UNITED STATES DISTRICT COURT

DISTRICT OF NEVADA

GOLDMAN, SACHS & CO.,

Plaintiff,

vs.

CITY OF RENO,

Defendant.

3:12-cv-00327-RCJ-WGC

ORDER

This case arises out of an alleged breach of fiduciary duty in connection with Defendant City of Reno's ("Reno") issuance of approximately $211 million in complex securities in order to fund various city projects in 2005 and 2006. Pending before the Court are Reno's motion to dismiss counterclaim-in-reply (ECF No. 91), Plaintiff Goldman, Sachs & Co.'s ("Goldman") cross-motion for summary judgment (ECF No. 108), and Reno's motion to disqualify Goldman's counsel (ECF No. 120). For the reasons given herein, the Court grants the motion to dismiss and denies the other motions.

I. FACTS AND PROCEDURAL BACKGROUND

In October 2005, Reno issued $73.45 million in auction rate securities ("ARS"), in order to fund various city projects, to be underwritten and brokered by Goldman pursuant to an October 19, 2005 agreement (the "2005 Underwriter Agreement") and an October 26, 2005 agreement (the "2005 Broker–Dealer Agreement"). (Compl. ¶¶ 12–13, June 18, 2012, ECF No.

1). The 2005 Broker-Dealer Agreement contains a forum selection clause, designating the District of Nevada as the required forum for all "actions and proceedings arising out of this Broker-Dealer Agreement or any of the transactions contemplated hereby," as well as a merger clause. (*See* 2005 Broker–Dealer Agreement §§ 5.04, 5.09, ECF No. 1-6 at 16–17.)

In May 2006, Reno and Goldman entered into substantially identical agreements (the "2006 Underwriter Agreement" and the "2006 Broker-Dealer Agreement") when Reno issued an additional $137.43 million in ARS for similar purposes. Neither the 2005 nor the 2006 Broker–Dealer Agreement contains an arbitration clause, and neither Underwriter Agreement contains either a forum selection or arbitration clause.

On February 10, 2012, Reno filed a claim against Goldman with the Financial Industry Regulatory Authority ("FINRA"), alleging wrongdoing with respect to the 2005 and 2006 agreements. (Compl. ¶¶ 27–29). Goldman then sued Reno in this Court, seeking a declaratory judgment that FINRA was an inappropriate forum for Reno's claims based on the mandatory forum selection clauses in the Broker–Dealer Agreements, and that claims arising out of those Agreements may only be heard in this District.

On November 26, 2012, the Court denied Goldman's motion for a preliminary injunction of the FINRA arbitration proceedings. The Court concluded that Reno was entitled to arbitration under the FINRA Rules, and that the forum selection clauses in the 2005 and 2006 Broker-Dealer Agreements did not supersede Reno's right to pursue FINRA arbitration. (*See* Order 5–8, ECF No. 41.) After stipulating to the entry of final judgment in Reno's favor, Goldman appealed to the Ninth Circuit, and the Court of Appeals reversed the Court's order and final judgment. (*See* Mem. Op., ECF No. 51.) The Court of Appeals stated:

> "[W]e will give full effect to the all-inclusive breadth of the forum selection clauses ('all actions and proceedings'), their mandatory nature ('shall'), and their reference to a judicial forum ('the United States District Court for the District of Nevada'). We therefore conclude that the forum selection clauses superseded

> Goldman's default obligation to arbitrate under the FINRA Rules and that, *by agreeing to these clauses, Reno disclaimed any right it might otherwise have had to the FINRA arbitration forum*."

(*Id.* at 26 (emphasis added).)

Following remand, Reno answered the Complaint filed in this action and asserted counterclaims against Goldman for breach of fiduciary duty, fraud, and negligent misrepresentation (three of the six claims Reno had previously asserted in the FINRA arbitration). (ECF No. 67.) Goldman then answered Reno's counterclaims and asserted a counterclaim-in-reply for contract damages based on Reno's alleged breach of the forum selection clauses in the 2005 and 2006 Broker-Dealer Agreements. (ECF No. 88.) Goldman alleges damages "in an amount equal to the costs and attorneys' fees [it] incurred as a result of Reno's breach of the forum selection clauses . . . ." (*Id.* at 22.)

