Brown v Cerebus Capital Mgt., L.P.
2018 NY Slip Op 32782(U)
October 30, 2018
Supreme Court, New York County
Docket Number: 655271/2017
Judge: O. Peter Sherwood
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 49

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TONYA BROWN, JOHN ELSTAD, ALBERT GOEKEN, ELIZABETH HOMAN, and JEFFREY SAMPERE,

Plaintiffs,

-against-

CEREBUS CAPITAL MANAGEMENT, L.P., CEREBUS COVIS LLC, COVIS HOLDINGS GP LLC, COVIS HOLDINGS L.P., COVIS MANAGEMENT INVESTORS LLC, COVIS US HOLDINGS, LLC, COVIS MANAGEMENT INVESTORS US LLC, and COVIS PHARMACEUTICALS, INC.,

Defendants.

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DECISION AND ORDER
Index No. 655271/2017

Motion Sequence No.: 002

O. PETER SHERWOOD, J.:

Plaintiffs Tonya Brown, John Elstad, Albert Goeken, Elizabeth Homan, and Jeffrey Sampere bring this action against defendants Cerberus Capital Management, L.P. (Cerberus), Cerberus Covis LLC (Cerberus Covis), Covis Holdings GP LLC (Covis GP), Covis Holdings L.P. (Covis Holdings), Covis Management Investors LLC (MIP I), Covis US Holdings, LLC (US Holdco), Covis Management Investors US LLC (MIP II) and Covis Pharmaceuticals, Inc. (CPI and, collectively with Covis GP, Covis Holdings, MIP I, US Holdco, and MIP II, the Covis Enterprise). Plaintiffs are former mid-level managers of CPI who were granted incentive compensation by MIP II in the form of interests in the profits of the Covis Enterprise. Following the end of their employment and the redemption of those profits interests in 2014, plaintiffs were paid, and accepted, $290,000 as the fair market value of the interests. After a third party purchased the assets of a Covis-related entity in 2015, plaintiffs filed suit in federal court, alleging that the prior redemption of their interests was part of a fraudulent scheme to deprive plaintiffs of proceeds from the eventual asset sale. The federal courts dismissed those claims, with prejudice. Plaintiffs now bring this action, asserting claims similar to those that they asserted in federal court.

Defendants move, pursuant to CPLR 3211 (a) (1), (5) and (7), for an order dismissing the complaint on the grounds of documentary evidence, collateral estoppel, and failure to state a cause of action.

For the reasons set forth below, the motion to dismiss the complaint is granted in part, and denied in part.

FACTS

The 2012 Award Agreements

The Covis Enterprise was a pharmaceutical start-up founded in 2011 by former employees of GlaxoSmithKline PLC as a vehicle to obtain interests in the commercial rights of certain pharmaceutical products (the Rights), rebrand them, and sell them to other healthcare companies (complaint ¶¶ 31-33, 52). The common parent of the initial Covis Enterprise was Covis Holdings (*id.* ¶¶ 24, 47). Covis Holdings owned Covis Pharma S.à.r.l. (Covis S.à.r.l.), a Switzerland-based pharmaceutical company which held the rights to the Covis Enterprise's pharmaceutical portfolio (*id.* ¶ 47). Covis Holdings also owned CPI, a North Carolina-based subsidiary which distributed the Covis Enterprise's pharmaceuticals pursuant to a Supply and Distribution Agreement with Covis S.à.r.l (*id.* ¶¶ 30, 47). Covis Holdings had two classes of limited partners: Class A partners, who contributed capital (i.e., Cerberus Covis); and a single Class B partner, MIP I (*id.* ¶ 80). MIP I was created to provide profits incentives to Covis executives, directors, and managers (*id. see* MIP I's Operating Agreement [affirmation of Gavin J. Rooney, exhibit A]). Covis GP was Covis Holdings' general partner (complaint ¶ 23).

Plaintiffs were each recruited to build the distribution network for the Covis Enterprise. Plaintiffs allege that they were told that they would be paid below-market salaries, but in exchange, they would also receive interests in the appreciation of the Rights, which would be worth more than tens of millions of dollars. Plaintiffs allege that, in reliance on this understanding, they built and managed CPI. (*id.* ¶¶ 3, 6)

Following their hire, plaintiffs received an award of unvested Profits Interests through agreements with MIP I (the 2012 Award Agreements) (*id.* ¶ 76; *see* 2012 Award Agreements [Rooney affirmation, exhibits B-F]). The Profits Interests did not grant plaintiffs any equity in the Covis Enterprise; instead, pursuant to contract, each received the potential to receive some of the profits of the Covis Enterprise, net of return of capital and repayment of debt. The 2012 Award Agreements allowed for 50% of the awarded Profits Interests to vest based upon continued employment over time, and the other 50% to vest if the company satisfied certain performance criteria (*see* 2012 Award Agreements § 3). If and when fully vested, the Profits Interests afforded plaintiffs a collective 1.25% stake in the Covis Enterprise's profits (complaint ¶ 76).

The 2012 Award Agreements made clear that continued employment was a condition of vesting, and that any unvested Profits Interests would be forfeit if employment was terminated, for any reason, whether voluntarily or involuntarily:

> "The Profits Interests are subject to forfeiture. If [plaintiff's] employment with Holdings (or, as applicable, any of its Subsidiaries) is Terminated for any reason . . . then all of [plaintiff's] Unvested Profits Interests as of the date of such Termination (the 'Termination Date') shall no longer be eligible for vesting and shall automatically and immediately . . . be forfeited and relinquished to [MIP I]"

(*see* 2012 Award Agreements § 4 [a]). MIP I's Operating Agreement contained similar forfeiture provisions (*see* Operating Agreement § 8.2).

