TO: The Official Pattern Jury Instructions Committee  
FROM: New York State Bar Association  
Commercial and Federal Litigation Section  
RE: Proposed Jury Instructions  
DATED: October 8, 2012

The Commercial and Federal Litigation Section of the New York State Bar Association submits for your consideration proposed jury charges and comments on existing charges. The first charge addresses alter ego or piercing the corporate veil. In addition to PJI language, we drafted a sample verdict sheet and commentary. The second addresses breach of fiduciary duty and is intended to supplement the existing PJI with sample PJIs for family members and majority versus minority shareholders. We also include a PJI for aiding and abetting breach of fiduciary duty. Finally, we drafted language to be added to your commentary on breach of contractual warranty and fraudulent inducement to reflect the current state of the law in New York.

We recognize that these materials only partially respond to the PJI Committee’s request in that we have not included sample instructions used or prepared for actual jury trials. During the second phase of our project, we continue soliciting comments and sample jury instructions from our members. We will also consider drafting PJIs for holder in due course claims and claims involving merger clauses.

I. Piercing the Corporate Veil

As a general matter, a corporation or similar business entity, such as a partnership or LLC, is legally separate from its owners or stockholders. It does business in its own right and with its own resources. The law encourages the independence of corporate entities to attract investors who can invest their money in the corporate entity without risking individual liability
for corporate acts and transactions. This protection an investor or owner enjoys is sometimes known as the “corporate shield.”

The protection of the corporate shield is not absolute, however. Circumstances may arise that justify the loss of the corporate shield. This is sometimes known as “piercing the corporate veil.” A defendant may face loss of the corporate shield where plaintiff can prove that: (1) defendant completely controlled the corporate defendant whose veil plaintiff is seeking to pierce AND (2) defendant abused its complete control of the corporate entity to perpetrate a wrongful or unjust act on plaintiff to plaintiff’s detriment.

Plaintiff AB claims that Sham Corp [name of allegedly sham corporation] was a mere instrument or tool of defendant CD. This means that plaintiff AB claims that defendant CD and Sham Corp. are in essence one and the same, such that it is possible to disregard the separate corporate existence of Sham Corp. and hold defendant CD responsible for Sham Corp.’s acts and obligations.

A. Domination and Control by Individual

To decide whether CD dominated and controlled Sham Corp., you should consider:

(1) the purpose for which CD formed or acquired the corporation;

(2) whether Sham Corp. maintained corporate books and records, whether its directors conducted regular meetings and whether Sham Corp observed other corporate legal formalities;

(3) whether Sham Corp had enough funds at its formation to meet its obligations;
(4) whether the funds of the corporation and CD’s funds were intermingled in the same accounts;

(5) the activity or inactivity of others as officers or directors in the business affairs of the corporation; and

(6) any other factors the evidence discloses tending to show that the corporation was or was not operated as an entity separate and apart from CD.

B. Domination and Control by Another Business Entity

[Where the defendant CD is a parent or affiliated corporation, as opposed to an individual, it is appropriate to consider]:

(1) whether CD caused the incorporation of the subsidiary or affiliate;

(2) whether CD and the subsidiary or affiliate have the same or many of the same officers, directors, shareholders and employees;

(3) whether the business purpose or function of the subsidiary or affiliate is separate and distinct from the that of the other entity;

(4) whether the two entities kept separate books and records (with the exception of joint tax returns the law may require);

(5) whether CD finances the subsidiary or affiliate or pays the salaries and other expenses of the subsidiary or affiliate;
(6) whether related companies performed the administrative services (i.e. accounting, payroll, bookkeeping) on behalf of the subsidiary or affiliate;

(7) whether the funds of the subsidiary or affiliate and CD were intermingled;

(8) the amount of business discretion CD has over the subsidiary or affiliate; and

(9) any other factor the evidence tends to show that the subsidiary or affiliate was or was not an entity separate and apart from CD.

C. Fraud or Inequitable Consequences Element

It is not necessary that plaintiff prove actual fraud to pierce the corporate veil. However, plaintiff bears a heavy burden to show that the corporation was dominated as to the transaction attacked and that this domination was the instrument of fraud or otherwise resulted in wrongful or inequitable consequences. Thus, without more, the circumstance that one or two individuals own and control more than one business entity or that two business entities have common officers and directors, does not mean that the corporate form may be disregarded. Abuse of that control must be proved.

