SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 49

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DB U.S. FINANCIAL MARKETS HOLDING CORP.,

Plaintiff,

-against-

BRUCE S. GELB, ROBERT M. KAUFMAN, as Co-Executor under the Will of Richard L. Gelb, Deceased, PHYLLIS N. GELB as Co-Executor, Co-Trustee, and Beneficiary under the Will and Testamentary Trusts of Richard L. Gelb, Deceased, and MITCHELL M. GASWIRTH as Co-Trustee under the Will of Richard L. Gelb, Deceased,

Defendants.

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DECISION AND ORDER
Motion Sequence No.: 001

Index No. 650906/2013

O. PETER SHERWOOD, J.:

This is an action for breach of the indemnification provision of a contract. Pursuant to a stock purchase agreement dated February 25, 2000 ("Purchase Agreement") (the Stock Purchase Agreement, attached as Exhibit 2 to the Harwood Affirmation ["Harwood Aff., Ex__"], NYSECF Doc. No. 9), plaintiff DB U.S. Financial Markets Holding Corp. ("Plaintiff"), an indirect, wholly-owned subsidiary of Deutsche Bank AG, purchased the capital stock of Charter Corporation ("Charter") from defendants Bruce S. Gelb and Richard L. Gelb (the "Gelbs" or "Defendants"). The Purchase Agreement required Defendants to indemnify Plaintiff for certain taxes arising from the transaction. The IRS later issued a notice of deficiency to Charter for the taxable period ended March 13, 2000, seeking a total of $71,623,783.60 in taxes and penalties. After Defendants declined to assume the defense against the IRS assessment, Plaintiff litigated with the IRS for over three years, and ultimately reached a settlement for the principal amount of $3,153,976.00. On April 20, 2009, Plaintiff paid the U.S. Treasury $6,075,474.13, representing the settlement amount plus interest from the deficiency date though the payment date. Plaintiff then brought this action, alleging a single cause of action for breach of the indemnification provision of the Purchase Agreement, and seeking to compel Defendants to pay the settlement amount plus interest, as well as Plaintiff's litigation costs and expenses.

Defendants now move, pursuant to CPLR 3211 (a) (1) and (a) (7), to dismiss the complaint for failure to state a cause a cause of action, and based on documentary evidence.

For the reasons set forth below, the motion to dismiss the complaint is denied.

FACTS

The following facts are drawn from the complaint (and assumed to be true for the purposes of this motion) and from the documentary evidence that is cited and incorporated by reference in the complaint.

Charter was a personal holding company jointly owned by the Gelbs (Complaint, ¶ 27 , NYSECF Doc. No. 2). Charter's primary asset was approximately 1% of the outstanding shares of Bristol-Myers Squibb Company (the BMY Stock) (*id.*). Charter also owned a variety of other investments (*id.*).

On March 13, 2000, pursuant to the Purchase Agreement (Harwood Aff, Ex 2, NYSECF Doc. No. 9) and various other related agreements, Plaintiff acquired Charter by purchasing all of its capital stock from the Gelbs (Harwood Aff., ¶ 30, NYSECF Doc. No. 7). In section 2.2 of the Purchase Agreement, Plaintiff agreed to buy all of Charter's stock at a price based on the "Current Market Value" of the BMY Stock, and the aggregate value of the "Other Assets" listed on schedule 2.2 (b) of the Purchase Agreement that Charter would still own at the time of the closing. At the time of the Purchase Agreement, the "Other Assets" consisted of interests in two investment funds.

Thus, pursuant to the Purchase Agreement, the parties agreed that Plaintiff would acquire all of Charter's stock at closing, but that Charter would own only the BMY Stock and the Other Assets listed on schedule 2.2 (b) as of the closing date (*see* Purchase Agreement, § 2.2 [the BMY Stock "together with the Other Assets, will be the only properties and assets owned by the Company at the Closing"]; § 3.16 ["At the Closing, the Company will not own, directly or indirectly, any Investment other than the Securities and the Other Assets"]). The Gelbs were obligated, prior to the closing, to cause Charter to transfer or distribute all of its other properties and assets so that Plaintiff was purchasing only the BMY Stock and the Other Assets listed on schedule 2.2 (b) (*id.*, § 5.6).

