

<b>Broyhill Furniture Indus., Inc. v Hudson Furniture Galleries, LLC</b>
2008 NY Slip Op 30636(U)
February 28, 2008
Supreme Court, New York County
Docket Number: 0109506/2005
Judge: Herman Cahn
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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: Cahn  
Justice

PART 49

Index Number : 109506/2005  
BROYHILL FURNITURE INDUSTRIES

INDEX NO. 109506/05

vs  
HUDSON FURNITURE GALLERIES

MOTION DATE \_\_\_\_\_

Sequence Number : 001

MOTION SEQ. NO. 1

SUMMARY JUDGMENT

MOTION CAL. NO. \_\_\_\_\_

is motion to/for \_\_\_\_\_

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

PAPERS NUMBERED

Answering Affidavits — Exhibits \_\_\_\_\_

Replying Affidavits \_\_\_\_\_

Cross-Motion:  Yes  No

Upon the foregoing papers, it is ordered that this motion

**MOTION IS DECIDED IN ACCORDANCE  
WITH ACCOMPANYING MEMORANDUM  
DECISION IN MOTION SEQUENCE.....**

**FILED**

MAR 07 2008

NEW YORK  
COUNTY CLERK'S OFFICE

Dated: February 28 2008

[Signature]

J.S.C.

Check one:  FINAL DISPOSITION  NON-FINAL DISPOSITION

Check if appropriate:  DO NOT POST  REFERENCE

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 49

-----X  
BROYHILL FURNITURE INDUSTRIES, INC.,

Plaintiff,

-against-

Index No. 109506/05

HUDSON FURNITURE GALLERIES, LLC,  
MICHAEL D. ROSENFELD, EDWARD  
ROSENFELD and HUDSON UNITED BANK,

Defendants.

**FILED**  
MAR 07 2008  
NEW YORK  
COUNTY CLERK'S OFFICE

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**HERMAN CAHN, J.:**

Defendants Michael D. Rosenfeld, Edward Rosenfeld (the Rosenfeld Defendants), and Hudson Furniture Galleries, LLC (HFG) (together with the Rosenfeld Defendants, the Hudson Defendants) move for partial summary judgment dismissing eight of the eleven causes of action in the complaint, and the cross-claims asserted against them, CPLR 3212.

TD Banknorth, N.A. (Banknorth), as successor by merger to defendant Hudson United Bank (HUB), cross-moves for summary judgment as to liability on its cross-claims against the Hudson Defendants.

**Background**

This action arises out of a series of secured transactions entered into between plaintiff Broyhill Furniture Industries, Inc., a furniture manufacturer, and HFG, a retail furniture business owned, managed and operated by the Rosenfeld Defendants, and between HFG and HUB, a bank. Broyhill and HUB obtained security interests in the same collateral.

Defendant HFG was previously known as IFR Hudson Valley LLC (IFR).

On December 20, 2002, IFR executed a note and security agreement with HUB, and the Rosenfeld Defendants personally guaranteed (Guaranties) the obligations contained therein (Compl, ¶¶ 52-55). On January 2, 2003, HUB filed a blanket UCC financing statement reflecting the creation of a security interest in all of the inventory and assets of IFR (*id.*).

Around this time, IFR and Broyhill began negotiations concerning the sale of Broyhill merchandise to IFR. A draft security agreement was circulated and the manager of Broyhill's credit department, Chris Canipe, inquired as to the status of Broyhill's prospective security interest vis-a-vis other secured creditors. On October 31, 2003, Canipe sent a letter to IFR that stated, "please check with your bank [HUB] to make sure that we [Broyhill] have first lien on the Broyhill product. If so, we ask that you sign [the security agreement] and return to us for filing" (Rosenfeld Aff, Exh D). Shortly thereafter, IFR returned an executed copy of the security agreement to Broyhill (Feinberg Aff, ¶ 4; Rosenfeld Depo Tr, 12:8-17).

Subsequently, on November 24, 2003, IFR changed its name to HFG, and filed with the Secretary of State a Certification of Amendment reflecting the name change (Canipe Aff, ¶ 6). Broyhill learned that IFR changed its name to HFG, and requested a revised security agreement. On January 28, 2004, HFG and Broyhill executed the revised security agreement (Security Agreement), that granted to Broyhill a purchase money security interest in all of the merchandise (Merchandise) that HFG acquired from Broyhill, in addition to all proceeds of the sale of the Merchandise (Compl, ¶ 5-10; Canipe Aff, Exh 6). The Security Agreement states that with the exception of Broyhill's, the Merchandise is not subject to any other security interest (Security Agreement, § 3 [b]).

Broyhill alleges that at this time, it conducted a UCC search of filed financing statements

to discover if there was a conflicting security interest filed against HFG. The search did not turn up any other filings. Broyhill did not conduct a search of financing statements filed under the debtor name of IFR (Canipe Aff, ¶¶ 14, 17).

On February 17, 2004, Broyhill filed a financing statement, reflecting its purchase money security interest in the Merchandise and proceeds from the sale of the Merchandise as collateral (*id.* at ¶ 6).

Between January 28, 2004 and February 15, 2005, Broyhill supplied HFG with Merchandise totaling \$228,104.58, pursuant to the Security Agreement (*id.* at ¶ 2).

On March 22, 2004, HFG executed an additional note with HUB (together with the note and security agreement, the Loan Documents), followed by the filing of an additional UCC financing statement reflecting its security interest therein.

In the following months, HFG began to experience financial difficulties. In October of 2004, HFG conducted a "cash-raising" sale of furniture. Thereafter, the Hudson Defendants conducted a "going-out of business" sale (the Sale), in an effort to liquidate its entire inventory of merchandise. Edward Rosenfeld testified that Broyhill Merchandise had approximately \$105,000 to \$120,000 of inventory on hand during the Sale (Rosenfeld Depo Tr, 58:6-11). According to Broyhill, a substantial amount of cash was raised at the Sale.

From December of 2004 through March of 2005, HFG transferred \$220,00.00, the proceeds of the Sale, to HUB, in an attempt to satisfy a portion of HFG's debt to HUB. Meanwhile, HFG defaulted under the Security Agreement, the entire balance of which remains outstanding.

