SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: BARBARA R. KAPNICK PART 39
Justice

Index Number : 113020/2009
ISLAND GLOBAL YACHTING
vs.
REUBEN HOPPENSTEIN &
SEQUENCE NUMBER : 003
SUMMARY JUDGMENT

INDEX NO. ______
MOTION DATE ______
MOTION SEQ. NO. ______

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

Notice of Motion/Order to Show Cause — Affidavits — Exhibits ______ | No(s). ______
Answering Affidavits — Exhibits ______ | No(s). ______
Replying Affidavits ______ | No(s). ______

Upon the foregoing papers, it is ordered that this motion ~~is~~ and cross motion are decided in accordance with the accompanying memorandum decision.

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

Dated: 6/25/13

______, J.S.C.
BARBARA R. KAPNICK

1. CHECK ONE: .... ☐ CASE DISPOSED ☒ NON-FINAL DISPOSITION
2. CHECK AS APPROPRIATE: ....MOTION IS: ☐ GRANTED ☒ DENIED ☒ GRANTED IN PART ☐ OTHER
3. CHECK IF APPROPRIATE: .... ☐ SETTLE ORDER ☐ SUBMIT ORDER
☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IA PART 39

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ISLAND GLOBAL YACHTING ACQUISITION LTD.,

Plaintiff,

v.

REUBEN HOPPENSTEIN and OHAVTA, LLC
Defendants/Counterclaimants

v.

ISLAND GLOBAL YACHTING ACQUISITION LTD. AND ISLAND GLOBAL YACHTING LTD.

Counter-Defendants.

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DECISION/ORDER
Index No. 113020/09
Motion Seq. No. 003

BARBARA R. KAPNICK, J.:

This action involves the sale and purchase of a marina for mega-yachts located in Sint Maarten, Netherlands Antilles,[1] and a disputed post-transaction purchase price adjustment made pursuant to the parties' Share Purchase Agreement ("Purchase Agreement").

Background

The facts are taken from Plaintiff's Response to Defendants' Rule 19-A Statement/Plaintiff's Further Statement of Undisputed Facts, unless otherwise noted.

Prior to the transaction at issue, defendant Reuben

[1] Saint Martin is the English name for the whole island. Sint Maarten is the name of the Dutch territory.

Hoppenstein and Ohavta, LLC (collectively "Hoppenstein") owned Hop-Inn Enterprises, N.V. ("Hop-Inn"), a Netherlands Antilles company which held long lease rights to the land underlying the marina, located in Simpson Bay, Sint Maarten and commonly known as Isle de Sol (the "Marina"). The Marina was owned and operated by Hop-Inn's wholly-owned subsidiary, Yacht Club Isle de Sol, B.V. ("Isle de Sol") (Purchase Agreement, p. 1).

Hoppenstein and plaintiff Island Global Yachting Acquisition Ltd. ("Acquisition") entered into the Share Purchase Agreement, dated June 7, 2007, pursuant to which Acquisition agreed to purchase all of the outstanding equity in Hop-Inn for a purchase price of $30 million, subject to post-closing adjustment as provided therein (the "Purchase Price"). The transaction closed on June 22, 2007 (the "Closing Date"). (*Id.*, §2[a], p. 7).

Counter-defendant Island Global Yachting Ltd. ("IGY") is also a party to the Purchase Agreement only insofar as it absolutely and unconditionally guaranteed the performance of Acquisition's duties, obligations and responsibilities thereunder. (*Id.*, §10[o], p. 29).

Section 2(d)(i) of the Purchase Agreement provides that

> [w]ithin 30 days after the Closing Date, [Acquisition] will prepare and deliver to Hoppenstein a draft pro forma balance sheet (the "***Draft Closing Date Balance Sheet***") for Hop-Inn as of the close of business on the Closing

[* 4]

> Date (determined on a pro forma basis as though the Parties had not consummated the transactions contemplated by this Agreement [. . .]). [Acquisition] will prepare the Draft Closing Date Balance Sheet in accordance with GAAP applied on a basis consistent with the preparation of the Financial Statements.

(emphasis in original).

Section 2(e)(i) of the Purchase Agreement provides that

> [t]he Purchase Price shall be adjusted as follows based upon the Closing Date Balance Sheet:
>
> (i) If the net current assets of Hop-Inn exceed the net current liabilities of Hop-Inn (including a provision for accrued Taxes), [Acquisition] shall pay to Hoppenstein and Ohavta an amount equal to such excess by wire transfer or delivery of other immediately available funds within three business days after the date on which such amount for Hop-Inn finally is determined pursuant to §2(d) above.
>
> (ii) If the net current assets are less than the net current liabilities of Hop-Inn (including a provision for accrued Taxes), Hoppenstein and Ohavta shall pay to [Acquisition] an amount equal to such deficiency by wire transfer or delivery of other immediately available funds within three business days after the date on which such amount for Hop-Inn is finally determined pursuant to §2(d) above.

