

**Orchard Mototcycle Distribs., Inc. v Morrison
Cohen Singer & Weinstein, LLP**

2007 NY Slip Op 32152(U)

July 11, 2007

Supreme Court, New York County

Docket Number: 0117445/2004

Judge: Doris Ling-Cohan

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

PRESENT: Hon. Doris Ling-Cohan

PART 36

Index Number : 117445/2004

ORCHARD MOTORCYCLE

vs

MORRISON COHEN LLP

Sequence Number : 005

PARTIAL SUMMARY JUDGMENT

INDEX NO. _____

MOTION DATE _____

MOTION SEQ. NO. _____

MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to/for cross-motion Summary judgment

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

Answering Affidavits -- Exhibits _____

Replying Affidavits _____

PAPERS NUMBERED

1, 2, 3, 4, 5, 6

9, 10

Cross-Motion: Yes No

7, 8

Upon the foregoing papers, it is ordered that this motion & cross-motion for Summary judgment are decided in accordance with the attached memorandum decision

FILED

JUL 18 2007

NEW YORK COUNTY CLERK'S OFFICE

HON. DORIS LING-COHAN

Dated: 7/11/07

[Signature]
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 36

-----x
ORCHARD MOTORCYCLE DISTRIBUTORS, INC.,
LEATHER AGENT, INC. and PETER FARKAS,

Plaintiffs,

- against -

MORRISON COHEN SINGER & WEINSTEIN, LLP,

Defendant.

Index No. 117445/04

Motion Seq. #005

FILED

JUL 18 2007

NEW YORK
COUNTY CLERK'S OFFICE

DORIS LING COHAN, J.:

In this action to recover damages for, *inter alia*, legal malpractice, defendant Morrison Cohen Singer & Weinstein, LLP ("Morrison Cohen"), moves, pursuant to CPLR 3212, for summary judgment dismissing the causes of action in the Amended Complaint and severing the counterclaims in its Answer. Plaintiffs Orchard Motorcycle Distributors, Inc. ("Orchard Motorcycle"), Leather Agent, Inc. ("Leather Agent"), and Peter Farkas oppose the motion and cross-move for partial summary judgment on the issue of defendant's liability on their second and third causes of action for legal malpractice. Plaintiffs also move, pursuant to CPLR 3211 and 3212, to strike defendant's seventeenth affirmative defense and dismiss its counterclaims.

BACKGROUND

The following facts are gleaned from the submissions of the parties. Orchard Motorcycle specializes in the manufacture of leather jackets for motorcyclists, military personnel, and police officers. Leather Agent is a leather tannery which provides tanned leather for use by Orchard Motorcycle and others. Peter

Farkas is the president of Orchard Motorcycle and Leather Agent, as well as the sole shareholder of both companies.

Prior to 1995, Orchard Motorcycle and Leather Agent enjoyed a mutually beneficial relationship, and both companies experienced expansion of their operations. However, on October 5, 1995, a burglary and fire caused substantial damage to Orchard Motorcycle's inventory. At the time of the burglary and fire, much of the inventory that was destroyed was needed to fulfill promotional contracts for which Orchard Motorcycle had received deposits. Although Orchard Motorcycle made timely claims under its insurance policies to recover for the loss due to the burglary and fire damage, the insurance companies disclaimed coverage. In addition, Orchard Motorcycle's available credit became further restricted, and both Orchard Motorcycle and Leather Agent experienced difficulty repaying their existing loans.

In 1996, Orchard Motorcycle and Leather Agent obtained an \$800,000 line of credit from European American Bank ("EAB") to purchase materials. Peter Farkas and his wife personally acquired the line of credit, which was secured by the assets, receivables, and inventory of the corporate debtors. Plaintiffs subsequently defaulted on the line of credit, and EAB commenced an action to collect the loan balance.

On May 29, 1996, plaintiffs retained Morrison Cohen to represent them in commencing a proceeding under Chapter 11 of the

United States Bankruptcy Code. The bankruptcy filing stayed the EAB foreclosure action.