If a manager-plaintiff's employment terminated without cause prior to a Winding Up Event (defined as a sale of substantially all assets), the 2012 Award Agreements allowed MIP I to require a manager-plaintiff to sell back his or her vested Profits Interests to MIP I by delivering a call notice (*see* 2012 Award Agreements § 4[a]). MIP I would then pay him or her "the Fair Market Value of such [Profits] [I]nterests as of the Termination Date". MIP I's Operating Agreement defined "Fair Market Value" as "the fair market value of such Profits Interest . . . as determined in good faith by the Board of Managers, taking into account all relevant factors, including without limitation the most recent valuation" of the Covis Enterprise (*see* Operating Agreement, exhibit A at A-2). In addition, MIP I's Operating Agreement expressly disclaimed any fiduciary duty that might be owed to the manager-plaintiffs by the entity's other managers or members (*see id.* § 5.8).

The 2013 Restructuring

In April 2013, the Covis Enterprise executed a corporate restructuring pursuant to a Master Restructuring Agreement (complaint ¶ 91; *see* Rooney affirmation, exhibit G). Covis Holdings remained the owner of Covis S.à.r.l., which continued to hold the rights to the Covis Enterprise's pharmaceutical portfolio, while CPI continued to distribute the pharmaceuticals pursuant to an amended Supply and Distribution Agreement, which, among other things, specified a termination payment to be made to CPI upon a Winding Up Event, including the sale of Covis S.à.r.l.'s assets (complaint ¶ 92; *see* Master Restructuring Agreement, exhibit A, § 4). US Holdco, a new entity, replaced Covis Holdings as the owner of CPI (*see* Master Restructuring Agreement). Just as before, US Holdco had two classes of limited partners: Class A partners that contributed capital,

and a single Class B Partner – MIP II (*see* Amended and Restated Limited Liability Company Agreement, § 3.1 [Rooney affirmation, exhibit H]).

Pursuant to agreements with MIP II (the 2013 Award Agreements), plaintiffs surrendered their MIP I Profits Interests in exchange for equivalent Profits Interests in MIP II (complaint ¶ 98). The MIP I and MIP II Award Agreements and Operating Agreements are substantively identical (*compare* Rooney affirmation, exhibits B-F, *with* exhibits J-N). Each plaintiff received a CPI Equity Schedule detailing their respective positions before and after the restructuring (complaint ¶ 133; *see* Rooney affirmation, exhibit I). The CPI Schedules explained that the Class A partners had recently contributed $40 million of new capital to fund the acquisition of additional pharmaceutical assets from Sanofi-Aventis U.S. LLC, which, while adding value to the Covis Enterprise, diluted all Profits Interests by approximately one-third (*see* CPI Equity Schedule). Accordingly, the CPI Schedules confirmed that plaintiffs' Profits Interests under MIP II, if fully vested, equaled a collective 0.86% stake in the Covis Enterprise's profits (*see id.*). Like the 2012 Award Agreements, the 2013 Award Agreements were fully integrated contracts that "supersede[d] all prior written or oral negotiations, commitments, representations and agreements with respect thereto" (*see* 2012 Award Agreements § 10; 2013 Award Agreements § 10). By signing the 2012 and 2013 Award Agreements, plaintiffs confirmed that they received a copy of MIP I and MIP II's Operating Agreements; "carefully considered and had the opportunity to discuss" the Award and Operating Agreements with their legal, tax, accounting and financial advisors; and "had a reasonable opportunity to ask questions of and receive answers from a person or persons acting on behalf of [MIP I and MIP II] concerning [the 2012 and 2013] Award Agreement[s] and all such questions have been answered to [the plaintiff's] satisfaction" (*see id.* § 8). Plaintiffs signed the 2013 Award Agreements and received, as replacements for their interests under MIP I, Profits Interests under MIP II that granted equivalent interests in the profits of the Covis Enterprise (*see id.*).

Alleged Misrepresentations and Fraudulent Conduct in Connection with the 2013 Award Agreements

Plaintiffs allege that the 2013 restructuring was a fraudulent scheme to wipe out their share of the Profits Interests and replace them with illusory interests in empty shell companies (complaint ¶¶ 90-97). Plaintiffs further allege that defendants made several extra-contractual false misrepresentations that they relied upon in executing the 2013 Award Agreements. Specifically, plaintiffs allege that various representatives of defendants falsely stated that plaintiffs were entitled

to 3.5% of the Covis Enterprise's profits, and that any payments would be increased by 31% to account for taxes. Defendants also falsely stated that the investment would be worth tens of millions of dollars (*id.* ¶¶ 129-132, 138).

According to plaintiffs, after they executed the 2013 Award Agreements, defendants employed various schemes to "cancel" the Profits Interests, including setting impossible performance targets, and terminating plaintiffs under false pretenses to prevent time-based vesting. Defendants also failed to update certain disclosures to reveal merger negotiations that occurred in 2014, and the sale process in late 2013 that failed to receive any bids, which, if revealed, would have indicated to Goeken that a sale of the Rights was imminent, and would have caused him not to resign (*id.* §§ 168-181).

