

SCANNED ON 1/22/2007
SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: HELEN E. FREEDMAN
Justice

PART 39

General Electric Capital Corp.,
Plaintiff,

INDEX NO. 600993/06

MOTION DATE _____

- v -

The Bank of New York et al.,
Defendants

MOTION SEQ. NO. 801

MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to/for _____

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

Answering Affidavits — Exhibits _____

Replying Affidavits _____

FILED
PAPERS NUMBERED
JAN 02 2007
NEW YORK
COUNTY CLERK'S OFFICE

Cross-Motion: Yes No

For the reasons set forth below, the motion by the defendants for an order dismissing the complaint pursuant to CPLR 3211 is granted.

Plaintiff General Electric Capital Corp. ("GECC"), which provided leasehold financing to a lessee of real property located in East Meadow, New York (the "Property"), brought this action for promissory estoppel, breach of contract, and related remedies against the Property's lessor and their agents after the lessee defaulted on its loan obligations and filed for bankruptcy. The gist of GECC's claims are that (1) when making the loan, GECC relied on the lessor's representation that the leasehold comprised only land, and the not the buildings situated on it, (2) without that representation, GECC would not have financed the leasehold, (3) as collateral for the loan, the lessee assigned its lease with the lessor, its subleases with third parties and the rents payable under the subleases to GECC, (4) thereafter, during arbitration between the lessor and lessee to set the rent for the upcoming renewal term, the lessor took a position that was at odds

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

with what it had represented to GECC by claiming that the leasehold comprised *both* the land and the buildings, (5) the arbitrators accepted the lessor's new position and as a result raised the rent by more than 1000%, (6) the arbitrators would have set a much lower rent if the lessor had represented to them, as it had to GECC, that the buildings were not part of the leasehold, (7) after the lessee defaulted on the loan and filed for bankruptcy, GECC could not prevent the lessor from terminating the lease and depriving GECC of its loan collateral unless it assumed the lease from the lessee and paid the "artificially inflated rent" to the lessor, and (8) in that case, the rental income GECC would receive from the subtenants would not cover both the repayment of its loan and the rent it owed to the lessor.

Allegations – In the complaint, GECC offers the following chronology: The Property, which has been leased since 1967, has had a succession of owner-lessors and lessees. The initial Lease, dated June 1, 1967 (the "Lease"), had a term of 35 years, and provided the lessee with an option to renew for two 21-year terms. Pursuant to the Lease, the lessor and lessee would try to negotiate a new rent for the renewal term, and if they were unable to agree, they would submit the issue to binding arbitration. According to GECC, when the Lease was executed the parties contemplated that the lessee would build a shopping center and office building (collectively, the "Buildings") on the land at the Property (the "Land"), and that the lessee would pay for the construction and own the Buildings. The complaint further alleges that the lessor's interest in the Lease was limited to the Land and did not include the Buildings or the income that the lessee derived from subleasing the Buildings to third parties.

In 1987, GECC provided \$ 13.5 million in leasehold financing (the "Loan") to a successor tenant, East Meadow Associates ("East Meadow"). As security for the Loan, East Meadow executed an Assignment of Rents and Leases (the "Assignment") providing among other things that its subtenants were to pay their rent directly into a lockbox under GECC's control, and that GECC would apply the lockbox funds towards repaying the Loan.

As a condition to closing, GECC required the then-lessors, Anna Weiss & the Estate of Kurt Weiss (the "Weisses") to deliver an Acknowledgment Agreement (the "Acknowledgment") and a Ground Lessor Estoppel Certificate (the "Certificate"), both dated July 2, 1987.

Defendants The Bank of New York ("BONY") and Leonara White signed the Acknowledgment and the Certificate in their capacity as executors of Kurt Weiss' will and as attorneys-in-fact for Anna Weiss. As explained below, the parties interpret the Acknowledgment and the Certificate differently, but according to GECC, the lessors represented in their Acknowledgment that the Lease was only for the Land and that it secured East Meadow's Loan obligations, and also agreed in the Acknowledgment that GECC would be entitled to certain rights under the Lease as an "Institutional Leasehold Mortgagee." In the Certificate, the complaint further alleges, the Weisses consented to the Assignment and certified that GECC was entitled to the rights granted to a leasehold mortgage holder under the Lease.

