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Berkshire Bank v Pioneer Bank
2021 NY Slip Op 50619(U)
Decided on July 1, 2021
Supreme Court, Albany County
Platkin, J.
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Decided on July 1, 2021

Supreme Court, Albany County

Berkshire Bank, Plaintiff,

against

Pioneer Bank, Defendant.

Chemung Canal Trust Company, Plaintiff,

against

Pioneer Bank, Defendant.

Index No. 901358-20 (Action No. 1) and No. 901359-20 (Action No. 2)

Nolan Heller Kauffman LLP

Attorneys for Berkshire Bank and Chemung Canal Trust Company

(Madeline H. Kibrick Kauffman and Brendan J. Carosi, of counsel)

80 State Street, 11th Floor

Albany, New York 12207

DLA Piper LLP (US)

Attorneys for Pioneer Bank

(Robert J. Alessi and Jeffrey D. Kuhn, of counsel)

677 Broadway, Suite 1205

Albany, New York 12207-2996

PHILLIPS LYTLE LLP Attorneys for Chemung Canal Trust Company

(David J. McNamara and Jeffrey D. Coren, of counsel)

One Canalside, 125 Main Street

Buffalo, New York 14203

Richard M. Platkin, J.

The above-captioned actions arise out of inter-bank agreements by which plaintiffs Berkshire Bank and Chemung Canal Trust Company purchased from defendant Pioneer Bank participation interests in certain revolving lines of credit extended to corporations owned and/or controlled by Michael Mann, an admitted fraudster.

Plaintiffs sue under theories sounding in breach of contract, fraud, constructive fraud and negligent misrepresentation to recover the amounts they reimbursed Pioneer Bank for their proportionate share of advances under the lines of credit, together with damages for their costs, expenses, increased administrative burdens and lost opportunity costs.

In lieu of answering, Pioneer Bank moves for the dismissal of plaintiffs' claims, other than those for breach of the 2019 participation agreements, for failure to state a cause of action (*see* CPLR 3211 [a] [7]) and as conclusively defeated by documentary evidence (*see* CPLR 3211 [a] [1]).

Given the common issues of law and fact, the Court informally consolidated Pioneer Bank's motions for argument and disposition.

BACKGROUND

A. The Parties

Berkshire Bank ("Berkshire") is a Massachusetts banking corporation, Chemung Canal Trust Company ("Chemung") is a New York chartered trust company, and Pioneer Bank ("Pioneer") is a bank organized under the laws of New York State (*see* Action No. 1, NYSCEF Doc No. 1 ["Berkshire Complaint" or "Complaint"], ¶¶ 1-2; Action No. 2, NYSCEF Doc No. 1 ["Chemung Complaint"], ¶¶ 1-2).[FN1]

The actions arise from Berkshire and Chemung's purchase of participation interests in revolving line of credit facilities (each, a "Revolving LOC") issued by Pioneer to ValueWise Corp. ("ValueWise") and certain subsidiaries and/or affiliates (*see* Berkshire Complaint, ¶ 3).

ValueWise is a Delaware corporation formed in 2005 (*see id*., ¶ 16). Michael Mann was the owner, president and chief executive officer of ValueWise at pertinent times (*see id*., ¶¶ 17-18). ValueWise owned a number of companies, including MyPayrollHR.com, LLC ("MyPayroll") and Viverant, LLC ("Viverant [NY]") (*see id*., ¶¶ 19-20), and Mann owned at least six other companies, including Ross Personnel Consultants, Inc. ("Ross Personnel") (*see id*., ¶ 21).

B. Pioneer's Relationship With Mann and ValueWise

In November 2009, Pioneer extended a Revolving LOC to ValueWise and Ross Personnel, as co-borrowers, in the maximum principal amount of $2 million (*see id*., ¶ 22). [*2]From 2010 through 2014, Pioneer, ValueWise and Ross Personnel entered into at least nine transactions whereby the maximum principal amount of the line of credit was increased to $6.25 million (*see id*., ¶ 23).

On June 11, 2014, the maximum principal amount was reduced to $6 million, and Viverant [NY], MyPayroll and certain other ValueWise affiliates were added as co-borrowers (*see id*., ¶ 24). The maximum principal amount then was increased to $15 million on June 2, 2015 ("$15 Million Revolving LOC") (*see id*., ¶ 25), and the credit line was modified and restated on July 6, 2016 at the same maximum principal amount (*see id*., ¶ 26). Each of the foregoing credit facilities was absolutely and unconditionally guaranteed by Mann (*see id*., ¶ 27).

Besides its role as lender, Pioneer maintained a longstanding depository relationship with Mann and his corporations. Since 2009, Mann opened and/or maintained at least 37 deposit accounts with Pioneer, either in his name or in the names of his companies (*see id*., ¶ 28).

Mann also was a personal friend of Pioneer's lending officer, Vice President David Blessing (*see id*., ¶ 29). Blessing allegedly represented to Berkshire in April 2017 that he had been Mann's longtime banker and that Mann would seek his counsel before making

significant business decisions (*see id*., ¶ 30). Blessing brought the ValueWise/Mann relationship to Pioneer when he joined the bank in 2009, and he served as Pioneer's manager for the relationship at pertinent times (*see id*., ¶¶ 31-32).

C. The Revolving LOCs Subject to Participation Agreements

1. The $22 Million Revolving LOC

On or about April 4, 2017, Berkshire Executive Vice President Scott Houghtaling was contacted by Blessing about the possibility of Berkshire purchasing a 50% participation interest in the $15 Million Revolving LOC and two term loans to ValueWise and certain subsidiaries/ affiliates in the total principal amount of $7 million (*see id*., ¶ 33).

Blessing met with Houghtaling and Berkshire Vice President Stephen Malinowski at Pioneer's headquarters to discuss the proposal (*see id*., ¶ 34). Blessing emphasized Pioneer's long-standing relationship with Mann and his companies, describing ValueWise as "a holding company akin to a 'mini Berkshire Hathaway,' with annual revenue approaching $100 million and exponentially increasing growth" (*id*., ¶ 35). Blessing also represented that ValueWise had four principal areas of business, including physical therapy services provided through Viverant [NY] and payroll management services provided through MyPayroll (*see id*., ¶ 36).

During its underwriting, Berkshire received from Pioneer "audited and internal consolidated financial statements and borrowing base certificates," including audited financial statements for ValueWise prepared by an independent certified public accountant (*id*., ¶ 37).

After the $15 Million Revolving LOC was amended and restated to increase its maximum principal sum to $22 million ("$22 Million Revolving LOC"), inclusive of a portion of the prior term loans (*see id*., ¶ 38), Berkshire entered into a participation agreement with Pioneer dated June 29, 2017 ("2017 Participation Agreement") by which Berkshire purchased a 50% participation interest in the $22 Million Revolving LOC and a $2.6 million term loan (*see id*., ¶ 39).

2. $32 Million Revolving LOC

Pioneer and Berkshire met with Mann at ValueWise's offices on May 15, 2018 to discuss Mann's claimed needs for: (i) an increase in the Revolving LOC to $32 million; and (ii) "a

$1,000,000 loan to finance the 'continued growth' of 'Viverant,' which, as Mann explained, had expanded to ten (10) locations across Minnesota" (*id*., ¶¶ 41-42).

On June 27, 2018, the $22 Million Revolving LOC was amended and restated to, among other things, increase the maximum principal sum to $32 million ("$32 Million Revolving LOC") (*see id*., ¶ 43).

Berkshire then entered into an Amended and Restated Loan Participation Agreement with Pioneer dated June 27, 2018 ("2018 Participation Agreement") by which Berkshire purchased a 50% participation interest in the $32 Million Revolving LOC (*see id*., ¶ 44).

3. $42 Million Revolving LOC

Blessing contacted Malinowski in December 2018 regarding a possible increase in the $32 Million Revolving LOC and the prospect of offering Chemung a participation interest in the enlarged credit facility (*see id*., ¶ 46).

Blessing telephoned Chemung Vice President Kevin Harrigan in early January 2019 to discuss these issues (*see* Chemung Complaint, ¶ 42). Harrigan met with Blessing and Pioneer Commercial Portfolio Manager Matthew Guidarelli at Pioneer's offices on January 8, 2019 to discuss the Mann/ValueWise relationship and Chemung's potential purchase of a participation interest in the contemplated $42 million revolving line of credit (*see id*., ¶ 43).

Mann then met with Blessing, Malinowski and Chemung Executive Vice President Lou DiFabio and Vice President Kevin Harrigan at Pioneer's offices on January 28, 2019 to discuss the need for a credit increase (*see id*., ¶ 45). Mann represented that ValueWise had four primary areas of operation — consulting, physical therapy, payroll and business advisory services — and provided a general overview of each area (*see id*., ¶ 46). During the meeting, Blessing told plaintiffs that the $32 Million Revolving LOC would not be modified until the 2018 audited financials had been completed, which was expected in the Spring of 2019 (*see id*., ¶ 47).

The parties met again in May 2019 at Pioneer's offices (*see* Berkshire Complaint, ¶ 52), and Malinowski stated that a field examination would be needed in connection with the proposed credit increase (*see id*., ¶ 53). "[B]efore Mann could respond to Malinowski, Blessing agreed to the performance of such a field exam" (*id*.).