The Purchase Agreement also provides that Plaintiff and the Gelbs are obligated to indemnify each other in the event that certain tax liabilities should arise in the future (*id.*, §§ 9.2 [f], 9.4 [e]). The respective indemnification obligations of the parties for Charter's tax liabilities are based on

whether the transaction incurring the tax liability occurred before or after the Closing (*id.*). Plaintiff agreed to indemnify the Gelbs for:

> "any Taxes of the Company that become due as a result of the sale of any Securities or Other Assets by the Company on or after the transfer of Shares to Purchaser at the Closing"

(*id.*, ¶ 9.4[e]). Similarly, the Gelbs agreed to indemnify Plaintiff for:

> "any Seller Taxes attributable to the pre-Closing restructuring of the Company or any pre-Closing transfer or distribution of the Company's assets or liabilities, and any Seller Taxes determined to be owing as a result of any audit or other agreement with the IRS"

(*id.*, § 9.2 [f]).

Thus, Plaintiff, as purchaser, was responsible for any taxes arising from actions it took to sell the BMY Stock or the Other Assets after it closed on the purchase of Charter, and the Gelbs were responsible for certain Seller Taxes that arose out of events that occurred while the Gelbs still owned the company.

The Gelbs' duty to indemnify was limited by the full definition of "Seller Taxes," which began:

> "'Seller Taxes' means any and all Taxes of the Company and the Subsidiaries, including those attributable to any pre-Closing restructuring of the Company or any pre-closing transfer or distribution of the Company's assets or liabilities (including transactions consummated pursuant to Section 5.6 hereof), for (i) any period ending on or prior to the Closing Date, or (ii) any period beginning prior to the Closing Date and ending after the Closing Date, to the extent of the Tax that would have been payable for such period had such period ended on the Closing Date"

(*id.*, § 1.1). The definition of "Seller Taxes" went on to exclude all taxes that resulted from any action by the Purchaser or Charter after the closing, and it particularly excluded any taxes that might arise out of the sale of the Other Assets:

> "Seller Taxes shall not include (i) any Taxes that may become due as a result of any action by Purchaser or the Company after the Closing (including, without limitation, the sale or other transfer of Securities or Other Assets by the Company) or (ii) any other Taxes that are attributable to Purchaser or the Company for any period beginning on or after the Closing Date as a result of, or in connection with, any transaction, including any transfer or distribution of the Company's assets or

liabilities, that occurs after the transfer of the Shares to Purchaser pursuant hereto" (*id.*).

The Purchase Agreement further provided that "matters that relate to Seller Taxes are within the scope of and subject to indemnification by the Selling Shareholders" (9.7 [b]). The Purchase Agreement gave the Gelbs the right, "at their option and expense, to assume . . . the defense of any audits relating to Seller Taxes (*id.*). It provided that if the Gelbs "fail[ed] to assume the defense of any such audits," they would be "bound by any determination made in such audits or any compromise or settlement effected by" Plaintiff (*id.*).

Prior to the closing, Charter, the Gelbs, and Plaintiff executed the "First Amendment" to the Purchase Agreement (Complaint, ¶ 33; Harwood Aff., Ex. 3, NYSECF Doc. No. 10). The First Amendment expanded the definition of the "Other Assets" to include two additional assets (First Amendment, § 1.4, schedule 2.2 [b]).

At the time that it entered into the Purchase Agreement, Plaintiff's main interest was the BMY Stock, and not the Other Assets. Thus, at the closing, the parties simultaneously executed a put and call agreement (the "Put and Call Agreement") (Complaint, ¶ 35; Harwood Aff., Ex. 4, NYSECF Doc. No. 11), that provided a mechanism for return of the Other Assets to the Gelbs. The Put and Call Agreement gave Charter "[a]t any time and from time to time on or prior to September 13, 2000 (the 'Put Option Period') . . . the right (each a 'Put Option') to require" the Gelbs to purchase "one or more of" the Other Assets (Put and Call Agreement, § 1.1). If Charter did not exercise its Put Option rights for any or all of the Other Assets by the expiration of Charter's six-month Put Option Period, the Gelbs had a six-month "Call Option Period" during which they could require Charter to sell the Other Assets to them (*id.*, § 1.2).

