

New York Commercial Division Round-Up

News & Updates on Cases Decided in the Commercial Division of the New York State Supreme Court

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[Fraud Claim Against Syndicated Lender Allowed To Proceed, Despite Express Disclaimer Of Reliance In Deal Documents](#)

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On May 10, 2010, Justice Barbara R. Kapnick permitted a fraud claim to proceed against a syndicated lender despite the fact that the plaintiffs were sophisticated parties and the loan documents contained express disclaimers of reliance. *See Harbinger Capital Partners Master Fund I Ltd. v. Wachovia Capital Markets LLC*, Index No. 602529/08 (Sup Ct, NY County, May 10, 2010) ("*Harbinger*"). The court held that it was too early in the litigation to determine whether "the true nature of the situation" might place plaintiffs within an exception to the bar on fraud claims that generally occurs where deal documents contain express contractual disclaimers.

Relevant Background

In *Harbinger*, Wachovia Capital Markets ("WCM") had created a loan syndication that plaintiff entered into with respect to Le Nature's, Inc. ("Le Nature") a beverage manufacturer, bottler, and distributor. For the year 2005, Le Nature's reported net sales were over \$275 million. However, a court-appointed custodian later discovered that Le Nature's actual revenues were as little as \$32 million. In its Complaint, plaintiffs alleged that WCM knew of, and attempted to conceal, the dire financial situation of Le Nature, including by attempting to conceal the company's failure to make timely interest payments by covertly fronting Le Nature's payments. Plaintiffs asserted that if WCM had disclosed these material facts to the syndicate lenders, they would not have entered into the syndication agreement.

As a result, plaintiffs asserted a cause of action for fraud, which, under New York law, requires that: (1) WCM made material false representations, (2) with the intent to defraud plaintiffs, (3) upon which the plaintiffs reasonably relied, and (4) as a result of which, plaintiffs suffered damage. In response, WCM argued that plaintiffs' fraud claim was barred because the loan documents contained an express disclaimer of reliance upon representations made by WCM. However, plaintiffs maintained that, under the "peculiar knowledge" exception, they were not precluded from claiming reliance because the facts allegedly misrepresented were peculiarly

within WCM's knowledge. *Harbinger* at 14–15.

In response, WCM argued that the peculiar knowledge exception did not apply because, among other things, plaintiffs had access to Le Nature's books, records, executives, employees and auditors, and New York courts typically find that sophisticated investor-plaintiffs who possess access to vital information cannot successfully establish that they entered into an agreement in justifiable reliance on alleged misrepresentations. *Id.* at 16. WCM cited to *DDJ Management, LLC v. Rhone Group, LLC*, 60 AD3d 421, 424 (1st Dep't 2009), in which the Appellate Division reversed the trial court's denial of a motion to dismiss a fraud claim in a strikingly similar fact pattern. However, Justice Kapnick disagreed that *DDJ Management* was dispositive, because whether the plaintiffs' reliance was reasonable is a question of fact, not of law, and because plaintiffs alleged that WCM was not just one of many bankers to Le Nature; it served as Le Nature's "exclusive financial advisor...and investment banker." As such, WCM may have had unusual access to crucial information not readily available to plaintiffs. Justice Kapnick also noted that WCM's unique access to information regarding Le Nature might place plaintiffs within another exception to the bar on fraud claims - the "special facts" doctrine, which dictates that "a duty to disclose arises 'where one party's superior knowledge of essential facts renders a transaction without disclosure inherently unfair.'" *Harbinger* at 19 (citing *P.T. Bank Cent. Asia, N.Y. Branch v. ABN AMRO Bank N.V.*, 301 AD2d 373, 378 (1st Dep't 2003)).

Justice Kapnick noted that while ultimately the evidence may demonstrate that defendants did not have special knowledge which plaintiffs could not have discovered by exercising reasonable diligence, these issues could not be resolved as a matter of law at the current state of litigation. Therefore, lending parties with contracts containing express disclaimers of reliance are still potentially susceptible to having to defend fraud claims, despite explicit disclaimers of reliance, where a plaintiff pleads that the contracting party possesses specialized knowledge or falls within the special facts doctrine.

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