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## Decisions of Interest

### *U-5 Notice Statements Privileged, but Claim Proceeds Over Allegations to Potential Employer*

**DEUTSCHE BANK SECURITIES INC. v. KONG, 110536/06,**

Decided 03/18/08

*Justice Marcy S. Friedman*

In this action, plaintiff Deutsche Bank Securities Inc. ("Deutsche Bank") seeks injunctive relief and damages against defendant Topang Kong ("Kong"), an investment banker formerly employed by Deutsche Bank, based on Kong's alleged theft of Deutsche Bank's proprietary and confidential information at the time he terminated his employment. Kong interposed an answer asserting counterclaims against Deutsche Bank and identical third-party claims against Deutsche Bank's officers, third-party defendants Ivan Zeron-Salazar and Justin Kennedy, based on the allegation that Deutsche Bank falsely accused Kong of theft of proprietary information for the sole purpose of preventing Kong from obtaining employment with a competitor. Deutsche Bank and third-party defendants (collectively "Deutsche Bank") move to dismiss Kong's claims.

Although Deutsche Bank does not specify the statute under which it moves to dismiss, it does not purport to seek summary judgment on the merits of the claims but, rather, argues that each of the claims as pleaded fails to state a cause of action. It is well settled that on a motion to dismiss addressed to the face of the pleading, "the pleading is to be afforded a liberal construction (see, CPLR 3026). We accept the facts as alleged in the complaint as true, accord plaintiffs the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal

theory." (Leon v. Martinez, 84 NY2d 83, 87-88 [1994]. See 511 W. 232nd Owners Corp. v. Jennifer Realty Co., 98 NY2d 144 [2002].) However, "the court is not required to accept factual allegations that are plainly contradicted by the documentary evidence or legal conclusions that are unsupported based upon the undisputed facts." (Robinson v. Robinson, 303 AD2d 234, 235 [1st Dept 2003]. See also Water St. Leasehold LLC v. Deloitte & Touche LLP, 19 AD3d 183 [1st Dept 2005], lv denied 6 NY3d 706 [2006].) When documentary evidence under CPLR 3211(a)(1) is considered, "a dismissal is warranted only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law." (Leon v. Martinez, 84 NY2d at 88; Arnav Indus., Inc. Retirement Trust v. Brown, Raysman, Millstein, Felder & Steiner, L.L.P., 96 NY2d 300 [2001].)

As to the first cause of action for fraud, it is further settled that "a cause of action for fraud does not arise when the only alleged fraud relates to a breach of contract." (Metropolitan Transp. Auth. v. Triumph Adv. Prods., Inc., 116 AD2d 526, 527 [1st Dept 1986]; Krantz v. Chateau Stores of Canada Ltd., 256 AD2d 186, 187 [1st Dept 1998]; Rubinberg v. Correia Designs, Ltd., 262 AD2d 474 [2d Dept 1999].) Further, "a contract action cannot be converted to one for fraud merely by alleging that the contracting party did not intend to meet his

contractual obligations." (*Rocanova v. Equitable Life Assur. Soc'y of the United States*, 83 NY2d 603, 614 [1994]; *Hudson v. Greenwich I Assocs.*, 226 AD2d 119 [1st Dept 1996], *lv dismissed* 89 NY2d 860.)

Kong's fraud cause of action alleges that Deutsche Bank made "representations [to Kong] about his past and future compensation at the firm" in order to induce him "to remain at the firm to complete a pending investment banking deal on which he was working." (Answer, 1175-76.) Similarly, Kong's second cause of action for breach of contract alleges that Kong "reached an agreement for his continued employment with [Deutsche Bank], which induced him to remain at the firm while he completed an investment banking deal." (*Id.*, 180.) The fraud cause of action is thus based on Deutsche Bank's alleged intent not to perform the alleged contract for Kong's compensation. Under the above standards, it is duplicative of the breach of contract cause of action and must therefore be dismissed.

The second cause of action for breach of contract alleges that Deutsche Bank breached an agreement both for Kong's continued employment at the firm and for compensation for his "past work" at the firm. (Answer, 1180-82.)

In order to withstand a motion to dismiss, a breach of contract cause of action must "allege, in nonconclusory language \*\*\* the essential terms of the parties' purported contract, including the specific provisions of the contract upon which liability is predicated." (*Matter of Sud v. Sud*, 211 AD2d 423, 424 [1st Dept 1995].)

