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

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LANTAU HOLDINGS LTD.,

Plaintiff,

- v -

GENERAL PACIFIC GROUP LTD., SVK CAPITAL MANAGEMENT, LTD., JOHN DOES 1 THROUGH 30, LANTAU HOLDINGS LLC, ROBERT MARINO

Defendants.

INDEX NO. 650085/2017

MOTION DATE N/A

MOTION SEQ. NO. 011

DECISION AND ORDER

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HON. BARRY R. OSTRAGER:

The following e-filed documents, listed by NYSCEF document number (Motion 011) 363, 364, 365, 366, 367, 368, 369, 370, 371, 372, 373, 374, 375, 376, 377, 378, 379, 380, 381, 382, 383, 384, 385, 386, 387, 388, 389, 390, 391, 392, 393, 394, 395, 396, 397, 398, 399, 400, 401, 402, 403, 404, 405, 406, 407, 408, 409, 410, 411, 412, 413, 414, 415, 416, 417, 418, 419, 420, 421, 422, 423, 424, 425, 426, 427, 428, 429, 430, 431, 432, 434, 435, 436, 437, 438, 439, 440, 441

were read on this motion to/for JUDGMENT - SUMMARY

HON. BARRY R. OSTRAGER:

Defendant SVK Capital Management, Ltd. ("SVK") moves for summary judgment dismissing the two causes of action asserted by Plaintiff Lantau Holdings Ltd. ("Lantau") alleging breach of Control Agreements and declaratory judgment regarding an indemnification provision therein. On SVK's pre-answer motion to dismiss, this Court denied dismissal of Lantau's breach of contract claim, finding that the Control Agreements at issue were ambiguous as to SVK's due diligence obligations, if any. (*See* Decision & Order at 4 [NYSCEF Doc. 242]). The extrinsic evidence produced during discovery—and submitted in support and opposition to the instant motion—fails to definitively resolve the ambiguities in the Control Agreements. Rather, the various agreements, loan documents, internal SVK policies, and expert reports

opining on SVK's purported due diligence obligations, present triable issues of material fact that preclude summary judgment and necessitate a trial. For the reasons stated herein, SVK's motion for summary judgment is denied.

Background

The pertinent background of this case is discussed in detail in this Court's prior decision on SVK's motion to dismiss. *See id.* at 1-3. In brief, Lantau, as seller, and General Pacific Group Ltd. ("GPG") as buyer, agreed to the sale and purchase of certain shares in REX, a company publicly traded on the Hong Kong Stock Exchange. Lantau originally received the shares from non-parties Orient Equal International Group Limited ("OEI") and Huang Dongpo ("Dongpo" and, together with OEI, the "Borrowers") by way of two Loan Agreements executed on May 6, 2016. (*See* O'Donnell Aff. Exs. 9-10 [NYSCEF Docs. 375-76]). Also, on May 6, 2016, Lantau and SVK entered into two tri-party Control Agreements with OEI and Dongpo, respectively, which sought to establish and clarify SVK's role as custodial broker to the transaction. (*See* O'Donnell Aff. Exs. 21-22 [NYSCEF Docs. 387-88]). Additionally, SVK agreed to receive a substantial fee in exchange for its services as custodial broker.

The Borrowers represented to Lantau that the shares were freely tradeable and unrestricted. Lantau made the same representations to GPG pursuant to Stock Purchase Agreements executed by the two parties. (*See* Complaint Exs. A-B [NYSCEF Doc. 2-3]). Ultimately, the shares were not freely tradeable at the time Lantau sold them to GPG, but rather were subject to lock-up undertaking agreements with REX. Lantau had the shares transferred to GPG's account and GPG failed to pay for the shares. GPG's purported failure to pay for the shares it received from Lantau are the subject of Lantau's claims against GPG in this action.

Additionally, after Lantau's transfer of the shares to GPG's account, and after GPG commenced trading in the shares, REX obtained an ex parte order in Hong Kong enjoining any further trades in the shares.

