Boesky v Levine
2018 NY Slip Op 33017(U)
November 27, 2018
Supreme Court, New York County
Docket Number: 650756/2017
Judge: Eileen Bransten
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK - CIVIL TERM: PART 3
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Index No. 650756/2017
Mot. Seq. Nos. 001-004

STUART J. BOESKY and ALAN P. HIRMES,

Plaintiffs,

- against -

HAROLD LEVINE, HERRICK FEINSTEIN LLP,
MORITT HOCK & HAMROFF LLP,
RONALD KATZ and MAZARS USA LLP,
as successor in interest to WEISER LLP,

Defendants.
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EILEEN BRANSTEN, J.

In this action, plaintiffs seek to recover damages for, among other things, defendants' alleged fraud and negligence in connection with their tax-related advice, in the preparation of plaintiffs' tax returns, and in their representation of plaintiffs in the litigation of a tax dispute. Defendants Mazars USA LLP as successor in interest to Weiser LLP (Mazars USA), Herrick Feinstein LLP (Herrick Feinstein), Moritt Hock & Hamroff LLP (Moritt Hock), and Harold Levine, separately move to dismiss the complaint insofar as asserted against them pursuant to CPLR 3211 (a) (5) and (a) (7) (Motion Sequence Nos. 001- 004, respectively).[1] For the following reasons, the motions are granted.

[1] Defendant Ronald Katz had not yet appeared in this action and, indeed, was subsequently ordered to respond to the Complaint in Motion Sequence 005. *See Decision and Order dated April 19, 2018.* The Defendant argued in his motion papers that he was not required to file a response to the Complaint as he had initiated a Bankruptcy Proceeding in the Southern District of Florida. *See id at Tr. 11:4-11:6.* On July 27, 2017 the Bankruptcy was dismissed with prejudice but leave was granted for Defendant Katz to file another petition within 180 days. *See NYSCEF Doc. 94.* It is unclear whether the Defendant ever filed a second bankruptcy petition within that 180-day period as nothing was subsequently filed with this court. Pursuant to a written clarification to the Decision on Motion sequence 005, Defendant Katz was to file a

I. Background

The following facts are drawn from the complaint. Defendant Harold Levine, an attorney, was a partner in the tax department of defendant law firm Herrick Feinstein from 2002 through September 2012, where he served as co-chair of the firm's Tax and Personal Planning Department and headed the firm's Tax Group. Comp. ¶ 9. In September 2012, Levine left Herrick Feinstein and began practicing at defendant law firm Moritt Hock, where he served as a partner and chair of the Tax Group until he was indicted for tax fraud in October 2016. *Id.* ¶¶4, 12.

Defendant Ronald Katz, an accountant, was a partner at defendant tax advisory and accounting firm Mazars USA, where he, among other things, oversaw the preparation of tax returns for certain entities and individuals. *Id.* at ¶18. Katz was also indicted for tax fraud in October 2016. *See id.* at ¶13.

Plaintiffs Boesky and Hirmes were senior executives of The Related Companies, Inc. (Related), a global real estate development firm to which Katz provided tax advice and accounting services. *Id.* at ¶¶ 22-24. In or about 2002, Boesky approached Katz, who had become a trusted advisor to plaintiffs, to inquire whether Katz knew of any legitimate real estate deals that would reduce Boesky's tax liability. *Id.* at ¶ 25. Katz informed Boesky that he knew of a strategy to take advantage of a legal loophole in the tax law, whereby Boesky could invest in a limited liability company (LLC) for the sole purpose of purchasing and then donating a

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motion to dismiss within 20 days of the April 19 Decision and Order, and the deadline to otherwise file an Answer only was extended to 10 days following the Decision on these instant

remainder interest in certain real estate (or a remainder interest in the rights to an entity that directly or indirectly holds the real estate). The amount of the charitable deduction claimed would be higher than the amount Boesky paid to acquire the remainder interest, thereby creating a tax deduction offsetting most of the income realized by Boesky for that tax year. *Id.* at ¶26. This strategy is referred to in the complaint as the "remainder interest tax strategy". *Id.*

At the behest of Katz, plaintiffs retained Katz's close friend Levine, to provide them with legal advice and services concerning the remainder interest tax strategy, including forming the LLCs required to execute the strategy. *Id.* at ¶27. In 2002, Levine and Herrick Feinstein began providing legal advice and services to plaintiffs pursuant to oral agreements. *See Comp.* at ¶28. At the time, plaintiffs did not have a written engagement letter with Levine or Herrick Feinstein. *Id.*

Levine advised plaintiffs that the charitable deduction created by the remainder interest tax strategy was legal and the "only legitimate way" to shelter income from taxation. *Id.* at ¶¶ 31-32. Levine also told plaintiffs that a taxpayer utilizing the remainder interest tax strategy had been audited by the Internal Revenue Service (IRS) and prevailed in the audit. *See id.* at ¶ 34. In addition, he told plaintiffs that the IRS had issued a letter ruling, or other position statement, that the remainder interest tax strategy was a legitimate tax savings transaction. *Id.*

In reliance on their relationship of trust and confidence with Katz, Levine's advice, and the reputation of Herrick Feinstein, plaintiffs decided to engage in the remainder interest tax strategy, the arrangement of which was primarily handled by Levine. *Id.* ¶ 36. From 2002 and

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motions. *See NYSCEF Doc. 114.*

2004, between them, plaintiffs invested in the following LLCs for the sole purpose of executing the strategy: PSRE Holdings LLC; RERI Holdings I LLC (RERI); BASH Real Estate LLC; RARE Investments IV LLC; and CMBH Real Estate Holdings, LLC (collectively the LLCs). *Id.* ¶37. Their investments in these LLCs totaled approximately $2.3 million. *Id.* ¶¶ 39-41.

Each of the LLCs executed a remainder interest tax strategy in order to create a large deduction for tax purposes that could be claimed by plaintiffs on their personal income tax returns. *Id.* ¶ 42. As a result, between them, plaintiffs claimed more than $14 million in charitable deductions on their federal and state income tax returns from 2002 to 2005. *Id.* Katz and Mazars USA prepared plaintiff Hirmes's personal income tax returns for the tax years 2002 through 2016, and plaintiff Boesky's personal income tax returns for the tax years 2005 through 2007. *See Comp.* ¶¶ 46-46. Katz and Mazars USA also prepared the income tax returns for the LLCs. *See id.* at ¶47.

In or about 2006, the IRS and the New York State Department of Taxation and Finance (NYSDTF) began to audit each of the LLCs and the individual members engaged in the remainder interest tax strategy. *Id.* at ¶ 62. On June 20, 2007, Levine sent Boesky a notice from the NYSDTF, dated June 13, 2007, which stated that the NYSDTF determined that the remainder interest tax strategy, was a "tax avoidance transaction" and that it intended to challenge any purported tax benefits from such a transaction on the grounds that the method of appraisal was inappropriate and resulted in an inflated fair market value for the donated property; the transaction was not done for a valid business purpose; and had no economic substance other than for obtaining tax benefits. *Id.* at ¶ 63. The notice also stated that, pursuant to NYSDTF

regulations, any taxpayer participating in such a transaction was required to disclose his or her participation. *Id.* at ¶¶ 64-65. Defendants failed to file these disclosure statements. Instead of advising plaintiffs of the applicability and implications of the notice, defendants continued to tell plaintiffs that the transactions were legal. *Id.* at ¶ 70.

Between 2006 and 2008, the IRS also sent plaintiffs notices of deficiency on the tax returns involving BASH Real Estate LLC, RARE Investments IV LLC, and CMBH Real Estate Holdings, LLC, demanding payment of several hundred thousand dollars in additional taxes and penalties. *Id.* at ¶¶ 127-138. Additionally, in or about 2007, the IRS issued a notice designating transactions similar, or identical to, the remainder interest tax strategy as "transactions of interest". *See Comp.* at ¶¶ 72-74. Under IRS regulations, if the IRS declares a certain transaction a "transaction of interest" after the filing of a tax return reflecting such transaction, the taxpayer must file a disclosure statement within 90 days. *See id.* at ¶77. However, defendants failed to file the disclosure statement within 90 days. *Id.* at ¶ 9. Instead of advising plaintiffs of the applicability or implications of the notice, defendants continued to tell them that the transactions were legal. *Id.* at ¶ 80.

