SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK
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FREEDOM HOLDING INC., ELITE WORLD GROUP LLC, E1972 INC. and SILVIO SCAGLIA,

Index No. 650661/2022

Plaintiffs,

-against-

JULIA HAART A/K/A JULIA HENDLER, and HAART DYNASTY LLC,

Defendants.

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DEFENDANTS' REPLY BRIEF IN FURTHER SUPPORT OF MOTION TO DISMISS IN WHOLE OR IN PART SEVERAL OF THE REMAINING CAUSES OF ACTION OF PLAINTIFFS' FIRST AMENDED COMPLAINT

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Defendants Julia Haart aka Julia Hendler ("Haart") and Haart Dynasty LLC ("Haart Dynasty") (collectively, "Defendants"), by their attorneys, Morrison Cohen LLP, respectfully submit this Reply Memorandum of Law in further support of their Motion to Dismiss the First, Third, Fourth, and Fifth Causes of Action of Plaintiffs Freedom Holding Inc., Elite World Group LLC, E1972, Inc., and Silvio Scaglia's (collectively, "Plaintiffs") First Amended Complaint dated February 22, 2022 ("Motion to Dismiss").

PRELIMINARY STATEMENT

The deficiencies plaguing the First Amended Complaint ("FAC") have not been remedied by Plaintiffs' Opposition to the Motion to Dismiss ("Opposition"). Nor can they be.

Conceding that their claims cannot prevail under Delaware law, Plaintiffs insist that New York law should apply to each claim. But the claims for conversion, unjust enrichment, breach of fiduciary duty and constructive trust all are subject to the internal affairs doctrine, which mandates application of Delaware law.

In all events, whether analyzed under New York law or Delaware law, none of the claims at issue can withstand dismissal. *First*, the FAC does not establish standing for Plaintiff Silvio Scaglia ("Scaglia") to assert any cause of action. Plaintiffs concede that Scaglia lacks standing to assert all claims, except for breach of contract. But to establish standing in this context (i.e., one shareholder suing another), Scaglia must show – which he has not – that he personally suffered damages separate from any damages sustained by FHI.

Second, the claims for conversion, breach of contract, and unjust enrichment fail as to all Plaintiffs for independent reasons. *Conversion*: Plaintiffs do not dispute that this claim fails under Delaware law. It also fails under New York law as it is based on the same facts as their breach of contract claim. *Breach of Contract*: This fails as Plaintiffs do not plead any damages whatsoever and because the contract cannot be fully performed within a year. *Unjust*

Enrichment: This claim is based on the same facts and seeks the same damages as the conversion and breach of fiduciary duty claims, and thus is fatally duplicative.

According, the Court should grant the Motion to Dismiss in its entirety.

ARGUMENT

I. PLAINTIFFS CANNOT AVOID APPLICATION OF DELAWARE LAW

At the outset, Plaintiffs' Opposition rests on the faulty premise that the laws of New York, and not Delaware, apply to every claim. (Opposition, at 5-7). But New York's choice-of-law rules do not support blind lumping of claims together. Defendants do not contest the application of New York law to the breach of contract claim. But Delaware law applies to Plaintiffs' claims for unjust enrichment, conversion, breach of fiduciary duty, and constructive trust.

As Plaintiffs are aware, the internal affairs doctrine mandates application of the laws of the state where an entity is incorporated, which here, is Delaware. (*See* Motion to Dismiss at 8-9, citing cases). To evade this, Plaintiffs urge the Court to reject the internal affairs doctrine in its entirety, citing to one case from nearly fifty years ago that chose not to apply it. (*See* Opposition, at 6, citing *Greenspun v. Lindley*, 36 N.Y.2d 473 (N.Y. 1975)). But contrary to Plaintiffs' suggestion, the Court of Appeals did not denounce the internal affairs doctrine or create a blanket rule against its application. It did not even so much as explain why it chose to reject it in that case. *See Greenspun*, 36 N.Y.2d at 474.