The present tenant, non-party Walsam EMP LLC ("Walsam"), succeeded East Meadow as the lessee and leasehold mortgagor in 1995. By that date and continuing until today, defendants Gordon and Lenora White, Kirk Weiss, and Laura Reid, individually and as trustees of the White Family Trust and the Weiss Family Trust (collective, the "Lessor") own and lease the property, and defendants BONY and Joseph J. Marraro act as agent for the Lessor with respect to the Lease.

The complaint alleges that, before the original Lease term expired in June 2003, BONY, Marraro, and other representatives of the Lessor "devised a plan to recharacterize the [Lease] as a master lease of the Land and Buildings so as exact a drastically higher rent during the [renewal term]." The Lease set the rent for the last year of the initial term at \$ 100 thousand; GECC alleges that the rent was based upon the value of the Land only. However, the complaint alleges, when the parties tried to negotiate a new rent for the renewal term, the defendants changed their position, claimed that the renewal term rent should be based upon the value of both the Land and

the Buildings, and demanded a new rent \$ 1.8 million for the first year of the renewal term. By taking that position, GECC alleges, defendants acted in bad faith and breached the Acknowledgment and the Certificate, and they knew or should have known that the rents that Walsam received from subleasing the Property would not cover both the loan payments to GECC and the increased rent due the Lessor under the Lease. The complaint alleges that defendants' conduct

was designed to cause a forfeiture of [Walsam's] interest in the [Lease], so that the Lessor either could gain possession of the Land, Buildings and [assigned rents] and recover for itself a windfall or force GECC to assume the position of [Walsam] under the [Lease] and pay an artificially inflated rent in order to prevent a termination of the [Lease.] In the latter case, since the [assigned rents] would be insufficient to pay both debt service on the leasehold mortgage and an artificially inflated rent based upon the Land, Buildings and [assigned rents], the Lessor could ensure that [they] would receive the benefit of the [assigned rents] for itself, rather than having [them] first utilized to service the Loan, and thereby destroy GECC's collateral for the loan.

In December 2002, the Lessor demanded arbitration against Walsam to determine the renewal rent (the "Arbitration.") In April 2003, Walsam filed a voluntary Chapter 11 bankruptcy petition with the United States Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court"), which automatically stayed the Arbitration. In June 2003, the Bankruptcy Court modified the automatic stay to permit the Arbitration to proceed in February, March, and April 2004. In August 2004, a divided arbitration panel issued an award (the "Award") that accepted the Lessor's new position and fixed the annual rent for the first seven years of the renewal term at \$ 1.35 million, based upon the value of the Land, Buildings, and assigned rent.

Upon Walsam's and GECC's motion, in September 2005 the Bankruptcy Court vacated the Award. The parties did not submit the Bankruptcy Court's decision, but according to the complaint the court held that the Award was irrational and procured by the lessor's misconduct. However, by judgment entered February 2006, the United States District Court for the Southern District of New York reversed the Bankruptcy Court's order, confirmed the Award, and directed

Walsam to pay back rent of about \$ 2.5 million. The District Court also vacated the automatic stay and allowed the Lessor to proceed against Walsam if it failed to pay the back rent by, among other things, terminating the Lease. In its decision on the record, the District Court found that the arbitrators had “grounded their decision on the lease,” and that the Award was “not irrational,” but rather “quite reasonable and appropriate.” The Court further held that “[t]here is no legitimate argument of improper activity on the part of the landlord [or] the tenant” and that “[t]here was no misrepresentation, there was no misstatement.”

After GECC had commenced this action, the United States Court of Appeals, Second Circuit, affirmed the judgment of the District Court. *Walsam EMP LLC v. White*, Nos. 06-1257-bk, 06-1258-bk, 06-1268-bk, & 06-1276-bk (2d Cir. Aug. 11, 2006).

The complaint asserts five causes of action. In the first, sounding in “promissory/equitable estoppel,” GECC alleges that it would not have made the Loan but for defendants’ representations (the “Representations”) that (1) only the Land was leased, (2) if GECC made the Loan, it would have a priority interest in the assigned rents and subleases that would be senior to the Lessor’s interest in the rent due under the Lease, and (3) the Lease would not be amended without GECC’s consent. As a result, GECC claims, the Lessor should be equitably estopped from claiming any interest in the assigned rents and subleases until the Loan is repaid.

GECC further claims that the Lessor’s “self-interested actions” breached the terms of the Acknowledgment and the Certificate (second cause of action), and also breached its duty of good faith and fair dealing (third). GECC also seeks a declaration that its interest in the assigned rents and subleases are superior to GECC’s (fourth), and seeks to have an equitable lien imposed on them (fifth).

