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**Eric L. Goldberg, Thomas D. Kearns, and Thomas J. Fleming on
Drafting General Releases After Centro: How to Preclude or
Preserve Future Claims of Fraud and Breach of
Fiduciary Duty**

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Court of Appeals Decision in *Centro*. A recent New York Court of Appeals decision highlights the shift in New York law towards the enforceability of general releases even in the context of fiduciaries. In *Centro Empresarial Cempresa, S.A. v. America Movil, S.A.B.*, [2011 NY Slip Op 4720](#), 2011 N.Y. LEXIS 1383 (N.Y. July 7, 2011), the New York Court of Appeals unanimously affirmed the appellate court's dismissal of a \$900 million lawsuit brought by former equity holders of a privately-held telecommunications company, America Movil SAB, on the grounds that a general release entered into by the parties barred the plaintiffs' claims. The Court held that "[a]s sophisticated entities, [the plaintiffs] negotiated and executed an extraordinarily broad release with their eyes wide open. They cannot now invalidate that release by claiming ignorance of the depth of their fiduciary's misconduct." [Id. at 14](#). This decision by New York's highest court underscores the extent to which sophisticated fiduciaries in an arms-length transaction may contract away future fraud claims, even "fraud claims ... unknown at the time of contract." [Id.](#)

Background of *Centro*. Pursuant to a purchase agreement entered into in 2003, the *Centro* plaintiffs sold their membership interests to defendants. Two releases were delivered by the plaintiffs in connection with the sale. In one, the plaintiffs executed the "Release for Agreement Among Members" ("Members Release"), which released defendants, their affiliates, shareholders, and agents from all present and future claims arising under or in connection with the operating agreement "and/or arising out of, based upon, attributable to or resulting from the ownership of membership interests." [Id. at 5](#). The second release, the "Release for Master Agreement" ("Master Release"), released the defendants from claims arising under the parties' master agreement and related documents. This release employed "nearly identical language" to the Members Release, but added a proviso to exclude fraud from the release. In 2008, the plaintiffs commenced an action against the defendants alleging, among other things, breach of fiduciary duty, breach of contract, and fraud. The plaintiffs sought to prove that the "defendants failed to provide them with accurate tax and financial statements ... and were unwilling to negotiate in good faith for a share exchange." [Id. at 6](#).

The *Centro* Court held that "a party that releases a fraud claim may later challenge that release as fraudulently induced only if it can identify a separate fraud from the subject of

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the release.” [Centro, at 10](#) citing *Bellefonte Reinsurance Co. v. Argonaut Ins. Co.*, [757 F.2d 523, 527-528](#) (2d Cir. 1984). Therefore, for a fraud claim to survive the release, the Court required the plaintiffs to demonstrate that fraud, independent from the released fraud, procured the release. The decision reflects the New York court’s view that the finality and certainty of contracted agreements should not be undermined. See *Mangini v. McClurg*, [24 N.Y.2d 556, 563](#) (1969).

Although plaintiffs argued that the fraud exception in the Master Release should be read into the Members Release, the Court found that the plaintiffs’ claims explicitly fell under the Members Release, and the Court should not interpret an agreement as stating something which the parties failed to specifically include. [Centro, at 4](#). Furthermore, the Court emphasized that New York courts should construe releases broadly in the commercial context where “sophisticated” parties are involved and there is a prior history of mistrust between the parties.

Examination of Precedent. The *Centro* Court follows the holding of the First Department in *Global Minerals and Metals Corp. v. Holme*, [35 A.D.3d 93, 99-99](#) (1st Dep’t 2006), which permitted the release of fraud by a fiduciary even though three prior Appellate Division cases held otherwise in similar fact patterns. See *Littman v. Magee*, [54 A.D.3d 14, 17](#), 860 N.Y.S.2d 24 (1st Dep’t 2008), *Blue Chip Emerald LLC v. Allied Partners, Inc.*, [750 N.Y.S.2d 291](#) (1st Dep’t 2002), *Collections v. Kolber*, [256 A.D.2d 240, 241](#), 682 N.Y.S.2d 189 (1st Dept. 1998) In *Global Minerals*, the court held that even if a person makes misrepresentations with intent to defraud, there is no triable issue of fraudulent inducement where “the evidence establishes that its reliance on any such alleged misrepresentation was unreasonable, and that [the opposing party] failed to fulfill its duty to investigate.” [Id.](#)

