

At an IAS Term, Part Comm-1 of the Supreme Court of the State of New York, held in and for the County of Kings, at the Courthouse, at Civic Center, Brooklyn, New York, on the 16<sup>th</sup> day of April, 2007.

P R E S E N T:

HON. CAROLYN E. DEMAREST,

Justice.

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PARKLEX ASSOCIATES, A NEW YORK LIMITED  
PARTNERSHIP, BY DIEDRICH K. HOLTkamp, ET AL.,

Index No. 14514/06

Plaintiffs,

- against -

PARKLEX ASSOCIATES, ET AL.,

Defendants.

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The following papers numbered 1 to 8 read on this motion:

	<u>Papers Numbered</u>
Notice of Motion/Order to Show Cause/ Petition/Cross Motion and Affidavits (Affirmations) Annexed_____	1 - 2    4 - 5
Opposing Affidavits (Affirmations)_____	3    6 - 7
Reply Affidavits (Affirmations)_____	
_____Affidavit (Affirmation)_____	
Other Papers <u>Transcript dated March 9, 2007</u> _____	8

Upon the foregoing papers in this action by Parklex Associates (Parklex), a limited partnership, brought by its limited partners (plaintiffs), alleging numerous causes of action, including fraud, breach of contract, breach of fiduciary duty, negligence, and conversion, defendants Joshua Deutsch (Joshua) and Penny Baird (Penny) move for an

order: (1) pursuant to CPLR 3211 (a) (7), dismissing plaintiffs' second amended complaint as against them, and (2) awarding them reasonable costs, including attorneys' fees incurred by them in connection with this motion, pursuant to 22 NYCRR § 130-1.1 (a). Plaintiffs cross-move for an order: (1) permitting them to file and serve a supplemental summons and a third amended verified complaint, (2) dismissing the thirty-fourth affirmative defense of defendants Fred Deutsch (Fred), Arie Deutsch (Arie), Parklex Associates, Inc. (Parklex Corporation), FAL Associates, LLC (FAL), 244 East LLC, Collateral Acquisition Corporation, Collateral Acquisition LLC, Voxonic Incorporated (Voxonic), Videosave, Inc., Videosave.com Incorporated, 32<sup>nd</sup> Street Associates, LLC (32<sup>nd</sup> Street), Citisites, Inc. (Citisites), Management Services LLC (Management), and 61<sup>st</sup> Street Associates LLC (61<sup>st</sup> Street) (collectively, the Deutsch defendants) regarding the wrap around mortgage and wrap around note and the conversion of the wrap around debt to partnership equity, and (3) granting them costs, fees, and disbursements.<sup>1</sup>

Parklex is a limited partnership, which was formed to acquire, own, and operate a 17-story (plus penthouse) office building located at 112-114 East 32<sup>nd</sup> Street, in Manhattan (the Parklex premises). The benefit of investment in Parklex, according to its

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<sup>1</sup> With respect to plaintiffs' cross motion insofar as it sought an order permitting them to amend the caption, the parties have agreed to enter into a stipulation permitting such amendment. The court, at oral argument held on March 9, 2007, denied plaintiffs' cross motion insofar as it sought an order requiring Parklex's new attorney to disclose copies of all evidence of payment from any source for his services.

private placement memorandum issued on September 30, 1983, was to provide partnership tax deductions to a limited partner's income. Parklex Corporation was Parklex's general partner, which was then owned by Bruce Ratner (Ratner), who was also Parklex's initial limited partner. In September 1983, plaintiffs became limited partners in Parklex pursuant to a limited partnership agreement (the Partnership Agreement) between them and Parklex.

On November 15, 1983, Parklex purchased the Parklex premises for \$8 million. At the closing of title, Parklex, to cover the cost of purchasing the building, executed two promissory notes and a wrap around note and wrap around mortgage (collectively, the wrap) in favor of East Side Associates, Inc. (East Side) in the amount of \$7,370,000. The wrap "wrapped" around the underlying mortgages (which totaled \$6,950,000) with the value of the wrap being \$7,370,000, thereby creating an additional \$420,000 of new indebtedness. The entire unpaid principal balance of the wrap was due and payable on October 31, 1998.

