to the direction and control of the Attorney General.

(k) Jurisdiction of actions against the Secretary of Labor. Suits by an administrator, fiduciary, participant, or beneficiary of an employee benefit plan to review a final order of the Secretary, to restrain the Secretary from taking any action contrary to the provisions of this Act, or to compel him to take action required under this title, may be brought in the district court of the United States for the district where the plan has its principal office, or in the United States District Court for the District of Columbia.

(l) Civil penalties on violations by fiduciaries.

(1) In the case of—

(A)any breach of fiduciary responsibility under (or other violation of) part 4 [*29 USCS §§ 1101* et seq.] by a fiduciary, or

(B)any knowing participation in such a breach or violation by any other person,

the Secretary shall assess a civil penalty against such fiduciary or other person in an amount equal to 20 percent of the applicable recovery amount.

(2) For purposes of paragraph (1), the term "applicable recovery amount" means any amount which is recovered from a fiduciary or other person with respect to a breach or violation described in paragraph (1)—

(A)pursuant to any settlement agreement with the Secretary, or

(B)ordered by a court to be paid by such fiduciary or other person to a plan or its participants and beneficiaries in a judicial proceeding instituted by the Secretary under subsection (a)(2) or (a)(5).

(3) The Secretary may, in the Secretary's sole discretion, waive or reduce the penalty under paragraph (1) if the Secretary determines in writing that—

(A)the fiduciary or other person acted reasonably and in good faith, or

(B)it is reasonable to expect that the fiduciary or other person will not be able to restore all losses to the plan (or to provide the relief ordered pursuant to subsection (a)(9)) without severe financial hardship unless such waiver or reduction is granted.

(4) The penalty imposed on a fiduciary or other person under this subsection with respect to any transaction shall be reduced by the amount of any penalty or tax imposed on such fiduciary or other person with respect to such transaction under subsection (i) of this section and *section 4975 of the Internal Revenue Code of 1986* [*26 USCS § 4975*].

(m) Penalty for improper distribution. In the case of a distribution to a pension plan participant or beneficiary in violation of section 206(e) [*29 USCS § 1056(e)*] by a plan fiduciary, the Secretary shall assess a penalty against such fiduciary in an amount equal to the value of the distribution. Such penalty shall not exceed $10,000 for each such distribution.

History

HISTORY:

Act Sept. 2, 1974, *P. L. 93-406*, Title I, Subtitle B, Part 5, § 502, *88 Stat. 891*; Sept. 26, 1980, *P. L. 96-364*, Title III, § 306(b), *94 Stat. 1295*; April 7, 1986, *P. L. 99-272*, Title X, § 10002(b), *100 Stat. 231*; Dec. 22, 1987, *P. L. 100-203*, Title IX, Subtitle D, Part II, Subpart D, §§ 9342(c), 9344, *101 Stat. 1330*-372, 1330-373, Dec. 19, 1989, *P. L. 101-239*, Title II, Subtitle B, § 2101(a), (b), Title VII, Subtitle G, Part V, Subpart C, § 7881(b)(5)(B), (j)(2), (3), Subpart D, §§ 7891(a)(1), 7894(f)(1), *103 Stat. 2123*, 2438, 2442, 2445, 2450; Nov. 5, 1990, *P. L. 101-508*, Title XII, Subtitle B, § 12021(d)(2), *104 Stat. 1388*-573; Aug. 10, 1993, *P. L. 103-66*, Title IV, Subtitle D, § 4301(c)(1)–(3), *107 Stat. 376*; Oct. 22, 1994, *P. L. 103-401*, §§ 2, 3, *108 Stat. 4172*; Dec. 8, 1994, *P. L. 103-465*, Title VII, Subtitle F, Part I, Subpart B, § 761(a)(9)(B)(ii), *108 Stat. 5033*; Aug. 21, 1996, *P. L. 104-191*, Title I, Subtitle A, Part 1, § 101(b), (e)(2), *110 Stat. 1951*, 1952; Sept. 26, 1996, *P. L. 104-204*, Title VI, § 603(b)(3)(E), *110 Stat. 2938*; Aug. 5, 1997, *P. L. 105-34*, Title XV, Subtitle A, § 1503(c)(2)(B), (d)(7), *111 Stat. 1062*; July 30, 2002, *P. L. 107-204*, Title III, § 306(b)(3), *116 Stat. 783*; April 10, 2004, *P. L. 108-218*, Title I, §§ 102(d), 103(b), 104(a)(2), *118 Stat. 602*, 603, 606; Aug. 17, 2006, *P. L. 109-280*, Title I, Subtitle A, § 103(b)(2), Title II, Subtitle A, § 202(b), (c), Title V, §§ 502(a)(2), (b)(2), 507(b), 508(a)(2)(C), Title IX, § 902(f)(2), *120 Stat. 816*, 884, 940, 941, 949, 951, 1039; May 21, 2008, *P. L. 110-233*, Title I, § 101(e), *122 Stat. 886*; Dec. 23, 2008, *P. L. 110-458*, Title I, Subtitle A, §§ 101(c)(1)(H), 102(b)(1)(H), (I), *122 Stat. 5097*, 5101; Feb. 4, 2009, *P. L. 111-3*, Title III, Subtitle B, § 311(b)(1)(E), *123 Stat. 70*; April 7, 2014, *P. L. 113-97*, Title I, § 102(b)(6), *128 Stat. 1117*; Dec. 16, 2014, *P. L. 113-235*, Div O, Title I, Subtitle A, § 111(d), *128 Stat. 2793*.