Since *Greenspun*, courts have applied the internal affairs doctrine to the very kinds of claims asserted here without hesitation. *See Barmash v. Perlman*, 40 Misc.3d 1231(A), at *3 (Sup. Ct. N.Y. Cty. 2013) (applying doctrine to breach of fiduciary duty, constructive trust, and unjust enrichment claims); *see also R.B. Dev., Co., Ltd. v. Tutis Capital LLC*, 12-CV-01460-CBA-SMG, 2018 WL 7076023, at *9 (E.D.N.Y. Nov. 14, 2018) (applying laws of place of

incorporation to conversion claims against shareholders); *Hau Yin To v. HSBC Holdings* PLC, No. 15 Civ. 3590 (LTS) (SN), 2017 WL 816136 (S.D.N.Y. Mar. 1, 2017) (applying internal affairs doctrine to claims of breach of fiduciary duty and unjust enrichment), *aff'd* 700 F. App'x 66 (2d Cir. 2017); *Binn v. Bernstein*, No. 19 Civ. 6122 (GHW) (SLC), 2020 WL 4550312, at *33 (S.D.N.Y. Jul. 13, 2020) ("Pursuant to the internal affairs doctrine, unjust enrichment claims are governed by the law of XpresSpa's state of incorporation, Delaware."). To hold otherwise would defeat the purpose of incorporating. *See, e.g., Kalb, Voorhis & Co. v. Am. Fin. Corp.*, 8 F.3d 130, 132 (2d Cir. 1993) ("Because a corporation is a creature of state law whose primary purpose is to insulate shareholders from legal liability, the state of incorporation has the greater interest in determining when and if that insulation is to be stripped away.").

Tellingly, Plaintiffs do not cite a single case involving the claims here that refuses to apply the internal affairs doctrine. And the cases Plaintiffs do cite are totally irrelevant. *See Schultz v. Boy Scouts of Am.*, 65 N.Y.2d 180 (N.Y. 1985) (claims of negligent hiring where employee committed sexual abuse); *Cooney v. Osgood Mach.*, 81 N.Y.2d 66 (N.Y. 1975) (product liability action by Missouri resident injured by machine manufactured in New York); *Elson v. Defren*, 283 A.D.2d 109 (1st Dep't 2002) (personal injury action by New York residents against an Idaho rental car company for injuries sustained in a car accident).[1]

In an effort to liken these cases to the instant action, without a single citation in support, Plaintiffs contend that the allegations here do not concern the affairs of FHI. (Opposition, at 7). But surely not even Plaintiffs would contend claims by one shareholder against another concerning the property and management of a corporation are akin to claims of sexual abuse or injuries from a faulty machine. Rather, the sole factual basis for all of Plaintiffs' claims –

[1] The only other case cited by Plaintiffs, *UBS Securities LLC v. Highland Capital Mgmt, L.P.*, involves a determination of whether one corporation served as another's alter ego, which is not asserted here. 30 Misc.3d 1230(A), at *3 (Sup. Ct., N.Y. Cty. 2011).

Haart's withdrawal of $850,000 from FHI's account – has everything to do with internal affairs, namely FHI's payment structure and Haart's right to money she earned as CEO.

Accordingly, the Court should apply Delaware law to these claims.

II. THE OPPOSITION CONFIRMS SCAGLIA'S LACK OF STANDING

A. Plaintiffs Admit That Scaglia Lacks Standing To State A Claim For Conversion, Unjust Enrichment, and Constructive Trust

Regardless of which state law applies, Plaintiffs expressly concede that Scaglia lacks standing to assert a claim for conversion, unjust enrichment, and constructive trust.[2] (*See* Opposition, at 14). Accordingly, the Court should dismiss those claims with prejudice.

B. Plaintiffs Concede That They Have Pleaded No Facts To Show Individual Harm To Scaglia From A Purported Breach Of Contract

The only claim that Plaintiffs argue Scaglia should be permitted to bring is the claim for breach of contract against Haart. (*Id*.). But neither the FAC nor the Opposition show why Scaglia, as a shareholder of FHI, has standing to bring this claim.