Section 6(g) of the Purchase Agreement provides as follows:

> *Taxes.* Hoppenstein and Ohavta shall be liable for all Taxes accruing for any pre-Closing period and [Acquisition] shall be liable for all Taxes accruing for any post Closing period. Hoppenstein and Ohavta shall indemnify, defend and hold harmless [Acquisition] for any Tax liability accruing prior to the Closing and [Acquisition] shall indemnify and hold harmless Hoppenstein and Ohavta for any Tax liability accruing after the Closing.

[* 5]

On or about July 25, 2007, Acquisition delivered to Hoppenstein an initial Draft Closing Date Balance Sheet (the "July 25 Draft Balance Sheet") which reflected an increase to the Purchase Price in the sum of $398,312.79. Hoppenstein formally objected[2] to the July 25 Draft Balance Sheet and, thus, on or about August 16, 2007, Acquisition delivered to Hoppenstein a revised Draft Closing Balance Sheet which reflected an increase of $509,303.98 to the Purchase Price("August 16 Revised Draft Balance Sheet"). On or about September 7, 2007, Acquisition delivered to Hoppenstein a further revised Draft Closing Date Balance Sheet which reflected an increase of $510,977.14 to the Purchase Price. ("September 7 Revised Draft Balance Sheet").

On September 20, 2007, Acquisition's Principal Accounting Officer involved in the Purchase Price Adjustment, Jan Cole ("Cole"), transmitted an email concerning Hop-Inn's profit tax[3] stating:

Based on Mike [Ragsdale]'s conversation with KPMG we do

[2] Section 2(d)(ii) of the Purchase Agreement provides the procedure to be followed in the event Hoppenstein has any objections to the Draft Closing Date Balance Sheet prepared by Acquisition.

[3] "Profit tax" in the Netherlands Antilles is akin to U.S. income tax. (Memo of Law in Support, fn 2, p.2). "Turnover tax," also at issue in this litigation, is akin to U.S. sales tax. (*Id.*, fn 3, p.3).

[* 6]

> not anticipate [fiscal year] 06/07 profit tax will be due but KPMG can not [sic] commit until the year end numbers have been provided to them. That is why we listed it on the schedule [to the Draft Closing Date Balance Sheet] at $-0- with a footnote.

On September 20, 2007, Acquisition delivered to Hoppenstein another revised Draft Closing Balance Sheet ("September 20 Revised Draft Balance Sheet"). The September 20 Revised Draft Balance Sheet incorporated a reduction of $162,000 as a turnover tax accrual purportedly for the results of a tax audit of Hop-Inn for the 2003-2006 fiscal years. It also reflected an increase to the Purchase Price of $347,303.98. With respect to profit tax liability for pre-Closing periods, the September 20 Revised Draft Balance Sheet provides:

> KPMG estimates the 06/07 fiscal tax profit to be $0...IGY will notify Hoppenstein within 90 days of filing the final 06/07 tax return if a liability exists and the portion relates to pre-closing. If any tax is due it shall be treated as a pre-closing liability as set forth in the tax indemnification section of the Purchase Agreement.

On or about October 5, 2007, Acquisition delivered a further revised Draft Closing Balance Sheet ("October 5 Revised Draft Balance Sheet") which reflected a liability for an aggregate profit tax of $476,668.22 purportedly for the portion of the 2007 fiscal year ending on the Closing Date.

[* 7]

According to defendants, the liability reflected in the October 5 Revised Draft Balance Sheet was allegedly based on a *pro forma* profit tax return KPMG prepared for Isle de Sol alone, and not as a fiscal unity with Hop-Inn as of the Closing Date. Defendants emphasize that no such amount, nor any accrual for profit taxes, appeared on any of the previous Draft Balance Sheets that Acquisition delivered to Hoppenstein. Plaintiff, on the other hand, asserts that the *pro forma* tax return prepared by KPMG reflected the taxes owed by both Hop-Inn and Isle de Sol. In particular, plaintiff points out that the October 5 Revised Draft Balance Sheet includes a page that calculates the taxes due by both entities.

Further defendants contend, and plaintiff admits, the tax return actually filed by Acquisition with the applicable tax authorities for Hop-Inn and Isle de Sol showed no profit tax due for fiscal year 2007. However, plaintiff argues that this fact is irrelevant for the reasons set forth in the November 18, 2011 affidavit of Stephen W. Shulman, CPA, ABV, CVA, CFF, FCPA ("Shulman"), discussed in detail below. The parties also agree that the 2007 tax return reflected the fiscal unity election Acquisition caused Hop-Inn and Isle de Sol to make effective beginning as of October 1, 2006 (i.e., the first day of the fiscal year during which the Closing occurred).

On or about October 29, 2008, Acquisition paid $540,175.87 to Hoppenstein as the amount which Acquisition calculated at the time to be the Purchase Price adjustment. Such payment included Acquisition's deduction of $476,668.22 attributable to the purported profit tax as set forth in the October 5 Revised Draft Balance Sheet.

