

Rosenau Beck, Inc. v Arazi

2007 NY Slip Op 32649(U)

August 15, 2007

Supreme Court, New York County

Docket Number: 0600583/2006

Judge: Helen E. Freedman

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

PRESENT:

PART 39

Index Number : 600583/2006

ROSENAU BECK

vs

ARAZI, FRANCES

Sequence Number : 003

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 _____

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

Answering Affidavits — Exhibits _____

Replying Affidavits _____

PAPERS NUMBERED

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered that this motion

is decided in accordance with the accompanying memorandum law.

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

FILED
AUG 20 2007
NEW YORK
COUNTY CLERK'S OFFICE

Dated: 8-15-07

JEG

J.S.C.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION

Check if appropriate: DO NOT POST REFERENCE

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

PART 39

-----X
ROSENAU BECK, INC. and M ENTERPRISES TOO, INC.,

Plaintiffs/Counterclaim Defendants,

Indcx No.: 600583/06

-against-

FRANCES ARAZI and MARMELLATA CORP.,

Defendants/Counterclaim Plaintiffs,

-against-

TOM ROSENAU and BARRY RICHMAN,

Additional Counterclaim Defendants.

-----X
Helen E. Freedman, J.:

FILED
AUG 20 2007
NEW YORK
COUNTY CLERK'S OFFICE

Motion by Marmellata Corp. and Frances Arazi for partial summary judgment pursuant to CPLR 3212(e) as to portions of claims related to misappropriation of assets of an alleged joint venture is granted as set forth below. Cross motion by Rosenau Beck, Inc. and M Enterprises Too, Inc. to strike pleadings pursuant to CPLR 3126 is denied.

This is an action to recover what plaintiffs claim is their share of the assets of a dissolved children's clothing joint venture. Plaintiffs include Rosenau Beck, Inc. ("RBI"), a Pennsylvania children's clothing company, and its affiliate, M Enterprises Too, Inc. ("METI"). Defendants include Marmellata Corp. ("MAR"), a New York children's clothing company and Frances Arazi ("Arazi"), MAR's designer and its sole owner during the relevant time period. RBI and MAR manufacture children's clothes that they sell to stores including Walmart, J.C. Penny, and Target. On June 9, 1998, RBI and MAR executed the Partnership/Business Agreement signed by Arazi and RBI's owners and principals, Tom Rosenau ("Roscnau") and Barry Richman ("Richman") (the

“Business Agreement”) under which MAR designed the clothing and RBI provided financial and “back office” support. RBI characterizes its business relationship with MAR as a joint venture, but MAR deems it a financing “business arrangement.” In December 2005, MAR terminated the Business Agreement.

Plaintiffs claim that defendants wrongfully terminated the Business Agreement and that they misappropriated assets of the joint venture, including trade names and vendor numbers. The Complaint asserts causes of action for breach of contract, conversion, breach of fiduciary duty, and plaintiffs seek monetary and injunctive relief, imposition of a constructive trust, and an accounting.

With respect to the aspect of the claims relating to the misappropriation of trade names and vendor numbers, defendants move for partial summary judgment pursuant to CPLR 3212(c), contending that MAR retained ownership of its trade names and vendor numbers throughout the parties’ business relationship, whether or not that relationship constituted a joint venture, and thus it could not have misappropriated its own assets. The only way under the Business Agreement that it could have relinquished ownership of those assets is if MAR and RBI had merged. However, defendants assert that no merger occurred. MAR seeks an order declaring that (1) RBI and MAR never merged, (2) Frances Arazi is the exclusive owner of MAR, including the MAR trade names and vendor numbers, (3) MAR did not misappropriate its own trade names and vendor numbers, and (4) plaintiffs are not entitled to recover any damages arising from ownership of MAR and/or MAR’s trade names and vendor numbers, including royalties and the value of the trade names and vendor numbers.