To establish standing in this context, Plaintiffs are required to show that Scaglia personally suffered damages that are separate from any damages sustained by FHI by a purported breach. *See Lawrence Ins. Group, Inc. v. KPMG Peat Marwick L.L.P.*, 5 A.D.3d 918, 919 (3d Dep't 2004) ("a shareholder … may [only] sue for damages caused by the defendant's negligence which results in ***injury that is personal to the shareholder and independent of the damage caused to the corporation***.") (emphasis added).

Plaintiffs' "showing" of damages consists of mentioning the word damages. (FAC, ¶ 53, inserting a boilerplate statement that Scaglia "has been damaged thereby."). Unapologetic for

[2] The Second Cause of Action for breach of fiduciary duty in the FAC was not asserted by Scaglia. Nonetheless, Plaintiffs admit that Scaglia lacks standing to bring this claim. (*See* Opposition, at 1, FN.1).

their failure to plead any damages, Plaintiffs instead fall back on a meek argument that damages need not be established at this stage. (*See* Opposition, at 14). This position is flawed.

The law does not, as Plaintiffs suggest, encourage boilerplate pleadings that give no insight whatsoever into the harm allegedly suffered. *See Bodum USA, Inc. v. Perez*, 148 A.D.3d 644, 645 (1st Dep't 2017) (dismissal warranted where plaintiff failed to allege damages); *Pitcock v. Kasowitz, Benson, Torres & Friedman LLP*, 74 A.D. 3d 613, 615 (1st Dep't 2010) ("the vague, boilerplate allegations of damages … were insufficient to sustain the causes of action asserted therein."); *Gordon v. Dino De Laurentis Corp.*, 529 N.Y.S.2d 777, 779 (1st Dep't 1988) ("In the absence of any allegations of fact showing damage, mere allegations of breach of contract are not sufficient to sustain a complaint…"); *Miller v. HSBC Bank U.S.A., N.A.*, No. 13 Civ. 7500 (RWS), 2015 WL 585589, at *4 (S.D.N.Y. Feb. 11, 2015) (plaintiff's "unsupported claim that she 'suffered damages' without any further factual enhancement, is not enough to properly plead the damages element of a breach of contract claim").[3]

Plaintiffs' insertion of a boilerplate line that Scaglia sustained damages is grossly insufficient to establish that Scaglia's standing. The FAC, as pled, leaves Defendants—and the Court—wholly guessing as to what, if any harm FHI suffered, and crucially, what, if any harm Scaglia suffered that is separate from that of FHI. And it is axiomatic that a shareholder may not sue for damages to a corporation. *See Brancaleone v. Mesagna*, 290 A.D.2d 467, 468 (2d Dep't 2002); *Schwartz v. Nordstrom, Inc.*, 160 A.D. 240, 241 (1st Dep't 1990).[4]

[3] The one case cited by Plaintiffs does not save their position. *Kempf v. Magida* concerned a claim for legal malpractice brought by an attorney's former clients – not claims made by a shareholder against another, whereby the court determined if the shareholder had standing to bring a claim. 37 A.D.3d 763 (2d Dep't 2007).

[4] In citing *Lawrence Ins. Group v. KPMG Peat Marwick*, Plaintiffs omitted that the court stated that the shareholder may sue for damages caused by the defendant's negligence, which typically "consist of loss in value of the plaintiff's shares in the corporation" which were established in that matter and not even alleged here. 5 A.D.3d 918, 919 (3d Dep't 2004). And unlike in *Matter of Schulman*, where the plaintiff asserted that he was damaged *individually*, Plaintiffs made no such allegation here. 165 A.D. 2d 499, 504 (3d Dep't 1991).