On September 25, 1991, Ascot Brokerage Ltd. (Ascot) (an entity operated by Ratner) entered into an Asset Purchase Agreement with 114 East 32<sup>nd</sup> Realty Corp., which is owned and operated by Fred. Fred claims to have acquired all of the shares of Parklex Corporation and to have become the holder of the wrap through 114 East 32<sup>nd</sup> Realty Corp. in November 1991.

On December 8, 1997, Parklex entered into a mortgage with Collateral Acquisition

Corporation. In December 1998, after the maturity date of the wrap, which then allegedly exceeded \$30 million, Fred, as the holder of the wrap, claims to have had the right to foreclose on the wrap around mortgage and extinguish the interests of Parklex in the Parklex premises. In order to avoid foreclosure, Fred claims to have converted a portion of the wrap around debt into equity, that is, a 94% limited partnership interest in Parklex. Fred then held 95% of the limited partnership (i.e., this 94% plus a 1% limited partnership interest held as the general partner). In May 2006, Fred, as the holder of this 95% limited partnership interest, sold the Parklex premises to Morgan 32 Holding, LLC (Morgan). The Deutsch defendants state that the sales price, as adjusted, was \$52,530,000, and that approximately \$33,678,000 was disbursed to Parklex's limited partners. In addition, in a reverse IRC § 1031 tax exchange, 244 East 62<sup>nd</sup> Street (the target property) was purchased by 244 East LLC.

This action was brought by plaintiffs against the Deutsch defendants, Joshua (Fred's father), Penny (Fred's wife), and others. As noted above, the Deutsch defendants include Fred, Arie (who is Fred's son), Parklex Corporation, FAL (an entity owned by Fred), 244 East LLC, Collateral Acquisition Corporation, Collateral Acquisition LLC (which pays bills on behalf of Collateral Corp.), Voxonic, Videosave, Inc. and Videosave.com Incorporated (entities owned by Fred), 32<sup>nd</sup> Street (a management company retained by the general partner to pay expenses of Parklex), Citisites (a prior management company), Management (a management company utilized to pay various

personal expenses of Fred), and 61<sup>st</sup> Street (an entity owned by Fred). By order dated December 18, 2006, the court granted a cross motion by plaintiffs for leave to file a second amended complaint. This second amended complaint asserts thirty causes of action.

In support of their instant motion, Joshua and Penny contend that the court, in its December 18, 2006 order, denied plaintiffs leave to amend their complaint to plead their proposed fourth cause of action for piercing the corporate veil against them (paragraphs 271-291 of the proposed second amended complaint). They argue that, therefore, plaintiffs should have deleted their names from the caption of the second amended complaint since there is not a single cause of action contained in the second amended complaint which is directed as against either of them. Joshua and Penny further argue that the filing of this second amended complaint, which included their names in the caption, was frivolous and warrants the imposition of sanctions against plaintiffs pursuant to 22 NYCRR § 130-1.1 (a).

With respect to this argument, the court does not find that plaintiffs' conduct is sanctionable as frivolous or in contravention of this court's December 18, 2006 order. This court, in its December 18, 2006 order, did not direct plaintiffs to remove Joshua or Penny as defendants, but merely ruled that "piercing the corporate veil" could not be pleaded as an separate independent cause of action. Thus, the motion by Joshua and Penny insofar as it seeks an award of costs and attorney's fees as sanctions pursuant to 22

NYCRR § 130-1.1 (a) must be denied.

Plaintiffs allege that subsequent to the filing of their second amended complaint, they have obtained additional documentary evidence supporting causes of action against Joshua and Penny. Plaintiffs, therefore, in their cross motion, seek permission to file a third amended complaint with five additional causes of action (their proposed thirtieth to thirty-fourth causes of action) based upon the new documentary evidence. Joshua and Penny oppose the cross motion with respect to four of these proposed causes of action (the thirtieth through thirty-third causes of action). They direct their arguments for dismissal as against these newly proposed claims.

Pursuant to CPLR 3025 (b), leave to amend a pleading should be liberally granted in the absence of surprise or prejudice resulting from the delay and where the amendment is not plainly lacking in merit or palpably insufficient as a matter of law (*see A. W. v County of Oneida*, 34 AD3d 1236, 1238 [2006]; *Hanchett v Graphic Techniques*, 243 AD2d 942, 943 [1997]). Joshua and Penny do not claim any surprise or prejudice resulting from the delay, but argue that the proposed thirtieth through thirty-fourth causes of action are lacking in merit and are palpably insufficient as a matter of law.