To decide whether the domination was the instrument of fraud or otherwise resulted in wrongful or inequitable consequences, you should decide whether defendant used the domination and control to (1) commit a fraud or deceit; (2) violate a statutory or other positive legal duty; (3) avoid an obligation to plaintiff or (4) to commit a dishonest or unjust act in violation of the plaintiff’s rights. In addition, the control and the wrongful use of that control together must be a proximate or direct cause of plaintiff’s loss.
In cases alleging fraud, plaintiff must prove fraud by clear and convincing evidence.

[For Pattern Jury Instructions Concerning Fraud, see PJI 3:20]. However, in cases falling short of fraud, plaintiff still has a heavy burden to prove wrongful or inequitable consequences. (See discussion infra regarding standard of proof).
SAMPLE VERDICT SHEET

1) Did CD exercise complete domination and control over Sham Corp. such that the two should be treated as one?

[ ] Yes  [ ] No

If your answer to question 1 is “No” stop and report to the court. If you answered “Yes” to question 1, proceed to the next question.

2) Did that complete domination and control result in any fraud, illegality or other wrong against plaintiff?

[ ] Yes  [ ] No

If your answer to question 2 is “No” stop and report to the court. If you answered “Yes” to question 2, proceed to the next question.
Comment

**Caveat: Standard of Proof**

Because plaintiff need not prove actual fraud to pierce the corporate veil, but must prove only that it suffered a wrongful or unjust act due to defendant’s misuse of the corporate form, a “clear and convincing” standard of proof may not be necessary where circumstances do not rise to the level of fraud. *See Rotella v Derner*, 283 AD2d 1026, 723 NYS2d 801 (4th Dep’t 2001) (Supreme Court misconstrued action as one for fraud and erred in holding plaintiffs to a clear and convincing standard of proof when it sufficed for wrongdoing that the corporation was undercapitalized and the defendant disregarded corporate formalities and made personal use of corporate funds). However, no court has addressed what the standard of proof is in cases falling short of fraud. The Court of Appeals has described the “heavy burden” that “those seeking to pierce the corporate veil of course bear.” *TNS Holdings, Inc., v MKI Sec. Corp.*, 92 NY2d 335, 339 (1998). This language might imply a standard of proof more stringent than preponderance of the evidence, but whether the standard is preponderance of the evidence or somewhere in between preponderance of the evidence and clear and convincing evidence is an open question.

**Caveat: Outlier Cases that Drop the Inequity Element**

The Court of Appeals has held, time and again, that mere dominance or control alone is insufficient to pierce the corporate veil. *TNS Holdings, Inc., v. MKI Securities Corp.*, 92 NY2d 335, 339 (1998) (“[e]vidence of domination alone does not suffice without an additional showing that it led to inequity, fraud or malfeasance”); *see also Morris v. New York State Department of Taxation and Finance et al.*, 82 NY2d 135, 141 (1993); *ABN Amro Bank, N.V. v. MBIA, Inc.*, 17 NY3d 208, 229 (2011) (reiterating that it is proper to dismiss a request to pierce the corporate
veil where plaintiff failed to allege any harm resulting from an abuse or perversion of the corporate form).

Despite this clear articulation from the Court of Appeals, some courts have apparently omitted the second factor, i.e. “fraud, inequity or malfeasance.” See, e.g. Fernbach v Calleo, 92 AD3d 831, 833, 939 NYS2d 501,504 (2d Dep’t 2012); Campone v Piscotta Services, Inc., 87 AD3d 1104, 1105, 930 NYS2d 62, 64 (2d Dep’t 2011). The deletion of the “fraud, inequity or malfeasance” requirement seems to have developed by isolating a quote from an Appellate Division, Third Department case. That case, Island Seafood Co. v Golub Corp, 303 AD2d 892, 893, 759 NYS2d 768 (3d Dep’t 2003) stated “[a]dditionally the corporate veil will be pierced to achieve equity, even absent fraud, when a corporation has been so dominated by an individual or another corporation and its separate entity so ignored that it primarily transacts the dominator’s business instead of its own and can be called the other’s alter ego.” Some courts have taken this quote out of context and assumed that domination alone will suffice in those cases where the domination and control is so severe that defendant primarily transacts the business of the other. However, all the Island Seafood court was attempting to convey is that the wrongdoing does not have to amount to fraud. It did not disavow the second requirement that there be inequity. Indeed, later in the decision, the Island Seafood court stated “domination, standing alone, is not enough” and upheld the dismissal of plaintiff’s veil piercing claim where “petitioner failed to meet its burden of demonstrating that [defendant] through his domination, abused his power over both corporations to commit a wrong or injustice to the detriment of petitioner.” Id at 896.
Reverse Veil Piercing

