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Commonwealth of Kentucky

Court of Appeals

NO. 2016-CA-001301-MR

CHRISTODULOS STAVENS AND
ELI HALLAL — APPELLANTS

APPEAL FROM JEFFERSON CIRCUIT COURT
v. HONORABLE A.C. MCKAY CHAUVIN, JUDGE
ACTION NO. 11-CI-001048

ABDUL G. BURIDI AND
KENTUCKIANA INVESTORS, LLC — APPELLEES

AND NO. 2016-CA-001841-MR

ABDUL G. BURIDI — CROSS-APPELLANT

CROSS-APPEAL FROM JEFFERSON CIRCUIT COURT
v. HONORABLE A.C. MCKAY CHAUVIN, JUDGE
ACTION NO. 11-CI-001048

CHRISTODULOS STAVENS, ELI R. HALLAL
AND KENTUCKIANA INVESTORS, LLC — CROSS-APPELLEES

NO. NO. 2017-CA-000063-MR

CHRISTODULOS STAVENS AND
ELI HALLAL APPELLANTS

APPEAL FROM JEFFERSON CIRCUIT COURT
v. HONORABLE A.C. MCKAY CHAUVIN, JUDGE
ACTION NO. 11-CI-001048

ABDUL G. BURIDI AND
KENTUCKIANA INVESTORS, LLC APPELLEES

AND NO. 2017-CA-000064-MR

ABDUL G. BURIDI CROSS-APPELLANT

CROSS-APPEAL FROM JEFFERSON CIRCUIT COURT
v. HONORABLE A.C. MCKAY CHAUVIN, JUDGE
ACTION NO. 11-CI-001048

CHRISTODULOS STAVENS, ELI R. HALLAL
AND KENTUCKIANA INVESTORS, LLC CROSS-APPELLEES

OPINION
AFFIRMING IN PART, REVERSING IN PART
AND REMANDING

** ** ** ** **

BEFORE: ACREE, JOHNSON[1] AND SMALLWOOD, JUDGES.

SMALLWOOD, JUDGE: Christodulos Stavens and Eli Hallal appeal, and Abdul G. Buridi cross-appeals, from a Jefferson Circuit Court judgment from a jury verdict in favor of Buridi. Stavens and Hallal argue that the trial court erred the following ways: in failing to direct a verdict in their favor on Buridi's fraud claim; in permitting Buridi to advance a derivative claim on behalf of a corporate entity; and, in erroneously instructing the jury on conversion. Buridi cross-appeals and argues that the circuit court erred in awarding 3% pre-judgment interest on the conversion and promissory note claims. For the reasons stated below, we find AFFIRM in part, REVERSE in part AND REMAND.

Kentuckiana Investors, LLC ("KI") is a Delaware limited liability company formed in 1993 for the purpose of establishing and funding Kentuckiana Medical Center ("KMC") in Southern Indiana. KMC was a new physician-owned startup hospital and it continues to operate as of mid-2018.

[1] Judge Robert G. Johnson concurred in this opinion prior to the expiration of his term of office. Release of the opinion was delayed by administrative handling.

Dr. Christodulos Stavens is a Louisville, Kentucky cardiologist and Dr. Eli Hallal is a New Albany, Indiana internist. Dr. Abdul Buridi is a nephrologist in Louisville, Kentucky. KI was owned by about 30 practicing physician investors, with Dr. Stavens serving as Manager of the entity during KMC's construction and startup phase. KMC opened in 2009, received its Medicaid license and began seeing a few patients. In 2010, and in accordance with its Operating Agreement, KI held elections and created a five-member board. The KI physician investors owned 49% of KMC, with the remaining 51% of KMC being owned by Cardiovascular Hospital of America, LLC ("CHA"). KMC owned the operations and leased the land and building from an affiliate called KMC Real Estate Investors, LLC ("KMCRE"). KI was a co-owner of KMCRE.

In 2006, an entity called Veterans Parkway Investors ("VPI") was created to purchase and operate an office building on a parcel adjacent to the KMC project. Stavens and Hallal, who were integral to both KI and KMC, believed that having a medical office building next to the hospital would be important for the long-term success of KMC. They paid the seller of the office building parcel and a developer $150,000 for certain rights and an easement. Ultimately, VPI was unable to secure financing and the medical office building was never developed.