For the remainder of 1996 and during 1997, Orchard Motorcycle and Leather Agent were able to continue their operations with reasonably healthy sales figures. For 1996, they had combined net sales of approximately \$5.3 million and combined gross profits of approximately \$1.8 million. For 1997, they had combined net sales of approximately \$4 million and combined gross profits of approximately \$.6 million. However, in 1998 and 1999, their gross profits declined to about \$200,000 each year.

Approximately four years after the burglary and fire, Orchard Motorcycle successfully challenged its insurers' disclaimer of coverage and received a settlement in the amount of \$433,130.59. Orchard Motorcycle used a portion of the insurance settlement and other resources to repay EAB.

Although their debt to EAB was satisfied, Orchard Motorcycle and Leather Agent were unable to secure third party financing to provide them with working capital. This prevented them from accepting many otherwise profitable orders.

In addition, plaintiffs could not achieve confirmations of proposed plans of reorganization. In 2002, their bankruptcy proceedings were dismissed. This action ensued.

The Amended Complaint alleges that Morrison Cohen failed to conclude the bankruptcy proceedings in a professional, proper, and competent manner, and caused them to lose suppliers and

contracts when it became known that they were in bankruptcy reorganization. Plaintiffs also accuse Morrison Cohen of paying itself legal fees from a confirmation escrow account without obtaining the requisite court approval, and failing to credit plaintiffs for erroneous payments made to itself from the confirmation escrow account. The Complaint alleges causes of action for conversion (first cause of action); legal malpractice (second cause of action); unjust enrichment (third cause of action); and rescission of the parties' retainer agreement (fourth cause of action).

Morrison Cohen answered, generally denying the allegations in the Amended Complaint, asserting numerous affirmative defenses, and alleging counterclaims for legal fees sounding in breach of contract, an account stated, and unjust enrichment. Defendant now seeks summary judgment dismissing the Amended Complaint against it and severing its counterclaims.

Plaintiffs oppose the motion and cross-move for partial summary judgment on the issue of defendant's liability on their causes of action for legal malpractice and unjust enrichment. Plaintiffs also move to strike defendant's affirmative defense that the action is barred by the applicable Statute of Limitations, and to dismiss its counterclaims.

Discussion

It is well settled that "[t]he proponent of a summary judgment motion must make a prima facie showing of entitlement to

judgment as a matter of law, tendering sufficient evidence to demonstrate the absence of any material issues of fact" (*Winegrad v New York Univ. Med. Ctr.*, 64 NY2d 851, 853 [1985]; see also *Zuckerman v City of New York*, 49 NY2d 557, 562 [1980]). Once this showing has been made, the burden shifts to the party opposing the motion for summary judgment to produce evidentiary proof in admissible form sufficient to establish the existence of material issues of fact which require a trial of the action (*Zuckerman v City of New York*, *supra* at 562). Mere conclusions, expressions of hope, or unsubstantiated allegations or assertions are insufficient to defeat summary judgment (*id.*).

As stated, the Amended Complaint alleges causes of action for conversion, legal malpractice, unjust enrichment, rescission of the parties' retainer agreement. The gravamen of the Amended Complaint is that defendant improperly withheld as legal fees fiduciary funds held in escrow for plaintiffs during the pendency of the bankruptcy proceeding, overbilled plaintiffs for unnecessary legal services, failed to obtain a discharge in bankruptcy for plaintiffs, and improperly allowed the bankruptcy proceeding to be dismissed.

Conversion is "the unauthorized assumption and exercise of the right of ownership over goods belonging to another to the exclusion of the owner's rights" (*Peters Griffen Woodward, Inc. v WCSC, Inc.*, 88 AD2d 883 [1st Dept 1982]). In order to establish a cause of action for conversion, the plaintiff must show "legal

ownership or an immediate superior right of possession to a specific identifiable thing and must show that the defendant exercised an unauthorized dominion over the thing in question, to the alteration of its condition or to the exclusion of the plaintiff's rights" (*Independent Discount Corp. v Bressner*, 47 AD2d 756, 757 [2d Dept 1975]).