Lantau's Second Amended Complaint alleges that SVK breached the Control Agreements by failing to perform various due diligence responsibilities to ensure that the shares at issue were unrestricted and freely tradeable at the time of the transaction. Lantau also seeks an order declaring that SVK has no right to indemnification from Lantau in connection with this dispute.

Arguments

SVK moves for summary judgment on Lantau's two remaining claims against SVK. First, SVK argues that there is no contractual basis for Lantau's assertion that SVK was obligated to investigate whether the Borrowers had agreed with REX to certain restrictions on the shares. Thus, SVK argues that the Control Agreements between Lantau and SVK, which were drafted entirely by Lantau, clearly show that SVK had no obligation to investigate whether the shares were the subject of lock-up restrictions.

Second, SVK argues that its obligations under applicable anti-money-laundering ("AML") or know-your-customer ("KYC") regulations did not require SVK to investigate whether there were *contractual* restrictions on the shares. Thus, SVK asserts that its AML and KYC obligations relate largely to due diligence as to potential criminal matters, and do not entail inquiry into possible contractual disputes between private parties. Further, SVK asserts that Lantau has adduced no evidence that SVK even violated potentially applicable AML or KYC requirements.

Finally, SVK asserts that the Control Agreements entitle SVK to complete indemnification from costs and expenses stemming from the transaction, absent SVK's own gross negligence or willful misconduct. Thus, SVK claims that it is entitled to be made whole for its costs in this litigation.

In opposition, Lantau argues that SVK failed to perform certain due diligence obligations that would have uncovered the existence of the lock-up undertaking agreements restricting the shares at issue. First, Lantau asserts that the extrinsic evidence that necessarily must be considered includes numerous other agreements between the parties, as well as expert opinions on industry custom and practice, that establish genuine disputes as to the level of due diligence SVK was required to perform and whether performance of such due diligence would have uncovered the restricted nature of the shares. Second, the issue of whether gross negligence or willful misconduct exists barring indemnification is necessarily one that must be left for trial and cannot be resolved by summary judgment.

Discussion

Summary judgment shall be granted pursuant to CPLR 3212(b) "if, upon all the papers and proof submitted, the cause of action or defense shall be established sufficiently to warrant the court as a matter of law in directing judgment in favor of any party." *Friends of Animals, Inc. v. Associated Fur Mfrs.*, 46 N.Y.2d 1065, 1067 (1979). However, "[i]t is well settled that summary judgment is a drastic remedy that should be employed only when there is no doubt as to the absence of triable issues." *Aguilar v. City of New York*, 162 A.D.3d 601, 601 (1st Dep't 2018). In deciding a motion for summary judgment, "[t]he court should accept as true the

evidence submitted by the opposing party and evidence of the movant that favors the opposing party" to determine whether a triable issue of fact exists. *Id.*

This Court previously found that SVK's precise due diligence obligations under the Control Agreements were unclear, precluding dismissal of Lantau's claims on a pre-answer motion to dismiss. (*See* Decision & Order at 4 [NYSCEF Doc. 242]). The Court referred to several, potentially conflicting, provisions in the Control Agreements that gave rise to ambiguities.

For instance, Section 1 of the Control Agreements provides that SVK will comply with all notifications it receives regarding the shares "provided that [SVK] considers that [SVK] is reasonably able to take such action and that doing so will be lawful without involving a significant risk of [SVK] or the Borrower contravening any applicable law or regulation." (O'Donnell Aff. Exs. 21-22 [NYSCEF Docs. 387-88]). Section 3 represents that SVK must "maintain[] the Account for Customer and [Lantau's] Loan transaction," and that SVK "does not know of any claim to or interest in the Account, except for claims and interests of the parties referred to in this agreement." *Id.* In deciding the 3211(a)(1) motion, this Court held that such provisions, when weighing every possible inference in favor of Lantau, could arguably provide for SVK to conduct certain due diligence necessary to "maintain" the Account or to "know of any claim to or interest in the Account."

