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Reporting on Significant Court of Appeals Opinions and Developments in New York Practice

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CASE LAW DEVELOPMENTS

Court of Appeals Holds that CPLR 203(f) Relation Back Doctrine Did Not Apply to New Reformation Claim

Finds That Original Complaint Asserted Allegations Concerning Breach of Contract Claim Only

CPLR 203(f) provides that a claim in an amended pleading is deemed to be interposed at the time the claims in the original pleading were interposed, so long as the original pleading gave notice of the transactions or occurrences to be proved in the amended pleading. Thus, a linchpin of the relation back doctrine is that proper notice be given.

The issue in *34–06 73, LLC v. Seneca Insurance Co.*, 2022 N.Y. Slip Op. 06029 (Oct. 27, 2022), was whether plaintiffs' original complaint, asserting a breach of contract claim, provided adequate notice supporting an untimely reformation claim based on mutual mistake and a preexisting oral agreement. In this case, the plaintiffs sought at trial to amend the complaint to conform the pleadings to the proof to add the reformation claim. A unanimous Court of Appeals concluded that the original pleadings did not give the requisite notice and reversed the lower court orders.

The Court criticized the lower courts for looking beyond the four corners of the complaint

> to determine whether defendant was on notice of transactions or occurrences underlying plaintiffs' reformation claim. Section 203 (f) requires the court to determine solely whether a plaintiff's or a defendant's original pleading gives notice of the transactions or occurrences underlying the proposed amendment (see CPLR 203 [f]). Whether the same trial evidence supports both the breach of contract and reformation claims or whether defendant here failed to produce the underwriting file in a timely fashion are irrelevant to the notice issue. Similarly, matters unearthed during discovery have no bearing on whether an untimely claim relates back under section 203 (f).

Id at *8–9.

Significantly, the Court distinguished between the pleading requirements for a reformation and a breach of contract claim. With respect to the former, the plaintiff is required to allege "sufficient facts supporting a claim of mutual mistake, meaning that 'the parties have reached an oral agreement and, unknown to either, the signed writing does not express that agreement' (citation omitted)." *Id* at *10. By contrast, a plaintiff asserting a breach of contract claim generally must allege that a contract exists, the plaintiff performed the contract, and the defendant breached it.

In ruling that the complaint here did not provide such notice, the Court noted that the original complaint referenced a specific written policy "which they identified as the parties' agreement and which they allege defendant breached." The Court found fatal (to the notice requirement) the allegation that the plaintiffs had complied "with all of the conditions precedent and subsequent pursuant to the terms of the subject policy." The court reasoned that by alleging total compliance "plaintiffs necessarily disclaimed any challenge to the policy's terms, . . ." *Id.* at *11.

In addition, the breach of contract claim provided no notice that there was a prior oral agreement

> that preceded the contract's formation, whereas the breach of contract claim in the original complaint was based on the written policy which includes the PSE [Protective Safeguards Endorsement] and with which plaintiffs alleged full compliance. Critically, nothing in the stand-alone breach of contract claim put defendant on notice that there was a prior oral agreement that excluded the PSE and that the PSE's inclusion in the written policy was a mistake.

Id. at *12.

IN THIS ISSUE

The Court maintained that generally the transactions and occurrences with respect to a breach of contract claim do *not* necessarily give the requisite CPLR 203(f) notice supporting a reformation claim based on mutual mistake and vice versa. While the Court acknowledged that there can be cases where such notice is provided, that was not the case here, where "[t]he complaint contained no alternate theory of recovery or factual allegations based on pre-formation transactions or occurrences." *Id*. at *13.

Parties United in Interest

Another Application of the Relation Back Doctrine

Another form of the relation back doctrine involves parties "united in interest." Thus, a claim asserted against a defendant in an amended pleading will relate back to claims previously asserted against a co-defendant if all three of the following conditions are met:

> 1. Both of the claims must arise out of the same conduct, transaction, or occurrence;
>
> 2. Both parties must be united in interest such that the co-defendant can be charged with notice of the institution of the action and will not be prejudiced thereby; and
>
> 3. The co-defendant must have known, or should have known, that but for plaintiff's mistake, the co-defendant would have been included in the original pleadings.

See CPLR 203(b), (c); *Buran v. Coupal*, 87 N.Y.2d 173 (1995).