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29 USCS § 1344

Current through Public Law 116-68, approved November 8, 2019.

United States Code Service > TITLE 29. LABOR (Chs. 1 — 32) > CHAPTER 18. EMPLOYEE RETIREMENT INCOME SECURITY PROGRAM (§§ 1001 — 1461) > PLAN TERMINATION INSURANCE (§§ 1301 — 1461) > TERMINATIONS (§§ 1341 — 1350)

§ 1344. Allocation of assets

(a) Order of priority of participants and beneficiaries. In the case of the termination of a single-employer plan, the plan administrator shall allocate the assets of the plan (available to provide benefits) among the participants and beneficiaries of the plan in the following order:

(1) First, to that portion of each individual's accrued benefit which is derived from the participant's contributions to the plan which were not mandatory contributions.

(2) Second, to that portion of each individual's accrued benefit which is derived from the participant's mandatory contributions.

(3) Third, in the case of benefits payable as an annuity—

(A)in the case of the benefit of a participant or beneficiary which was in pay status as of the beginning of the 3-year period ending on the termination date of the plan, to each such benefit, based on the provisions of the plan (as in effect during the 5-year period ending on such date) under which such benefit would be the least,

(B)in the case of a participant's or beneficiary's benefit (other than a benefit described in subparagraph (A)) which would have been in pay status as of the beginning of such 3-year period if the participant had retired prior to the beginning of the 3-year period and if his benefits had commenced (in the normal form of annuity under the plan) as of the beginning of such period, to each such benefit based on the provisions of the plan (as in effect during the 5-year period ending on such date) under which such benefit would be the least.

For purposes of subparagraph (A), the lowest benefit in pay status during a 3-year period shall be considered the benefit in pay status for such period.

(4) Fourth—

(A)to all other benefits (if any) of individuals under the plan guaranteed under this title (determined without regard to section 4022B(a) [*29 USCS § 1322b(a)*]), and

(B)to the additional benefits (if any) which would be determined under subparagraph (A) if section 4022(b)(5)(B) [*29 USCS § 1322(b)(5)(B)*] did not apply.

For purposes of this paragraph, section 4021 [*29 USCS § 1321*] shall be applied without regard to subsection (c) thereof.

(5) Fifth, to all other nonforfeitable benefits under the plan.

(6) Sixth, to all other benefits under the plan.

(b) Adjustment of allocations; reallocations; mandatory contributions; establishment of subclasses and categories. For purposes of subsection (a)—

(1) The amount allocated under any paragraph of subsection (a) with respect to any benefit shall be properly adjusted for any allocation of assets with respect to that benefit under a prior paragraph of subsection (a).

(2) If the assets available for allocation under any paragraph of subsection (a) (other than paragraphs (4), (5), and (6)) are insufficient to satisfy in full the benefits of all individuals which are described in that paragraph, the assets shall be allocated pro rata among such individuals on the basis of the present value (as of the termination date) of their respective benefits described in that paragraph.

(3) If assets available for allocation under paragraph (4) of subsection (a) are insufficient to satisfy in full the benefits of all individuals who are described in that paragraph, the assets shall be allocated first to benefits described in subparagraph (A) of that paragraph. Any remaining assets shall then be allocated to benefits described in subparagraph (B) of that paragraph. If assets allocated to such subparagraph (B) are insufficient to satisfy in full the benefits described in that subparagraph, the assets shall be allocated pro rata among individuals on the basis of the present value (as of the termination date) of their respective benefits described in that subparagraph.

(4) This paragraph applies if the assets available for allocation under paragraph (5) of subsection (a) are not sufficient to satisfy in full the benefits of individuals described in that paragraph.

(A) If this paragraph applies, except as provided in subparagraph (B), the assets shall be allocated to the benefits of individuals described in such paragraph (5) on the basis of the benefits of individuals which would have been described in such paragraph (5) under the plan as in effect at the beginning of the 5-year period ending on the date of plan termination.

(B) If the assets available for allocation under subparagraph (A) are sufficient to satisfy in full the benefits described in such subparagraph (without regard to this subparagraph), then for purposes of subparagraph (A), benefits of individuals described in such subparagraph shall be determined on the basis of the plan as amended by the most recent plan amendment effective during such 5-year period under which the assets available for allocation are sufficient to satisfy in full the benefits of individuals described in subparagraph (A) and any assets remaining to be allocated under such subparagraph shall be allocated under subparagraph (A) on the basis of the plan as amended by the next succeeding plan amendment effective during such period.

(5) If the Secretary of the Treasury determines that the allocation made pursuant to this section (without regard to this paragraph) results in discrimination prohibited by *section 401(a)(4) of the Internal Revenue Code of 1986* [*26 USCS § 401(a)(4)*] then, if required to prevent the disqualification of the plan (or any trust under the plan) under section 401(a) or 403(a) of such Code [*26 USCS § 401(a)* or *403(a)*], the assets allocated under subsections (a)(4)(B), (a)(5), and (a)(6) shall be reallocated to the extent necessary to avoid such discrimination.