Motion – Defendants move for an order dismissing this action on the ground that GECC cannot maintain its claims because of documentary evidence and arbitration and award, and

cannot maintain its claims because of documentary evidence and arbitration and award, and because the complaint fails to state a cause of action. The threshold issue is whether, as GECC alleges, the defendants represented in the Acknowledgment and the Certificate that only the Land was being leased. Defendants submit those documents, along with the Lease, and correctly point out that they refute GECC's core allegation. It is appropriate to review those documents while addressing defendants' motion for dismissal, since "[a]lthough on a motion addressed to the sufficiency of a complaint, the facts pleaded are presumed to be true and accorded every favorable inference, nevertheless . . . factual claims [that are] flatly contradicted by documentary evidence . . . are not entitled to such consideration." *Kliebert v. McKoan*, 228 A.D.2d 232, 232 (1st Dept. 1996).

The Lease will be examined first, because the Acknowledgment and the Certificate both refer to the Lease and they can only be construed in conjunction with it. The original Lease specifies on its first page that the "Demised Premises" being leased include "the property (hereinafter referred to as the 'Land') situate, lying and being in East Meadow, Nassau County, State of New York, bounded and described as in Exhibit A annexed hereto and made a part hereof; together with the Building (as said term 'Building' is defined in Section 2.01 hereof)" Exhibit A sets forth the metes and bounds description of the Land. Section 2.01 defines "Building" as "all structures or improvements hereafter erected or situated on the land described in Exhibit A"

The Lease further provides that the lessee can mortgage the Lease and the leasehold estate it creates without the lessor's consent. Under the Lease, an "Institutional Leasehold Mortgagee" has the right to cure the lessee's default and assume its rights and obligations under the lessee's rights and obligations; moreover, the lessee's assignment of sublease rents to the lessor in the event of a default "shall be subject to any assignment of rent of the sublease made to the holder or any Leasehold Mortgagee."

Before GECC financed the leasehold in 1987, the Lease was amended in November 1968 and October 1970. The first recitals in both amendments refer to the original Lease: the 1968 amendment describes it as “affecting the premises described in Exhibit ‘A’ attached hereto,” and the 1970 amendments states that the Lease “demised to . . . [l]essee the premises hereinafter described in Exhibit A” Each amendment annexes an “Exhibit A” that sets forth the metes and bounds of the Land but does not include the Buildings. The substantive changes to the Lease set forth in the amendments are minor and irrelevant here.

Turning to the Acknowledgment and Certificate, which allegedly contain defendants’ misrepresentations to GECC, the bulk of the Acknowledgment is comprised of recitals. The first states that Kurt and Anna Weiss, defined as the “Ground Lessor”, “entered into a certain Indenture of Lease (said lease, as amended prior to the date hereof, the “Ground Lease”), dated June 1, 1967 . . . affecting the property more particularly described in Exhibit “A” annexed hereto and made a part hereof (the “Premises”)” Exhibit A to the Acknowledgment also sets forth the Land’s metes and bounds but omits the Buildings.

Next, the recitals detail the execution, delivery, and recording of the “Ground Lease” and its amendments, and identify the successors-in-interest to the original lessors, The Acknowledgment next recites that GECC has given the new lessors a commitment for a mortgage loan “to be secured by the Premises” and that GECC would not make the loan unless the “Ground Lessor” acknowledged that

GECC fits within the definition of ‘Institutional Leasehold Mortgage’, as set forth in . . . the Ground Lease and, accordingly, is entitled to all of the benefits granted to an Institutional Leasehold Mortgagee pursuant to the Ground Lease

The Acknowledgment concludes by reciting that the Ground Lessor has consented to GECC’s conditions to the loan, and sets forth the parties’ agreement that (1) the Ground Lessor acknowledges that GECC is an “Institutional Leasehold Mortgagee under the “Ground Lease” and (2) except as specified, this acknowledgment does not amend the “Ground Lease” or extend

to any other loan.