Plaintiffs oppose the motion, contending that it is actually a tardy objection to discovery demands and is procedurally improper since plaintiffs have not alleged the existence of a merger in

their pleadings. However, plaintiffs do contend that the companies merged or “effectively merged” after the Business Agreement had been in effect for two years, and that a supplemental agreement confirms that the merger occurred and that RBI and METI obtained an interest in vendor numbers and trade names. Plaintiffs cross move pursuant to CPLR 3126 to strike MAR’s pleadings for failure to comply with its discovery requests.

As a threshold matter, defendants’ partial summary judgment motion is procedurally proper under CPLR 3212(e). That provision states that summary judgment may be granted as to “one or more causes of action, or part thereof” in favor of one or more parties. Additionally, CPLR 3212(g) provides that the Court “shall, if practicable, ascertain what facts are not in dispute or are incontrovertible” and may issue an order specifying such facts, which shall be deemed established for all purposes in the action. Although there is no specific claim in the Complaint relating to the use of trade names or vendor numbers, plaintiffs allege that defendants misappropriated assets of the joint venture including trade names and vendor numbers. The first cause of action for breach of contract, the third cause of action for conversion, and the fourth cause of action for breach of fiduciary duty are all based, in part, on plaintiffs’ allegation that defendants misappropriated assets of the joint venture, and plaintiffs allege that those assets include trade names and vendor numbers. Thus, defendants’ partial summary judgment motion relates to portions of the first, third, and fourth causes of action.

Background:

The extent of the parties’ business relationship and the relevant agreements are described below.

The purpose of the 1998 Business Agreement was “to finance the orders held by MAR and

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develop an ongoing business initially as a division of Roscnau Beck (NMAR).” Under the Business Agreement, MAR operated a sales, design, and production company, and RBI paid MAR’s weekly expenses based on bills due or paid as transmitted by MAR. MAR was entitled to 33.3% of NMAR’s profits, and RBI was entitled to 66.6% of the profits. RBI was also entitled to an interest reimbursement at rate of 10% or prime plus 2.5%, whichever was greater, for all funds it invested.

With respect to MAR’s trade names and vendor numbers, the Business Agreement provided that

MAR will license to RBI the right to use all trade names and will allow the use of MAR’s vendor numbers necessary for the sole purpose of producing orders that now exist or future orders generated that are expected to be produced by NMAR.

If the business relationship terminated within the first 1.5 to two years, MAR would retain all trade names and vendor numbers that it owned prior to execution of the agreement. MAR’s trademarks and vendor numbers remained MAR’s sole property except that

After 1.5 to 2.0 years or sooner if all parties agree, the parties will merge the NMAR division of RB and the MAR operations. Such company will be owned 33.3% by MAR or their [sic] assign and 66.6% by RB or their [sic] assign. At the merger date the partners will provide cash contributions equal to their equity interest and the balance of the financing will come from loans. (no free book value is created to and no dilution of book value will occur to any partner). After this merger all trade names previously owned by MAR will become the common property of the new company created by the merger.

The Business Agreement did not contain a termination provision.

In October 2003, RBI and other companies that Richman owned restructured. METI formed with Richman as its sole owner. At that time, RBI executed factoring and security agreements with Capital Factors, Inc. (“Capital Factors”) in order to finance RBI’s manufacture, purchase, and sale of inventory, including inventory bearing the “Marmellata” name. MAR consented to these factor and security agreements in a letter agreement addressed to Capital

Factors dated October 22, 2003 (“the Supplemental Agreement”). The Supplemental Agreement referenced the Business Agreement, stating that it gave RBI the right to use inventory bearing Marmellata’s name, and it provided that MAR “agreed to permit RBI to assign any and all of its [sic] rights under the Business Agreement to RBI’s affiliate, ... METI such that as of said date, METI has the exclusive right to manufacture and sell Articles bearing the [Marmellata] Trademark.”

In a letter dated October 22, 2003, Arazi as President of MAR wrote a letter to Richman stating that she was willing to sign the Supplemental Agreement “as long as you agree that signing their letter and agreeing to their terms in no way changes or redefines our (Marmellata Corp. and Roscnau Beck) existing arrangement.” Richman, RBI’s Chief Executive Officer, signed that letter.