Kong does not specifically oppose the branch of the motion to dismiss the breach of contract claim for future compensation. Moreover, the allegations of the claim do not set forth with the necessary specificity the essential terms of an agreement for future compensation. In support of the general allegation that Deutsche Bank breached an agreement for future compensation, the pleading alleges that UBS Financial Services, Inc. offered Kong \$300,000 for the remainder of 2006, with a raise of his base salary to \$105,000 (Answer, 1(34), and that third party defendant Kennedy orally agreed to match the UBS offer. (*Id.*, 135.) However, the

pleading further acknowledges that Kennedy "was supposed to follow up with a formal offer in writing (*id.*, 135), and that Kennedy ultimately returned with an offer that came close to the UBS offer but did not match it. (*Id.*, 136.) As to Kennedy's offer, the pleading states merely that Kennedy "offered additional monies in 2007," and that Kong believed he had reached a firm commitment with Deutsche Bank "under terms for his compensation that were acceptable to him." (Answer, 136.) These allegations, lacking in any details as to the amount of money actually offered or the other terms of the agreement, are insufficient to plead a claim for breach of a contract for future compensation.

The court reaches a different result as to Kong's claim for past compensation. The pleading alleges that in July 2005, at the end of his first full year, he received a bonus that exceeded his salary, and that he was scheduled to have a meeting in July 2006 about his bonus compensation for the prior year, (Answer, 1123, 25.) These allegations as to the parties' course of conduct are sufficient to support a cause of action for a bonus for the past year's work based on an "implied promise"<sup>3</sup> that annual bonus payments constituted a part of Kong's compensation. (See *Mirchel v. RMJ Sees. Corp.*, 205 AD2d 388;<sup>1</sup> 390 [1st Dept 1994].) Contrary to Deutsche Bank's contention this claim is not barred by the fact that Kong was an at will employee. (See *id.*)

Kong's third cause of action alleges that Deutsche Bank's instant lawsuit and its motion in the lawsuit for a preliminary injunction constitute an abuse of process. This claim is not maintainable as a matter of law. It is well settled that "the institution of a civil action by summons and complaint is not legally considered process capable of being abused." (*Curiano v. Suozzi*, 63 NY2d 113, 116 [1984].) The motion for a preliminary injunction also may not serve as a predicate for this cause of action under these circumstances in which Kong consented to the preliminary injunction.

The fourth cause of action for defamation alleges that Deutsche Bank made defamatory statements in a Uniform Termination Notice (Form U-5), a required filing with the National Association of Securities Dealers, that Kong was "under internal review" for "fraud or

the wrongful taking of property" at the time of his termination, and that Deutsche Bank "has undertaken an internal review of the unauthorized possession of [Deutsche Bank] proprietary information and its possible transfer to a third party by Topang Kong." (Answer, 1158, 59.) This cause of action also alleges that Deutsche Bank made similar defamatory allegations in this lawsuit, as well as to UBS, a potential employer of Kong, and to professional recruiters in the securities industry.

As held by the Court of Appeals, statements in a Form U-5 are protected by an absolute privilege. (*Rosenberg v. MetLife, Inc.*, 8 NY3d 359 [2007].) To the extent that Kong seeks damages for defamation based on the statements in the Form U-5, the claim is therefore barred. (See *id.*) However, as the Court of Appeals also noted, "registered employees who are maliciously defamed on a Form U-5 are not wholly without remedy as they may commence an arbitration proceeding or court action to expunge any alleged defamatory language." (*Id.* at 368.) As Kong's pleading seeks not only damages but an order expunging defamatory statements on the Form U-5, the latter claim is maintainable.

To the extent that Kong's defamation claim is based on statements in this lawsuit, the claim is also barred. Statements in a judicial proceeding are also subject to an absolute privilege so long as they are, as indisputably appears from the face of the instant pleading, "material and pertinent to the questions involved." (See *id.* at 365.)

To the extent that Kong's defamation claim is based on statements to UBS as a prospective employer or to recruiters, the complaint is sufficiently pleaded to withstand dismissal at this juncture. "A qualified privilege exists for the purpose of permitting a prior employer to give a prospective employer honest information as to the character of a former employee even though such information may prove ultimately to be inaccurate." (*DeSapio v. Kohlmeyer*, 52 AD2d 780, 781 [1st Dept 1976]. *Accord Serratore v. American Port Servs.*, 293 AD2d 464 [2d Dept 2002].) As Deutsche Bank acknowledges, a qualified privilege "cannot shelter statements published with malice or with knowledge of their falsity or reckless disregard

as to their truth or falsity." (*Loughry v. Lincoln First Bank, N.A.*, 67 NY2d 369, 376 [1986].)

Deutsche Bank argues that Kong cannot meet his burden, in order to overcome the qualified privilege, of demonstrating that the statements were made with actual malice. (See Deutsche Bank's Memo. Of Law In Support at 17.) This argument, however, misperceives Kong's burden on this motion. While he will have the ultimate burden at trial of demonstrating malice (see *DeSapio*, 52 AD2d at 781), "on a motion to dismiss, a plaintiff is not obligated to show evidentiary facts to support [the plaintiff's] allegations of malice." (*Pezhman v. Cjfr of New York*, 28 AD3d 164, 169 [1st Dept 2006]. See generally *Matherson v. Marchello*, 100 AD2d 233, 238-239 [2d Dept 1984] ["[T]here is no requirement that the plaintiff establish an evidentiary basis for the allegations of the complaint on a motion to dismiss made pursuant to CPLR 3211."].)

