

Fragin v First Funds Holdings LLC
2016 NY Slip Op 31537(U)
August 11, 2016
Supreme Court, New York County
Docket Number: 652673/2014
Judge: Eileen Bransten
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART THREE

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GARY FRAGIN,

Plaintiff,

-against-

Index No. 652673/2014

Motion Date: 7/22/2016

Motion Seq. No. 002

FIRST FUNDS HOLDINGS LLC f/k/a FIRST FUNDS
LLC, PRINCIPIS CAPITAL LLC f/k/a FIRST FUNDS
LLC f/k/a FF 2008 LLC, NORTHERN LEASING
SYSTEMS, INC., ECONOMIC GROWTH GROUP
INC., LEONARD MEZEI, and MOSES & SINGER
LLP,

Defendants.
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BRANSTEN, J.

This matter comes before the Court on Plaintiff Gary Fragin's motion to compel the production of documents and testimony from Defendant Moses & Singer LLP ("Moses & Singer"). Moses & Singer has refused to produce certain documents or to allow two of its attorneys to answer certain deposition questions, asserting the attorney-client privilege and work product protection. Through the instant motion, Fragin contends that the crime-fraud exception applies, rendering the privilege and protection unavailable and the documents and testimony subject to disclosure. The Court has allowed Moses & Singer to select a representative sample of documents from the approximately one hundred at issue.¹ After reviewing the representative sample, the

¹ The disputed documents are each marked on Moses & Singer's privilege log with an asterisk. The Court asked counsel during oral argument to identify the number of disputed documents on

Court concludes that the crime-fraud exception applies to each documents presented for *in camera* review and Moses & Singer is directed to apply the Court's reasoning herein as to the representative sample to produce those withheld documents and testimony that fall within the ambit of the crime-fraud exception.

I. **Background**

This is a fraud and breach of contract action brought by Plaintiff Gary Fragin against his investment advisor, Leonard Mezei, and Mezei's legal counsel, Moses & Singer LLP. Fragin also asserts claims against certain entities allegedly controlled by Mezei.

The instant litigation stems from Fragin's \$1.2 million investment in assets held by one of Defendant Mezei's companies, non-party Chilmark LLC. Mezei reportedly regretted the investment almost immediately and asked Fragin for his money back. To forestall litigation by Fragin, Mezei agreed in 2009 to have another Mezei-controlled entity, Defendant First Funds Holdings LLC ("FFH"), purchase the assets in Fragin's account in exchange for a \$1.42 million promissory note, as well as a payment guaranty from one of Mezei's other companies – Defendants Northern Leasing Systems, Inc.

the privilege log. Neither counsel could answer; however, Plaintiff's counsel guessed that about a hundred documents were at issue. *See* 6/1/16 Oral Arg. Tr. at 10:5.

and/or Economic Growth Group. The promissory note was due on September 12, 2011, and neither FFH nor the guarantors have made any payments.

Fragin maintains that Defendant FFH is a shell company that fraudulently conveyed its assets to other Mezei-controlled entities, including Defendant Principis Capital, to render itself insolvent in the weeks before the promissory note was issued. Specific to the instant motion to compel, Plaintiff asserts that Moses & Singer advised Fragin on the fraudulent transfer of FFH assets to Principis, and therefore, knew of, and assisted in Fragin's wrongful conduct.

A. *First Funds LLC's Disputes with Fortress & New World*

First Funds LLC, like other businesses owned and controlled by Defendant Mezei and his business partner, non-party Jay Cohen, was a Moses & Singer client. *See Hyland Affirm. Ex. A at 29:11-16; id. Ex. B at 37:8-14.* First Funds LLC allegedly owed tens of millions of dollars to its two major lenders – non-parties New World Equipment Funding LLC (“New World”) and Fortress Credit Corporation (“Fortress”). *See Hyland Affirm. Ex. P at M&S_413665-66.* In November 2008, Moses & Singer attorneys began work on a potential transfer of First Funds LLC's assets, following a discussion between Moses & Singer attorney Arnold Bressler and Mezei's business partner, Jay Cohen, regarding the New World “situation.” *Id. Ex. I at M&S_413878.* Moses & Singer time records from

around this time also reflect work by the firm on First Funds LLC's dispute with Fortress.

Id. Ex. I at M&S_413881-86 & Ex. Q at ¶¶ 58-65.

Concurrent with his work on the asset transfer, attorney Bressler met with a colleague at Moses & Singer to discuss whether the potential transfer of assets from First Funds LLC to a new company would constitute a fraudulent transfer. *See Hyland Affirm.* Ex. A at 64:6-65:19. Bressler testified in his deposition that this colleague – a bankruptcy and creditor's rights lawyer – advised him that such a transfer would not be deemed fraudulent. *Id.* at 65:16-19.