Two months after the closing, on May 17, 2000, Plaintiff sold Charter's stock to BMY Trust (Complaint, ¶ 41). On May 18, 2000, Charter notified the Gelbs that it was exercising its Put Option to sell the Other Assets to the Gelbs (*id.*, ¶ 36). Pursuant to the terms of the Put and Call Agreement, Charter and the Gelbs executed an "Assignment Agreement," dated May 18, 2000 (Harwood Aff., Ex. 6, NYSECF Doc. No. 13), which provided that Charter Holding:

> "sells, transfers, and conveys to the Selling Shareholders, and the Selling Shareholders hereby purchase, all of the Company's right, title and interest in and to the [Other Assets] and all interest, dividends and distributions actually received by the Company with respect thereto on or after March 13, 2000"

(*id.*, ¶ 1).

The Assignment Agreement further provided that Charter "represents and warrants to the Selling Shareholders [that] the [Other] Assets are owned of record and beneficially by [Charter] free and clear of any Encumbrance" as of May 18, 2000 (*id.*, ¶ 2 [a]), and that Charter was also transferring "all interest, dividends or other distributions actually received by the Company with respect to its interest in such [Other] Assets from March 13, 2000 through and including the date hereof" (*id.*, ¶ 2 [d]).

More than three years later, on November 20, 2003, the IRS sent a notice of deficiency (IRS Notice) to Charter for the taxable period ending March 13, 2000 – the date on which the Gelbs' sale to plaintiff closed (Complaint, ¶ 42). The IRS claimed that Charter owed unpaid taxes of $59,758,570 for this period, and a penalty of $11,865,213.60 (*id.*). According to the IRS Notice, a portion of those taxes related to the Other Assets (*see id.*, ¶¶ 5-7).

By letter dated February 4, 2004, Plaintiff "notified the Gelbs of the IRS Notice and [asserted] that 'the Notice may result in an indemnification claim against the Selling Shareholders under Section 9.2 of the [Purchase] Agreement" (Harwood Aff., Ex. 7, NYSECF Doc. No. 14; *see also* Complaint, ¶ 44).

By letter dated February 5, 2004, the Gelbs' counsel denied any obligation to indemnify Plaintiff, stating that "[i]t appears that the deficiency and penalty referenced in the Notice are the result of the sale of any Securities or Other Assets by the Company on or after the transfer of Shares to Purchasers at the Closing and that they are not Seller Taxes" (Harwood Aff., Ex. 8, NYSECF Doc. No. 15; *see also* Complaint, ¶ 45).

By letter dated February 11, 2004, Plaintiff notified the Gelbs that it elected to assume the defense of the issues raised in the IRS Notice (Harwood Aff., Ex. 9, NYSECF Doc. No. 16; *see also* Complaint, ¶ 46). Plaintiff, on Charter's behalf, challenged the IRS Notice by filing a petition in the U.S. Tax Court on February 18, 2004 (Complaint, ¶ 47). Plaintiff litigated for more than three and

half years, and, on October 30, 2007, reached a preliminary settlement with the IRS (*id.*, ¶ 48). On November 8, 2007, the U.S. Tax Court entered a stipulated decision, finding an income tax deficiency due from Charter in the amount of $3,153,976, with no penalty, but with interest to accrue on the deficiency (the Settlement) (Complaint, ¶¶ 49, 53). The stipulated decision set forth no basis for the determination of the amount.

According to Plaintiff, the settlement was based on the IRS's determination that (1) $899,460 in legal and accounting expenses incurred for the taxable period ending with the closing should be disallowed; and (2) the Other Assets should be treated as having been constructively distributed by Charter to the Gelbs as of March 13, 2000 in conjunction with and immediately prior to the closing (*id.*, ¶ 48). As to the latter point, the Settlement assessed taxes on capital gains of $20 million for the Other Assets, discounted by 50% to reflect litigation risk (*id.*, ¶ 49). Plaintiff persuaded the IRS not to impose any penalty on the deficiency (*id.*).