Sometime earlier, in 2006 or 2007, Stavens approached Buridi about becoming an investor in KMC by purchasing an interest in KI. Buridi would later

assert that he believed hospitals were generally not profitable investments, but he purchased one share of KI – the minimum investment – in order to have staff privileges at KMC to treat his existing patients in the Clarksville, Indiana area. On January 18, 2007, Buridi wrote a check to KI in the amount of $26,370, representing the purchase price of one share of KI.

In 2008 or 2009, and shortly before construction of the hospital was completed, a national financial crisis loomed and credit markets tightened. During this time, BB&T and Siemens withdrew from agreements to provide equipment financing. This withdrawal, in conjunction with the ongoing costs of developing the project, contributed to serious financial issues for KI – of which Stavens and Hallal were the largest investors. Stavens and Hallal infused KI with cash and loans of $380,000 and $498,300, respectively. In late 2008, Buridi loaned the venture $100,000, but after learning that about only half of the physician investors had provided similar loans, he demanded and received his money back. Two years later, Buridi loaned KI and/or KMC another $25,000, for which he received a promissory note signed by Stavens and Hallal. CHA committed $1 million to the project.

During this time, several factors converged to place financial stress on the project and its investors. The Patient Protection and Affordable Care Act (commonly known as Obamacare) was enacted, which had provisions limiting

physician-owned hospitals. At the same time, credit markets collapsed making it difficult or impossible for the investors to obtain additional financing. This presented the KI investors with the option of continuing with the project by finding alternative financing or abandoning it. The KI investors decided to continue with the project.

In the absence of BB&T, several providers were still willing to furnish hospital equipment, but all wanted joint and several guarantees from the physicians. One such provider was Steris. In late 2008, Stavens, Hallal and Buridi, along with seven other investors, executed guarantees of the Steris debt. In early to mid-2009, the parties executed additional loan guarantees to Diversified Lending ("DivLend") and the Leasing Group.

At issue is the nature of these loan guarantees. The KI Operating Agreement provides that debt would be assumed or guaranteed on a pro rata basis. In other words, an investor owning one share of KI would assume or guarantee only half the debt of an investor owning two shares. Buridi would later allege that the guarantees executed by him and in favor of Steris, DivLend and the Leasing Group were characterized by Stavens and Hallal as being on a pro rata basis, when the documents he executed actually provided for joint and several liability. Buridi alleged that in April or May 2009, he expressly asked Stavens what "joint and several" meant, and that Stavens falsely stated that it only meant that all of the

physician investors were signing the document, but that each obligation was pro rata only. Buridi would state that he asked Hallal the same question and received the same answer. Buridi would contend that he was shocked to learn in 2010 that "joint and several" liability meant that he owed $9 million to equipment lessors.

Thereafter, KMC filed Chapter 11 Bankruptcy while the hospital continued to operate. Eventually a deal was reached to bring it out of bankruptcy when the hospital's largest creditor agreed to infuse the hospital with capital and take over its operations.

On February 9, 2011, Buridi in his individual capacity filed the instant action in Jefferson Circuit Court against Stavens, Hallal, and CHA. He asserted claims including breach of contract, conversion, breach of fiduciary duty, fraudulent misrepresentation, and unjust enrichment. Buridi alleged: that Stavens and Hallal were required to pay the balance of a $25,000 promissory note they had executed in Buridi's favor; that they violated fiduciary obligations in connection with a series of decisions related to the financing, development, and operation of KMC; and, that Stavens and Hallal committed fraud and violated their fiduciary duties to Buridi by misleading him into signing three joint and several equipment lease guarantees in the spring of 2009. In 2012, Buridi amended his complaint to assert derivative claims on behalf of KI. The amended complaint also asserted a claim of conversion based on Stavens and Hallal's alleged payment of investor

funds, rather than personal funds, to KDW Developers LLC ("KDW) as part of the attempted acquisition of the parcel of land adjacent to the hospital property.