Without pleading any facts to establish damage to Scaglia personally, Plaintiffs cannot establish standing on behalf of Scaglia to bring a breach of contract claim. Accordingly, the Court should dismiss the Third Cause of Action for breach of contract with prejudice.

III. THE OPPOSITION CANNOT OTHERWISE SAVE PLAINTIFFS' CLAIMS

Regardless of the Court's determination of standing as to Scaglia, the first, third, and fourth causes of action nonetheless must be dismissed.

A. Breach of Contract

1. Without Having Pled Any Damages, Scaglia Fails To State A Claim For Breach Of Contract

Scaglia's failure to plead individual damages mandates dismissal of his breach of contract claim against Haart due to a lack of standing pursuant to CPLR 3211(a)(3). (*See* Part II.B, *supra* (citing cases)). Independently, Plaintiffs' failure to plead any facts supporting damages renders the claim procedurally deficient and unable to withstand dismissal. (*Id*.).

2. There Is No Likelihood That The Oral Agreement Could Have Been Performed Within One Year

As Plaintiffs correctly state, "an oral agreement is unenforceable that by its terms is not to be performed within one year from the making thereof." (Opposition, at 10 (internal citations omitted)). However, often it is the case, such as here, where courts are faced with a more complex question of whether oral agreements that have indefinite duration (i.e., the agreement does not, by its terms, provide an end date), fall under the statute of fraud's purview. Courts applying New York law have clearly held such agreements are "deemed to be incapable of being performed within a year, and thus fall within the ambit of the Statute of Frauds." *Computech Int'l., Inc. v. Compaq Computer Corp.*, No. 02 Civ. 2628(RWS), 2002 WL 31398933, at *3 (S.D.N.Y. Oct. 24, 2002). *See also In re Bayou Hedge Fund Litig.*, 534 F. Supp. 2d 405, 420

(S.D.N.Y. 2007) (statute of frauds violated where it was neither fair nor reasonable to claim that oral contract of indefinite term was capable of being performed within a year).

Plaintiffs contend that where there is a possibility of performance within a year, an oral contract escapes the statute of frauds' application. (*See* Opposition, at 10). As this may generally be the case, Plaintiffs' contention that the purported oral agreement between Haart and Scaglia "not only could, but most certainly would, have been completed within a year" flies in the face of reality and thus fails as a matter of law. (*Id*.).

Plaintiffs state that the oral agreement was entered into in conjunction with the anticipated divorce between Haart and Scaglia. (*Id*., at 11). According to Plaintiffs, because as of January 2022, both Haart and Scaglia contemplated divorce, hired divorce attorneys, and because Haart has filed for divorce, the oral agreement was capable of being fully performed within a year. (*Id*.). But for this to be true, the divorce would need to be finalized within a year. Ignoring the realities of a divorce procedure, Plaintiffs assume this limited timing is feasible such that it should remove the oral agreement from the statute of frauds. Plaintiffs are mistaken.

Divorce proceedings have been notoriously slow in New York courts – and this is without the added burden of the COVID-19 pandemic. *See* Bryan L. Salamone, *Backlog of Divorces Can Make It Harder to Get Divorced in New York*, Bryan L. Salamone & Assoc., P.C., (Aug. 22, 2017) *available at* https://www.divorcelawyerlongisland.com/blog/backlog-of-divorces-can-make-it-harder-to-get-divorced-in-new-york/ (Manhattan has "the most unresolved divorces in 2015" and attributing delays to changes to state law permitting no-fault divorces and thus increases in divorces since 2010); Melkorka Licea and Melissa Klein, *Massive Backlog of Divorce Cases Makes it Hard for New Yorkers to Split*, New York Post (Sept. 25, 2016), *available at* https://nypost.com/2016/09/25/massive-backlog-of-divorce-cases-makes-it-hard-for-

new-yorkers-to-split/ ("Nearly 4,500 contested divorces were pending in [New York] last year, up 10 percent since 2011").

