

Whitney Group, LLC v Hunt-Scanlon Corp.
2010 NY Slip Op 33805(U)
September 10, 2010
Sup Ct, NY County
Docket Number: 602775/08
Judge: Charles E. Ramos
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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY FILE

PRESENT: Charles Edward Ramos

PART 53

Index Number : 602775/2008

WHITNEY GROUP, LLC,

vs

HUNT-SCANLON CORPORATION,

Sequence Number : 006

DISMISS

INDEX NO. _____

MOTION DATE _____

MOTION SEQ. NO. _____

MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to/for _____

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...

Answering Affidavits — Exhibits _____

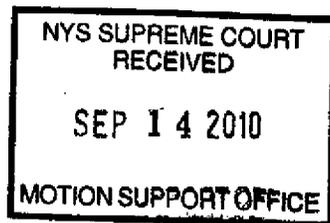
Replying Affidavits _____

PAPERS NUMBERED

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered that this motion

to be decided in accordance with accompanying memorandum decision and order.



Dated: 9/10/2010

[Signature]
CHARLES E. RAMOS

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION

Check if appropriate: DO NOT POST REFERENCE

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

SUPREME COURT OF THE STATE OF NEW YORK
 COUNTY OF NEW YORK: COMMERCIAL DIVISION

-----x
 WHITNEY GROUP, LLC,

Index No. 602775/08

Plaintiff,

-against-

HUNT-SCANLON CORPORATION, CHRISTOPHER W. HUNT,
 SCOTT SCANLON, JEFFREY T. SUSSMAN, JASPAN
 SCHLESINGER HOFFMAN LLP, ROBERT LONDIN,

Defendants.

-----x
 JASPAN SCHLESINGER LLP s/h/a JASPAN SCHLESINGER
 HOFFMAN LLP and ROBERT LONDIN,

Third-Party Plaintiffs,

-against-

GARY GOLDSTEIN, ALICIA LAZARO, JEFFREY BELL,
 HARRY O'NEILL, SIMON HALL, ESTATE OF TOM
 SEADON, RICHARD FISHER, CHRIS MANFIELD, DARIN
 WHITE VOLPE, CHARLES PEAT, WILLIAM COHAN,
 DANIEL CARMICHAEL, ELLEN HELLER, NIALL MCDONALD,
 and CHRIS HARNED,

Third-Party Defendants.

-----x
Charles Edward Ramos, J.S.C.:

Motion sequence numbers 006 and 007 are consolidated for
 disposition.

In motion sequence 006, third-party defendants Gary
 Goldstein, Alicia Lazaro, Jeffrey Bell, Darin White Volpe,
 William Cohan, Daniel Carmichael, Ellen Heller, and Chris Harned
 (together, TP Defendants) move to dismiss the third-party
 complaint (CPLR 3211 [a] [1], [4], [7]).

In motion sequence 007, plaintiff Whitney Group LLC (Whitney
 Group) moves to dismiss the second counterclaim of defendants
 Robert Londin and Jaspan Schlesinger Hoffman for contractual

indemnification (CPLR 3211 [a] [7]).

Background

In August 2008, Whitney Group, an executive recruiting firm, discovered that beginning in 2004, its chief executive officer, defendant Jeffrey Sussman, misappropriated a total of \$7 million over several years in corporate advances (the Funds) to defendants Hunt-Scanlon Corporation (Hunt-Scanlon), Scott Scanlon and Christopher W. Hunt (together, the HS Defendants).

Sussman concealed the misappropriation, that was made without Whitney Group's authorization or knowledge and for no apparent legitimate business purpose, until August 2008. At the time of the filing of this action, Whitney Group is insolvent.

According to Whitney Group, its outside corporate counsel, defendants/third-party plaintiffs, Jaspan Schlesinger Hoffman, LLP (Jaspan), and Jaspan partner, Robert Londin (together, the Jaspan Defendants), were aware that Sussman was causing Whitney Group to advance the Funds to the HS Defendants without Whitney Groups' knowledge. The Jaspan Defendants even purportedly had numerous conversations with Sussman concerning his wrongdoing and what remedial steps should be taken.

For instance, in February 2007, Sussman sought advice from Londin with respect to the first \$2 million of the Funds advanced. At the time, the Jaspan Defendants allegedly advised him to make a full disclosure of his wrongdoing to Whitney Group's board of directors. However, at no point did the Jaspan Defendants inform the Whitney Group's board of Sussman's

wrongdoing.