In support of their cross motion, plaintiffs have submitted a letter, dated January 22, 2007, from the United States Department of the Treasury, Internal Revenue Service (the IRS), informing them that Parklex has failed to file tax returns for the tax periods ending December 31, 1995 through December 31, 2005. The Deutsch defendants, in their

answer to the second amended complaint, admit that these tax returns were not filed. Plaintiffs' proposed thirtieth through thirty-third causes of action are based upon the failure of Parklex Corporation and Fred, Arie, Joshua, and Penny, who are alleged to have had complete dominion and control over Parklex Corporation, to file these tax returns. Plaintiffs state that as a result of this failure, they have not received K-1 tax statements for filing with the IRS, causing their tax returns from 1995 through 2005 to be incomplete, which may cause them to be subjected to penalties and fines.

Plaintiffs' proposed thirtieth and thirty-first causes of action allege breach of fiduciary claims against Parklex Corporation, Fred, Arie, Joshua, and Penny. Plaintiffs' proposed thirtieth cause of action asserts that Parklex Corporation, as Parklex's general partner, and Fred, Arie, Joshua, and Penny, by virtue of their complete dominion and control over Parklex Corporation, owed Parklex and them, as Parklex's limited partners, a fiduciary duty regarding Parklex's administration. Plaintiffs' proposed thirty-first cause of action alleges that Parklex Corporation, as Parklex's general partner, was appointed the Tax Matters Partner in the Partnership Agreement at § 12.08, and, as such, it had a fiduciary duty to them, as limited partners, and to Parklex, to file tax returns with the IRS. It further alleges that since Fred, Arie, Joshua, and Penny, had complete dominion and control over Parklex Corporation, they also owed this fiduciary duty to Parklex and to them, as limited partners. Both of these proposed causes of action allege that these defendants breached these fiduciary duties when they failed to file taxes for

Parklex with the IRS for the tax periods of December 31, 1995 through December 31, 2005.

With respect to the proposed thirtieth cause of action, it is well established that “a managing or general partner of a limited partnership is bound in a fiduciary relationship with the limited partnership” (*Riviera Congress Assocs. v Yassky*, 18 NY2d 540, 547 [1966]; *see also Lichtyger v Franchard Corp.*, 18 NY2d 528, 536-537 [1966]; *Friedman v Dalmazio*, 228 AD2d 549, 550 [1996]). Additionally, with respect to the proposed thirty-first cause of action, it has been held that a Tax Matters Partner has a fiduciary duty to the limited partners and the partnership (*see Transpac Drilling Venture 1982-12 v Commissioner of Internal Revenue*, 147 F3d 221, 225 [2d Cir 1998]). Thus, Parklex Corporation, as the general partner of Parklex, had a fiduciary duty to Parklex and to plaintiffs, as the limited partners (*see Riviera*, 18 NY2d at 540; *Friedman*, 228 AD2d at 550).

“[I]t is well settled that ‘[a]ny one who knowingly participates with a fiduciary in a breach of trust is liable for the full amount of the damage caused thereby’” (*Talansky v Schulman*, 2 AD3d 355, 359 [2003], quoting *Wechsler v Bowman*, 285 NY 284, 291 [1941]; *see also Fallon v Wall St. Clearing Co.*, 182 AD2d 245, 251 [1992]). “This includes an officer of a corporation who knowingly participates in a breach of the corporation’s fiduciary duties” (*Talansky*, 2 AD3d at 360).

An incumbency certificate dated May 16, 2006 lists Fred as president/treasurer and

Arie as vice-president/secretary of Parklex Corporation. However, earlier incumbency certificates, i.e., one dated May 30, 2000 and one dated May 18, 1994, are executed by Joshua as vice-president/secretary and Fred as president/treasurer of Parklex Corporation, and Penny as president/treasurer and Fred as vice-president/secretary of Parklex Corporation. Thus, according to these incumbency certificates, Joshua was the vice-president/secretary of Parklex Corporation from 2000 up to some time prior to 2006, during which time the failure to file taxes for Parklex occurred. Similarly, Penny was the president/treasurer from May 18, 1994, and may have served as such until May 30, 2000 (when Fred is listed as the president/secretary), which also encompasses the time period when the failure to file taxes for Parklex occurred. While the Deutsch defendants, Joshua, and Penny contend that these documents do not establish the exact parameters of time during which Joshua and Penny served as officers, such documents are in these defendants' exclusive possession and plaintiffs must be afforded the opportunity to obtain these documents from defendants through discovery.