The matter proceeded to trial, whereupon the jury found: that Stavens and Hallal had fraudulently represented to Buridi that the guarantees he signed were pro rata; that Stavens and Hallal had converted $255,000 belonging to KI; and, that KI had no contractual or equitable obligation to repay Stavens and Hallal for their capital investments. The jury also found that Stavens and Hallal individually were obligated to repay the promissory note in the amount of $25,000.00 to Buridi. The Jefferson Circuit Court rendered judgment reflecting the verdict, and Buridi was awarded attorney fees and pre-judgment interest on certain claims. This appeal and cross-appeal followed.

Stavens and Hallal first argue that the Jefferson Circuit Court erred in failing to direct a verdict in their favor or enter a judgment notwithstanding the verdict on Buridi's fraud claims. The jury awarded Buridi compensatory and punitive damages for fraud, based on his claim that Stavens and Hallal misrepresented the nature of his payment obligation on the guarantees that he signed to keep the project viable. Stavens and Hallal contend that the legal sufficiency of Buridi's claim should be determined by reference to Indiana rather than Kentucky law, and that his pleadings and proof were insufficient to raise a colorable case of fraud. Stavens and Hallal argue that the alleged

misrepresentations directly contradict a written document that Buridi - who they characterize as a sophisticated businessman - acknowledges having read and signed. They also assert that Buridi's fraud claims concern alleged misrepresentations about the legal effect of a written document and, therefore, cannot be actionable as fraud.

On the issue of whether Kentucky or Indiana law applies, "any significant contact with Kentucky is sufficient to allow an application of Kentucky law." *Reichwein v. Jackson Purchase Energy Corp.*, 397 S.W.3d 413, 416 (Ky. App. 2012) (citing *Foster v. Leggett*, 484 S.W.2d 827 (Ky. 1972)). Further, Kentucky favors the application of its own law whenever it can be justified. *Johnson v. S.O.S. Transp., Inc.*, 926 F.2d 516, 519 n. 6 (6th Cir. 1991). In the matter below, both Plaintiff Buridi and Defendant Stavens were Kentucky residents. Further, third-party complaints against Buridi which precipitated the instant action were filed in Kentucky by the Leasing Group and Steris, judgment against Buridi on the Leasing Group guarantee was entered in Kentucky, and the purported conversion was accomplished using accounts maintained in Kentucky. While there were also significant contacts with Indiana, as it was the locus of the hospital, the totality of the record supports the trial court's application of Kentucky law on Buridi's claim of fraud. We find no error.

Stavens and Hallal go on to argue that Buridi's pleadings and proof were not adequate to raise a colorable case of fraud. They maintain that the who, what, when and where of the alleged misrepresentation as to Buridi's loan guarantees were a muddle of inconsistencies, and that his failure to offer proof concerning the timing of the alleged statements is fatal to his claim. As such, Stavens and Hallal argue that they were entitled to a verdict on this issue.

The record rebuts the contention of Stavens and Hallal on this issue. Buridi's claim of fraud was pled with particularity, consisting of four pages of detailed allegations describing the fraud claims against them. Buridi alleged the time, place and substance of the purported fraud, *i.e.*, that the guarantee sought was described by Stavens as pro rata, and the action procured by the misrepresentation in the form of Buridi's signature. We have no basis for concluding that Buridi's claim of fraud was not alleged with particularity in contravention of Kentucky Rule of Civil Procedure (CR) 9.02.

Additionally, we are not persuaded that Buridi's proof was insufficient to prosecute his claim. A party claiming fraud must establish six elements by clear and convincing evidence: "a) material representation b) which is false c) known to be false or made recklessly d) made with inducement to be acted upon e) acted in reliance thereon and f) causing injury." *United Parcel Service Co. v. Rickert*, 996 S.W.2d 464, 468 (Ky. 1999) (citing *Wahba v. Don Corlett Motors*,

Inc., 573 S.W.2d 357, 359 (Ky. App 1978)). The jury's verdict in favor of Buridi on this claim was based on evidence presented that Buridi signed Leasing Group and Steris guarantees in the lobby at KMC on May 29, 2009; that Buridi asked Stavens and Hallal individually what "joint and several" meant; and, that both Stavens and Hallal stated to Buridi that "joint and several" meant that all the doctors were signing the guarantees, but each obligation was pro rata. Further, Buridi offered corroborating testimony establishing that Stavens and Hallal had made similar deceptive statements to Drs. Digenis and Melo.