Plaintiffs' Profits Interests are Called

On June 24, 2014 and June 30, 2014, plaintiffs Brown and Elstad were terminated as employees during a corporate reorganization (complaint ¶¶ 182-184, 186, 187). On August 14, 2014, plaintiff Goeken voluntarily resigned (*id.* ¶ 192). Plaintiffs Homan's and Sampere's employment ended on December 1, 2014, and December 15, 2014, respectively, after CPI announced that it was eliminating its cardiovascular sales team (*id.* ¶¶ 194, 196-97). Pursuant to the 2013 Award Agreements, all of plaintiffs' unvested Profits Interests automatically forfeited back to MIP II as of their respective termination dates (*id.* ¶¶ 186-87, 192, 198). At year-end, on December 31, 2014, MIP II exercised its call right for plaintiffs' vested Profits Interests (*id.* ¶ 204).

Defendants contend that, as required by the 2013 Award Agreements and MIP II's Operating Agreement, MIP II paid plaintiffs the fair market value of their vested Profits Interests as of their termination dates (*see* 2013 Award Agreements § 4 [a]; Operating Agreement, exhibit A, at A-2). According to defendants, to determine fair market value, the MIP II Board of Managers employed a two-fold approach to value the Covis Enterprise, including the pharmaceutical rights held by Covis S.à.r.l. First, the MIP II Board of Managers considered the payment due to CPI pursuant to the Master Restructuring Agreement and Amended Supply and Distribution Agreement between CPI and Covis S.à.r.l. upon the occurrence of a Winding Up Event, which payment would put CPI in an effectively economically equivalent position to that it would have been in on the occurrence of a Winding Up Event before the corporate restructuring (*see* Master Restructuring Agreement, exhibit A, § 4). Second, as an effective "check," the MIP II Board of Managers considered the Covis Enterprise's most recent valuation: $487 million, which reflected

$180 million in profit after return of capital and repayment of debt (*see* complaint ¶ 212). Defendants asserts that each independent approach to valuation supported a valuation of $1.26 for each of plaintiffs' Profits Interests, for a total of $290,000 (*see id.*) MIP II tendered that money to plaintiffs, which they accepted.

Brown Releases Any and All Claims Against Defendants

Pursuant to a December 31, 2014 Repurchase Agreement, plaintiff Brown was paid $17,298 for her 13,701 vested Profits Interests (*see* Rooney affirmation, exhibit O, § 1 [a]). The Repurchase Agreement provided that, "for and in consideration of the mutual promises, terms and conditions set forth in th[e] Agreement, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged," Brown agreed to:

> "fully release, remise, acquit and forever discharge each of the Covis Entities, Cerberus Capital Management, L.P. ('Cerberus') and their respective affiliates and subsidiaries . . . from any and all proceedings, claims, demands, rights, causes or manners of action . . . whether known or unknown, matured, unmatured or contingent, potential or direct, at law or in equity, whether based in statute, common law or otherwise in any way regarding, arising from, on account of, related to or in connection with, directly or indirectly, the Released Parties or Brown's acquisition, ownership or disposition of the Brown Interests . . . Brown covenants and agrees not to assert or assist in the assertion of any Claim released hereunder against [defendants]. Brown acknowledges that the releases granted . . . shall be effective as a bar to any of the Claims described herein and all damages and remedies related thereto of every kind . . . The releases set forth . . . above shall be and remain in effect as full and complete general releases as to the Claims set forth therein, notwithstanding the discovery or existence of any additional or different facts relating to the subject matter of this Agreement"

(Repurchase Agreement § 2). The Repurchase Agreement defined the Released Parties to include MIP II, US Holdco, CPI, and all of their subsidiaries and affiliates (*see id.*) It likewise defined the "Brown Interests" to include the Profits Interests held by Brown under her Award Agreements (*see id.*)

The Repurchase Agreement made clear that Brown could not seek to invalidate the release by claiming ignorance of later-discovered facts:

> "(i) [Defendants] currently may have, and later may come into possession of, non-public information with respect to the Covis Entities that is not known to Brown, (ii) Brown has determined to sell the Brown Interests to [MIP II] for the Purchase Price pursuant to the terms of this Agreement notwithstanding her lack of knowledge of such non-public information and (iii) none of the [Defendants] shall have any liability to Brown with respect to any such nondisclosure of such non-public information in connection with the transactions contemplated by this Agreement"

(*id.* § 3 [d]).

Brown signed the Repurchase Agreement on January 21, 2015, and accepted her $17,298.

The Federal Litigation

On March 9, 2015, months after plaintiffs' respective termination dates, and after MIP II exercised its call right, the Covis Enterprise announced that it was selling substantially all of its assets to Concordia Healthcare Corporation for $1.2 billion (complaint ¶ 225). Plaintiffs filed suit, claiming they were entitled to exponentially greater payments based on the ultimate Concordia transaction.

Plaintiffs filed their original action in the United States District Court for the Southern District of New York, asserting federal and state-law claims under the securities laws and the common law. When defendants moved to dismiss, plaintiffs filed an amended complaint. Defendants then moved to dismiss that amended complaint. By decision and order dated December 12, 2016, Judge George B. Daniels granted defendants' motion (*see* Rooney affirmation, exhibit Q).

