STATE OF NORTH CAROLINA

MECKLENBURG COUNTY

IN THE GENERAL COURT OF JUSTICE
SUPERIOR COURT DIVISION
23CV031985-590

ALCOF III NUBT, L.P.; ALTA FUNDAMENTAL ADVISERS LLC, on behalf of funds it manages; BLACKCOMB DEBT HOLDINGS, L.P.; CTC ALTERNATIVE STRATEGIES, LTD; NUVEEN ASSET MANAGEMENT, LLC; SCULPTOR SPECIAL MASTER FUND, LTD; TBK BANK, SSB; TRANSAMERICA LIFE INSURANCE COMPANY; VENTURE 28A CLO, LIMITED; VENTURE XXX CLO, LIMITED; VENTURE 31 CLO, LIMITED; VENTURE 32 CLO, LIMITED; VENTURE 33 CLO, LIMITED; VENTURE 36 CLO, LIMITED; VENTURE XV CLO, LIMITED; VENTURE XIX CLO, LIMITED; VENTURE XXII CLO, LIMITED; and VENTURE XXIII CLO, LIMITED,

Plaintiffs,

v.

JAMES M. CHIRICO, JR.; KIERAN MCGRATH; and STEPHEN D. SPEARS,

Defendants.

ORDER AND OPINION ON DEFENDANT STEPHEN D. SPEARS'S MOTION TO DISMISS

1. Plaintiffs are investors that hold interests in loans made to Avaya, Inc.[1] in July 2022. The value of their interests plunged when Avaya declared bankruptcy the following year. In this lawsuit, Plaintiffs accuse three of Avaya's former officers—James M. Chirico, Jr., Kieran McGrath, and Stephen D. Spears—of wrongfully

[1] Some allegations refer to both Avaya and its parent company, Avaya Holdings Corp. For ease of comprehension, the Court will follow the parties' lead and refer to the two Avaya entities simply as "Avaya."

inducing them to invest based on false statements and omissions about the company's financial condition and expectations for future earnings.

2. This opinion addresses Spears's motion to dismiss for failure to state a claim.[2] (*See* ECF No. 82.) For the following reasons, the Court **GRANTS** his motion.

Parker Poe Adams & Bernstein LLP, by Melanie Black Dubis and Andrew Tabeling, and Glenn Agre Bergan & Fuentes LLP, by Andrew Glenn, Marissa E. Miller, Eric J. Carlson, George L. Santiago, and Trevor J. Welch, for Plaintiffs ALCOF III NUBT, L.P. et al.

Johnston, Allison & Hord, P.A., by William D. McClelland, Kenneth Lautenschlager, and Austin R. Walsh, and Dorsey & Whitney, LLP, by Thomas O. Gorman and Stephen Weingold, for Defendant James M. Chirico, Jr.

Robinson, Bradshaw & Hinson, P.A., by David C. Wright, Adam Doerr, and Ethan R. White, and Kellogg, Hansen, Todd, Figel & Frederick, PLLC, by Reid Mason Figel, Minsuk Han, and Jordan Gonzalez, for Defendant Kieran McGrath.

James, McElroy & Diehl, P.A., by Jennifer M. Houti and Adam L. Ross, for Defendant Stephen D. Spears.

Conrad, Judge.

I.
BACKGROUND

3. The Court does not make findings of fact on a motion to dismiss. The following background assumes that the allegations of the amended complaint are true.

4. Avaya specializes in multifunction communications. It provides unified "video, audio, phone, and chat" software, related technical support, and

[2] Chirico and McGrath have filed their own motions to dismiss for improper venue and failure to state a claim. A separate opinion addresses those motions and similar ones in a related case, *Brigade Cavalry Fund Ltd. v. Chirico* (23CV031948-590).

communications hardware to its customers. During the relevant period, Chirico was its president and chief executive officer, McGrath was its executive vice president and chief financial officer, and Spears was its chief revenue officer. (*See* Am. Compl. ¶¶ 32–34, 37–39, ECF No. 76.)