The Deutsch defendants, Joshua, and Penny also assert that plaintiffs have not adequately alleged Joshua's or Penny's actual knowledge or knowing participation in Parklex Corporation's alleged breach of fiduciary duty in failing to file tax returns for Parklex, or that Joshua or Penny even knew that the tax returns had not been filed. They argue that there is, therefore, no basis for these breach of fiduciary duty claims as against

either of them.

Such argument must be rejected. At this preliminary stage of the action, the allegations of plaintiffs' complaint must be accepted as true, liberally construed, and afforded the benefit of every possible favorable inference (*see Leon v Martinez*, 84 NY2d 83, 87-88 [1994]). Plaintiffs have not yet had an opportunity to engage in discovery, including the taking of depositions, so as to ascertain the extent of Joshua's and Penny's actual knowledge and participation in the alleged breach of fiduciary duty by Parklex Corporation. Thus, the motion by Joshua and Penny is premature with respect to these proposed causes of action since plaintiffs must be given an opportunity to engage in such discovery (*see Talansky*, 2 AD3d at 360).

Plaintiffs' proposed thirty-second and thirty-third causes of action assert breach of contract claims as against Parklex Corporation, Fred, Arie, Joshua, and Penny. Plaintiffs' proposed thirty-second cause of action alleges that pursuant to the Partnership Agreement at § 12.08, which appointed the general partner as the Tax Matters Partner, and § 7.01, Parklex Corporation had a contractual obligation to file tax returns with the IRS. It further alleges that Fred, Arie, Joshua, and Penny had complete dominion and control over Parklex Corporation, so that they also had a contractual obligation to Parklex and to them, as limited partners, to file these tax returns. Plaintiffs' proposed thirty-third cause of action, alleges that in § 7.01 of the Partnership Agreement, Parklex Corporation, as Parklex's general partner, was granted "full, complete and exclusive discretion to manage

and control the business of the Partnership for the purpose herein stated and shall make all decisions affecting the business of the Partnership.” Plaintiffs allege that pursuant to this section, Parklex Corporation, and Fred, Arie, Joshua, and Penny, by virtue of their alleged complete dominion and control over Parklex Corporation, had a contractual obligation to Parklex and to them, as limited partners, to file the aforesaid tax returns. These proposed causes of action assert that these defendants breached these contractual obligations to them, causing them to sustain damages.

The Deutsch defendants, Joshua, and Penny, in opposing this amendment, point out that neither Joshua nor Penny signed the partnership agreement and were, thus, not parties to it. Generally, where a defendant was not a party to an agreement, he or she may not be held liable for breach of contract (*see Black Cart Livery Ins. v H & W Brokerage*, 28 AD3d 595, 595-596 [2006]). In addition, the Deutsch defendants, Joshua, and Penny point out that an officer of a corporation will generally not be held personally liable for a corporation’s breach of contract unless he or she purports to personally bind himself or herself thereto (*see Maranga v McDonald & T. Corp.*, 8 AD3d 351, 352 [2004]).

This limit on liability, however, only applies where the officer acted in good faith (*see First Bank of Ams. v Motor Car Funding*, 257 AD2d 287, 294 [1999]). Joshua and Penny can be personally liable for breach of contract if they, as officers, took the challenged actions on Parklex Corporation’s behalf and the breach involved bad faith misrepresentations (*see Ledy v Wilson*, \_\_\_ AD3d \_\_\_, 2007 WL 611200, \*1 [2007]; *First*

*Bank of Ams.*, 257 AD2d at 294).

Joshua and Penny further assert that these proposed causes of action would involve the piercing of the veils of two entities (i.e., Parklex and Parklex Corporation) to reach them, as officers of Parklex Corporation. They contend that these proposed new causes of action are, therefore, “repackaged versions” of the “piercing of the corporate veil” cause of action, which this court had rejected in its December 18, 2006 order. They argue that, as such, these proposed claims cannot be maintained since the court has already found them to be legally deficient.