On July 11, 2005, Broyhill commenced this action. In the complaint, Broyhill pleads

eleven causes of action, including breach of contract against HFG for the unpaid balance of the Merchandise and for attorney's fees under the Security Agreement. Additionally, Broyhill pleads three causes of action for fraudulent conveyance against the Rosenfeld Defendants for violation of Debtor and Creditor Law sections 272, 274 and 276, tortious interference with contract, breach of fiduciary duty, violation of Limited Liability Company Law (LLCL) section 704 based upon improper corporate distributions, conversion, and seeks punitive damages and attorney's fees pursuant to DCL section 276-a. Broyhill additionally seeks to pierce Hudson's corporate veil in order to hold the Rosenfeld Defendants jointly and severally liable.

On July 22, 2005, HUB commenced an action against the Rosenfeld Defendants and IFR/Acorn Realty, LLC (a non-party co-guarantor of the loans) in the United States District Court for the Southern District of New York (SDNY Action), seeking to enforce the Guaranties after HFG defaulted under the Loan Documents. In November of 2005, the action was resolved pursuant to a written settlement agreement (Settlement Agreement). Pursuant to the Settlement Agreement, the Rosenfeld Defendants agreed to pay Banknorth \$147,500, plus interest and attorney's fees.

In August of 2006, Broyhill added HUB as a co-defendant in this action, seeking a declaration that Broyhill's security interest in the Merchandise has priority over HUB's, and directing HUB pay to Broyhill the proceeds of the Sale that HUB received from HFG.

In its answer dated September 22, 2006, HUB asserts cross-claims for breach of contract against HFG based on the Loan Documents, and for breach of the Guaranties against the Rosenfeld Defendants, seeking costs of collection and attorney's fees, in addition to implied indemnification based upon unjust enrichment and contribution in the event that HUB is found to

be liable to Broyhill.

### Discussion

#### I. Hudson Defendant's Motion for Summary Judgment; UCC Filing Priority

The Hudson Defendants move for summary judgment dismissing the eight causes of action of the complaint wherein Broyhill alleges wrongdoing on their part for transferring the proceeds of the Sale to HUB. The Hudson Defendants maintain that HFG was legally entitled and obligated to transfer these funds in order to partially satisfy HFG's obligations to HUB under the Loan Documents, because HUB's security interest in HFG's assets, that included the Merchandise, has priority over Broyhill's security interest. They argue that Broyhill failed to perfect its security interest in the Merchandise because it did not comply with UCC § 9-324, the section that sets forth the rules for establishing priority over a conflicting security interest in the same collateral.

In opposition, Broyhill contends that it was not obligated to comply with the requirements of UCC § 9-324 in order to achieve priority over HUB's security interest in the Merchandise. Broyhill argues that IFR's name change to HFG, which occurred on November 24, 2003, rendered HUB's financing statement "seriously misleading," under UCC § 9-506, and triggered HUB's affirmative duty to amend its financing statement to reflect the name change in order to preserve its financing statement as to Merchandise acquired by HFG more than four months after the name change, under UCC § 9-507 (c).

Consequently, Broyhill argues that HUB's significant delay in amending its financing statement results in the lapse of perfection of its security interest for Merchandise acquired by HFG more than four months after changing its name, and the automatic advancement of

Broyhill's perfected security interest over HUB's, as of March 24, 2004, the end of the four-month grace period established by UCC § 9-507 (c).

Alternatively, Broyhill argues that HFG should be estopped from denying that HUB's security interest has priority over Broyhill's, thereby entitling Broyhill to the return of the proceeds from the Sale from HUB, because HFG allegedly represented to Broyhill that it would have priority over HUB. In addition, the Security Agreement contains a provision that states that no other security interest exists in the Merchandise (Security Agreement, § 3 [b]). According to Broyhill, it reasonably relied upon these representations, and substantially changed its position by entering into the Security Agreement.

The Hudson Defendants and HUB attempt to defeat Broyhill's contention that HUB was required to re-file or amend its financing statement following IFR's name change in order to preserve the perfection of its earlier-filed security interest, or that Broyhill detrimentally relied on the representations, by submitting evidence attempting to establish that Broyhill had actual notice that HFG was previously known as IFR, and that HUB had a security interest running in its favor vis-a-vis IFR.

For the reasons stated below, Broyhill's security interest achieved priority as of March 24, 2004. However, issues of fact remain as to whether Broyhill's security interest attached to the proceeds of the Sale. Therefore, the Hudson Defendants' motion for summary judgment is denied in part, and granted in part.

#### A. Priority of Security Interests

The enforcement of Broyhill's security interest in the Merchandise is governed by Article 9 of the UCC (UCC § 9-102 [1] [a]). Under the UCC, filing a financing statement is necessary in

order to perfect a security agreement (UCC § 9-310 [a]), with several exceptions. The UCC distinguishes “perfection” of a security interest from “attachment.”<sup>1</sup> The date of perfection of the security interest is the date from which priority is measured vis-a-vis other perfected secured creditors: the secured party which first perfects its security interest is deemed to have the senior interest (UCC 9-322 [a] [1]; *Fleet Factors Corp. v Bandolene Indus. Corp.*, 86 NY2d 519, 523 [1995]).

It is undisputed that HUB’s security interest was perfected prior to Broyhill’s; HUB filed on January 2, 2003 a blanket financing statement covering the assets and inventory of IFR as collateral (Canipe Aff, Exh 3). Broyhill’s security interest became perfected on February 17, 2004, when it filed a financing statement establishing a purchase money security interest in the Merchandise (Rosenfeld Aff, Exh F).

Although the holder of an earlier-filed security interest is deemed to have priority over later filed secured parties, the holder of a purchase money security interest can achieve priority over an earlier-filed security interest in the same collateral by complying with the procedures set forth in the UCC, including by providing written notification to the holder of the earlier-filed security interest indicating that the purchase money security interest holder intends to obtain a conflicting security interest in the same collateral (UCC § 9-324 [b]). Consequently, Broyhill, as a purchase money security interest holder in the Merchandise, could have immediately obtained priority over HUB’s security interest in the same collateral, had Broyhill complied with these

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<sup>1</sup> The UCC sets forth the steps a party must take to create an Article 9 security interest, in order to render it enforceable against the debtor and third parties (UCC § 9-203). A security interest becomes enforceable against the debtor when it “attaches,” value has been given to the debtor, the debtor has rights in the collateral, and has “authenticated a security agreement that provides a description of the collateral” (UCC § 9-203 [a], [b]).

procedures. However, Broyhill did not do so, either prior to the temporary perfection of its security interest when it made the Merchandise available to HFG for sale on January 28, 2004 (UCC 9-312 [f]), or prior to filing of its financing statement on February 17, 2004.