In early August 2008, Sussman informed Whitney Group's present counsel, Rottenberg Lipman Rich, P.C. (RLR), of the misappropriation, and that the current outstanding indebtedness from the HS Defendants was \$3 million. RLR subsequently learned that Sussman had misappropriated in excess of \$7 million that remained outstanding, and threatened to inform Whitney Group if Sussman failed to. Several days later, RLR informed Whitney Group of Sussman's misappropriation that he had caused to be advanced to the HS Defendants.

Whitney Group terminated Sussman for cause and unsuccessfully attempted to recoup the funds from Hunt-Scanlon.

In September 2008, Whitney Group commenced this action and asserted thirteen claims. The claims are for breach of fiduciary duty, and disgorgement of compensation against Sussman; aiding and abetting breach of fiduciary duty, piercing the corporate veil, and unjust enrichment against the HS Defendants; conversion against Sussman and the HS Defendants; fraud and breach of contract against Sussman, Hunt-Scanlon and Hunt; money had and received against Scanlon; and breach of fiduciary duty and malpractice against the Jaspán Defendants.

In December 2008, the Jaspán Defendants served an answer with affirmative defenses, cross-claims against the HS Defendants and Sussman for contribution, and counterclaims against Whitney Group for breach of contract and contractual indemnity arising out of an indemnification clause contained in Whitney Group's

operating agreement (Operating Agreement).

In October 2009, the Jaspan Defendants commenced a third-party action against Gary Goldstein, Alicia Lazaro, Jeffrey Bell, Harry O'Neil, Simon Hall, and the Estate of Tom Seaden, members of Whitney Group's board of managers (Board of Managers), and Richard Fisher, Chris Manfield, Darin White Volpe, Charles Peat, William Cohan, Daniel Carmichael, Ellen Heller, Niall McDonald and Chris Harned, Whitney Group's shareholders (Shareholders) (together, the TP Defendants).

In its third-party complaint, the Jaspan Defendants assert claims for contribution against the Board of Managers, and claims for contractual indemnification and third-party beneficiary against the TP Defendants.¹

Discussion

I. Contractual Indemnification

In its counterclaim against Whitney Group for contractual indemnification, the Jaspan Defendants assert that they are "indemnitees" under section 5.7 of the Operating Agreement. On this basis, they argue that Whitney Group is obligated to indemnify them for any liability or losses that they incur with respect to this action.

Similarly, the Jaspan Defendants seek contractual indemnification from the TP Defendants in their capacity as

¹ The Jaspan Defendants originally asserted claims for common law indemnification and negligence against the TP Defendants, which it agreed to discontinue (Jaspan Defendants' Memo. of Law in Opp., 2-3).

officers, directors and shareholders of Whitney Group, as intended beneficiaries of the identical provision. The Jaskan Defendants assert that, in the event that they are found liable for damages in the main action, the TP Defendants are obligated to return their pro rata share of distributions received in their capacity as shareholders.

In the alternative, the Jaskan Defendants assert that an ambiguity exists in the Operating Agreement with respect to which persons are covered under the indemnification provision.

Whitney Group and the TP Defendants (together, Movants) move to dismiss the claim for contractual indemnification.² The Movants assert that the claim fails because the Operating Agreement expressly disavows the creation of third party rights, on the basis of New York public policy that disfavors exculpatory provisions for own's own negligent acts, and enforcement of the provision violates Disciplinary Rule (DR) 6-102.

With respect to indemnification, section 5.7 of the Operating Agreement states,

"Each member of the Board, each member of the Advisory Executive Committee, and each of the officers, directors, agent, Shareholders, members, managers of the Company [Whitney Group] and each Affiliate of the Company and **any other person who serves at the request of the Board on behalf of the Company** (in each case, an "Indemnatee") **shall not be liable to the Company**, to such Affiliate or to any Shareholders for any act or omission by such Indemnatee taken or omitted with respect to the Company, in the absence of such Indemnatee's fraud, willful misconduct, or bad faith. The Company shall indemnify each such Indemnatee for

² Whitney Group incorporates those arguments made by the TP Defendants (Whitney Group's Memo. of Law, 2).

any loss, liability, damage or expense incurred by such Indemnitee on behalf of the Company or any Affiliate of the Company ... except for losses arising from such Indemnitee's own fraud, willful misconduct or bad faith" (emphasis added).

With respect to Whitney Group's shareholders, section 5.7 provides:

"Shareholders shall not be individually obligated to provide such indemnification beyond their respective capital investment in the Company and/or equity in the Company. However, each Shareholder shall be obligated to return to the Company the pro rata share of Distributions received by such Shareholder."