On May 24, 2019, Pioneer Senior Vice President Joseph Fleming telephoned Malinowski to advise that Blessing was taking a leave of absence, he would be taking over ValueWise's relationship, and Pioneer "would engage a field examiner to conduct a limited scope field exam," which "exclud[ed] various customary field exam areas of investigation expected by Berkshire to have been covered in the requested field exam" (*id*., ¶ 54). Malinowski informed Harrigan of Pioneer's decision on May 31, 2019 (*see* Chemung Complaint, ¶ 52).

The limited field exam began on July 2, 2019, and the $32 Million Revolving LOC was amended and restated on August 12, 2019 to increase the maximum principal sum to $42 million ("$42 Million Revolving LOC") (*see* Berkshire Complaint, ¶¶ 56, 58). Following the closing, Berkshire entered into an Amended and Restated Loan Participation Agreement dated August 12, 2019 by which it purchased a 44.04761905% participation interest in the $42 Million Revolving LOC ("2019 Participation Agreement") (*see id*., ¶ 60), and Chemung purchased an 11.90476190% participation interest ("Chemung Participation Agreement") (*see* Chemung Complaint, ¶ 58).

D. The Collapse of Mann's "House of Cards"

On August 29, 2019 — a little more than two weeks after the closings on the $42 Million Revolving LOC, the 2019 Participation Agreement and Chemung Participation Agreement —Bank of America ("BofA") froze the deposit accounts of certain Borrowers due to suspicious activity and returned at least 36 checks drawn on the BofA accounts and deposited in the [*3]Mann/ValueWise accounts at Pioneer ("Pioneer Accounts") (*see* Complaint, ¶ 63). Pioneer responded on August 30, 2019 by freezing the Pioneer Accounts (*see id*., ¶ 64).

Mann resigned from ValueWise on September 3, 2019, and ValueWise and MyPayroll ceased operations on September 5, 2019 (*see id*., ¶¶ 65-67). Mann appeared at the office of federal law enforcement authorities on September 10, 2019 and "confessed that MyPayroll's cessation of operations was 'precipitated by his decision' to forego routing MyPayroll clients' payroll payments to . . . [its] Automated Clearing House ('ACH') intermediary, and instead direct those payments to one or more of the . . . Pioneer Accounts 'in order to temporarily reduce the amount of money he owed to Pioneer'" (*id*., ¶ 68). Mann further confessed that:

(a) starting in 2010 or 2011 "he began borrowing large sums of money from banks and financing companies under false pretenses," (b) he had created companies "that had no purpose other than to be used in the fraud; falsely representing to banks and financing companies that his fake business had certain receivables that they did not have; and obtaining loans and lines of credit by borrowing against these non-existent receivables," and (c) as part of the fraudulent scheme, he had kited millions of dollars between BofA and Pioneer from August 1 to August 30, 2019" (*id*., ¶ 69).

E. Pioneer's Alleged Misrepresentations and Concealments

Plaintiffs complain that Pioneer failed to disclose material information relevant to Mann and ValueWise's scheme to defraud, including information pertaining to substantial overdrafts, suspicious activity indicative of kiting and commingling, and substantial third-party financing. Chemung further alleges affirmative misrepresentations on the part of Pioneer concerning the same matters.

1. Significant overdrafts in the Pioneer Accounts

Based upon the limited documentation provided by Pioneer in late 2019 (*see id*., ¶¶ 74-76), plaintiffs allege there were at least 30 overdrafts in the Pioneer Accounts "during January, June, July and August of 2019, each ranging from $992,472.49 to $8,926,510.38, and totaling *$106,084,574.31*" (*id*., ¶ 77).

Thirteen of the overdrafts, totaling almost $40 million, occurred in January and June 2019 — prior to Pioneer's commencement of a field exam that "excluded various customary field exam areas of investigation" (*id*., ¶ 79).

Overdrafts continued "into July, 2019, with 8 overdrafts over 6 business days, totaling $23,134,326.39" (*id*., ¶ 80).

There were nine additional overdrafts over eight business days in August 2019, totaling $43,045,506.87 (*see id*., ¶ 81). The "timing of [these] overdrafts is particularly significant inasmuch as 6 of the 9 overdrafts (totaling $32,824,119.40) occurred over the 6 consecutive business days immediately preceding the August 12, 2019 closing of the $42 Million Revolving LOC and the 2019 Participation Agreement transactions, and 2 of the 9 overdrafts (totaling $8,423,208.04) occurred on [the day of the closings]" (*id*., ¶ 82 [emphasis omitted]).

Plaintiffs maintain that "overdrafts of the size and frequency [identified in the Complaints] indicated that serious cash flow issues existed with respect to Borrowers ValueWise and Ross Personnel (and possibly others) by as early as January 2019" (*id*., ¶ 84). "The size and frequency of the overdrafts . . . warranted a downgrade of the risk classification of the $32 Million Revolving LOC" (*id*., ¶ 85).

Relatedly, plaintiffs emphasize that "overdrafts of the size described [above] would have required approval from Pioneer senior or executive management" (*id*., ¶ 86), but "[a]t no time [*4]prior to [execution of the 2019 Participation Agreements] did Pioneer disclose to [plaintiffs] the occurrence of any such overdrafts" (*id*., ¶ 87).

2. Suspicious activity indicative of kiting and commingling

Plaintiffs allege that Pioneer failed to disclose suspicious activity in the Pioneer Accounts indicative of kiting and commingling. This activity, which is alleged to have occurred as early as November 2018, included: "(i) frequent (in many cases, on every business day) and large (six- and seven-figure) round-dollar mobile deposits and internet transfers . . . , and then (ii) the same-day withdrawal thereof, usually by check, in large round-dollar amounts, and . . . the deposit of same into other accounts of ValueWise, Mann or their respective affiliates" (*id*., ¶ 90).

3. Kiting activity between BofA and Pioneer accounts

Relatedly, plaintiffs complain that Pioneer failed to disclose kiting activity between the Pioneer Accounts and certain BofA accounts. The Complaints cite Mann's admission to kiting millions of dollars in checks in August 2019, and Pioneer's knowledge of the BofA accounts (*see id*., ¶¶ 93-95). Plaintiffs also rely on "copies of thirty-six (36) checks dated August 29, 2019 that BofA had returned as unpaid to Pioneer, totaling $15,588,000" (*id*., ¶ 96).

4. ValueWise's receipt of third-party financing

The account statements provided to plaintiffs show 34 incoming wire transfers to ValueWise from Canfield Funding, LLC ("Canfield Funding") from September 7, 2018 through August 2, 2019, totaling $18,727,677.67 (*see id*., ¶¶ 97-98). Canfield Funding, which does business as Millenium Funding, provides commercial financing services, including accounts receivable factoring, purchase order funding and asset-based lending (*see id*., ¶ 99).

5. The two Viverants

Beginning as early as the April 6, 2017 meeting between Pioneer and Berkshire, and at various times thereafter, Blessing represented that one of the co-borrowers on the prior Pioneer term loans "was 'Viverant,' which operated physical therapy clinics in Minnesota . . . that [Blessing] had visited" (*id*., ¶ 102; *see* Chemung Complaint, ¶ 95 [citing similar representations made at January 8, 2019 meeting]).

Further, on June 7, 2017, Pioneer provided Berkshire with a copy of its May 30, 2017 Credit Request & Approval, which represented that "Value[W]ise Corporation provides management and technology consulting services with subsidiaries providing physical therapy services (Viverant, LLC) . . ." (Complaint, ¶ 103). Pioneer also provided Berkshire on June 19, 2017 with documentation about a New York limited liability company named "Viverant, LLC," described herein as Viverant [NY] (*see id*., ¶ 105; *see also* Chemung Complaint, ¶ 96).

Unbeknownst to plaintiffs, a different entity named Viverant, LLC had been formed on December 16, 2011 as a Delaware limited liability company ("Viverant [DE]") with its principal place of business in Minnesota (*see* Complaint, ¶ 106). "Viverant [NY] was in fact one of Mann's 'fake businesses,' created for 'no other purpose than to be used in the [above-referenced] fraud' and having no actual business operations (in Minnesota or otherwise)" (*id*., ¶ 107). "[I]t was non-borrower Viverant [DE] — and not Borrower Viverant [NY] — that operated (and continues to operate) physical therapy clinics in Minnesota, and whose purported financial information (including accounts receivable) was reported in the Borrowers' internal and audited financial statements" (*id*., ¶ 108).

Plaintiffs allege that Pioneer obtained a copy of the LLC agreement of Viverant [DE] prior to the closing on the $42 Million Revolving LOC, inasmuch as that document was included in a batch of 21 documents sent by Pioneer to Berkshire immediately after the closing (*see id*., ¶¶ [*5]109-111; *see also* Chemung Complaint, ¶¶ 105-107).

6. The freezing of the BofA and Pioneer accounts

Plaintiffs complain that Pioneer failed to immediately disclose the freezing of the BofA accounts and Pioneer Accounts, Mann's resignation from ValueWise, and ValueWise and MyPayroll's cessation of business operations (*see* Complaint, ¶¶ 113-114).