5. A few years ago, Avaya shifted its sales strategy toward its cloud-based product. In May 2022, Chirico told investors that this "strategy [was] taking hold" and was "reflected in our revised second half guidance." Avaya had filed its Form 8-K with the Securities and Exchange Commission that same day and provided bullish earnings guidance for the third quarter of its fiscal year (which was the second quarter of the calendar year). McGrath signed the Form 8-K on Avaya's behalf. (Am. Compl. ¶¶ 37, 39, 42–45; *see also* Am. Compl. ¶ 69.)

6. Several weeks later, Avaya began trying to raise money to pay off existing debt and for general purposes. In "a pre-marketing call" with potential investors on 2 June 2022, McGrath shared a lender presentation that incorporated the company's third-quarter guidance. Avaya provided substantially the same presentation to Plaintiffs on 8 June 2022, which was the date that the company publicly launched its marketing campaign. The presentation named McGrath and Avaya's treasurer as presenters and listed Chirico, McGrath, Spears, and others as members of Avaya's "Experienced Management Team." Around this time, Avaya also created a virtual data room so that potential investors could conduct due diligence. The data room included a letter stating that estimates and projections in the lender presentation were "developed by management" of Avaya and that "management believes such

assumptions and estimates to be reasonable." As alleged, Chirico and McGrath were responsible for reviewing, approving, and developing the third-quarter guidance and including it within the lender presentation. Eventually, Plaintiffs agreed to lend Avaya $236 million in a deal that closed on 12 July 2022. (Am. Compl. ¶¶ 2, 47, 49–55.)

7. Just two weeks after the signing of the loan agreement, Avaya published preliminary results for the third quarter, missing its revenue guidance by nearly twenty percent and its EBITDA (earnings before interest, taxes, depreciation, and amortization) guidance by over sixty percent. The situation deteriorated rapidly. In August 2022, Avaya disclosed that it doubted its "ability to continue as a going concern." Then, in February 2023, Avaya filed for bankruptcy protection. (Am. Compl. ¶¶ 76, 79, 88.)

8. Plaintiffs now claim to have been defrauded. They say that Chirico and McGrath knew that the company's cloud-based strategy was failing even as they told investors that it was succeeding. In April 2022, for example, Avaya's senior director of sales finance told Spears that the revenue projection for North America was "scary"—a concern that Spears said was "spot on" and that he would raise to a "smaller audience." In a related conversation, another member of the finance team confirmed that this concern "made its way to" Chirico, and by early June 2022, Chirico was telling Spears and others that internal revenue projections were "clearly not good at all." Despite this, Chirico and McGrath reaffirmed Avaya's third-quarter guidance

to Plaintiffs and others in the lender presentation. (*See, e.g.*, Am. Compl. ¶¶ 2, 58–62, 64, 65, 71–74.)

9. According to Plaintiffs, any doubt about Avaya's performance was removed when its third quarter ended. On 1 July 2022, the first day of the new quarter, the company received a report that it had substantially underperformed, confirming the finance team's fears. Spears drafted an e-mail addressed to Avaya's board of directors about the results. He sent that draft to Chirico, who did not send it to the board. On 3 July 2022, though, the board received a message from a whistleblower, which denounced Chirico's and McGrath's alleged "financial engineering" and "fabrications," including their creation of "fake EBITDA numbers." No one shared any of this with Plaintiffs before the loan agreement closed just over a week later. (Am. Compl. ¶¶ 67–70, 83–85.)

10. In this action, Plaintiffs say that they would not have invested in Avaya had they known the truth. They assert claims for fraudulent misrepresentation, fraudulent omission, and negligent misrepresentation against Chirico and McGrath. They assert only the claim for fraudulent omission against Spears.

11. Spears has moved to dismiss that claim. The motion is fully briefed, and the Court held a hearing on 21 May 2024. The motion is ripe for decision.

