COPY Short Form Order

Supreme Court - State of New York
I.A.S. Term, Part 23, Suffolk County

Present:

Hon. Emily Pines
Justice Supreme Court

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DAMIANOS REALTY GROUP, LLC,

Plaintiff,

-against-

Index Number: 12550-2003

MICHAEL J. FRACCHIA, PORT JEFFERSON ORTHOPAEDICS, P.C., and LONG ISLAND BONE & JOINT LLP f/k/a PORT JEFFERSON SPECIALTY ASSOCIATES, INC.,

Defendants.

_____X

DECISION AFTER TRIAL

In this action Plaintiff-creditor seeks to recover funds from the individual and corporate Defendants based on an alleged fraudulent conveyance of assets from a defunct professional corporation against which Plaintiff obtained a money judgment in the amount of $140,195.49 on January 23, 2003. The gravamen of Plaintiff's complaint is that after Defendant Port Jefferson Orthopaedics, P.C. ("PJO") breached its lease with Plaintiff landlord, that Defendant's sole owner and shareholder, Michael J. Fracchia ("Fracchia") wrongfully removed PJO's remaining assets, including equipment and valuable accounts receivable, transferring such to himself and to his newly formed corporations, Defendants Long Island Bone & Joint, LLP and Port Jefferson Specialty Associates, Inc. without consideration in derogation of the rights of the Plaintiff. For these reasons, the Plaintiff seeks to pierce the corporate veil of PJO to collect its awarded money judgment against Fracchia personally and/or against his newly formed corporations.

The Defendants counter that there exists no basis for Plaintiff to pursue the extraordinary remedy since the contract that existed with

Plaintiff was solely between plaintiff and PJO; any transfers made from PJO to Fracchia were for valuable consideration; i.e., based on monies owed Fracchia for medical services he rendered on behalf of such corporation; and that no proof was submitted concerning transfers to the new corporations, over whom the individual Defendant does not exercise sole dominion and control. With regard to the issue of the assets transferred in the form of medical equipment, cabinets and supplies, according to Defendants, those were transferred to the new entities with the Plaintiff's express consent, upon PJO's termination of its lease with Plaintiff. Defendants also argue that Plaintiff has offered no other evidence than that submitted to the Appellate Division, Second Department, in this case, on appeal from a denial of a motion for Summary Judgment, and, therefore, Plaintiff is bound essentially by the law of the case.

Christopher Damianos, the general manager of Plaintiff, testified that he met Dr. Fracchia in 1991, when Fracchia was looking for commercial space for his orthopaedic medical practice. PJO and Damianos Realty Group, LLC, entered into a written lease agreement on January 3, 1991 (**Defendant's A**) for a five year period. Under the terms of the original lease, Fracchia signed as a personal guarantor of PJO's obligations under the agreement. Although the term of the guarantee was for five years, the provision also stated that it would not be affected by an extension of time on the lease and it also stated that the guarantee would terminate "(w)hen and if title to the Units passes to Tenant". In addition, that agreement obligated the Plaintiff to install cabinets in PJO's space, with PJO being responsible for the payment of the first $2,500 of the expense (**Defendant's A**). Thereafter, in March, 1996, Plaintiff and PJO entered into a Lease Extension and Amendment Agreement **(Defendant's B**), which extended the lease term for five years. The extension gave the tenant the option to terminate "(n)o later than one hundred twenty (120) days prior to the 2nd, 3rd, or 4th anniversary of the ... lease". The option required the tenant to notify the landlord by certified mail of the tenant's intent to vacate on either the 2nd , 3rd or 4th anniversary of the lease (**Defendant's B**). The Lease also provided that in the event the tenant did not notify the landlord in the manner and at the appropriate time of the intent to terminate, the lease would remain in effect for its full term. The extension did not contain a guarantee by Fracchia ; however, it did state that "(e)xcept as herein extended and amended, the Lease referred herein shall remain in full force and effect, and is hereby ratified and confirmed" **(Defendant's B**).

According to Damianos, he first learned of the PJO's intent to terminate the lease, when he received a letter, dated January 8, 1998 from Fracchia, exercising his "three month notice" of intent to terminate (**Plaintiff's 1**). Damianos received a second letter dated January 9, 1998, essentially reiterating PJO's intent to terminate the lease and referred to a verbal conversation the parties had on that date (**Plaintiff's 2**). He then responded by letter dated January 13, 1998 that the termination notice was of no force and effect since it was required to be given by certified mail, no later than November 1, 1997. The letter advised PJO and Fracchia that the full term of the lease was therefore still in effect (**Plaintiff's 3**). Damianos testified that when he attempted to speak to Fracchia about the issue, he was told to chase him for the money. Finally, Damianos stated that although he sued PJO and ultimately obtained a Judgment against the corporation in January 2003, all attempts to collect the Judgment have been unsuccessful.