Defendants assert that in or about late April 2009, consistent with section 2(d)(ii) of the Purchase Agreement, Hoppenstein sought advice from the parties' mutual tax advisor, KPMG, regarding what profit tax Hop-Inn owed as of the Closing Date.[4] In response, KPMG clarified that no profit tax would have been owed at the Closing Date if Hop-Inn, together with Isle de Sol as a fiscal unity, utilized all so-called fiscal facilities available to it. (5/2/09 email from Wendell Meriaan ["Meriaan"] of KPMG). Plaintiff, however, maintains that the information received by Hoppenstein is part of many pieces of advice given by KPMG, including KPMG's specific written advice as to taxes accrued as of the Closing Date. In particular, KPMG purportedly made clear that the use of accelerated depreciation only defers a tax - it does not eliminate

[4] KPMG had historically advised Hoppenstein with respect to tax matters and making the required tax filings for Hop-Inn (and Isle de Sol) prior to the closing of the sale of shares of Hop-Inn under the Purchase Agreement (the "Closing"). Following the Closing, KPMG also advised Acquisition with respect to such matters. (Belcher Affid., ¶ 3).

[* 9]

the tax liability that had accrued at the time of the Closing Date.

Acquisition delivered a final Revised Draft Closing Date Balance Sheet to Hoppenstein on April 24, 2009 ("Final Revised Draft Balance Sheet"). This Balance Sheet contains a line item for turnover taxes for pre-Closing periods of $122,732, purportedly reflecting the results of a turnover tax audit of Hop-Inn completed after the October 29, 2008 payment to Hoppenstein. Defendants assert that, of that $122,732 turnover tax amount, $40,170 was already included in the amount Acquisition paid Hoppenstein on October 29, 2008. Plaintiff denies that claim and insists instead that the Final Revised Draft Balance Sheet increases the liability from $40,170 to $122,732 and, as shown in the detail of that Balance Sheet, there was no double-counting.

The additional turnover tax payable on account of pre-Closing periods would reduce the profit of Hop-Inn subject to profit tax resulting in a reduction of the disputed profit tax liability for the portion of the 2007 fiscal year through the Closing Date from $476,668.22 to $426,997.42. The calculation resulting in the $59,353.13 which Acquisition demands in its third cause of action in the Amended Complaint incorporates Hoppenstein's purported liability for the turnover tax audit concluding that $122,732 was owed for Hop-Inn turnover tax on account of pre-Closing periods.

On October 12, 2010, about eighteen months after the date of the Final Draft Balance Sheet and while this case was pending, Acquisition issued a written demand to Hoppenstein for indemnification in the amount of Netherlands Antillean Guilder ("ANG") 200,007, as well as for Isle de Sol turnover tax on fuel and lubricants, the subject of a settlement Hoppenstein believed was jointly made by the parties to the St. Maarten Tax Authority (the "Tax Authority"). (Am. Compl., ¶¶ 26-30). Plaintiff, however, asserts that, by definition, its indemnification claims can only seek amounts which are in addition to amounts shown as liabilities on the Final Revised Draft Balance Sheet. In particular, the settlement that Hoppenstein believed was jointly made by the parties to the Tax Authority was only approved by the Tax Authority on November 16, 2011 and includes a penalty.[5] (Affirmation of Adam B. Gilbert in Support of Plaintiff's Cross-Motion for Partial Summary Judgment, Ex. 2 [11/16/11 Fax from Sint Maarten Tax

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[5] Following the parties' joint negotiation with the Tax Authority over its turnover tax on fuel and lubricants audit for fiscal years 2003 through 2009, Acquisition was to have made a settlement proposal to the Tax Authority to satisfy such tax liability for pre-Closing and post-Closing periods. That proposal contemplated a settlement payment of ANG 157,664, or $89,965, for turnover tax of Isle de Sol on account of pre-Closing periods. The parties agreed to dispute an associated penalty the Tax Authority had assessed. (Belcher Affid., Ex. F [2/2/10 Letter from Belcher]). The Tax Authority responded to Acquisition's settlement proposal on November 16, 2011, accepting the settlement amount but also imposing penalties covering all periods, including the pre-Closing period. The amount of the penalty for the pre-Closing period is ANG 23,648, or $13,242.88.

[* 11]

Department to Meriaan of KPMG]).

By letter dated October 29, 2010, Hoppenstein's counsel, responding to Acquisition's October 12 demand for indemnification, (i) confirmed Acquisition's and IGY's prior suggestion to incorporate the tax on fuel and lubricants into this litigation, (ii) expressed Hoppenstein's belief that Acquisition and IGY had already paid such Isle de Sol turnover tax on fuel and lubricants as well as their earlier determined Hop-Inn turnover tax, and (iii) notified Acquisition and IGY that under no circumstances would Hoppenstein be liable for additional monies incurred, such as interest, assessments or penalties, as a consequence of the delay in payments of the amounts.