II.
LEGAL STANDARD

12. A motion to dismiss for failure to state a claim "tests the legal sufficiency of the complaint." *Isenhour v. Hutto*, 350 N.C. 601, 604 (1999) (citation and quotation marks omitted). Dismissal is proper when "(1) the complaint on its face reveals that

no law supports the plaintiff's claim; (2) the complaint on its face reveals the absence of facts sufficient to make a good claim; or (3) the complaint discloses some fact that necessarily defeats the plaintiff's claim." *Corwin v. Brit. Am. Tobacco PLC*, 371 N.C. 605, 615 (2018) (citation and quotation marks omitted). In deciding the motion, the Court must treat all well-pleaded allegations as true and view the facts and permissible inferences in the light most favorable to the nonmoving party. *See, e.g.*, *Sykes v. Health Network Sols., Inc.*, 372 N.C. 326, 332 (2019).

III.
ANALYSIS

13. Fraud has five "essential elements": (a) a false representation or concealment of a material fact, (b) calculated to deceive, (c) made with intent to deceive, (d) that did in fact deceive, and (e) that resulted in damage to the injured party. *Rowan Cnty. Bd. of Educ. v. U.S. Gypsum Co.*, 332 N.C. 1, 17 (1992). The injured party's reliance on the misrepresentation or concealment "must be reasonable." *Forbis v. Neal*, 361 N.C. 519, 527 (2007).

14. Because "silence is fraudulent only when there is a duty to speak," a claim based on "concealment or nondisclosure" requires the plaintiff to allege with particularity that the defendant "had a duty to disclose material information." *Lawrence v. UMLIC-Five Corp.*, 2007 NCBC LEXIS 20, at *8 (N.C. Super. Ct. June 18, 2007) (citing *Griffin v. Wheeler-Leonard & Co.*, 290 N.C. 185, 198 (1976)); *see also* N.C. R. Civ. P. 9(b) (requiring allegations of fraud to "be stated with particularity"). A duty to disclose arises when the parties are in a fiduciary relationship, when one party "has taken affirmative steps to conceal material facts from the other," or when

"one party has knowledge of a latent defect in the subject matter of the negotiations about which the other party is both ignorant and unable to discover through reasonable diligence." *Harton v. Harton*, 81 N.C. App. 295, 297–98 (1986). In addition, "a party who chooses to speak has a duty to make a full and fair disclosure of facts concerning the matters on which he chooses to speak." *Tillery Env't LLC v. A&D Holdings, Inc.*, 2018 NCBC LEXIS 13, at *22 (N.C. Super. Ct. Feb. 9, 2018) (citing *Ragsdale v. Kennedy*, 286 N.C. 130, 139 (1974)).

15. Spears denies that he had a duty to speak. In his view, the allegations of the amended complaint show that he played no role in making any misrepresentations to Plaintiffs, did not draft or sign the lender presentations or regulatory filings at issue, and never communicated with Plaintiffs in any way. He further contends that the allegations that he took affirmative steps to conceal information from Plaintiffs are conclusory.

16. Plaintiffs do not contend that they had a fiduciary relationship with Spears or that he was a party to the negotiations with knowledge of a latent defect in their subject matter. Instead, they offer three other arguments, none convincing.

17. First, they argue that Spears participated in the alleged misrepresentations in Avaya's third-quarter guidance. This argument is based partly on allegations concerning a lender presentation that incorporated the third-quarter guidance. The presentation, which McGrath delivered, identified Spears as Avaya's chief revenue officer and part of its "Experienced Management Team." A different document given to potential lenders stated that the projections contained in McGrath's presentation

were "developed by" unnamed members of "management" and that "management believes such assumptions and estimates to be reasonable." (Am. Compl. ¶¶ 34, 50, 53, 54.)

18. Even if true, these allegations are insufficient. Spears's status as an officer, without more, does not make him liable for the corporation's acts or the acts of other officers. *See* Russell M. Robinson, II, *Robinson on North Carolina Corporation Law* § 16.08 (7th ed. 2018). Nowhere do Plaintiffs allege that Spears was among the management group that developed the third-quarter guidance, that he "actively participat[ed] in the production of due diligence information" to Plaintiffs, or that he prepared or approved any of the documents containing the alleged misrepresentations about Avaya's financial state or its expected financial performance. *See Tillery Env't*, 2018 NCBC LEXIS 13, at *49. Nor do they allege that he "was actively involved . . . in the negotiations" that led to the loan agreement. *See Oberlin Cap., L.P. v. Slavin*, 147 N.C. App. 52, 58 (2001). In fact, there are no allegations that Spears had any contact with Plaintiffs at all. *See id.* at 57 (affirming dismissal of fraudulent concealment claim, among others, for failure to "clarify how and to what extent [officer] defendants actively and personally participated").