(6) The term “mandatory contributions” means amounts contributed to the plan by a participant which are required as a condition of employment, as a condition of participation in such plan, or as a condition of obtaining benefits under the plan attributable to employer contributions. For this purpose, the total amount of mandatory contributions of a participant is the amount of such contributions reduced (but not below zero) by the sum of the amounts paid or distributed to him under the plan before its termination.

(7)A plan may establish subclasses and categories within the classes described in paragraphs (1) through (6) of subsection (a) in accordance with regulations prescribed by the corporation.

(c) Increase or decrease in value of assets. Any increase or decrease in the value of the assets of a single-employer plan occurring during the period beginning on the later of (1) the date a trustee is appointed under section 4042(b) [*29 USCS § 1342(b)*] or (2) the date on which the plan is terminated is to be allocated between the plan and the corporation in the manner determined by the court (in the case of a court-appointed trustee) or as agreed upon by the corporation and the plan administrator in any other case. Any increase or decrease in the value of the assets of a single-employer plan occurring after the date on which the plan is terminated shall be credited to, or suffered by, the corporation.

(d) Distribution of residual assets; restrictions on reversions pursuant to recently amended plans; assets attributable to employee contributions; calculation of remaining assets.

(1) Subject to paragraph (3), any residual assets of a single-employer plan may be distributed to the employer if—

(A)all liabilities of the plan to participants and their beneficiaries have been satisfied,

(B)the distribution does not contravene any provision of law, and

(C)the plan provides for such a distribution in these circumstances.

(2)

(A) In determining the extent to which a plan provides for the distribution of plan assets to the employer for purposes of paragraph (1)(C), any such provision, and any amendment increasing the amount which may be distributed to the employer, shall not be treated as effective before the end of the fifth calendar year following the date of the adoption of such provision or amendment.

(B)A distribution to the employer from a plan shall not be treated as failing to satisfy the requirements of this paragraph if the plan has been in effect for fewer than 5 years and the plan has provided for such a distribution since the effective date of the plan.

(C) Except as otherwise provided in regulations of the Secretary of the Treasury, in any case in which a transaction described in section 208 [*29 USCS § 1058*] occurs, subparagraph (A) shall continue to apply separately with respect to the amount of any assets transferred in such transaction.

(D) For purposes of this subsection, the term "employer" includes any member of the controlled group of which the employer is a member. For purposes of the preceding sentence, the term "controlled group" means any group treated as a single employer under subsection (b), (c), (m) or (o) of *section 414 of the Internal Revenue Code of 1986* [*26 USCS § 414(b)*, (c), (m) or (o)].

(3)

(A) Before any distribution from a plan pursuant to paragraph (1), if any assets of the plan attributable to employee contributions remain after satisfaction of all liabilities described in subsection (a), such remaining assets shall be equitably distributed to the participants who made such contributions or their beneficiaries (including alternate payees, within the meaning of section 206(d)(3)(K) [*29 USCS § 1056(d)(3)(K)*]).

(B) For purposes of subparagraph (A), the portion of the remaining assets which are attributable to employee contributions shall be an amount equal to the product derived by multiplying—

(i)the market value of the total remaining assets, by

(ii)a fraction—

(I)the numerator of which is the present value of all portions of the accrued benefits with respect to participants which are derived from participants' mandatory contributions (referred to in subsection (a)(2)), and

(II)the denominator of which is the present value of all benefits with respect to which assets are allocated under paragraphs (2) through (6) of subsection (a).

(C) For purposes of this paragraph, each person who is, as of the termination date—

(i)a participant under the plan, or

(ii)an individual who has received, during the 3-year period ending with the termination date, a distribution from the plan of such individual's entire nonforfeitable benefit in the form of a single sum distribution in accordance with section 203(e) [*29 USCS § 1053(e)*] or in the form of irrevocable commitments purchased by the plan from an insurer to provide such nonforfeitable benefit,

shall be treated as a participant with respect to the termination, if all or part of the nonforfeitable benefit with respect to such person is or was attributable to participants' mandatory contributions (referred to in subsection (a)(2)).

(4) Nothing in this subsection shall be construed to limit the requirements of *section 4980(d) of the Internal Revenue Code of 1986* [*26 USCS § 4980(d)*] (as in effect immediately after the enactment of the Omnibus Budget Reconciliation Act of 1990 [enacted Nov. 5, 1990]) or section 404(d) of this Act [*29 USCS § 1104(d)*] with respect to any distribution of residual assets of a single-employer plan to the employer.

(e) Bankruptcy filing substituted for termination date. If a contributing sponsor of a plan has filed or has had filed against such person a petition seeking liquidation or reorganization in a case under title 11, United States Code, or under any similar Federal law or law of a State or political subdivision, and the case has not been dismissed as of the termination date of the plan, then subsection (a)(3) shall be applied by treating the date such petition was filed as the termination date of the plan.

(f) Valuation of section 4062(c) liability for determining amounts payable by corporation to participants and beneficiaries.

(1) In general. In the case of a terminated plan, the value of the recovery of liability under section 4062(c) [*29 USCS § 1362(c)*] allocable as a plan asset under this section for purposes of determining the amount of benefits payable by the corporation shall be determined by multiplying—

(A)the amount of liability under section 4062(c) [*29 USCS § 1362(c)*] as of the termination date of the plan, by

(B)the applicable section 4062(c) [*29 USCS § 1362(c)*] recovery ratio.