The Court is now faced with three motions centered on Goldman's counterclaim-in-reply. First, Reno has moved to dismiss the counterclaim-in-reply on the basis that attorneys' fees and litigation costs are not proper elements of contract damages under the laws of New York, which adheres to the American Rule. In response, Goldman moved for summary judgment on the same issue, arguing that New York's intermediate appellate court has opined that awarding damages based on attorneys' fees in an action for breach of a forum selection clause does not contravene the American Rule. Lastly, Reno moved to disqualify Goldman's attorneys because they are "necessary witnesses" with respect to the damages element of Goldman's contract claim.

II. LEGAL STANDARDS

a. Dismissal for Failure to State a Claim

Federal Rule of Civil Procedure 8(a)(2) requires only "a short and plain statement of the claim showing that the pleader is entitled to relief" in order to "give the defendant fair notice of what the . . . claim is and the grounds upon which it rests." *Conley v. Gibson*, 355 U.S. 41, 47

(1957). Federal Rule of Civil Procedure 12(b)(6) mandates that a court dismiss a cause of action that fails to state a claim upon which relief can be granted. A motion to dismiss under Rule 12(b)(6) tests the complaint's sufficiency. *See N. Star Int'l v. Ariz. Corp. Comm'n*, 720 F.2d 578, 581 (9th Cir. 1983). When considering a motion to dismiss under Rule 12(b)(6) for failure to state a claim, dismissal is appropriate only when the complaint does not give the defendant fair notice of a legally cognizable claim and the grounds on which it rests. *See Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007). In considering whether the complaint is sufficient to state a claim, the court will take all material allegations as true and construe them in the light most favorable to the plaintiff. *See NL Indus., Inc. v. Kaplan*, 792 F.2d 896, 898 (9th Cir. 1986). The court, however, is not required to accept as true allegations that are merely conclusory, unwarranted deductions of fact, or unreasonable inferences. *See Sprewell v. Golden State Warriors*, 266 F.3d 979, 988 (9th Cir. 2001).

A formulaic recitation of a cause of action with conclusory allegations is not sufficient; a plaintiff must plead facts pertaining to his own case making a violation "plausible," not just "possible." *Ashcroft v. Iqbal*, 556 U.S. 662, 677–79 (2009) (citing *Twombly*, 550 U.S. at 556) ("A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged."). That is, under the modern interpretation of Rule 8(a), a plaintiff must not only specify or imply a cognizable cause of action (*Conley* review), but also must allege the facts of his case so that the court can determine whether the plaintiff has any basis for relief under the cause of action he has specified or implied, assuming the facts are as he alleges (*Twombly-Iqbal* review).

"Generally, a district court may not consider any material beyond the pleadings in ruling on a Rule 12(b)(6) motion. However, material which is properly submitted as part of the complaint may be considered on a motion to dismiss." *Hal Roach Studios, Inc. v. Richard Feiner*

& *Co.*, 896 F.2d 1542, 1555 n.19 (9th Cir. 1990) (citation omitted). Similarly, "documents whose contents are alleged in a complaint and whose authenticity no party questions, but which are not physically attached to the pleading, may be considered in ruling on a Rule 12(b)(6) motion to dismiss" without converting the motion to dismiss into a motion for summary judgment. *Branch v. Tunnell*, 14 F.3d 449, 454 (9th Cir. 1994). Moreover, under Federal Rule of Evidence 201, a court may take judicial notice of "matters of public record." *Mack v. S. Bay Beer Distribs., Inc.*, 798 F.2d 1279, 1282 (9th Cir. 1986). Otherwise, if the district court considers materials outside of the pleadings, the motion to dismiss is converted into a motion for summary judgment. *See Arpin v. Santa Clara Valley Transp. Agency*, 261 F.3d 912, 925 (9th Cir. 2001).

b. Summary Judgment

A court must grant summary judgment when "the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(a). Material facts are those which may affect the outcome of the case. *See Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). A dispute as to a material fact is genuine if there is sufficient evidence for a reasonable jury to return a verdict for the nonmoving party. *See id.* A principal purpose of summary judgment is "to isolate and dispose of factually unsupported claims." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323–24 (1986).

