

Kagan v HMC-New York, Inc.

2010 NY Slip Op 33769(U)

May 28, 2010

Supreme Court, New York County

Docket Number: 601306/09

Judge: Richard B. Lowe

Republished from New York State Unified Court System's E-Courts Service.
Search E-Courts (<http://www.nycourts.gov/ecourts>) for any additional information on this case.

This opinion is uncorrected and not selected for official publication.

SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

JUDGE: HON. RICHARD B. LOWE, III

PART 56

PRESENT: _____
Justice

Howard Kagan

- v -

Amc - New York

INDEX NO. 601306/09
MOTION DATE 11/18/09
MOTION SEQ. NO. 001
MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to/for _____

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...
Answering Affidavits — Exhibits _____
Replying Affidavits _____

PAPERS NUMBERED

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered that this motion

MOTION IS DECIDED IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DATED

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: MAY 28 2010

HON. RICHARD B. LOWE, III

J.S.C.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION
Check if appropriate: DO NOT POST

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 56

-----X

HOWARD KAGAN,

Plaintiff,

Index No. 601306/09

-against-

HMC - NEW YORK, INC., HARBINGER
CAPITAL PARTNERS GP, L.L.C., HARBINGER
CAPITAL PARTNERS FUND L.L.P., HMC
INVESTORS, L.L.C., HARBINGER CAPITAL
PARTNERS OFFSHORE MANAGER, L.L.C.,
HARBINGER CAPITAL PARTNERS OFF-SHORE
FUND 1, LTD., HARBINGER HOLDINGS, LLC,
PHILIP A. FALCONE, RAYMOND J. HARBERT,
MICHAEL D. LUCE, WILLIAM W. BROOKE,
CHARLES D. MILLER, DAVID A. BOUTWELL,
JOEL B. PIASSICK, MICHAEL P. WHITE,
CAROLE B. SCHAFER, LAWRENCE M. CLARK,
KATHLEEN K. MURPHY, IAN W. ESTUS, RAYMOND
JONES HARBERT ACCUMULATION TRUST U/A
12/22/99, MARY KATHRYN HARBERT
ACCUMULATION TRUST U/A 12/22/99, JOHN
MURDOCH HARBERT 11 ACCUMULATION TRUST
U/A 12/22/99 and JOHN AND JANE DOES 1
through 100.

Defendants.

-----X

Hon. Richard B. Lowe, III.:

Defendants HMC - New York, Inc. (HMC - New York), Harbinger Capital Partners GP,
L.L.C. (Onshore Manager), Harbinger Capital Partners Fund 1, L.P. (Onshore Fund), HMC
Investors, L.L.C. (HMC Investors), Harbinger Capital Partners Offshore Manager, L.L.C.
(Offshore Manager), Harbinger Capital Partners Offshore Fund 1, Ltd. (Offshore Fund), and

Harbinger Holdings, LLC (Harbinger Holdings) (collectively, the Harbert Defendants), Philip A. Falcone, Raymond J. Harbert and Michael D. Luce, William W. Brooke, Charles D. Miller, David A. Boutwell and Joel B. Piassick, Michael P. White, Carole B. Schafer, Lawrence M. Clark, Kathleen K. Murphy, Ian W. Estus, Raymond Jones Harbert Accumulation Trust U/A 12/22/99 (RJH Trust), Mary Kathryn Harbert Accumulation Trust U/A 12/22/99 (MKH Trust) and John Murdock Harbert 11 Accumulation Trust U/A 12/22/99 (JMH Trust) (the Trust Defendants) move for an order: (i) pursuant to CPLR 3211 (a) (8) dismissing the complaint as against defendants William W. Brooke, Charles D. Miller, David A. Boutwell, Michael P. White, Carole B. Schafer, RJH Trust, MKH Trust, and JMH Trust on the ground that the court lacks in personam jurisdiction over these defendants; (ii) pursuant to CPLR 3211 (a) (7), dismissing the first cause of action as against defendants HMC Investors; (iii) pursuant to CPLR 3211 (a) (7), dismissing the second cause of action as against defendants HMC - New York and Harbinger Holdings; (iv) pursuant to CPLR 3211 (a) (7), dismissing causes of action three through nine as against all the defendants.