At some point, the IRS and the NYSDTF began to focus specifically on auditing RERI because of the significant size of the deduction RERI claimed on its 2003 federal income tax return. *Id.* at ¶ 82. In or about 2008, the IRS denied approximately $30 million of RERI's $33 million charitable deduction, on the ground that RERI overstated the value of the charitable contribution reported on its 2003 income tax return and assessed an accuracy-related penalty on any resulting underpayment of income tax. *Id.*

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Levine, in his capacity as the tax matters partner (TMP) for RERI, received a notice from the IRS and a tax deficiency notice from the NYSDTF. *Id.* at ¶84. On March 4, 2008, he e-mailed plaintiffs, advising them that "there are many issues with NY's notice including statute of limitations, penalties imposed, and the denial of the deduction". *Id.* Levine requested that plaintiffs send any notices they received, or may receive, from the IRS or the NYSDTF to Levine or to Kyle Wissel, a tax attorney employed by Mazars USA. *Id.* Levine also advised plaintiffs to participate in a "coordinated response" or "group protest" to the New York State notices and the IRS audits. *Id.*

On or about April 21, 2008, Levine, in his capacity as the TMP for RERI, petitioned the United States Tax Court, challenging the IRS's determination regarding the charitable deduction reported on RERI's 2003 income tax return. *Id.* at ¶¶ 85-86; *RERI Holdings I, LLC, Harold Levine, Tax Matters Partner v Commissioner*, Docket No. 9323-08. The petition, filed by San Francisco-based attorney Randall G. Dick, asked the Tax Court to find that RERI's charitable contribution was properly computed and that any adjustments found by the court would not be subject to penalties. *Comp.* at ¶ 85. This proceeding is referred to in the complaint as the "RERI Tax Case."

Plaintiffs each provided Herrick Feinstein with approximately $50,000 as their share of the "litigation fund" for the RERI Tax Case. *Id.* at ¶98. A trial took place in the RERI Tax Case in June 2015. *Id.* at ¶119. However, at the time plaintiffs commenced the instant action on February 10, 2017, the United States Tax Court had yet to decide the case. *Id.* On July 3, 2017, the Tax Court issued a decision disallowing RERI's claimed charitable contribution in full on the

ground that RERI failed to satisfy Income Tax Regulation 1.170A-13 (c) (2), which required it to disclose its costs or other basis in the charitably contributed property. The Tax Court also upheld the IRS's imposition of a "gross valuation misstatement" penalty against RERI. S*ee RERI Holdings I, LLC, Jeff Blau, Tax Matters Partner v Commissioner*, 149 T.C. No. 1 (United States Tax Court 2017) (Docket No. 9324-08). On December 18, 2017, RERI filed a notice of appeal from the Tax Court's decision. As of this writing, the appeal remains pending before the DC Circuit Court of Appeals.

In the meantime, on April 23, 2008, Levine e-mailed plaintiffs advising them that RARE Investments IV LLC had been selected by New York State as a test case with respect to challenging the charitable contribution deduction and stating: "[w]e believe NYS is incorrect for a number of reasons and plan on challenging their assessment". *Comp.* at ¶ 87. Levine also advised plaintiffs to retain Ellis Reemer, an attorney at the law firm DLA Piper, to represent them in challenging the NYSDTF's audit. *Id.*

In or about May 2008, plaintiffs sent payment to Levine and Herrick Feinstein to prepare and file a response to the NYSDTF's audit. *Id.* ¶88. On or about May 16, 2008, Boesky signed a power of attorney form permitting Levine and Reemer to represent Boesky before the NYSDTF. *Id.* ¶89).

On August 21, 2008, Boesky e-mailed Katz and Wissel seeking advice on how to respond to a deficiency notice he received from the IRS for 2005. *Id.* at ¶90. On or about February 20, 2009, Wissel wrote to Levine stating: "[a]s you are aware, New York State has categorized certain charitable contributions of remainder interests in real property as listed transactions and

taken steps in some instances to assess tax based on a reduction of that deduction taken in prior years. As part of the ongoing effort to resolve these matters, we have negotiated a settlement offer with NYS whereby the State has agreed to allow a charitable deduction equal to 2 ½ times an investor's original cash investment, calculate the increase in tax on that adjustment, and then add to that amount an interest charge plus a penalty equal to 50% of that calculated interest, all subject to adjustment once a final determination is made by the [IRS]". *Comp.* at ¶91. Levine forwarded this correspondence to Boesky, who responded by asking Levine what he should do. *Id.*

On April 20, 2011, Levine e-mailed RERI's members, including plaintiffs, stating that some of them had received a letter from the IRS asking them to voluntarily cooperate with the investigation of RERI. *Id.* at ¶ 94. Levine advised in his e-mail: "You should NOT reply. You should ignore the letter and if they contact you tell them that you are represented by counsel. Also please let me know if the IRS contacts you in this matter. The partnership and therefore you are represented by Randall Dick an attorney based in SF in this matter". *Id.* at ¶94.

On April 25, 2011, Randall Dick wrote a letter to the IRS which was copied to Levine and RERI's members. The letter stated: "Take note that the following individuals are represented by me in connection with the IRS's determination that members of RERI . . . will owe additional tax as a result of the denial of RERI's charitable contribution set forth in the pleadings on file in *RERI Holdings I, LLC, Harold Levine, Tax Matters Partner v Commissioner*, Docket No. 9323-08: . . . Alan Hermes [sic] [and] Stuart Boesky" *Comp.* at ¶ 95.

On or about July 10, 2012, Levine sent an e-mail to Boesky, stating that Levine, Dick, and Wissel "have been defending each entity/contributor since" since 2007 and opined that the IRS's "main theory of the case was 'weak at best' and that '[t]here is plenty of case law that supports the notion that there does not need to be a business purpose for a charitable contribution'". *Id.* at ¶ 97. Levine further stated in his e-mail that he had "been trying to settle the cases without going to trial for the past 5 years" and "made some proposals . . . trying to avoid the cost of litigation and have been consistently rebuffed". *Id.* Levine stated: "10 days ago, under the guise of budget cuts, [the IRS] finally made an offer to settle the cases. Their offer was to reduce the deductions by 60% of the claimed amounts. They of course would impose interest but offered to eliminate penalties". *Id.* Levine stated that both he and Dick believed the offer to be deficient and requested that Boesky contribute approximately $50,000, as his "share of the litigation fund" to pay for the trial of the RERI Tax Case, and to make the check payable to "Herrick, Feinstein LLP Attorney Trust Account". *Id.*

On April 29, 2013, Katz sent an e-mail to the participants of the remainder interest tax strategy, including plaintiffs, providing them with an update on the RERI Tax Case. *Id.* at ¶ 99. Katz stated: "as a legal matter, all of the participants in the remainder interest donation cases will be bound by the legal conclusions advanced in the case". *See id.* He further stated that the "only proposal offered by the IRS was that if ALL of the entities agreed to concede 60% of the charitable deductions the IRS would allow the investors to deduct 40% of the original claimed deduction. Randal [Dick] countered (over 10 months ago) with our proposal that we would

concede 25% of the deduction in order to settle the cases. We have, as of yet, not received a response from the IRS". *See Comp. at* ¶99.