19. Second, Plaintiffs argue that Spears took affirmative steps to conceal material facts. This argument is based on an e-mail that Spears drafted and sent to Chirico less than two weeks before the loan agreement closed. The draft was addressed to Avaya's board of directors and stated that the company would not meet its third-quarter guidance. Chirico sent it to a third individual but apparently did

not send it to the board. Having alleged these facts, the amended complaint goes on to allege in a conclusory manner that Spears "intentionally concealed" the draft from Plaintiffs as well as Avaya's board and other investors. (Am. Compl. ¶¶ 68, 70, 109.)

20. As our Court of Appeals has explained, "[m]ere generalities and conclusory allegations of fraud will not suffice." *Sharp v. Teague*, 113 N.C. App. 589, 597 (1994) (quoting *Moore v. Wachovia Bank & Tr. Co.*, 30 N.C. App. 390, 391 (1976)). Plaintiffs had to "allege the specific affirmative acts"—something beyond nondisclosure itself, such as deleting or destroying the information or directing others not to disclose it—that Spears took "to conceal" the draft. *Vitaform, Inc. v. Aeroflow, Inc.*, 2020 NCBC LEXIS 132, at *31 (N.C. Super. Ct. Nov. 4, 2020); *see also Maxwell Foods, LLC v. Smithfield Foods, Inc.*, 2023 NCBC LEXIS 20, at *7 (N.C. Super. Ct. Feb. 3, 2023) ("Nondisclosure alone is not an affirmative act of concealment."). They haven't done so. *See Aym Techs., LLC v. Scopia Cap. Mgmt. LP*, 2021 NCBC LEXIS 29, at *25 (N.C. Super. Ct. Mar. 31, 2021) (concluding that party "fail[ed] to specifically allege what steps [wrongdoer] took to hide this information"); *see also Lee v. McDowell*, 2022 NCBC LEXIS 51, at *46–47 (N.C. Super. Ct. May 26, 2022) (collecting cases).

21. Third, Plaintiffs point to several allegations to show that Spears knew the truth about Avaya's third-quarter guidance. As early as April 2022, Spears expressed concern about the guidance for Avaya's North American revenue. Two months later, Chirico told Spears that the available revenue estimates were "clearly not good at all." And the day after the third quarter ended, Spears learned that Avaya had not

met its targets, prompting him to send to Chirico the draft e-mail intended for Avaya's board. (Am. Compl. ¶¶ 58, 59, 64, 68–70.)

22. Again, even if true, these allegations show only that Spears knew certain facts and remained silent. No allegations suggest that Spears created the third-quarter guidance, approved the inclusion of the guidance in presentations to Plaintiffs, or had any interactions with Plaintiffs concerning negotiations for the loan agreement or any other subject. All that is alleged is Spears's "silence," and that alone "is insufficient under North Carolina law to establish a duty to disclose." *Lee*, 2022 NCBC LEXIS 51, at *46 (concluding that "allegations and arguments on [defendant's] failure to correct" someone else's "representations" were inadequate).

23. In sum, Plaintiffs have not alleged with particularity facts showing that Spears was personally involved in making the alleged misrepresentations or that he had a duty to disclose material information to them. As a result, Plaintiffs have not stated a claim for fraudulent omission against him.

IV.
CONCLUSION

24. For all these reasons, the Court **GRANTS** Spears's motion to dismiss. Plaintiffs' claim against him is **DISMISSED** with prejudice.

SO ORDERED, this the 21st day of August, 2024.

/s/ Adam M. Conrad
Adam M. Conrad
Special Superior Court Judge
for Complex Business Cases