Since the COVID-19 pandemic swept through New York City, the entire city has struggled to pick up the pieces and attain pre-pandemic efficacy. The courts are no exception. *See* Dalton, Kristen, *The Lasting Impact of COVID-19 on Divorce*, New York Law Journal (Jun. 23, 2021), *available at* https://www.law.com/newyorklawjournal/2021/06/23/the-lasting-impact-of-covid-19-on-divorce/?slreturn=20220601120651; Molly Crane-Newman and Noah Goldberg, *NYC Courts Back in Session Facing Two Years of COVID-19 Backlog*, Daily News (Mar. 13, 2022), *available at* https://www.nydailynews.com/news/ny-two-years-since-global-coronavirus-pandemic-shut-down-nyc-courts-20220313-327hwn77fbelhprgtpcs6xon54-story.html ("The already burdened court system, which was trudging through a backlog of hundreds of thousands of pending cases before the pandemic pause, has been set back even farther."). The combination of steep increases in divorce cases and short-staffed courts has certainly not helped these delays improve, and, conversely, have attributed to even worse delays. *See* Mallozzi, Vincent M., *As Courts Reopen, Divorce Filings Are on the Rise*, The New York Times (Sept. 9, 2021), *available at* https://www.nytimes.com/2021/09/09/style/as-courts-reopen-divorce-filings-are-on-the-rise.html ("divorces seem to be on the rise almost everywhere" and noting one New York firm reported "an avalanche of covid-caused divorces"); Paul Sullivan, *The Pandemic Has Slowed the Divorce Process. Here's What To Expect*, The New York Times (May 8, 2020), *available at* https://www.nytimes.com/2020/05/03/your-money/divorce-coronoavirus-courts.html (noting at the onset of the pandemic, "many state courts are effectively closed or operating only on an emergency basis, adding disruption and delay"). As one reporter stated, "many families are still facing staggering waits for relief, with their next court dates scheduled more than a year out."

Melissa Russo and Hilary Weissman, *NYC Family Court in Crisis, New Report Says*, NBC New York (Feb. 4, 2022, 12:19 PM), *available at* https://www.nbcnewyork.com/investigations/nyc-family-court-in-crisis-new-report-says/3532144/.

The problems plaguing the courts do not seem to be improving any time soon. Russo and Weissman report "[e]ven with the court in its current state of crisis, the I-Team has learned six judges are about to be transferred out … [and] their collective 4,500 cases are likely to be disrupted even further during the transfer." *Id*.

Thus, it is highly speculative and naïve to assume that Haart and Scaglia's divorce – and thus the oral agreement regarding FHI funds – could be resolved within one year. To the contrary, the objective evidence concerning the current state of the New York court system establishes a more likely *impossibility* of resolution within that time.

Accordingly, the Court should dismiss the third cause of action for breach of contract.

B. Conversion

Plaintiffs also fail to state a claim for conversion. Delaware law does not permit the claim to proceed, as Plaintiffs do not dispute.[5] (*See* Opposition, at 8-9). Thus, Plaintiffs unsurprisingly urge the Court to apply New York law to their claim. But even then, the FAC still fails to state a claim and should be dismissed.

Plaintiffs argue that conversion claims for money are permissible under New York law. (*See* Opposition, at 8-9). While this is generally true, New York law clearly provides that "an action for conversion cannot be validly maintained where damages are merely being sought for breach of contract." *Peters Griffin Woodward, Inc. v. WCSC, Inc.*, 88 A.D.2d 883, 884 (1st Dep't 1982). Where identical damages are sought, dismissal of the conversion claim is

[5] Plaintiffs also concede that Scaglia has no standing to maintain a conversion claim against Defendants, which, on its own, requires dismissal of the first cause of action claim as to him.

appropriate. *See Gorra Holding v. Nu-Tech Bio-Med, Inc*., No. 98 CIV. 0764(HB), 1999 WL 4922, at *5 (S.D.N.Y. Jan. 5, 1999) ("Here, the damages sought in conversion are identical to those in the breach of contract claim. Consequently, the defendants' motion to dismiss the conversion claim is granted."); *see also* 10 N.Y. Jur., Conversion, § 27.