In reaching that decision, Judge Daniels held that plaintiffs had failed to adequately plead scienter for their federal securities claims under the heightened pleading requirements of Rule 9 (b) of the Federal Rules of Civil Procedure and the Private Securities Litigation Reform Act of 1995, 15 USC § 78u-4 (the PSLRA), which require a "strong inference" of fraud. Plaintiffs' theories of liability included (1) plaintiffs' theory that defendants violated Rule 10b-5(b) of the Exchange Act by telling plaintiffs at the time of the 2013 restructuring that CPI's managers were entitled to 3.5% of the Covis Enterprise's profits, and promising that any payments would be increased by 31% to account for taxes; (2) plaintiffs' theory that defendants violated Rules 10b-5(a) and (c) of the Exchange Act by plotting "schemes of bad faith, deceit, and manipulation" by terminating plaintiffs' employment and setting impossible performance targets, all to keep

plaintiffs' Profits Interests from vesting; and (3) plaintiff Goeken's theory that defendants violated Rule 10b-5(b) of the Exchange Act by failing to inform him of nascent discussions to sell the Covis Enterprise's assets, in order to dissuade him from resigning from his employment in August 2014 (SDNY decision at *4-6). Judge Daniels dismissed all of plaintiffs' federal claims, without leave to amend, and declined to exercise supplemental jurisdiction over plaintiffs' state-law claims (*id.*). By summary order dated July 11, 2017, the United States Court of Appeals for the Second Circuit affirmed (*see* Rooney affirmation, exhibit R).

Plaintiffs then filed this action asserting fraud under the common law and state blue-sky laws of each of the plaintiffs' states of residence, together with a variety of contract-based and quasi-contract claims: common law fraud (count one); violations of the North Carolina Securities Act, NCGS § 78-56 (a) (1) and (2) (counts two and three); control person liability under NCGS § 78-56 (c) (1) (count four); violations of the Minnesota Uniform Securities Act, Minn Stat § 80A.68 (count five); control personal liability under Minn Stat § 80A.76 (g) (count six); violations of the New Jersey Uniform Securities Law, NJ Stat § 49:3-71 (count seven); control person liability under NJ Stat § 49:3-71 (d) (count eight); breach of fiduciary duty/constructive fraud (count nine); equitable fraud/negligent misrepresentation (count ten); mutual mistake (count eleven); breach of the 2012 and 2013 Award Agreements (counts twelve and thirteen); breach of the covenant of good faith and fair dealing (count fourteen); civil conspiracy (count fifteen); tortious interference with contract (count sixteen); unjust enrichment (count seventeen); and promissory and equitable estoppel (counts eighteen and nineteen).

DISCUSSION

A party may move for judgment dismissing one or more causes of action asserted against him on the ground that the pleading fails to state a cause of action under CPLR 3211 (a) (7). Although on a motion to dismiss a complaint pursuant to CPLR 3211 (a) (7), "the pleading is to be afforded a liberal construction," and "the facts as alleged in the complaint [are presumed] as true" (*Leon v Martinez*, 84 NY2d 83, 87 [1994]; *see also Rovello v Orofino Realty Co.*, 40 NY2d 633 [1976]), "'factual claims [that are] either inherently incredible or flatly contradicted by documentary evidence are not entitled to such consideration'" (*Mark Hampton, Inc. v Bergreen*, 173 AD2d 220, 220 [1st Dept 1991] [citation omitted]; *see also Caniglia v Chicago Tribune-N.Y. News Syndicate*, 204 AD2d 233 [1st Dept 1994]).

In order to prevail on a motion to dismiss based upon documentary evidence, 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]). In addition, "[f]actual allegations presumed to be true on a motion pursuant to CPLR 3211 may properly be negated by affidavits and documentary evidence" (*Wilhelmina Models, Inc. v Fleisher*, 19 AD3d 267, 269 [1st Dept 2005]). Thus, dismissal is warranted where documentary evidence establishes that "the allegations of the complaint fail to state a cause of action" (*L.K. Sta. Group, LLC v Quantek Media, LLC*, 62 AD3d 487, 491 [1st Dept 2009]).

Fraud Claims

In the first through eighth causes of action, plaintiffs bring claims for common law fraud and state blue-sky law claims. Specifically, plaintiffs allege that defendants fraudulently misrepresented that US Holdco and MIP II owned material, appreciable assets (complaint ¶¶ 233, 235, 239); and (2) that plaintiffs were entitled to 2.9% of the Covis Enterprise's profits and a gross-up (*id.* ¶ 234). Plaintiffs also allege that defendants "fraudulently" set "impossible and unreasonable performance targets" in the 2012 and 2013 Award Agreements (*id.* ¶ 245); "fraudulently" terminated plaintiffs "in bad faith for pre-textual and false reasons" when defendants "anticipated a Winding Up Event" (*id.* ¶ 246); failed to disclose merger negotiations to Goeken (*id.* ¶ 247); and "fraudulently" exercised MIP II's call right (*id.* ¶ 248).

Defendants argue that four of these claims (counts one, two, five and seven) are each barred by the doctrine of collateral estoppel because they all require scienter, and the federal court dismissed plaintiffs' federal claims for lack of scienter. However, the federal dismissal of plaintiffs' failed securities fraud claims for failure to allege a "strong inference" of scienter is not preclusive.

"Collateral estoppel comes into play when four conditions are fulfilled: '(1) the issues in both proceedings are identical, (2) the issue in the prior proceeding was actually litigated and decided, (3) there was a full and fair opportunity to litigate in the prior proceeding, and (4) the issue previously litigated was necessary to support a valid and final judgment on the merits'" (*Conason v Megan Holding, LLC*, 25 NY3d 1, 17 [2015] [citation omitted]). Collateral estoppel will bar claims over which a federal court declined to exercise supplemental jurisdiction if "the federal court decided issues identical to those raised by the plaintiff's state claims" (*Clifford v County of Rockland*, 140 AD3d 1108, 1110 [2d Dept 2016]; *see also Hudson v Merrill Lynch &*

Co., Inc., 138 AD3d 511, 516 [1st Dept 2016]; *Sanders v Grenadier Realty, Inc.*, 102 AD3d 460, 461 [1st Dept 2013]; *see e.g. Pinnacle Consultants v Leucadia Natl. Corp.*, 94 NY2d 426, 431-432 [2000] [dismissing shareholder derivative action on collateral estoppel grounds, where issues had been raised and decided against plaintiff in a prior federal court action]).