With respect to third party rights, section 12.3 of the Operating Agreement provides:

"This Agreement is entered into by and among the Company and the Shareholders for the exclusive benefit of the Company, its Shareholders, and their Permitted Transferees. This Agreement is expressly not intended for the benefit of ... any other Person ... **no third party shall have any rights under this Agreement**" (emphasis added).

The court's role in interpreting an agreement is to ascertain the intent of the parties at the time that the agreement was entered into (*Evans v Famous Music Corp.*, 1 NY3d 452, 458-59 [2004]). Nonetheless, an agreement is ambiguous where it contains internal inconsistencies or on its face is reasonably susceptible to more than one interpretation, whereupon extrinsic evidence is admissible to determine the parties' intent (*Gessin Elec. Contractors, Inc. v 95 Wall Assocs., LLC*, 74 AD3d 515 [1st Dept 2010]).

The Court determines that the Operating Agreement contains an ambiguity with respect to whether persons who serve at the

request and on behalf of Whitney Group's board are entitled to indemnification, as expressly contemplated by section 5.7, in light of the provision disclaiming the creation of rights in unnamed third parties, under section 12.3.

Specifically, section 12.3, by its express terms, disavows that it confers enforceable rights in unnamed third parties, and the Jaspán Defendants are not signatories of the Operating Agreement.

Generally, where an agreement expressly provides that it is for the sole and exclusive benefit of certain named parties, that provision is controlling and unnamed third parties may not claim rights thereunder (*Board of Mgrs. of Alexandria Condo. v Broadway/72nd Assocs.*, 285 AD2d 422, 424-25 [1st Dept 2001]). Thus, section 12.3 alone can be read as negating the creation of any enforceable rights in the Jaspán Defendants, including the right to indemnification, because they are not signatories to the Operating Agreement.

However, other language contained in the Operating Agreement can be read as entitling persons who are non-signatories to the Operating Agreement to enforce the indemnification provision, to the extent that these persons "serve[d] at the request of the Board on behalf of" Whitney Group (Operating Agreement, § 5.7). In this regard, section 5.7 entitles unnamed persons to seek indemnification from Whitney Group for "act[s] or omission[s] ... taken or omitted with respect to" Whitney Group.

Because the Operating Agreement contains an internal

inconsistency in this regard, it cannot be construed as a matter of law at the pre-answer motion to dismiss stage (*Hambrecht & Quist Guar. Finance, LLC v El Coronado Holdings, LLC*, 27 AD3d 204, 204 [1st Dept 2006]). Thus, an issue arises concerning Whitney Group's intent to permit the Jaspán Defendants' to be included within the scope of the indemnification provision.

Notwithstanding this lingering ambiguity, in light of the claims asserted against the Jaspán Defendants in the main action, the Court must address the Movants' remaining arguments in support of dismissal of the claim for contractual indemnification.

New York courts frown upon agreements intended to exculpate a party from the consequences of its own negligence (*Gross v Sweet*, 49 NY2d 102, 106-07 [1979]). Although such agreements are enforceable, with certain exceptions,³ they are subject to close judicial scrutiny (*Id.*; *Banc of America Securities LLC Solow Bldg. Co. II, L.L.C.*, 47 AD3d 239, 245 [1st Dept 2007]).

Consequently, courts have carved out a rule of interpretation applicable to such provisions, and unless the intention of the parties is expressed in unmistakable language, an exculpatory provision will not be deemed to insulate a party from liability for its own negligence acts (*Id.*).

Here, the complaint in the main action asserts claims for legal malpractice and breach of fiduciary duty against the Jaspán

³ Agreements that purport to exempt liability for willful or grossly negligent acts are void (*Sommer v Federal Signal Corp.*, 79 NY2d 540, 553-559 [1992]).

Defendants. Assuming *arguendo* that the parties intended to permit unnamed third parties, including legal professionals, to enforce the indemnification provision with respect to certain types of loss or liability, the language of that provision does not set forth the unmistakable intent of the parties, in unambiguous, readily understandable terms, that Whitney Group is required to indemnify the Jaspan Defendants from their own legal malpractice (see *Lachonna v Consolidated Edison Co. of New York*, 170 AD2d 191 [1st Dept 1991]; *Swift v Choe*, 242 AD2d 188, 193-94 [1st Dept 1998]).

Accordingly, irrespective of whether extrinsic evidence establishes the parties' intent that the Jaspan Defendants should benefit from the indemnification provision, the Court concludes that this provision will not exculpate them from liability for legal malpractice, if so adjudicated.