Here, Plaintiffs seek identical damages in the conversion and breach of contract claims. In both claims, Plaintiffs seek the return of the $850,000 withdrawn from the account in FHI's name. (*Compare* FAC, ¶¶ 36-42, *with* ¶¶ 49-53). Other than a change to the wording to fit the elements of each claim, there is no difference between the two claims and the relief they seek.

Accordingly, the Court should dismiss Plaintiffs' claim for conversion.

C. Unjust Enrichment

Plaintiffs' claim for unjust enrichment cannot stand either. Plaintiffs claim they can plead unjust enrichment in the alternative to their other claims. (*See* Opposition, at 12-13). But alternative pleading is not permitted where the unjust enrichment claim "relies on the ***same facts*** as [the] other causes of action." *Nelson v. MillerCoors, LLC*, 246 F. Supp. 3d 666, 679 (E.D.N.Y. 2017) (emphasis added). *See also Corsello v. Verizon New York, Inc.*, 18 N.Y.3d 777, 790 (N.Y. 2012) ("unjust enrichment is not a catchall cause of action when others fail").

Plaintiffs erroneously argue that because an unjust enrichment claim has different legal elements than claims for breach of fiduciary duty and conversion, the claims are not duplicative. (*See* Opposition, at 12-13). But it is not the similarity of the *elements* that renders claims as duplicative; it is the similarity between the *underlying facts* that will be used to prove the elements. Where the underlying facts and relief sought overlap, dismissal is proper. *See Apollo Mgmt, Inc. v. Cernich*, 202 A.D.3d 527, 528 (1st Dep't 2022) ("the unjust enrichment claim … was duplicative … and should have been dismissed"); *Testani v. Russell & Russell, LLC*, 204 A.D.3d 1260, 1262 (3d Dep't 2022) ("Supreme Court correctly concluded that the unjust

enrichment cause of action should be dismissed as it was essentially grounded in the same allegations of misconduct as set forth in, and was therefore duplicative of, the fraud and breach of fiduciary duty claims."); *Maomonides Med. Ctr. v. First United Am. Life Ins. Co.*, 35 Misc.3d 570, 581 (Sup. Ct. Kings Cty. 2012) ("[B]ecause plaintiff … pleads no alternative basis for its claim that defendant has been unjustly enriched at its expense, plaintiff's … cause of action must be dismissed"); *Huang v. Sy*, 18 Misc.3d 1141(A), at *12 (Sup. Ct. Queens Cty. 2008) ("the claim for unjust enrichment … is … duplicative of their claims of fraud and breach of fiduciary duty as they arose from the same facts and did not allege distinct and different damages.").

Plaintiffs' claim for unjust enrichment is based on the same facts as those forming the bases of the breach of fiduciary duty and conversion claims. In each, Plaintiffs allege that Haart used her access to FHI's account at J.P. Morgan Bank to withdraw $850,000, and in each, Plaintiffs seek the return of the money. (*Compare* FAC, ¶¶ 36-42, *with* ¶¶ 43-48, *and* ¶¶ 54-60).

Accordingly, the Court should dismiss the unjust enrichment claim with prejudice.

CONCLUSION

For the foregoing reasons, Defendants' Motion to Dismiss should be granted in its entirety, along with such other and further relief as the Court deems just, proper, and equitable.

Dated: New York, New York
July 6, 2022

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WORD COUNT CERTIFICATION

Pursuant to Rule 17 of subdivision (g) of section 202.70 of the Uniform Rules for the Supreme Court and County Court (Rules of Practice for the Commercial Division of the Supreme Court), I hereby certify that the total number of words in this Reply Brief in Further Support of Defendant's Motion to Dismiss, excluding the caption, signature block, and word count certification is 4166.

/s/Erika L. Shapiro
Erika L. Shapiro

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