Hernandez v Warsinske
2021 NY Slip Op 30188(U)
January 22, 2021
Supreme Court, New York County
Docket Number: 162212/2019
Judge: David Benjamin Cohen
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART IAS MOTION 3EFM

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JOSEPH HERNANDEZ

Plaintiff,

- v -

MICHAEL WARSINSKE,

Defendant.

---X

INDEX NO. 162212/2019

MOTION DATE 09/21/2020

MOTION SEQ. NO. 002

DECISION + ORDER ON MOTION

HON. JOEL M. COHEN:

The following e-filed documents, listed by NYSCEF document number (Motion 002) 35, 36, 37, 38, 39, 41, 42, 43, 44

were read on this motion to DISMISS.

This case arises from the sale of a majority interest in Sydys Corporation ("Sydys") by Defendant Michael Warsinske ("Defendant") to Plaintiff Joseph Hernandez ("Plaintiff").

In short, Plaintiff purchased the interest in Sydys in order "to operate a business focused on the development and commercialization of pharmaceuticals" and aimed "to list the company on the NASDAQ exchange" (Amended Complaint ["AC"] ¶¶5, 7 [NYSCEF 29]). But upon acquiring his interest in Sydys from Defendant, Plaintiff discovered that "Sydys was an inactive shell corporation, and accordingly, did not qualify for listing on NASDAQ" (*id.* ¶9). In his Amended Complaint, Plaintiff asserts a single cause of action for fraud, based on Defendant's alleged "material misrepresentations of fact to Plaintiff, specifically falsely representing to him that Sydys was an active operating company and was therefore eligible for immediate uplisting to NASDAQ" (*id.* ¶16).

Previously, in a Decision and Order dated July 23, 2020, this Court dismissed Plaintiff's original Complaint "solely on the ground that Plaintiffs' factual allegations fail[ed] to state a claim of fraud with the required particularity," but granted Plaintiff leave to amend his Complaint within thirty days (NYSCEF 27). Plaintiff filed his Amended Complaint on August 31, 2020 (NYSCEF 29), and Defendant now, once again, moves to dismiss. For the reasons set forth below, the motion is granted.

On a motion to dismiss pursuant to CPLR §§ 3211 (a)(1) and (7), the Court must "accept the complaint's factual allegations as true, according to plaintiff the benefit of every possible favorable inference, and determining only whether the facts as alleged fit within a cognizable legal theory" (*Weil, Gotshal & Manges, LLP v Fashion Boutique of Short Hills, Inc.*, 10 AD3d 367, 270-71 [1st Dept 2014] [internal quotation marks and citation omitted]; *see also Leon v Martinez*, 84 NY2d 83, 88 [1994]). However, bare legal conclusions and "factual claims which are either inherently incredible or flatly contradicted by documentary evidence" are not "accorded their most favorable intendment" (*Summit Solomon & Feldman v Lacher*, 212 AD2d 487, 487 [1st Dept 1995]).

A fraud claim requires "a misrepresentation or a material omission of fact which was false and known to be false by defendant, made for the purpose of inducing the other party to rely upon it, justifiable reliance of the other party on the misrepresentation or material omission, and injury" (*Lama Holding Co. v Smith Barney Inc.*, 88 NY2d 413, 421 [1996]; *P.T. Bank Cent. Asia v ABN AMRO Bank N.V.*, 301 AD2d 373, 376 [1st Dept 2003]). "A claim rooted in fraud must be pleaded with the requisite particularity under CPLR 3016 (b)" (*Eurycleia Partners, LP v Seward & Kissel, LLP*, 12 NY3d 553, 559 [2009]). "[M]ere recitation of the elements of fraud is insufficient to state a cause of action" (*Friedman v Anderson*, 23 AD3d 163, 166-167 [1st Dept

2005] [dismissing fraud claim]). If "sufficient factual allegations of even a single element are lacking," the claim must be dismissed (*RKA Film Fin., LLC v Kavanaugh*, 2018 WL 3973391, at *3 [Sup Ct, New York County 2018] [quoting *Shea v Hambros PLC*, 244 AD2d 39, 46 [1st Dept 1998]).