Defendants cannot demonstrate that they have satisfied the elements of collateral estoppel because the federal court did not decide issues identical to those raised here. The federal securities claims brought in the federal action were subject to Rule 9 (b) and the PSLRA, which require a plaintiff to allege "facts giving rise to a strong inference that the defendant acted with the required state of mind" (15 USC § 78u-4). In contrast, the complaint's fraud claims are subject to the CPLR and "3016 (b) may be met when the facts are sufficient to permit a reasonable inference of the alleged conduct" (*Pludeman v North Leasing Sys., Inc.*, 10 NY3d 486, 492 [2008]). New York courts have uniformly held that the federal strong inference standard is higher than New York's reasonable inference standard (*see Syncora Guar. Inc. v Alinda Capital Partners, LLC*, 2013 NY Slip Op 31489[U], * 18 [Sup Ct, NY County 2013] [CPLR 3016 (b) "is a more lenient test than the Second Circuit's 'strong inference of fraud' test, in that it requires only that the complaint include 'facts from which it is possible to infer defendant's knowledge of the falsity of its statements'"] [citation omitted]; *see also PMC Aviation 2012-1 LLC v Jet Midwest Grp., LLC*, 2016 NY Slip Op 30972[U], * 14 [Sup Ct, NY County 2016] ["The particularity required by CPLR 3016 [b] is not as exacting as what is required under Rule 9 (b) in federal court"]; *NRAM PLC v Societe Generale Corp.*, 2014 NY Slip Op 32155[U], * 20 [Sup Ct, NY County 2014] ["The applicable New York standard requires only a 'reasonable inference' of scienter, while Rule 9 (b) of the Federal Rules of Civil Procedure and its interpreting case law is far more demanding"]).

Accordingly, because the federal court applied the strong inference standard to the federal action's allegations of scienter, the federal dismissal is not preclusive of plaintiffs' state law fraud claims (*see Williams v Citigroup, Inc.*, 104 AD3d 521, 522 [1st Dept 2013] ["dismissal with prejudice of plaintiff's Sherman Act claim at the pleading stage has no preclusive effect, in light of the heightened pleading requirements for antitrust claims in federal court"]). Indeed, a dismissal pursuant to the PSLRA cannot be preclusive because "the district court rendered a decision on a claim rooted in federal statutory law, based on federal rules of pleading" (*Small v Arch Capital Grp.*, 2008 NY Misc LEXIS 9284, * 9 [Sup Ct, NY County 2008]). Accordingly, defendants' motion for dismissal of counts one, two, five and seven of the complaint is denied.

Defendants also argue that count three, which is plaintiffs' only blue-sky cause of action that does not require scienter, must also be dismissed because plaintiffs have not alleged that defendants offered or sold them a security by public offering. Defendants' argument is based solely on the fact that North Carolina courts have stated that the statute upon which this claim is based (NCSA § 78A-56 [a] [2]) "is the state equivalent of a federal section 12 (a) (2) claim of the Securities Act of 1933" (defendants' memorandum at 17), and that the United States Supreme Court has held that the "intent of Congress and the design of the statute require that § 12 (2) liability be limited public offerings" (*id.*, quoting *Gustafson v Alloyd Co., Inc.*, 513 US 561, 578 [1995]).

The court rejects this argument because in *Piazza v Kirkbride* (246 NC App 576, 599 [2016]), the North Carolina appellate court specifically affirmed liability under this statute in connection with a non-public offering. Accordingly, defendants' motion to dismiss count three of the complaint is denied.

Defendants further argue that plaintiffs' remaining Blue Sky claims for control person liability (counts four, six, and eight) and the claim for civil conspiracy (count fifteen) must all be dismissed on the ground that there is no underlying primary fraud. This argument lacks merit in that defendants have failed to establish the veracity of their collateral estoppel arguments. The motion is denied with regard to the fraud claims, as discussed above.

Defendants secondarily argue that these claims must be dismissed for failure to allege "overt acts" in furtherance of an agreement to commit a fraud on plaintiffs, or evidence that Cerebus, Cerebus Covis and Covis GP "'intentionally'" participated "'in the furtherance of a plan or purpose'" to defraud plaintiffs" (defendants' memorandum at 17, note 3, citing *Abacus Fed. Sav. Bank v Lim,* 75 AD3d 472, 474 [1st Dept 2010]; *Gallagher v Ruzzine*, 147 AD3d 1456, 1458 [4th Dept 2017]). However, as plaintiffs note, the state laws at issue do not contain an "overt act" requirement. To make out a prima facie case of control person liability, a plaintiff must allege a primary violation and defendant's control of the primary violator, and then the burden shifts to the control person to prove that it did not know, and could not have known, of the misconduct (NCGS 78A-56 [b] [1]; Minn Stat § 80A.77 [g]), NJSA 49:3-71 [d]). Plaintiffs have sufficiently stated claims under the relevant blue-sky laws, given their allegations of primary violations and how Cerebus, Cerebus Covis and Covis GP controlled the violators (*see* complaint ¶¶ 41-51, 79-97, 101-102, 302-308, 332-336 and 365-369).

Plaintiffs also adequately state a civil conspiracy claim (*see Prairie Capital III, LP v Double E Holding Corp.*, 132 A3d 35, 62-65 [Del Ch 2015]). Plaintiffs have alleged numerous "overt acts" by defendants, including the issuance of illusory new equity and material misrepresentations, and that defendants profited from those allegedly unlawful acts (*see* complaint ¶¶ 437-441).

