

People v National Home Protection, Inc.

2009 NY Slip Op 32880(U)

December 8, 2009

Supreme Court, New York County

Docket Number: 400431/09

Judge: O. Peter Sherwood

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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: O. PETER SHERWOOD
Justice

PART 61

THE PEOPLE OF THE STATE OF NEW YORK,
by ANDREW M. CUOMO, Attorney General of the
State of New York,

INDEX NO. 400431/09

Petitioner,

MOTION DATE June 17, 2009

-against-

MOTION SEQ. NO. _____

NATIONAL HOME PROTECTION, INC., et al.,

MOTION CAL. NO. _____

Respondents.

The following papers, numbered 1 to _____ were read on this petition to, *inter alia*, enjoin respondents from engaging in false advertising and deceptive practices

PAPERS NUMBERED

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...

Answering Affidavits — Exhibits _____

Replying Affidavits _____

Cross-Motion: Yes No

Upon the foregoing papers, the petition to, *inter alia*, enjoin respondents from engaging in false advertising and deceptive practices in connection with sale of home warranty agreements is decided in accordance with the accompanying decision, order and judgment.

UNFILED JUDGMENT

This judgment has not been entered by the County Clerk and notice of entry has not been based thereon. To obtain entry, court representative must appear in person at the Judgment Clerk's Desk (Room 141B).

Dated: 12/8/09

O.P. Sherwood
O. PETER SHERWOOD, J.S.C.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION

Check if appropriate: DO NOT POST

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 61

UNFILED JUDGMENT
This judgment has not been entered by the County Clerk and notice of entry cannot be served based hereon. To appear in person at the Judgment Clerk's Desk (Room 141B)-----X

-----X
THE PEOPLE OF THE STATE OF NEW YORK,
by ANDREW M. CUOMO, Attorney General of the
State of New York,

Petitioner,

-against-

**DECISION, ORDER
AND JUDGMENT**

NATIONAL HOME PROTECTION, INC., LEO
SERRUR, DAVID SERUYA, and VICTOR HAKIM,
individually, and as principals of NATIONAL
HOME PROTECTION, INC.

Index.: 400431/2009

Respondents.

-----X
O. PETER SHERWOOD, J.:

This proceeding was commenced by the Office of the Attorney General of the State of New York ("OAG") or petitioner against National Home Protection, Inc. ("National" or "NHP"), Leo Serrur ("Serrur"), David Seruya ("Seruya") and Victor Hakim ("Hakim") (collectively "respondents") pursuant to New York Executive Law § 63(12) and Article 22-A of New York General Business Law ("GBL") seeking to enjoin NHP from engaging in alleged false advertising and deceptive practices in connection with the sale of home warranty agreements to consumers in New York State and other states. OAG is seeking a summary determination in its favor, injunctive relief, restitution, damages, civil penalties and costs.

National is a New York corporation with principal offices in New York City. National markets Home Warranty Plans ("HWP") on the internet and by telephone solicitation. For an annual fee, NHP will repair or replace household systems and appliances such as air conditioners, refrigerators and heating systems, without regard to "age, make or model" provided that the appliance is in "good working order" at the time the HWP contract is signed and properly maintained thereafter. National alleges that since 2006 it has sold one or multi-year home warranty contracts to over 20,000 customers. Serrur, Seruya and Hakim are principals in the company. Although required by law, National has not registered with the New York State Department of Insurance and has not demonstrated proof of financial responsibility.

The OAG alleges that it has received over 500 consumer complaints from more than 30 states, 300 of which were received during the first five months of 2009, regarding National's practices. The OAG has received inquiries from several agencies in other states and alleges that aggrieved consumers have filed approximately 1,000 complaints with the Better Business Bureau of Metropolitan New York ("BBB") in 2008.