Typical veil piercing involves holding an individual liable for actions of a business entity he or she controls. New York also recognizes “reverse veil piercing” that holds the business entity accountable for actions of its owners or shareholders (see Sweeney, Cohn, Stahl & Vaccaro v. Kane, 6 AD3d 72, 74, 773 NYS2d 420, 424 (2d Dep’t 2004); Colonial Sur. Co. v. Lakeview Advisors, LLC, 93 A.D.3d 1253, 941 N.Y.S.2d 371, 374 (4th Dep’t 2012). “Although reverse veil piercing is rare, it may be appropriate in cases where the alter ego is being used as a ‘screen’ for the dominating entity.” Miramax Film Corp. v. Abraham, No. 01 CV 5202, 2003 WL 22832384, at *7 (S.D.N.Y. Nov.25, 2003) (citations omitted). The standard for reverse veil piercing is the same, namely domination plus misuse of the corporate form to cause injury (see, e.g., Monteleone v. The Leverage Group, 2009 WL 249801 at *3 (E.D.N.Y., January 28, 2009).
II. **Breach of Fiduciary Duty**

*(Majority Shareholder to Minority Shareholder)*

The plaintiff, a minority shareholder in TR Corp., claims that the defendants, majority shareholders in TR Corp., have breached their fiduciary duty to him as a minority shareholder. As majority shareholders of a close corporation like TR Corp., the majority shareholders owe a fiduciary duty to the minority shareholders. Specifically, such fiduciary duties include the duty not to cause the corporation to effect a transaction that would benefit majority shareholders, at the expense of the minority shareholders. *Richbell Info. Servs., Inc v. Jupiter Partners, L.P.*, 309 A.D. 2d 288, 300 (1st dep’t. 2003); *Cottone v. Selective Services, Inc.*, 68 A.D. 3d 1038, 1039 (2d Dep’t. 2009).

If you find that the defendant majority shareholders, breached their obligation to the minority shareholders of TR Corp. by [describe act, i.e. Diluting shares], and were not acting in the best interests of, or contrary to, the interests of the plaintiff minority shareholders, then you will find in favor of the plaintiff.

If however, you find that the action taken by the defendant majority shareholders was not taken at the expense of or contrary to the best interests of the minority shareholders, but was taken as a result of the exercise of sound business judgment, then you will find in favor of the defendants.
**Family Member, Friend, Relationship of Trust**

Plaintiff claims that the defendant violated what is called a “fiduciary duty” or obligation that the defendant owed plaintiff. Such obligation is based on a relationship of trust, and, as a result, the confidence one person places in another. A fiduciary duty exists, where influence has been acquired and relied upon. 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 relationship. When a person has a fiduciary duty to act on behalf of another, he must act in good faith to carry out the intention of the other.

Where such a relationship exists and influence has been acquired and abused, or where one places trust or confidence in another, and that trust or confidence has been betrayed, there is a breach of that duty. *JP Morgan Chase Bank, N.A. v. IDW Group, LLC*, No. 08 Civ 9116, 2009 WL 321222 at *8 (S.D.N.Y. February 9, 2009); *Giblin v. Murphy*, 97 A.D. 2d 668, 670, 469, N.Y.S. 2d 211, 215 (3rd Dep’t. 1983); *Braddock v. Braddock*, 60 A.D. 3rd 84, 88, 871 N.Y.S. 2d 68, 72 (1st Dep’t. 2009); *Mandelblatt v. Devon Stones*, 132 A.D. 2d 162, 168 (1st Dep’t 1987); *Dolan v. Cummins*, 114 A.D. 787, 789 (2nd Dep’t 1907), *affid*, 193 NY 638 (1908). *Venizelos v. Oceania Maritime Agency, Inc.*, 268 A.D. 2d 291, 702 NYS 2d 17, 18 (1st Dep’t 2000).