(2) Section 4062(c) recovery ratio. For purposes of this subsection—

(A) In general. Except as provided in subparagraph (C), the term "section 4062(c) [*29 USCS § 1362(c)*] recovery ratio" means the ratio which—

(i)the sum of the values of all recoveries under section 4062(c) [*29 USCS § 1362(c)*] determined by the corporation in connection with plan terminations described under subparagraph (B), bears to

(ii)the sum of all the amounts of liability under section 4062(c) [*29 USCS § 1362(c)*] with respect to such plans as of the termination date in connection with any such prior termination.

(B) Prior terminations. A plan termination described in this subparagraph is a termination with respect to which—

(i)the value of recoveries under section 4062(c) [*29 USCS § 1362(c)*] have been determined by the corporation, and

(ii)notices of intent to terminate were provided (or in the case of a termination by the corporation, a notice of determination under section 4042 [*29 USCS § 1342*] was issued) during the 5-Federal fiscal year period ending with the third fiscal year preceding the fiscal year in which occurs the date of the notice of intent to terminate (or the notice of determination under section 4042 [*29 USCS § 1342*]) with respect to the plan termination for which the recovery ratio is being determined.

(C) Exception. In the case of a terminated plan with respect to which the outstanding amount of benefit liabilities exceeds $20,000,000, the term "section 4062(c) recovery ratio" means, with respect to the termination of such plan, the ratio of—

(i)the value of the recoveries on behalf of the plan under section 4062(c) [*29 USCS § 1362(c)*], to

(ii)the amount of the liability owed under section 4062(c) [*29 USCS § 1362(c)*] as of the date of plan termination to the trustee appointed under section 4042 (b) or (c) [*29 USCS § 1342(b)* or (c)].

(3) Subsection not to apply. This subsection shall not apply with respect to the determination of—

(A)whether the amount of outstanding benefit liabilities exceeds $20,000,000, or

(B)the amount of any liability under section 4062 [*29 USCS § 1362(c)*] to the corporation or the trustee appointed under section 4042 (b) or (c) [*29 USCS § 1342(c)*].

(4) Determinations. Determinations under this subsection shall be made by the corporation. Such determinations shall be binding unless shown by clear and convincing evidence to be unreasonable.

History

HISTORY:

Act Sept. 2, 1974, *P. L. 93-406*, Title IV, Subtitle C, § 4044, *88 Stat. 1025*.; Sept. 26, 1980, *P. L. 96-364*, Title IV, § 402(a)(7), *94 Stat. 1299*; April 7, 1986, *P. L. 99-272*, Title XI, § 11016(c)(12), (13), *100 Stat. 274*; Dec. 22, 1987, *P. L. 100-203*, Title IX, Subtitle D, Part II, Subpart B, § 9311(a)(1), (b), (c), *101 Stat. 1330*-359, 1330-360; Dec. 19, 1989, *P. L. 101-239*, Title VII, Subtitle G, Part V, Subpart C, § 7881(e)(3), Subpart D, §§ 7891(a)(1), 7894(g)(2), *103 Stat. 2440*, 2445, 2451; Nov. 5, 1990, *P. L. 101-508*, Title XII, Subtitle A, § 12002(b)(2)(B), *104 Stat. 1388*-566; Aug. 17, 2006, *P. L. 109-280*, Title IV, §§ 404(b), 407(b), 408(b)(2), *120 Stat. 928*, 930, 931; Dec. 23, 2008, *P. L. 110-458*, Title I, Subtitle A, § 104(c), *122 Stat. 5104*.

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NY CLS CPLR R 3222

Current through 2019 released Chapters 1-491

New York Consolidated Laws Service > Civil Practice Law And Rules (Arts. 1 — 100) > Article 32 Accelerated Judgment (§§ 3201 — 3222)

R 3222. Action on submitted facts

(a) Commencement. An action, except a matrimonial action, may be commenced by filing with the clerk a submission of the controversy, acknowledged by all parties in the form required to entitle a deed to be recorded. The submission shall consist of a case, containing a statement of the facts upon which the controversy depends, and a statement that the controversy is real and that the submission is made in good faith for the purpose of determining the rights of the parties. If made to the supreme court, the submission shall specify the particular county clerk with whom the papers are to be filed.

(b) Subsequent Proceedings. Subsequent proceedings shall be had according to the civil practice law and rules except that:

1.an order of attachment or a preliminary injunction shall not be granted;

2.the controversy shall be determined on the case alone;

3.if the submission is made to the supreme court, it shall be heard and determined either by the court, or by the appellate division, or, with his consent, by a specified judge or referee, as the parties may stipulate;

4.on such a submission the court, judge or referee may find facts by inference from the facts stipulated; and

5.if the statement of facts in the case is not sufficient to enable the court to enter judgment the submission shall be dismissed or the court shall allow the filing of an additional statement.

History

Add, L 1962, ch 308, eff Sept 1, 1963; amd, L 1984, ch 313, § 1, eff July 3, 1984; L 1986, ch 355, § 9, eff July 17, 1986.