Deutsche Bank also appears to argue that the cause of action is without merit on undisputed facts. It thus asserts that its statements "were made for the purpose of protecting Deutsche Bank's trade secrets, not with malicious intent," and that Deutsche Bank did not commit a tort because it merely communicated comments in the public record. However, this assertion is made by Deutsche Bank's attorney and is without probative value. (See Deutsche Bank's Memo. Of Law In Support at 17.)

On this record, the court also rejects Deutsche Bank's argument that the Form U-4 that Kong signed at the commencement of his employment with Deutsche Bank released Deutsche Bank from any liability for furnishing information, including information in the Form U-5, to prospective employers. The language in the Form U-5 that Deutsche Bank quotes in its brief (see Memo. Of Law In Support at 18) is different than that of the U-4 annexed to the moving papers. Moreover, Deutsche Bank fails to discuss the applicable legal authority on whether such language should be construed as a bar to defamation claims.

The court is unpersuaded by Deutsche Bank's further argument that the allegations of the defamation claim are conclusory or insufficient to support an inference that the

statements were made with actual malice. Kong's claim pleads not merely the general allegation that Deutsche Bank's accusations that Kong stole its confidential information were intentionally made to harm Kong and prevent him from going to work for a competitor (Answer, 155), but also more specific allegations, among others, that he had the "express authorization" of his supervisor to email files to his home (*id.* 141), and that Deutsche Bank knew of these transfers weeks before his resignation and only "manufactured" the claims of theft and misappropriation "after Kong had resigned and was headed to a competitor." (*Id.*, 1115.3, 54.) The claim also alleges that Deutsche Bank accused him of theft of models that could not possibly have been stolen. (*Id.*, 147.) The court finds that these allegations are sufficient to support an inference of malice. (See *Hanlin v. Sternlicht*, 6 AD3d 334 [1st Dept 2004], rearg denied\_ AD3d \_\_, 2004 NY App Div Lexis 9434; *Sborgi v. Green*, 281 AD2d 230 [1st Dept 2001].)

In any event, as Kong correctly argues, the defamation claim should withstand dismissal pending discovery because facts necessary to plead with greater specificity are within the defendant's exclusive knowledge. (See CPLR3211[d].) Here, Deutsche Bank's knowledge of the truth or falsity of its statements at the time they were made to UBS or recruiters is within Deutsche Bank's exclusive knowledge.

Kong's fifth and sixth claims for tortious interference with business relations and prima facie tort are based on the same allegations as, and are therefore duplicative of, the defamation claim. (See *Ramsay v. Mary Imogene Bassett Hosp.*, 113 AD3d 149 [3d Dept 1985], *lv* dismissed 67 NY2d 608 [1986].) These claims will accordingly be dismissed.

Kong's seventh claim for unjust enrichment is based on Kong's development of financial models for structuring collateralized debt obligation deals, as well as an allegation that, "[t]o the extent no agreement existed, Kong is entitled to compensation \*\*\* for the reasonable value of the services he rendered. (Answer, 11111, 114.) Kong does not dispute that paragraph 4 of his written employment

agreement expressly required him to assign his interest in any inventions to Deutsche Bank. As Kong also does not dispute that this agreement applied to financial models and that the agreement is enforceable, the unjust enrichment claim may not be based on Kong's development of such models. The claim is maintainable only based on Kong's allegation that he was entitled to a bonus for work during the year 2005.

Kong pleads no allegations to support liability against the individual defendants for any of the claims other than the defamation claim. All other claim will therefore be dismissed.

It is hereby ORDERED that the motion of plaintiff Deutsche Bank Securities Inc. and of third-party defendants Zeron-Salazar and Kennedy to dismiss is hereby granted to the following extent: 1) Kong's first counterclaim and third-party claim (fraud) is dismissed in its entirety; and 2) Kong's second counterclaim and third-party claim (breach of contract and implied contract) is maintainable against Deutsche Bank only and only to the extent it is based on an alleged oral agreement to pay Kong a bonus for 2005; and 3) Kong's third counterclaim and third-party claim (abuse of process) is dismissed in its entirety; and 4) Kong's fourth counterclaim and third-party claim (defamation) is dismissed to the extent it seeks damages based on statements in the Form U-5 or on statements made in the instant action, and is otherwise maintainable against Deutsche Bank and third-party defendants; and 5) Kong's fifth counterclaim and third-party claim (tortious interference with business relations) is dismissed in its entirety; and 6) Kong's sixth counterclaim and third-party claim (prima facie tort) is dismissed in its entirety; and 7) Kong's seventh counterclaim and third-party claim (unjust enrichment and quantum meruit) is maintainable against Deutsche Bank only and only to the extent it is based on a claim for a bonus for the year 2005.

This constitutes the decision and order of the court.

The parties shall appear in Part 57 of this Court on April 17, 2008 at 2:30 p.m. for a compliance conference.