A fiduciary duty can exist between or among family members. Plaintiff [defendant father, mother, sister, cousin, friend] claims that he trusted defendant [plaintiff’s son, daughter, brother, friend] because [state facts-- defendant had superior knowledge of ...; possessed influence over plaintiff because...; plaintiff relied upon defendant because...], that he reasonably
relied upon defendant to [insert facts] and that defendant breached his fiduciary duty to him by [state facts]. Plaintiff claims that as a result of this breach, he suffered damages.

Defendant, on the other hand, denies that a relationship of trust existed between him and plaintiff. He contends that plaintiff could not have reasonably relied upon him because [he did not possess superior knowledge in regard to...; plaintiff should have known......], or that he breached any duty he owed plaintiff by [put in facts].

I charge you that if you find, by a fair preponderance of the credible evidence, (1) that a relationship of confidence and trust existed between plaintiff and defendant, (2) that plaintiff reasonably relied upon defendant and (3) that defendant failed to act for the benefit of plaintiff within the scope of the relationship of trust, you will find for plaintiff. If you do not so find, you will find for defendant.
SAMPLE VERDICT SHEET

1) Did a fiduciary relationship exist between plaintiff and [a father, mother, sister, cousin, friend]?

   ____     ____
   Yes     No

   If the answer is “no,” stop and return to the courtroom. If the answer is “yes,” go on to question 2.

2) Did the defendant breach his/her fiduciary duty to the plaintiff?

   ____     ____
   Yes     No

   If the answer to question 2 is “no” stop and report to the court. If the answer is “yes,” go on to question 3.

3) What is the amount of damage, if any, due to the plaintiff? $___________________
Aiding and Abetting a Breach of Fiduciary Duty

In addition to the breach of fiduciary duty which I have described to you, a person or persons can be found to have aided and abetted an individual or an entity in breaching a fiduciary duty or obligation owed to another.

In order to be found responsible for aiding and abetting a breach of fiduciary duty, the plaintiff must show, by a preponderance of the evidence, that the defendant provided substantial assistance in effecting the breach, together with resulting damages.

The plaintiff [once a majority shareholder in TR Corp] claims that Mr. X owed him a fiduciary duty and that the defendant [present majority shareholder in TR Corp] aided and abetted [Mr. X] in breaching his fiduciary duty to the plaintiff by [describe act, i.e. Purchasing plaintiff’s shares in TR Corp without plaintiff’s consent with knowledge that Mr. X had no authority to sell plaintiff’s shares]. Plaintiff alleges that this act [i.e. Sale of his shares in TR Corp to defendant] was to his detriment. The defendant denies that he aided and abetted Mr. X’s breach of fiduciary duty [and that he was an innocent purchaser of the plaintiff’s shares].

If you find that the defendant acted purposely to aid and abet or substantially assisted Mr. X, in the act which plaintiff claims caused him harm [purchasing the plaintiff’s shares which Mr. X sold without plaintiff’s consent], or that the defendant acted as a co-agent to induce, enable, or substantially assist Mr. X in breaching Mr. X’s fiduciary duty to the plaintiff, and that the plaintiff suffered damages as a result of such aiding and abetting, then you will find in favor of the plaintiff.
If however you find that the defendant did not substantially assist in or effect Mr. X’s breach of fiduciary duty as plaintiff alleges, then you will find in favor of the defendant. 

SAMPLE VERDICT SHEET

1) Did Mr. X breach a fiduciary duty to plaintiff?

Yes     No

If you answered “no” stop and report to the court. If you answered “yes”
go on to question 2.

2) Did the defendant aid and abet Mr. X in breaching his fiduciary duty to the
plaintiff?

Yes     No

If you answered “no” stop and report to the court. If you answered “yes”
go on to question 3.