Plaintiff notified the Gelbs of the settlement and informed the Gelbs that they were responsible for paying the full amount (*id.*, ¶ 50). In response, the Gelbs acknowledged that they were responsible for the disallowed-expense-related portion of the settlement, but denied responsibility for the rest (*id.*, ¶ 51).

On April 20, 2009, Plaintiff's parent company, on behalf of Plaintiff, paid the U.S. Treasury $6,075,474.13, fully satisfying the Settlement, which included $3,153,976 in income taxes plus $2,921,498.13 in interest through the date of payment (*id.*, ¶ 54).

Plaintiff informed Defendants of the payment to the U.S. Treasury resolving the deficiency notice and asked them for indemnification, and Defendants refused to comply (*id.*, ¶ 55). Plaintiff then brought this suit, which contains a single cause of action for indemnification, seeking payment for the full settlement amount paid to the IRS, as well as repayment for more than $869,000 in litigation costs and attorneys' fees, plus interest (*id.*, ¶ 61).

Defendants now seek to dismiss the complaint in its entirety on the ground that the settlement amount is not covered by the indemnity clause.

DISCUSSION

"The scope of a court's inquiry on a motion to dismiss under CPLR 3211 is narrowly circumscribed" (*P.T. Bank Cent. Asia, N.Y. Branch v ABN AMRO Bank N.V.*, 301 AD2d 373, 375 [1st Dept 2003]). Thus, on "a motion to dismiss pursuant to CPLR 3211, the pleading is to be afforded a liberal construction" (*Leon v Martinez*, 84 NY2d 83, 87 [1994]). The court "must accept as true the facts as alleged in the complaint and submissions in opposition to the motion, accord plaintiffs the benefit of every possible favorable inference and determine only whether the facts as alleged fit within any cognizable legal theory" (*Sokoloff v Harriman Estates Dev. Corp.*, 96 NY2d 409, 414 [2001]).

In order to prevail on a motion to dismiss based upon documentary evidence pursuant to CPLR 3211 (a) (1), the movant must demonstrate that the documentary evidence conclusively refutes the plaintiff's claims (*AG Capital Funding Partners, L.P. v State St. Bank & Trust Co.*, 5 NY3d 582, 590-591 [2005]; *see McCully v Jersey Partners, Inc.*, 60 AD3d 562, 562 [1st Dept 2009] [a motion to dismiss pursuant to CPLR CPLR 3211 (a) (1) "'may be appropriately granted only where the documentary evidence *utterly refutes* plaintiff's factual allegations, *conclusively establishing* a defense as a matter of law'"] [citation omitted, emphasis in original]).

With respect to a motion to dismiss for failure to state a cause of action under CPLR 3211 (a) (7), the court is not called upon to determine the truth of the allegations (*Campaign for Fiscal Equity v State of New York*, 86 NY2d 307, 317 [1995]). Rather, the "'criterion is whether the proponent of the pleading has a cause of action, not whether he has stated one'" (*Leon*, 84 NY2d at 88 [citation omitted]).

Defendants' motion to dismiss is denied, as they have failed to set forth documentary evidence that utterly refutes plaintiff's allegations, and Plaintiff has sufficiently pled its claim for breach of the indemnity provision of the Purchase Agreement.

In support of the motion to dismiss the complaint, Defendants contend that this action presents a simple question of contract interpretation, and that the plain language of the Purchase Agreement precludes indemnification for taxes arising out of Plaintiff's post-closing transfer of the Other Assets to the Gelbs. Defendants further argue that the Purchase Agreement imposes on Plaintiff the duty to pay "any Taxes of the Company that become due as a result of the sale of any

Securities or Other Assets by the Company on or after the transfer of the shares to Purchaser at the Closing (Purchase Agreement, § 9.4), and that Defendants' indemnification obligations do not include any taxes that result from any action by Plaintiff or Charter to sell the Other Assets after the Closing. It is undisputed that, two months after closing, Plaintiff exercised its Put Option to sell the Other Assets, the basis for the tax assessment. Defendants argue that, by definition, this was an action taken by Plaintiff after the closing and, therefore, the taxes that allegedly arose out of that sale are Plaintiff's obligations. Thus, Defendants contend, there can be no indemnification duty for that portion of the assessment, and no claim against Defendants.