On November 6, 2013, Dick sent an e-mail to the participants of the remainder interest tax strategy, including plaintiffs, regarding the RERI Tax Case, stating that 18 months prior, he requested from more than 100 investors that they send him their pro rata share to the "litigation fund". *Id.* at ¶100. Dick stated that over 50 individuals sent their pro rata share, but that plaintiffs and the other recipients of the e-mail had not. Dick stated that if he did not receive payment promptly, he would be "resigning from your representation and will inform the [IRS] of this". *Id.* Dick also stated the following:

> "You are hereby advised to hire independent counsel to advise you in all dealings with the [IRS] regarding remainder interests. In addition, you should be aware that due to the fact that the litigation fund, that has been collected to date, is almost exhausted my next act will be to attempt to settle (on whatever terms the IRS is willing to settle) the RERI litigation. This settlement, however disadvantageous to the taxpayer, will become the threshold for the [IRS] in all your cases. As you know we have an informal agreement with the IRS to try only the RERI case and have it control the other cases. Once I resign that agreement will no longer apply to you or your entities" *See Comp.* ¶ 101.

On November 7, 2013, Boesky responded to Dick's e-mail stating:

> "From your e-mail it is not clear to me how much money is uncollected and if collected it is enough to positively influence the outcome of your representation and our case . . . . Has Harold [Levine] washed his hands of this? He had been the one communicating and coordinating with the group. Maybe the thing to do is set up an escrow arrangement and if enough is paid in to continue your 'vigorous' representation of the cases the escrow would be released" (*id.*). That same day, Dick responded to Boesky's e-mail as follows:

> "Harold [Levine] has in no way 'washed his hands' of this . . . . It would really be a waste to have to throw in the towel at this late date since I believe we have a good case. I also think the government is beginning to agree with me . . . . I am unwilling to accept

> the escrow concept. There is already too much red tape involved in this representation and I believe having the funds deposited into my trust account is more than sufficient. If you need additional information please contact [Levine]". *Id.* at ¶ 102.

On June 4, 2014, the United States Attorney's Office for the Southern District of New York (US Attorney) filed a civil complaint against Levine in the Southern District of New York, alleging that he promoted, implemented, and/or participated in at least 90 unlawful tax strategies and acquired more than $5 million in fees for his role in the unlawful transactions. *See id.* at ¶103. The US Attorney sought to enjoin Levine from promoting any tax plan, including tax shelter strategies. *Id.* The complaint also sought to require Levine to produce a list of names of individuals and entities that participated in any tax scheme promoted by Levine from 2005 onward. *Id.* In addition, it listed a number of tax shelter strategies believed to be unlawful and the entities that were alleged to have participated in them. However, the remainder interest tax strategy and the LLCs in which plaintiffs invested were not listed. *Id.* at ¶100.

After the US Attorney filed the complaint against Levine, Levine downplayed the risk of losing the RERI Tax Case and of its members, including plaintiffs, becoming liable to the IRS and the NYSDTF for significant tax assessments, penalties and interest. *Id.* at ¶105. In June and September 2014, Levine forwarded to plaintiffs status reports on the RERI Tax Case that were prepared by Dick. *Id.* at ¶¶ 106-107.

On September 6, 2014, Boesky e-mailed Levine with respect to the RERI Tax Case, stating: "Someone needs to calculate what this will cost us if we lose so we can start planning". *Comp.* at ¶108. Levine responded: "You should speak to your accountant. He is the only one who will know that answer". *Id.*

On September 7, 2014, Boesky e-mailed Levine stating: "Harold I think the group is owed more color and assessment of the status. . . . I get the feeling we are in a very bad situation with a low probability of succeeding in litigation with a party that is not inclined to settle. You owe me and the others [sic] defendants an assessment of the situation". *Id.* at ¶109. Levine replied that he would "ask . . . Dick to respond". *Id.*

In September and October 2014, Levine sent Boesky several e-mails from his Moritt Hock account advising Boesky in regard to potential settlement deals with the IRS and New York State. *Id.* at ¶110. The e-mails included a confidentiality notice stating that the information contained in the e-mail and attachments were "legally privileged and confidential information". *Id.*

On November 4, 2014, Levine advised Boesky in an e-mail that RARE Investments IV LLC was subject to a written stipulation with the IRS that the assessment of tax deficiencies and penalties against it would be subject to the outcome of the RERI Tax Case. Further, the assessment of tax deficiencies and penalties against the other LLCs would also be subject to the outcome of the RERI Tax Case. *Id.* at ¶113.

On April 7, 2015, Boesky e-mailed Levine stating: "I appreciate your efforts . . . . Given the amount of liability I could bear and the lack of information I have about this matter, I hope you understand my concern". *Comp.* at ¶114. Levine replied: "I have always been willing to help you (if I can) and I know the exposure is big (we all have it to some degree)". *Id.*

On or about April 27, 2015, Jeffery Blau, the CEO of Related and a member of RERI, wrote to the other members of RERI informing them that Levine had resigned as RERI's TMP

and that Dick was no longer representing RERI due to serious health issues. *Id.* at ¶115. However, Levine continued to provide counsel to plaintiffs regarding the RERI Tax Case and the related audits through at least June of 2016. *Id.* at ¶¶116-118.

When Levine and Katz were called to testify at the June 2015 trial of the RERI Tax Case, they both refused to testify based upon their Fifth Amendment privilege against self-incrimination. *Id.* at ¶120. During the RERI Tax Case, plaintiffs discovered that approximately two years after the LLCs made their donations of the remainder interests, Levine and Katz approached the charities that received the donations, and directly purchased, or entered into agreements to purchase, the previously donated remainder interests from those charities. In most instances, Levine and Katz sold the remainder interests, or the rights to purchase the remainder interests back to the present interest holders at a profit, or, in the alternative, brokered the remainder interests to the present interest holder for a fee. Levine and Katz never disclosed such transactions to the individuals who invested in the remainder interest tax strategy. *Id.* at ¶121.

On October 26, 2016, the US Attorney filed an eight-count indictment against Levine and Katz alleging that they engaged in a multi-year tax evasion scheme involving the diversion of millions of dollars of fees from a Manhattan law firm and failed to report that fee income to the IRS. *See Comp.* at ¶125. According to the press release issued by the US Attorney, Levine diverted from the law firm more than $3 million in fee income from tax shelters and related transactions that Levine worked on while serving as a partner of the firm. *Id.* With respect to Katz, the press release stated that he received and failed to report more than $1.2 million in fee income. *Id.* The press release indicated that Levine was charged with obstructing the IRS,

conspiracy, tax evasion, wire fraud, and making false statements. *Id.* at ¶126. Katz was charged with obstructing the IRS, conspiracy, and tax evasion. *See id.* at ¶126.

On February 10, 2017, plaintiffs commenced the instant action against Levine, Herrick Feinstein, Morrit Hock, Katz, and Mazars USA, alleging that none of the defendants informed plaintiffs that the remainder interest tax strategy was likely to be challenged by the taxing authorities and/or found to be unlawful. *Id.* at ¶139. Instead, they continuously overstated the legitimacy of the strategy and understated its risks and the likelihood of an audit resulting in additional tax assessments, interest, and penalties. *Id.* at ¶140. All of the defendants were illegally promoting an unregistered tax shelter while advising plaintiffs to the contrary. *See id.* at ¶144. In filing their tax returns, plaintiffs relied upon these misrepresentations. *See id.* at ¶148.

Plaintiffs further allege in their complaint that defendants had a financial, business, and proprietary interest to induce plaintiffs, and others, to enter into these tax shelter transactions, and in doing so, assured them that the transactions would enable them to reduce their taxes. *See Comp.* at ¶¶ 139-151. Defendants never disclosed to plaintiffs that their representation and advice would be materially limited and impaired by their own interests in the transactions they were promoting *Id.* Defendants never retracted their advice regarding the propriety of the strategy they promoted or advised them to amend their returns, even after the IRS issued a notice unmistakably referring to the remainder interest tax strategy or after Levine and Katz were indicted, for among other things, the work they performed at Herrick Feinstein, Moritt Hock, and Mazars USA. *Id.* at ¶168-170.