7. Affirmative Misrepresentations

Finally, plaintiffs cite certain affirmative misrepresentations made by Pioneer, including: (1) representations that one of the co-borrowers was and would be Viverant, LLC, a New York limited liability company that operated physical therapy clinics in Minnesota; (2) a chart provided by Pioneer purporting to show its existing deposit relationships with Mann, ValueWise and affiliated entities that did not disclose the significant overdraft credit facility extended by Pioneer; (3) representations that ValueWise experienced significant revenue growth in 2018 and that all receivables had balances over $300 million; and (4) a representation by Pioneer that the Mann/ValueWise accounts "have been handled as agreed" (Chemung Complaint, ¶¶ 130-132, 134-135, 137, 141, 154-155, 164; *see also* Complaint, ¶¶ 144, 172).

F. This Litigation

Berkshire and Chemung commenced these actions against Pioneer on February 4, 2020 through the filing of verified complaints (collectively, "Complaints"). Berkshire's complaint alleges six causes of action: (1) breach of the 2018 Participation Agreement; (2) breach of the 2019 Participation Agreement; (3) constructive fraud; (4) fraudulent inducement; (5) fraudulent concealment; and (6) negligent misrepresentation. Chemung's complaint alleges four causes of action: (1) breach of the Chemung Participation Agreement; (2) fraud; (3) constructive fraud; and (4) negligent misrepresentation.

In lieu of answering, Pioneer has moved separately against the Complaints under CPLR 3211 (a) (1) and (7) for the dismissal of plaintiffs' fraud-based claims, the negligent misrepresentation claims and Berkshire's claim for breach of the 2018 Participation Agreement.

Oral argument was held on May 21, 2021, a copy of the argument transcript was filed on June 24, 2021 (*see* Action No. 1, NYSCEF Doc No. 48 ["Oral Arg Tr"]), and this Decision & Order follows.

DISCUSSION

On a motion to dismiss made under CPLR 3211 (a) (7), the courts' "sole criterion is whether the pleading states a cause of action, and if from its four corners factual allegations

are discerned which taken together manifest any cause of action cognizable at law[,] a motion for dismissal will fail" (*Polonetsky v Better Homes Depot*, 97 NY2d 46, 54 [2001] [internal quotation marks and citation omitted]). The pleading "is to be given a liberal construction, the allegations contained within it are assumed to be true and the plaintiff is to be afforded every favorable inference" (*State of New York v Jeda Capital-Lenox, LLC*, 176 AD3d 1443, 1445 [3d Dept 2019] [internal quotation marks and citations omitted]). "Dismissal . . . is warranted if the plaintiff fails to assert facts in support of an element of the claim, or if the factual allegations and inferences to be drawn from them do not allow for an enforceable right of recovery" (*Connaughton v Chipotle Mexican Grill, Inc.*, 29 NY3d 137, 142 [2017] [citations omitted]).

"Under CPLR 3211 (a) (1), dismissal is warranted if documentary evidence conclusively establishes a defense as a matter of law" (*Haire v Bonelli*, 57 AD3d 1354, 1356 [3d Dept 2008], [citations omitted]; *see Goshen v Mutual Life Ins. Co. of NY*, 98 NY2d 314, 326 [2002]).

A. Negligent Misrepresentation

Berkshire's sixth cause of action and Chemung's fourth cause of action allege negligent misrepresentation. Pioneer seeks dismissal of the claims on the ground that the Complaints fail to sufficiently allege the fiduciary, confidential or special relationship necessary to support a claim for negligent misrepresentation.

1. Background

Berkshire's claim for negligent misrepresentation is directed at Pioneer's representations and omissions about "Viverant, LLC" (*see* Complaint, ¶ 172). Berkshire alleges that Pioneer consistently misrepresented "that one of the co-borrowers was and would be a 'Viverant, LLC," a *New York limited liability company* that operated physical therapy clinics in Minnesota" (*id*.).

Chemung's claim for negligent misrepresentation is broader, alleging that Pioneer "omitted material facts and made false representations" concerning: (1) substantial overdrafts in the Pioneer Accounts; (2) suspicious activity in the Pioneer Accounts indicative of kiting and commingling; (3) deposit and withdrawal activity between the BofA and Pioneer

Accounts indicative of check kiting; (4) ValueWise's receipt of substantial third-party financing; (5) the nature and extent of the credit accommodations extended by Pioneer to ValueWise and other Borrowers; and (6) Pioneer's statement that it handled all of the Mann/ValueWise accounts "as agreed" (Chemung Complaint, ¶ 164).

"A claim for negligent misrepresentation requires the plaintiff to demonstrate (1) the existence of a special or privity-like relationship imposing a duty on the defendant to impart correct information to the plaintiff; (2) that the information was incorrect; and (3) reasonable reliance on the information" (*J.A.O. Acquisition Corp. v Stavitsky*, 8 NY3d 144, 148 [2007] [citations omitted]). Thus, "[a] claim for negligent misrepresentation can only stand in the presence of a special relationship of trust or confidence, which creates a duty for one party to impart correct information to another" (*United Safety of Am. v Consolidated Edison Co. of NY*, 213 AD2d 283, 285-286 [1st Dept 1995]).

Pioneer moves for dismissal of the negligent misrepresentation claims on the ground that plaintiffs' purchases of participation interests in the Revolving LOCs were arm's length transactions between sophisticated banking institutions that did not give rise to any fiduciary, confidential or special relationship of trust and confidence.

2. Plaintiffs' Contentions

In seeking to allege the fiduciary, confidential and/or special relationship necessary to support a cause of action for negligent misrepresentation, Berkshire and Chemung rely upon Pioneer's long-standing lending and depository relationship with Mann and ValueWise, as well as the close personal relationship between Mann and Blessing (*see* Berkshire Complaint, ¶¶ 28-32; Chemung Complaint, ¶¶ 36-40; *see also* NYSCEF Doc No. 29 ["Dunham Aff."], ¶¶ 5, 10; Action No. 2, NYSCEF Doc No. 31 ["Harrigan Aff."], ¶ 4). These relationships are said to have given Pioneer "special knowledge of . . . the business operations of Borrowers, Mann and their respective affiliates" (Complaint, ¶ 170; Chemung Complaint, ¶ 162).

Plaintiffs also cite Pioneer's conduct in providing Berkshire with its internal May 30, 2017 Credit Request & Approval (*see* Complaint, ¶ 103; Dunham Aff., ¶ 10) and Chemung with its June 1, 2018 Commercial Loan Executive Summary and May 23, 2019 Credit Request & Approval (*see* Chemung Complaint, ¶¶ 98, 129, 141; Harrigan Aff., ¶¶ 4, 10, 14).

Additionally, plaintiffs maintain that Pioneer strictly controlled access to Mann and the Borrowers, as well as the dissemination of financial information obtained from them (*see* Dunham Aff., ¶¶ 12-14; Harrigan Aff., ¶ 16). Plaintiffs cite Pioneer's conduct in: (1) [*6]orchestrating their meetings with Mann, which generally were held at Pioneer's offices (*see* Dunham Aff., ¶ 12; Harrigan Aff., ¶ 17); (2) supplying virtually all of the financial information about Mann and the Borrowers (*see* Complaint, ¶¶ 37, 48; Dunham Aff., ¶ 12; Chemung Complaint, ¶ 97; Harrigan Aff., ¶ 17); and (3) conducting only a limited scope field exam, rather than the full exam requested by plaintiffs (*see* Complaint, ¶¶ 53-54; Dunham Aff., ¶ 13; Chemung Complaint, ¶¶ 49-52; Harrigan Aff., ¶ 18). "Quite simply, Pioneer understood that [plaintiffs were] relying on it for all material information relating to the Borrowers, Mann and the loan, and understood to act on behalf of and for the benefit of" plaintiffs (NYSCEF Doc No. 28 ["Berkshire Opp"], p. 11; *see* Action No. 2, NYSCEF Doc No. 27 ["Chemung Opp"], p. 7).

Finally, plaintiffs cite language in the Participation Agreements (*see* NYSCEF Doc Nos. 13-14; Action No. 2, NYSCEF Doc No. 13), in which Pioneer acknowledges that it has provided plaintiffs with "all . . . documents which are material to the Loan" (Participation Agreements, § 3 [e]) and represents that Pioneer had "no knowledge of any fact not apparent on the face of any [d]ocument which would materially and adversely affect the Loan" (*id*., § 5 [b]).

Plaintiffs therefore allege that they reposed their trust and confidence in Pioneer as a fiduciary based on Pioneer's long-standing and extensive relationship with Mann and the Borrowers, Pioneer's provision of its own internal credit underwriting materials, and Pioneer's control over access to Mann, the Borrowers and their financial information.

Relying on essentially the same allegations, plaintiffs argue that they have pleaded a "special relationship" with Pioneer beyond the typical arm's length relationship between banking institutions. Plaintiffs cite Pioneer's solicitation of their business and the special emphasis that was placed on Pioneer and Blessing's long-standing ties to Mann and the Borrowers (*see* Berkshire Opp, pp. 20-21; Chemung Opp, pp. 14-15).

3. Analysis

A fiduciary relationship "exists between two persons when one of them is under a duty to act for or to give advice for the benefit of another upon matters within the scope of the

relation. Such a relationship, necessarily fact-specific, is grounded in a higher level of trust than normally present in the marketplace between those involved in arm's length business transactions" (*EBC I, Inc. v Goldman, Sachs & Co.*, 5 NY3d 11, 19 [2005] [internal quotation marks and citations omitted]; *see Board of Mgrs. of Brightwater Towers Condominium v FirstService Residential NY, Inc.*, 193 AD3d 672, 673 [1st Dept 2021]; *New York State Workers' Compensation Bd. v Program Risk Mgt., Inc.*, 155 AD3d 1484, 1485 [3d Dept 2017]; *Faith Assembly v Titledge of NY Abstract LLC*, 106 AD3d 47, 62 [2d Dept 2013]).

