

**Matter of Carpet Resources, Ltd. v JP Morgan Chase
Bank, N.A.**

2009 NY Slip Op 32924(U)

December 7, 2009

Supreme Court, New York County

Docket Number: 600978/09

Judge: Michael D. Stallman

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

PRESENT: Hon. MICHAEL D. STALLMAN
Justice

PART 7

In the Matter of the Application of
CARPET RESOURCES, LTD.,

INDEX NO. 600978/09

Petitioner,

- v -

MOTION DATE 5/6/09

MOTION SEQ. NO. 001

JP MORGAN CHASE BANK, N.A.,

MOTION CAL. NO. 18

Respondent.

The following papers, numbered 1 to 7 were read on this petition

	PAPERS NUMBERED
Notice of Petition— Petition — Affirmation— Exhibits A-F	<u>1-3</u>
Affidavit — Exhibits A-G; Affidavit; Answer	<u>4-6</u>
Replying Affirmation — Exhibits 1-8	<u>7</u>

Cross-Motion: Yes No

Upon the foregoing papers, it is hereby ORDERED that this petition is decided in accordance with the annexed memorandum decision and order.

FILED

MICHAEL D. STALLMAN
J.S.C.

DEC 16 2009

Dated: 12/17/09
New York, New York

NEW YORK
COUNTY CLERK'S OFFICE


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):

NEW YORK COUNTY SUPREME COURT - SPECIAL REFEREE CALENDAR**INFORMATION SHEET**

Title of Action: Carpet Resources, LTD. v JP MORGAN CHASE, N.A.

Index No.: 600978/2009

Issues Referred to HEAR AND DETERMINE: The remaining issues.

Estimated Time Needed for Hearing: ½ to 1 day

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Please attach this form to a copy of the order of reference or transcript and file, as soon as possible after issuance and in any event within 60 days thereof, with:

Special Referee Clerk - Motion Support Office
60 Centre Street - Room 119, New York, New York 10007

- You will be notified by mail of the date and time of the hearing.
- Please direct all inquiries to the Special Referee Clerk (646-386-3028)
- Usually, cases are assigned to a Referee and the hearing commences on the original hearing date. Counsel therefore should be prepared with witnesses and evidence on the original date. Counsel are required to consult with all adversaries in regard to requests or applications for an adjournment.

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK : IAS PART 7

----- X

Application of CARPET RESOURCES, LTD.,

Petitioner,

INDEX NO.
600978/09

For a Judgment Pursuant to CPLR 5225(b) and
CPLR 5227 to compel payment of debts owed
to Judgment Debtor and for related relief

Decision and Order

-against-

JP MORGAN CHASE BANK, N.A.,

Respondent

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HON. MICHAEL D. STALLMAN, J.:

Petitioner brought this proceeding to obtain a judgment pursuant to CPLR 5225(b) and 5227 against respondent JP Morgan Chase Bank, N.A. ("Chase") in the amount of \$104,085.03 plus interest, costs and disbursements.

The \$104,085.03 sought by petitioner represents the unsatisfied portion of a \$112,892.28 default judgment (index no. 601392/08 entered in New York County on June 13, 2008) which petitioner, a subcontractor on flooring work at various Chase branches in New York and New Jersey, obtained against the project's general contractor, Candor Construction Group, Inc. ("Candor") as a result of Candor's failure to pay petitioner for its work on the Chase branches.

Three days after entering its judgment, petitioner served a restraining notice on Chase as both Candor's depositor bank and its third-party creditor/garnishee, seeking to preserve "bank accounts, see in particular Montclair, NJ branch. Monies owed on projects, including but not

limited to Hamilton Square, NJ, Woodbridge, NJ, Green Lawn, NY, Yonkers, NY" (petitioner's reply papers, exhibit 1). A few weeks later, Chase commenced two lawsuits against Candor in U.S. District Court, one in the federal District of New Jersey filed on July 31, 2008, based on four New Jersey branch constructions (see *id.*, exhibit 3), and the other in the Southern District of New York filed July 29, 2008, based on three New York branch constructions (see *id.*, exhibit 5). Petitioner also served Chase with information subpoenas, which elicited that the combined balance of Candor's accounts at Chase was less than \$1,000 (see exhibit A to Chase's response to first information subpoena, at exhibit D to petition). Thereafter, the Sheriff served Chase with a notice of execution with levy focusing on Chase's contractual debt to Candor (exhibit F to petition), which was unheeded. This proceeding ensued.