Accordingly, defendants' motion to dismiss counts four, six, eight and fifteen of the complaint is also denied.

Breach of Fiduciary Duty and Negligent Misrepresentation Claims

In counts nine and ten of the complaint, plaintiffs allege that Cerberus breached a fiduciary duty to plaintiffs, and that all defendants negligently made misrepresentations that induced plaintiffs to relinquish their Profits Interests in MIP I in exchange for Profits Interests in MIP II. These claims fail.

The claim for breach of fiduciary duty cannot be dismissed based on express disclaimer. The Delaware Limited Liability Company Act expressly allows the parties to an operating agreement to "eliminate[]" the fiduciary duties that a member, manager, or other person might otherwise owe (6 Del C § 18-1101 [c]). The MIP II Operating Agreement expressly disclaims any such duty (*see* Operating Agreements, § 5.8 ("Members and Managers shall have no fiduciary duty to [MIP I or MIP II], any Member or any other Person") but only with respect to certain "Members and Managers" as set forth in the agreement. Because Cerberus is not included in the list of Members, its express disclaimer defense fails (*see* MIP LLC Operating Agreement at 1, Schedule A)

However, the claim should be dismissed because plaintiffs are not stockholders and therefore are owed no fiduciary duty as a matter of law. A profits interest is materially distinct from stock ownership, because it "is merely a hope, and clearly not more than a speculative estimate. It is a remote proprietary interest" (*Popkin v Dingman*, 366 F Supp 534, 539 [SD NY 1973]). Such expectancy interests do not create a fiduciary relationship (*see Simons v Cogan*, 549 A2d 300, 304 [Del 1988] ["a mere expectancy interest does not create a fiduciary relationship. Before a fiduciary duty arises, an existing property right or equitable interest supporting such a duty must exist"]). Fiduciary duties are owed to stockholders, and not to holders of expectancies such as warrants to buy stock or profits interests (*Matter of Nine Sys. Corp. Shareholders Litig.*, No. 3940, 2013 WL 771897, *7 [Del Ch, Feb. 28, 2013]).

Plaintiffs' claim for negligent misrepresentation also fails. A claim for negligent misrepresentation requires a special duty or close relationship creating an obligation to disclose accurate information. For the reasons stated above, no such duty exists here (*see Vague v Bank One Corp.*, 2006 WL 290299, *7, n 61 [Del Ch, Feb. 1, 2006] [negligent misrepresentation requires "'a particular duty to provide accurate information, based on the plaintiff's pecuniary interest in that information'"] [citation omitted]; *JP Morgan Chase Bank v Winnick*, 350 F Supp 2d 393, 400 [SD NY 2004] [in a commercial context, there is only a duty "'on those persons who possess unique or specialized expertise, or who are in a special position of confidence and trust with the injured party such that reliance on the negligent misrepresentation is justified'"] [citation omitted]). Indeed, the parties contractually and affirmatively disclaimed any such duty (*see* Operating Agreements, § 5.8 ["no implied duties, covenants or obligations shall be read into this Operating Agreement . . . the provisions of this Operating Agreement, to the extent that they restrict or eliminate the duties (including fiduciary duties) and liability of the Member or Manager otherwise existing at law or equity, are hereby agreed by [MIP I and MIP II], each Member and any other Person bound by this Operating Agreement to replace such other duties and liabilities").

Accordingly, plaintiffs' claims for breach of fiduciary duty and negligent misrepresentation (counts nine and ten) must be dismissed.

Mutual Mistake (Count Eleven)

In count eleven of the complaint, plaintiffs seek to have the 2013 Award Agreements reformed on the basis of mutual mistake concerning the supposed lack of assets underlying MIP II's Profits Interests. However, a contract may only be reformed because of a mutual mistake if "both parties were mistaken as to a material portion of the written agreement" *(CC Fin. LLC v Wireless Props., LLC*, 2012 WL 4862337, *6 [Del Ch, Oct. 1, 2012]; *see also Martin Marietta Materials, Inc. v Vulcan Materials Co.*, 56 A3d 1072, 1145, n 283 [Del Ch 2012], *affd* 45 A3d 148 [2012]).

Plaintiffs' claim for mutual mistake fails because the complaint does not allege any mistake of fact that was mutually made by the parties. Indeed, the complaint itself belies any claim that either plaintiffs or MIP II labored under any misconception about US Holdco's and MIP II's assets and value (*see* complaint ¶ 395). Plaintiffs admit that, prior to signing the 2013 Award Agreements, they understood the restructuring to mean that US Holdco would assume ownership over CPI (*id.* ¶ 92). That understanding is accurately reflected in the Restructuring Agreement.

US Holdco could not possibly have been a "shell" because it owned CPI – the entity responsible for distributing the Covis Enterprise's pharmaceuticals (complaint ¶¶ 47, 92). Moreover, after exercising the call right, the MIP II Board of Managers did not tell plaintiffs that they held worthless interests in a "shell" company, but instead, considered the formula payment due to CPI from Covis S.á.r.l. upon a Winding Up Event to determine the value of plaintiffs' Profits Interests and valued the entire Covis Enterprise at $487 million (*id.* ¶¶ 205, 212). Indeed, plaintiffs concede that their Profits Interests were valued based on the entire Covis Enterprise's most recent valuation, and that they were paid $290,000 (*id.* ¶¶ 212).

Thus, the complaint fails to allege facts showing MIP II's mutual mistake as to the assets and value of US Holdco and MIP II.