This argument is rejected. This court, in its order dated December 18, 2006, did not make a substantive ruling on the merits of the issue of whether the corporate veil could be pierced to reach the individual defendants. Rather, as noted above, this court merely ruled that a claim for “piercing the corporate veil” could not be pleaded as a separate independent cause of action. Thus, this prior ruling has no bearing on the determination of whether the corporate veil may be pierced to reach Joshua and/or Penny.

Plaintiffs’ alter-ego/piercing of the corporate veil theory of liability is based upon their factual allegations of the exercise of complete domination and control by Fred, Arie, Joshua, and Penny over Parklex Corporation. “Veil-piercing is a fact-laden claim” that is not well suited for resolution on a motion to dismiss (*First Bank of Ams.*, 257 AD2d at 294; *see also Forum Ins. Co. v Texarkoma Transp. Co.*, 229 AD2d 341, 342 [1996]). Before dismissal can be granted, plaintiffs are entitled to obtain necessary discovery to

ascertain whether there are grounds to pierce the corporate veil (*see First Bank of Ams.*, 257 AD2d at 294; *Aubrey Equities v SMZH 73<sup>rd</sup> Assocs.*, 212 AD2d 397, 398 [1995]).

Thus, the issue of whether Fred, Arie, Joshua, and Penny so dominated Parklex Corporation so as to justify a piercing of the corporate veil is not ripe for determination at this early stage of the action (*see Ledy*, 2007 WL 611200 at \*1; *Berry Packing Corp. v Atlantic Veal Corp.*, 302 AD2d 417, 418 [2003]; *Board of Managers of Regal Walk Condominium I v Community Mgt. Servs. of Staten Island*, 226 AD2d 414, 415 [1996]; *Toroy Realty Corp. v Ronka Realty Corp.*, 113 AD2d 882, 883 [1985]).

The court finds that plaintiffs' allegations, in their proposed third amended complaint, suffice to support their claims at this preliminary stage of the proceedings. Consequently, plaintiffs should be given leave to amend their second amended complaint to assert their proposed thirtieth, thirty-first, thirty-second, and thirty-third causes of action (*see CPLR 3025 [b]*; *A.W.*, 34 AD3d at 1238).

Plaintiffs' proposed thirty-fourth cause of action alleges a claim of unjust enrichment as against Penny. Specifically, it asserts that Penny owns property located at 15 Jeffries L Arie, in East Hampton, New York (the East Hampton property), and that Parklex has paid for repairs and services for this property, and has paid for security cameras to be installed and maintained at this property. It states that Penny has received the benefit of Parklex's monies for her personal use in maintaining the East Hampton property, but has not paid Parklex for the benefit of using this money, resulting in her

unjust enrichment. Joshua and Penny do not oppose the amendment of plaintiffs' second amended complaint to assert this claim, and do not seek its dismissal. Thus, inasmuch as plaintiffs have alleged a legally viable claim for unjust enrichment (*see Lake Minnewaska Mountain Houses v Rekis*, 259 AD2d 797, 798 [1999]), a granting of leave to amend the second amended complaint to assert this claim is warranted (*see AYW Networks v Teleport Communications Group*, 309 AD2d 724, 725 [2003]).

Plaintiffs' cross motion seeks dismissal of the thirty-fourth affirmative defense set forth in the Deutsch defendants' answer, pursuant to CPLR 3211 (b), which permits a party to "move for judgment dismissing one or more defenses, on the ground that a defense is not stated or has no merit." This thirty-fourth affirmative defense alleges that if the court determines that the conversion of debt on the wrap around loan secured by the wrap around mortgage to a limited partnership interest in Parklex was invalid, then all of the net proceeds of the sale of the Parklex premises must be used to satisfy the wrap around loan, which amount exceeds the sale proceeds. The Deutsch defendants, in their amended answer to the second amended complaint, also assert a counterclaim/cross claim on behalf of 114 East 32<sup>nd</sup> Realty Corp. and Fred, as the holders of the wrap around note, for a declaration that both the principal and all accrued interest on the wrap around loan, plus legal fees, are extant and valid obligations of Parklex, and that the net proceeds of the sale of the Parklex premises must be used to satisfy the wrap around debt.