The OAG alleges that by prominently claiming in internet advertising that it offers "sensible protection against repair costs" and "affordable coverage that could save you thousands," National falsely and misleadingly suggests that its HWP will protect against expensive household repairs. Instead, National applies "ultra restrictive" conditions that can only be found after clicking on the small-print heading "Terms & Conditions" ("T&C") at the bottom of the internet advertising. The T&C itself is a multiple page, small type, single spaced document. It is alleged that consumers solicited by telephone are not given a copy in advance of being signed up.

The OAG also alleges that National routinely engages in a variety of fraudulent tactics to deny consumers' claims under the HWP. These tactics include denial for lack of maintenance records or for baseless "pre-existing conditions, refusal to provide replacement appliances, false claims that items are not covered, and unilateral cancellation of HWP contracts. In addition, National failed to resolve claims in a timely manner, did not provide refunds and engaged in deceptive gift card practices.

Specifically, the OAG alleges that National relies on fine print in the HWP contract that reserves to National the right to request annual maintenance records in order to deny service claims by falsely alleging (a) that the records are inadequate, (b) that the records were forged by the customer or (c) that the maintenance work was not performed by a licensed service contractor even though the HWP contains no such condition. The OAG claims that National denies service based on pre-existing conditions which requirement is not clearly and conspicuously disclosed and that it has asserted baseless pre-existing conditions despite production by consumers of home inspection reports showing that the system or appliance was in working order prior to purchase of the HWP or National's own service contractors not finding a pre-existing condition upon their inspection. The OAG contends that National induces consumers to purchase its HWP by falsely advertising that if an item is beyond repair, National "will replace your unit with the same or like model" but that in

practice it flatly denies replacement claims even where its own service contractors recommend it, and relies on fine print in the T&C to offer unreasonably low cash payments in lieu of replacement. It maintains that New York Insurance Law §7903(e) requires service contract providers to provide full refunds of the purchase price if the contract is cancelled within twenty or thirty days depending on the method by which the contract is delivered to the consumer but that the HWP provides only a three-day cancellation period, with a \$50.00 charge. The OAG also alleges that National prominently advertises “[r]eceive your *Free* \$50 Home Depot [or Lowes] Gift Card today!!!” to induce consumers to enter into its HWPs but fails to disclose that the gift card promised “today” are disguised rebate offers and cannot be obtained until a minimum of five months have passed. The rebate form is sent only after the consumer purchases the HWP and must be submitted in a narrow thirty-day period which is sixty to ninety days after purchase of the HWP. Unaware of this waiting period restriction, many consumers mail the form immediately and, as a result, never receive their gift card.

National strenuously disputes the OAG’s claim that it engages in misleading and deceptive practices. It asserts that it has handled more than 50,000 customer claims with no complaints except in a few instances. It emphasizes that it stands by its commitment to provide “affordable coverage that could save customers thousands” and has spent more than \$1.8 million in repairing or replacing covered appliances and systems without regard for the age, make or model, provided that the appliance is in “good working order” at the time the contract is signed and properly maintained thereafter.

National acknowledges that the HWP is subject to many limitations which are set forth in Terms and Conditions that appear as an easy link on every page of National’s website. National states that the T&C is clearly and conspicuously set forth in understandable English. Specifically, the T&C (which customers purchasing the HWP online must indicate that they have read and agree to be bound by) discloses to consumers National’s policy concerning cancellation of the contract; which home systems and appliances are covered and excluded; the limitations, if any, which National places on cost of repairing or replacing certain items; National’s discretion to provide the consumer cash in lieu of repair or replacement; its policy regarding the pre-approval of technicians and repairs; the exclusion from coverage of pre-existing conditions; and various other items.

National maintains that it receives approximately 1,200 calls per day at its call center which operates between the hours of 9:00 AM. through 6:00 PM, Monday through Friday. At other times customer calls are handled by an outside vendor.

National also criticizes the quality of the evidence presented by the OAG in support of the petition. It argues that the petition is accompanied by just 140 complaints, 46 of which are unsworn. Only two of the sworn complaints and nine unsworn letters were from New York residents. It also submitted an affidavit to respond, on the basis of company records, to each consumer complaint.