Had Levine and Moritt Hock provided plaintiffs with appropriate and accurate advice regarding the strength of the IRS's position in the RERI Tax Case, plaintiffs would have settled their respective liabilities with the IRS and the NYSDTF in an effort to avoid their exposure to incurring additional interest and penalties on all their tax liabilities stemming from the remainder interest tax strategy investments. *See id.* at ¶122. In addition, they would not have contributed towards the legal costs incurred in prosecuting the RERI Tax Case. *See id.* ¶123-122.

The complaint further alleges, upon information and belief, that "Dick, who was unilaterally chosen by Levine and Katz . . . to act as lead counsel in the RERI Tax Case, was not acting in the best interests of RERI's members in prosecuting and attempting to settle [the case], but was mainly acting to benefit Levine and Katz in an effort to whitewash their wrongdoing with respect to promoting unlawful tax shelters". *See id.* ¶124. According to the complaint, plaintiffs did not discover, and could not have discovered, defendants' "fraudulent misconduct" until after Levine and Katz's indictment in October 2016. *See id.* at ¶154.

The complaint sets forth the following causes of action: legal malpractice; fraud; constructive fraud/negligent misrepresentation; conspiracy to commit fraud; the imposition of a constructive trust; forfeiture of fees and unjust enrichment; breach of fiduciary duty; failure to supervise; and a declaratory judgment. Defendants Mazars USA, Herrick Feinstein, Moritt Hock, and Levine separately move to dismiss the complaint insofar as asserted against them pursuant to CPLR 3211 (a) (5) as barred by the statute of limitations, and CPLR 3211 (a) (7) for failure to state a cause of action. The motions are decided as follows.

II. Discussion

A. Motion to Dismiss Standard

"On a motion to dismiss a cause of action pursuant to CPLR 3211 (a) (5) on the ground that it is barred by the statute of limitations, a defendant bears the initial burden of establishing, prima facie, that the time in which to sue has expired. In considering the motion, a court must take the allegations in the complaint as true and resolve all inferences in favor of the plaintiff. Further, "plaintiff's submissions in response to the motion must be given their most favorable intendment". *See Norddeutsche Landesbank Girozentrale v. Tilton,* 149 A.D.3d 152, 158 (1st Dept 2017). Once the defendant meets the "burden of proving, prima facie, that the time in which to sue has expired, the burden then shifts to the plaintiff to raise a question of fact as to whether the statute of limitations is tolled or is otherwise inapplicable". *See Stein Indus., Inc. v. Certilman Balin Adler & Hyman, LLP*, 149 A.D.3d 788, 789 (2d Dept 2017); *CLP Leasing Co., LP v. Nessen*, 12 A.D.3d 226, 227 (1st Dept 2004).

"On a CPLR 3211 (a) (7) motion to dismiss for failure to state a cause of action, the complaint must be construed in the light most favorable to the plaintiff and all factual allegations must be accepted as true. . . . Further, on such a motion, the complaint is to be construed liberally and all reasonable inferences must be drawn in favor of the plaintiff". *See Alden Global Value Recovery Master Fund, L.P. v. KeyBank N.A.*, 159 A.D.3d 618, 621-622 (1st Dept 2018). "However, factual allegations . . . that consist of bare legal conclusions, or that are inherently incredible . . . , are not entitled to such consideration" *Mamoon v. Dot Net Inc.*, 135 A.D.3d 656, 658 (1st Dept 2016).

B. First Cause of Action: Legal Malpractice

The first cause of action is for legal malpractice and is asserted against Levine, Herrick Feinstein, and Moritt Hock. *See Comp.* ¶¶ 172-185. Plaintiffs allege that these defendants breached their duty to represent plaintiffs with such reasonable skill, care and diligence as members of the legal profession commonly exercise in similar situations by: failing to implement adequate controls to protect clients such as plaintiffs from the intentional fraud and the negligent misconduct of Levine; not doing anything to prevent Levine from marketing and promoting unlawful tax shelters and in profiting from those acts; failing to apprise plaintiffs as additional legal developments, rulings and decisions were issued by the IRS and the courts making it clear the tax shelters they were promoting were not legitimate; and in continuing to provide flawed and erroneous advice despite their continuing representation of plaintiffs through 2016. *See id.* at ¶¶174-181.

In connection with the first cause of action, plaintiffs seek monetary damages, "including . . . the payment to Levine, Herrick Feinstein, and Moritt Hock for tax and legal advice; the loss of legitimate tax savings opportunities and tax deductions; having paid or incurring tax penalties and interest; having to make tax payments they were promised they would not have to make and were advised not to make; and having paid and continuing to incur substantial additional costs to hire new tax and legal advisors to rectify the situation". *Id.* at ¶185.

Levine, Herrick Feinstein, and Moritt Hock each contend that this cause of action is time-barred. Plaintiffs have conceded that their malpractice claim insofar as asserted against Herrick Feinstein is untimely. *See* Plaintiffs' Memorandum of Law in Opposition to Defendant Herrick

Feinstein's Motion to Dismiss Complaint, at 8 n3. Therefore, the only remaining defendants against whom this cause of action is asserted are Levine and Moritt Hock.

With respect to Levine, the complaint alleges that he initially promoted the remainder interest tax strategy in 2002 and then proceeded to form the LLCs needed to execute the strategies from 2002 to 2004. Between 2002 and 2004, plaintiffs invested various amounts in these entities and claimed charitable deductions based upon the strategy from 2002 to 2005. Pursuant to CPLR 214 (6), an action for nonmedical professional malpractice must be commenced within three years of the date of accrual. Claims for legal malpractice "accrue when the malpractice is committed, not when the client learns of it". *See Palmeri v. Willkie Farr & Gallagher LLP*, 156 A.D.3d 564, 567 (1st Dept 2017). Therefore, any claims sounding in professional malpractice that are based upon Levine's advice to participate in the remainder interest tax strategy and the services he provided in order to implement the strategies are untimely under the three-year statute of limitations set forth in CPLR 214(6).

Plaintiffs assert, however, that the complaint pleads allegations that Levine continued to represent them in connection with the remainder interest tax strategy until 2016 by advising them on how to proceed with the IRS's and the NYSDF's challenges to their use of the strategy. Therefore, plaintiffs contend, the continuous representation doctrine applies to toll the statute of limitations.

"[P]ursuant to the doctrine of continuous representation, the time within which to sue on the claim is tolled until the attorney's continuing representation of the client with regard to the particular matter terminates". *See Aqua-Trol Corp. v. Wilentz, Goldman & Spitzer, P.A.*, 144

A.D.3d 956, 957 (2d Dept 2016); *Rodeo Family Enters., LLC v. Matte*, 99 A.D.3d 781, 784 (2d Dept 2012); *Sun Graphics Corp. v. Levy, Davis & Maher, LLP*, 94 A.D.3d 669, 669 (1st Dept 2012). "The continuous representation doctrine tolls the running of the statute of limitations on a cause of action against a professional defendant only so long as the defendant continues to represent the plaintiff in connection with the particular transaction which is the subject of the action and not merely during the continuation of a general professional relationship". *See Transport Workers Union of Am. Local 100 AFL-CIO v. Schwartz*, 32 A.D.3d 710, 713 (1st Dept 2006). For the doctrine to apply, there must be "a mutual understanding of the need for further representation on the specific subject matter underlying the malpractice claim". *McCoy v. Feinman*, 99 N.Y.2d 295, 306 (2002); *see also Williamson v. PricewaterhouseCoopers LLP*, 9 N.Y.3d 1, 11 (2007) (explicit contemplation of further representation regarding the matter at issue is required).

Here, the complaint does not allege that there was an "express, mutual agreement to advise" plaintiffs on the effect of the remainder interest tax strategy after Levine's original advice. *Apple Bank for Sav. v. PricewaterhouseCoopers LLP*, 70 A.D.3d 438, 438 (1st Dept 2010); *Johnson v. Proskauer Rose LLP*, 129 A.D.3d 59, 68 (1st Dept 2015) ("while there was certainly the *possibility* that the need for future legal work would be required with respect to the tax strategy (promoted by the defendants), plaintiffs could not have 'acutely' anticipated the need for further counsel from defendants that would trigger the continuous representation toll").