As explained by the Court of Appeals:

> Generally, where parties have entered into a contract, courts look to that agreement to discover the nexus of the parties' relationship and the particular contractual expression establishing the parties' interdependency. If the parties do not create their own relationship of higher trust, courts should not ordinarily transport them to the higher realm of relationship and fashion the stricter duty for them. However, it is fundamental that fiduciary liability is not dependent solely upon an agreement or contractual relation between the fiduciary and the beneficiary but results from the relation (*EBC I*, 5 NY3d at 19-20 [internal quotation marks, citations and alterations omitted]).

"A special relationship may be established by 'persons who possess unique or specialized expertise, or who are in a special position of confidence and trust with the injured party such that reliance on the negligent misrepresentation is justified'" (*Mandarin Trading Ltd. v Wildenstein*, [*7]16 NY3d 173, 180 [2011], quoting *Kimmell v Schaefer*, 89 NY2d 257, 263 [1996]). In the commercial context, courts "should consider whether the person making the representation held or appeared to hold unique or special expertise; whether a special relationship of trust or confidence existed between the parties; and whether the speaker was aware of the use to which the information would be put and supplied it for that purpose" (*Kimmell*, 89 NY2d at 264).

"[A] duty to speak with care exists when the relationship of the parties, arising out of contract or otherwise, [is] such than in morals and good conscience the one has the right to rely upon the other for information'" (*J.P. Morgan Sec. Inc. v Ader*, 127 AD3d 506, 506 [1st Dept 2015], quoting *Kimmell*, 89 NY2d at 263). As with fiduciary relationships, however, an "arm's length transaction" between "sophisticated parties . . . [ordinarily] precludes a finding of a special relationship" (*Basis Pac-Rim Opportunity Fund [Master] v TCW Asset Mgt. Co.*, 124 AD3d 538, 539 [1st Dept 2015]).

The Participation Agreements assented to by plaintiffs expressly disclaim the formation of any relationship with Pioneer concerning the sale of participation interests other than that of seller and purchaser. "Th[ese] Agreement[s] constitute[] a sale of the Purchaser's Interest by the Seller to the Purchaser and shall in no way be construed . . . as creating any other relationship than Seller and participant between the parties" (Participation Agreements, § 3 [c]).

Further, plaintiffs represented and warranted to Pioneer that, "to the extent deemed necessary, [they] ha[ve] conducted an independent assessment of the Borrower and any guarantors, including without limitation an assessment relating to the creditworthiness . . . and the risks involved . . . in purchasing the Purchaser's Interest in the Loan" (*id*., § 7 [a]). Plaintiffs also "acknowledge[d] that [they] ha[ve] made an analysis and investigation of the Borrowers' financial condition and creditworthiness to the extent [they] deemed necessary" (*id*., § 12 [a]).

In executing the Participation Agreements, the parties also carefully defined Pioneer's disclosure and notification obligations. Thus, Pioneer "acknowledge[d] that [it] has provided [plaintiffs] with true and complete copies of all Loan Documents, together with . . . all other documents which are material to the Loan (collectively 'the Documents')," including credit information in Pioneer's possession (*id*., § 3 [e]). Pioneer further "represent[ed] and warrant[ed] to [plaintiffs]" that it "has no knowledge of any fact not apparent on the face of any Document which would materially and adversely affect the Loan" (*id*., § 5 [b]). Pioneer also agreed to "immediately notify [plaintiffs] should [it] . . . learn or have actual knowledge of . . . any change in the financial condition . . . which may have a material adverse effect upon the continuation of payments under the Loan, or the Loan's ultimate collectability" (*id*., § 6 [i]). And except as set forth in the Participation Agreements, Pioneer "ma[d]e no warranty or representation, express or implied," to plaintiffs (*id*., § 12 [c] [i]).

Thus, examination of the Participation Agreements shows that plaintiffs' purchases of participation interests in the Revolving LOCs were arm's length transactions between sophisticated financial institutions in which plaintiffs acknowledged and agreed that they had conducted an independent analysis and investigation of the creditworthiness of the Borrowers and the attendant risks, and Pioneer made no representations or warranties to plaintiffs other than those expressly set forth in the agreements.

In stark contrast, Article 9 of the Participation Agreements obliges Pioneer to "act[] as a trustee" for plaintiffs in servicing and administering the Revolving LOCs (*id*., § 9 [c]). Thus, the Participation Agreements explicitly impose "fiduciary duties" upon Pioneer when "act[ing] in all Loan administration and servicing matters" (*id*.).

In this connection, the Court rejects plaintiffs' argument that paragraph 9 (c) of the Participation Agreements is ambiguous. The pertinent language reads:

> [Pioneer] in acting as a servicer hereunder shall be acting as a trustee for [plaintiffs] and not as a partner or joint venturer of or agent for [plaintiffs]. As trustee [Pioneer] shall . . . act in all Loan administration and servicing matters as an independent contractor and as trustee, with fiduciary duties, to hold the participating Interests in the Loan and to make advances and remittances as specified under th[ese] Agreement[s].

Plaintiffs' strained attempt to read this language, pertaining to loan servicing and administration, as encompassing a pre-contractual fiduciary "duty of disclosure" (Berkshire Opp, p. 14; *see* Chemung Opp, pp. 8-9) simply is not a reasonable construction of the Participation Agreements (*see Ellington v EMI Music, Inc.*, 24 NY3d 239, 244 [2014]), particularly when the agreements are read "as a whole" and in light of "the intention of the parties as manifested thereby" (*Atwater & Co. v Panama R.R. Co.*, 246 NY 519, 524 [1927]).

Thus, where the contracting parties intended to subject Pioneer to the heightened legal duties of a fiduciary or trustee, they said so explicitly in the Participation Agreements using clear and unmistakable language (*see Sterling Inv. Servs., Inc. v 1155 Nobo Assoc., LLC*, 30 AD3d 579, 581 [2d Dept 2006]).

Plaintiffs' allegation of a special relationship with Pioneer fares no better. "[A] special relationship requires a closer degree of trust than an ordinary business relationship" (*Fleet Bank v Pine Knoll Corp*., 290 AD2d 792, 795 [3d Dept 2002] [internal quotation marks and citation omitted]) and "does not arise merely from an arm's-length business transaction" (*Waterscape Resort LLC v McGovern*, 107 AD3d 571, 571 [1st Dept 2013]; *accord RKA Film Fin., LLC v Kavanaugh*, 171 AD3d 678, 680 [1st Dept 2019]; *Lantau Holdings Ltd. v Orient Equal Intl. Group Ltd*., 161 AD3d 714, 714 [1st Dept 2018]; *Greentech Research LLC v Wissman*, 104 AD3d 540, 540 [1st Dept 2013]; *US Express Leasing, Inc. v Elite Tech. [NY], Inc.*, 87 AD3d 494, 497 [1st Dept 2011]; *Sebastian Holdings, Inc. v Deutsche Bank AG.*, 78

AD3d 446, 447 [1st Dept 2010]; *Dobroshi v Bank of Am., N.A.*, 65 AD3d 882, 884 [1st Dept 2009], *lv dismissed* 14 NY3d 785 [2010]).

Consequently, "[n]o special relationship typically exists between sophisticated financial institutions that negotiate agreements in arm's length transactions" (*Deutsche Zentral-Genossenschaftsbank AG v HSBC N. Am. Holdings, Inc.*, 2013 WL 6667601, *16, 2013 US Dist LEXIS 178462, *47 [SD NY, Dec. 17, 2013, No. 12 Civ. 4025 (AT)]; *see ABL Advisor LLC v Peck*, 147 AD3d 689, 691 [1st Dept 2017]; *Banque Arabe Et Internationale D'Investissement v Maryland Natl. Bank*, 57 F3d 146, 158 [2d Cir 1995]; *In re Enron Corp.*, 292 BR 752, 787-788 [SD NY 2003]).

The Court therefore rejects plaintiffs' argument that Pioneer's superior knowledge of business operations of Mann and the Borrowers, its longstanding lending and depository relationship with them, the Blessing/Mann personal relationship and/or Pioneer's role in acting as a liaison to Mann and the Borrowers gave rise to a special relationship of trust and confidence. The parties are sophisticated financial institutions that entered into comprehensive written agreements negotiated by counsel, and those agreements directly refute plaintiffs' allegations of a fiduciary, confidential or special relationship, except as to Pioneer's limited role as a loan servicer and administrator (*see Banque Arabe*, 57 F3d at 158; *Hawthorne Funding, LLC v Karish Kapital, LLC*, 192 AD3d 779, 780 [2d Dept 2021]; *ABL Advisor*, 147 AD3d at 691; *Basis Pac-Rim Opportunity Fund*, 124 AD3d at 539; *Greentech Research*, 104 AD3d at [*8]540-541; *330 Acquisition Co., LLC v Regency Sav. Bank*, 306 AD2d 154, 155 [1st Dept 2003]).