Plaintiff fails to plead the element of justifiable reliance as a matter of law. "[R]eliance must be found to be justifiable under all the circumstances before a complaint can be found to state a cause of action in fraud" (*VisionChina Media Inc. v Shareholder Representative Services, LLC*, 109 AD3d 49, 57 [1st Dept 2013] [dismissing fraud claim on motion to dismiss]). "What constitutes reasonable reliance is 'always nettlesome' because it is so fact-intensive" (*id.*, citing *DDJ Mgt., LLC v Rhone Group L.L.C.*, 15 NY3d 147, 155 [2010]). As a result, and as this Court has observed in other cases, "the question of what constitutes reasonable reliance is not ***generally*** a question to be resolved as a matter of law on a motion to dismiss" (*Hall v RPRT AG*, 2020 N.Y. Slip Op. 31294[U] [Sup Ct, New York County 2020] [emphasis added]).

The key word there is "generally," because despite the fact-intensive nature of the inquiry, courts can and do dismiss fraud claims for failing to plead justifiable reliance at the motion to dismiss stage. Defendant cites to many such examples in his papers, particularly in the context of sophisticated parties conducting arm's-length transactions (*see* NYSCEF 39 at 8-10 [Def.'s Mem. of Law in Supp. of Motion to Dismiss]). Therefore, it is clear that Plaintiff's allegations, taken as true, must make a threshold showing of justifiable reliance in order to survive a motion to dismiss. The question is what that showing entails.

Courts articulate the pleading requirements for justifiable reliance in different ways, but arrive at the same conclusion: "as a matter of law, a sophisticated plaintiff cannot establish that it entered into an arm's length transaction in justifiable reliance on alleged misrepresentations if

that plaintiff failed to make use of the means of verification that were available to it" (*HSH Nordbank AG v UBS AG*, 95 AD3d 185, 194-95 [1st Dept 2012] [dismissing fraud claim on motion to dismiss] [collecting cases]). Or as the Court of Appeals put it:

> [I]f the facts represented are not matters peculiarly within the party's knowledge, and the other party has the means available to him of knowing, by the exercise of ordinary intelligence, the truth or the real quality of the subject of the representation, he must make use of those means, or he will not be heard to complain that he was induced to enter into the transaction by misrepresentations.

(*Centro Empresarial Cempresa S.A. v Am. Movil, S.A.B. de C.V.*, 17 NY3d 269, 278-79 [2011] [dismissing fraud claim on motion to dismiss]). As a result, "[s]ophisticated investors must show they used due diligence and took affirmative steps to protect themselves from misrepresentations by employing what means of verification were available at the time" (*VisionChina Media*, 109 AD3d at 57; *see Global Mins. & Metals Corp. v Holme*, 35 AD3d 93, 100 [1st Dept 2006], lv denied 8 NY3d 804 [2007] ["New York law imposes an affirmative duty on sophisticated investors to protect themselves from misrepresentations . . . by investigating the details of the transactions"]). Otherwise, "plaintiffs [who] have been so lax in protecting themselves . . . cannot fairly ask for the law's protection" (*Centro Empresarial Cempresa S.A.*, 17 NY3d at 279).

Here, Plaintiff fails to allege that he "used due diligence," "investigat[ed] the details of the transaction," "ma[de] use of the means of verification that were available," or otherwise took *any* "affirmative steps to protect" himself from Defendant's alleged misrepresentation. Plaintiff is a sophisticated investor, "a biotechnology entrepreneur" who intended to purchase a majority stake in Sydys and then list the company on NASDAQ (AC ¶¶1, 7). Yet Plaintiff apparently purchased the interest in Sydys without verifying – or even attempting to verify – that it was an "active operating company." Based on the allegations in the Amended Complaint, Plaintiff apparently did not request any information about the company he was about to own, did not

consult any publicly-available data about Sydys (which was a publicly-traded company, albeit over the counter), and did not consult any regulatory filings about its activities.[1] Sydys's status as an "active operating company" was not some trivial issue; it was supposedly the cornerstone of Plaintiff's business plan, which makes the absence of due diligence even more egregious. The Amended Complaint's perfunctory nod to pleading justifiable reliance – simply reciting the boilerplate that "Plaintiff relied on these misrepresentations to his detriment" (AC ¶18) – cannot paper over these stark defects.