Background

Plaintiff Howard Kagan (Kagan) commenced this action to recover money damages he allegedly sustained as a result of defendants' actions in connection with the parties' written agreements. Plaintiff alleges breach of contract, unjust enrichment, breach of fiduciary duty, and aiding and abetting breach of fiduciary duty, arising out of the defendants' failure to pay him approximately \$62 million. In addition, he seeks the imposition of a constructive trust.

Kagan is an investment professional in the money management industry, and the Harbart defendants, which include two investment funds, i.e., the Onshore Fund and the Offshore Fund

(together referred to at times as the Funds), are part of a group of entities that constitute a New York-based private investment firm. The Funds are managed by the Onshore Manager and the Offshore Manager (the Management Companies). The individual defendants were officers and directors of, or investors in, the Management Companies.

In or about March 2003, Kagan began providing consulting services to HMC -New York, and in or about November 2004, he became a Vice President and Director of Investments of HMC - New York. In 2006, Kagan was issued interests in, and became a member of the Onshore Manager and the Offshore Manager (collectively, the Manager Entities). Kagan alleges, upon information and belief, that the actions of the Manager Entities were controlled by Philip A. Falcone, the Chief Investment Officer and Senior Managing Director of the Manager Entities, Raymond J. Harbert, the Chairman and Chief Executive Officer of the Manager Entities, and Michael D. Luce, the President and Chief Operating Officer of each of the Manager Entities.

Kagan claims that, as a holder of membership interests in the Manager Entities, he was entitled to receive payment of a portion of the Manager Entities' performance compensation pursuant to the limited liability company agreements (the LLC Agreements) of the Manager Entities, to which Kagan was a party. The LLC Agreements required that a portion of the amounts owed to Kagan with respect to 2007 be held back by the Manager Entities and paid to Kagan only if such amounts vested. Vesting occurred upon a number of events, including the involuntary termination of Kagan's relationship with Harbert without cause. Once the withheld amounts vested, they were required to be paid to Kagan within 30 days after Kagan's termination without cause in the case of amounts owed by the Offshore Manager, and immediately after his termination in the case of amounts owed by the Onshore Manager.

It is alleged that the LLC Agreements also provided for the amounts owed to Kagen to be increased or decreased based on the performance of the Onshore Fund; however, the amounts would be fixed if such amounts vested in connection with an involuntary termination of Kagan's relationship with Harbert without cause, and, in the event of Kagan's termination without cause, the Manager Entities are required to pay to Kagan amounts equal to his pro-rated share of the performance compensation of the manager Entities for 2008.

Kagan contends that, on August 27, 2008, Falcone, without prior notice, terminated Kagan's relationship with Harbert without cause. Kagan claims that at the time of his involuntary termination, Falcone assured him that he would be paid. Kagan also claims that, although Harbert has acknowledged that it owes Kagan at least approximately \$36.5 million, the LLC Agreements require that he be paid amounts totaling no less than \$62,141,783, which the defendants have refused to pay.

Defendants argue that plaintiff has failed to allege facts demonstrating that this court has personal jurisdiction over non-domiciliary defendants William W. Brooke, Charles D. Miller, David A. Boutwell, Michael P. White, Carole B. Schafer, and the three Trust Defendants. Defendants claim that said defendants are, and were, merely investors in the Offshore Manager, and that plaintiff has failed to establish any connection between his claims and the defendants' limited contacts with New York. They further submit an affidavit by John McCullough, Senior Vice-President and General Counsel of Harbert Management Corporation, who avers that, as of September 1, 2006, William W. Brooke was no longer an officer, employer, or manager of the Manager Entities.

In opposition, Kagan argues that there are sufficient facts to confer personal jurisdiction over the said defendants with regard to the claims for unjust enrichment and constructive Trust. He alleges, inter alia, that, upon information and belief, the defendants, who have an ownership in the Manager Entities, improperly received monies that properly belong to him; that defendants frequently traveled to New York to conduct investment-related activity; and attended meetings in New York relating to their ownership interests in the Manager Entities. Kagan requests that, in the event that this court finds that Kagan is not yet able to allege sufficient facts to establish jurisdiction, that he be permitted to conduct discovery with respect to jurisdictional contacts of said defendants.¹