Plaintiff filed a Complaint, dated November 30, 2009, and an Amended Complaint, dated December 7, 2010, asserting six causes of action seeking: (1) and (2) declaratory relief; (3) a money judgment against defendants in the same amount by which plaintiff overpaid defendants following all post-Closing adjustments; (4) a money judgment against defendants in the amount by which defendants underpaid turnover taxes during all periods pre-Closing; (5) a money judgment against defendants in the amount by which defendants underpaid taxes on fuels and lubricants during all periods pre-Closing; and (6) indemnification.

With respect to its first cause of action for declaratory relief, plaintiff seeks a declaration that (1) the Final Balance Sheet correctly presents an accrual for such taxes as required by the terms of the Purchase Agreement; and (2) there has been no underpayment in purchase price to defendants as a result of plaintiff's accrual for profit taxes for the period October 1, 2006 through June 22, 2007.

With respect to its second cause of action for declaratory relief, plaintiff seeks a declaration that (1) as of the Closing Date, defendants' operating entity did not have an additional asset in the form of a $100,000 deposit (the "Deposit") ; (2) the Deposit has been forfeited prior to the Closing Date; (3) the Closing Date Balance Sheet correctly excluded the Deposit as an asset; and (4) there has been no underpayment in the purchase price in the amount of $100,000.

Defendants/Counterclaimants filed an Answer to Amended Complaint and Counterclaim, dated December 27, 2010, asserting counterclaims for (1) breach of contract; (2) breach of contract[6]; and (3) promissory estoppel.

Defendants now move for summary judgment in their favor on the

[6] The parties have since resolved the second counterclaim.

first and third counterclaims asserted against plaintiff/counterclaim defendant Acquisition and counterclaim defendant IGY, and against plaintiff on all the claims asserted in the Amended Complaint.

Plaintiff cross-moves pursuant to CPLR 3212 for partial summary judgment dismissing defendants' third counterclaim for promissory estoppel.

Analysis

A party seeking summary judgment "must make a prima facie showing of entitlement to judgment as a matter of law, tendering sufficient evidence to eliminate any material issues of fact from the case." *Winegrad v. New York Univ. Med. Ctr.*, 64 NY2d 851, 853 (1985) (internal citation omitted). Once this showing is made, the burden shifts to the opposing party to produce evidentiary proof in admissible form sufficient to establish the existence of triable issues of fact. *Zuckerman v. City of New York*, 49 NY2d 557, 562 (1980). "[M]ere conclusions, expressions of hope or unsubstantiated allegations or assertions are insufficient" to defeat a summary judgment motion. *Id.* A motion for summary judgment must be denied if there is any doubt as to the existence of a triable issue of material fact. *Rotuba Extruders, Inc. v. Ceppos*, 46 NY2d 223, 231 (1978).

Promissory Estoppel

The Court will first consider the parties' motions as they relate to the third counterclaim for promissory estoppel asserted by defendants against Acquisition and IGY. Defendants allege in their Answer and Counterclaims that Acquisition, through its representatives and KPMG, expressly represented to Hoppenstein that no profit taxes were accrued, would become due, or ever were paid with respect to the Marina operations prior to the Closing Date. They further allege that they relied on these representations, including on Acquisition's filing of the 2007 tax return showing no profit taxes due and, as a result, have been injured in an amount of no less than $426,997.24 minus the amount actually paid for the fuel and lubricant turnover tax for pre-Closing periods. (Answer to Am. Compl. and Counterclaims, ¶¶ 39-41).

Defendants further assert in their reply memorandum submitted in support of their motion for summary judgment and in opposition to plaintiff's cross-motion for partial summary judgment that their claim for promissory estoppel is actually premised on that portion of the September 20 Draft Balance Sheet which provides that

> KPMG estimates the 06/07 fiscal profit tax to be $0.
>
> ...[Acquisition] will notify Hoppenstein within 90 days of filing the final 06/07 tax return if a liability exists and the portion relates to pre-closing. If any

> tax is due it shall be treated as a pre-closing liability as set forth in the tax indemnification section of the Purchase Agreement.
>
> * * *
>
> ...Any [turnover] tax due and payable for the time period prior to closing would be subject to the indemnification set forth in the Purchase Agreement.

Specifically, defendants allege that plaintiff failed to notify Hoppenstein within the requisite 90-day period that there was no profit tax liability reflected on the 2006/2007 tax return and that, instead, they found this information out directly from KPMG.[7] (Defendants' Memo in Reply/Opp., p. 7).

Plaintiff, however, argues that promissory estoppel cannot apply here by virtue of the parties' written Purchase Agreement. Moreover, it insists that any representations made pre-Closing were merged into that Agreement.[8] In any event, plaintiff claims that

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[7] They further argue that since there was no actual liability for profit tax on account of pre-Closing periods, there was nothing for which indemnification was required. (Defendants' Memo in Reply/Opp., p. 7).

