

Court of Appeals Revisits the Doctrine of Anticipatory Repudiation

David B. Saxe and Danielle C. Lesser discuss ‘Princes Point v. Muss Dev.’, in which the Court of Appeals found that a prospective purchaser’s commencement of an action seeking to rescind an amendment to a purchase agreement one month prior to the last day to close on the purchase did not constitute an unequivocal communication to the seller of the purchaser’s intention not to perform. The result is a detour into an area of murky jurisprudence that may prove unsettling to the commercial bar that relies on the certainty of precedent and its application in a way that conforms to the realities of commercial practice.

David B. Saxe and Danielle C. Lesser, *New York Law Journal* – January 2, 2018

The ancient and often complex common law doctrine of anticipatory repudiation in the law of contracts has recently bedeviled a series of courts in New York, including our Court of Appeals. In *Princes Point v. Muss Dev.*, No. 92, 2017 N.Y. LEXIS 3139 (N.Y. Oct. 19, 2017), the Court of Appeals addressed a claim of anticipatory repudiation, finding that a prospective purchaser’s commencement of an action seeking to rescind an amendment to a purchase agreement one month prior to the last day to close on the purchase did *not* constitute an unequivocal communication to the seller of the purchaser’s intention not to perform. In doing so, it reversed the Appellate Division, First Department, which upheld the trial court’s finding that the filing of the rescission claim *was* an unequivocal and definite act of anticipatory repudiation. *Princes Point v. Muss Dev.*, 138 A.D.3d 112 (1st Dep’t 2016). Both the Court of Appeals and the Appellate Division grappled with whether the asserted rescission claim was analogous to a declaratory judgment filing, which, under New York law, does not constitute an anticipatory repudiation. Nevertheless, the Court of Appeals did not consider issues that might have produced a different result—one in accord with the determination of the Appellate Division and the trial court. The result the Court of Appeals reached—it is respectfully submitted—is a detour into an area of murky jurisprudence that may prove unsettling to the commercial bar that relies on the certainty of precedent and its application in a way that conforms to the realities of commercial practice.

The issues that the high court might have considered, but did not, were:

- (1) whether the amendment the plaintiff-purchaser sought to rescind was an integral part of an indivisible contract that it attempted to modify or whether it was a severable, stand-alone agreement that could be rescinded, and what was the effect, if any, of the denominated severability clause contained in the original contract;
- (2) whether the plaintiff-purchaser’s failure to seek a preliminary injunction to maintain the status quo at the time of the filing of its action—freezing the parties’ positions until the court could address the enforceability of the amendment to the purchase agreement—evidenced the plaintiff-purchaser’s intent to avoid closing on its purchase.

Factual Background. The Muss family (the defendants-sellers) owned and managed a 23-acre parcel of land in Staten Island known as Princes Point, which had been declared an inactive hazardous waste site. The defendants-sellers remediated the site and obtained its delisting in 2001. Thereafter, the

defendants-sellers began to seek government approvals to develop the property in anticipation of selling it.

In 2004, the plaintiff-purchaser, Princes Point, entered into an agreement with defendants-sellers Allied Princes Bay Co. and Allied Princes Bay Co. #2 to purchase the property for over \$35 million, on an as-is basis, with the plaintiff-purchaser having the unlimited right to conduct any type of testing or investigation of the property it wanted. One of the conditions precedent to closing was the defendants-sellers' delivery of various development approvals by the government. The contract provided for an "outside closing date," which was defined as eighteen months from the execution and delivery of the agreement by the parties. If the defendants-sellers were unable to obtain all the approvals prior to the outside closing date, then either party could terminate the agreement. In the event of a termination, the plaintiff-purchaser would receive a refund of its deposit. Alternatively, the plaintiff-purchaser had the option of waiving the development approvals and closing on the sale without an abatement in the purchase price.