Conversely, Plaintiff argues that the Complaint adequately alleges Defendants' liability for all of the taxes at issue in this action. Section 1.1 of the Purchase Agreement provides that Seller Taxes include "any and all Taxes . . . for . . . any period on or prior to the Closing Date" and section 9.2 makes Defendants liable for Seller Taxes. As the complaint alleges, the IRS's notice of deficiency was "for the taxable period ending March 13, 2000." Plaintiff argues that the IRS's claim was, therefore, for a period "ending on . . . the Closing Date," and thus was for Seller Taxes. Consequently, Plaintiff argues, the Gelbs are responsible for the taxes imposed for that period, and their liability does not arise from or depend on the reasons that the IRS and Plaintiff later settled the dispute between them. According to Plaintiff, the court need not examine the reasons that Plaintiff and the IRS agreed on in reaching a settlement; all it has to look at is the period for which the taxes were imposed.

A written agreement that is clear and complete on its face "must be enforced according to the plain meaning of its terms" (*Samuel v Druckman & Sinel, LLP*, 12 NY3d 205, 210 [2009]). Extrinsic evidence may be considered to discern the parties' intent only if the contract is ambiguous, and the intention of the parties cannot be gathered from the instrument itself (*Greenfield v Philles Records*, 98 NY2d 562, 569 [2002]). In determining whether an ambiguity exists, "'[t]he court should examine the entire contract and consider the relation of the parties and the circumstances under which it was executed. Particular words should be considered, not as if isolated from the context, but in the light of the obligation as a whole and the intention of the parties as manifested thereby'" (*Currier, McCabe & Assoc., Inc. v Maher*, 75 AD3d 889, 890-891 [3d Dept 2010], quoting

Atwater & Co. v Panama R.R. Co., 246 NY 519, 524 [1927], *accord Kass v Kass*, 91 NY2d 554, 566 [1998]).

The relevant terms of the Purchase Agreement are clear. Plaintiff is obligated to indemnify the Gelbs for "any Taxes of the Company that become due as a result of the sale of...Other Assets...on or after...the Closing" (Harwood Aff., Ex. 2, NYSECF Doc. No. 9). The Put and Call Agreement is dated as of March 13, 2000, which is the date of the Closing. Plaintiff acquired Charter stock at the same time. Plaintiff exercised the Put Option on May 18, 2000. Thus, whether the event that triggered the tax liability occured on March 13, 2000, as part of the sale of Charter stock, or on May 18, 2000, when the Put Option was exercised, Plaintiff is obligated to indemnify Defendants.

Plaintiff argues that even if the court were to determine that Defendant is entitled to be indemnified as to the capital gains taxes, the motion to dismiss must be denied because CPLR 3211 allows for dismissal of a cause of action, not parts thereof, and there remains an element of the sole cause of action that may not be dismissed (*see Lacks v Lacks*, 12 NY2d 268, 271 [1963]) ("if any portion of a cause of action is sufficient, it shall not be dismissed on [a] motion [to dismiss]").

Defendants concede that the deductions taken for legal and accounting expenses were incurred pre-Closing and that the IRS disallowance is attributable to them. Therefore, the Gelbs are obligated to indemnify Plaintiff in the amount of $899,460 plus interest paid by Plaintiff pursuant to the terms of the IRS settlement. The motion to dismiss is due to be denied because of this portion of the claim. However, there is no substantial dispute on this issue. Accordingly, summary judgment (upon proper notice) may be a vehicle for addressing the split claim issue *(see* CLPR 3211 [c]). The case shall be held in abeyance for 60 days from the date of this Decision and Order. If the parties are unable to agree on the amount (including interest) owed by Defendants within 30 days of the date of this Decision and Order, this aspect of the case shall be converted to a motion for summary judgment. In that event, the parties shall make simultaneous written submissions pursuant to CPLR 3211 (c) not later than 45 days after the date of this Decision and Order.

It is hereby;

ORDERED that counsel shall appear at a status conference on May 14, at 9:30 am at which time (or before) the parties shall advise the court whether there are any disputed facts requiring a

hearing under CPLR 3211(c).

This constitutes the decision and order of the court.

DATED: April 10, 2014

ENTER,

O. PETER SHERWOOD
J.S.C.