In Ellis v. Newmark & Co. Real Estate, Inc., 2022 N.Y. Slip Op. 05785 (1st Dep't Oct. 18, 2022), a slip-and-fall case, the plaintiff sued the property owner's agent, who had assumed via agreement with the owner (515 Madison) the property management and leasing responsibilities for the property. That same agreement required the owner to defend and indemnify the agent for any injuries on the property, except those caused by defendant's own negligent conduct. Before the end of the five-year term of the agreement, the defendant agent subcontracted out its management and leasing responsibilities to NFP. Those agreements contained reciprocal indemnification provisions between 515 Madison and NFP. A year later, NFP contracted with GFP to become the successor in interest. Note that each of the proposed defendants – 515 Madison, NFP, and GFP – are associated with one family (the Gural family).

The Appellate Division affirmed the trial court's grant for leave to serve the proposed defendants after the expiration of the statute of limitations. With respect to the first condition, the existing defendant did not contest that the claims against the proposed defendants arose out of the same conduct, transaction, or occurrence (that is, the slip and fall). In addition, the unity of interest component was met. The Court noted that the classic test for determining whether there is a unity of interest is "whether the defenses between the parties are the same such that their interests stand or fall together." Where one is vicariously liable to the other, as is the case here, the unity of interest component is satisfied:

> Here, 515 Madison owed a nondelegable duty to maintain its property in a safe condition, and defendant, NFP, and GFP, as agents of 515 Madison, were also obligated to maintain the property in a safe condition. 515 Madison, by operation of law, remained vicariously liable for the negligence of its agents and contractors that caused injury to those who might be on the property. Reciprocal indemnification clauses in the agreements as between defendant and the proposed defendants provide a basis for finding vicarious liability. Plaintiff's evidence as to the indemnification obligations, the common association of the Gural family with each of the entities, and the sharing of offices, supports the motion court's finding that the proposed defendants can be charged with having notice of the institution of this action (citations omitted).

Id. at *3–4.

Finally, the court stated that, with respect to the third condition, a plaintiff is required only to show a mistake for not adding a defendant before the expiration of the limitation period and there is no need to show that the mistake was excusable. That condition was also met here:

> Here, plaintiff demonstrated that information related to the Gural family and their real estate holdings, as well as the various entities associated with such holdings, was confusing and misleading in regard to what entity owned the property. Furthermore, considering the Covid-19 restrictions in place after the suit was filed there is no evidence that plaintiff failed to take prompt action to add the appropriate defendants after being informed of their identity.

Id. at *4–5.

In *Chandler v. New York City Tr. Auth*., 2022 N.Y. Slip Op 05830 (2d Dep't Oct. 19, 2022), however, the Second Department held that the second condition had not been met. Here, plaintiff alleged personal injuries when a bus driver allegedly closed the door on the plaintiff's hand and started to drive away. The plaintiff only sued the New York City Transit Authority (NYCTA), the wrong party, although the plaintiff served timely notices of claim on both the NYCTA and MTA Bus. After the relevant statute of limitations had run, plaintiff sought to add MTA Bus. The court focused on the lack of vicarious liability:

> "Defendants are united in interest only when their interest 'in the subject-matter [of the action] is such that [the defendants] stand or fall together and that judgment against one will similarly affect the other.'" "In a negligence action, 'the defenses available to two defendants will be identical, and thus their interests will be united, only where one is vicariously liable for the acts of the other.'" Here, NYCTA and MTA Bus are separate and distinct entities, and the plaintiff failed to establish that they are united in interest in this case (citations omitted).

Id. at *3–4.

Court Holds Party Not Entitled to Recover Attorneys' Fees Under Broad Indemnification Provision

Finds That Provision Did Not Effect Waiver of "American Rule" Against Successful Party Recovering Attorneys' Fees

Generally, under the American rule, a prevailing party cannot recover attorneys' fees from the losing party. The issue in *Sage Systems, Inc. v. Liss*, 2022 N.Y. Slip Op. 05918 (Oct. 20, 2022), was whether a broad indemnification provision in a partnership agreement effected a waiver of the benefit of the rule. A unanimous Court of Appeals rejected the plaintiff's argument here, holding that the relevant provision lacked "express language or indicia of the parties' 'unmistakably clear' intent to indemnify each other for attorneys' fees in an action between the parties on the contract."

The relevant provision in the partnership agreement stated:

> The Partnership and the other Partners shall be indemnified and held harmless by each Partner from and against any and all claims, demands, liabilities, costs, damages, expenses and causes of action of any nature whatsoever arising out of or incidental to any act performed by a Partner which is not performed in good faith or is not reasonably believed by such Partner to be in the best interests of the Partnership and within the scope of authority conferred upon such Partner under this Agreement, or which arises out of the fraud, bad faith, willful misconduct or negligence of such Partner.