Other provisions provide for a narrower interpretation of SVK's obligations under the Control Agreements. For instance, Section 6, entitled "Broker's Responsibility," states that the Control Agreement "does not create any obligation of [SVK] except for those expressly set forth in this agreement.... [SVK] may rely on, without inquiry, notices and communications it believes

given by the appropriate party." *Id.* Thus, Section 6 ostensibly contemplates SVK's limited obligations as custodial broker, with few, if any, due diligence responsibilities.

Therefore, certain provisions in the Control Agreements themselves give rise to a reasonable inference that SVK was obligated to conduct certain due diligence with respect to the shares at issue. However, certain other provisions in the Control Agreements seemingly limit SVK to a narrower, administrative role.

"The existence of ambiguity must be determined by examining the entire contract and considering the relation of the parties and the circumstances under which it was executed, with the wording to be considered in the light of the obligation as a whole and the intention of the parties as manifested thereby." *Perella Weinberg Partners LLC v. Kramer*, 153 A.D.3d 443, 446 (1st Dep't 2017) (internal quotations omitted).

Here, SVK's responsibilities as custodial broker under the Control Agreements is unclear, particularly when considering the full relationship of the parties and the circumstances under which the Control Agreements were executed. It cannot be seriously disputed that the Control Agreements were but one part of a larger contractual relationship between the parties regarding the transaction at issue. The Control Agreements themselves refer to a Loan Agreement, Springing Pledge Agreement, and a brokerage account that, necessarily, would have been created pursuant to some other, prior agreement. (*See* O'Donnell Aff. Exs. 21-22 [NYSCEF Docs. 387-88]). Given the unclear obligations of SVK under the Control Agreements, as well as the complicated contractual relationship of the parties with regard to the instant transaction, the Court must rely on extrinsic evidence to determine what, if any, SVK's due diligence responsibilities are under the Control Agreements.

The extrinsic evidence, however, fails to definitively clarify SVK's due diligence obligations and, instead, presents several triable issues of fact.

For instance, on February 10, 2015, Lantau opened its brokerage account with SVK pursuant to a Memorandum of Understanding ("MOU"). (*See* O'Donnell Aff. Ex. 2 [NYSCEF Doc. 368]). In the MOU, Lantau expressly attests that it is "relying exclusively on [Lantau's] own due diligences." *Id.* at 78. Thus, the MOU indicates that Lantau, and not SVK, was charged with the responsibility of conducting any necessary due diligence.

However, the MOU also acknowledges Lantau's reliance on "representations only expressly set forth in the 'Loan Agreement' and the 'Control Agreement.'" *Id.* The Loan Agreement between Lantau and the Borrowers contemplates certain responsibilities entrusted to SVK as custodial broker. The Loan Agreement provides that no action shall be taken on the shares until "Final Acceptance," which occurs when: "(a) [SVK] has confirmed to [Lantau] that (i) [Dongpo] has opened a professional client sub-account under the auspices of the prime account of [Lantau] at [SVK]; (ii) the Collateral has been delivered into such account and *resides there without restrictions*, and (b) [SVK] has confirmed compliance with the Patriot Act and anti-money laundering statutes." (*See* O'Donnell Aff. Exs. 9-10 [NYSCEF Docs. 375-76]) (emphasis added).

This provision arguably confers certain due diligence responsibilities on SVK to confirm that the shares have been properly transferred to the correct account free of restrictions. Further, the Loan Agreements explicitly reference the Control Agreements currently in dispute. And, while SVK was not a signatory to the Loan Agreements, SVK did receive copies of the Loan Agreements before the transaction was consummated. (*See* Cochrane Tr. at 152:19-154:23 [NYSCEF Doc. 418]). Ultimately, however, the extrinsic documentary evidence submitted in

connection with the instant motion fails to definitively clarify SVK's obligations under the Control Agreements.