In *Global Minerals*, the defendant served as a fiduciary to a sophisticated business entity. After the defendant sold his shares back to the company, the releasing party sued the defendant for breach of fiduciary duty, contending that the general release should be vitiated because the fiduciary failed to disclose facts that materially affected the value of the company. Although the defendant owed a fiduciary duty to other shareholders to disclose any information that could reasonably bear on the releasing party’s consideration of the offer, the Court held that “New York law imposes an affirmative duty on sophisticated investors to protect themselves from misrepresentations made during business acquisitions by investigating the details of the transaction.” [Id. at 100](#). See *Abrahami v. UPC Constr. Co.*, [224 A.D.2d 231, 234](#) (N.Y. App. Div. 1996) (holding that a sophisticated business person had a duty to exercise ordinary diligence and conduct an

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LexisNexis® Emerging Issues Analysis

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independent appraisal of the risk he was assuming). Consequently, a sophisticated party must exercise an even greater degree of diligence regardless of the relationship it may have with a fiduciary where the sophisticated party has indications that the fiduciary may have made material misrepresentations or omissions, *i.e.*, where a prior history of mistrust exists. *Id.*

Blue Chip Revisited: Fiduciary Duties and Fraud. *Centro* surprised some observers in light of the recent Appellate Division decisions which prevented a broad application of general releases in the context of an alleged breach of fiduciary duty. See *Littman*, [54 A.D.3d 14 at 17](#), *Blue Chip Emerald LLC*, [750 N.Y.S.2d 291 at 295](#), *Collections*, [256 A.D.2d 240 at 241](#). In *Blue Chip*, the Appellate Division, reversing the lower court's grant of summary judgment, upheld a fraud claim involving the buy-out of a minority partner who alleged that the majority kept secret a third-party offer for the Company's sole asset at a substantially higher price. [750 N.Y.S.2d at 295](#). Similar to the *Centro* court, Justice Cahn writing the majority opinion of the lower court found that the contractual representations, which released all claims for fraud, breach of loyalty and fiduciary duty, were sufficient to defeat the plaintiff's fraud claims. *Blue Chip Emerald LLC v. Allied Partners Inc.*, Index No. 601.415/01 (trial order) (Sup. Ct. N.Y. C'ty September 26, 2001). Nevertheless, despite the existence of a general release and the specific written disclosure in the parties' agreement that the company was selling the property at a substantial profit, the Appellate Division reversed the lower court's decision. Construing the release narrowly, the Court found that a general release did not insulate the fiduciary from allegations of breach of fiduciary duty because "a fiduciary cannot by contract relieve itself of the fiduciary obligation of full disclosure by withholding the very information the beneficiary needs in order to make a reasoned judgment whether to agree to the proposed contract." *Id.*

The *Centro* Court rejected *Blue Chip*, and affirmed the notion that "[a] sophisticated principal is able to release its fiduciary from claims - at least where, as here, the fiduciary relationship is no longer one of unquestioning trust - so long as the principal understands that the fiduciary is acting in its own interest and the release is knowingly entered into." *Centro*, at 13. See *Alleghany Corp v. Kirby*, [333 F.2d 327, 333](#) (2d Cir. 1964) (finding that "there is no prerequisite to the settlement of a fraud case that the (fiduciary) defendant must come forward and confess to all his wrongful acts in connection with the subject matter"). In making its determination, the Court relied on the *Global Minerals* decision.

Like the Court in *Global Minerals*, the *Centro* Court was particularly influenced by the parties' history of dealings which demonstrated that the defendant was not always forth-

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right with information, and yet, the releasing party still entered into the sale and executed the release without any further investigation. Following the *Global Minerals* reasoning, the *Centro* court reiterated that “[w]hen a party to whom a misrepresentation is made has hints of falsity, a heightened degree of diligence is required of it. It cannot reasonably rely on such representations without making the additional inquiry to determine their accuracy.” [Centro, at 16](#) (quoting *Global Minerals*, [35 A.D.3d at 100](#)). As a result, the plaintiffs in *Centro* failed to allege justifiable reliance because “plaintiffs knew that defendants had not supplied them with the financial information necessary to properly value the [property], and that they were entitled to that information.” [Id. at 12-13](#).