In so concluding, the Court rejects plaintiffs' effort to dismiss *Banque Arabe* as a pre-*Kimmell* decision that must be confined to its "particular facts and circumstances" (Berkshire Opp, p. 20; Chemung Opp, p. 13). Perhaps the Second Circuit went too far in stating that there is no fiduciary or special relationship between parties to a loan participation agreement "unless expressly and unequivocally created by contract" (*Banque Arabe*, 57 F3d at 158; *but see 330 Acquisition*, 306 AD2d at 155), but sophisticated banking institutions certainly have the freedom under New York law to disclaim contractually the existence of a fiduciary, confidential or special relationship, which is exactly what happened in *Banque Arabe* (*see* 57 F3d at 158 ["Banque Arabe and MNB engaged in arm's length negotiations and the Participation Agreement explicitly disclaims any reliance by Banque Arabe on MNB for information regarding its credit analysis and funding decision"]; *see also EBC I*, 5 NY3d at

19-20 [courts ordinarily look to parties' agreement to discover the nexus of their relationship]).

The Appellate Divisions have relied on the foregoing principles in concluding that allegations of a fiduciary, confidential or special relationship were conclusively defeated by the terms of the parties' written agreements. In *ABL Advisor*, for example, the First Department held that "plaintiffs' allegation of a fiduciary relationship is directly refuted by the Participation Agreements, which were arm's length business transactions that did not create any fiduciary duty" (147 AD3d at 691; *see 330 Acquisition*, 306 AD2d at 155; *CIBC Bank & Trust Co. v Credit Lyonnais*, 270 AD2d 138, 139 [1st Dept 2000]). To similar effect is the Second Department's recent decision in *Hawthorne Funding*, which held that "plaintiff's allegation of a fiduciary relationship between it and the defendant is directly refuted by the parties' agreement, which was an arm's length business transaction between sophisticated business people and which did not create any fiduciary duty" (192 AD3d at 780).

"Whether a duty exists presents a question of law to be determined by the court based upon the facts and circumstances of each case" (*Hooper v Anderson*, 157 AD2d 939, 940 [3d Dept 1990] [citations omitted]). Even assuming the truth of plaintiffs' factual allegations regarding Pioneer's relationship with Mann and his companies, the Blessing/Mann relationship and Pioneer's role in acting as a liaison to Mann as the originating lender,[FN2] the Court concludes that plaintiffs' allegations of a fiduciary, confidential or special relationship with Pioneer are utterly refuted by the terms of the Participation Agreements to which they assented.

Accordingly, the claims for negligent misrepresentation must be dismissed.

B. Constructive Fraud

Plaintiffs' third cause of action alleges constructive fraud, based on Pioneer's alleged concealment of material information, including: (1) substantial overdrafts in the Pioneer Accounts; (2) suspicious deposit activity; (3) deposit and withdrawal activity indicative of check kiting; (4) ValueWise's receipt of substantial third-party financing; and (5) the existence of Viverant [DE] (*see* Berkshire Complaint, ¶¶ 142, 144-147; Chemung Complaint, ¶¶ 154-155).

"The elements of a cause of action for fraud require a material misrepresentation of a [*9]fact, knowledge of its falsity, an intent to induce reliance, justifiable reliance by the plaintiff and damages" (*Eurycleia Partners, LP v Seward & Kissel, LLP*, 12 NY3d 553, 559 [2009] [citations omitted]). Constructive fraud has the same elements "with the crucial exception that the element of scienter is dropped and is replaced by a requirement to prove the existence of a fiduciary or confidential relationship warranting the trusting party to repose his or her confidence in a defendant and therefore to relax the care and vigilance he or she would ordinarily exercise in the circumstances" (*Mme. Pirie's, Inc. v Keto Ventures, LLC*, 151 AD3d 1363, 1364 [3d Dept 2017] [internal quotation marks, citations and alterations omitted], *amended on rearg* [Oct. 19, 2017]).

A claim of constructive fraud also may be based on the "special facts" doctrine. "Under that doctrine, a duty to disclose arises where one party's superior knowledge of essential facts renders a transaction without disclosure inherently unfair" (*P.T. Bank Cent. Asia, NY Branch v ABN AMRO Bank N.V.*, 301 AD2d 373, 378 [1st Dept 2003] [internal quotation marks and citations omitted]).

Pioneer argues that it is entitled to the dismissal of the constructive fraud claims because (1) the Complaints fail to allege a fiduciary or confidential relationship with Pioneer, and (2) the special facts doctrine is inapplicable as a matter of law.

"In the context of constructive fraud, a confidential or fiduciary relationship will be found when the relations between the contracting parties appear to be of such a character as to render it certain that they do not deal on terms of equality but that either on the one side from superior knowledge of the matter derived from a fiduciary relation, or from overmastering influence, or on the other from weakness, dependence, or trust justifiably reposed, unfair advantage in a transaction is rendered probable" (*Mme. Pirie's*, 151 AD3d at 1364-1365 [internal quotation marks and citation omitted]).

For the reasons stated above in connection with the dismissal of plaintiffs' claims for negligent misrepresentation, the Court concludes that plaintiffs have not sufficiently alleged a fiduciary or confidential relationship with Pioneer so as to support a cause of action for constructive fraud (*see Sears v First Pioneer Farm Credit, ACA*, 46 AD3d 1282, 1286 [3d Dept 2007]; *see also Benzies v Take-Two Interactive Software, Inc.*, 159 AD3d 629, 630-631 [1st Dept 2018]; *Refreshment Mgt. Servs., Corp. v Complete Off. Supply Warehouse Corp.*, 89 AD3d 913, 915 [2d Dept 2011]).

The viability of the constructive fraud claims therefore turns on the applicability of the special facts doctrine. The party seeking to invoke the special facts doctrine must satisfy "a two-prong test: that the material fact was information peculiarly within the knowledge of one party and that the information was not such that could have been discovered by the other party through the exercise of ordinary intelligence" (*Greenman-Pedersen, Inc. v Berryman & Henigar, Inc.*, 130 AD3d 514, 516 [1st Dept 2015], *lv denied* 29 NY3d 913 [2017]; *see Jana L. v West 129th St. Realty Corp.*, 22 AD3d 274, 278 [1st Dept 2007]).[FN3]

For purposes of the instant motion practice, Pioneer accepts, as it must, the truth of plaintiffs' allegations that it knew of the substantial overdrafts, suspicious account activities, ValueWise's receipt of substantial third-party financing and that the Minnesota physical therapy clinics were operated by Viverant [DE] and not Viverant [NY]. However, Pioneer contends that none of this information was "peculiarly within [its] knowledge" because the same information was known to Mann and the Borrowers. Pioneer further argues that plaintiffs have not alleged that they made any inquiries or otherwise made use of available means to discover the allegedly concealed information. Pioneer also cites plaintiffs' representation in the Participation Agreements that they conducted an "independent assessment" of the Borrowers' creditworthiness and the risks attendant to participating in the Revolving LOCs.

As to the first prong, Pioneer contends that the allegedly concealed information was not "peculiarly within [its] knowledge" (*Greenman-Pedersen*, 130 AD3d at 516), because the same information was known to Mann and the Borrowers. Even so, plaintiffs allege that Pioneer controlled and limited access to Mann, the Borrowers and their financial information (*see* Complaint, ¶¶ 37, 48, 53-54; Chemung Complaint, ¶¶ 49-52, 97; Dunham Aff., ¶¶ 12-14; Harrigan Aff., ¶¶ 16-18). And even if plaintiffs could have requested and obtained bank statements and other financial documents directly from Mann or the Borrowers, plaintiffs' opposition to the motion raises a legitimate question as to whether the requested documentation would have been truthfully disclosed. Plaintiffs emphasize that Mann's scheme to defraud was predicated on concealment of the true state of the Borrowers' finances, and Mann apparently provided falsified financial information to Pioneer's field examiners (*see* Dunham Aff., ¶ 16 & Ex. E; Harrigan Aff., ¶ 21 & Exs. E-F).

Moreover, as plaintiffs observe, that a third party knew, or may have known, of the undisclosed information is not a *per se* bar to application of the special facts doctrine (*see*

Madison Apparel Group Ltd. v Hachette Filipacchi Presse, S.A., 52 AD3d 385, 385 [1st Dept 2008] ["ongoing negotiations with a third-party licensee"]; *S & L Metro Prop., LLC v Clear Channel Outdoor, Inc.*, 2011 NY Slip Op 33841[U], *6 [Sup Ct, NY County 2011] ["Any such negotiations (with the third party) would be within the 'peculiar knowledge' of Clear Channel (and) could not have been discovered by plaintiffs through the exercise of ordinary intelligence"]; *accord LC Footwear, L.L.C. v L.C. Licensing, Inc.*, 2011 NY Slip Op 33894[U], *22 [Sup Ct, NY County 2011] [Kapnick, J.]).

Thus, the present record fails to conclusively defeat plaintiffs' allegation that the concealed information was within the "peculiar knowledge" of Pioneer.

The second prong of the special facts doctrine looks to whether the information was such that it could not have been discovered by the other party through the exercise of ordinary intelligence. As Pioneer observes, plaintiffs do not allege that they asked Pioneer to produce account statements or any other documents concerning the finances of Mann or the Borrowers during their "independent assessment of the Borrower and any guarantors" (Participation Agreements, § 7 [a]). Nor do plaintiffs allege that Pioneer ever denied them access to any [*10]documents.