Broyhill maintains that prior to the perfection of its security interest and the filing of its financing statement, it conducted a UCC search of the name HFG, which search did not disclose the existence of any other security interest filed against HFG. HUB acknowledges that it did not amend its financing statement to reflect the name change, until February 1, 2005. Thus, Broyhill argues that because its UCC search of filed financing statements did not reveal any conflicting security interest, the procedures set forth in UCC § 9-324 are irrelevant to the determination of the respective secured parties' priority at this juncture. According to Broyhill, the perfection of HUB's earlier-filed security interest automatically lapsed as to new collateral acquired by HFG more than four months after IFR's name change, by HUB's significant delay in amending its financing statement, thereby resulting in the advancement of Broyhill's security interest over HUB's as of March 24, 2004, under UCC § 9-507 (c).

The Hudson Defendants argue that Broyhill had actual knowledge of IFR's name change to HFG and that IFR had an existing loan with HUB. This, it is asserted, defeats Broyhill's contention that HUB's failure to amend its financing statement, to reflect the name change, results in the lapse of perfection of its security interest in the collateral. Further, Broyhill's failure to comply with UCC § 9-324 defeated the advancement of its security interest over HUB's.

The defendants' interpretation of UCC § 9-324 is correct to the extent that Broyhill would have obtained priority over HUB's security interest for all of the Merchandise, had it complied

with the notification procedures set forth therein. However, the application of UCC § 9-324 in isolation, as the defendants urge, does not properly take into consideration the effect of IFR's name change to HFG, and its impact on the perfection of its security interest, as reflected in its financing statement.

#### B. The Effect of Debtor's Name Change on a UCC Financing Statement

A change in a debtor's name will not affect the perfection, and corresponding priority, of a creditor's security interest in collateral acquired prior to the name change (*Fleet Factors Corp.*, 86 NY2d at 524-25). However, a secured party is required to re-file or amend its financing statement upon a debtor's name change, if the name change renders the filed financing statement "seriously misleading," and the debtor obtains collateral more than four months after the name change, in order to preserve perfection with respect to the goods acquired more than four months after the name change (UCC § 9-507 [c]; *Fleet Factors Corp.*, 86 NY2d at 519, 524-25; White and Summers, Uniform Commercial Code, § 31-19 at 212-13 [4<sup>th</sup> ed]). Thereafter, a secured party's failure to re-file or amend its financing statement renders the financing statement "not effective to perfect a security interest in collateral" (UCC § 9-507 [c]), irrespective of the secured party's awareness thereof (*Fleet Factors Corp.*, 86 NY2d at 524-25).

The parties do not dispute that HFG acquired collateral from Broyhill more than four months after IFR changed its name to HFG.<sup>2</sup> Neither do the parties dispute that HUB only amended its financing statement to reflect IFR's name change more than a year after the name

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<sup>2</sup> Broyhill alleges that of the \$228,104.58 balance due from HFG, approximately \$195,101.31 was for merchandise delivered to HFG by Broyhill subsequent to March 24, 2004 (Canipe Aff, ¶ 3). The Hudson Defendants do not dispute this figure; rather, they dispute the quantity of the Merchandise that was disposed of during the Sale (Rosenfeld Aff, ¶¶ 15-16).

change occurred on November 24, 2003 (Exhibit 9, annexed to the Affidavit of Chris Canipe).

The issue that necessarily arises is whether HUB's security interest, reflected in an unamended financing statement, takes priority as to collateral acquired by HFG more than four months after its name change. Additionally, the issue involves the situation where Broyhill, the subsequent security interest holder, did not comply with UCC § 9-324 and may have had actual knowledge of the debtor's name change.

The UCC provides a clear answer. IFR's name change to HFG rendered HUB's financing statement "seriously misleading," insofar as it did not sufficiently provide the name of the debtor (UCC § 9-506 [b]). In light of HFG's acquisition of collateral more than four months after changing its name, HFG was under an affirmative duty to re-file or amend its financing statement to reflect the debtor's name change, no later than March 24, 2004, four months to the date that the name change occurred (UCC § 9-507 [c]; *Fleet Factors Corp.*, 86 NY2d at 524). HUB's failure to amend its financing statement until February 1, 2005, renders its financing statement unperfected as to collateral acquired by HFG as of March 24, 2004 and later (UCC § 9-507 [c]). Consequently, as of March 24, 2004, Broyhill's security interest advanced in priority over HUB's (*see* UCC § 9-322 [a] [2] ["A perfected security interest . . . has priority over a conflicting unperfected security interest;" *see also* UCC § 9-317; UCC § 9-308, Comment 4]).

Broyhill's failure to comply with UCC § 9-324, and its alleged actual knowledge of the name change, is of no moment. Neither Article 9 of the UCC, nor the cases cited by defendants, suggest that a subsequent potential creditor's actual knowledge of a debtor's name change or knowledge of another creditor's existence relieves a secured party of its affirmative duty to re-file or amend its financing statement to preserve the perfection of its security interest as to collateral

acquired by the debtor more than four months after its name change (*see Fleet Factors Corp.*, 86 NY2d at 524-25; *compare P.T. Bank Cent. Asia v Chinese Am. Bank*, 229 AD2d 224, 231-34 [1<sup>st</sup> Dept 1997] [where a senior creditor's security interest partially lapsed by operation of UCC § 9-501, formerly UCC § 9-401, due to its failure to timely file a continuation statement in one of the two offices where filing was required. As a result of its good faith submission of the wrong documents, under the good-faith exception to the dual-filing requirement contained in UCC § 9-501, the senior creditor's second filing of the continuation statement in compliance with the requirements of Article 9, was effective against the junior creditor's interest, where the junior creditor had actual knowledge of the senior creditor's security interest in the collateral]).