Discussion

Generally, a nondomiciliary is subject to the jurisdiction of a court in the State of New York if it has purposefully transacted business within the State (*Deutsche Bank Sec., Inc. v Montana Bd. of Invs.*, 7 NY3d 65, 72 [2006]; *Kreutter v McFadden Oil Corp.*, 71 NY2d 460, 467 [1988]), and there is a “substantial relationship” between this activity and the plaintiff’s claim (*Bunkoff Gen. Contrs. v State Auto. Mut. Ins. Co.*, 296 AD2d 699, 700 [3rd Dept 2002]; see also *George Reiner & Co. v Schwartz*, 41 NY2d 648 [1977]; CPLR 302 [a] [1]).

Although the plaintiff seeking to assert personal jurisdiction bears the burden of proof on this issue (*O’Brien v Hackensack Univ. Med. Center*, 305 AD2d 199, 200 [1st Dept 2003]; see also *Brandt v Toraby*, 273 AD2d 429, 430 [2d Dept 2000]), the plaintiff is not required to make a prima facie showing of personal jurisdiction, but need only demonstrate that facts “may exist” to

¹In September 2, 2009, counsel for Kagan served Notices for Discovery and Production of Documents on all defendants, which included requests for documents relating to personal jurisdiction.

exercise personal jurisdiction over the defendant (*Peterson v Spartan Indus.*, 33 NY2d 463, 467 [1974]).

Here, plaintiff has established that facts “may exist” to exercise personal jurisdiction over said defendants, and has made a “sufficient start” to warrant further discovery on the issue of personal jurisdiction over them (*id.*). Accordingly, this court denies defendants’ motion to dismiss this action against the nondomiciliary defendants on the basis of lack of personal jurisdiction.²

This court will now turn to defendants’ motion to dismiss the complaint³ for failure to state a cause of action. On a motion to dismiss for failure to state a cause of action pursuant to CPLR 3211 (a) (7), it is well settled that courts must liberally construe a pleading, accept all the facts alleged therein to be true, and accord those allegations the benefit of every possible favorable inference in order to determine whether those facts fit within any cognizable legal theory (*see Leon v Martinez*, 84 NY2d 83, 87-88 [1994]; *Guggenheimer v Ginzburg*, 43 NY2d 268, 275 [1977]). The presumption of truth does not apply, however, to legal conclusions or to factual claims that are either inherently incredible or contradicted by documentary evidence (*Mark Hampton, Inc. v Bergreen*, 173 AD2d 220 [1st Dept 1991]).

Defendants argue that the first and second causes of action for breach of contract as against HMC Investors, HMC - New York, and Harbinger Holdings should be dismissed because

²This court would have denied defendants’ motion to dismiss without prejudice to renewal of this motion upon completion of discovery, however, inasmuch as the claims against these nondomiciliary defendants will be dismissed (*see infra*), there is no cause for further discovery.

³Defendants move to dismiss the complaint except for the first two causes of action for breach of contract asserted against the Offshore and Onshore Managers.

these entities, as managing members of the companies, do not owe any duties to Kagan under sections 4.5, 4.6 and 8.7 of the Offshore Manager Agreement, and sections 4.5 and 8.7 of the Onshore Manager Agreement, the provisions allegedly breached. They argue that the LLC Agreements imposed duties only on the “Company” as defined in the LLC Agreements, i.e., the Offshore Manager and the Onshore Manager, and not on the managing members.

Sections 4.5, 4.6 and 8.7 of the Offshore Manager LLC Agreement contain provisions that set forth certain duties of “the Company” with regard to the withholding of distributions, revenue deferral election, and termination of employees, respectively. The term “Company” is defined in sections 1.2 of the Offshore Manager Agreement as “Harbinger Capital Partners Offshore Manager, L.L.C.” Similarly, sections 4.5 and 8.7 of the Onshore Agreement set forth the duties of “the Company” with regard to the withholding of distributions and the termination of employees, respectively. The “Company” is defined in section 1.2 as “Harbinger Capital Partners GP, L.L.C.”

In opposition to the motion, plaintiff argues that as signatories to the LLC Agreements, and as the managing members possessing sole authority to conduct the business and affairs of the Onshore Manager and Offshore Manager, HMC - New York is liable to Kagan for breach of the Onshore Manager Agreement, and HMC Investors is liable to Kagan for breach of the Offshore Manager Agreement. It is undisputed that the breach of contract claims are governed by Delaware law because both LLC Agreements contain Delaware choice-of-law provisions.