Plaintiffs seemingly rely on the principle that "[t]he law recognizes that the supposed completion of the contemplated work does not preclude application of the continuous

representation toll if inadequacies or other problems with the contemplated work timely manifest themselves after that date and the parties continue the professional relationship to remedy those problems". *See Regency Club at Wallkill, LLC v. Appel Design Group, P.A.*, 112 A.D.3d 603, 607 (2d Dept 2013); *see also Stein Indus., Inc. v. Certilman Balin Adler & Hyman, LLP*, 149 A.D.3d at 789. "In this regard, a motion to dismiss pursuant to CPLR 3211 (a) (5) will be denied unless the facts establish that a gap between the provision of professional services on the particular matter is so great that the representation cannot be deemed continuous as a matter of law". *Regency Club at Wallkill, LLC v. Appel Design Group, P.A.*, 112 A.D.3d at 607.

Here, the complaint alleges that plaintiffs received counsel from Levine between 2002 to 2004 regarding the tax strategy. However, it was not until three years later, in 2007, that Levine began to counsel them on the same subject matter -- i.e., how to handle the IRS's and NYSDTF's challenges to the strategy. This three-year gap between the provision of Levine's services on this matter is so great that the representation cannot be deemed continuous. *See Landow v. Snow Becker Krauss, P.C.*, 111 A.D.3d 795, 797 (2d Dept 2013) (stating "as evidenced by, inter alia, the more than four-year period of time between the issuance of the opinion letter and the plaintiff's alleged retention of the defendants in July 2007, during which no further legal representation was undertaken with respect to the subject matter of the opinion letter, the parties did not contemplate that any further representation was needed"). As such, any claims based upon the advice rendered by Levine from 2002 through 2004 are untimely.

As discussed above, in July 2017, the Tax Court disallowed RERI's claimed charitable contribution in full on the ground that RERI failed to satisfy the substantiation requirements of

Income Tax Regulation 1.170A-13(c)(2), which required it to disclose its costs or other basis in the charitably contributed property and also upheld the IRS's imposition of a "gross valuation misstatement" penalty against RERI.[2] The deficient advice which led to the failure to satisfy the substantiation requirements and to properly value the donated property was received by plaintiffs

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[2] Income Tax Regulation 1.170A–13(c) sets forth substantiation requirements that apply to certain charitable contributions of property worth more than $5,000. The failure to satisfy the substantiation requirements results in the denial of a deduction for the contribution (*see* Income Tax Regulations § 1.170A–13[c][1][I]). In order to satisfy the requirements of section 1.170A–13(c) , the donor must obtain a qualified appraisal of the contributed property, attach a "fully completed" appraisal summary to the return on which the deduction is first claimed, and maintain records containing specified information (*see* Income Tax Regulations § 1.170A–13[c][2][I]). The summary must include the adjusted cost or other basis of the donated property (*see* Income Tax Regulations § 1.170A–13[c][4][ii][E]).

In the case of RERI, the Tax Court found that since the appraisal summary form it attached to its 2003 return showed no amount in the space provided for the "Donor's cost or other adjusted basis," RERI's appraisal summary did not satisfy the substantiation requirements. Since the omission prevented the appraisal summary from achieving its intended purpose, the court refused to excuse the failure on the grounds of "substantial compliance" and denied the deduction for the entire contribution (*see RERI Holdings I, LLC, Jeff Blau, Tax Matters Partner v Commissioner*, 149 T.C. No. 1 at *9).

The Tax Court noted that since RERI did not meet the substantiation requirements set forth in regulation 1.170A–13(c) , the value of the donated property was irrelevant to the issue of the deduction amount to which RERI was actually entitled for the contribution (*see id.* at *13). The court nonetheless determined the value of the donated property in order to decide whether to impose an accuracy-related "gross valuation misstatement" penalty against RERI pursuant to section 6662(h)(2) of the Internal Revenue Code. Under section 6662(h)(2), a property value claimed on a return results in a "gross valuation misstatement" penalty if that value is 400% or more of the property's correct value.

The Tax Court determined that the contribution made by RERI had an actual fair market value of $3,462,886 on the date it was made (*see id.* at *19). Since the $33,019,000 value that RERI had assigned to the contribution on its tax return was 953.5% of the contribution's actual fair market value, RERI's claimed deduction resulted in a "gross valuation misstatement," the penalty rate for which is 40% of the underpayment. The court concluded that RERI did not make a "good-faith investigation" of the contribution's value as of the date of the contribution and therefore no RERI partner would be able to avoid the penalty on the basis of the "reasonable cause" exception provided in section 6664(c) (*see id.* at *20-*22).

from 2002 to 2004. Therefore, a malpractice claim based upon the damages caused by this advice is time-barred.

The complaint alleges that plaintiffs received advice from Levine from 2007 forward regarding the taxing authorities' challenge to their use of the remainder interest tax shelter strategy. As just discussed, this advice does not warrant application of the continuous representation doctrine. Moreover, this advice, alone, cannot form the basis for a malpractice action. Plaintiffs are essentially contending that Levine overstated the strength of their case, and that but for Levine's deficient advice, they would have settled with the taxing authorities rather than pursuing the RERI tax case, resulting in a more favorable outcome. However, the impact of Levine's advice in this regard is predicated on speculation. Therefore, it cannot support a legal malpractice claim. *See Pellegrino v. File*, 291 A.D.2d 60, 63 (1st Dept 2002) ("speculative damages cannot be a basis for legal malpractice"); *Dweck Law Firm v Mann*, 283 A.D.2d 292, 293 (1st Dept 2001) (legal malpractice action requires "specific factual allegations establishing that but for counsel's deficient representation, there would have been a more favorable outcome to the underlying matter"); *Zarin v. Reid & Priest*, 184 A.D.2d 385, 387-388 (1st Dept 1992) ("damages claimed in a legal malpractice action must be 'actual and ascertainable' resulting from the proximate cause of the attorney's negligence"). As such, the first cause of action is dismissed insofar as asserted against Levine.

Turning to Morrit Hock, there is no indication that Levine had any involvement or affiliation with Morrit Hock prior to September 2012. By September 2012, the harm caused by Levine's advice to pursue the remainder interest tax strategy (i.e., plaintiffs' problems with state

and federal taxing authorities) was already done and the decision to pursue the RERI tax case in order to challenge the IRS's determination was already made. The post-September 2012 allegations involving Levine, standing alone, fail to satisfy the threshold standard necessary to maintain a legal malpractice action, which requires "specific factual allegations establishing that but for counsel's deficient representation, there would have been a more favorable outcome to the underlying matter". *Dweck Law Firm, LLP v. Mann*, 283 A.D.2d at 293. According to the complaint, Levine's actions after September 2012 consisted of forwarding status reports prepared by Dick to the plaintiffs and keeping them apprised of potential settlement deals. The complaint does not allege that these particular actions were deficient or caused them harm or that if Levine had not undertaken them, the outcome would have been different. Furthermore, for the reasons stated above, any damages caused by Levine's post-2007 advice are speculative. As such, the first cause of action is also dismissed insofar as asserted against Morrit Hock.

The first cause of action is dismissed in its entirety against Defendants Herrick Feinstein, Harold Levine, and Morritt Hock.

C. Second Cause of Action: Fraud

The second cause of action is for fraud. *Comp.* ¶¶ 186-199. Plaintiffs allege that all of the defendants knowingly made affirmative misrepresentations and omissions with the intent that plaintiffs would rely upon them in deciding to retain defendants, in entering into the tax shelter transactions, and in paying defendants' fees. But for the intentional misrepresentations and material omissions described in the complaint, plaintiffs would have availed themselves of

legitimate tax savings opportunities and would have promptly amended their returns. Plaintiffs did not know, and could not have known, that defendants' fraud occurred because of the continued concealment of the circumstances surrounding Levine's and Katz's actions to defraud not only the IRS and the NYSDF, but their clients as well, which were unknown to plaintiffs until Levien and Katz were indicted in October 2016. *See Comp. at* ¶195.