Here, plaintiffs allege that defendant improperly paid itself from escrow and fiduciary funds without obtaining the necessary approval from the bankruptcy court. Plaintiffs also accuse defendant of improperly taking \$9,000 in merchandise and a \$10,000 motorcycle, which was returned a year later with a blown motor. Plaintiffs further claim that defendant failed to credit them for erroneous payments made to it from the escrow account. Plaintiffs maintain that defendant breached a fiduciary duty to them and, as such, should be compelled to make restitution for converting the funds in the confirmation escrow account to its own use.

In seeking summary judgment on plaintiffs' conversion claim, however, defendant submits copies of the Bankruptcy Court orders, dated January 13, 1997, and May 8, 2000, granting interim attorneys' fees totaling \$72,811 and expenses in the sum of \$5,741.77 to defendant (Affidavit of Jeffrey P. Englander, Exhs A, B). In addition, defendant concedes that it remitted to itself one payment in excess of what the Bankruptcy Court had authorized, due to a bookkeeping error in failing to credit a

prior payment, but insists that it is prepared to repay any funds as to which it is determined that it is not entitled to retain (¶5, Aff. Of Jeffrey P. Englander dated Sept. 11, 2006).¹

Under the circumstances, the Court concludes that defendant's actions do not amount to the unauthorized assumption and exercise of the right of ownership over goods belonging to another to the exclusion of the owner's rights so as to establish a conversion claim (see *Peters Griffen Woodward, Inc. V WCSC, Inc., supra*). As such, defendant is entitled to judgment dismissing the conversion claim as a matter of law. Plaintiffs offer no evidentiary proof to demonstrate the existence of a triable issue of fact. Thus, the first cause of action in the Amended Complaint must be dismissed.

The second cause of action alleges that defendant committed professional malpractice by failing to bring the bankruptcy proceeding to a successful and expeditious conclusion. In addition, plaintiffs allege damages, including the loss of valuable contracts and suppliers, the inability to enjoy the benefit of a discharge of the debt owed to EAB, and lost profits, as a direct result of defendant's actions and alleged malpractice.

In order to establish a cause of action to recover damages for legal malpractice, a plaintiff must show that (1) the

¹ In accordance with this issue, such issue shall be resolved in conjunction with defendant's counterclaim seeking legal fees.

attorney failed to exercise the degree of skill, care, and diligence commonly possessed by a member of the legal community; (2) the attorney's conduct was a proximate cause of plaintiff's injury or damage; (3) the plaintiff incurred damages as a direct result of the attorney's negligent actions; and (4) the plaintiff would have been successful but for the attorney's failure to exercise due care (see *Moran v McCarthy, Safrath & Carbone, P.C.*, 31 AD3d 725 [2d Dept 2006]). "A plaintiff's burden of proof in a legal malpractice action is a heavy one" (*Nazario v Fortunato & Fortunato, PLLC*, 32 AD3d 692, 695-96 [1st Dept 2006], quoting *Lindenman v Kreitzer*, 7 AD3d 30, 34 [1st Dept 2004]). "The plaintiff must prove first the hypothetical outcome of the underlying litigation and, then, the attorney's liability for malpractice in connection with that litigation" (*id.* at 695-696).

Only after the plaintiff establishes that he would have recovered a favorable judgment in the underlying action can he proceed with proof that the attorney engaged to represent him in the underlying action was negligent in handling that action and that the attorney's negligence was the proximate cause of the plaintiff's loss since it prevented him from being properly compensated for his loss.

(*id.*).

Here, plaintiffs assert that the findings of fact made by the Bankruptcy Court Judge at the dismissal hearing, coupled with the cross moving affidavit of Peter Farkas, sufficiently establish the elements of a prima facie legal malpractice claim so as to justify this Court granting summary judgment on the

issue of liability for legal malpractice against defendant. Plaintiffs urge that the Bankruptcy Court's finding should be afforded collateral estoppel effect in this action.