However, unlike *P.T. Bank Cent. Asia v Chinese Am. Bank* (229 AD2d at 231-34), where only one of two filings of the senior creditor's security interest had lapsed in a dual-filing jurisdiction under UCC § 9-501, the perfection of HUB's security interest lapsed entirely, under the express language of UCC § 9-507 [c]. This section does not contain any language that could be construed as exempting the duty to amend a financing statement, even against a person who had actual knowledge of the name change. Thus, Broyhill's claimed actual knowledge of the name change does not relieve HUB of its affirmative duty to re-file or amend its financing statement for after-acquired collateral, under UCC § 9-507 (c).

In any event, even if the degree of Broyhill's knowledge of IFR's name change was relevant in the determination of whether HUB's affirmative duty to amend could appropriately be dispensed with as against Broyhill, the Hudson Defendants neither allege nor raise an issue of disputed fact that Broyhill had actual knowledge of the contents of HUB's financing statement. Thus, even assuming that Broyhill had both actual knowledge of IFR's name change to HFG, and

of IFR's existing loans with HUB, such knowledge would likely be insufficient to alter HUB's obligations to re-file under Article 9 of the UCC, as to Broyhill. Rather, Broyhill's knowledge would likely have to rise to the level of actual knowledge of the contents of HUB's filed financing statement, and not merely knowledge that HUB is a secured creditor vis-a-vis HFG (*compare Enark Indus., Inc. v Bush*, 86 Misc 2d 985, 987 [2d Dept 1976] [junior creditor does not become a superior creditor where the senior creditor failed to perfect its security interest as the result of an improper filing, where the junior creditor had actual knowledge of the contents of the senior creditor's improperly filed financing statement. On the other hand, mere knowledge of the existence of the security agreement on the part of the junior creditor would have been insufficient.]).

### C. Estoppel

Although Broyhill achieved priority over HUB as to collateral acquired by HFG subsequent to March 24, 2004, as above stated, an issue exists as to whether Broyhill's security interest achieved priority over HUB as to an earlier date, due to its reliance upon HFG's alleged representations that Broyhill would have priority, under the doctrine of equitable estoppel.

The UCC's priority rules are rooted in the concept of "first in time, first in right" (UCC § 9-322, Official Comment 3; White and Summers, *Uniform Commercial Code*, § 33-4 at 316-17, § 33-20 at 378 [4<sup>th</sup> ed]). However, occasionally courts have altered the priority rules where their strict enforcement would lead to inequities.

In some instances the common law doctrine of equitable estoppel may provide a sufficient basis under the UCC to subordinate a security interest entitled to priority. However, the vast majority of cases that rely upon equitable principles as the basis for denying a secured

party's status under Article 9, involve wrongdoing on the part of the secured party (*see e.g. Limor Diamonds, Inc. v D'Oro By Christopher Michael, Inc.*, 558 F Supp 709, 711 [SDNY 1983] [secured party's rights in collateral may be subordinated to the holder of a junior security interest due to bad faith seizure of collateral]). Here, there is no allegation that HUB participated in any wrongdoing vis-a-vis Broyhill that would justify subordinating its interest to Broyhill's.

Moreover, Broyhill could have easily ensured that its security interest would have priority by conducting a diligent search of the financing statements on file under the name IFR, in light of Broyhill's undisputed notice that HFG was formerly known as IFR.

In any event, having failed to establish a sufficient basis for justifying a deviation from well-established UCC principles to reverse HUB's priority under the doctrine of equitable estoppel, and even assuming that HFG did represent that Broyhill would have priority over HUB, there remains no disputed issue of fact that Broyhill's security interest achieved priority over HUB's for Merchandise acquired by HFG subsequent to March 24, 2004, and not prior to that date, as Broyhill contends.

In light of this determination, the subsequent issue raised is whether that security interest continued even after the sale of the Merchandise and attached to the proceeds from the Sale, that HFG transferred to HUB.

D. Survival of Broyhill's Security Interest in Funds Paid to HUB

Broyhill alleges that the Merchandise it shipped to HFG subsequent to March 24, 2004 totaled approximately \$195,101.31 (Canipe Aff, ¶ 3). Of this amount, \$166,716.18 worth of the Merchandise was on hand at the time of the Sale. Thus, Broyhill contends that a large portion of the funds generated by the Sale and transferred to HUB were proceeds from the sale of

Merchandise subject to Broyhill's superior security interest. Broyhill submits summaries of invoices from its account with HFG that purportedly indicate inventory supplied to HFG subsequent to March 24, 2004 by date (*id.*, Exh 1).

The Hudson Defendants dispute that the inventory disposed of during the Sale included any of the post March 24, 2004 Merchandise subject to Broyhill's security interest. (Rosenfeld Aff, ¶¶ 15-16). However, they do not submit any evidence to refute Broyhill's assertion. Further, Edward Rosenfeld provided deposition testimony that on the eve of the Sale, Broyhill Merchandise comprised approximately \$105,000 to \$120,000 worth of inventory (Rosenfeld Depo Tr, 58:6-11). This raises an issue of fact as to what post March 24, 2004 Broyhill Merchandise, if any, was sold during the Sale, the proceeds of which were thereafter transferred to HUB.

Assuming that a portion of the funds transferred to HUB were proceeds from the sale of post March 24, 2004 Broyhill Merchandise, a determination must be made as to what interest, if any, Broyhill has in these proceeds.

For the reasons set forth below, disputed issues of fact remain as to whether Broyhill's security interest survived HFG's sale of the Merchandise. This is because the court is unable to determine on the record before it whether the funds transferred to HUB constitute "identifiable proceeds" from the sale of merchandise subject to Broyhill's superior security interest, and whether HUB received these funds from HFG in the ordinary course of business.

Under the UCC, a security interest generally continues in collateral, "notwithstanding its sale, disposition, or otherwise" (UCC § 9-315 [a]), and is effective against purchasers of the collateral, subject to several exceptions. Generally, a buyer will take collateral free of the

security interest created by the seller if the secured party authorized the sale of collateral, or the buyer purchased the goods in the ordinary course of business (UCC § 2-403 [2]; *Fleet Capital Corp. v Yamaha Motor Corp., U.S.A.*, 2002 WL 31174470, at \*16 [SDNY Sept 26, 2002]).