Buridi directs our attention to *Cline v. Allis-Chalmers Corp.*, 690 S.W.2d 764, 766 (Ky. App. 1985), holding that a signatory to a contract is bound by its terms unless there was some fraud in the process of obtaining his signature. That is, even though Buridi either should have or did read the terms of the guarantees, the presence of contemporaneous fraudulent misrepresentations operates to excuse him because his signature was fraudulently induced.

Ample evidence was adduced at trial upon which the jury could reasonably conclude that Stavens and Hallal made fraudulent misrepresentations as to the nature of the guarantees when Buridi executed them. Accordingly, we

cannot conclude that the Jefferson Circuit Court erred in failing to direct a verdict or entered a judgment notwithstanding the verdict in favor of Stavens and Hallal.[2]

Stavens and Hallal next argue that the trial court erred in allowing Buridi to advance claims on KI's behalf. They note that beginning with his First Amended Complaint, Buridi proceeded against Stavens and Hallal on his own behalf, but also in a derivative capacity as representative of KI. KI ultimately recovered $255,000 on Buridi's claim of conversion based on Stavens and Hallal's usage of KI funds to keep open the VPI option. Stavens and Hallal assert that Buridi never should have been allowed to assert derivative claims on KI's behalf. They maintain: that Buridi did not make a pre-litigation demand on KI's board; did not plead nor prove that any board members other than Stavens and Hallal had any conflicts of interest that would have disqualified them from considering pre-litigation demands; and, did not establish that he was an appropriate representative of KI. Stavens and Hallal go on to argue that because KI is a Delaware entity, this issue must be addressed by application of Delaware Court of Chancery Rule 23.1 and may be reviewed *de novo*.

[2] As part of this argument, Stavens and Hallal maintained that Buridi offered no specific proof of "fraud in the inducement." Because the evidence showed that the signature and the inducement to obtain that signature were integral to each other and part of one larger occurrence, we find no error on this issue.

This matter was extensively briefed and argued below. On February 18, 2015, the Jefferson Circuit Court rendered an opinion and order determining that Delaware Rule 23.1 applied in its totality. Citing *King v. VeriFone Holdings, Inc.*, 12 A.3d 1140 (Del. Supr. 2011), the trial court stated:

> Grounds for alleging demand futility, as a prerequisite to a shareholder derivative action, include that a reasonable doubt exists as to whether the board is capable of making an independent decision to assert the claim if demand were made, a majority of the board has a material financial or familial interest, a majority of the board is incapable of acting independently for some other reason such as dominion or control, or the underlying transaction is not the product of a valid exercise of business judgment.

The court then held that Buridi's Complaint sufficiently set forth the reasons that he did not make a demand on KI, and that "a reasonable doubt exists as to whether the Board is capable of making an independent decision to assert the claim if demand were made."

Buridi asserts that the determination of whether a plaintiff has pled particularized facts demonstrating demand futility must be considered on appeal under an abuse of discretion standard rather than *de novo* as Stavens and Hallal maintain. We need not address this distinction, as Buridi's Complaint amply set forth specific and detailed allegations that demand on Stavens and Hallal would prove futile. Further, the litigation conduct of Stavens, Hallal and KI further demonstrated that KI was not an independent and neutral party. When Stavens and

Hallal cross-claimed against KI seeking damages, KI did not answer. Buridi, apparently at his own expense, defended the claims against KI. Ultimately, we agree with the Jefferson Circuit Court that one may reasonably doubt whether the Board was capable of making an independent decision to assert a claim had Buridi so demanded.[3] We find no error.

Stavens and Hallal's final argument is that the Jefferson Circuit Court erroneously instructed the jury on the derivative claim of conversion. The jury awarded KI $255,000 for conversion upon finding that Stavens and Hallal converted that amount of KI assets when they "loaned" those sums to VPI to keep open the real estate option on the land adjoining the KMC facility.[4] Stavens and Hallal tendered the following proposed instruction:

> Plaintiff alleges, derivatively on behalf of KI, a claim against Defendants Stavens and Hallal for conversion. Defendants Stavens and Hallal deny this claim.
>
> You will find for Plaintiff only if you are satisfied from the evidence:
>
> 1. Defendants Stavens and Hallal took property that belonged to KI; and
> 2. Defendants Stavens and Hallal took the property for their own use and benefit in exclusion and defiance of KI's rights.