With respect to damages, the second cause of action alleges that in reasonable reliance on defendants' false representations and misleading omissions, plaintiffs paid defendants and have incurred, or will incur, penalties, interest, and additional taxes and other expenses. *Id.* ¶197. As a result of the fraud, plaintiffs also failed to avail themselves of legitimate tax savings available to them. Additionally, to correct the consequences of the fraud, plaintiffs incurred, and will continue to incur, substantial additional costs to hire new tax and legal advisors to rectify the situation. *Id.* at ¶197. Plaintiffs further assert that they are entitled to punitive damages in order to punish defendants and deter similar misconduct in the future. *Id.* at ¶199.

The crux of defendants' argument in seeking to dismiss this cause of action is that while it is denominated a cause of action for fraud, it is, in essence, a time-barred professional malpractice claim and should therefore be dismissed. "Where . . . a fraud claim is asserted in connection with charges of professional malpractice, it is sustainable only to the extent that it is premised upon one or more affirmative, intentional misrepresentations -- that is, something more egregious than mere concealment or failure to disclose [one's] own malpractice -- which have caused additional damages, separate and distinct from those generated by the alleged malpractice". *See White of Lake George v. Bell*, 251 A.D.2d 777, 778 (3d Dept 1998); *see also*

Weiss v. Manfredi, 83 N.Y.2d 974, 977 (1994) ("attorney's failure to disclose malpractice does not give rise to a fraud claim separate from the customary malpractice action"); *Carl v. Cohen*, 55 A.D.3d 478, 478-479 (1st Dept 2008) (fraud claim deemed duplicative of legal malpractice claim where it "was not based on an allegation of independent, intentionally tortious conduct and failed to allege separate and distinct damages"). Where the "plaintiffs have not shown that their reliance upon the[] alleged misrepresentations subjected them to any damages beyond those resulting from the purported malpractice alone, their fraud claim is not maintainable." *White of Lake George v. Bell*, 251 A.D.2d at 778; *cf. Johnson v. Proskauer Rose LLP*, 129 A.D.3d at 69 "damages plaintiffs seek for the fraud and malpractice causes of action do not completely overlap with each other"; complaint "seeks far more money in damages under the fraud cause of action than under the malpractice cause of action"). "The key to determining whether a claim is duplicative of one for malpractice is discerning the essence of each claim". *Johnson v. Proskauer Rose LLP*, 129 A.D.3d at 68. Indeed, "[t]he test of a cause of action, for Statute of Limitations purposes, is its gravamen not the form in which it is pleaded". *Wilson v. Bristol-Myers Co.*, 61 A.D.2d 965, 965 (1st Dept 1978).

Here, plaintiffs' fraud claim is not based simply upon errors of professional judgment or the failure to disclose one's own malpractice. Rather, plaintiffs are asserting that defendants intentionally and knowingly promoted a tax shelter strategy they knew to be unlawful, or at best risky, in an effort to profit from it and did so without disclosing that they had a direct financial interest in promoting the strategy. They are also asserting that defendants continued to reassure them about the legitimacy of the strategy and the viability of their position in order to keep

collecting fees for their services and to cover up Levine's and Katz's involvement in promoting and profiting from illegal tax shelters. Although the complaint does not allege separate and distinct damages from the malpractice claim, the essence of the fraud and malpractice claims are sufficiently distinct. *See Johnson v. Proskauer Rose LLP,* 129 A.D.3d at 70 ("Proskauer's narrow focus on what each claim seeks in damages ignores its own statement as to what the focus should be in determining whether claims are duplicative; that is, the essence of the claims. Here, the essences of the fraud and malpractice claims are sufficiently distinct from one another that the court properly did not invoke the duplicative claims doctrine").

Nevertheless, the fraud cause of action is time-barred. "An action based upon fraud must be commenced within the greater of six years from the date the cause of action accrued or two years from the time plaintiff discovered or, with reasonable diligence, could have discovered the fraud". *Gutkin v. Siegal,* 85 A.D.3d 687, 687 (1st Dept 2011); *see* CPLR 213 [8]. "[W]here the circumstances are such as to suggest to a person of ordinary intelligence the probability that he has been defrauded, a duty of inquiry arises, and if he omits that inquiry when it would have developed the truth, and shuts his eyes to the facts which call for investigation, knowledge of the fraud will be imputed to him". *Gutkin v Siegal,* 85 A.D.3d at 688; *see CSAM Capital, Inc. v. Lauder*, 67 A.D.3d 149, 156 (1st Dept 2009).

Here, plaintiffs' fraud claims accrued in 2002, when they entered into the first allegedly fraudulent transaction promoted and facilitated by Levine and Katz. S*ee Kanterakis v. Kanterakis*, 125 A.D.3d 814, 816 (2d Dept 2015). Plaintiffs did not commence this action until 2017 -- 15 years later. Plaintiffs also did not initiate this action within two years of when they

could, with reasonable diligence, have discovered the facts constituting the alleged fraud. Plaintiffs allege that it was not until the 2016 indictment that plaintiffs discovered Levine and Katz inflated the legitimacy of the remainder interest tax strategy, that they had a conflict of interest in promoting it, or that they had a conflict of interest in counseling them to pursue the RERI Tax Case as opposed to settling the matter. However, the 2016 indictment was unrelated to the remainder interest tax strategy. More importantly, plaintiffs should have been aware of the circumstances sooner.

In 2006, the IRS and NYSDTF began to audit the entities and individual members engaged in the remainder interest tax strategy. In 2007, plaintiffs were in receipt of a notice from the NYSDTF stating that it had determined transactions identical to, or similar to, the remainder interest tax strategy were "avoidance transactions". *Comp.* ¶ 63. That same year, the IRS deemed such transactions to be "transactions of interest". *See id at* ¶¶ 72, 75. Therefore, by 2007 at the latest, plaintiffs should have been aware that, contrary to the advice given by Levine and Katz, the remainder interest tax strategy was problematic. S*ee TMG-II v. Price Waterhouse & Co.*, 175 A.D.2d 21, 22-23 (1st Dept 1991) (knowledge that IRS is questioning legitimacy of transaction creates duty of inquiry for related fraud claim).

Further, by February 2013, it should have been apparent to plaintiffs that Levine and Katz were benefitting from the transactions at issue by re-purchasing the remainder interests because on February 15, 2013 and May 22, 2014, filings in the RERI tax case revealed they were doing so. *See* Zaiger Affirm. Ex. 10 at *3; Ex. 12 ¶¶ 18-21. Additionally, in June 2014, the civil case filed by the US Attorney put plaintiffs on notice that Levine promoted, implemented and/or

participated in at least 90 unlawful tax schemes and that he acquired more than $5 million in fees for his role in the unlawful transactions. The same lawsuit identified Katz as an individual who received millions of dollars from the transactions. *See* Zaiger Affirm. Ex. 13 at ¶¶ 1, 11, 103-104. Therefore, even assuming defendants concealed Levine's and Katz's self-interest, the two-year discovery period would have begun in 2014 and expired in 2016. Plaintiffs did not commence this action until 2017. Accordingly, even if the cause of action for fraud is adequately pleaded, and even if it is not duplicative of the malpractice claim, it is nonetheless untimely, and it is therefore dismissed insofar as asserted against Defendants Mazars USA LLP, Herrick Feinstein LLP, and Moritt Hock & Hamroff LLP, and Harold Levine.