In determining summary judgment, a court uses a burden-shifting scheme. The moving party must first satisfy its initial burden. "When the party moving for summary judgment would bear the burden of proof at trial, it must come forward with evidence which would entitle it to a directed verdict if the evidence went uncontroverted at trial." *C.A.R. Transp. Brokerage Co. v. Darden Rests., Inc.*, 213 F.3d 474, 480 (9th Cir. 2000) (citation and internal quotation marks omitted). In contrast, when the nonmoving party bears the burden of proving the claim or

defense, the moving party can meet its burden in two ways: (1) by presenting evidence to negate an essential element of the nonmoving party's case; or (2) by demonstrating that the nonmoving party failed to make a showing sufficient to establish an element essential to that party's case on which that party will bear the burden of proof at trial. *See Celotex Corp.*, 477 U.S. at 323–24.

If the moving party fails to meet its initial burden, summary judgment must be denied and the court need not consider the nonmoving party's evidence. *See Adickes v. S.H. Kress & Co.*, 398 U.S. 144 (1970). If the moving party meets its initial burden, the burden then shifts to the opposing party to establish a genuine issue of material fact. *See Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986). To establish the existence of a factual dispute, the opposing party need not establish a material issue of fact conclusively in its favor. It is sufficient that "the claimed factual dispute be shown to require a jury or judge to resolve the parties' differing versions of the truth at trial." *T.W. Elec. Serv., Inc. v. Pac. Elec. Contractors Ass'n*, 809 F.2d 626, 631 (9th Cir. 1987). In other words, the nonmoving party cannot avoid summary judgment by relying solely on conclusory allegations unsupported by facts. *See Taylor v. List*, 880 F.2d 1040, 1045 (9th Cir. 1989). Instead, the opposition must go beyond the assertions and allegations of the pleadings and set forth specific facts by producing competent evidence that shows a genuine issue for trial. *See* Fed. R. Civ. P. 56(e); *Celotex Corp.*, 477 U.S. at 324.

At the summary judgment stage, a court's function is not to weigh the evidence and determine the truth, but to determine whether there is a genuine issue for trial. *See Anderson*, 477 U.S. at 249. The evidence of the nonmovant is "to be believed, and all justifiable inferences are to be drawn in his favor." *Id.* at 255. But if the evidence of the nonmoving party is merely colorable or is not significantly probative, summary judgment may be granted. *See id.* at 249–50. Notably, facts are only viewed in the light most favorable to the nonmoving party where there is

a genuine dispute about those facts. *Scott v. Harris*, 550 U.S. 372, 380 (2007). That is, even where the underlying claim contains a reasonableness test, where a party's evidence is so clearly contradicted by the record as a whole that no reasonable jury could believe it, "a court should not adopt that version of the facts for purposes of ruling on a motion for summary judgment." *Id.*

III. ANALYSIS

a. Reno's Initiation of FINRA Arbitration Was a Breach of the Broker-Dealer Agreement's Forum Selection Clause.

"To establish a breach of contract under New York law a plaintiff must prove the following elements: (i) the existence of a contract; (ii) breach by the other party; and (iii) damages suffered as a result of the breach." *Bear Stearns Inv. Prod., Inc. v. Hitachi Auto. Prod. (USA), Inc.*, 401 B.R. 598, 615 (S.D.N.Y. 2009). The Court has no trouble concluding that a valid contract existed between Reno and Goldman, and that Reno breached that contract by initiating arbitration with FINRA.

"Under the 'law of the case' doctrine, a court is generally precluded from reconsidering an issue that has already been decided by the same court, or a higher court in the identical case." *United States v. Alexander*, 106 F.3d 874, 876 (9th Cir. 1997) (quotation marks omitted). The Ninth Circuit's opinion reversing the Court's prior order and remanding the case establishes that an enforceable forum selection clause existed between Reno and Goldman, and that Reno contravened the forum selection clause by initiating a proceeding in an impermissible forum. The Ninth Circuit specifically held that by agreeing to the forum selection clause, "Reno disclaimed any right it might otherwise have had to the FINRA arbitration forum." (ECF No. 51 at 26.) Moreover, nowhere in the various briefs filed on these motions does Reno attempt to argue that it did not breach the contract, and therefore it presents no compelling reason to depart from the law of the case doctrine. *See Alexander*, 106 F.3d at 876. Therefore, by commencing the FINRA