In the end, taking Plaintiff's allegations with respect to Sydys's inactivity as a business to be true, minimal "kicking of the tires" would have revealed to even an *unsophisticated* investor – let alone one with Plaintiff's business experience – that there were no tires. In these circumstances, Plaintiff's pleading of justifiable reliance fails as a matter of law.

Plaintiff's failure to plead justifiable reliance also evinces, more generally, a lack of specificity in the Amended Complaint. The two problems reinforce each other. Plaintiff says he relied on Defendant's assurances that "Sydys was an active operating company," (*id.* ¶8), but it is not clear what that term even means in this context. In other words, it is not clear what *facts* Plaintiff was relying on. That confusion in the pleadings persists following the acquisition. Plaintiff alleges, for example, that Sydys was "an inactive shell corporation" (*id.* ¶11) when he acquired the majority interest, but that he continued "running the Sydys [sic] as a public company for more than a year" (*id.* ¶13). It is difficult to discern what business Sydys engaged

[1] Plaintiff argues that "[t]he operation of Defendant's investment and advisory services business is a matter 'peculiarly within' his knowledge" (NYSCEF 42 at 7 [Pl.'s Mem. of Law in Opp. to Motion to Dismiss]). That argument is unavailing. First, it is a conclusory statement of fact appearing only in counsel's motion papers, not in the Amended Complaint. Second, to the extent it is true, it highlights that Plaintiff apparently did not seek such clearly crucial information from Defendant prior to the sale.

in as a publicly-traded, inactive shell company, mirroring the vagueness surrounding the term "active operating company." The lack of particularity provides a further, independent ground for dismissing the fraud claim.[2]

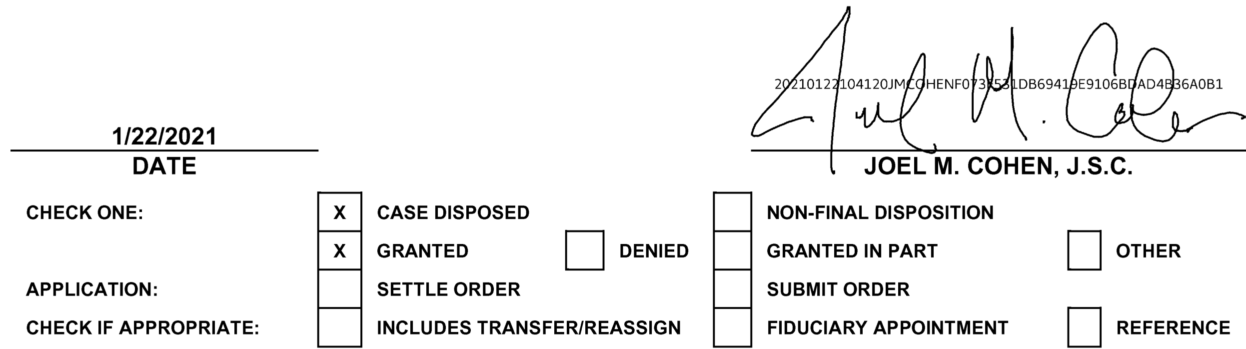
Moreover, to the extent the alleged misrepresentation embodies a combined statement not only as to whether Sydis was "active" but also that its activities were sufficient to qualify for "an immediate uplisting to NASDAQ," the representation involves a legal assertion as to which Plaintiff could (and should) have obtained his own guidance.

* * * *

Therefore, it is

ORDERED that Defendant's motion to dismiss is **GRANTED**, and Plaintiff's Amended Complaint is dismissed with prejudice, and the Clerk of the Court is directed to enter judgment accordingly.

This constitutes the decision and order of the Court.



1/22/2021
DATE

JOEL M. COHEN, J.S.C.

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

[2] The Court need not, and therefore does not, address Defendant's alternative argument that *res judicata* bars Plaintiff's claim.