D. Third Cause of Action: Constructive Fraud/Negligent Misrepresentation

The third cause of action is for constructive fraud/negligent misrepresentation. *See Comp. at* ¶¶ 200-208). Plaintiffs allege in this regard that defendants made numerous false affirmative representations and concealed and/or failed to disclose material facts to plaintiffs as to the legitimacy of the remainder interest tax strategy. *See id.* at ¶¶ 202-203. They did so in order to induce plaintiffs to: (1) retain defendants; (2) enter into the tax shelter transactions; and (3) pay defendants' fees. *See id.* at ¶ 204. The complaint alleges that but for the "negligent or innocent misrepresentations and material omissions" made by defendants, plaintiffs would have availed themselves of legitimate tax savings opportunities and deductions, would never have claimed the tax shelter losses on their state and federal tax returns, and would have promptly amended their returns. *See id.* at ¶ 205. It further alleges that defendants failed to correct their past tax advice

and continued to provide flawed and erroneous advice "despite their continued representation of Plaintiffs through 2016". *See id.* at ¶206. Plaintiffs did not know, and could not have known, that this constructive fraud occurred "because of the negligent misrepresentation and omissions of Defendants . . . as well as the continued concealment of the circumstances surrounding Levine's and Katz's actions to defraud not only the IRS and [the NYSDTF], but their clients as well, which were unknown to Plaintiffs until Levine and Katz were indicted in October 2016". *See id.* at ¶207.

"A cause of action predicated upon the ground of constructive fraud must be commenced within six years from the date of the commission of the fraud (CPLR 213(1))". *See Quadrozzi Concrete Corp. v. Mastroianni*, 56 A.D.2d 353, 355-356 (2d Dept 1977). The two-year discovery rule does not apply. *See Schoen v. Martin*, 187 A.D.2d 253, 254 (1st Dept 1992). A cause of action for negligent misrepresentation is also subject to a six-year statute of limitations and "accrues on the date of the alleged misrepresentation which is relied upon by the plaintiff". *Fandy Corp. v. Lung-Fong Chen*, 262 A.D.2d 352, 353 (2d Dept 1999); *see also* CPLR 213 [1]. This action was commenced more than six years after plaintiffs were allegedly induced by misrepresentations to participate in the remainder interest tax strategy and more than six years after they were allegedly induced by misrepresentations to challenge the taxing authorities' determination by pursuing the RERI Tax Case. Therefore, the third cause of action for constructive fraud/negligent misrepresentation is also dismissed as time-barred insofar as asserted against Defendants Mazars USA LLP, Herrick Feinstein LLP, and Moritt Hock & Hamroff LLP, and Harold Levine.

E. Fourth Cause of Action: Conspiracy to Commit Fraud

The fourth cause of action is for conspiracy to commit fraud. *See Comp.* at ¶¶ 200-215. Plaintiffs allege in this regard that defendants engaged in a civil conspiracy to commit the wrongful acts alleged in the first three causes of action. *See id.* at ¶211. Since "the State of New York does not recognize an independent cause of action in tort for conspiracy". *See Salerno v. Pandick, Inc.*, 144 A.D.2d 307, 308 (1st Dept 1988), citing *Alexander & Alexander of N.Y. v. Fritzen*, 68 N.Y.2d 968, 969 (1986), this cause of action is dismissed insofar as asserted against Defendants Mazars USA LLP, Herrick Feinstein LLP, and Moritt Hock & Hamroff LLP, and Harold Levine.

F. Fifth Cause of Action: Imposition of a Constructive Trust

The fifth cause of action seeks to impose a constructive trust. *See Comp.* at ¶216-219. This cause of action alleges that defendants "acquired fees, and the value of the remainder interests from the plaintiffs through fraud, constructive fraud/negligent misrepresentation, malpractice, breach of fiduciary duties, and other improper means, including civil conspiracy". *Id.* at ¶217. The retention, for their own benefit, of the fees received from plaintiffs is contrary to the principles of equity and therefore, plaintiffs are entitled to "the imposition of a constructive trust on each Defendant in the amount of fees paid by Plaintiffs". *Id.* at ¶ 219.

This cause of action is also time-barred. "It is well settled that the Statute of Limitations applicable in actions to impress constructive trusts can be found in CPLR 213(1), which prescribes a six-year period that commences to run upon occurrence of the wrongful act giving

rise to a duty of restitution . . . and not from the time when the facts constituting the fraud were discovered". *Matter of Sakow*, 219 A.D.2d 479, 482 (1st Dept 1995); *see also Knobel v. Shaw*, 90 A.D.3d 493, 496 (1st Dept 2011). Here, the wrongful acts alleged to have given rise to the duty of restitution occurred more than six years prior to the commencement of this action.

This cause of action is therefore dismissed against Defendants Mazars USA LLP, Herrick Feinstein LLP, and Moritt Hock & Hamroff LLP, and Harold Levine.

G. Sixth Cause of Action: Unjust Enrichment and Recision

The sixth cause of action is for unjust enrichment. It seeks disgorgement of improperly obtained fees received by Herrick Feinstein, Moritt Hock, and Mazars USA based upon allegations that the services provided by them had no value and the fees charged by them were invalid and unreasonable. *See Comp.* at ¶¶ 220-222; 226-227; 231-232. The sixth cause of action further alleges that plaintiffs were induced to pay fees to these defendants as a result of their misrepresentations, omissions, and continued concealment of the circumstances surrounding Levine's and Katz's actions to defraud not only the IRS and the NYSDTF, but their clients as well, which were unknown to plaintiffs until Levine and Katz were indicted in October 2016. *See id.* at ¶¶ 223; 228; 234. Plaintiffs allege that defendants were unjustly enriched by their receipt of the fees paid by plaintiffs in that they benefitted, at plaintiffs' expense, by collecting fees that were excessive, unreasonable, unethical and improper. Equity and good conscience demand the return of those fees. Accordingly, plaintiffs assert, they are entitled to rescind the agreements to

pay these defendants and are entitled to restitution or recoupment of that amount from defendants, who must disgorge those fees to plaintiffs. *See id.* at ¶¶ 224-225; 229-230; 234-235.

The statute of limitations for unjust enrichment is six years and "accrues upon 'the occurrence of the alleged wrongful act giving rise to restitution'" *See Swain v Brown*, 135 A.D.3d 629, 632 (1st Dept 2016); *Gerschel v Christensen*, 143 A.D.3d 555, 556 (1st Dept 2016); CPLR 213 [1]. Here, the wrongful acts alleged to have given rise to the duty of restitution occurred more than six years prior to the commencement of this action and therefore, the claim for unjust enrichment is time-barred.

As to rescission claims, "[w]here, as here, 'rescission is sought on the ground of actual fraud, the Statute of Limitations is six years from the commission of the fraud or two years from when the plaintiff discovered or should have discovered the fraud, whichever is later'". *Percoco v Lesnak*, 24 A.D.3d 427, 427 (2d Dept 2005), quoting *Hoffman v Cannone*, 206 A.D.2d 740, 740-741 (2d Dept 1994). As discussed above, plaintiffs failed commence this action within the limitations period for fraud. Therefore, this cause of action is also dismissed insofar as asserted against Defendants Mazars USA LLP, Herrick Feinstein LLP, and Moritt Hock & Hamroff LLP, and Harold Levine.

H. Seventh Cause of Action: Breach of Fiduciary Duty

The seventh cause of action is for breach of fiduciary duty. *See Comp.* at ¶¶ 236-251. This cause of action alleges that defendants, through their representation of plaintiffs, had a fiduciary duty not to make negligent misrepresentations or conceal material facts, and owed

plaintiffs a duty to represent them with the utmost degree of loyalty and with such reasonable skill, care and diligence as members of the legal and accounting profession commonly possess and exercise in similar situations. *See id.* at ¶¶ 236-245. Defendants breached their duties to plaintiffs by failing to inform them that the remainder interest tax strategy was highly risky and likely to be challenged by taxing authorities. Further, as additional legal developments, rulings and decisions were issued by the IRS, the NYSDTF, and the courts, making it clear that the remainder interest tax strategy was problematic, defendants failed to timely apprise plaintiffs of those developments, to correct their misrepresentations and improper advise, to advise plaintiffs to amend and correct their tax returns, or take steps to ensure that the accountants and/or attorneys who knew or learned of these developments did so. *See id.* at ¶¶ 242; 249. Defendants had a continuing duty to correct their past financial and tax advice provided between 2002 and 2016 but failed to do so. *See id.* at ¶¶ 243; 250.