[8] The Purchase Agreement contains a merger clause in Section 10(d)(the "Merger Clause") which provides that

> this Agreement (including the documents referred to herein) and the confidentiality agreement previously executed by the Parties (or their representatives) constitutes the entire agreement among the Parties and supersedes any prior understandings, agreements, or representations, including without limitation that certain Contribution Agreement, written or oral, to the extent they relate in any way to the subject matter

defendants cannot prove any of the elements of promissory estoppel for a number of reasons. First, it argues that a party's provisional statements regarding estimates or possible positions to be taken in the future cannot sustain a claim of promissory estoppel, *citing Johnson & Johnson v. American Nat'l Red Cross*, 528 F.Supp.2d 462, 464 (SDNY 2008)(defendant's oral and written statements to the U.S. Congress that it had not engaged in commercial ventures for profit, nor had any intention of doing so, was not clear and unambiguous promise that it would never engage in such a venture "for the indefinite future"). Second, plaintiff argues that it was contractually obligated to accrue taxes under the express language of Section 2(e) of the Purchase Agreement. *See Leff v. TIAA-CREF Life Ins. Co.*, 81 AD3d 422, 422-23 (1st Dep't 2011)(holding that it was unreasonable for plaintiff to rely on alleged promise that was in clear violation of the contract that was already in his possession); *DDCLAB Ltd. v. E.I. du Pont de Nemours & Co.*, 2005 WL 425495, *18 (SDNY 2005)(promissory estoppel cannot be applied to create "obligations inconsistent with the terms of a contract"). Third, given the Purchase Agreement's Merger Clause and No Waiver Clause[9], plaintiff argues that the

hereof.

[9] Section 10(j) of the Purchase Agreement provides as follows:

> *Amendments and Waivers.* No amendment of any provision of this Agreement shall be valid unless the same shall be in

[* 17]

defendants could not have justifiably relied on any purported representations as a matter of law. Finally, plaintiff asserts that the defendants cannot point to any actions that they took in detrimental reliance that are "unequivocally referable" to any alleged promise by plaintiff. [Plaintiff's Memo in Opp/Support, pp. 8-11].

The Court agrees with plaintiff that defendants' counterclaim for promissory estoppel is barred due to the existence of the parties' explicit, written Purchase Agreement. "Because it is a quasi-contractual claim,...promissory estoppel generally applies only in the absence of a valid and enforceable contract." *Kwon v. Yun*, 606 F.Supp.2d 344, 368 (SDNY 2009)(applying New York law); *Clark-Fitzpatrick, Inc. v. Long Island R.R. Co.*, 70 NY2d 382, 388 (1987)("The existence of a valid and enforceable written contract governing a particular subject matter ordinarily precludes recovery in quasi contract for events arising out of the same subject matter. A 'quasi contract' only applies in the absence of an express agreement, and is not really a contract at all, but rather a legal obligation imposed in order to prevent a party's unjust

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writing and signed by [Acquisition] and Hoppenstein and Ohavta. No waiver by any Party of any provision of this Agreement or any default, misrepresentation, or breach of warranty or covenant hereunder, whether intentional or not, shall be valid unless the same shall be in writing and signed by the Party making such waiver..."

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enrichment." [internal citations omitted]). Defendants do not dispute the validity of the parties' express, written Purchase Agreement with its Merger and Waiver Clauses. Thus, the Court grants plaintiff's cross-motion for partial summary judgment dismissing defendants' third counterclaim for promissory estoppel, and denies that portion of defendants' motion seeking summary judgment on this counterclaim.

Remaining Claims

The parties' remaining dispute concerns the amount of the provision for accrued tax liabilities and the related tax expense as of June 22, 2007 that needed to be included in the Final Balance Sheet. Defendants believe that no provision for a tax expense or accrued tax liability should be included on the June 22, 2007 Balance Sheet, because no taxes were subsequently paid by Hop-Inn when it filed its profit tax return for the fiscal year ending September 30, 2007. In particular, defendants contend that the filing by Hop-Inn of its September 30, 2007 profit tax return on a consolidated basis (that is, that treated Hop-Inn and Isle de Sol as one fiscal unit as a result of an election that was made after June 22, 2007) had the effect of eliminating any provision for accrued tax liabilities from the June 22, 2007 Balance Sheet. Moreover, defendants insist that such election was the reason that Hop-Inn had no tax due on the September 30, 2007 profit tax return, and that the election took effect retroactively on October 1, 2006 (before the Closing Date). Thus, defendants claim that there were no tax liabilities (or expenses) as of June 22, 2007 to report on the Draft Closing Balance Sheet. (9/6/11 Affid. of Leonard Weinstock, CPA ["Weinstock"] in support of defendants' motion, ¶ 19; 11/18/11 Shulman Affid. in opposition to defendants' motion and in support of plaintiff's cross-motion, ¶ 12).

Conversely, plaintiff believes that a provision for accrued tax liabilities must be reported on the Draft Closing Balance Sheet calculated and based on (a) the current years' profit before taxes through June 22, 2007 as reported in Hop-Inn's financial statements[10] and (b) any liabilities and deferred assets that may be carried forward from the previous year. Plaintiff argues that such provision may not be based upon Hop-Inn's tax returns and that taxes had in fact accrued as of June 22, 2007, and were legitimate liabilities of defendants as of that date. (Shulman Affid., ¶ 13).