Plaintiffs respond that there were no "red flags" that should have prompted them to make inquiry (*see ACA Fin.*, 25 NY3d at 1045), and they satisfied their obligation to perform due diligence by relying on the documents provided to them by Pioneer, including Pioneer's credit approvals, various audited and internal consolidated financial statements, tax returns and borrowing base certificates (*see* Complaint, ¶¶ 37, 103; Chemung Complaint, ¶ 97) — all of which were the subject of contractual representations and warranties. Thus, plaintiffs argue, there was no reason to ask Pioneer (or anyone else) for additional information.

"Where . . . a plaintiff has taken reasonable steps to protect itself against deception, it should not be denied recovery merely because hindsight suggests that it might have been possible to detect the fraud when it occurred. In particular, where a plaintiff has gone to the trouble to insist on a written representation that certain facts are true, it will often be justified in accepting that representation rather than making its own inquiry" (*DDJ Mgt., LLC v Rhone Group L.L.C.*, 15 NY3d 147, 154 [2010]; *see CIFG Assur. N. Am., Inc. v Goldman, Sachs & Co.*, 106 AD3d 437, 438 [1st Dept 2013] [analysis performed on the basis of warrantied facts]; *cf. Federal-Mogul Corp. v UTi, United States, Inc.*, 146 AD3d 468, 471 [1st Dept

2017] ["plaintiffs did not obtain representations and warranties that defendant's statements (the ones plaintiffs now claim they relied on) were true"]).

In executing the Participation Agreements, Pioneer "acknowledge[d] that [it] has provided [plaintiffs] with true and complete copies of all Loan Documents . . . and all other documents which are material to the Loan" (Participation Agreements, § 3 [e]). Pioneer also represented and warranted to plaintiffs that it "ha[d] no knowledge of any facts not apparent on the face of any Document which would materially and adversely affect the Loan" (*id*., § 5 [b]) and that it was "unaware of any material events of default" (*id*., § 5 [d]). Pioneer further agreed to immediately notify plaintiffs should it "learn or have actual knowledge of . . . any change in the financial condition of the Borrower . . . which may have a material adverse effect upon the continuation of payments under the Loan, or the Loan's ultimate collectability" (*id*., § 6 [i]).

And while plaintiffs did conduct an independent assessment of the Borrowers' financial condition and creditworthiness (*see id*., §§ 7 [a], 12 [a]), they did so in express reliance on "the truthfulness of the representations made by [Pioneer]" (*id*., § 12 [a]), including Pioneer's representation that it had "no knowledge of any facts not apparent on the face of any Document which would materially and adversely affect the Loan" (*id*., § 5 [b]).

Having negotiated for the inclusion of robust "prophylactic provision[s]" in the Participation Agreements (*ACA Fin.*, 25 NY3d at 1045), plaintiffs "made a significant effort to protect themselves against the possibility of [fraud]" (*DDJ Mgt*., 15 NY3d at 156). Under the circumstances, plaintiffs were not obliged, as a matter of law, to assume that Pioneer was concealing material information bearing on the creditworthiness and risks associated with participation in the Revolving LOCs and attempt to look behind Pioneer's representations and warranties (*see IKB Intl. S.A. v Morgan Stanley*, 142 AD3d 447, 450-451 [1st Dept 2017]).

Accordingly, the reasonableness of plaintiffs' reliance on the representations and warranties of the Participation Agreements is not a question that can be decided at this early stage of the litigation (*see Dillon v Peak Envtl., LLC*, 187 AD3d 1517, 1520 [4th Dept 2020]; *Towne v Kingsley*, 163 AD3d 1309, 1312 [3d Dept 2018]; *Remediation Capital Funding LLC v Noto*, 147 AD3d 469, 471 [1st Dept 2017]; *Lunal Realty, LLC v DiSanto Realty*, LLC, 88 AD3d 661, 665 [2d Dept 2011]).

The branch of Pioneer's motion seeking dismissal of the constructive fraud claims therefore is denied.

C. Berkshire's Fraudulent Inducement and Fraudulent Concealment Claims

Pioneer next moves for the dismissal of Berkshire's fourth and fifth causes of action, alleging fraudulent inducement and fraudulent concealment, respectively. These claims are founded on allegations that Pioneer concealed material facts (*see* Complaint, ¶¶ 154-159, 162-167).

According to Pioneer, the claims must be dismissed for lack of a fiduciary, confidential or special relationship warranting Berkshire "to repose [its] confidence in [Pioneer] and therefore to relax the care and vigilance [it] would ordinarily exercise in the circumstances" (*Mme. Pirie's*, 151 AD3d at 1364 [internal quotation marks and citation omitted]), and for Berkshire's failure to plead a viable claim under the "special facts" doctrine (*see P.T. Bank.*, 301 AD2d at 378).

For the reasons stated above, the Court concludes that Berkshire has failed to sufficiently allege a fiduciary, confidential or special relationship with Pioneer, but has stated claims for fraudulent inducement and fraudulent concealment under the special facts doctrine.

D. Viability of the Parallel Fraud and Contract Claims

Pioneer's final argument for dismissal of plaintiffs' fraud-based claims is that they are redundant of the claims alleging breach of the 2019 Participation Agreements. Pioneer contends that the alleged concealments and misrepresentations giving rise to the fraud-based claims — the substantial overdrafts, suspicious deposit and withdrawal activity, ValueWise's receipt of substantial third-party financing, and the existence of a Viverant [DE] — are precisely the same concealments and misrepresentations that are said to constitute Pioneer's breaches of the representations and warranties in the Participation Agreements.

The parties agree that, "under New York law, parallel fraud and contract claims may be brought if the plaintiff (1) demonstrates a legal duty separate from the duty to perform under the contract; (2) points to a fraudulent misrepresentation that is collateral or extraneous to the

contract; or (3) seeks special damages that are unrecoverable as contract damages" (*Merrill Lynch & Co. Inc. v Allegheny Energy, Inc.*, 500 F3d 171, 183 [2d Cir 2007], citing *Bridgestone/Firestone, Inc. v Recovery Credit Servs., Inc.*, 98 F3d 13, 20 [2d Cir 1996]; *see Cole, Schotz, Meisel, Forman & Leonard, P.A. v Brown*, 109 AD3d 764, 765 [1st Dept 2013]; *Krantz v Chateau Stores of Canada*, 256 AD2d 186, 187 [1st Dept 1998]; *see also* NYSCEF Doc No. 11 ["MOL"], p. 25; Berkshire Opp, p. 30; Chemung Opp, p. 24).

Pioneer asserts that Berkshire and Chemung's fraud-based claims satisfy none of these criteria. Specifically, Pioneer maintains that: (1) it did not owe plaintiffs a legal duty separate from its duty to perform under the Participation Agreements; (2) the purported concealments and misrepresentations are not collateral or extraneous to the claimed breaches of the Participation Agreements and, in fact, are identical to the breaches of representations and warranties sued upon by plaintiffs; and (3) the fraud-based claims do not seek special damages unrecoverable as a matter of law under a contractual theory.

1. Separate Legal Duty

Pioneer acknowledges that the special facts doctrine gives rise to a legal duty separate from any contractual duty of performance (*see* MOL, pp. 25-26). Having concluded that the Complaints sufficiently allege fraud-based claims under the special facts doctrine, plaintiffs also have alleged the breach of a legal duty separate from Pioneer's duty to perform under the [*11]Participation Agreements.

2. Collateral or Extraneous Misrepresentations/Concealments

Pioneer argues that the misrepresentations and concealments underlying the fraud-based claims cannot be considered collateral or extraneous to the Participation Agreements because plaintiffs rely on the exactly same misrepresentations and concealments to support their claims for breach of contract (*compare* Berkshire Complaint, ¶¶ 121, 126, 129-130, *with id.*, ¶¶ 142, 144-147, 154, 162; Chemung Complaint, ¶¶ 113, 116, 119, 121-122, *with id.*, ¶¶ 128-130, 134, 137-138, 141, 154-155).

"A separate cause of action seeking damages for fraud cannot stand when the only fraud alleged relates to a breach of contract" (*Gizzi v Hall*, 300 AD2d 879, 880 [3d Dept 2002] [citations omitted]). "A present intent to deceive must be alleged and a mere misrepresentation of an intention to perform under the contract is insufficient to allege fraud"

(*East Coast Intl. Tire Group, Inc. v New York Tire Factory, Inc.*, 185 AD3d 662, 663 [2d Dept 2020]).

But "a misrepresentation of present fact, unlike a misrepresentation of future intent to perform . . . , is collateral to the contract, even though it may have induced the plaintiff to sign it, and therefore involves a separate breach of duty" (*GoSmile, Inc. v Levine*, 81 AD3d 77, 81 [1st Dept 2010], *lv dismissed* 17 NY3d 782 [2011]). "For example, if a plaintiff alleges that it was induced to enter into a transaction because a defendant misrepresented material facts, the plaintiff has stated a claim for fraud even though the same circumstances also give rise to the plaintiff's breach of contract claim" (*First Bank of Ams. v Motor Car Funding*, 257 AD2d 287, 291-292 [1st Dept 1999]).