arbitration, Reno breached its contract with Goldman. *See, e.g., Versatile Housewares & Gardening Sys., Inc. v. Thill Logistics, Inc.*, 819 F. Supp. 2d 230, 239 (S.D.N.Y. 2011) (holding that bringing an action in a state outside the chosen forum constitutes an actionable breach of contract); *Allendale Mut. Ins. Co. v. Excess Ins. Co.*, 992 F.Supp. 278, 285 (S.D.N.Y. 1998) (same).

b. Allowing Goldman to Claim Attorneys' Fees as Contract Damages Would Contravene the American Rule.

As an initial matter, Goldman has already received significant relief from Reno's breach of the forum selection clause in the form of specific performance. Reno has consented to a permanent injunction of the FINRA arbitration and the parties are now pursuing their claims in this Court. (ECF No. 58.) Of course, this relief does not foreclose an action for damages based on the same breach. *See Versatile Housewares*, 819 F. Supp. 2d at 239 ("[W]here a party seeks specific performance of a contract, New York courts will award, in addition to specific performance of the contract, such items of damage as naturally flow from the breach, are within the contemplation of the parties, and can be proven to a reasonable degree of certainty."). However, Goldman does not assert it suffered any damages beyond the attorneys' fees and costs incurred in defending the FINRA arbitration. Thus, the question is whether these are proper elements of contract damages.

Like Nevada, New York follows the American Rule. "Under the general rule, attorneys' fees and disbursements are incidents of litigation and the prevailing party may not collect them from the loser unless an award is authorized by agreement between the parties or by statute or court rule." *A.G. Ship Maint. Corp. v. Lezak*, 69 N.Y.2d 1, 5, 503 N.E.2d 681, 683 (N.Y. 1986). Goldman does not assert that any contract, statute, or rule authorizes an award of attorneys' fees

and costs against Reno; rather, it relies on *Indosuez Int'l Fin., B.V. v. Nat'l Reserve Bank*, 304 A.D.2d 429 (N.Y. App. Div. 2003), to argue that the American Rule does not apply in this case.

In *Indosuez*, the New York Supreme Court Appellate Division did "not detail the facts of the case, but it appears that the lower court had permanently enjoined the defendant from pursuing certain foreign litigation, concluding that the defendant was in breach of the relevant agreement's forum selection clause, and also awarded damages for the breach." *Versatile Housewares*, 819 F. Supp. 2d at 243 (discussing *Indosuez* opinion). The Appellate Division held: "Contrary to defendant's contention, damages may be obtained for breach of a forum selection clause, and an award of such damages does not contravene the American rule that deems attorneys' fees a mere incident of litigation." *Indosuez*, 304 A.D.2d at 431.

The U.S. Supreme Court has held that "in cases where jurisdiction rests on diversity of citizenship, federal courts, under the doctrine of *Erie Railroad Co. v. Tompkins*, must follow the decisions of intermediate state courts in the absence of convincing evidence that the highest court of the state would decide differently." *Stoner v. N.Y. Life Ins. Co.*, 311 U.S. 464, 467 (1940) (citation omitted). More recently, the Second Circuit Court of Appeals explained:

> In addressing unsettled areas of state law, we are mindful that our role as a federal court sitting in diversity is not to adopt innovative theories that may distort established state law. Instead we must carefully predict how the state's highest court would resolve the uncertainties that we have identified. In making this prediction, we give the fullest weight to pronouncements of the state's highest court . . . while giving proper regard to relevant rulings of the state's lower courts. We may also consider decisions in other jurisdictions on the same or analogous issues.

Travelers Ins. Co. v. Carpenter, 411 F.3d 323, 329 (2d Cir. 2005) (citations and brackets omitted). Some New York courts have recognized that "the question of the damages available for breach of a forum selection clause is somewhat of an uncertain issue under New York law." *See, e.g., GE Oil & Gas, Inc. v. Turbine Generation Servs., L.L.C.*, 51 Misc. 3d 1226(A) (N.Y. Sup.