Although plaintiffs assert, for the first time in their opposition memorandum, a claim for unilateral mistake, "[i]t is well settled that claims asserted for the first time in opposition papers should not be considered by the court" (*Zutty v Rye Select Broad Market Prime Fund, L.P.*, 33 Misc 3d 1226[A], *15 [Sup Ct, NY County 2011]).

Accordingly, the cause of action for mutual mistake shall be dismissed.

Breach of Contract (Counts 12 and 13)

In counts twelve and thirteen of the complaint, plaintiffs allege breach of both the 2012 Award Agreements and the 2013 Award Agreements. However, plaintiffs cannot recover for both the MIP I and MIP II Profits Interests, because the MIP II Profits Interests were expressly issued to replace and supersede the MIP I Profits Interests (*see* Master Restructuring Agreement, § 3.1 ["the [MIP I] Profits Interests . . . shall be automatically redeemed without the payment of any consideration therefor . . . and [plaintiffs] shall have no further rights with respect to the [MIP I] Profits Interests"]). Indeed, the complaint freely admits that plaintiffs "agreed to swap their [MIP I Profits Interests] for [MIP II Profits Interests]" (complaint ¶ 6). Accordingly, count twelve of the complaint for breach of contract relating to the 2012 Award Agreements must be dismissed.

In count thirteen of the complaint, plaintiffs allege that US Holdco and MIP II breached the 2013 Award Agreements by: (1) wrongfully calling plaintiffs' MIP II Profits Interests (complaint ¶ 417); (2) valuing plaintiffs' Profits Interests as of their termination dates (*id.* ¶ 418); (3) failing to calculate the value of plaintiffs' Profits Interests in good faith (*id.* ¶ 419); and (4) using the termination payment set forth in the Supply and Distribution Agreement between CPI and Covis S.à.r.l. to value plaintiffs' Profits Interests (*id.* ¶ 420).

To sustain a breach of contract claim under New York law, a plaintiff must offer evidence to establish: (1) the existence of a valid contract; (2) performance of the contract by the injured party; (3) breach by the injured party; and (4) resulting damages (*Harris v Seward Park Hous. Corp.*, 79 AD3d 425, 426 [1st Dept 2010]; *see also Palmetto Partners, L.P. v AJW Qualified Partners, LLC*, 83 AD3d 804, 806 [2d Dept 2011]). "The fundamental rule of contract interpretation is that agreements are construed in accordance with the parties' intent . . . and '[t]he best evidence of what parties to a written agreement intend is what they say in their writing' . . . . Thus, a written agreement that is clear and unambiguous on its face must be enforced according to the plain terms, and extrinsic evidence of the parties' intent may be considered only if the agreement is ambiguous" (*Riverside S. Planning Corp. v CRP/Extell Riverside, L.P.*, 60 AD3d 61, 66 [1st Dept 2008] [citation omitted], *affd* 13 NY3d 398 [2009]). Whether a contract is ambiguous presents a question of law for resolution by the courts (*id.* at 67). Courts should adopt an interpretation of a contract which gives meaning to every provision of the contract, with no provision left without force and effect (*see RM 14 FK Corp. v Bank One. Trust Co., N.A.*, 37 AD3d 272, 274 [1st Dept 2007]).

Defendants contend that, under the plain terms of the 2013 Award and Operating Agreements, plaintiffs' claim for breach of contract fails as a matter of law. The 2013 Award Agreements allowed MIP II to "require [plaintiffs] to sell all of the Vested Profits Interests held as of the Termination Date to [MIP II] (the 'Call Right'), which right shall be exercisable by delivery of a written notice to [plaintiffs] (the 'Call Notice')" (2013 Award Agreements, § 4 [a]). Defendants argue that the 2013 Award Agreements place no time limit on the Call Right, and that plaintiffs cannot point to any provision in the 2013 Award Agreements that MIP II violated by exercising its call right on December 31, 2014.

However, the plain terms of the 2013 Award Agreements, as well as the Operating Agreement, do not support defendants' reading regarding the timeliness of their call notice. Plaintiffs allege that defendants' call exercise was untimely because they did not exercise the call either on plaintiffs' termination dates, or, in the alternative, within 30 days thereafter (complaint ¶¶ 110-112, 204-210). The terms of the Operating Agreement were incorporated into the 2013 Award Agreements, as the 2013 Award Agreements expressly state that they are "subject in [their] entirety to the terms and provisions of the [Operating Agreement]" and "[i]n the event of a conflict . . . the terms of the Operating Agreement shall control unless this Award Agreement expressly

states otherwise (2013 Award Agreements preamble). The Operating Agreement provides for a 30-day "Option Period" within which the defendants would be entitled to exercise their call rights (*see* Operating Agreement, § 8.2 [b] [ii], at A-3]). It is thus clear that the Operating Agreement's 30-day Option Period controlled the 2013 Award Agreements, which were silent as to the Option Period, and merely summarized the call provisions of the governing document. Because the 2013 Award Agreements do not expressly state that they control, the Operating Agreement controls.

Accordingly, by alleging that defendants' call exercise was untimely because they did not exercise the call either on the termination dates or within the 30-day Option period, plaintiffs have sufficiently pled breach of contract through defendants' improper exercise of their call rights. Because defendants concede that their valuation was based on the dates of termination (which was only to be used if the Call Right was properly exercised), plaintiffs have also sufficiently alleged a breach with respect to defendants' valuation. Hence, defendants' motion to dismiss count thirteen of the complaint is denied.