3) What is the amount of damages, if any, owed by the defendant to the plaintiff?

$__________________
The rule had long been that a fraudulent inducement claim for breach of a contractual warranty would be dismissed as duplicative of the breach of warranty claim, unless the plaintiff alleged a misrepresentation made outside the contract. The rule protected the parties bargained-for and negotiated contract term: recovery of contractual damages for breach of a warranty. Recent decisions have conflated the concepts of reasonable reliance in claims for fraudulent inducement and reliance on contractual warranties. The result is that in virtually every contract dispute for breach of warranty, the plaintiff also pleads fraud in the inducement and both causes of action survive a motion to dismiss.

A long line of cases have held that to sustain a claim for fraudulently inducing a party to contract, the plaintiff must allege a representation that is collateral to the contract, not simply a breach of a contractual warranty and damages not recoverable in an action for breach of contract. *RGH Liquidating Trust v Deloitte & Touche LLP*, 47 AD3d 516 (1st Dept 2008), app den 11 NY3d 804 (2008)(fraudulent inducement duplicative because it alleged no misrepresentations collateral or extraneous to agreements); *Hawthorne Group, LLC v RRE Ventures*, 7 AD3d 320, 323 (1st Dept 2004) (alleged misrepresentation should be one of then-present fact, extraneous to contract and involve duty separate from or in addition to that imposed by contract); *Varo v Alvis PLC*, 261 AD2d 262 (1st Dept 1999)(duplicitive because misrepresentations not collateral to contract); *JE Morgan Knitting Mills, Inc. v Reeves Bros., Inc.*, 243 AD2d 422 (1st Dept 1997)(fraudulent inducement duplicative because based on same facts as contract claim, not collateral to contract and all damages recoverable for breach of contract); *Krantz v Chateau Stores of Can., Ltd.*, 256 AD2d 186 (1st Dept 1998)(fraud claim dismissed as duplicative of
breach of contract claim); *Mastropieri v Solmer Constr. Co.*, 159 AD2d 698, 700 (2d Dept 1990) (well-settled that cause of action to recover damages for fraud will not lie when only fraud charged related to breach of contract); *Trusthouse Forte Mgmt., Inc. v Garden City Hotel, Inc.*, 106 AD2d 271, 272 (1st Dept 1984) (well-settled that cause of action for fraud seeking punitive damages will not lie when only fraud charged related to breach of contract); cf. *GoSmile, Inc. v Levine*, 2010 NY Slip Op 9408; 915 NYS2d 521; 2010 NY App. Div LEXIS 9485 (1st Dept 2010) (nor) (fraud claim sustained because “many ‘additional’ facts” in addition to warranty misrepresented); *RAG Am. Coal Co. v Cyprus Amax Minerals Co.*, 299 AD2d 259 (1st Dept 2002) (fraud claim sustained because it relied on representations not contained in contractual warranty).

However, in *DDJ Management, LLC v Rhone Group, LLC*, 15 NY3d 147, 154 (2010), the Court of Appeals extended the notion of justifiable reliance in tort to breaches of contractual warranties. In *DDJ*, the plaintiff alleged that it relied on a contractual warranty as to the accuracy of financial statements. The Court of Appeals held that:

> where a plaintiff has gone to the trouble to insist on a written representation [the contractual warranty] that certain facts are true, it will often be justified in accepting that representation [or warranty] rather than making its own inquiry. [emphasis supplied]

_Id._ Where such are the facts, whether a party was “justified in relying on the warranties [it] received is a question to be resolved by the trier of fact.” *Id.* at 156. Very possibly, the Court reached this conclusion because there was no breach of contract claim in *DDJ*, as is made clear from the Supreme Court decision. *DDJ Management, LLC v Rhone Group, LLC*, 19 Misc3d 1124A (Sup Ct NY Co 2008).
As the New York Court of Appeals explained in *CBS Inc v Ziff-Davis Publishing Co.*, the analysis of reliance in a tort action based on fraud or misrepresentation [tort reliance] differs from the analysis of reliance in actions for breach of express warranties [warranty reliance]. *CBS Inc v Ziff-Davis Publishing Co.*, 75 NY2d 496, 502-506 (1990). The Court of Appeals in *Ziff-Davis* adopted the reasoning of the Southern District of New York in *Ainger*, which clarifies that for the purposes of tort reliance the plaintiff must have:

believed [the representation] to be true. If it appears that he knew the facts, or believed the statement to be false, or that he was in fact so skeptical as to its truth that he reposed no confidence in it, it cannot be regarded as a substantial cause of his conduct. [emphasis supplied]