National concedes that service technicians cannot always respond quickly enough to satisfy the customer. It argues that during peak periods (e.g. July and August for air conditioning repairs), service technicians can become overwhelmed and may take days to respond, despite company policy that require service technicians to contact the customer to schedule an appointment within four hours of getting a service work order, that in certain geographic areas capable technicians may be in short supply and that parts are not always available. It states that pursuant to the T&C, customers who have systems serviced or repaired without prior approval may have their claims for reimbursement denied. Where National suspects that the damage pre-existed or resulted from neglect, it may require submission of home inspection and repair records or maintenance records.

DISCUSSION

GBL §§349 and 350 have territorial limitations. Their application is limited to transactions in New York State (*see Goshen v. Mut. Life Ins. Co.*, 98 NY2d 314, 324 [2002]). National contends that the petition must be dismissed for lack of jurisdiction because the deceptive transactions alleged did not occur in New York. It argues that the crux of the petition centers on National's allegedly deceptive advertising, that its computer server is in Texas and that only two of the sworn complaints received by the OAG and nine unsworn complaint letters sent to BBB were from New York residents.

National's position lacks merit because it overlooks a substantial number of New York actions that tie National and the alleged deceptive practices to New York. National is a New York corporation and operates from a single office in New York. It solicited business and serviced customers using telephones in New York and made allegedly false and misleading statements during those telephone conversations. It directed customers to send gift card rebate forms to National's

New York office. The HWP provides for submission of all controversies to binding arbitration in New York. These alleged actions are more than sufficient to satisfy the requirement that “at least some part” of the deceptive acts take place in New York (*see id.*). New York has an interest in securing an honest marketplace in which to transact business. When New York is used to complete the deceptive transaction, as is alleged here, a cause of action under the GBL may be stated and the OAG is authorized to recover on behalf of all aggrieved consumers, including non-residents (*see People v. H&R Block Inc.*, 58 AD3d 415, 417 [1st Dept 2009] and *People v. Telehublink Corp.*, 301 AD2d 1006, 1007 [3d Dept 2003]).

New York Executive Law §63(12) empowers the OAG to bring special proceedings for permanent injunctive relief, restitution and damages whenever a person or business engages in repeated or persistent “fraud or illegality”. “Repeated” is defined as conduct which affects more than one person (*see People v. Empyre Inground Pools, Inc.*, 227 AD2d 731, 732 [3d Dept 1996]). The test of fraudulent conduct under Executive Law §63(12) is whether the targeted act “has the capacity or tendency to deceive or creates an atmosphere conducive to fraud”. *In re People v. Applied Card Systems, Inc.*, 27 AD3d 104, 107 (3d Dept 2005) *aff’d on other grounds*, 11 NY3d 105 (2008).

GBL §349, like Executive Law §63(12), is “intended to be broadly applicable, extending far beyond the reach of common law fraud” (*State v. Feldman*, 210 F Supp 2d 294, 301 [SDNY 2002]). GBL §349(a) declares that “[d]eceptive acts or practices in the conduct of any business, trade or commerce or in the furnishing of any service” in New York State are unlawful.

The OAG has established that National violated Executive Law §63(12) and GBL §§349 and 350 by engaging in false and misleading advertising. It has also shown that National (1) failed to register the HWP with the superintendent of insurance and establish financial responsibility in violation of Insurance Law §§7709(a) and 7903(c); (2) did not offer full refunds within the time frame prescribed by Insurance Law §7903(e); and (3) failed to post the rebate forms on its website and to provide rebates within the time frame required by GBL §391-p.

The OAG has shown National’s online advertising to be deceptive in several respects. National displayed prominently on the homepage of its website, “receive your *Free* \$50 Home Depot [or Lowe’s] gift card today!!!” In fact, the gift card is not “free.” They are rebates to consumers who purchase the HWP. Further, although the gift cards are promised “today,” National does not disclose

on its homepage (1) that the customer must complete and send in a rebate form, (2) that the form must be mailed within a narrow 30-day window between 60 and 90 days after purchase of the HWP and (3) that the customer must then wait 12-14 weeks to receive the rebate. The OAG showed that many customers complained¹ that they never received the rebate because of alleged failure to follow onerous terms and conditions buried in fine print of rebate forms copies of which were not provided until after purchase of the HWP. Several customers who met the rebate terms and conditions complained that they did not receive gift cards.