End of Document

1971 IRB LEXIS 501

US Internal Revenue Service

January 1971

Rev. Rul. 71-2331971-1 C.B. 113

Reporter
1971 IRB LEXIS 501 *; Rev. Rul. 71-233; 1971-1 C.B. 113

Revenue Ruling 71-233

Subject Matter

Section 368.-Definitions Relating to Corporate Reorganizations

Applicable Sections

26 CFR 1.368-1: Purpose and scope of exception of reorganization exchanges. (Also Sections 354, 381; 1.354-1, 1.381 (c) (22)-1.)

[*1]

Core Terms

policy-holders, proprietary interest, life insurance company, merger, preferred stock, reorganization, insurance company, state law, acquiring, insurance contract, mutual life, earnings, reserves, profits, zero, continuity of interest, contractual right, the will, outstanding, provisions, transferor, surplus, newly, stock

Text

A merger of a mutual life insurance company into a newly organized stock life insurance company under state law, whereby policy-holders exchange their proprietary interests for preferred stock, is a reorganization under section 368 (a) (1) (A) of the Code.

Advice has been requested with respect to the Federal income tax consequences of the merger of a mutual life insurance company into a stock life insurance company under the circumstances described below.

Corporation *X* is a mutual life insurance company with no excess of gain from operations over taxable investment income. It is subject to tax imposed by section 802 of the Internal Revenue Code of 1954. Pursuant to a plan of reorganization, *X* will be merged under state law into corporation *Y* , a newly organized life insurance company taxable under section 802 of the Code.

Y will acquire all of the assets, subject to all of the liabilities of *X,* including all liabilities under the outstanding insurance policies issued by *X.* Consequently, the contractual **[*2]** rights of the policyholders of *X* with respect to their outstanding insurance contracts will be unaffected by the merger except that *Y* will become the insurer of such contracts.

Upon consummation of the merger, Y corporation will issue solely all of its four percent nonvoting cumulative preferred stock to the policyholders of *X* in exchange for their proprietary interests in its assets. Since both participating and nonparticipating policy-holders of *X* are the owners of the assets of *X,* both will be entitled to receive preferred stock of Y on the exchange, and none will receive less than one share.

By operation of state law all of the policyholders of a mutual insurance company have a dual legal relationship to the company: (1) as members of a membership corporation they have proprietary interests, and (2) as policy-holders they possess the contractual rights provided for in their insurance contracts. See, for example, *Duffy v. Mutual Benefit Life Insurance Co., 272 U.S. 613, 71 L. Ed. 439, 47 S. Ct. 205, 1927-1 C.B. 278, T.D. 3959 (1926)*, T.D. 3959, C.B. VI-1, 278 (1927), *Ohio State Life Insurance Co. v. Clark, 274 F. 2d 771, 83 Ohio Law Abs. 166 (1960)*; *State v. Willett, 171 Ind. 296, 86 N.E. 68*. **[*3]** *171 Ind. 296, 86 N.E. 68 (1908)*. See also *section 7701 (a) (7)* and *section 7701 (a) (8) of the Code*.

Payment by each policyholder of the premiums called for by the insurance contracts issued by *X* represents payment for the cost of insurance and an investment in his contract but not an investment in the assets of *X.* His proprietary interest in the assets of *X* arises solely by virtue of the fact that he is a policyholder of *X.* Therefore, the basis of each policyholder's proprietary interest in *X* is zero.

Section 368 (a) (1) (A) of the Code defines the term "reorganization" as a statutory merger or consolidation. However, an otherwise qualified transaction does not constitute a reorganization within the meaning of the Code unless the continuity of interest requirement of *section 1.368-1 (b) of the Income Tax Regulations* is satisfied.

In the instant case, since the policy-holders of *X* received solely preferred stock of Y in exchange for their proprietary interest in *X,* the continuity of interest requirement is met.

Accordingly the merger of *X* into *Y* in compliance with state law is a reorganization under *section 368 (a) (1) (A) of the Code*. Both *X* and Y will be parties to the reorganization **[*4]** pursuant to *section 368 (b) of the Code*. No gain or loss will be recognized to either *X* or Y because of the application of *sections 361 (a)* and *1032 (a) of the Code*. No gain or loss will be recognized to the policyholder-members of *X* upon the exchange of their proprietary interests in *X* for the preferred stock of *Y* pursuant to *section 354 (a) (1) of the Code*. Pursuant to the provisions of *section 358 (a) of the Code*, each policyholder will have a zero basis in the preferred stock issued to him by *Y* since the basis in his proprietary interest exchanged therefor was zero.

The instant transaction is one to which *section 381 (c) of the Code* applies. Pursuant to *section 381 (c) (22) of the Code* and section 1.381 (c) (22)-1 of the Income Tax Regulations, the acquiring life insurance company is required to take into account the appropriate items that the transferor was required to take into account for purposes of part I, subchapter L, chapter 1 of the Code. The acquiring life insurance company also is required to take into account the items described in paragraphs (2) through (21), other than paragraphs (14), (15), and (17) of *section 381 (c) of the Code*. For example, the acquiring life insurance **[*5]** company must take into account the reserves described in *section 810 (c) of the Code* transferred to it as of the close of the date of transfer by the transferor life insurance company in accordance with the provisions of *section 381 (c) (4) of the Code* and the regulations thereunder.