The petition asserts three causes of action: (i) Chase's disregard of the sheriff's levy; (ii) Chase's violation of the restraining order by subsequently paying over \$1 million to other subcontractors with liens on project sites worked on by petitioner, while not paying anything to petitioner, which had a judgment in addition to its liens (see petition, ¶ 14); and, (iii) estoppel, based on alleged representations by Chase's counsel "that Chase would be paying all Candor subcontractors who had filed mechanics liens ... including [petitioner]" (petition, ¶ 19), which induced petitioner to cease its efforts to enforce the judgment" while Chase paid other subcontractors (*id.*, ¶ 20).

In its answer, Chase alleges that it made progress payments to Candor at the various sites to be used toward payments to subcontractors in accordance with the sites' respective contracts; instead, Candor withheld payments to the subcontractors and diverted funds for its own purposes. When many subcontractors filed mechanics' liens on the projects, Chase exercised its contractual

right to terminate Candor and paid the subcontractors directly, offsetting those payments against the unpaid contract amount due Candor, which was significantly smaller than the amount Chase had to pay the subcontractors. Based on these averments, Chase now contends that the petition must be dismissed because, since it is not indebted to Candor, the restraining notice was ineffectual. Chase further argues as an additional ground for dismissal of the petition that under the Debtor and Creditor Law, it has a prior right to offset payments to Candor's subcontractors against any amounts it allegedly owed to Candor.

Both sides have a statute in their quiver.

Petitioner relies on CPLR 5227, which provides that "[u]pon a special proceeding commenced by the judgment creditor, against any person who it is shown is or will become indebted to the judgment debtor, the court may require such person to pay to the judgment creditor the debt upon maturity, or so much of it as is sufficient to satisfy the judgment." That is exactly the situation at hand; petitioner has a money judgment against Candor, and there are still payments due to Candor under its contract with Chase.

However, CPLR 5227 is trumped by the statute relied on by Chase, Debtor and Creditor Law § 151, which "confer[s] upon a garnishee a right to set off any debt owed to it by a judgment debtor" (*Trojan Hardware Company v Bonaquisti Construction Corporation*, 141 AD2d 278, 281 [3d Dept 1988]) against any indebtedness it may have to that debtor, and to exercise such setoff against other creditors of the debtor, including a judgment creditor such as petitioner (Debtor and Creditor Law § 151). Under section 151, Chase, as "the third party debtor (garnishee) is entitled to utilize ... [against petitioner] judgment creditor ... all defenses and setoffs [it] may have had against the judgment debtor," Candor (*Industrial Commissioner of the State of New York v Five Corners*

Tavern, Inc., 47 NY2d 639, 646 [1979]), and "the issuance of any execution against any property of [Candor] shall not work to preclude the right of [Chase] to set off any amount owing from [Candor to Chase]" (*ibid.*). "[T]he rights conferred under a restraining notice, which in actuality, is but a 'junior remedy' in the arsenal of enforcement mechanisms ..., clearly are subject to the superior right of setoff [afforded by] section 151 of the Debtor and Creditor Law" (*Aspen Industries, Inc. v Marine Midland Bank*, 52 NY2d 575, 582 [1981]).

Petitioner does not dispute that Chase's rights under section 151 are greater than its own under CPLR 5227; rather, it questions what Chase is allowed to offset, and argues that Chase has a debt to Candor far in excess of petitioner's judgment even after being offset by any payments to subcontractors made by Chase before it was served with the restraining notice.

With respect to the existence of Chase's debt to Candor, without proof of which petitioner cannot prevail under either CPLR 5225(b) or 5227 (see *Gabor v Renaissance Associates*, 170 AD2d 390 [1st Dept 1991]), petitioner argues that: its work was done under Candor's supervision about five months before Chase terminated Candor after it had substantially completed the job; Chase admitted its indebtedness to Candor (Chase's response to petitioner's second information subpoena, exhibit E to petition); and, the validity of Chase's debt to Candor is established by the New Jersey court's refusal to dismiss Candor's counterclaim against Chase for more than \$3 million in outstanding contractual payments (see petitioner's reply papers, exhibit 4).