Quasi-Contract Claims

In addition to the breach of contract claims, the complaint pleads claims under a series of quasi-contract theories: breach of the implied covenant of good faith and fair dealing, tortious interference with contract, unjust enrichment, promissory estoppel, and equitable estoppel (counts fourteen, and sixteen through nineteen). Each of these claims alleges purported flaws in the bargaining process leading to the Award Agreements, or challenges the amount paid to plaintiffs by MIP II as "fair market value." However, plaintiffs' rights and remedies are governed by the 2013 Award Agreements and the MIP II Operating Agreement, and it is black letter law that plaintiffs may not avoid those contracts by asserting a quasi-contract claims.

1. *Breach of the Implied Covenant of Good Faith and Fair Dealing*

In the fourteenth cause of action for breach of the implied covenant of good faith and fair dealing, plaintiffs allege that defendants violated the implied covenant by (1) canceling plaintiffs' original MIP I Profits Interests under the 2012 Award Agreements, (2) setting "impossible and unreasonable" performance targets in bad faith, so as to cancel the unvested performance-based equity, (3) terminating plaintiffs' employment arbitrarily and unreasonably, so as to cancel the unvested time-based equity, and (4) purporting to exercise the call option (complaint ¶¶ 430-433).

The parties dispute whether New York or Delaware law should be applied with respect to this claim, but at minimum, plaintiffs have sufficiently pled count fourteen by asserting that

defendants set impossible performance targets. If true, these allegations would establish behavior that, although not in violation of the explicit terms of any agreement, would "have the effect of destroying or injuring the right of the other party to receive the fruits of the contract" (*511 W. 232nd Owners Corp. v Jennifer Realty Co.*, 98 NY2d 144, 153 [2002]). Accordingly, the motion is denied with respect to count fourteen.

2. *Unjust Enrichment and Estoppel*

The existence of valid and enforceable contracts governing the parties' relationship means that the unjust enrichment and estoppel claims cannot be maintained, especially where, as here, the allegations comprising the claims relate to defendants' performance under the contracts (*Susman v Commerzbank Capital Markets Corp.*, 95 AD3D 589, 590 [1st Dept 2012] [stating that claims for estoppel "cannot stand when there is a contract between the parties"]; *Raske v Next Mgt., LLC*, 2013 WL 5033149, *9 [Sup Ct, NY County 2013] ["A cause of action for unjust enrichment . . . may not be maintained where there exists a contract governing the same subject matter"]).

Accordingly, the causes of action for unjust enrichment (count seventeen) and promissory and equitable estoppel (counts eighteen and nineteen) are dismissed.

3. *Tortious Interference With Contract*

Plaintiffs allege that CPI tortiously interfered with the 2012 and 2013 Award Agreements by terminating plaintiffs in bad faith (complaint ¶¶ 442-448). To prove a claim for tortious interference with contract, the plaintiff must show: (1) the existence of a valid contract; (2) defendant's knowledge of the contract; (3) defendant's intentional procurement of the third-party's breach without justification; (4) actual breach of the contract; and (5) damages caused by breach of the contract (*Lama Holding Co. v Smith Barney*, 88 NY2d 413, 424 [1996]; *Kronos, Inc. v AVX Corp.*, 81 NY2d 90, 94 [1993]). This claim must be dismissed because plaintiffs have failed to plead that CPI's termination of plaintiffs caused MIP LLC or MIP US to breach either of the Award Agreements.

Brown's Claims

In this action, plaintiff Brown seeks recovery on the same claims that she has expressly released in the Repurchase Agreement. Releases like the one contained in the Repurchase Agreement "will not be treated lightly" and "'constitute[] a complete bar to an action on a claim which is the subject of the release'" (*Allen v Riese Org., Inc.*, 106 AD3d 514, 516-517 [1st Dept

2013] [finding that "plaintiffs are nevertheless barred from challenging the releases on those grounds because they ratified the releases" by "accept[ing] the benefits of a contract and fail[ing] to act promptly to repudiate it"]). A release that is "complete, clear, and unambiguous on its face must be enforced according to the plain meaning of its terms," and it is appropriate to do so on a CPLR 3211 motion (*Alvarez v Amicucci*, 82 AD3d 687, 688 [2d Dept 2011]).

The Repurchase Agreement's release completely, clearly, and unambiguously discharged all of the claims Brown now purports to assert against defendants. She released all claims "arising from, on account of, related to or in connection with" either defendants or her Profits Interests (Repurchase Agreement § 2). Brown offers no explanation as to why the Repurchase Agreement does not bar her claims. Moreover, by accepting the $17,298 for her Profits Interests, Brown ratified the Repurchase Agreement and its release (*see Allen*, 106 AD3d at 517 [a plaintiff who ratifies a release cannot later challenge it on the grounds of fraud, duress, overreaching, illegality, or mutual mistake]). The Repurchase Agreement makes clear that Brown's release was valid even though defendants may have had, or may have later come into the possession of, non-public information unknown to her; and she released defendants from liability "with respect to any nondisclosure of such non-public information" (Repurchase Agreement § 3[d]). Accordingly, Brown's claims are barred by the Repurchase Agreement and must be dismissed.

The court has considered the remaining arguments and finds them to be without merit.

Accordingly, it is

ORDERED that the motion to dismiss is granted in part, and the ninth, tenth, eleventh, twelfth, fourteenth, sixteenth, seventeenth, eighteenth and nineteenth causes of action of complaint are dismissed; and it is further

ORDERED that all claims brought by plaintiff Tonya Brown are dismissed as against defendants; and it is further

ORDERED that defendants are directed to serve an answer to the complaint within twenty (20) days after service of a copy of this order with notice of entry.

This constitutes the decision and order of the court.

DATED: October 30, 2018

ENTER,

O. PETER SHERWOOD J.S.C.