The Bankruptcy Court dismissed the Chapter 11 proceedings of Orchard Motorcycle and Leather Agent, finding, in essence, that the debtors had not been represented by counsel for some time; that the estate of the debtors continued to suffer losses without any reasonable likelihood of rehabilitation; and that the debtors had incurred substantial unpaid administrative and tax obligations (Transcript, dated December 18, 2001, Reply Affid on Cross Motion, Exh 10). The Farkas affidavit outlines defendant's alleged negligence, including, *inter alia*, the failure to follow instructions to initiate prompt and amicable negotiations with EAB regarding repayment of the loan; the failure to suggest a meeting between plaintiffs and EAB to propose a settlement of the EAB action to collect the loan balance; the failure to pursue dismissal of the EAB action based on improper service of process; the failure to notify plaintiffs of the commencement of actions to recover funds paid to plaintiffs' suppliers within the 90 days before the filing of the bankruptcy proceedings, which actions served to alienate plaintiffs' suppliers and cripple their daily operations; the failure to disclose monthly fees and expenses; and the filing of bankruptcy proceedings simply to stay EAB's collection litigation, without any real expectation that the plan could be confirmed (Farkas Affid, Not of Cross Motion, pp 3-10).

In seeking summary judgment on plaintiffs' legal malpractice claim, defendant argues that such claim is time-barred and, in any event, plaintiffs cannot establish that, but for its alleged actions, they would have had a favorable outcome in the bankruptcy proceedings.

To substantiate its position, defendant submits, *inter alia*, an expert affidavit from the Honorable Roy Babitt, a professor of bankruptcy law and a former United States Bankruptcy Judge (Babitt Aff, attached to Motion for Summary Judgment). The Babitt affidavit states, in part, that defendant did not depart from the appropriate standard of professional practice in representing plaintiffs in the bankruptcy proceedings (*id.* at 3). The Babitt affidavit also states that it is the obligation of the debtor company to come up with the basis of a proposed reorganization plan, including the financial basis for reorganizing (*id.* At 9-10). The affidavit further notes that the debtors' attorneys are responsible for preparing the plan documents and shepherding the proposed plan through the confirmation process, but that the attorneys cannot propose a plan, where, as here, the debtor lacks the funding to reorganize (*id.* at 10).

Defendant further argues that it cannot be held responsible for plaintiffs' inability to achieve a successful reorganization. Defendant asserts that it diligently pursued plaintiffs' interests in the bankruptcy proceedings until January 2000, when

defendant acquiesced to Mr. Farkas' request that his personal attorney, Anthony G. Bianchi, Esq., assume the function of proposing a plan of reorganization for the corporate debtors. Defendant also maintains that at plaintiffs' insistence, it simply waited for Mr. Bianchi to propose a plan. Defendant maintains that in any event, plaintiffs' legal malpractice claim must be dismissed because, plaintiffs cannot establish that their reorganization efforts would have been successful, but for its alleged actions. Defendants rely on the April 24, 2000 First Disclosure Statement, accompanying the Plan of Reorganization, also dated April 24, 2000, filed for plaintiffs by Mr. Bianchi, which details the irreversible downturn in plaintiffs' business following a burglary and fire.

Preliminarily, the Court rejects defendant's assertion that the legal malpractice claim is time-barred. The statute of limitations for a claim for legal malpractice is three years (see CPLR 214[6]). Plaintiffs filed the subject action on December 14, 2004, less than three years after the dismissal hearing on December 18, 2001 when defendant last acknowledged that it was still the attorney for the corporate debtors (Transcript, dated December 18, 2001, Reply Affid on Cross Motion, Exh 10, p. 4). Thus, the subject action was timely commenced.

Furthermore, contrary to plaintiffs' position, the ruling in the Bankruptcy Court does not have any collateral estoppel effect on the legal malpractice claim. In dismissing plaintiffs'

bankruptcy proceeding, the Court noted, *inter alia*, significant gaps in the legal representation of plaintiffs. However, the doctrine of collateral estoppel is not implicated here since there was no identity of issues which was necessarily decided in the prior action (see *Schwartz v Public Admin. of Bronx County*, 24 NY2d 65, 71 [1969]). Moreover, defendant was not a party to the bankruptcy proceeding and, thus, did not have a full and fair opportunity to contest the decision now said to be controlling (see *Weiss v Manfredi*, 83 NY2d 974, 976-77 [1994]).