Furthermore, the *Centro* Court stated that a sophisticated party, who is represented by counsel, can release a fiduciary from fraud claims, particularly where the release is executed in the course of a transaction where the “fiduciary relationship is no longer one of unquestioning trust.” [Id. at 13](#). As a result of these factors, the Court found that the releasing party entered into the transaction with his eyes wide open to the insufficiency of the financial information that had been provided to him. In turn, the releasing party “willingly assumed the business risk” that he was not in receipt of all the material facts necessary. [Id.](#) See *Global Minerals*, [35 A.D.3d at 100](#). Therefore, because the plaintiffs failed to protect “themselves...they cannot fairly ask for the law’s protection.” [Centro, at 15](#).

Fraudulent Inducement Claims Are Not Barred By General Releases

Under New York law, a valid release constitutes a complete bar to an action on a claim that is the subject of the release. However, “a release is treated just as any other contract...and may be set aside on the traditional basis of fraudulent inducement, misrepresentations, mutual mistake or duress.” *Consortio Prodipe, S.A. de C.V. v. Cinci, S.A.*, [544 F. Supp. 2d 178, 189](#) (S.D.N.Y. 2008). Where a party releases claims, it can later challenge that release for fraudulent inducement only by identifying a separate and distinct fraud from that contemplated by the agreement. [Id.](#); *DIRECTV Group, Inc. v. Darlene Invs., LLC*, [2006 U.S. Dist. LEXIS 69129](#) (S.D.N.Y. Sept. 27, 2006). Furthermore, to state a claim for fraudulent inducement under New York law, “the defendant must have made a misrepresentation of material fact that was known to be false and intended to be relied on when made, and that the plaintiff justifiably relied on the misrepresentation to its injury.” *Amida Capital Management v. Cerberus Capital Management*, [699 F. Supp. 2d 430, 444](#) (S.D.N.Y. 2009); *Nat’l Union Fire Ins. Co. v. Worley*, [690 N.Y.S.2d 57, 61](#) (N.Y. App. Div. 1999).

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The *Centro* Court recognized the broad and encompassing nature of releases when it considered whether a general release precluded, as a matter of law, a claim that a party was fraudulently induced into executing the agreement. [See Centro, at 7-8](#). Justice Catterson, who wrote the dissenting opinion in the *Centro* Appellate Division case (“*Centro II*”), argued that the release was fraudulently induced because the releasing parties did not fully comprehend the depths of the alleged fraud and a fiduciary cannot be released from liability unless he has fully disclosed his tortuous act. *See Centro v. America Movil*, [76 A.D.3d 310, 317](#), 901 N.Y.S.2d 618 (1st Dept. 2010) (Catterson, J., dissenting). However, the Court of Appeals unanimously rejected this argument and resolved the split in the Appellate Division by holding that to assert a claim of fraudulent inducement, the releasing parties must show that the release was itself induced by a separate fraud, outside the scope of the release. [Centro, at 11-14](#); *See Alleghany Corp. v. Kirby*, [333 F.2d 327, 333](#) (2d Cir. 1964); *Bellefonte Re Ins. Co. v. Argonaut Ins. Co.*, [757 F.2d 523, 527](#) (2d Cir. 1985); *Easterbrook Caribe, A.V.V. v. Fresh Del Monte Produce, Inc.*, [11 A.D.3d 296, 297](#) (N.Y. App. Div. 2004).

The Appellate Division in *Blue Chip* found critical the argument that the plaintiff did not have “at its disposal ready and efficient means” for ascertaining whether an offer in the relevant price range even existed. [Id.](#) Whereas in *Centro II*, the Appellate Division found that the plaintiff’s fraudulent inducement claim fell squarely within the scope of the broad release given in the purchase agreement, and that whether or not plaintiffs had reason to suspect defendants misrepresented the value of the company, they cannot “reasonably contend that they did not intend to release possible fraud claims as to that matter of which they were unaware.” *Centro II*, [76 A.D.3d at 317](#). In *Centro II*, the Court stated that because plaintiffs were well aware that the company had a value and nonetheless chose to cash out their interests without investigating the value, they could not make a claim for fraudulent inducement. *Id.* at 321. (It is interesting to note that Justice David Friedman, the author of the majority opinion in *Centro II*, was also a justice on the panel that unanimously decided *Blue Chip*. This shift towards allowing a release of a fraud claim is more reflective of the well-settled principle of New York law that “a valid release constitutes a complete bar to an action on a claim which is the subject of a release.” *Global Minerals*, 35 A.D.3d at 98 (citing *Hack v. United Capital Corp.*, 247 A.D.2d 300, 301 (1st Dept. 1998)).