[3] Buridi asserted that Stavens and Hallal were the only directors of KI. Stavens and Hallal later responded that KI had a properly-constituted 5-member Board. When a hearing on this issue was conducted, the Jefferson Circuit Court determined that Stavens and Hallal failed to overcome Buridi's *prima facie* case of demand futility.

[4] At trial, Stavens and Hallal first argued that the KI funds belonged to them at the time of the transfers to VPI. Later, they characterized the transfers as loans to address their bad accounting.

> Otherwise, you will find for the Defendants Stavens and Hallal.

The jury originally received this instruction, but thereafter the phrase "in . . . defiance of KI's rights" was redacted by Judge Chauvin. Stavens and Hallal now argue that the removal of this phrase made the jury's finding in favor of KI inevitable. The corpus of their argument on this issue is that the revised version of the instructions failed to take into account that the KI Operating Agreement gave Stavens and Hallal the authority to make such loans.

We agree with Buridi that there is no effective difference between the jury instruction tendered by Stavens and Hallal and the one ultimately used by the jury. The final version of the instructions employed by the jury expressly required a verdict in favor of KI only if the jury found that Stavens and Hallal took property that belonged to KI for their own use and benefit. The phase at issue - "defiance of rights" - is not an element of the tort of conversion and is effectively subsumed in the language presented to the jury. *See Jasper v. Blair*, 492 S.W.3d 579 (Ky. App. 2016). Additionally, Stavens and Hallal repeatedly make issue of the phrase "intent to deprive" as if it is the functional analog of "defiance of rights," but the phrase "intent to deprive" was not included in the instructions they tendered.

Jury instructions are reviewed *de novo*. *Sargent v. Shaffer*, 467 S.W.3d 198, 204 (Ky. 2015) ("The content of a jury instruction is an issue of law that must remain subject to *de novo* review by the appellate courts."). When

reviewing the instant instruction in this manner, we conclude that the substance of the instruction is not diminished by the removal of the phrase "in . . . defiance of KI's rights," as this phrase is not an element of the tort of conversion. We find no error.

In his cross-appeal, Buridi argues that the circuit court erred in awarding 3% pre-judgment interest on the promissory note and the conversion judgment. In support of this argument, Buridi asserts that the promissory note provides for 10% pre-judgment interest. He also directs our attention to Kentucky Revised Statute (KRS) 360.010 for the proposition that 8% pre-judgment interest is statutorily required on the conversion claim.

When addressing this issue below, the Jefferson Circuit Court found that pre-judgment interest is allowed as matter of sound discretion as to both the derivative claim and the promissory note. Citing *Friction Materials Co. v. Stinson*, 833 S.W.2d 388, 392 (Ky. App. 1992), the court determined that the question is not whether the claim is liquidated or unliquidated, but whether justice and equity demand an allowance of interest to the injured party. The court determined that 3% pre-judgment interest per annum was "a fair and equitable interest rate on the damages amount awarded for the conversion claim and the promissory note."[5]

[5]*Opinion and Order (Corrected)* rendered December 7, 2016.

The promissory note, which is found in the record as Plaintiff's Exhibit 54, expressly provides for interest at the rate of 10% per annum commencing on March 4, 2010. This is the rate to which Buridi is entitled thereon. Further, KRS 360.010 states that the legal rate of interest on liquidated (*i.e.*, determined or fixed) damages is 8% per annum. *See also Poundstone v. Patriot Coal Co., Ltd.*, 485 F.3d 891, 903 (6th Cir. 2007). We therefore conclude that 10% interest is payable on the promissory note in accord with its express terms and 8% interest is payable on the derivative claim for conversion.

For the foregoing reasons, we REVERSE and REMAND the Judgment of the Jefferson Circuit Court as to its entry of pre-judgment interest on the promissory note and conversion claim, but, in all other respects AFFIRM.

ALL CONCUR.

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