Where a subsequent purchaser of collateral takes subject to a security interest, the secured creditor may maintain an action against the purchaser for repossession of the goods or conversion (UCC § 9-315 (a) Comment 1; *Bank of India v Weg and Myers, P.C.*, 257 AD2d 183, 191 [1<sup>st</sup> Dept 1999]). Broyhill has not attempted to maintain an action for either repossession or conversion against the non-party buyers of the furniture in which it maintains a security interest, and likely would be unsuccessful if such actions were commenced.<sup>3</sup>

Alternatively, the Security Agreement extends Broyhill's security interest to "all proceeds realized by the Debtor [HFG] for the sale of the Collateral [the Merchandise]" (Security Agreement, § 11). In any event, under the UCC, irrespective of a secured party's authorization of the sale of collateral, a perfected security interest continues in any "identifiable proceeds"<sup>4</sup> of the sale of collateral, so long as the secured party did not waive or otherwise relinquish its security interest therein (UCC 9-315 [a]; *Fleet Capital Corp.*, 2002 WL 31174470 at \*16).

Where cash proceeds of collateral goods are paid out by the debtor in the ordinary course of the debtor's business in order to satisfy a legitimate liability, the person or entity receiving such payments from the debtor takes the funds clear of any security interest in the proceeds. A

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<sup>3</sup> The UCC provides that where a secured party entrusts collateral to a buyer in the ordinary course of business, the general rule that a security interest survives disposition does not apply (UCC § 2-403 [2]). The UCC gives the merchant the power to transfer all of the secured party's rights to the purchaser, even if the sale is wrongful as against the secured party (*id.*).

<sup>4</sup> The UCC defines "proceeds" as "whatever is acquired upon the sale, lease . . . or other disposition of collateral" (UCC § 9-102 [64]).

secured party is not entitled to the return of the proceeds from the recipient (*Ford Motor Credit Co. v State of New York*, 219 AD2d 202, 204 [3d Dept] [secured party with a perfected interest in proceeds received by car dealer-debtor could not claim proceeds received by defendant-creditor paid by the car dealer in satisfaction of tax liabilities owed to the defendant, because the payments were made in the ordinary course of business and therefore, were clear of the creditor's security interest], *lv denied* 88 NY2d 813 [1996]; *Lake Ontario Prod. Credit Assoc. v Partnership of Grove*, 138 AD2d 930 [4<sup>th</sup> Dept] [a debtor's use of proceeds from unauthorized sale of collateral to pay his attorney for outstanding legal fees did not entitle the secured party to recover the funds from the attorney because they were paid in the ordinary course of business], *appeal denied* 72 NY2d 806 [1988]).

However, where a secured party can establish that the recipient of the identifiable proceeds did not receive them in the ordinary course of business, including with notice of an outstanding right of possession or a superior security interest, the secured party may establish entitlement to the proceeds under a conversion theory (*SK Global Am., Inc. v John Roberts, Inc.*, 6 AD3d 179, 179-80 [1<sup>st</sup> Dept 2004]; *Bank of India*, 257 AD2d at 191; *Sterling National Bank v Goldberg*, 277 AD2d 45, 46 [1<sup>st</sup> Dept 2000]).

Several issues of fact remain as to the inventory sold during the Sale, and whether any of the proceeds transferred to HUB included proceeds from the sale of post March 24, 2004 Broyhill Merchandise. Further, if so, issues of fact remain as to whether these funds are identifiable proceeds within the meaning of the UCC.<sup>5</sup> Additionally, the fact-finder must

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<sup>5</sup> Equitable tracing methods may be invoked to find identifiable cash proceeds even though they have been commingled with cash in other accounts of the debtor (UCC § 9-315, Note 8).

determine whether HFG's payment of the proceeds to HUB, although in satisfaction of an undisputed antecedent debt, were made in the ordinary course of business, in light of the Rosenfeld Defendants' execution of personal Guaranties with HUB (*see e.g. Sterling Natl. Bank*, 277 AD2d at 46; *Les Fourrures Global Canada, Ltd. v Lord & Taylor, Inc.*, 1997 WL 442144, at \*4 [SDNY Aug 6, 1997]), and whether HUB received the funds from the Sale with notice that it was violating Broyhill's superior security interest (*Bank of India*, 257 AD2d at 191; *SK Global America, Inc.*, 6 AD3d at 179-80; *Ford Motor Credit Co.*, 219 AD2d at 204; *see also Textron Fin. Corp. v Firststar Bank Wisconsin*, 217 Wis 2d 582, 591 [Wis App 1988]).

## II. Broyhill's Remaining Causes of Action

The Hudson Defendants do not specifically address Broyhill's remaining causes of action. Rather, they proffer a general denial. They argue that HFG was legally entitled to transfer the proceeds of the Sale to HUB because of their good faith belief that HUB's security interest was superior to Broyhill's.

### A. Fraudulent Conveyance

Broyhill maintains that the Rosenfeld Defendants wrongfully, and with the intent to defraud Broyhill, transferred the proceeds of the Sale to HUB, thereby causing HFG to become insolvent and unable to pay its debts, including the debt to Broyhill, in violation of sections 272, 274 and 276 of the DCL.

#### (i) Sections 272 and 274 DCL

Under the DCL, sections 272 and 274<sup>6</sup> govern transfers that are constructively fraudulent,

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<sup>6</sup> DCL § 274 governs constructively fraudulent transfers by a person engaged in business for which capital is unreasonably small.

and thus, apply to transfers without regard to the actual intent of the transferor or the transferee (*MFS/Sun Life Trust-High Yield Series v Van Dusen Airport Servs. Co.*, 910 F Supp 913, 936 [SDNY 1995]). Thus, without regard to intent, a transfer will be considered a fraudulent conveyance if it was made without fair consideration, when the debtor is insolvent, or which renders the debtor insolvent (DCL § 272; *CIT Group/Commercial Servs., Inc. v 160-09 Jamaica Ave. Ltd. Partnership*, 25 AD3d 301, 302, 306 [1<sup>st</sup> Dept 2006]). Good faith is required of both the transferor and transferee, and is lacking when there is a failure to deal openly, honestly and fairly (*CIT Group/Commercial Services, Inc.*, 25 AD3d at 303). A transfer made in satisfaction of an antecedent debt constitutes fair consideration (*id.*), unless there is evidence of bad faith (*Posner v S. Paul Posner 1976 Irrevocable Family Trust*, 12 AD3d 177, 178-79 [1<sup>st</sup> Dept 2004]).