On December 7, 2005, MAR sent one letter to Richman and Roscnau and one letter to Capital Factors, informing them that MAR was terminating the Business Agreement as of December 9, 2005. In the letter to RBI’s principals, MAR claimed ownership of all of its intellectual property, including trade names and vendor numbers, and stated that RBI had outstanding payment obligations to MAR. The letter to Capital Factors stated that Capital Factors could no longer benefit from RBI’s rights under the Business Agreement and that MAR withdrew the consent that it had provided in the Supplemental Agreement.

In a letter dated December 22, 2005 in response to the termination letter, counsel for RBI, Rosenau, Richman, and METI stated that Arazi and MAR “certainly have the right to terminate the Agreement, but there is no basis for them to claim to be relieved of any further obligations under the Agreement and expect METI to ‘make all payments in connection with any merchandise

shipped prior to December 9, 2005.” The letter also provided that the joint venture’s assets would be distributed according to the 66.66% and 33.33% split pursuant to the Business Agreement. Plaintiffs understood that the joint venture’s assets consisted of the following: (i) projected net income for the first quarter of 2006, (ii) partnership inventory, (iii) prepaid commissions to Bill Sloe, which equals \$100,000, (iv) personal property including office furniture and equipment, and (v) a lease security deposit.

Contentions:

MAR contends that it could not have misappropriated trade names and vendor numbers that it owned and that it never transferred to plaintiffs. MAR asserts that, under the Business Agreement, a transfer would only occur if a merger between it and RBI was consummated. However, MAR and RBI never fulfilled the contractual prerequisites to a merger of contributing capital to a new entity and actually forming a new entity. MAR contends that plaintiffs’ December 22, 2005 letter, which listed what plaintiffs considered to be assets of the joint venture, further establishes that MAR retained ownership of its trade names and vendor numbers because that letter made no mention of trade names and vendor numbers. Even if the parties had intended to merge and had fulfilled the contractual prerequisites to merger, there is no evidence of compliance with Article 9 of the New York Business Corporation Law or of actions that would amount to a “de facto” merger.

Plaintiffs contend that the merger provision in the Business Agreement establishes that the parties automatically merged after the Business Agreement had been in effect for two years. Although Richman acknowledges that no shares of stock were exchanged and no new entity was formed, he contends that an “effective” merger occurred because the parties acted as though they

were a single entity.

Discussion:

The first issue is whether the parties created a contractual obligation to merge. A contract must be read as a whole, and “single clauses cannot be construed by taking them out of their context and giving them an interpretation apart from the contract of which they are a part.” *Bijan Designer for Men, Inc. v. Fireman’s Fund Insurance Co.*, 264 A.D.2d 48, 51 (1st Dept. 2000) citing *Atwater & Co. v. Panama R.R. Co.*, 246 N.Y. 519 (1927). Here, when read in its entirety, the Business Agreement stated that as prerequisites to a merger, the parties were obligated to form a new entity and each contribute capital to that entity. That did not happen. Merely setting forth a date for a merger to occur was insufficient without the capital contribution to effect the merger. Under the Business Agreement, MAR’s trade names and vendor numbers would not be transferred until the merger was consummated.

The Supplemental Agreement, executed four and a half years after the Business Agreement, if anything, confirmed that the parties did not merge and continued to function as separate entities. Plaintiffs contend that that agreement demonstrates that MAR transferred its assets to METI, relying upon the provision that states that MAR would permit RBI to assign the rights that it had under the Business Agreement, a license to use MAR’s trade names and vendor numbers, to METI. However, the Supplemental Agreement does not demonstrate any asset transfer. First, if, as plaintiffs contend, the companies had automatically merged two years after the Business Agreement was executed, MAR’s consent to an assignment to METI of RBI’s rights under the Business Agreement would be superfluous. Second, since RBI could only assign to METI the rights that it had, and it only had a license to use trade names and vendor numbers for

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a limited purpose, the Supplemental Agreement does not provide for a transfer of MAR's trade names and vendor numbers to METI. The December 7, 2005 termination letters clearly revoked any earlier license MAR had given to RBI and METI to use MAR's trade names and vendor numbers.