Further, consistent with *section 806 (a) of the Code* the mean of such reserves and the mean of the assets will be appropriately adjusted on a daily basis to reflect the amounts involved in the transfer.

The earnings and profits of *X* will, pursuant to *section 381 (c) (2) of the Code*, carry over and be added to the earnings and profits of Y. The accumulated earnings and profits of *X* at the date of the merger will be not less than the amount of its total surplus, including the mandatory securities valuation reserve and any other surplus reserves on that date.

Load Date: 2005-08-12

NY CLS Ins § 1211

Current through 2019 released Chapters 1-491

New York Consolidated Laws Service > Insurance Law (Arts. 1 — 99) > Article 12 Organization and Corporate Procedure (§§ 1201 — 1221)

§ 1211. Mutual insurance corporations; membership and dividends

(a) Every domestic mutual insurance corporation shall be organized, maintained and operated for the benefit of its members as a non-stock corporation. Every policyholder shall be a member of such corporation and shall, except as provided in subsection (d) hereof, be entitled to vote at any regular or special meeting of such corporation, to notice thereof pursuant to the by-laws and to share equitably in dividends declared by the board of directors. The board of directors may, subject to limitations in this chapter, from time to time declare a dividend from the corporation's surplus. No dividend shall be declared or paid if thereby the company's minimum or other required surplus will be impaired. In declaring and paying any dividend the board of directors may make reasonable classifications of policies, and shall declare and pay such dividend in a manner that is fair and equitable to the policyholders. Unless otherwise provided in the corporation's charter or by-laws, each member shall be entitled to one vote at any regular or special meeting. The charter or by-laws may, with the approval of the superintendent, provide for distribution of voting power among members on the basis of the amount of insurance held, number of policies held, amount of premiums paid by them or on any other basis the superintendent finds fair and equitable.

(b)A member of any such corporation may vote at any such meeting in person or by proxy. No proxy or power of attorney given by him, to vote at any meeting of such corporation, shall be valid or effective after the next meeting. No person shall directly or indirectly sell or purchase, or offer to sell or purchase, any proxy or power of attorney to vote at any such meeting, nor shall any person directly or indirectly give or receive, or offer to give or receive, any proxy or power of attorney to vote at any such meeting as an inducement to the negotiation or making of a contract of insurance or any renewal thereof, to the settlement of any claim thereunder, or to any other act relating thereto.

(c) All corporations, their directors and representatives and all persons, firms or corporations holding property in trust may insure the same in mutual insurance corporations and by so doing such directors, representatives or trustees, in their representative capacity, may assume the liabilities and be entitled to the rights of a member of such insurer, but shall not be personally liable as individuals upon such contract of insurance.

(d) The provisions of this section as to members' voting rights and the election of directors shall not apply to any domestic mutual life insurance company governed by the provisions of section four thousand two hundred ten of this chapter, nor shall they require any such company to hold a meeting of its members.

(e) As to any surety or fidelity bond or like obligation executed by a mutual property/casualty insurance company as a surety or guarantor, the principal, and not the obligee, shall be a member of such corporation.

History

Add, L 1984, ch 367, § 1, eff Sept 1, 1984.

End of Document

NY CLS Ins § 7307

Current through 2019 released Chapters 1-491

New York Consolidated Laws Service* > *Insurance Law (Arts. 1 — 99)* > *Article 73 Conversion to Different Type of Insurer (§§ 7301 — 7317)

§ 7307. Conversion of domestic mutual property/casualty insurance companies or advance premium corporations into domestic stock property/casualty insurance companies; insurers not in rehabilitation

(a) In this article:

(1)"Affiliate" of a mutual insurer means any person who controls, is controlled by or is under common control with, the mutual insurer being converted. A corporation is an affiliate of another corporation, regardless of ownership, if substantially the same group of persons manage the two corporations.

(2)"Control" has the meaning assigned to it in paragraph two of subsection (a) of section one thousand five hundred one of this chapter.

(3)A "domestic mutual insurer" or "mutual insurer" means a domestic mutual property/casualty insurance company organized under article twelve of this chapter and licensed under article forty-one of this chapter, or a domestic advance premium corporation organized and licensed under article sixty-six of this chapter, in either case authorized to issue non-assessable policies only and not operating under an order of rehabilitation.

(4)A "holder of a section 1307 agreement" means the holder of an agreement executed pursuant to section one thousand three hundred seven of this chapter.

(b)A domestic mutual insurer may apply to the superintendent for permission to convert into a domestic stock property/casualty insurer complying with the relevant organization and licensing provisions of articles twelve and forty-one of this chapter. The application to the superintendent shall be pursuant to a resolution, adopted by no less than a majority of the entire board of directors, specifying the reasons for and the purposes of the proposed conversion, and the manner in which the conversion is expected to benefit policyholders and the public. A copy of the resolution, together with a statement of its adoption, both certified by the president and secretary, or officers corresponding to either of them, and affirmed by them as true under the penalties of perjury and under the seal of the mutual insurer, shall accompany the application. The superintendent may thereafter request any additional documents and information which he may reasonably require. Unless the superintendent finds that:

(1)the resolution is defective upon its face;

(2)the proposed conversion is contrary to law or is not in the best interests of the policyholders or the public; or

(3)the mutual insurer does not have a surplus to policyholders at least equal to the minimum capital and surplus required to be maintained for a newly organized stock insurer doing the same kinds of insurance, in which cases the proposed conversion shall terminate, the superintendent shall order an examination of the mutual insurer pursuant to section three hundred ten of this chapter as of the last day of the period covered in its latest filed statement. The superintendent may also examine any affiliate of the mutual insurer.