The existence of an antecedent, bona fide debt between HUB and HFG, formerly IFR, is undisputed and well-documented (*see* Loan Documents, Edwards Aff, Exhs 1-6). However, the issue that arises is whether the preferential transfer of corporate funds to a creditor to satisfy an antecedent debt, which the corporation's sole owners and directors had personally guaranteed, fulfills the requirement of good faith, an indispensable element of fair consideration. This is in light of their obvious motive of seeking to avoid personal liability (*see e.g. P.A. Bldg. Co. v Silverman*, 298 AD2d 327, 327-28 [1<sup>st</sup> Dept 2002]; *American Panel Tec v Hyrise, Inc.*, 31 AD3d 586, 588 [2d Dept 2006]; *Julien J. Studley, Inc. v Lefrak*, 66 AD2d 208, 212-13 [2d Dept], *affd* 48 NY2d 954 [1979]). The submission of affidavit and deposition testimony of Edward Rosenfeld on behalf of the Hudson Defendants, in an attempt to establish their good faith belief that HUB's security interest was superior to Broyhill's, does not eliminate all factual issues, where issues of credibility are necessarily raised (*Boston Concessions Group v Criterion Ctr.*

Corp., 200 AD2d 543, 544 [1<sup>st</sup> Dept 1994]).

(ii) Section 276 DCL

Section 276 of the DCL, unlike sections 272 and 274, governs transfers made with the actual intent, as opposed to constructive intent, to defraud creditors. Under this section, a transfer is fraudulent even if the transferor pays fair consideration, so long as the transfer was made with the actual intent to hinder, delay or defraud (*Lippe v Bairnco Corp.*, 249 F Supp 2d 357, 374 [SDNY 2003], *affd* 99 Fed Appx 274 [2d Cir 2004]). Only the actual intent to hinder or delay creditors need be established, not an actual intent to defraud (*U.S. v Carlin*, 948 F Supp 271, 277 [SDNY 1996]).

In determining whether a transfer was made with the actual intent to defraud or delay creditors, a plaintiff may rely on "badges of fraud," i.e. common circumstances that accompany fraudulent transfers that give rise to an inference of intent (*CIT Group/Commercial Services, Inc.*, 25 AD3d at 303). Badges of fraud include the close relationship among the parties to the transaction, the transferor's knowledge of the creditor's claims, and questionable transfers not made in the ordinary course of business (*Wall St. Assocs. v Brodsky*, 257 AD2d 526, 529 [1<sup>st</sup> Dept 1999]; *Lippe*, 249 F Supp 2d at 374).

The Hudson Defendants' evidence does not eliminate all factual issues that are raised concerning their alleged intent to delay or hinder payment of HFG's debt to Broyhill. Accordingly, the Rosenfeld Defendants' motion to for summary judgment to dismiss the causes of action for violation of DCL sections 272, 274 and 276 is denied (*see Northpark Assocs., L.P. v S.H.C. Mergers, Inc.*, 8 AD3d 642, 644 [2d Dept 2004]). Further, resolution of whether the Rosenfeld Defendants intended to delay or hinder payment of the debt to Broyhill is required

before a determination can be made on Broyhill's cause of action for attorney's fees under DCL § 276-a.<sup>7</sup>

As for the prayer for punitive damages, even assuming that the challenged transfer was effected with the requisite intent, such conduct would not justify the award of punitive damages (*see Blakeslee v Rabinor*, 182 AD2d 390, 391-92 [1<sup>st</sup> Dept 1992], *lv denied* 82 NY2d 655 [1993]; *Cadle Co. v Organes Enters., Inc.*, 29 AD3d 927, 929 [2d Dept 2006]), and the prayer for punitive damages is stricken.

#### B. Veil-Piercing

Broyhill maintains that the Rosenfeld Defendants used HFG as their alter ego in transferring the proceeds of the Sale to HUB to partially satisfy HFG's debt for their personal benefit. This was done in order to avoid personal liability under the Guaranties that the Rosenfeld Defendants executed with HUB.

Generally, piercing the corporate veil requires that the owners exercised complete domination over the corporation with respect to the transaction attacked, and that such domination was used to commit a fraud or wrong against the plaintiff, causing injury (*First Capital Asset Mgt., Inc. v N.A. Partners, L.P.*, 300 AD2d 112, 116 [1<sup>st</sup> Dept 2002]). A plaintiff bears a heavy burden of establishing domination (*Matias v Mondo Props. LLC*, 43 AD3d 367, 367-68 [1<sup>st</sup> Dept 2007]). Further, certain indicia of conduct sufficient to justify veil-piercing includes: (1) the absence of corporate formalities; (2) inadequate capitalization; (3) whether funds are put in and taken out of the corporation for personal, rather than for corporate purposes;

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<sup>7</sup> DCL § 276-a provides for the payment of attorney's fees in the event a party establishes that a transfer is made and received with actual intent to hinder, delay or defraud creditors.

(4) overlap in ownership; and (5) the payment or guarantee of debts of the dominated corporation by other corporations in the group (*Shisgal v Brown*, 21 AD3d 845, 848 [1<sup>st</sup> Dept 2005]).

The decision to pierce the corporate veil is a fact-laden inquiry, that is often not well-suited for summary judgment resolution (*Ledy v Wilson*, 38 AD3d 214, 215 [1<sup>st</sup> Dept 2007]). Further, in light of numerous issues of fact that remain regarding the Rosenfeld Defendant's alleged preferential transfer of corporate funds to HUB in bad faith in order to avoid personal liability, and otherwise the use of the corporate entity as their alter ego, a determination as to veil-piecing is premature.

Accordingly, the Hudson Defendants' motion for summary judgment as to this cause of action is denied.

#### C. Tortious Interference With Contract

Broyhill alleges that the Rosenfeld Defendants wrongfully interfered with its Security Agreement by inducing HFG not to perform. This was allegedly done for the purpose of favoring another creditor, HUB, because the Rosenfeld Defendants had executed personal Guaranties in favor of HUB.