Plaintiff further contends that the "fiscal unity," or consolidated tax return, election did not directly result in the elimination of tax liabilities reported on Hop-Inn's 2007 consolidated return for any profit that had accrued through June

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[10] Plaintiff asserts that before any adjustment for the tax expense, deferred tax assets and tax liabilities are to be made for the current year's activities. (Shulman Affid., fn 6, p. 5).

22, 2007. Rather, the elimination of the tax liability arose from losses from operations post-Closing and from the accelerated depreciation deducted on the tax return generated primarily at the parent company level. Plaintiff argues that since defendants did not fund the capital outlay to finance the post-Closing operating expenses, they have no right to claim any portion of the benefit. In addition, the accelerated depreciation deducted on the tax return (and which never appeared in any pre-Closing Hop-Inn or Isle de Sol financial statements) created a deferred tax liability to be paid by Acquisition after the Closing Date. (Shulman Affid., ¶ 14).

The parties' dispute turns on the meaning of the applicable language found in the Purchase Agreement, and in particular the terms "*pro forma*" and "in accordance with GAAP" as used therein. The defendants submit two affidavits from Weinstock, one dated September 6, 2011 ("Weinstock Affid. in Support") and another dated December 13, 2011 ("Weinstock Affid. in Reply"), in which Weinstock opines with respect to the meaning of the term "pro forma," as used in Section 2(d)(i) of the Purchase Agreement, that

> [w]hile for financial statement purposes the word "pro forma" is usually taken to mean to give effect in the current historical financial statements to a transaction having occurred or expected to occur at a later date...in this instance the language in the Purchase Agreement has the exact opposite effect, since it specifically states "determined on a pro forma basis as though the parties

> had not consummated the transactions contemplated by this Agreement..." Accordingly, the Purchase Agreement has clearly defined pro forma to mean an on-going, continuing business as if no sale transaction contemplated by the Agreement was occurring.

(Weinstock Affid. in Support, ¶ 12). As such, Weinstock concludes that the Final Closing Balance Sheet "should have been prepared from the perspective of an interim financial statement (i.e., one that is for a part of the ongoing fiscal year, rather than one as if the entity's fiscal year was ending on the Closing Date)." (*Id.*, ¶ 13).

In support of its cross-motion for partial summary judgment, Acquisition submits the Shulman Affidavit, dated November 18, 2011, in which he asserts that nothing within section 2(d) of the Purchase Agreement calls for the parties to prepare an interim financial statement, as Weinstock suggests. Shulman claims that if the parties had intended as much, they certainly could have said so in the Purchase Agreement. (Shulman Affid., ¶ 23). Moreover, in Shulman's view, from the standpoint of an accountant, the phrase identified by Weinstock instructs the accountant to prepare a pro forma balance sheet which excludes transaction costs, matches costs and expenses related to the operation of Hop-Inn as of June 22, 2007, and recognizes that - for several purposes, including tax purposes - there are two significant periods, namely, the period of ownership by the seller, and the period of ownership by the buyer.

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(*Id.*, ¶ 31).

Shulman further states that by ignoring the requirement that the parties were to agree upon a pro forma financial statement prepared in accordance with GAAP and, rather, concluding that GAAP standards for interim financial statements apply, Weinstock gives Hoppenstein tax benefits that rightly were the result of Acquisition's invested capital that it contributed after the Closing Date. (*Id.*, ¶ 32).

Weinstock rejects what he considers to be Shulman's incorrect belief that the words "interim" and "pro forma" share an either/or relationship as if they are mutually exclusive. (Weinstock Affid. in Repy, ¶ 4). Weinstock states that "[a]n interim financial statement is one prepared for only part of an entity's year, while a pro forma statement is intended to be based on certain assumptions, as stated therein. Thus, it is possible to have a pro forma statement prepared for an interim period." (*Id.*, ¶ 7).

In any event, Weinstock admits that "there is no actual definition of 'pro forma' contained within the glossary of terms in the [Financial Accounting Standards Board ("FASB")] Codification," (Weinstock Affid. in Reply, ¶ 5), and that the "absence of an authoritative definition of the word pro forma" was confirmed to

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him by "staff members at both the FASB and the American Institute of Certified Public Accountants." (*Id.*, fn 1, p. 2). Indeed, defendants concede that "pro forma" is "a term which really both sides' experts acknowledge requires further explanation to be meaningful."[11] (Defendants' Memo in Reply/Opp to cross-motion, p. 4).

In addition, while section 2(d)(i) of the Purchase Agreement provides that Acquisition "will prepare the Draft Closing Balance Sheet in accordance with GAAP applied on a basis consistent with the preparation of the Financial Statements," the parties also disagree over what, specifically, GAAP mandates.

> Accountants long have recognized that "generally accepted accounting principles" are far from being a canonical set of rules that will ensure identical accounting treatment of identical transactions. "Generally accepted accounting principles," rather, tolerate a range of "reasonable" treatments, leaving the choice among alternatives to management.