"Where an allegation of fraud is essential to a breach of fiduciary duty claim, the statute of limitations is six years, and [t]he discovery accrual rule . . . applies". *Gerschel v. Christensen*, 143 A.D.3d at 557). As discussed above, plaintiffs' claims are untimely under the six-year statute of limitations for fraud. Therefore, this cause of action is also dismissed insofar as asserted against Defendants Mazars USA LLP, Herrick Feinstein LLP, and Moritt Hock & Hamroff LLP, and Harold Levine.

I. Eighth Cause of Action: Failure to Supervise

The eighth cause of action is for failure to supervise and is asserted only against Herrick Feinstein, Moritt Hock, and Mazars USA. *See Comp.* at ¶¶ 252-256. The complaint alleges that these defendants "failed to adopt or implement adequate controls to protect their clients from wrongdoing and negligence by their own and their co-conspirator's personnel, in marketing and promoting various tax shelter, including the Remainder Interest Tax Strategy, in inducing clients to enter into costly and risky transactions, and in issuing improper, incompetent, and baseless advice or in assuring that contrary views within the firm were discussed with clients" *Id.* at ¶255.

"The statute of limitations applicable to causes of action alleging negligent hiring and negligent supervision is three years" *Calamari v. Panos*, 131 A.D.3d 1088, 1090 (2d Dept 2015); *see also Green v. Emmanuel African M.E. Church*, 278 A.D.2d 132, 132 (1st Dept 2000); *Jarvis v. Nation of Islam*, 251 A.D.2d 116, 117 (1st Dept 1998); CPLR 214 (5). The claim accrues "on the date of the last alleged underlying act". *See Pichardo v. New York City Dept. of Educ.*, 99 A.D.3d 606, 607 (1st Dept 2012). Here, all of the underlying acts alleged in this cause of action occurred before 2014. Therefore, this cause of action is time-barred and is dismissed against Defendants Herrick Feinstein, Morritt Hock and Hamroff, and Mazars LLP.

J. Ninth Cause of Action: Breach of Fiduciary Duty against Levine in his Capacity as TMP[3] for RERI

The ninth cause of action is for breach of fiduciary duty and is asserted only against Levine in his capacity as RERI's TMP. *See Comp.* at ¶¶ 257-262. In this regard, plaintiffs allege that Levine served as the TMP for RERI from 2003 until 2015 and was responsible for representing RERI before the IRS and the NYSDTF, preparing and filing RERI's tax returns, providing tax information to RERI's partners, and managing the audit processes and investigations. *Id.* at 55, ¶258. Accordingly, Levine had a fiduciary duty to the partners of RERI, including plaintiffs. In violation of that duty, Levine intentionally or recklessly made numerous misrepresentations and concealed or failed to disclose material facts by representing that the remainder interest tax strategy was legal and that attorneys at Herrick Feinstein and Moritt Hock had independently and objectively reviewed the strategy and concluded that it was lawful. *See id.* at ¶¶ 141, 250.

The ninth cause of action further alleges that due to his role as plaintiffs' attorney, "Levine had an incentive to breach his fiduciary duty to Plaintiffs in his capacity as RERI's [TMP] as a result of his material interest in generating fees from soliciting Plaintiffs as clients, inducing them to invest in RERI, forming RERI, organizing and implementing the Remainder Interest Tax Strategy through RERI, and entering into subsequent undisclosed transactions involving the purchase and sale of the remainder interest. This conflict of interest caused

[3] TMP refers to Levine's title as the "Tax Matters Partner". *See supra Part I; see also Comp.* ¶¶*83-84*.

Levine, in his capacity as RERI's [TMP], to become incapable of rendering independent judgment to avoid violating his fiduciary duty to Plaintiffs". *See id.* at ¶261.

As discussed above, "[w]here an allegation of fraud is essential to a breach of fiduciary duty claim, the statute of limitations is six years, and [t]he discovery accrual rule . . . applies". *See Gerschel v Christensen*, 143 A.D.3d at 557. Although Levine acted as RERI's TMP until 2015, the wrongful acts alleged to have been committed by him (i.e., his self-motivated advice to enter into the tax shelter transactions and to pursue to the RERI Tax Case) occurred more than six years prior to the commencement of this action. Further, for the reasons discussed above, his alleged conflict of interest could have been discovered by plaintiffs more than two years prior to the commencement of this action. As such, this claim is also time-barred and is dismissed.

K. Tenth Cause of Action: Declaratory Judgment

The tenth cause of action seeks a declaratory judgment. *See Comp.* at ¶¶263-268. Plaintiffs allege that the IRS and the NYSDTF have audited their tax returns and interest and/or penalties may be assessed against them by these entities. *See id.* at ¶266. Plaintiffs assert that defendants are legally responsible for such interest, penalties, and/or professional fees that may be incurred by plaintiffs on account of defendants' professional malpractice, fraud, constructive fraud/negligent misrepresentation, breach of fiduciary duty and civil conspiracy. *See id.* at ¶267. Accordingly, plaintiffs seek a judgment declaring that defendants are liable to them "for such damages as have not yet been paid and will be incurred in the future". *See id.* at ¶268.

[4] RERI refers to RERI Holdings I LLC. *See supra Part I; see also Comp.* ¶37.

Plaintiffs concede in their opposition papers that the viability of their declaratory judgment claim depends upon the viability of their other claims. Therefore, this cause of action is also dismissed insofar as asserted against Defendants Mazars USA LLP, Herrick Feinstein LLP, and Moritt Hock & Hamroff LLP, and Harold Levine..

L. Equitable Estoppel

Lastly, it is noted that to the extent plaintiffs may be understood as arguing that defendants are equitably estopped from asserting the statute of limitations as a defense, the argument lacks merit. Equitable estoppel may bar a defendant's reliance on the statute of limitations as a defense "where plaintiff was induced by fraud, misrepresentations or deception to refrain from filing a timely action". *Simcuski v. Saeli*, 44 N.Y.2d 442, 448-449 (1978). However, it does not apply "where the misrepresentation or act of concealment underlying the estoppel claim is the same act forming the basis of the underlying substantive cause of action". *See Transport Workers Union of Am. Local 100 AFL-CIO v. Schwartz*, 32 A.D.3d 710, 714 (1st Dept 2006). Since that is the case here, equitable estoppel is inapplicable.

III. Conclusion and Order

In accordance with the foregoing, it is hereby

ORDERED that defendant Mazars USA LLP as successor in interest to Weiser LLP's motion to dismiss the complaint insofar as asserted against it is granted, the complaint is

dismissed insofar as asserted against it, and the Clerk is directed to enter judgment accordingly (Mot. Seq. 001); and it is further

ORDERED that defendant Herrick Feinstein LLP's motion to dismiss the complaint insofar as asserted against it is granted, the complaint is dismissed insofar as asserted against it, and the Clerk is directed to enter judgment accordingly (Mot. Seq. 002); and it is further

ORDERED that defendant Moritt Hock & Hamroff, LLP's motion to dismiss the complaint insofar as asserted against it is granted, the complaint is dismissed insofar as asserted against it, and the Clerk is directed to enter judgment accordingly (Mot. Seq. 003); and it is further

ORDERED that defendant Harold Levine's motion to dismiss the complaint insofar as asserted against him is granted, the complaint is dismissed insofar as asserted against him, and the Clerk is directed to enter judgment accordingly (Mot. Seq. 004); further

ORDERED that the action is severed and continued against the remaining defendant Ronald Katz for the reasons stated in footnote 1; and it is further

ORDERED Defendant Katz shall have 10 days to file an Answer, for the reasons stated in footnote 1.

This constitutes the decision and order of the Court.

Dated: November 27, 2018

ENTER:

HON. EILEEN BRANSTEN
J.S.C.