Alternatively, the Movants assert that it is improper for the Jaspan Defendants, as Whitney Group's former counsel, to attempt to assert a claim under the Operating Agreement that they themselves prepared.

At the outset, an issue of fact exists with respect to whether the Jaspan Defendants represented the Whitney Group during the negotiation and execution of the Operating Agreement, and whether Londin actually drafted it, in light of the submission of conflicting affidavit and deposition testimony. Consequently, the factual circumstances of the drafting, negotiation and execution of the Operating Agreement cannot be

resolved at the pre-answer stage.

For these reasons, the motions to dismiss are denied with respect to the counterclaim and third-party claim for contractual indemnification, as limited herein.

II. Contribution

The Jaspan Defendants assert a third-party claim for contribution against the Board of Managers under CPLR § 1401. In the third-party complaint, the Jaspan Defendants allege that the Board of Managers, in their capacity as officers and directors, failed to monitor the financial activities of Whitney Group and failed to implement safeguards to ensure that corporate officers did not have unfettered access to corporate funds, which were purportedly contributing causes of Whitney Group's injuries.

In its answer in the main action, as affirmative defenses to Whitney Group's claims, the Jaspan Defendants allege that the culpable conduct of Whitney Group's employees, members and agents, including the Board of Managers, caused, in whole or in part, Whitney Group's injuries, and seek an offset or reduction to the extent that the Jaspan Defendants are found liable to Whitney Group.

The TP Defendants assert, inter alia, that the third-party claim for contribution is redundant of the Jaspan Defendants' affirmative defenses in the main action. The Court agrees.

Where a defendant has raised a plaintiff's negligence as an affirmative defense to its own liability, that defendant may not simultaneously seek contribution from that plaintiff's agent

(*Lachonna*, 170 AD2d 191; *Hercules Chemical Co. v North Star Reinsurance Corp.*, 72 AD2d 538 [1st Dept 1979]; *Ruszkowski v Sears, Roebuck & Co.*, 188 AD2d 967, 968 [3d Dept 1992], *lv denied* 82 NY2d 654 [1993]; *Ivor Wolfson Corp. SA v Locke Liddell & Sapp LLP*, 2001 WL 246384, *4 [SD NY 2001]; *Iannucci v Kucker & Bruth, LLP*, 2009 WL 3765040, *2 [Sup Ct, NY County 2009]).

Stated differently, where a third-party defendant served as an agent to the plaintiff throughout the transaction at issue, dismissal of a third-party claim for contribution is warranted because any culpable conduct of the third-party defendant is attributable to the plaintiff under agency principles (*Id.*).

Here, the Jaspan Defendants have raised the Board of Managers' negligence as an affirmative defense to its own liability to the Whitney Group, which is the identical basis upon which it seeks contribution from the Board of Managers in the third-party action. Because any culpable conduct of the Board of Managers committed within the scope of their duties is attributable to Whitney Group, any recovery by the Whitney Group against the Jaspan Defendants would be subject to an appropriate reduction for the Board of Managers' negligence, if any, under agency and comparative negligence principles. Therefore, the third-party claim for contribution is redundant of the Jaspan Defendants' affirmative defenses in the main action.

In opposition, the Jaspan Defendants assert that their third-party claim for contribution is not redundant insofar as they allege that certain Board of Managers committed culpable

acts beyond the scope of their employment. However, the third-party complaint, answer, and affidavits submitted in opposition to the motions are completely devoid of any allegations that a member of the Board of Managers committed culpable acts beyond the alleged negligent performance of its duty as an officer and director of Whitney Group. Consequently, the claim for contribution must be dismissed.

Nonetheless, the Jaspan Defendants are granted leave to replead their answer in the main action, if so advised and upon an appropriate showing of merit, in order to afford them the opportunity to adequately plead their affirmative defenses to include allegations of culpable conduct by the Board of Managers beyond the scope of their duties (*Elliman v Elliman*, 259 AD2d 341 [1st Dept 1999]).

Accordingly, it is

ORDERED the third-party defendants' motion to dismiss (006) is denied with respect to contractual indemnification, as reflected herein, and is otherwise granted with respect to the third-party claim for contribution, with leave to replead the answer in the main action upon the submission of an affidavit of merit within 30 days of service of a copy of this order with notice of entry; and it is further

ORDERED that the plaintiff's motion (007) to dismiss is denied with respect to the second counterclaim, as reflected herein.

Dated: September 10, 2010

ENTER:
J.S.C.

CHARLES E. RAMOS