Thor Power Tool Co. v. Comm'r, 439 US 522, 544 (1979).

> GAAP encompasses the conventions, rules, and procedures that define accepted accounting practice at a particular point in time. GAAP changes and, even at any one point,

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[11] In addition, plaintiff argues that the interpretation of each of the accounting terms and phrases found in the purchase price adjustment clause of the Purchase Agreement is subject to good faith disagreement among experts. (Plaintiff's Reply Memo, p. 3).

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> is often indeterminate. The determination that a particular accounting principle is generally accepted may be difficult because no single source exists for all principles. There are 19 different GAAP sources, any number of which might present conflicting treatments of a particular accounting question. When such conflicts arise, the accountant is directed to consult an elaborate hierarchy of GAAP sources to determine which treatment to follow.

Shalala v. Guernsey Memorial Hosp., 514 US 87, 101 (1995)(internal citations and quotation marks omitted). Thus, in seeking to comply with GAAP, "an ethical, reasonably diligent accountant may choose to apply any of a variety of acceptable accounting procedures when that accountant prepares a financial statement." *Lovelace v. Software Spectrum Inc.*, 78 F3d 1015, 1021 (5th Cir. 1996). Moreover, these "flexible accounting concepts 'do not always (or perhaps ever) yield a single correct figure.'" *SEC v. Todd*, 642 F3d 1207, 1216 (9th Cir. 2011).

Here, Weinstock asserts in his affidavits submitted on behalf of defendants that, in the United States, GAAP is determined principally through the various pronouncements of the FASB and certain of its predecessor organizations. These pronouncements purportedly have been codified into one authoritative source, but the rules for interim financial statements and interim tax accruals, as now codified, are "quite similar" to those in effect in 2007. (Weinstock Affid. in Support, ¶ 15). Further, in June 2007, GAAP for interim income tax accruals was set forth in FASB

Interpretation No. 18 "Accounting for Income Taxes in Interim Periods (an Interpretation of APB Opinion No. 28)" ("FIN 18"), now known under the FASB codification as ASC 740-270. As defendants read that rule, tax expense or benefit for an interim period is to be computed based on the income or loss for that period at an estimated annual effective tax rate (citing ¶ 6, FIN 18). (*Id.*, ¶¶ 16-17).

Moreover, the determination of the estimated annual effective tax rate is addressed in paragraph 8 of FIN 18, which provides that the rate "should reflect anticipated investment tax credits, foreign tax rates, percentage depletion, capital gains rates, and other available tax planning alternatives." Paragraph 8 further provides that in some cases the rate will be the statutory rate modified as may be appropriate in the particular circumstances. In other cases, the rate will be the enterprise's estimated tax (or benefit) that will be provided for the fiscal year, stated as a percentage of its estimated "ordinary" income (or loss) for the fiscal year. (Weinstock Affid. in Support, ¶ 18).

Weinstock concludes that it was evident when the Balance Sheet was prepared that Hop-Inn and its subsidiaries could avoid all profit tax payments for the year by filing a fiscal unity election. Thus, he maintains that it is moot whether such election was physically made at that time, because the "other available tax planning alternatives" condition under paragraph 8 of FIN 18 was met. Moreover, Weinstock concludes that when the Balance Sheet was prepared, the documentation clearly showed that no profit tax accrual should have been recorded therein, since the then-annual effective tax rate estimated by KPMG was zero, based on the election of fiscal unity. (Weinstock Affid. in Support, ¶ 19).

Weinstock also asserts that plaintiff's reference to the pro forma tax return for the period October 1, 2006 through the Closing Date on June 22, 2007, prepared by KMPG, should have no effect on the determination of a tax accrual under GAAP because plaintiff admits that it is only based on the results for part of the year, as if that were the period for the filing of the tax return, while the reference to "pro forma" in the Purchase Agreement specifically states "as though the Parties had not consummated the transaction." (Weinstock Affid. in Support, ¶ 21).

In sum, Weinstock asserts that the inclusion of the $426,997.24 liability for the Netherlands Antilles Profit Tax in the Balance Sheet was not in accordance with GAAP, nor was it determined on a basis consistent with the Financial Statements referred to in the Purchase Agreement. Based on the language in the Purchase Agreement, the Balance Sheet was to be prepared for an ongoing entity, which would make it an interim financial statement based on that entity's normal fiscal year end. GAAP for interim income taxes is based on the expected annual effective rate for the entity's full year and allows for consideration of available tax planning alternatives. Here, the record indicates that at the time the Balance Sheet was prepared the parties clearly understood, or should have understood, that by taking advantage of the fiscal unity filing election, the effective profits tax for the year would be zero. Therefore, according to Weinstock, no profits tax liability should have been included in the Balance Sheet under the terms of the Purchase Agreement. (Weinstock Affid. in Support, ¶ 26).