According to Michael Fracchia, he told Damianos about his potential move when the parties entered into the lease extension and that Damianos added the early termination clauses, known as "good guy" clauses, with the understanding that PJO was likely to terminate before the end of the second five year period. He also stated that he had a good relationship with his landlord, and always paid PJO's rent in a timely manner. When he and Damianos spoke on January 9, 1998 and he told Damianos of his intent to leave within three months, Damianos accepted it and told him it would not be a problem. Although Fracchia perceived the letter of January 13, 1998 to be at odds with what he believed to be the parties' understanding, he stated that Damianos was present during the move in March 1998 and specifically told Fracchia to remove the cabinets and equipment. Thereafter, Fracchia states that PJO was sued by Plaintiff, first in an eviction proceeding in July 1998 (**Defendant's C**) which was dismissed and thereafter for the breach of the lease (**Defendant's C**). Fracchia stated he was aware that the breach of contract lawsuit against PJO resulted in a Judgment of $140,195.49 dated January 24, 2003 (**Plaintiff's 4**). Fracchia was not sued on the personal Guarantee in that lawsuit (**Defendant's D**).

In Response to a Notice to Admit, Fracchia stated that PJO ceased operations on March 31, 1998,when its principal (referring to himself) formed a new business entity. Fracchia stated that he thereafter formed Port Jefferson Specialty Associates, LLP, with another physician and that such entity ultimately became and was, as of the date of trial, Long Island Bone & Joint LLP. He asserts that the medical equipment owned by PJO was transferred to the new entity and that in return

therefore, he personally received certain benefits, including fewer "on-call" hours and the benefits of economies of scale.

It is undisputed that PJO, in April 1998, retained no assets except its accounts receivable. Fracchia testified that he used the monies that came in to PJO from April 1998 through the date of trial both to pay debts of that corporation and to pay himself, as an employee of PJO for his work as a physician. According to Fracchia, he is still owed more money than he has obtained in those receivables. As a physician, Fracchia claims he was owed money for services rendered as result of work he performed for PJO before April 1998, including seeing patients of PJO, providing surgical services for such patients, providing consults for referring physicians, and for visits to the emergency room. He states that in the period since termination of the lease, he has collected between $100,000 and $200,000 in receivables which he has awarded himself as payment for services rendered PJO. Fracchia asserts that as the sole shareholder and director of PJO, he alone decides what he is entitled to as compensation. He testified that his income from PJO was slightly less than $500,000 for 1997 and approximately $350,000 for the first three months of 1998. Fracchia, although asked, did not produce records demonstrating the services he provided for PJO , for which he asserts he is still owed funds.

The parties stipulated that PJO has collected receivables in the amount of $150,331 from April, 1998 through the present. Of this amount, Defendant states that $26,835.23 has been collected since January 1999.

Following a denial of Summary Judgment to the Plaintiff by the IAS Court (Oliver, J.) on July 21, 2005, Plaintiff herein appealed based on all the theories contained in the Complaint, including right to pierce the corporate veil, tortious interference with contract and violation of various provisions of the **NYS Debtor and Creditor Law**. In affirming the denial, the Appellate Division, Second Department, set forth that piercing the corporate veil is not suited for summary judgment and often depends on the particular facts of a case. That Court stated further that although Fracchia exercised dominion and control over PJO, "(t)he Plaintiff failed to establish, **prima facie**, that Fracchia used such dominion and control to commit a fraud or wrong against the Plaintiff which resulted in injury". Accordingly, in the view of this Court, that was the precise question left for the trial court and was to be established or not based on the facts set forth at trial.

INDIVIDUAL LIABILITY FOR A CORPORATE DEBT

The law permits the incorporation of a business for the very explicit purpose of avoiding any personal liability, and, indeed, such form is not lightly to be disregarded. **see, Ventresca Realty Corp. v Houlihan**, 28 AD 3d 537, 813 NYS 2d 196 (2d Dep't 2006). However, equity will intervene and permit the imposition of personal liability for the express purpose of avoiding fraud or injustice. **see, Matter of Morris v New York State Dept. Of Taxation & Fin.**, 92 NY 2d 135, 603 NYS 2d 807, 623 NE 2d 1157 (1993). In order to prevail on such a claim, the party seeking to pierce the corporate veil must demonstrate that: 1) the owner(s) exercised complete dominion and control over the corporation in respect to the transaction attacked; and 2) that such dominion was used to commit a fraud or wrong against the plaintiff which resulted in the plaintiff's injury. **see, Morris v State Dept. Of Taxation & Fin., supra; Letizia v Executive Coach Auto Repair**, 213 AD 2d 382, 623 NYS 2d 327 (2d Dep't 1995). On the other hand, the Plaintiff is not required to plead or prove actual fraud in order to pierce the corporate veil; but rather, that the exercise of control was utilized to commit a wrong. **see, Lederer v King**, 21 AD2d 354, 625 NYS 2d 149 (1st Dep't 1995).

In order to prove a claim of tortious interference with contract, the Plaintiff must demonstrate that: 1) a contract exists between Defendant and a third party; 2)Defendant's knowledge of the contract; 3) Defendant's intentional inducement of the third party to breach the contract; and 4) resultant damages to the plaintiff. **see, Bernberg v Health Management Systems, Inc.**, 756 NYS 2d 496 (2d Dep't 2003).