A claim for tortious interference with contract requires the existence of a valid contract between the plaintiff and a third party, the defendant's intentional procurement of the third party's breach of the contract without justification, and resulting damages (*Lama Holding Co. v Smith Barney, Inc.*, 88 NY2d 413, 424 [1996]). A "third party" for the purposes of a cause of action for tortious interference with contract is someone who is not party to the contract (*Finley v Giacobbe*, 79 F 3d 1285, 1296 [2d Cir 1996]). A corporate officer or director generally cannot be held liable for tortiously interfering with a contract between the corporation and a plaintiff,

unless the corporate officer or director acts in bad faith and engages in independently tortious conduct (*Murtha v Yonkers Child Care Assn.*, 45 NY2d 913, 915 [1978]). However, in response to a cause of action for tortious interference with contract, a defendant may raise the economic interest defense, that applies when the alleged tortfeasor has a pre-existing legal or economic relationship with the breaching party (*White Plains Coat & Apron Co. v Cintas Corp.*, 8 NY3d 422, 425-26 [2007]), unless there is a showing of malice (*Foster v Churchill*, 87 NY2d 744, 749 [1996]).

Even assuming that Broyhill demonstrates that the Rosenfeld Defendants tortiously interfered with the Security Agreement by causing HFG to prefer HUB over Broyhill, they have an undisputed and evident economic justification for doing so: to avoid personal liability under the Guaranties. In light of this undisputed motivation, and in the absence of an allegation of malicious conduct, Broyhill's cause of action for tortious interference with contract is meritless.

Therefore, the motion for summary judgment as to this cause of action is granted, and this cause of action is dismissed.

#### D. Breach of Fiduciary Duty

Broyhill's cause of action for breach of fiduciary duty against the Rosenfeld Defendants alleges that, as members and officers of Hudson, they owed a fiduciary duty to Hudson's creditors to distribute the proceeds of the Sale to them, including Broyhill. According to Broyhill, the Rosenfeld Defendants breached this fiduciary duty by failing to pay the proceeds to Broyhill, despite its perfected security interest therein.

Directors or officers of an insolvent corporation owe a fiduciary duty to preserve the

assets of the corporation for the benefits of creditors; insolvency causes the duty to arise (*Credit Agricole Indosuez v Rossiyskiy Kredit Bank*, 94 NY2d 541, 549 [2000]; *C3 Media & Marketing Group, LLC v Firstgate Internet, Inc.*, 419 F Supp 2d 419, 431 [SDNY 2005]). The Court of Appeals has held that the application of the “trust fund doctrine” is for the purpose of imposing liability upon corporate directors or transferees for the wrongful dissipation of the corporate assets of an insolvent corporation (*Credit Agricole Indosuez*, 94 NY2d at 549), thereby entitling its creditors to an equitable lien and the right to priority of payment over stockholders (*New York Credit Men’s Adjustment Bur. v Weiss*, 305 NY 1, 13 [1953]).

Here, Broyhill alleges that by selling the Merchandise that was subject to its security interest and transferring the proceeds of the Sale to HUB, the Rosenfeld Defendants breached their fiduciary duty to Broyhill. Additionally, Broyhill argues that the transfer of the proceeds of the Sale to HUB rendered HFG insolvent. However, the fiduciary duty between the Rosenfeld Defendants and Broyhill, if any, only arose at the moment of insolvency (*Credit Agricole Indosuez*, 94 NY2d at 549). Thus, if the allegedly tortious act that the Rosenfeld Defendants committed, the transfer of the proceeds of the Sale, occurred prior to HFG’s alleged insolvency, then the Rosenfeld Defendants owed no fiduciary duty to Broyhill at the time that the alleged breach occurred (*C3 Media & Mktg. Group, LLC*, 419 F Supp 2d at 431).

Accordingly, the motion for summary judgment as to this cause of action is granted, and it is dismissed.

#### E. Violation of Section 704, LLCL

Broyhill seeks damages from the individual Rosenfeld Defendants for making corporate

distributions in violation of LLCL section 704.

Under LLCL section 704, upon the winding up of a limited liability company, the assets shall be distributed “to creditors . . . in satisfaction of liabilities of the limited liability company.” However, there is no private right of action for violation of this provision.

Accordingly, the motion for summary judgment as to this cause of action is granted, and it is dismissed

#### F. Conversion

Broyhill alleges that the individual Rosenfeld Defendants wrongfully converted the Merchandise by disbursing the funds generated from the Sale to pay off a portion of its debt to HUB in disregard of Broyhill’s valid and superior security interest in the Merchandise, and the proceeds for the sale thereof.

A cause of action for conversion requires a showing that the plaintiff had an immediate superior right of possession to identifiable funds, and that the defendant exercised unauthorized dominion over the funds to the exclusion of the plaintiff’s rights (*Bank of India*, 257 AD2d at 191). A party may be liable in conversion for paying out identifiable proceeds from disposed collateral covered by a security interest without satisfying the secured party’s interest (*Bank of New York v Margiotta*, 99 Misc 2d 423, 425 [Dis Ct, Suffolk County 1979]; *see also Sterling Natl. Bank*, 277 AD2d at 46; *Princeton Capital Fin. Co., LLC v Webster Bank*, 2002 WL 241444, at \*2 [Sup Ct, Conn Feb 4, 2002]).

Because material issues of fact exist as to whether Broyhill had a superior right of possession to certain proceeds derived from the Sale, and whether these funds constitute

identifiable proceeds, a determination of whether the Rosenfeld Defendants interfered with Broyhill's superior right of possession by transferring the proceeds to HUB would be premature.

Accordingly, the motion for summary judgment as to the cause of action for conversion is denied.

### III. HUB's Cross-Motion For Summary Judgment

HUB cross-moves for summary judgment on its cross-claims against the Hudson Defendants as to liability, for attorney's fees and any sums that HUB may be required to pay to Broyhill, in addition to unjust enrichment. HUB maintains that its cross-claims against the Hudson Defendants are not barred by the release contained in the Settlement Agreement, because it includes only those matters that were raised or could have been raised in the SDNY Action, and that its cross-claims, asserted nearly nine months after the Settlement Agreement was executed, could not have been raised in that action. Additionally, HUB seeks to be indemnified by the Hudson Defendants on the basis of unjust enrichment.

The Hudson Defendants move for summary judgment dismissing HUB's cross-claims against them, on the ground that the Settlement Agreement constitutes an accord and satisfaction with respect to any liability of Hudson to HUB, based upon the Loan Documents. Further, the Hudson Defendants argue that this action was filed prior to the execution of the Settlement Agreement and, thus, HUB's cross-claims could have been raised in the SDNY Action.