(c) The superintendent shall also appoint one or more qualified disinterested persons to appraise and report to the superintendent the fair market value of the mutual insurer and, to the extent necessary, its affiliates, on the basis of its latest filed annual or quarterly statement, and of any significant subsequent developments. Such persons shall consider the assets and liabilities of the mutual insurer and any factors bearing on the value of the mutual insurer or its affiliates. The appraisers shall receive reasonable compensation and be reimbursed for reasonable expenses incurred in discharging their duties. They may, as necessary, employ consultants to advise them on any technical matters.

(d) The superintendent shall make copies of such examination report and appraisal report available to the board of directors within fifteen days of his receipt of the reports. After receiving such reports the superintendent may grant or deny permission to the board of directors to submit to him a plan of conversion. If permission is granted, the plan shall include the provisions, and be submitted in the manner and under the conditions, required by subsection (e) hereof. If permission is denied, the superintendent shall make a written statement of his findings and the board shall have the right to a hearing before the superintendent within thirty days of the date of denial.

(e) Such plan shall be adopted by a majority of the entire board. It shall be signed by the president and attested by the secretary, or officers corresponding to either of them, under the corporate seal of the insurer. A copy of the plan and resolution, both certified by such officers as true under the penalties of perjury and under the seal of the insurer, shall be submitted to the superintendent not later than forty-five days after permission was granted under subsection (d) hereof. The plan shall include:

(1) The proposed charter and by-laws of the insurer as a stock corporation set out in accordance with paragraph five of subsection (a) of section one thousand two hundred one of this chapter.

(2) The manner of treating a holder of a section 1307 agreement, if any; such holder, if otherwise qualified, may, at its option, exchange such agreement for an equitable share of the securities or other consideration, or both, of the corporation into which the insurer is to be converted.

(3) The manner and basis of exchanging the equitable share of each eligible mutual policyholder for securities or other consideration, or both, of the stock corporation into which the mutual insurer is to be converted and the disposition of any unclaimed shares. The plan shall also provide that each person who had a policy of insurance in effect at any time during the three year period immediately preceding the date of adoption of the resolution described in subsection (b) hereof shall be entitled to receive in exchange for such equitable share, without additional payment, consideration payable in voting common shares of the insurer or other consideration, or both. The equitable share of the policyholder in the mutual insurer shall be determined by the ratio which the net premiums (gross premiums less return premiums and dividend paid) such policyholder has properly and timely paid to the insurer on insurance policies in effect during the three years immediately preceding the adoption of the resolution by the board of directors under subsection (b) hereof bears to the total net premiums received by the mutual insurer from such eligible policyholders. In computing a policyholder’s equitable share, no credit shall be given for any net premiums which result from an endorsement which is effective on or after the date of adoption of the resolution; except that credit shall be given for any net premiums resulting from an audit or retrospective premium adjustment which is billed within one hundred eighty days after such date, provided such premium is paid timely. If the equitable share of the eligible policyholder entitles such policyholder to the purchase of a fractional share of stock, the policyholder shall have the option to receive the value of the fractional share in cash or purchase a full share by paying the balance in cash.

(4) The number of voting common shares proposed to be authorized for the stock corporation, their par value and the price at which they shall be offered, which price may not exceed one-half of the median equitable share of all policyholders under paragraph three hereof.

(5) Any other features requested by the superintendent.

(f) Prompt notice shall be given by the mutual insurer to all persons who become policyholders or holders of section 1307 agreements on or after the date of the adoption of the resolution described in subsection (b) hereof, of the pendency of a proposed conversion and of the effect thereof on them.

(g) The superintendent shall hold a public hearing, adequate notice of which shall be mailed by the mutual insurer to each person who was a policyholder on the day preceding the date of adoption of the resolution described in subsection (b) hereof, accompanied by a copy of the plan of conversion and any comment the superintendent considers necessary for the adequate information of the policyholders. In addition, the insurer shall give notice of the hearing by publication in a newspaper of general circulation in the county in which the insurer has its principal office and in the two largest cities in each state in which the insurer has underwritten insurance within the five years preceding the date of the adoption of the resolution described in subsection (b) hereof; such notice shall be accompanied by a summary approved by the superintendent of the plan and any comment the superintendent considers necessary for the adequate information of former policyholders and the public.

(h)

> **(1)**After the hearing the superintendent shall approve the plan as submitted, refuse to approve the plan, or request modification of the plan before granting approval. If the superintendent finds that the plan does not violate this chapter, is not inconsistent with law, is fair and equitable and is in the best interests of the policyholders and the public, he shall approve such plan. If the superintendent finds that the plan does not meet the foregoing standards for approval he shall either refuse to approve the plan and the plan shall become null and void or return the plan to the mutual insurer for modification to meet his stated objections.
>
> **(2)**If within ninety days after receipt of the superintendent's request for modifications the insurer submits an amended plan which meets the superintendent's objections and complies with the standards for approval he shall approve such amended plan.