In addition to the absence of a bilateral intent to merge, the parties have not complied with the merger provisions of Article 9 of the New York Business Corporation Law. The BCL procedures include adoption of a plan to merge by each corporation's board of directors (§ 902), followed by a shareholder vote on the plan (§ 903). Corporations must then execute a certificate of merger on behalf of each constituent corporation to be delivered to the Secretary of State, (§ 904) after which all of the property, real and personal, shall vest in the surviving corporation. (§ 906(b))¹

Alternatively, courts have recognized the concept of "de facto merger." Factors that establish a de facto merger are set forth in *Washington Mutual Bank, F.A. v. SIB Mortgage Corp.*, 21 A.D.3d 953 (2nd Dept. 2005). They include (1) continuity of ownership, (2) cessation of ordinary business and dissolution of the predecessor as soon as possible, (3) assumption by the successor of the liabilities ordinarily necessary for the uninterrupted continuation of the business of the acquired corporation, and (4) a continuity of the management, personnel, physical location, assets, and general business operation. Here, RBI, METI, and MAR remained separate legal

¹ A merger between a foreign (non-New York) and a domestic corporation must comply with the laws of the corporations' respective jurisdictions. BCL § 907. Neither party has submitted evidence of compliance with either New York's or Pennsylvania's merger laws. Under Pennsylvania law, a domestic and foreign (non-Pennsylvania) corporation may merge into a surviving corporation or consolidate to form a new corporation. 15 Pa.C.S.A. § 1921. A plan of merger adopted by a shareholder vote is required. 15 Pa.C.S.A. §§ 1922 and 1924. The articles of merger or consolidation must be filed with the Department of State. 15 Pa.C.S.A. § 1926.

entities, operated in separate places, and neither one assumed the liabilities of other. RBI, METI, Richman, and Rosenau never owned MAR shares.

Plaintiffs' reliance on *Decker, Decker & Associates, Inc. v. Association of Nat. Advertisers, Inc.*, 15 Misc.3d 1117(A) (Sup. Ct. N.Y. Cty. 2007) is misplaced. In that case, the Court denied a motion to dismiss plaintiff's claim that it and defendant formed a magazine publishing joint venture entitling plaintiff to a portion of the magazine's profits. Ownership of the magazine's intellectual property was not at issue because the relevant agreement provided that the defendant, the party that terminated the agreement, retained ownership of it. While the joint venture issue is relevant to the underlying claims, the issue here is whether MAR and RBI merged and not whether they operated a joint venture. Plaintiffs' claim that a joint venture existed, entitling plaintiffs to two thirds of the profits from the Sprint 2006 season, is separate from the issue of a corporate merger that transferred MAR's trade names and vendor numbers to a merged entity.

Cross Motion:

Plaintiffs' cross motion to strike defendants' pleadings for failure to comply with discovery requests is denied. Defendants have responded to plaintiffs' interrogatories. Plaintiffs seek documents from non-parties Dalk Enterprises, Inc., MAR's manufacturer, and Westgate Financial Corporation, MAR's factor, and plaintiffs seek MAR's damages calculation from MAR's accountant. In a decision dated July 26, 2007, this court already granted the motion to compel production from Dalk "to the extent that the documents exist." Defendants' accountant Stewart Farber attests in his May 22, 2007 affidavit that he would complete his report in July 2007. Thus, many of the issues raised in plaintiffs' cross motion may be moot, and it does not

appear that defendants have "wilfully fail[ed] to disclose," CPLR 3126.

Conclusion:

Because the parties never merged, MAR retained ownership of its trade names and vendor numbers. Accordingly, it is

ORDERED that defendants' motion for partial summary judgment is granted to the extent that the following facts are deemed established in this action:

- (1) RBI and MAR never merged;
- (2) MAR retained ownership of its trade names and vendor numbers; and
- (3) MAR did not misappropriate its own trade names and vendor numbers; and it


is further

ORDERED that plaintiffs' cross motion is denied.

Parties are directed to appear for a status conference in Room 208 on August 21, 2007 at 9:30 a.m. as previously scheduled.

DATED: August 15, 2007

ENTER:



 Helen E. Freedman, J.S.C.

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 AUG 20 2007
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