Ct. 2016). Moreover, it does appear that, having decided *Indosuez*, the Appellate Division is the highest New York court to address the question presented here. Therefore, the *Indosuez* opinion must be given "proper regard," and must be followed absent convincing evidence that the New York Court of Appeals would decide differently.

Notwithstanding, Reno urges the Court to follow the holding of *Versatile Housewares*, a Southern District of New York opinion which analyzed and declined to follow *Indosuez*. This Court agrees that, absent a definitive ruling from the New York Court of Appeals, *Versatile Housewares* is the more persuasive and well-reasoned opinion. First, the value of *Indosuez* as persuasive authority is severely undercut by its lack of meaningful analysis. *See Versatile Housewares*, 819 F. Supp. 2d at 243–44. Moreover, there exists "other persuasive data" that New York's highest court would disagree with the conclusions of *Indosuez*. *Id.* at 244. As was the case in *Versatile Housewares*, the general rule Goldman's position would require this Court to adopt is that "a party may recover attorneys' fees from an opposing party whenever the fees can be characterized as 'damages' resulting from the opposing party's wrong, rather than as collateral consequences of litigation." *Id.* However, the New York Court of Appeals has consistently held that "[e]ven when an opposing party's conduct directly causes attorneys' fees to be incurred, fee recovery is unavailable unless a specific exception applies." *Id.* (analyzing cases). Even more persuasive is that New York courts have recognized a pertinent exception to the American Rule, but have also foreclosed its availability in the situation presented here:

> The so-called *Shindler* exception to the American Rule is instructive. *Shindler* allows the recovery of fees incurred in prior litigation against third parties caused by a wrongful act, including a breach of contract, of the defendant. *See, e.g.*, *Travelers*, 734 F. Supp. 2d at 385–86. This is a "narrow exception," and the Court of Appeals has been very clear that "[w]hatever the proper scope of [the *Shindler*] exception, it is unavailable where . . . the purported 'third-party' wrongdoer is, either legally or as a practical matter, the same as the claimant's opponent in the main action." *Hunt v. Sharp*, 85 N.Y.2d 883, 626 N.Y.S.2d 57, 649 N.E.2d 1201, 1202 (1995).

Id. Here, Reno's breach caused Goldman to incur litigation costs not against a third party but against Reno itself; *Hunt* forecloses the possibility of fee recovery in such a circumstance.

Therefore, the Court will not adopt the conclusion of *Indosuez*, because there is convincing evidence—as articulated in *Versatile Housewares*—that the New York Court of Appeals would disagree with that conclusion. "Allowing [a party] to collect attorney's fees as damages simply by characterizing them as damages based on a breach of contract would create an exception that would swallow the American Rule, as it is well-established that a party cannot recover attorney's fees from a contract-breaching opponent, even where the breach makes litigation eminently foreseeable." *Brown Rudnick, LLP v. Surgical Orthomedics, Inc.*, No. 13-CV-4348 JMF, 2014 WL 3439620, at *14 (S.D.N.Y. July 15, 2014); *see also JP Morgan Chase Bank, N.A. v. Reifler*, No. 11 CIV. 4016 (DAB), 2014 WL 11350916, at *4 n. 3 (S.D.N.Y. May 16, 2014) (expressing agreement with *Versatile Housewares*). This is not to say that Goldman can never recover the costs and fees it incurred in defending the FINRA arbitration; it just means that any award of such expenses must be permitted by rule or statute in accordance with the American Rule.

The Court will therefore grant Reno's motion to dismiss the counterclaim-in-reply for breach of the forum selection clause, due to Goldman's failure to plead the element of recoverable damages.

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CONCLUSION

IT IS HEREBY ORDERED that the Motion to Dismiss (ECF No. 91) is GRANTED.

IT IS FURTHER ORDERED that the Motion for Summary Judgment (ECF No. 108) is DENIED.

IT IS FURTHER ORDERED that the Motion to Disqualify (ECF No. 120) is DENIED as moot.

IT IS SO ORDERED.

ROBERT C. JONES
United States District Judge

Dated: January 4, 2017.