Debtor and Creditor Law §§§ 273, 274 and **275** prohibit the transfer of assets of a business without fair consideration to the extent that such transfers leave the transferring entity without sufficient capital to pay debts and render such transfers fraudulent as to present and future creditors. When such transfers are made with actual intent to defraud creditors, a violation of **Debtor and Creditor Law §276** is stated. **see, Shisgal v Brown**, 21 AD3d 845, 801 NYS 2d 581 (1st Dep't 2005).

The application of the above principals to this case requires an assessment of the parties' credibility, the one real issue left to this Court by the Appellate Division. In this vein, the Court disagrees with the argument of Defendants' counsel that the December 2006 denial of Summary Judgment essentially disposes of the case. In this Court's view, the recurring theme of the case law, stating that determinations

to pierce the corporate veil are not appropriate for summary dismissal, is an indication that allegations made by motion can be sufficient, if they are supported by credible testimony. While it is true that Fracchia exercised complete dominion and control over PJO and testified that he made the decision to terminate PJO's lease, whether he transferred the assets of PJO to himself and other creditors in order to harm the Plaintiff is less clear. This Court found credible that portion of Fracchia's testimony that related that he utilized the accounts receivable of PJO during calendar year 1998, the year that such corporation was essentially terminated, save for its general winding up tasks, in order to pay corporate creditors and to pay himself for services rendered by Fracchia to patients of the PJO medical practice. Although the Defendant did not produce documentation, he stated credibly that he had reviewed what records he had left and that from the assets of PJO, he made substantial payments in 1998 to creditors and to himself. While such transfers may have had the effect of depriving the Plaintiff of his remaining payments under the lease, they were, in this Court's view, made for legitimate purposes and for adequate consideration.

However, following the end of calendar year 1998, monies continued, albeit at a much slower pace, to continue to be collected by PJO. By that time, Fracchia had, according to his tax returns, awarded himself an income that was far higher than that of the previous calendar year. Thus, while he may believe that the monies that continued to be collected are part of his income, it is this Court's determination, that such funds were collected without adequate consideration and belong to the Plaintiff, Fracchia having testified that all other debts of the corporation were paid. At the point beginning in January 1999, the Court finds Fracchia's continued claim for such funds one not supported by credible evidence. Accordingly, this Court finds that Fracchia's transfer of $26,836.23 (collected as accounts receivable by PJO and then transferred to Fracchia), constitutes the exercise of dominion over PJO that resulted in commission of a wrong against the Plaintiff and a violation of **Debtor and Creditor Law §§ 274** and **275**. To the extent that this Decision sustains the Plaintiff's claims and allows the piercing of the corporate veil, the Court believes this case is distinguishable from **Treeline Mineola LLC v Berg**, 21 AD3d 1028, 801 NYS 2d 407 (2d Dep't 2005) and its progeny. In the case at Bar, the original Guarantee, although coextensive with the lease's five year term, specifically states that it will not be affected by an extension and also states that it will terminate only when the unit is transferred to the tenant. As set forth above, the lease extension specifically incorporates by reference all terms of the original lease to the extent not specifically amended

therein. Thus, although the Plaintiff did no sue Fracchia on the Guarantee, and such claim is long since barred by the applicable statute of limitations, the factual underpinning present in **Treeline, supra**, does not exist in this case.

There was insufficient evidence, in the Court's view, to find liability under any theory proffered against either of the corporate Defendants (other than PJO which is already subject to a Judgment). Neither entity is controlled by Fracchia and the Court found credible Fracchia's testimony that Plaintiff's general manager specifically instructed him to remove the equipment from the medical office, when PJO terminated the lease. In addition, the Court finds no evidence of intentional wrongdoing by any party, under the tortious interference claim or under the **Debtor and Creditor Law § 276.** The Court finds credible Fracchia's testimony that he believed during much if not all of 1998 that he had complied with all terms of his lease by paying for occupancy while he was present in the space and acted otherwise as a model tenant. Thus, Plaintiff failed to sustain its burden of proof with regard to either of its claims for intentional conduct.

REMEDY

Based on the above determination, the Court awards Plaintiff Judgment against the Defendant Michael Fracchia in the amount of $26,836.23 plus statutory interest from the date of the Judgment against PJO, January 24, 2003. In addition, in view of Fracchia's testimony that receivables of PJO continue to be received from time to time, although such amounts are small and rare, the Court directs, as part of the Judgement herein, that Fracchia provide an assignment of all future accounts receivable of PJO, to the Plaintiff, Damianos Realty Corp, LLC. To the extent not set forth specifically herein, all other claims of the Plaintiff are denied. This constitutes the Decision and Order of the Court. Submit Judgment on notice to Defendants' counsel, in accordance with the terms of this Decision.

Dated: May 24, 2007
Riverhead, New York

Emily Pines

EMILY PINES
J. S. C.