National advertises that it provides “sensible protection against repair costs” and “affordable coverage that could save you thousands.” The homepage includes a chart listing a consumer’s estimated heating system or air conditioning repair/ replacement costs of “as much as \$3,400” or “as much as \$4,200” respectively so as to falsely suggest that the HWP will protect against costly repairs and replacements. National claims that the HWP covers specified working household appliances “regardless of age, make or model” with “no home inspection required to enroll” and that if the item is beyond repair, National “*will* replace your unit with the same or like model” (emphasis added). In fact, the T&C reserves to National the option to offer cash in lieu of replacement. Several consumers complained of offers of replacement of appliances with appliances that are substantially inferior to the customer’s existing appliance or of cash back offers that were a small fraction of the actual cost of the appliance. Customers also complain of denial of claims for failure to produce maintenance records, inadequacy of records and that the work was not performed by a licensed technician, an asserted requirement that appears nowhere in the T&C.

National cannot rely, as a defense, on the T&C. First, the link which appears at the bottom of the homepage and directs the consumer to seven (7) pages of densely worded, fine-print, single spaced terms and conditions are too far removed from the main portions of the web page and are insufficient to alter consumers’ net impressions that the HWP covers existing systems and appliances which break down due to normal wear and tear. Fine-print disclosures and disclaimers that are placed in portions of an advertisement that are less likely to be read or remembered are inadequate to disclaim or modify a claim that is made in the main body or text of the advertising (*see Applied*

¹The court’s references to customer complaints refer to sworn complaints in the record.

Card Systems Inc., 27 AD3d *Supra* at 107; *Removatron Int'l. Corp. v. FTC*, 884 F2d 1489, 1497 [1st Cir 1989]). Second, a number of the false advertising claims are so misleading that they could not be saved by any of the disclosures made in the T&C. For example, the website contains a promise to replace appliances that cannot be repaired with the same or like model. In fact, the T&C gives National the option, which it often exercises, to offer cash back (at National's often lower cost) in lieu of replacement. Additionally, National has refused to replace appliances with the same or like models and instead insisted on providing cheaper, lower quality appliances. The website also suggests that National would pay for repair/replacements costing "as much as \$3,400" or "as much as \$4,200" but the T&C limits monetary recovery to \$1,500 per item.

Although the Insurance Law does not expressly authorize the OAG to bring claims under Article 79, the OAG has authority to bring a special proceeding pursuant to Executive Law §63(12) whenever a business engages in repeated or persistent fraud or illegality. The authority of the OAG under §63(12) to bring claims for violation of the Insurance Law and other laws over which other New York agencies have regulatory authority have been upheld (*see, e.g. People v. American Motor Club*, 179 AD2d 277 [1st Dept 1992][New York Insurance Department]; *State v. Winter*, 121 AD2d 287 [1st Dept 1986][New York State Division of Housing and Community Renewal]).

Businesses in New York may incorporate for the express purpose of limiting liability of their owners (*see Morris v. State Dep't of Taxation and Finance*, 82 NY2d 135 [1993]; *Total Care Health Indus., Inc. v. Dep't of Soc. Servs.*, 144 AD2d 678, 679 [2d Dept 1988]). Individuals who are principals in a business who are not shown to have acted in bad faith or outside their capacity as corporate officers may not be held individually liable for corporate acts that are found to be unlawful (*see Murtha v. Yonkers Child Care Ass'n*, 45 NY2d 913, 915 [1978]). Absent evidence that the individual respondents have personally participated in or had personal knowledge of specifically identified fraud, they may not be held personally liable (*see Mora v. RGB, Inc.*, 17 AD3d 849 [3d Dept 2005]; *Rothstein v. Equity Ventures, LLC*, 299 AD2d 472 [2d Dept 2002]; *People v. Apple Health & Sports Clubs, Ltd., Inc.*, 206 AD2d 266 [1st Dept 1994]).

