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ALERT

July 2010

RECENT CASE LAW DEVELOPMENTS

As part of Moritt Hock Hamroff & Horowitz LLP's continuing efforts to service its client base, from time to time we provide Alerts as to recent developments in various areas of the law which are of interest to our clients as a whole or to specific segments of our practice. This Alert addresses three recent cases which should be of particular interest to lenders, financial institutions and equipment lessors, but which should also provide guidance to any entity that engages in commercial business transactions.

Limitations on the Enforceability of Contractual Disclaimers of Reliance

Very often, loan documents, equipment lease agreements or commercial contracts, contain provisions which provide that one or both of the parties disclaims having entered into the agreement in reliance on any representation or warranty made by the other. These disclaimers are often set forth in very broad, general language. However, a recent decision by the Commercial Division of the New York Supreme Court, New York County, should serve as a warning that such general disclaimers do not provide the protection that the drafters may have intended.

Harbinger Partners Masterfund I Ltd. v. Wachovia Capital Markets LLC arose from an alleged fraud orchestrated by a beverage manufacturer who ultimately ended up in bankruptcy. For years prior to the bankruptcy, the company issued allegedly false financial statements. Just months prior to the bankruptcy filing, Wachovia syndicated a $285 million loan it made to the manufacturer. The syndicate lenders sued Wachovia, alleging that Wachovia knew, but failed to disclose, amongst other things, that the financial reports were false. Wachovia moved to dismiss based upon a disclaimer of reliance contained in the credit agreement with the syndicate lenders.

In deciding the motion, the court engaged in a thorough discussion of the enforceability of disclaimers under New York law and ultimately decided that the case should not be dismissed at such an early stage.

The court's decision applied a two-pronged approach to the analysis of reliance disclaimers. The first prong of the analysis addresses whether or not the disclaimers are sufficiently specific to cover claims of fraud. Under New York law, general disclaimers of reliance are insufficient to preclude a claim of fraud. In order to preclude a fraud claim, the disclaimer must track the substance of the alleged misrepresentation. On this first prong, the *Harbinger* court found that while the disclaimer did contain general language that would not ordinarily preclude a fraud claim, it also contained a specific disclaimer stating that the syndicate lenders had independently and without reliance on Wachovia, made their own appraisals of the borrower's financial condition. The court found that this specific disclaimer was sufficient to preclude a fraud claim based on false financial reports.

However, the second prong of the analysis requires a determination as to whether or not there were facts within the "peculiar knowledge" of the party seeking to enforce the disclaimer, that the claimant could not have discovered by reasonable due diligence. With respect to this prong, the *Harbinger* court noted that the plaintiffs had alleged that Wachovia had been acting

as the borrower's exclusive financial advisor and investment banker for years, and that in those roles, Wachovia had unusual access to the borrower's financial records, personnel, outside accountants and law firms. Therefore, the court held that, given these allegations, it was too early to dismiss the case based solely on the pleadings, even though the facts may ultimately establish that Wachovia did not have "peculiar knowledge".

Class Action Certified Against Leasing Company

In the latest chapter in the ongoing saga of *Pludeman v. Northern Leasing Systems Inc.*, a New York Appellate Court has affirmed a decision certifying a class of plaintiffs who entered into equipment leases with Northern which allegedly failed to make sufficient disclosure of charges for "loss and damage waivers". While most of the decision focuses on the standards for class certification under New York law, the part which is of particular interest, is the court's analysis as to whether individual issues among the class members will predominate over common issues.

Northern had argued that since the plaintiffs can prevail on their claims only if they establish a valid excuse for failing to read the lease in its entirety and thereby discovering the loss and damage waiver charges, the excuse will be unique to each class member and therefore individual issues will predominate. However, the court rejected this argument. The court acknowledged that absent a valid excuse for failing to read a document, a party who signs a document without reading it is bound to its terms, and therefore, class certification would be inappropriate if the breach of contract claims hinged on individual excuses for failing to read the lease. But the court went on to find that this case could, however, turn on a single issue, *i.e.*, whether the first page of the four page lease could be construed as a complete contract, thereby justifying all of the class members' failure to read the additional three pages, one of which contained the disclosure of the loss and damage waiver charges. The court stated that since the first page of the lease contained all of the basic terms of an agreement, including a space for detailing fees, a merger clause and signature lines, the trial court could determine that the merger clause would preclude the examination of any extrinsic evidence, such as the circumstances regarding each lease's execution, thereby precluding individualized proof.

Implied Covenant of Good Faith in Loan Documents Does Not Require Bank To Restructure Loan

In another case from the Commercial Division in New York County, a trial court recently held that the implied obligation to act in good faith, which is imputed to every contract, does not require a bank to restructure a loan agreement. In *KBS Preferred Holding I LLC v. Petra Fund REIT Corp.*, the lender and borrower had entered into negotiations to restructure the defaulted loan, but the negotiations failed. After being sued by the lender, the borrower asserted as a defense, the lender's failure to negotiate in good faith to restructure the loan. The court rejected that defense, finding that notwithstanding the negotiations, the implied covenant of good faith and fair dealing cannot be construed so broadly as to nullify the express terms of a contract or to create independent contractual rights. Since the lender was not required by the loan documents to attempt to restructure the debt, the failed negotiations could not impose upon the lender any such obligation.

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Moritt Hock Hamroff & Horowitz LLP is a broad based commercial law firm with 42 lawyers and a staff of paralegals. The firm has experience in commercial foreclosure; construction law; corporate, securities & financial services; creditors' rights & bankruptcy; employment & labor law; equipment & vehicle leasing; healthcare law; intellectual property, unfair competition & licensing; litigation; marketing & advertising law; not-for-profit law; real estate law; tax; and trusts & estates.

This Alert was written by Marc L. Hamroff and Robert M. Tils.

Mr. Hamroff, a partner with the firm, heads the firm's financial services practice group which includes, among others, its creditors' rights, bankruptcy and equipment leasing practice areas.

Mr. Tils, a partner with the firm and co-chair of its litigation and bankruptcy practice groups, concentrates his practice in the areas of commercial litigation, creditors' rights and equipment leasing.

Any questions concerning the matters raised in this Alert should be addressed to either Mr. Hamroff or Mr. Tils. They can be reached at (516) 873-2000 or by email at mhamroff@moritthock.com or rtils@moritthock.com

400 Garden City Plaza, Garden City, NY 11530 | Tel (516) 873-2000 | Fax (516) 873-2010
330 Fifth Avenue, Suite 1300, New York, NY 10001 | Tel (212) 239-2000 | www.moritthock.com