In *Kuroda v SPJS Holdings, L.L.C.* (971 A2d 872 [Del Ch 2009]), the court, in deciding a motion to dismiss for failure to state a claim, addressed the issue of whether managing members of a limited liability company were liable for the limited liability company’s failure to, inter alia,

pay incentive allocations owed to an employee who was a non-managing member of the company. The agreement at issue, as in the instant case, purportedly limited the liability of members of the company for breaches of the agreement.

The Court denied the motion to dismiss the breach of contract claims against the managers of the company, notwithstanding that the language of the agreements conferred duties only on the company. The Court found that, since the managing members had signed the limited liability agreement, and the agreement did not clearly limit their liability to preclude the breach of contract claims alleged in the complaint, there was ambiguity in the provisions of the agreement regarding whether the managing members and signatories to the agreement could be held liable for their breach.

Section 7.9 of the subject LLC Agreements states: “Duties of Managers. The Managers shall act in good faith and in the best interest of the Company and with such care as an ordinarily prudent person in a like position would use under similar circumstances.”

Section 7.10 of the LLC Agreements states, in relevant part:

Limitation of Liability. No Manager or Officer shall have any liability to the Company or any Member or Holder for any loss suffered by the Company or any Member or Holder that arises out of any act or omission by the Manager or Officer, if such Manager or Officer performs its duty in compliance with the standard set forth in the immediately preceding sentence, except loss or damage resulting from intentional misconduct, knowing violation of law, gross negligence or a transaction from which the Manager or Officer received a personal benefit in violation or breach of the provisions of this Agreement.

Here, similar to *Kuroda*, HMC - New York signed the Onshore Manager Agreement and HMC Investors signed the Offshore Manager Agreement. Moreover, the LLC Agreements

specifically set forth certain circumstances wherein the managers or officers of the company can be held liable for losses. Kagan alleges that HMC - New York and HMC Investors breached the terms of several provisions of the LLC Agreements, including sections 4.5, 4.6 and 8.7 of the Offshore Agreement, and sections 4.5 and 8.7 of the Onshore Agreement, by, inter alia, failing to properly calculate the amounts due him, and to timely pay him such amounts, and by wrongfully transferring to certain of the defendants assets that belong to plaintiff.

He further alleges that their acts were willful in breach of the implied covenant of good faith and fair dealing. Similar to *Kuroda v SPJS Holdings, L.L.C.*, (971 A2d 872, *supra*), this court finds that defendants' interpretation of the LLC Agreements, that whether the managing members are not liable for breach of the provisions, cannot be concluded as a matter of law. Accordingly, the defendants' motion to dismiss the first and second claims against defendants HMC - New York and HMC Investors is denied.

The third cause of action asserts a claim for unjust enrichment against the individual defendants and John and Jane Doe defendants. Plaintiff alleges, upon information and belief, that certain assets which should have been paid to him were transferred to the individual defendants, and that said defendants have unjustly accepted and retained these assets. Defendants argue that this claim should be dismissed because the parties' dispute is governed by the LLC Agreements.

"The essential inquiry in any action for unjust enrichment...is whether it is against equity and good conscience to permit the defendant to retain what is sought to be recovered [citation omitted]" (*Sperry v Crompton Corp.*, 8 NY3d 204, 215 [2007]). However, the existence of a valid and enforceable written contract governing a particular subject matter precludes recovery under a quasi-contract theory for events arising out of the same subject matter (*see Clark-*

Fitzpatrick, Inc. v Long Is. R.R. Co., 70 NY2d 382 [1987]; *Chadirjian v Kanian*, 123 AD2d 596 [2d Dept 1986]).

Here, the plaintiff's unjust enrichment cause of action relates to the defendants' breach of the LLC Agreements, i.e., their failure to properly distribute monies which Kagan claims he was entitled to following his termination. Since Kagan's unjust enrichment claim arises out of the LLC Agreements, the plaintiff is precluded from recovering for unjust enrichment. Accordingly, the third cause of action for unjust enrichment is dismissed.