Thus, a plaintiff may allege parallel claims for fraudulent inducement and breach of contract under New York law even where the same misrepresentations and concealments are alleged to constitute a breach of contractual representations and warranties:

> [P]laintiff's fraud claim is premised on allegations that defendants misrepresented various pertinent facts about the individual loans that plaintiff purchased under the Agreement. This cannot be characterized merely as an insincere promise of future performance. Nor is the fraud claim rendered redundant by the fact that these alleged misrepresentations breached the warranties made . . . in the Agreement. These warranties certified that as of the date of sale . . . , any individual loan would comply with certain underwriting guidelines. The core of plaintiff's claim is that defendants intentionally misrepresented material facts about various individual loans so that they would appear to satisfy these warranties. . . . This is fraud, not breach of contract. *A warranty is not a promise of performance, but a statement of present fact*. Accordingly, a fraud claim can be based on a breach of contractual warranties notwithstanding the existence of a breach of contract claim

(*id*. at 292 [emphasis added]; *accord U.S. Tsubaki Holdings, Inc. v Estes*, 194 AD3d 590, 591 [1st Dept 2021] ["Plaintiffs allege misrepresentation of numerous present facts, in the form of defendants' alleged breaches of various . . . representations and warranties"]; *Ohm NYC LLC v Times Sq. Assoc. LLC*, 170 AD3d 534, 534 [1st Dept 2019]; *Wyle Inc. v ITT Corp.*, 130 AD3d 438, 439-440 [1st Dept 2015] ["intentional failure to disclose an ongoing audit" is collateral, even though same "nondisclosure is a breach of a contractual warranty"]; *MBIA Ins. Corp. v Countrywide Home Loans, Inc.*, 87 AD3d 287, 293 [1st Dept 2011]; *GoSmile*, 81 AD3d at 81; *see also Deerfield Communications Corp. v Cheesebrough-Ponds, Inc.*, 68 NY2d 954, 956 [1986]; *Merrill Lynch & Co. v Allegheny Energy, Inc.*, 500 F3d 171, 184 [2d Cir 2008] ["A [*12]plaintiff may elect to sue in fraud on the basis of misrepresentations that breach express

warranties. Such cause of action enjoys a longstanding pedigree in New York."]; *cf.* *Cronos Group Ltd. v XComIP, LLC*, 156 AD3d 54, 64 [1st Dept 2017] [fraud claim based on oral misrepresentations made *after* contract formation is "duplicative . . . , inasmuch as the only fraud alleged is (defendant's) unkept promise to perform certain of its preexisting obligations"]).

To be sure, some courts applying this aspect of New York law, particularly the federal district courts, take a stricter approach to the viability of parallel fraud and contract claims and what it means for a misrepresentation or concealment to be collateral or extraneous (*see e.g. Kriegel v Donelli*, 2014 WL 2936000, *14, 2014 US Dist LEXIS 90086, *47 [SD NY, June 30, 2014, No. 11 Civ. 9160 (ER)] ["From Plaintiff's view, the exact representations made by Defendant in the warranty in Section 10(c) also fraudulently induced Plaintiff's entry into the contract; therefore, his claim is wholly duplicative."]; *Koch Indus. v Hoechst Aktiengesellschaft*, 727 F Supp 2d 199, 215 [SD NY 2010]; *DynCorp v GTE Corp.*, 215 F Supp 2d 308, 326 [SD NY 2002] ["(T)he Purchase Agreement made clear that GTE would have no liability or indemnification obligation to Buyer,' 'except for the representations and warranties contained in this Agreement.' . . . . DynCorp's claims of fraud concerning the breach of contractual warranties are not 'collateral or extraneous' to these terms and conditions; rather, they contradict them" (brackets omitted)]). But this Court is obliged to follow the precedent of the New York State Court of Appeals and the Appellate Divisions, not the lower federal courts (*see generally People v Kin Kan*, 78 NY2d 54, 59-60 [1991]; *Maple Med., LLP v Scott*, 191 AD3d 81, 90-91 [2d Dept 2020]).

The Court therefore concludes that plaintiffs' fraud-based claims sufficiently allege misrepresentations and concealments that are collateral or extraneous to the Participation Agreements.[FN4]

3. Special Damages

Finally, Pioneer contends that plaintiffs' fraud-based claims do not seek special damages unrecoverable as contract damages because: (1) rescissory damages are available in an action for breach of contract; and (2) plaintiffs' acceptance of a certain litigation settlement concerning Viverant bars plaintiffs from recovering rescissory damages.

Pioneer explains that plaintiffs' fraud-based claims seek the same damages as their contractual claims, together with the "additional damages necessary to place [plaintiffs] in the economic position [they] would have achieved absent Pioneer's fraud, including but not

limited to [plaintiffs'] costs, expenses, increased administrative burden, and lost opportunity cost" (Berkshire Complaint, Wherefore clause; Chemung Complaint, Wherefore clause). "In other words, the only difference between the breach of contract and fraud claims is that [plaintiffs'] fraud claims also seek rescissory damages" (MOL, p. 28).

The Court does not find Pioneer's argument to be convincing. Plaintiffs are suing to recover out-of-pocket losses due to Pioneer's alleged fraud, including their "costs [and] expenses" (Berkshire Complaint, Wherefore Clause, [C-E]; *accord* Chemung Complaint, Wherefore Clause, [B-E]; *see Lama Holding Co. v Smith Barney*, 88 NY2d 413, 421 [1996] [*13]["The true measure of damage is indemnity for the actual pecuniary loss sustained as the direct result of the wrong or what is known as the 'out-of-pocket' rule. . . . Damages are to be calculated to compensate plaintiffs for what they lost because of the fraud, not to compensate them for what they might have gained" (internal quotation marks and citations omitted)]; *Connaughton v Chipotle Mexican Grill, Inc.*, 135 AD3d 535, 538 [1st Dept 2016], *affd* 29 NY3d 137 [2017]). Pioneer has failed to conclusively establish that all of plaintiffs' out of pocket losses are recoverable under their claims for breach of contract.[FN5]

4. Conclusion

For all of the foregoing reasons, Pioneer has failed to demonstrate that the fraud-based claims should be dismissed as redundant of plaintiffs' claims for breach of the 2019 Participation Agreements.

E. Breach of 2018 Participation Agreement

Finally, Pioneer moves for dismissal of Berkshire's first cause of action, alleging breach of the 2018 Participation Agreement. Pioneer contends that, by "amend[ing] and restat[ing] in its entirety" the 2018 Participation Agreement, the 2019 Participation Agreement extinguished any claims for breach of contract that may have accrued in favor of Berkshire under the earlier agreement.

"It is well settled that where the parties have clearly expressed or manifested their intention that a subsequent agreement supersede or substitute for an old agreement, the subsequent agreement extinguishes the old one and the remedy for any breach thereof is to sue on the superseding agreement" (*Northville Indus. Corp. v Fort Neck Oil Terms. Corp.*,

100 AD2d 865, 867 [2d Dept 1984] [internal quotation marks and citations omitted], *affd on opn below* 64 NY2d 930 [1985]; *accord Lnzro Pizza Empire v Brown*, 229 AD2d 947, 948 [4th Dept 1996]).

In such cases, the superseding agreement is a novation (*see Citigifts, Inc. v Pechnik*, 67 NY2d 774, 775 [1986] ["there was a novation which extinguished the old agreement and relegated plaintiffs to an action for breach of the new agreement"], *affg* 112 AD2d 832 [1st Dept 1985]). "The elements of a novation are a previously valid obligation, agreement of the parties to the new obligation, extinguishment of the old contract, and a valid new contract. A novation will not discharge obligations created under a prior agreement unless it was so intended, and this question may be determined from the writings and conduct of the parties or, in certain cases, from the documents exclusively. The party claiming a novation has the burden of proof of establishing that it was the intent of the parties to effect a novation" (*Warberg Opportunistic Trading Fund L.P. v GeoResources, Inc.*, 151 AD3d 465, 472-473 [1st Dept 2017] [internal quotation marks and citations omitted]).

Applying these principles, the First Department held in *Leeward Isles Resorts, Ltd. v Hickox* (49 AD3d 277 [1st Dept 2008], *lv dismissed* 11 NY3d 914 [2009]) that a 1989 loan agreement that "expressly 'supersede[d] and replace[d]' [a] 1986 loan agreement[] did not merely modify the 1986 loan agreement, as defendant argue[d], but constituted a novation thereof" (*id*. [*14]at 278). In so concluding, the First Department distinguished *CrossLand Fed. Sav. Bank v A. Suna & Co., Inc.* (935 F Supp 184, 199 [ED NY 1995]), where the material terms of the loan, other than the time for payment and rate of interest, remained the same (*see Leeward Isles*, 49 AD3d at 278).

Here, the only substantive change made in the 2019 Participation Agreement was to modify Berkshire's 50% interest in the $32 Million Revolving LOC ($16 million) to a 44.04761905% interest in the $42 Million Revolving LOC ($18.5 million). Concerning the earlier agreement, the 2019 Participation Agreement states: "This Agreement amends and restates in its entirety [the 2018 Participation Agreement]" (2019 Participation Agreement, § 29). The 2019 Participation Agreement also includes a merger clause (*see id*., § 17).