Plaintiffs, in support to their cross motion, assert that East Side, as the holder of a

wrap around mortgage which created an additional indebtedness on the property, was required to pay a mortgage recording tax pursuant to Tax Law § 258 (1) (*see Matter of First Fiscal Fund Corp. v State Tax Commission*, 49 AD2d 408, 409 [1975], *affd* 40 NY2d 940 [1976]). Despite the existence of the wrap around mortgage, however, it was never recorded with the New York County Clerk. Tax Law § 258 (1) provides that “[n]o mortgage of real property which is subject to the taxes imposed by this article shall be . . . received in evidence in any action . . . unless the taxes imposed thereon by this article shall have been paid as provided in this article.” Plaintiffs contend that the Deutsch defendants were required to pay the mortgage recording tax as a condition precedent to introducing the wrap around mortgage in this action and that since they have not paid this tax, the court is not permitted to receive the wrap around mortgage into evidence in this action for any purpose, including the defense against plaintiffs’ claims. The court notes, however, that this issue has no bearing upon the wrap around note, which is not impaired by the failure to pay a mortgage tax (*see Corey v Collins*, 10 AD3d 341, 343 [2004]).

Plaintiffs further assert that the Deutsch defendants cannot enforce the wrap as against them because the wrap is non-recourse. The Deutsch defendants, however, are not seeking a deficiency liability, but, rather, they claim that the net proceeds of the sale of the Parklex premises must be used to satisfy the wrap around debt (*see generally 56 Marquis, Inc. v Mosello*, 239 AD2d 544, 545 [1997]).

Plaintiffs also argue that the six-year Statute of Limitations of CPLR 213 (4)

precludes the Deutsch defendants from attempting to enforce the terms of the wrap since the entire unpaid principal balance of the wrap was due and payable on October 31, 1998, and this action was commenced on May 11, 2006. The Deutsch defendants, in opposition, rely upon checks paid by 32<sup>nd</sup> Street to Collateral Acquisition Corporation, which they allege were payments toward the wrap debt. They contend that every time one of these payments were made, this started the Statute of Limitations to run anew. Plaintiffs, in response, argue that the records do not demonstrate whether these payments were actually for the wrap. In addition, plaintiffs argue that there was no “payment of a portion of an admitted debt, made and accepted as such, accompanied by circumstances amounting to an absolute and unqualified acknowledgment by the debtor of more being due, from which a promise may be inferred to pay the remainder,” as is required in order to toll the Statute of Limitations (*Lew Morris Demolition Co. v Board of Educ. of City of N.Y.*, 40 NY2d 516, 521 [1976]). The Deutsch defendants, in response, argue that even if their defense is time-barred, they, under the doctrine of equitable recoupment, should nevertheless be permitted to assert their first counterclaim/cross claim based upon this defense as a set-off against plaintiffs’ claims pursuant to CPLR 203 (d).

As the parties have agreed at oral argument, however, the issue of the liability of the wrap around mortgage is premature for decision by the court at this time since the court has not yet determined the issue of whether the conversion of debt on the loan secured by the wrap around mortgage to a limited partnership interest in Parklex was

invalid. Thus, plaintiffs' cross motion, insofar as it seeks dismissal of the Deutsch defendants' thirty-fourth affirmative defense must be denied as premature at this early stage of the action. Plaintiffs' cross motion insofar as it seeks an order granting them costs, fees, and disbursements must also be denied as there is no basis for this relief.

Accordingly, the motion by Joshua and Penny for an order dismissing plaintiffs' second amended complaint, and awarding them reasonable costs, including attorney's fees incurred by them in connection with this motion, pursuant to 22 NYCRR § 130-1.1 (a), is denied as premature. Plaintiffs' cross motion is granted insofar as it seeks an order permitting them to file and serve a supplemental summons and a third amended verified complaint. Plaintiffs' cross motion is denied as premature insofar as it seeks an order dismissing the Deutsch defendants' thirty-fourth affirmative defense. Plaintiffs' cross motion is also denied insofar as it seeks an order granting them costs, fees, and disbursements.

This constitutes the decision and order of the court.

E N T E R,

J. S. C.