By contrast, in warranty reliance, “the critical question is not whether the [plaintiff] believed in the truth of the warranted information . . . but whether it believed it was purchasing the [defendant’s] promise as to its truth.” [citations omitted] [emphasis supplied] *Ziff-Davis Publishing Co.*, 75 NY2d at 503; *see also Merrill Lynch & Co. Inc. v Allegheny Energy, Inc.*, 500 F3d 171, 186 (2d Cir 2007) (applying New York law) (“In contrast to the reliance required to make out a claim for fraud, the general rule is that a buyer may enforce an express warranty even if it had reason to know that the warranted facts are untrue. . . . [as long as] it believed that it was purchasing seller’s promise regarding the truth of the warranted facts.”). The distinction
between tort and warranty reliance is grounded on the definition of a warranty, which is “a promise to indemnify the promisee for any loss if the fact warranted proves untrue, for obviously the promisor cannot control what is already in the past.” *Metropolitan Coal Co. v Howard*, 155 F2d 780, 784 (2d Cir 1956) (Hand, J).

There are good policy reasons for the original rule that fraudulent inducement duplicates breach of warranty, unless it involves representations outside the contract. Permitting fraudulent inducement claims to go forward for breach of contractual warranty breeds uncertainty in contracting. In a fraud case, instead of recovering damages for breach of the warranty, the plaintiff has the potential remedies of rescission or rescissory damages, which undoes the contract. Fraudulent inducement claims also raise the cost and complexity of garden variety breach of contract actions. Whether or not reliance was justifiable under the circumstances is a complex factual issue that significantly widens the scope of discovery and trial. On the other hand, damages for breach of warranty are clearly contemplated by the parties and promote the reasonable expectations of the contracting parties. The litigation is simpler and less costly. The plaintiff still has a remedy.

**Present Intention Not to Perform**

There have been many conflicting New York decisions on whether a fraud claim can be based on a contractual promise made with present intention not to perform the contract. As noted in one federal decision:

There have been a number of conflicting rulings as to whether, under New York law, an allegation that a contracting party never intended to perform its obligations sets forth a cognizable claim in fraud. In the recent case of *New York University v. Continental Insurance Co.*, No. 302, 1995 N.Y. LEXIS 4752, 1995 WL 761955 (N.Y., December 27, 1995), the New York Court of Appeals stated that “general allegations that [a] defendant entered into a contract while lacking
the intent to perform it are insufficient to support the claim” of fraud. *Id.* at *12. Yet in *Sabo v. Delman*, 3 N.Y.2d 155, 164 N.Y.S.2d 714, 143 N.E.2d 906 (1957), the Court of Appeals had clearly held to the contrary, finding that “a contractual promise made with the undisclosed intention not to perform it constitutes fraud . . . .” *Id.* at 162. In the years between these two holdings, New York law has come to focus on the rather elusive concept of whether a misrepresentation is one of “present fact” or “future intent.” See *Deerfield Communications Corp. v. Chesebrough-Ponds, Inc.*, 68 N.Y.2d 954, 956, 510 N.Y.S.2d 88, 502 N.E.2d 1003 (1986) (holding that misrepresentation of present fact collateral to contract gives rise to an action for fraud, while misrepresentation of future intent does not); *Citibank, N.A. v. Plapinger*, 66 N.Y.2d 90, 94, 495 N.Y.S.2d 309, 485 N.E.2d 974 (1985) (finding misrepresentation as to present fact is not subject to summary judgment).


The result of permitting fraud claims for present intention not to perform creates myriad problems. Intention is a fact that must be inferred from the circumstances. Where a party has breached, it is always possible to infer that the party did not intend to perform. The fraud claim almost always survives a motion to dismiss. In this way, every breach of contract is a potential fraud, with expansive discovery and potential rescission. This undermines commercial certainty.