In 2005, the DEC discovered problems with a man-made shoreline called a "revetment," and called for additional work to be done. Due to the anticipated time and cost for this additional work, the defendants-sellers notified the plaintiff-purchaser that they would exercise their right to terminate the contract and return the deposit to the plaintiff-purchaser unless the plaintiff-purchaser agreed to amend the contract.

In 2006, the parties amended the contract to: extend the outside closing date to July 22, 2007, increase the purchase price, increase the down payment, require the plaintiff-purchaser to reimburse the defendants-sellers for 50 percent of the costs related to completing the revetment and obtaining the development approvals, and require the plaintiff-purchaser to forbear from commencing "any legal action" against the defendants-sellers in the event that the approvals were not issued or the revetment work was not completed by the new outside closing date. The amendment made clear that it amended certain terms and incorporated the remaining unchanged terms of the 2004 agreement, making the 2004 agreement and the 2006 amendment one indivisible whole which defined the universe of rights and obligations of the parties.

There were new problems with the revetment and the parties extended the outside closing date on a month-to-month basis. The final date to which the outside closing date was extended was July 22, 2008. The plaintiff-purchaser commenced an action in New York Supreme Court on June 20, 2008, about a month prior to the final outside closing date, alleging it was fraudulently induced into entering into the 2006 amendment by the alleged misrepresentation that the revetment was properly built. The plaintiff-purchaser sought to surgically excise the amendment from the original agreement, seeking the amendment's rescission *only*.

The Trial Court. All of the plaintiff-purchaser's causes of action were dismissed in prior trial court rulings (Ramos, J.). The defendants-sellers moved for partial summary judgment on their first and third counterclaims. The first counterclaim sought a judgment declaring that based on the expiration of the final outside closing date, either the contract was terminated or the plaintiff-purchaser must immediately proceed to closing without an abatement in price. The third counterclaim alleged that by filing the rescission action, the plaintiff-purchaser defaulted on the agreement, entitling defendants-sellers to retain the down payment as liquidated damages.

The Supreme Court granted summary judgment to the defendants-sellers on both counterclaims, determining that: the contract had expired and was terminated by its own terms, plaintiff-purchaser

anticipatorily breached the contract by commencing the action, and the defendants-sellers were entitled to retain the down payment and payments made under the 2006 amendment as liquidated damages. *Princes Point v. AKRF Eng'g, P.C.*, 42 Misc. 3d 1219(A) (Sup. Ct. N.Y. Cty. 2014). The plaintiff-purchaser only appealed summary judgment as to the third counterclaim, bringing the issue of anticipatory repudiation into clear focus. The issue of whether the plaintiff-purchaser anticipatorily repudiated the contract was critical because it could potentially determine whether the nearly \$4 million deposit would be retained by the defendant-seller or returned to the plaintiff-purchaser.

The First Department's Affirmance. The Appellate Division agreed with the trial court, finding that anticipatory repudiation had occurred. Although recognizing that there is no case on point that holds that the commencement of litigation, standing alone, constitutes an anticipatory repudiation, the First Department held that the plaintiff-purchaser anticipatorily breached the contract by commencing the action. *Princes Point*, 138 A.D.3d at 117-18. It explained that “[a]n anticipatory breach, or repudiation, occurs when a party to a contract unequivocally communicates to its counterpart before performance is due, a statement or voluntary affirmative act, that it will avoid performance of its contractual duties.” *Id.* at 116 (citation omitted).

The First Department acknowledged cases holding that “an action seeking a declaratory judgment does not constitute an anticipatory breach” (*id.* at 117, citing *Cato Corp. v. Roaman*, 214 A.D.2d 383 (1st Dep’t 1995)), but distinguished them, explaining that “[a]n action seeking rescission of a contract is markedly different” from an action seeking a declaratory judgment. *Id.* A “plaintiff who succeeds in obtaining rescission can no longer perform; his or her contractual duties will have evaporated. Indeed, by bringing this action for rescission, plaintiff sought to have a court declare the contract void from its inception and to put or restore the parties to *status quo*.” *Id.* (citation and internal quotation marks omitted). The plaintiff-purchaser “did not simply seek to define its rights under the parties’ agreement; it sought to nullify the agreement entirely.” *Id.* at 118.