(i) After approval by the superintendent the plan shall be submitted to a vote of the persons who were policyholders of the mutual insurer on the day preceding the date of adoption of the resolution described in subsection (b) hereof. The plan shall provide for proxy voting in a manner to be prescribed by the superintendent. The board shall submit the question of the plan to such policyholders at a meeting thereof, by causing a full, true and correct copy or a summary thereof approved by the superintendent, together with notice, stating the time, place and purpose of such meeting, to be delivered personally, or deposited in the post office, postage prepaid, at least thirty days (unless a shorter time, not less than ten days, be approved by the superintendent) prior to the time fixed for such meeting, addressed to each such policyholder at his last post office address appearing on the records of the insurer.

(j) Each such policyholder eligible to vote pursuant to subsection (i) hereof shall be entitled to such number of votes as may be provided for in the by-laws of the mutual insurer. The votes of two-thirds of all the votes cast by policyholders represented at the meeting in person or by proxy, shall be necessary for the adoption of the plan. Upon the conclusion of the vote the insurer shall submit to the superintendent a certified copy of the plan voted on together with a certificate setting forth the results of the vote, both of which shall be subscribed by the president and attested by the secretary, or officers corresponding to either of them, under the corporate seal of the insurer, and affirmed by them as true under the penalties of perjury.

(k) No domestic mutual insurer which is affiliated with other mutual companies may be converted to a stock company unless all such affiliated companies are converted to stock companies at the same time, except to the extent the superintendent may determine that the interests of the policyholders of any of the other mutual companies can be permanently protected by limitations on the corporate powers of the stock corporation or on its authority to do business.

(l) If at any stage in the process of a conversion under this section the superintendent finds that the mutual insurer is impaired or that the further transaction of business will be hazardous to its policyholders, its creditors, or the public, the proposed conversion shall terminate.

(m) If the conversion plan is adopted pursuant to subsection (j) hereof, the superintendent, upon being satisfied that the insurer will have at least the minimum capital and surplus required to be maintained for a newly organized domestic stock insurer doing the same kinds of insurance, shall issue a new certificate of authority to the insurer, thereby converting the mutual insurer into a stock insurer. At the same time, the superintendent may issue such license as may be required pursuant to section one thousand two hundred four of this chapter.

(n) Upon such conversion, the stock insurer shall give notice thereof by publication in a newspaper of general circulation in the county in which the insurer has its principal office and in the two largest cities in each state in which the insurer shall be licensed to do business. The notice shall include a correct copy of the plan, or a summary thereof approved by the superintendent.

(o) Upon the conversion of the mutual insurer in the manner herein provided, all the rights, franchises and interests of the former mutual insurer, in and to every species of property, real, personal and mixed, and things in action thereunto belonging, shall be deemed as transferred to and vested in the stock insurer, without any other deed or transfer; and simultaneously therewith such company shall be deemed to have assumed all of the obligations and liabilities of the former mutual insurer.

(p) No action or proceeding, pending at the time of the conversion to which the mutual insurer may be a party shall be abated or discontinued by reason of such conversion, but the same may be prosecuted to final judgment in the same manner as if the conversion had not taken place, or the stock corporation may be substituted in place of such mutual insurer by order of the court in which the action or proceeding may be pending.

(q) The directors and officers of the mutual insurer shall serve until new directors and officers have been duly elected and qualified pursuant to the charter and by-laws of the stock insurer.

(r) The insurer, whether before or after conversion, shall pay no compensation of any kind to any person other than regular salaries to existing personnel, in connection with the proposed conversion, other than for clerical and mailing expenses, except that, with the superintendent’s approval, payment may be made at reasonable rates for printing costs, and for legal and other professional fees for services actually rendered. All expenses of the conversion, including the expenses incurred by the department of financial services, shall be borne by the insurer.

(s) No voting common shares shall be subscribed by or issued to persons other than eligible policyholders or holders of section 1307 agreements until all subscriptions by such policyholders or agreement holders have been filled or other consideration has been provided in accordance with the plan. Thereafter, any new issue of common shares within three years after the conversion shall first be offered to the persons who have become voting common shareholders, pursuant to subsection (e) hereof in proportion to their holdings of such shares.

(t) No insurer becoming a domestic stock insurer under the provisions of this section shall: for a period of ten years after conversion, redomesticate directly or indirectly or remove its principal offices from within the state; or for a period of five years after conversion:

> **(1)**enter into any agreement by the terms of which any person, partnership or corporation agrees to pay all or a portion of the expenses of management of the insurer in consideration of the insurer’s agreement to pay him or it either commissions on premiums due the insurer or any other compensation for his or its services, or
>
> **(2)**enter into any agreement with an officer or director of the insurer or with any firm or corporation in which any officer or director of the insurer is pecuniarily interested, directly or indirectly, under which agreement the insurer agrees to pay, for the acquisition of business, any commissions or other compensation which by the terms of such agreement varies with the amount of such business or with the earnings of the insurer on such business.

(u) Any action taken pursuant to the provisions of this section shall in no way impede or impair the exercise by the superintendent of his authority under any other provision of this chapter.

History

Add, L 1984, ch 367, § 1, eff Sept 1, 1984; amd, L 1984, ch 805, § 168, eff Sept 1, 1984; *L 2011, ch 62, § 104* (Part A), eff Oct 3, 2011.

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