After an unsuccessful partnership dissolution action, the plaintiff here (Sage) brought an action to recover attorneys' fees incurred in defending that action. The trial court concluded that the indemnification agreement applied, the plaintiff was entitled to attorneys' fees, and the prior dissolution action was commenced in bad faith under the relevant provision. The Appellate Division affirmed.

In reversing the Appellate Division order, the Court of Appeals noted that "in the context of private agreements to avoid the Rule, courts have had to determine the intent of vague fee-shifting language and broad indemnification provisions that do not explicitly allow for the prevailing party in an action between contracting parties to collect attorney's fees (citations omitted)." *Id* at *3–4. The Court cautioned that some of the decisions in this area that presumed "that broadly worded indemnification provisions by their nature are intended to cover attorney's fees in direct party actions, . . . deviate from this Court's exacting standard that the agreement must contain 'unmistakably clear' language of the parties' intent to encompass such actions." *Id.* at *4.

In this action, the Court concluded that there was nothing in the agreement that made "unmistakably clear" that attorneys' fees were recoverable in an action between the partners on the contract. The indemnification provision neither explicitly nor implicitly permitted the parties to recover attorneys' fees in a contract action. It broadly applied to all types of actions, was not limited to actions between the partners but instead included actions involving third parties, and the only limitation provided was that the partner had to have committed some misconduct.

The Court suggested that if parties wished to deviate from the American rule, they "must determine how best to articulate their agreement to ensure their intentions are clear. However, inclusion of clear language stating that the prevailing party is entitled to recover attorney's fees in an action between the parties would avoid potential litigation on the issue." *Id.* at *7. Simply stated, if you want something, say something.

Court Upholds Amended Regulation Providing That Financial Professionals Must Act in "Best Interest" of Their Clients

Rules that Petitioners Failed to Sustain Burden to Establish Facial Due Process Challenge

In *Matter of Independent Ins. Agents & Brokers of N.Y., Inc. v. New York State Dept. of Fin. Servs.*, 2022 N.Y. Slip Op. 05917 (Oct. 20, 2022), the petitioners were challenging a recently amended regulation, promulgated by the Department of Financial Services (DFS), titled Suitability and Best Interests in Life Insurance and Annuity Transactions. The regulation adopted a uniform standard of care that must be met by agents and brokers: that all financial professionals who provide retirement planning and investment advice, both insurers and brokers dealing with annuities and life insurance, must act in the "best interest" of their clients. It applies to any transaction or recommendation concerning a proposed or in-force policy. The best interest standard requires producers to exercise "care, skill, prudence and diligence," and to consider "suitability information" for consumers, nine factors for life insurance sales, and 14 for annuity contracts.

The primary objections advanced by petitioners were that the amended regulation was unconstitutionally vague "because certain key terms, including 'best interest,' 'recommendation,' and 'suitability information,' are indefinite, ambiguous, and subjective, and thus, incapable of satisfying the test for constitutional vagueness"; "DFS exceeded its authority in promulgating the amendment because it purportedly conflicts with the statutory scheme and the common law, and constitutes improper policymaking"; DFS violated the State Administrative Procedure Act (SAPA); and "the amendment was arbitrary and capricious, unreasonable, and lacked a rational basis." *Id.* at *5–6.

While the trial court granted DFS's motion to dismiss, the Appellate Division reversed, finding that the amended regulation was unconstitutionally vague.

A unanimous Court of Appeals reversed the Appellate Division order. The Court first dealt with the petitioners' facial challenge, noting that the term "recommendation" in the amended regulation has both an objective and subjective meaning:

> The objective definition is a statement or act that "reasonably may be interpreted by a consumer to be advice and that results in a consumer entering into or refraining from entering into a transaction in accordance with that advice." The subjective definition is a statement or act that "is intended by the producer, or an insurer where no producer is involved, to result in a consumer entering into or refraining from entering into a transaction." The regulation also clarifies that "general factual information to consumers, such as advertisements, marketing materials, general education information regarding insurance or other financial products, and general administrative services to the consumer" are not "recommendations" (citations omitted).

Id. at *10–11.

The Court maintained that the "regulation's text shows that DFS carefully considered what communications would and would not be considered 'recommendations' and provided a clear definition employing standard legal terminology." *Id*. at *11. Moreover, the Court has previously ruled that an objective reasonableness standard is suitably definite, perhaps necessary to support a regulation that could otherwise be subjective.