In contrast, Shulman opines on behalf of plaintiff that GAAP requires the recognition of the tax liabilities on profit before taxes produced during the reporting period, as reported on the financial statements - without giving effect to losses in operations post-Closing and the recognition of deferred tax liabilities that defer, and do not eliminate, a present tax burden. (Shulman Affid., ¶ 15 [citing ASC 740-10-30-1]). He insists that GAAP does not intend for a financial statement to ignore deferred tax liabilities when calculating the tax liabilities of a current period. (*Id.*, ¶ 36). Shulman further contends that Weinstock's application of GAAP for interim financial statements is incorrect

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and directly contrary to what GAAP dictates. Critically, under Weinstock's interpretation, economic benefits that are created by and for the new owners after the Closing Date accrue to the benefit of the old owners. According to Shulman, Acquisition will ultimately have to pay a profit tax on the earnings that had been earned prior to the Closing Date that were sheltered by accelerated depreciation. Similarly, Acquisition will lose all tax benefits associated with the losses it incurred after June 22, 2007. (*Id.*, ¶¶ 19-20).

Finally, Shulman asserts that GAAP requires that benefits from net operating losses be recorded in a company's financial statements as a deferred tax asset when the company knows they can be utilized in the future. (*Id.*, ¶ 51 [citing ASC 740-30-5(c)]).

In submitting the foregoing conflicting opinions of their respective experts, the parties are, in effect, asking this Court to determine within its finite knowledge of accounting concepts, the credibility of such experts as a matter of law. It is, however, established that conflicting expert opinions raise issues of fact, (*Frobose v. Weiner*, 19 AD3d 258 [1st Dep't 2005]), and "[w]hen experts offer conflicting opinions, a credibility question is presented requiring a jury's resolution." *Shields v. Baktidy*, 11 AD3d 671, 672 (2d Dep't 2004)(denying summary judgment); *see* *also Gleeson-Casey v. Otis Elevator Co.*, 268 AD2d 406, 407 (2d Dep't 2000)(finding that since the weight to be afforded the conflicting testimony of experts is a matter within the province of the jury, the denial of summary judgment was proper). It is, therefore, this Court's opinion that defendants' motion for summary judgment on the first three causes of action must be denied. The experts will need to testify during trial, be subjected to the usual vigorous cross-examination of opposing counsel and let the fact finder decide, as a question of fact, which of the experts it believes presents a more credible picture of the applicable accounting principles and their effect as applied to the parties' transaction.

Finally, defendants seek summary judgment in their favor on plaintiff's fourth, fifth and sixth causes of action because they argue such claims are brought prematurely and unnecessarily. (Memo in Support, pp. 14-15). They contend that in order for Acquisition to recover damages from Hoppenstein it must have incurred them. However, during discovery in this case, Acquisition attested under oath that the amounts it seeks have "not yet been finally quantified." (*Id.*, citing Ex. 2 to Affidavit of David M. Belcher ["Belcher"] in Support [Resp. to Interrog. No. 3]).

Plaintiff argues that "[w]hile technically an action for indemnification does not arise until a party has been forced to pay damages that were caused by someone else, New York law permits the party seeking indemnification to commence an action prematurely, so that all claims can be tried and resolved in a single proceeding." *St. Nicholas Cathedral of the Russian Orthodox Church in North Am. v. Colonial Coop. Ins. Co.*, 19 Misc.3d 1108(A), *3 (Sup Ct, NY Co 2008).

Plaintiff emphasizes that the Tax Inspector of St. Maarten has demanded payments from Hop-Inn or Isle de Sol representing amounts it claims are owing, including for pre-Closing periods. In fact, on November 16, 2011, the amount in dispute in the fifth cause of action was finally determined by the St. Maarten Tax Authority. It argues that the liabilities at issue are real and that an actual dispute exists here that is ripe for adjudication - even if the exact amount of damages remains unknown, *citing ECOR Solutions, Inc. v. Malcolm Pirnie, Inc.*, 2005 WL 1843253 (NDNY 2005); *H.P.S. Mgt. Co. v. St. Paul Surplus Lines Ins. Co.*, 2011 WL 2182597 (Sup Ct, Nassau Co 2011), *aff'd,* 101 AD3d 1081 (2d Dep't 2012).

It would be inappropriate at this stage to grant defendants' motion based on the foregoing arguments as to damages. Whether and to what extent either party was injured here will become clear once the remaining factual questions are elucidated at trial.

Accordingly, for all the foregoing reasons, defendants' motion for summary judgment in their favor on the first and third counterclaims, and against plaintiff on all its claims asserted in the Amended Complaint is denied. Plaintiff's cross-motion for partial summary judgment seeking to dismiss defendants' third counterclaim is granted.

The parties are directed to file a Note of Issue forthwith. Counsel are then directed to appear for a pre-trial conference in IA Part 39, 60 Centre St., Rm. 208 on August 14, 2013 at 10:00 prepared to select a trial date.

This constitutes the decision and order of this Court.

Date: June 25, 2013

Barbara R. Kapnick
J.S.C.

BARBARA R. KAPNICK
J.S.C.