Plaintiffs also fail to establish that they would have been successful in their pursuit of confirmation of a reorganization plan but for the defendant's alleged failure to exercise due care. The First Disclosure Statement, dated April 24, 2000, and the accompanying Plan of Reorganization sufficiently outline the numerous impediments to plaintiffs obtaining confirmation of their reorganization plan, wholly independent of defendant's actions. Plaintiffs' hopeless financial picture, as outlined by Mr. Bianchi in the First Disclosure Statement, undermined any efforts at reorganization. In addition, defendant's expert affidavit sufficiently established that defendant afforded plaintiffs the degree of skill commonly exercised by an ordinary member of the legal community.

As such, defendant has satisfied its burden of establishing entitlement to judgment as a matter of law dismissing the legal malpractice claim. Plaintiffs simply fail to raise any triable

issues of fact. Thus, the branch of the motion that seeks summary judgment dismissing the second cause of action must be granted.

The third cause of action essentially alleges that by reason of its alleged malpractice, defendant would be unjustly enriched if it were permitted to retain the legal fees it charged plaintiffs. The essential inquiry in any action for unjust enrichment is whether it is against equity and good conscience to permit the defendant to retain what is sought to be recovered (*Paramount Film Distr. Corp. v State of New York*, 30 NY2d 415, 421 [1972]). A party seeking to recover on the theory of unjust enrichment must allege and prove that (1) the defendant was enriched; (2) such enrichment was at the plaintiff's expense; and (3) in equity and good conscience the defendant should be required to return the money or property to the plaintiff (*New York City Economic Dev. Corp. v T.C. Foods Import and Export Co.*, 11 Misc3d 1087 [Sup Ct, Queens County 2006]).

Here, the Bankruptcy Court orders approving defendant's legal fees sufficiently establish entitlement to judgment dismissing the claim for unjust enrichment. Counsel for a debtor in bankruptcy never serves as a guarantor that a plan will be promptly filed, and counsel is entitled to compensation for its services to the debtor "[s]o long as the services are reasonably necessary to further [the] goal", which is the case whether or not the reorganization is successful" (*In re City Mattress, Inc.*,

174 B.R. 23, 26 [WD NY 1994])). Here, too, plaintiffs fail to raise any triable issues of fact. Thus, request for summary judgment dismissing the third cause of action is granted.

For the same reason, defendant is entitled to summary judgment dismissing the fourth cause of action, which seeks equitable rescission of the parties' retainer agreement and restitution to restore the parties to their original condition. Thus, defendant's motion is granted to the extent that it seeks summary judgment dismissing the Amended Complaint.

In light of the foregoing, the branch of plaintiffs' cross motion that seeks to strike defendant's affirmative defense that plaintiffs' claims are barred by the applicable statute of limitations is denied as moot.

Turning to defendant's request for severance and continuance of its counterclaims for legal fees, plaintiffs argue that the Court lacks subject matter jurisdiction over the counterclaims since they arose out of a federal bankruptcy matter. However, it is well established that upon dismissal of the bankruptcy proceedings involving plaintiffs, this Court is automatically vested with jurisdiction to entertain defendant's claims for legal fees (see *George F. Weaver & Sons. Co. v Burgess*, 7 NY2d 172, 178 [1959])). Thus, the request for severance and continuance of defendant's counterclaims is also granted, and the branch of plaintiffs' cross motion that seeks to dismiss said counterclaims is denied.

Accordingly, it is

ORDERED that defendant's motion for summary judgment is granted and the Amended Complaint is dismissed with costs and disbursements to defendant as taxed by the Clerk of the Court upon the submission of an appropriate bill of costs; and it is further

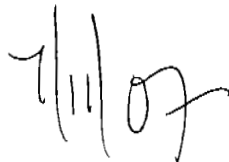
ORDERED that defendants' counterclaims for legal fees is severed and continued; and it is further

ORDERED that the cross motion is denied; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly; and it is further

ORDERED that within 20 days of entry of this order, defendant shall serve a copy upon plaintiffs with notice of entry.

Dated:



Hon. Doris Ling-Cohan, J. S. C.

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