Releases from liability are strictly interpreted according to contract principles (*Wells v Shearson Lehman/American Express, Inc.*, 72 NY2d 11, 19, *rearg denied* 72 NY2d 953 [1988]). The scope of a release depends upon the controversy being settled and the purpose for which the

release is actually given (*Commissioners of State Ins. Fund v Fortune Interior Dismantling Corp.*, 7 AD3d 427, 428 [1<sup>st</sup> Dept 2004]). If from the recitals contained in the settlement it appears that the parties intended to limit the release to only particular claims, demands or obligations, the instrument will be operative as to those matters alone (*Kaminsky v Gamache*, 298 AD2d 361, 361 [2d Dept 2002]).

Here, the Settlement Agreement reflects the parties' intent to:

release . . . each and every matter specifically or generally referred to herein and which was raised or could have been raised in the [SDNY] Action . . . [T]his release shall release forever and forever discharge each of the Parties . . . from all actions, causes of actions, suits, debts . . . which the Parties ever had, now have, or hereafter can, shall or may have against each other which was or could have been asserted in the Action

(Settlement Agreement at ¶ 8, Edwards Aff, Exh 7).

It is evident from the broad language used that the parties intended the Settlement Agreement to operate as a general release of all claims arising under the Loan Documents. HUB ignores this clear and unambiguous language, and seeks to limit the release to the claims specifically raised in the SDNY Action. However, the language contained in the Settlement Agreement manifests the parties' intent to release all claims that arose under the Loan Documents, in addition to those claims that could have been litigated as a result of pre-existing controversies (*see Hack v United Capital Corp.*, 247 AD2d 300, 302 [1<sup>st</sup> Dept 1998]). The Settlement Agreement contains a provision that states that the parties acknowledge that they may subsequently discover facts "different from those which they now know or believe to be true," and

it is their intention to settle and release, fully, finally and forever, any

and all matters . . . known or unknown, suspected or unsuspected, which do now exist, may exist or heretofore have existed . . . [T]he release herein shall be and remain in effect as full and complete general release of those matters, notwithstanding the discovery or existence of any such additional or unknown facts

(Settlement Agreement, § 9).

This language establishes the parties' intent to resolve all disputes between them, even if they later discover additional facts, indicated in the provision cited above.

HUB's contention that, because it asserted the cross-claims only nine months after the execution of the Settlement Agreement, it could not have raised them in the SDNY Action, is meritless. This action was commenced by filing against the Hudson Defendants on July 11, 2005, and the complaint was amended to name HUB as a co-defendant approximately nine months later. The SDNY Action was commenced on July 22, 2005, and amended on August 9, 2005; the Settlement Agreement was executed in October of 2005. It is evident that at the time that HUB executed the Settlement Agreement, HUB was aware of a potential claim against it by Broyhill to recover the proceeds of the Sale that the Hudson Defendants transferred to HUB, even though HUB was not yet named as a defendant. Had HUB intended to limit the scope of the release contained in the Settlement Agreement to exclude the relief sought in its cross-claims, it could have easily done so (*see Coppola v WE Magazine, Inc.*, 268 AD2d 303, 304 [1<sup>st</sup> Dept 2000]).

Thus, having subscribed to the release contained in the Settlement Agreement, HUB cannot now seek to avoid it by seeking attorney's fees under contractual provisions of the Loan documents, in addition to indemnification and contribution from the Hudson Defendants.

Alternatively, HUB seeks indemnification from the Hudson Defendants under the theory of unjust enrichment, in the event that it is found liable to Broyhill.

In the absence of an express agreement to indemnify, an obligation to indemnify may be implied to prevent unjust enrichment, where the circumstances warrant (*Rosado v Proctor & Schwartz, Inc.*, 66 NY2d 21, 23-24 [1985]). In order to be entitled to implied indemnity, either the proposed indemnitor must owe a duty to the plaintiff, which it breached by its wrongful conduct, or the proposed indemnitor must owe a separate duty to the proposed indemnitee (*id.* at 24; *Insurance Co. of the State of Penn. v HSBC Bank USA*, 37 AD3d 251 [1<sup>st</sup> Dept 2007]; *Biondi v Beekman Hill House Apt. Corp.*, 257 AD2d 76, 83 [1<sup>st</sup> Dept 1999], *affd* 94 NY2d 659 [2000]; *Raquet v Braun*, 90 NY2d 177, 183 [1997]).

The classic case of implied indemnity arises where a party is held liable vicariously or by implication for another's wrongdoing (*Trump Vill. Section 3, Inc. v New York State Hous. Fin. Agency*, 307 AD2d 891, 895 [1<sup>st</sup> Dept], *lv denied* 1 NY3d 504 [2003]). In such circumstances, implied indemnification may be invoked in favor of the party compelled to pay for the wrong of another, provided that the proposed indemnitee has not participated in any wrongdoing causing injury to the plaintiff (*id.*).

The broad Settlement Agreement notwithstanding, HUB, if it is found liable to Broyhill, can not shift that burden to the Hudson Defendants under the doctrine of implied indemnity. HUB does not allege that Broyhill seeks to hold it liable for a breach of duty owed by the Hudson Defendants to Broyhill (*Insurance Co. of the State of Penn.*, 2007 WL 473696 at \*6). Nor does it allege that the Hudson Defendants owe a duty upon which an obligation to indemnify HUB may be implied (*Raquet*, 90 NY2d at 183).

As such, the Hudson Defendants' motion for summary judgment dismissing the cross-claims is granted, and HUB's cross-motion for summary judgment as to liability is denied.

Accordingly, it is

ORDERED that the motion by Michael D. Rosenfeld, Edward Rosenfeld, and Hudson Furniture Galleries, LLC for partial summary judgment is granted only to the extent that the sixth cause of action for tortious interference with contract, the seventh cause of action for breach of fiduciary duty, the eighth cause of action for violation of section 704 of the Limited Liability Company Law, and the cross-claims are dismissed, and the prayer for punitive damages is struck; and it is further

ORDERED that the cross-motion by TD Banknorth, N.A. is denied; and it is further

ORDERED that the remainder of the action shall continue.

February 28, 2008

ENTER:

*Hen. C. Lu*

J.S.C.

**FILED**  
MAR 07 2008  
NEW YORK  
COUNTY CLERK'S OFFICE