B. Drafting of the Asset Purchase Agreement and the Name Changes

Thus, on November 25, 2008, Moses & Singer attorneys began drafting the Asset Purchase Agreement ("APA") that would govern the sale of assets from First Funds LLC to FF 2008 LLC – later renamed Defendant Principis Capital LLC ("Principis") – which was formed expressly for this purpose. *See Hyland Affirm.* Ex. I at M&S_413862, M&S_413869; *id.* Ex. K. As explained by Moses & Singer attorney Wai Chen, who was principally responsible for drafting the APA, the goal of the agreement was to transfer the business of First Funds LLC's business to Principis and for Principis then to run that business. *See Hyland Aff.* Ex. B at 142:19-24.

The APA was executed as of May 1, 2009. Two provisions of the APA are relevant to the instant motion: (1) Section 1.01 provides for sale of all of First Funds

LLC's assets to FF 2008, including but not limited to the name "First Funds LLC"; and (2) Section 4.04 requires that First Funds LLC change its name to "First Funds Holdings LLC" (FFH) and that all necessary papers be filed so that FF 2008 LLC can assume the name "First Funds LLC." *See* Hyland Affirm. Ex. D. Shortly thereafter, M&S filed documents to swap the names of the seller and buyer – i.e. to change names of "First Funds LLC" to FFH and FF 2008 to "First Funds LLC." *See* Hyland Affirm. Ex. G & H. "First Funds LLC" later changed its name to Principis Capital LLC because the "First Funds" name had a "negative connotation in the market." *See* Hyland Ex. E at 272:13-18. Even Defendant Mezei struggled to keep the names straight. *See* Hyland Affirm. Ex. C at 190:22-24 ("I would need a chart myself to keep track of some of these name changes.").

C. *Fragin's Investment*

Notwithstanding the transfer of FFH's assets to Principis, Defendant FFH granted a \$1.4 million promissory note to Plaintiff Fragin, dated as of July 12, 2009. *See* Hyland Affirm. Ex. V. In addition to the promissory note, Mezei issued a guarantee. This guarantee was contained in a September 17, 2009 memorandum, sent to several individuals, including attorney Bressler. In the memorandum, Mezei stated that, in the event of his death or incapacitation, the promissory note to Fragin "survives" and that

“Jay [Cohen] or other heirs would honor our arrangement.” *Id.* Ex. Y. This memorandum was sent by email to Fragin. *Id.*

Neither Mezei nor the guarantors have made any payments due under the promissory note.

D. *The Instant Dispute*

Fragin now seeks documents and testimony reflecting communications between the Defendants relating to (1) the transfer of assets from FFH to Principis and (2) the 2009 transaction between Fragin and Mezei and/or the entities controlled by Mezei. Defendant Moses & Singer has refused to produce certain documents relating to these requests on the basis of attorney-client privilege. The withheld documents currently consist primarily of e-mail communications and draft agreements exchanged between Moses & Singer and representatives of FFH and/or Principis between January and December 2009. *See* Hyland Affirm. Ex. BB (Moses & Singer privilege log). In addition, Plaintiff seeks to compel attorneys Bressler and Chan to respond to deposition questions regarding the asset transfer, as well as the promissory note and guaranty.

Fragin does not argue that the attorney-client privilege itself is misapplied. Instead, Fragin maintains that the crime-fraud exception negates the privilege. During oral argument on the motion, the Court determined that Plaintiff made a sufficient factual showing “to support a good faith belief by a reasonable person that *in camera* review of

the materials may reveal evidence to establish the claim that the crime-fraud exception applies.” See 6/1/16 Oral Arg. Tr. at 8:24-9:2 (quoting *In re N.Y. City Asbestos Litig.*, 109 A.D.3d 7, 11 (1st Dep’t 2013)). Accordingly, the Court ordered an *in camera* review. Given the length of the privilege log and counsel’s representation that about a hundred documents were in dispute, the Court gave Moses & Singer the opportunity to select a representative sample of documents for the Court to review. This representative sample was intended by the Court to provide the guidance necessary for the parties to resolve their dispute regarding the scope of the privilege and its applicability to the remainder of the documents and testimony.

II. Discussion

The central issue on this motion is whether the documents that Moses and Singer seeks to shield under the attorney-client privilege are nonetheless discoverable pursuant to the crime-fraud exception. The crime-fraud exception encompasses “a fraudulent scheme, an alleged breach of fiduciary duty or an accusation of some other wrongful conduct.” *In re N.Y. City Asbestos Litig.*, 109 A.D.3d 7, 10 (1st Dep’t 2013). A party seeking to invoke the crime-fraud exception must demonstrate that there is a factual basis for a showing of probable cause to believe: (1) that a fraud or crime has been committed and (2) that the communications in question were in furtherance of the fraud or crime. *Id.* Fragin has made this requisite two-part showing.