The Certificate takes the form of a letter agreement which is executed by the "Ground Lessor," defined as the landlord under the Lease, and is addressed to GECC. The "Ground Lessor" sets forth its understanding that East Meadow intends to grant GECC a leasehold mortgage for the "Property," defined as "the Premises located at East Meadow Plaza, East Meadow, New York." It acknowledges that East Meadow is the tenant under the Lease "affecting the referenced Property," and that GECC's loan is "secured by a leasehold mortgage covering the leasehold estate created by the Lease." The "Ground Lessor" then certifies that (1) the Lease is in full and effect and has only been amended twice, (2) the Lease represents the entire agreement between the "Ground Lessor" and the "Borrower" (defined as the Lessee) about the property, (3) the "Ground Lessor" does not know of any current default under the Lease, (4) the rent and term of the Lease are as specified, (5) while the Lessee owes money to GECC, amounts payable under the Lease will be applied as set forth in the mortgage, *unless* the Lease provides otherwise, (6) the "Ground Lessor" consents to the Assignment and acknowledges that the mortgage transaction does not constitute a default under the Lease, and (7) until GECC's loan is satisfied, the "Ground Lessor" will notify GECC of any default under the Lease, and accept GECC's cure.

None of the documents described above contains any actionable misrepresentation by the Lessor that the Lease is for the Land alone. The original Lease, which of course creates and defines the leasehold interest, explicitly covers not only the Land but also the buildings "hereafter erected" on it. The Lease amendments omit the Buildings, but they do not modify the extent of the leasehold under the Lease. They merely refer to the Lease in recitals, which provide a context for the actual contractual terms but which do not constitute them. *See Hutchison v. Ross*, 262 N.Y. 381, 399 (1933).

Like the amendments, the Acknowledgment refers to the Lease in its recitals and states

that it affects property whose description does not include the Buildings. This may constitute an incorrect statement about the extent of the leasehold, but it cannot give rise to an estoppel or breach of contract claim. A plaintiff cannot invoke the doctrine of equitable estoppel against a defendant for its deception if the plaintiff with reasonable diligence could have discovered the truth. *See McGarr v. Guardian Life Ins. Co. of Am.*, 19 A.D.3d 254, 256 (1st Dept. 2005). Moreover, the plaintiff's reliance on the deception must be reasonable. *See Bank of N.Y. v. Murphy*, 230 A.D.2d 607, 608 (1st Dept. 1996).

The estoppel claim fails because GECC could have easily determined the true extent of the leasehold by reviewing the Lease. As a sophisticated business party to a \$ 13.5 million loan transaction, GECC should have examined the Lease as a matter of basic diligence. In fact, it would have been patently unreasonable for GECC to rely on the Acknowledgment without consulting the Lease, since the purpose of the Acknowledgment was to establish GECC's rights under that Lease, and the Acknowledgment referred to provisions of the Lease without quoting them.

GECC also complains that the Acknowledgment and the Certificate both refer to the Lease as a "Ground Lease," and claims that the term gave the false impression that only the Land was leased. Yet both documents defined the "Ground Lease" to mean the Lease, which granted a leasehold in the Land and the Buildings. Reasonable diligence required GECC to examine the Lease to construe the term "Ground Lease" in the Acknowledgment and the Certificate. In its motion papers, GECC points to additional statements which it characterizes as the Lessor's misdescription of the leasehold. These alleged misrepresentations cannot give rise to an estoppel claim because either the Lessors did not direct them at GECC, or the Lessors made the statements after GECC had financed Walsam's leasehold and GECC could not have detrimentally relied upon them. GECC does not refer to these alleged misstatements in the complaint.

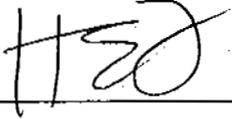
The mis-description of the leasehold in the Acknowledgment recitals cannot give rise to a breach of contract claim because, as noted above, contract recitals are not part of the parties' enforceable agreement. GECC also fails to state a claim for breach of the implied duty of good faith and fair dealing. A party to a contract cannot breach that duty merely by exercising its rights under the contract. *Murphy v. Am. Home Products Corp.*, 58 N.Y.2d 293, 304 (1983). Defendants acted within their contractual rights under the Lease, the Acknowledgment, and the Certificate by seeking a higher rent for the renewal term to maximize the return on the Property, and by requiring GECC to pay that rent in order to assume the Lease and avoid its termination.

The remaining claims for a declaratory judgment and for the imposition of an equitable trust depend on the viability of the estoppel and breach of contract claims, which have been dismissed. Accordingly, it is

ORDERED that the motion is granted and the complaint is dismissed, and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

Dated: December 20, 2006



Helen E. Freedman, J.S.C.

Check one: FINAL DISPOSITION

NON-FINAL DISPOSITION

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