New York courts have found that sophisticated business people have a heightened responsibility to use available resources to verify the truth of the information upon which they intend to rely. As a matter of law, a sophisticated plaintiff cannot establish that it entered into an arm’s length transaction in justifiable reliance on alleged misrepresenta-

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Eric L. Goldberg, Thomas D. Kearns, and Thomas J. Fleming on

Drafting General Releases After Centro: How to Preclude or Preserve Future Claims of Fraud and Breach of Fiduciary Duty

tions if that plaintiff failed to make use of the means of verification that were available to it. *UST Private Equity Investors Fund v. Salomon Smith Barney*, 288 A.D.2d 87, 88 (1st Dep't 2001). Therefore, in order to sustain a claim for fraud, sophisticated parties "must have discharged their own affirmative duty to exercise ordinary intelligence and conduct an independent appraisal of the risks they are assuming." *DDJ Management, LLC v. Rhone Group, LLC*, 60 A.D.3d 421, 424 (1st Dep't 2009).

In a case decided the same day as *Centro*, the Court of Appeals in *Arfa v Zamir*, 2011 NY Slip Op 4719, 2011 N.Y. LEXIS 1386 (N.Y. June 7, 2011), affirmed the *Centro* opinion and held that the plaintiffs failed to allege that the release was induced by a separate fraud or that they justifiably relied on the fraudulent misstatements in executing the release. Read together, *Centro*, *Centro II*, *Blue Chip* and *Arfa* suggest that fraud claims can be released in the context of a business relationship, but not if the release is itself procured by an independent fraud (*i.e.*, a claim of fraudulent inducement is not waived by a general release). Rather, such claims may be used to invalidate a general release only if the misrepresentations alleged to have induced the signing of the release are separate and distinct from the misrepresentations covered by the release.

Practical Implications

In light of *Centro*, it is now prudent for lawyers to consider an additional set of factors when advising clients whether to give or accept a general release. So long as the release is not procured by fraud, New York courts will enforce broad releases even where they waive fraud and fiduciary duties.

According to the *Centro* court, a release that has broad language, such as the Members Release discussed in *Centro*, can waive fraud if the release contains the phrase "all manner of actions...whatsoever..." in conjunction with the reference to "whether past, present or future" and "contingent" actions. The Court reasoned that together these words indicate an intent to release fraud claims, even if they are unknown at the time of the contract. *Centro*, at 3. Further, the Court emphasized that the absence of the exception for fraud indicated that the Members Release was "not so limited."

Given that parties can contract away fiduciary duties and claims of fraud with releases, it is prudent to include a section of specific disclaimers articulating what a person is waiving in a general release. For example, if a party wishes to ensure that it is not waiving fraud, it should include language that is similar to that of the second release in *Cen-*

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Eric L. Goldberg, Thomas D. Kearns, and Thomas J. Fleming on

Drafting General Releases After Centro: How to Preclude or Preserve Future Claims of Fraud and Breach of Fiduciary Duty

tro, which states, in part, “that the foregoing release shall not release any claims involving fraud.” *Centro*, at 6.

On the other hand, if parties wish to release fraud claims they would be prudent to include the identical language that the *Centro* Court found persuasive. In addition, parties should also consider including other specific disclaimers in the release. A general release could include a statement that a releasing party disclaims any claim for breach of loyalty or fiduciary duty arising out of the relationship with the company. The agreement pursuant to which the release is granted should also recite, where warranted, the sophisticated parties’ nature, and their history of dealings with each other which reveal a breach of trust. The release could also include a provision that the releasing party has performed its own valuation, without reliance on the other party, and assumes all risks of any error in judgment with computation relating to that valuation. Furthermore, the general release could stipulate that the releasing party acknowledges that the other party may sell the company or property for a profit and the releasing party shall have neither any interest in the sale nor any claim relating to it. By including such provisos, contracting parties can more likely ensure that a court will hold that the general release covers what the parties actually intended at the time it was granted.

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Drafting General Releases After Centro: How to Preclude or Preserve Future Claims of Fraud and Breach of Fiduciary Duty

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