The Court rejected the argument that the term "recommendation" was unconstitutionally vague:

> Employing long-accepted terms, the definition establishes clear, objective legal guidelines to ensure that a communication's legal impact will not depend on the sensitivities of a communication's recipient, and is both sufficiently definite to provide notice to those regulated and to prevent arbitrary enforcement. The result is broad categories of conduct for which the application of the term "recommendation" is clear.

Id. at *12–13.

Similarly, the term "suitability information" was not vague; the term is well-defined, and guidance was provided as to its application. "Read as a whole, the regulation specifies that information that is not in one of the enumerated categories and is not provided by the consumer need not be considered for a producer to comply with the best interest standard (citations omitted)." *Id*. at *14.

Finally, the Court rejected the notion that the term "best interest" was vague since the regulation explicitly advises that the producers must act in the best interest of the consumer, and it uses standard legal terms to elaborate on what a producer has to do to discharge this duty.

The Court also dispensed with petitioners' other arguments for invalidating the amendment, concluding that DFS did not exceed its authority in promulgating the amended regulation, it did not violate the SAPA, and the amended regulation was not arbitrary and capricious. It found, among other things, that DFS did not cross the line into impermissible "legislative policy-making" (applying the Boreali factors); nothing DFS did constituted violations of SAPA; and the "goal of the amendment is straightforward and supported by the administrative record, and the amendment is plainly tailored to achieve those objectives. Ultimately, petitioners' quarrel is with the policy and objectives of the regulation, not with its rationality. DFS reasonably concluded that the 'best interest' framework was needed to protect consumers, and petitioners cannot show that the amended regulation is 'essentially arbitrary.'" *Id*. at *24.

Second Department Concludes That Failure to Effect Service Under CPLR 306-b Did Not Preclude Plaintiff From Seeking Judicial Appointment of a Receiver

Statutory Provisions Permitted Plaintiff to Seek Appointment *Ex Parte*

In the July 2020 edition of the *Law Digest*, we discussed the decision in *State of New York Mortgage Agency v. Braun,* 182 A.D. 3d 63 (2d Dep't 2020). There, a majority of the Second Department ruled that a court can entertain a motion for an extension of time to serve under CPLR 306-b, even after a motion to dismiss is granted, as long as a judgment has yet to be entered. It reasoned that "'[a]n action is deemed pending until there is a final judgment' (citations omitted)." *Id*. at 68.

More recently, in *HSBC Bank USA, N.A. v. Rubin*, 2022 N.Y. Slip Op. 05682 (2d Dep't Oct. 12, 2022), a mortgage foreclosure action, the Second Department dealt with a different fact pattern but harkened back to its decision in *Braun* for guidance. In *HSBC Bank*, the trial court granted the plaintiff an extension of time (an additional 120 days) to serve the defendant. However, the plaintiff ignored the order, did not serve within the extended period, and then waited an additional 15 months before moving again under CPLR 306-b. That motion was denied, but no judgment was entered dismissing the action.

Three months later, the plaintiff moved for the appointment of a temporary receiver for the rents and profits of the mortgaged property. The trial court denied the motion on the ground that "this case was already dismissed." Thus, the trial court never reached the merits of the motion.

The issue here focused on a paragraph in a rider to the mortgage describing a temporary receiver as someone who would be "judicially appointed." Significantly, as noted above, service was never effected and could not be effected anymore on the defendant. However, the Second Department noted that, in this case, the appointment of a temporary receiver could be statutorily sought *ex parte* (see RPAPL 254(10), applicable here). As a result, once the plaintiff commenced this action by filing, the failure to effect service did not prevent the plaintiff from seeking judicial appointment of a receiver. Moreover,

> the existence of an action against at least one defendant provides a predicate for the appointment of a temporary receiver when an appointment is authorized under the terms of the mortgage, even if the mortgagor entitled to the equity of redemption is not named in the action or, by logical extension, named but not served with process under New York's current filing procedures. Here, the action was commenced against the defendant, permitting the Supreme Court to consider the appointment of a temporary receiver on that basis; but even without that basis, the commencement of the action against the codefendants provides the court with an additional predicate under which to consider a temporary receiver's appointment (citations omitted).

Id. at *17.

The court distinguished between personal jurisdiction and notice of an application to a party. In this case, the failure to validly serve the defendant with the summons and complaint did not require the denial of plaintiff's motion for the appointment of the temporary receiver. In addition, the defendant did receive notice of the motion and opposed it on the merits.

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