On appeal, the plaintiff-purchaser argued that this finding was not on point because the plaintiff-purchaser had only sought to rescind the 2006 amendment (which changed the time to perform, the amount of the down payment, and the contract price) and to compel performance of the original 2004 agreement at a lower price.

The Court of Appeals' Reversal. The Court of Appeals reversed the First Department’s decision on the issue of anticipatory breach. The Court of Appeals acknowledged that the issue of whether the commencement of an action for rescission constitutes an anticipatory breach is “unsettled.” *Princes Point*, 2017 N.Y. LEXIS 3139, at *7. In reversing the First Department, the Court of Appeals held that it “cannot conclude that the commencement of this action reflects a repudiation of the contract.” *Id.* The Court of Appeals disagreed with the First Department that an action seeking rescission in this context is “markedly different” from a declaratory judgment action. *Id.* at *7-8. Here, the plaintiff-purchaser’s amended complaint sought, among other things, “reformation of the amendments to the contract and specific performance of the original agreement,” which was not a “positive and unequivocal repudiation.” *Id.* at *8 (internal quotation marks omitted). Although this action and a declaratory judgment action “would produce different results,” “[t]here is no material difference between this action and a declaratory judgment action. At bottom, both actions seek a judicial determination as to the terms of the contract, and the mere act of asking for judicial approval to avoid a performance obligation is not the same as establishing that one will not perform that obligation absent such approval.” *Id.* at *7-8.

Was the 2006 Amendment Separate, Distinct, and Capable of Being Enforced as a Standalone Component, From the 2004 Agreement? Inherent in the Court of Appeals' anticipatory repudiation analysis is that the plaintiff-purchaser could lawfully repudiate just the 2006 amendment, leaving the original 2004 agreement intact and subject to specific performance. But this legal issue was not analyzed by the Court of Appeals and this oversight may have consequences for lawyers who draft and litigate the enforceability of amendments to contracts.

As a general rule, a contract is whole and indivisible when by its terms, nature, and purpose, it reflects that each of its parts is interdependent. On the other hand, a contract is considered severable and divisible when by its terms and purpose, it is susceptible of division and apportionment. *First S&L Ass'n v. Am. Home Assur. Co.*, 29 N.Y.2d 297, 299-300 (1971). The Court of Appeals has held that "[w]hen a contract is separable or divisible into a number of elements or transactions, each of which is so far independent of the others that it might stand or fall by itself, and good cause for rescission exists as to one of such portions, it may be rescinded and the remainder of the contract affirmed." *Ripley v. Int'l Rys. of Cent. Am.*, 8 N.Y.2d 430, 437 (1960); see also *Empire State Bldg. Co. v. N.Y. Skyline*, 432 B.R. 66, 76-80 (Bankr. S.D.N.Y. 2010) (relying on New York law to conclude that an amendment could not be severed from the original lease and rescinded).

Here, the absence of analysis as to whether the 2006 amendment would be severable from the 2004 agreement creates a question as to under what circumstances an amendment might be invalidated and thus subject to the doctrine of anticipatory repudiation. The parties in *Princes Point* agreed to modify the original 2004 agreement in the 2006 amendment, and both documents together contained the totality of terms of the parties' agreement. The 2006 amendment contained the purchase price, how approvals were to be funded, and the time by when performance was to have taken place. The original agreement contained a description of the property being conveyed, provisions relating to obtaining regulatory approvals, the termination provision, a provision related to the down payment, and other important covenants. The plaintiff-purchaser sought to reject certain terms of the integrated agreement to which the plaintiff-purchaser no longer wanted to be bound or which it found to be unpalatable. The Court of Appeals, offering no analysis or discussion as to whether the two agreements, the 2004 contract and the 2006 amendment to it, were so inextricably bound as to negate the possibility of the interpretive division that the court apparently made, focused only on whether the plaintiff-purchaser's intention was to repudiate the entire agreement or just a portion of it. But, there is no legal presumption that an amendment is severable from the agreement it modifies. Without knowing whether only a portion could be legally severed, the opinion provides no guidance as to when or if an amendment may be severed from the agreement it modifies.