The parties' competing expert reports similarly fail to clarify the Control Agreements. SVK's expert, William Meehan, opines that SVK was not required to perform due diligence on the shares because SVK "(1) did not have a discretionary or fiduciary relationship with Lantau, (2) did not explicitly contractually agree to perform due diligence in the shares, and (3) was not required to conduct such due diligence by regulation under broker dealer rules for maintaining accounts, accepting electronic book entry shares into an account, or the AML and KYC components of client-onboarding." (Meehan Expert Report at ¶ 40 [NYSCEF Doc. 383]). Specifically, Meehan asserts that SVK's obligation under the Control Agreements to "maintain" the brokerage account does not contain an implicit obligation to investigate restrictions on shares—as brokerage accounts can be "maintain[ed]" with both restricted and unrestricted shares. *Id.* at ¶ 33. Further, Meehan opines that SVK took reasonable steps to satisfy its AML and KYC onboarding requirements to identify and verify the parties to the transaction and the nature of their relationship. *Id.* at ¶ 27.

In contrast, Lantau's expert, Robert Almanas, opines that the Loan Agreements and Control Agreements required SVK to confirm that the shares resided in the accounts without any restrictions. (Almanas Expert Report at ¶¶ 63-66 [NYSCEF Doc. 389]). Importantly, Almanas also asserts that SVK failed to follow AML regulatory guidance and SVK's own AML policies which, if followed, would have uncovered the lock-up undertaking agreements restricting the shares. *Id.* at ¶ 71. However, SVK did not consider OEI and Dongpo to be high risk clients, and therefore never conducted enhanced due diligence. Thus, had SVK conducted such diligence consistent with regulatory requirements, and followed SVK's own internal procedures and

industry custom and practice, SVK would have discovered that the shares were restricted, and Lantau would not have agreed to the transaction. *Id.*

The evidentiary record presented on this motion for summary judgment is thus replete with issues of fact. "If there is ambiguity in the terminology used, [] and determination of the intent of the parties depends on the credibility of extrinsic evidence or on a choice among reasonable inferences to be drawn from extrinsic evidence, then such determination is to be made by the jury." *Hartford Acc. & Indem. Co. v. Wesolowski*, 33 N.Y.2d 169, 172 (1973). Here, the due diligence responsibilities of SVK under the Control Agreements are unclear and the extrinsic evidence submitted—including the Loan Agreements, MOU, and competing expert reports—fail to definitively clarify the intent of the parties such that summary judgment may be entered. These material issues must be resolved by a finder of fact during trial. Therefore, SVK's motion for summary judgment dismissing Lantau's breach of contract claim is denied.

Likewise, there exists a clear issue of material fact as to whether SVK's actions or inactions rose to the level of gross negligence or willful misconduct such that SVK would not be indemnified under Section 7 of the Control Agreements. It is unclear at this stage whether SVK even breached the Control Agreements, let alone whether such breach amounted to gross negligence or willful misconduct. *See Modern Settings v. American Dist. Tel. Co.*, 121 A.D.2d 266, 269 (1st Dep't 1986) ("Whether plaintiff can prove that A.D.T. deactivated the alarm system without notice, and whether this constituted 'gross negligence' and 'willful misconduct', must await a trial."). Therefore, SVK's motion for summary judgment dismissing Lantau's declaratory judgment claim is denied.

Accordingly, it is hereby

ORDERED that SVK's motion for summary judgment is denied in its entirety; and it is further

ORDERED that all parties in this matter appear for a pre-trial conference on October 5, 2018 at 9:30 a.m.

9/12/2018
DATE

BARRY R. OSTRAGER, J.S.C.

CHECK ONE:		CASE DISPOSED		X	NON-FINAL DISPOSITION		
		GRANTED	X DENIED		GRANTED IN PART		OTHER
APPLICATION:		SETTLE ORDER			SUBMIT ORDER		
CHECK IF APPROPRIATE:		INCLUDES TRANSFER/REASSIGN			FIDUCIARY APPOINTMENT		REFERENCE