Pioneer argues that the parties' agreement to amend and restate the 2018 Participation Agreement in its entirety manifests their intention that the 2019 Participation Agreement supersede and replace the earlier agreement. Pioneer cites several federal district court decisions holding that the contracting parties' "desire to amend and restate [an agreement] in

its entirety" is clear evidence of "the parties' intent to supersede the original [agreement]" (*L-3 Communs. Corp. v OSI Sys.*, 2004 WL 42276, *9 & n 3; 2004 US Dist LEXIS 165, *25 & n 3 [SD NY, Jan. 8, 2004, No. 02 Civ. 9144 (DC)]; *accord BNP Paribas Mtge. Corp. v Bank of Am., N.A.*, 778 F Supp 2d 375, 401-402 [SD NY 2011]).

Contrary to Berkshire's contention, the Court is satisfied that the language used in the 2019 Participation Agreement — that it "amends and restates [the earlier agreement] in its entirety" — is an objective manifestation of the parties' intention to supersede and replace the 2018 Participation Agreement. In *Matter of Kneznek* (284 AD2d 698 [3d Dept 2001]), for example, the Third Department held that a 1990 agreement, which "amended and restated in its entirety" an earlier agreement, constituted clear evidence that the subsequent agreement was intended to supersede and replace the earlier one (*id.* at 701).

Further, while Berkshire argues that there is nothing in the 2019 Participation Agreement that expressly waived, discharged or released claims under the 2018 Participation Agreement, the absence of such language is not dispositive. "Ordinarily, where an agreement alleged to have been breached has been rescinded, the claim is determined by reference to the rescission agreement, and in general no such claim can be made unless expressly or impliedly reserved upon the rescission" (*Mallad Constr. Corp. v County Fed. Sav. & Loan Assn.*, 32 NY2d 285, 293 [1973] [internal quotation marks and citation omitted]; *see Matter of Kneznek*, 284 AD2d at 701; *M. J. Posner Constr. Co. v Valley View Dev. Corp.*, 118 AD2d 1001, 1001-1002 [3d Dept 1986]; *see also Citigifts*, 67 NY2d at 775; *Northville Indus. Corp.*, 100 AD2d at 867; *cf. Citibank, N.A. v Outdoor Resorts of Am., Inc.*, 1992 WL 162926, *5, 1992 US Dist LEXIS 9624, *15-16 [SD NY, June 29, 1992, No. 91 CIV. 1407 (MBM)]).

But even accepting Pioneer's position that the text of the 2019 Participation Agreement evinces an intention to supersede and replace the 2018 Agreement, the Court is left with questions as to whether the elements of a novation have been conclusively established by Pioneer so as to extinguish Berkshire's claim for breach of the 2018 Participation Agreement.

One element of a novation is a valid earlier agreement (*see Warberg,* 151 AD3d at 472). Here, Berkshire alleges that, unbeknownst to it, Pioneer was in material breach of the 2018 Participation Agreement at the time of the alleged novation based on, among other things, its concealment of material information concerning the finances of Mann, ValueWise and the other Borrowers (*see* Complaint, ¶¶ 117-119; *see* Berkshire Opp, p. 8). In this regard, there is [*15]appellate authority holding that a novation cannot take place under New York law if the

original contract already has been breached: "If a party breaches a preexisting contract, there can be no novation because the first element (of a previously valid obligation) is negated" (*Lambert v Schiller*, 156 AD3d 1285, 1287 [3d Dept 2017]; *see Wasserstrom v Interstate Litho Corp.*, 114 AD2d 952, 954 [2d Dept 1985]; *Benjamin v Yeroushalmi*, 2018 NY Slip Op 33655[U], *7-8 [Sup Ct, Nassau County 2018], *affd as mod on other grounds* 178 AD3d 654 [2d Dept 2019]; *see also Berkshire Bank v Tedeschi*, 2013 WL 1291851, *11, 2013 US Dist LEXIS 43214, *32 [ND NY, Mar. 27, 2013, No. 1:11-CV-0767 (LEK/CFH)]; *In re Cohen*, 418 BR 785, 804 [ED NY 2009], *affd in part, revd in part on other grounds* 422 BR 350 [ED NY 2010]).[FN6]

Another essential element of a novation is a valid new agreement (*see Warberg*, 151 AD3d at 472). Here, Berkshire alleges that it was fraudulently induced to enter the 2019 Participation Agreement through Pioneer's concealment of material information concerning Mann, ValueWise and the other Borrowers — the same information that Pioneer allegedly failed to disclose in contravention of the 2018 Participation Agreement. Pioneer has not cited any authority that speaks directly to the situation where the superseding agreement is alleged to have been procured by fraudulent concealment, particularly where the concealment is alleged to constitute a breach of the earlier agreement.[FN7]

Finally, "[a] novation will not discharge obligations created under a prior agreement unless it was so intended" (*id*. at 473). While section 29 of the 2019 Participation Agreement provides strong textual support for Pioneer's contention that the subsequent agreement was intended to supersede and replace the earlier one, the circumstances surrounding execution of the 2019 Participation Agreement and the limited changes that were made by the new agreement leave the Court questioning whether the parties intended to extinguish accrued but unknown claims under the old agreement (*see Globe Food Servs. Corp. v Consolidated Edison Co. of NY*, 184 AD2d 278, 279 [1st Dept 1992]).

It may well be, however, that Berkshire's claim under the 2018 Participation Agreement is foreclosed by the text of the 2019 Participation Agreement and/or Berkshire's decision to treat the 2019 Participation Agreement as valid and subsisting (*see* Berkshire Opp., p. 37). But given the lack of clear authority and unanswered questions, the Court believes that it would be premature to dismiss Berkshire's claim for breach of the 2018 Participation Agreement at this juncture.[FN8]

[*16]CONCLUSION

For all of the foregoing reasons,[FN9] it is

ORDERED that the sixth cause of action in the Berkshire Complaint (Action No. 1) and the fourth cause of action in the Chemung Complaint (Action No. 2), alleging negligent misrepresentation, are dismissed; and it is further

ORDERED that Pioneer's motions are granted to the limited extent indicated above and denied in all other respects in accordance with the foregoing; and finally it is

ORDERED that a remote preliminary conference shall be scheduled, and the parties are directed to confer in advance of such conference regarding the matters set forth in Commercial Division Rule 8, as well as the use of mediation or other forms of alternative dispute resolution to bring about an early resolution of these actions.

This constitutes the Consolidated Decision & Order of the Court, the original of which is being uploaded to NYSCEF in Action Nos. 1 & 2 for electronic entry by the Albany County Clerk. Upon such entry, counsel for plaintiffs shall promptly serve notice of entry on all parties entitled thereto.

Dated: July 1, 2021

Albany, New York

RICHARD M. PLATKIN

A.J.S.C.

Papers Considered:

Action No. 1: NYSCEF Doc Nos. 10-19, 28-38, 41, 48.

Action No. 2: NYSCEF Doc Nos. 10-18, 27-37, 40, 45.

Footnotes

Footnote 1: Where the allegations of plaintiffs' complaints are essentially the same, the Court will, in the interest of economy, generally cite only to the Berkshire Complaint.

Footnote 2: Given the nature of inter-bank participation agreements, the originating lender invariably will possess greater knowledge of the transaction and the borrower(s). Yet, plaintiffs do not cite a single case finding a fiduciary, confidential or special relationship arising from such a transaction.

Footnote 3: This two-prong test is the mirror image of the requirement that a party pleading fraudulent inducement or fraudulent concealment "allege facts to support the claim that it justifiably relied on the alleged misrepresentations. It is well established that if the facts represented are not matters peculiarly within the defendant's knowledge, and the plaintiff has the means available to it of knowing, by the exercise of ordinary intelligence, the truth or the real quality of the subject of the representation, the plaintiff must make use of those means, or it will not be heard to complain that it was induced to enter into the transaction by misrepresentations'" (*ACA Fin. Guar. Corp. v Goldman, Sachs & Co.*, 25 NY3d 1043, 1044 [2015] [internal quotation marks, citation and alterations omitted]).

Footnote 4: The parties agree that there is nothing in the Participation Agreements that "preclude[s] a fraud suit on the basis of the alleged misstatement[s and concealments]" (*Koch Indus.*, 727 F Supp 2d at 215).

Footnote 5: In reply, Pioneer raises a new argument concerning plaintiffs' alleged failure to plead their special damages with the heightened particularity required by CPLR 3016 (b). However, this argument is not properly before the Court (*see Mikulski v Battaglia*, 112 AD3d 1355, 1356 [4th Dept 2013]).

Footnote 6: Neither the First Department's decision in *Leeward Isles* nor the Third Department's decision in *Matter of Kneznek* involved allegations that the earlier agreement had been breached when the novating agreement was executed. Moreover, it bears emphasis that Berkshire was unaware of the alleged breaches of the 2018 Participation Agreement

when it executed the 2019 Participation Agreement.

Footnote 7: There were allegations of fraud in *L-3* and *BNP Paribas*, but the decisions do not discuss the interrelationship, if any, between the fraud claims and the defense of novation.

Footnote 8: The burden of proceeding to fact discovery on Berkshire's claim for breach of the 2018 Participation Agreement should be minimal, as the facts surrounding that claim overlap substantially with Berkshire's claim for breach of the 2019 Participation Agreement and its fraud-based claims.

Footnote 9: The Court has considered the parties' remaining arguments and contentions but finds them unavailing and/or unnecessary to reach given the disposition ordered herein.

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