In addition to providing no guidance as to the circumstances under which an amendment to a contract may be severed from the agreement it modifies, the Court of Appeals' decision also provided no guidance as to whether seeking to rescind a contract in its entirety—as opposed to merely seeking to rescind an amendment to a contract—would constitute anticipatory repudiation, a point put forward in a recent *New York Law Journal* article. Lynn K. Neuner & William T. Russell Jr., "Court Decides Case Closely Watched by Real Estate Industry," N.Y.L.J., Nov. 14, 2017.

After a determination of whether the contract and amendment are an indivisible whole, another issue is whether the parties' severability clause should play a role in the analysis. Section 11.4 in the purchase agreement, entitled "Severability and Waiver" provides that: "Invalidation of any one Section ... of this Agreement by judgment or court order shall in no way affect any other Section ... The provisions of this Section shall survive the closing." Under this section, therefore, upon a "judgment or court order" that a

section of the agreement is invalidated, such section may be excised from the agreement, leaving the others in force. Whether the provisions of the 2006 amendment could be invalidated by application of this provision was not addressed because all of the plaintiff-purchaser's contract and fraud claims had been dismissed. Here, there was no judgment or court order invalidating the 2006 amendment but this clause may suggest that the parties contemplated the consequences of invalid provisions and did not want them to undermine the enforceability of the other remaining valid provisions.

Finally, the plaintiff-purchaser claimed it wanted to close on the purchase but it failed to seek a temporary restraining order and/or preliminary injunction to maintain the status quo while the parties litigated the rescission claim. This oversight speaks volumes about whether the plaintiff-purchaser believed that it was likely to succeed on its claim to rescind the 2006 amendment. An application for a temporary restraining order and preliminary injunction, had it been brought, would have subjected the plaintiff-purchaser's claim for rescission based on fraud to immediate and intense judicial scrutiny of whether the plaintiff-purchaser's claim was likely to succeed. See, e.g., *Doe v. Axelrod*, 73 N.Y.2d 748, 750-51 (1988) (a court should not issue a preliminary injunction if the plaintiff cannot demonstrate a likelihood of success on the merits); *Eljay Jrs., Inc. v. Rahda Exps.*, 99 A.D.2d 408, 409 (1st Dep't 1984) (reversing order granting preliminary injunction because the plaintiff had not shown a likelihood of success on the merits of its fraud claim); *Etzion v. Etzion*, 62 A.D.3d 646, 655 (2d Dep't 2009) (affirming denial of motion for preliminary injunction because the plaintiff failed to establish a likelihood success on the merits of fraud claim).

Conclusion. The Court of Appeals' decision has practical ramifications for parties to contracts that are later amended. The decision provides no guidance as to when an amendment may be split off from the agreement it modifies, for purposes of enforcement. Opening the door to severing an amendment from the original contract without further clarification or guidance may undermine the stability of contracts. It could also create a dangerous precedent for parties who seek to avoid the ramifications of amendments to which they have agreed to be bound but no longer believe to be economically sound. The decision of the Court of Appeals may require the careful draftsman to consider including a clause in each successive amendment that addresses the unintended possibility of severability and its consequences.

David B. Saxe is a former Associate Justice of the Appellate Division, First Department where he served for 19 years before becoming a partner at Morrison Cohen. Danielle C. Lesser is a partner at the firm and co-chair of the business litigation group. Michael Mix, an associate at the firm, assisted in the preparation of this article.