In this case, the OAG seeks to hold Serrur, Seruya and Hakim, three principals of National, individually liable. This claim is based on allegations that they are owners and managers of a small business and that as such they were involved in or had actual knowledge of the fraudulent business

practices of National, “including the continued offering of gift cards and illegal operations in various states without obtaining the necessary licenses or registrations (*see* OAG Reply Memorandum of Law in Support of the Verified Petition, p.10).

These allegations fall far short of the requirements of CPLR 3016 which provides that “the circumstances constituting the wrong shall be stated in detail” in the petition. In order to survive a motion to dismiss, the petition must give proper notice of the transactions or occurrences intended to be proved (*see Lynch v. Upper Crust, Inc.*, 294 AD2d 237 [1st Dept 2002]). The petition must allege that the individual respondents made specific representations with the required scienter (*see Feldman v. Grant*, 213 AD2d 340 [1st Dept 1995]). Where, as here, multiple individuals are alleged to be guilty of fraud, the petition must specifically allege the fraud perpetuated by each respondent (*see Clifford v. Hughson*, 992 F Supp 661, 666 [SDNY 1998]). Petitioner has not satisfied these standards. The petition shall be dismissed as to Serrur, Seruya and Hakim.

Having established violations of Executive Law §63(12), the OAG is entitled to an appropriate permanent injunction (*see, State v. Princess Prestige Co.*, 42 NY2d 104, 108 [1977]; *State v. Mgmt. Transition Res., Inc.*, 115 Misc.2d 489 [Sup Ct NY Co 1982]; *In re State v. Daro Chartours, Inc.*, 72 AD2d 872 [3d Dept 1979]; *In re State v. Scottish-Am. Ass'n*, 52 AD2d 528 [4th Dept 1976]; *State v. Midland Equities of NY, Inc.*, 117 Misc.2d 203, 206 [Sup. Ct. NY Co. 1982]; *In re State v. Hotel Waldorf-Astoria Corp.*, 67 Misc.2d 90 [Sup. Ct. NY Co. 1971]). Petitioner shall also have an order directing respondent, National, to make restitution to victims of its deceptive and misleading practices (*see In re. State v. Ford Motor Co.*, 74 NY2d 495 [1989]; *Princess Prestige Co.*, 42 NY2d at 104) and to pay civil penalties (*see Telehublink Corp.*, 301 AD2d at 1006) and costs in the amount of \$2,000 (*see CPLR §8303[a][6]*; *Daro Chartours*, 72 AD2d at 873).

Accordingly, it is

ORDERED and **ADJUDGED** that the petition is **GRANTED** as to respondent, National Home Protection, Inc.; and it is further

ORDERED and **ADJUDGED** that the petition is **DISMISSED** as to respondents, Leo Serrur, David Seruya and Victor Hakim; and it is further

ORDERED that effective ten (10) days after the date hereof, all stays applicable to the personal assets of respondents Serrur, Seruya and Hakim shall dissolve; and it is further

ORDERED that within thirty (30) days of service with notice of entry of this Decision, Order and Judgement, petitioner shall serve and file a proposed Injunction Order which shall include appropriate injunctive relief; directions to make restitution to adversely affected consumers, including procedures for distribution; an amount of penalties and costs in the amount of \$2,000, and it is further

ORDERED that National shall have ten (10) days after service of the proposed Injunction Order to serve and file its opposition or comment.

DATED: December 8, 2009

ENTER,



**O. PETER SHERWOOD
J.S.C.**

UNFILED JUDGMENT
This judgment has not been entered by the County Clerk and no return has been filed hereon. To obtain a return, the party and representative must appear in person at the Judgment Clerk's Desk (Room 141B).