The fourth cause of action seeks the imposition of a constructive trust as against all the defendants, over any and all assets of the Manager Entities that should have been used to satisfy payment of the amounts alleged to be due to Kagan. Plaintiff alleges the existence of a confidential relationship of trust between himself and defendants; that he relied on the Manager Entities' promises that he would be paid certain amounts in the event that he was terminated without cause; that they refused to pay him the amounts owed to him; and that they have wrongfully retained and will wrongfully continue to transfer some portion of the assets that should have been used to pay plaintiff.

Defendants argue that the constructive trust claim should be dismissed because there is no disputed title to property, and plaintiff fails to allege the elements of a constructive trust. The essential elements of a constructive trust are: (1) a confidential or fiduciary relationship, (2) a promise, (3) a transfer in reliance thereon, and (4) unjust enrichment (*see Sharp v Kosmalski*, 40 NY2d 119 [1976], *Cruz v McAneney*, 31 AD3d 54, 59 [2d Dept 2006]). "The ultimate purpose of a constructive trust is to prevent unjust enrichment and, thus, a constructive trust may be imposed

‘when property has been acquired in such circumstances that the holder of the legal title may not in good conscience retain the beneficial interest’[citations omitted]” (*id.* at 58-59).

Kagan has failed to sufficiently allege the elements of a cause of action for the imposition of a constructive trust. He does not allege that he transferred something of value to defendants in reliance on their promise to make payments to him under the LLC Agreements. Nor does the element of unjust enrichment exist, since there is a written contract between the parties.

Accordingly, defendants’ motion to dismiss the fourth cause of action for the imposition of a constructive trust is granted.

The fifth and sixth causes of action are for breach of fiduciary duty as against HMC Investors and/or Harbinger Holdings (which Kagan claims, upon information and belief, is the successor manager to the Offshore Manager), and HMC - New York and/or Harbinger Holdings, respectively. Kagan alleges that the Manager Entities, as managing members of the Offshore Manager and the Onshore Manager, respectively, have a fiduciary duty to Kagan, as a member of the Offshore Manager and Onshore Manager, to act in good faith and engage in fair dealing with him. He contends that defendants breached their fiduciary duty to Kagan by, *inter alia*, purposefully failing to pay him the amounts owed to him, and failing to properly calculate the amounts owed to him.

It is undisputed that Delaware Law applies to Kagan’s claims for breach of fiduciary duty. Under Delaware Law, when a duty sought to be enforced arises out of the parties’ contractual relationship, and the same facts that underlie the contract claim also form the basis of plaintiff’s fiduciary claim, the fiduciary claim is precluded (*see Gale v Bershad*, 1998 WL 118022, 1998 Del Ch LEXIS 37 [Del Ch 1998]; *HB Korenvaes Invs., L.P. v Marriott Corp.*, 1993 WL 205040, 1993

Del Ch LEXIS 90 [Del Ch 1993]; *accord William Kaufman Org., Ltd. v Graham & James LLP*, 269 AD2d 171, 173 [1st Dept 2000]).

Here, the complaint asserts contractual and fiduciary claims that arise from the same alleged facts and underlying conduct. Defendants' obligation to properly calculate and distribute the amount of monies owed to Kagan arises out of the LLC Agreements. Since the fiduciary claims are substantially identical to Kagan's breach of contract claims, defendants' motion to dismiss the sixth and seventh causes of action for breach of fiduciary duty is granted.

Finally, the seventh, eighth and ninth causes of action, which allege aiding and abetting breach of fiduciary duty as against Phillip A. Falcone, Raymond J. Harbert, and Michael D. Luce, respectively, are likewise dismissed. It is axiomatic, that in granting defendants' motion to dismiss the breach of fiduciary claims, there can be no recovery for aiding and abetting breach of fiduciary duty.

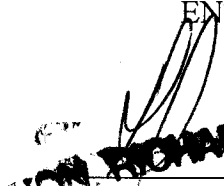
Accordingly, it is

ORDERED that defendants' motion to dismiss is granted to the extent that the third through ninth causes of action of the complaint are dismissed; and it is further

ORDERED that defendants are directed to serve an answer to the complaint within 10 days after service of a copy of this order with notice of entry.

Dated: May 28, 2010

ENTER:


RICHARD B. LOWE, III

J.S.C.