A. *Commission of a Fraud*

Fragin has demonstrated facts adequate to support a conclusion by probable cause that the asset transfer between FFH and Principis,² executed around the time of Fragin's investment, was a fraudulent conveyance under DCL § 276. Section 276 provides that "[e]very conveyance made and every obligation incurred with actual intent ...to hinder, delay, or defraud either present or future creditors, is fraudulent as to both present and future creditors." To establish a Section 276 claim, plaintiff may rely on "badges of fraud," which are "circumstances so commonly associated with fraudulent transfers that their presence gives rise to an inference of intent." *Wall St. Assoc. v. Brodsky*, 257 A.D.2d 526, 529 (1st Dep't 1999). "Badges of fraud" include "a close relationship between the parties to the alleged fraudulent transaction," "inadequacy of the consideration," "the transferor's knowledge of the creditor's claim and the inability to pay it," and "retention of control of the property by the transferor after the conveyance." *Id.* Those badges are demonstrated sufficiently here.

Through the APA, FFH – an entity controlled by Mezei and Jay Cohen – transferred its assets to Principis – also controlled by Mezei and Cohen. Moses & Singer attorneys advised both sides of the transaction, with Chan receiving instructions from

² As noted above, the asset transfer was between First Funds LLC and FF 2008 LLC; however, to avoid confusion with regard to the name changes, the Court here will refer to these entities by the names they ultimately assumed – FFH and Principis.

Cohen on behalf of FFH and from Mezei on behalf of Principis. *See* Hyland Affirm. Ex. B at 101:8-20. The close relationship between the transacting parties and the fact that Mezei and Cohen were left in control of the property after the transfer satisfies two of the “badges of fraud.”

Further, this transfer left FFH almost, if not entirely, without assets in the midst of the New World litigation and the dispute with Fortress. Section 1.01 of the APA rendered FFH without “right, title and interest in and to substantially all of” its assets, including but not limited to its name, goodwill, account receivables, customer lists, customer data, and equipment. *See* Hyland Affirm. Ex. D § 1.01. Moreover, the transfer left FFH with no employees. *See* Hyland Affirm. Ex. C at 218:2-6. As consideration for this transfer, Principis paid no cash for FFH’s assets; instead, it purportedly assumed between \$3.3 and \$3.9 million in debt. *See id.* Ex. N & Ex. O at M&S_408266, 408270, and 408272. Nevertheless, FFH’s debt to its creditors was alleged in the New World litigation – pending at the time of the asset transfer – to be at least several times that amount. *See id.* Ex. U.

Through these facts, Fragin has demonstrated probable cause sufficient to believe that a fraudulent conveyance may have occurred. Accordingly, Fragin satisfied the first element of the crime-fraud exception analysis.

In addition, Fragin has demonstrated by probable cause that he was defrauded when he entered into the promissory note transaction shortly after the asset transfer. To

the extent that FFH was shorn of its assets in May 2009, there is probable cause to believe that the \$1.4 million promissory note accepted by Fragin in September 2009 was induced by fraud.

B. *Communications in Furtherance of the Fraud*

The seventeen documents produced *in camera* for the Court's review likewise contain communications made in furtherance of the alleged fraudulent conveyance and fraud. By this, the Court does not find for the purpose of this motion that Moses & Singer attorneys knowingly participated in Mezei's allegedly fraudulent conduct. Such a showing is not required. *See In re Grand Jury Subpoena Duces Tecum Dated Sept. 15, 2983*, 731 F.2d 1032, 1038 (2d Cir. 1984) ("Such communications are properly excluded from the scope of the privilege even if the attorney is unaware that his advice is sought in furtherance of such an improper purpose."). Instead, the documents demonstrate work by Moses & Singer attorneys at Mezei and Cohen's behest, and on Mezei and Cohen's behalf, in furtherance of the asset transfer, which as addressed above, satisfies the first prong of the crime-fraud exception test. These documents include drafts of the asset purchase agreement, related emails and handwritten notes, as well as communications related to the name swap that occurred as a result of the asset transfer. Accordingly, Fragin has satisfied the second requisite element of the crime-fraud exception.

Since the seventeen documents reviewed by the Court fall within the crime-fraud exception, the Court orders them produced. This decision likewise provides guidance to Moses & Singer for the further production of any withheld documents and testimony reflecting communications between the Defendants relating to (1) the transfer of assets from FFH to Principis and (2) the 2009 transaction between Fragin and Mezei and/or the entities controlled by Mezei. Such documents shall be produced within ten days of entry of this Decision and Order. Moreover, Plaintiff's motion to compel is granted insofar as Moses & Singer objected to deposition questions posed to Chan and Bressler pertaining to these two topics on the basis of attorney-client privilege.

(Order follows on next page.)

III. Conclusion

Accordingly, it is

ORDERED that Plaintiff's motion to compel is granted as to the seventeen documents produced for *in camera* review and as to the deposition questions posed to Chan and Bressler; and is further

ORDERED that Defendant Moses & Singer shall produce the seventeen *in camera* review documents and all documents withheld on the basis of attorney-client privilege that fall within the scope of the Court's instant Decision and Order within ten days of the filing of a Notice of Entry of this Decision and Order.

Dated: New York, New York
August 11, 2016

ENTER

A handwritten signature in black ink, appearing to read "Eileen Bransten", is written over a horizontal line.

Hon. Eileen Bransten, J.S.C.