The court is not persuaded. The "admission" cited by petitioner refers to Chase's acknowledgment that it did not make all the payments called for under the contracts; it does not mean that Chase agreed Candor was entitled to receive those payments. Similarly, the New Jersey court's decision to uphold Candor's counterclaim (at Chase's exhibit G) was based on the existence

of factual questions about Chase's justification for terminating Candor and Candor's possible entitlement to payment for work done prior to its termination; it is not tantamount to summary judgment on Candor's behalf, which it would have to be to have the impact ascribed to it by petitioner, and has no bearing on the legitimacy of Chase's payments to subcontractors or its ability to offset those payments.

Relying on *Trojan Hardware Co. v Bonaquisti Construction Corp.*, *supra*, 141 AD2d at 282, petitioner also argues that Chase did not have the right to offset against its indebtedness to Candor to defeat petitioner's right to collect its judgment because Debtor and Creditor Law § 151 does not encompass contingent liabilities, and Chase's claims against Candor are speculative and contingent on the outcome of the two lawsuits it filed in federal court. Chase distinguishes this proceeding from *Trojan*, where setoff was contingent on outcome of litigation between a lending bank and a subcontractor, and this proceeding, where "Candor has no hope of recovering any unpaid contract amounts because such amounts are dwarfed by subcontractor claims" (Belmonte affidavit, fn 1).

Finally, there is the question of timing. Petitioner argues that Debtor and Creditor Law § 151 applies only to those debts of Candor paid by Chase before it was served with the restraining notice, and the bulk of Chase's payments to subcontractors took place after service of the restraining notice, in breach thereof. In particular, petitioner contends that Chase violated the restraining order served on it on June 16, 2008, by making four payments to subcontractors on June 17, 20 and 23, 2008, in an aggregate amount of \$544,526 (see Smith supporting affirmation, unnumbered pages 2-3). Chase argues that it is the date the debt becomes payable, not its payment, that must precede service of the restraining notice to allow its offset.

Here, Candor had been terminated and subcontractors had filed their liens before petitioner served the restraining notice. Under these circumstances, Chase was entitled under its contracts with Candor to pay the subcontractors directly and deduct those payments from the amount payable to Candor (see General Conditions of the Contract for Construction, §§ 14.2, 2.4.1, at Chase's exhibit A). "This right of setoff ... is superior to the rights of intervening judgment creditors and may be exercised even after the judgment creditor has undertaken enforcement of his claims against the judgment debtor" (*Aspen Industries, Inc. v Marine Midland Bank, supra*, 52 NY2d at 582). Thus, Chase was entitled to offset any subcontractor claims payable under the contracts at the time the restraining notice was served even if the actual payment was not made until later. A restraining notice served upon anyone other than the judgment debtor is effective only if the person on whom it is served actually owes a debt to the judgment debtor at the time of service of the notice (*Gallant v Kanterman*, 198 AD2d 76, 78 [1st Dept 1993]; *Burstin Investors, Inc. v K.N. Investors, Ltd.*, 255 AD2d 478, 479-480 [2d Dept 1998]). If, at the time of service of the notice, the amount offsetable by Chase exceeded its contractual debt to Candor, Chase was entitled to make those payments notwithstanding service of the notice. However, neither side has provided the court with a clear picture of the aggregate liens and invoices versus the aggregate of contractual payments to Candor not made by Chase as of the date petitioner served Chase with the restraining notice. It is thus impossible for the court to ascertain, based solely on the papers, whether Chase, at the date the notice was served, had the right to disregard it. Because a court reviewing a petition must apply summary judgment analysis, this unresolved factual issue requires a trial and precludes determination of the petition as a matter of law (see *Trustco Bank, National Association v Strong*, 261 AD2d 25, 27-28 [3d Dept 1999]).

Petitioner also requests relief pursuant to CPLR 5225(b), which "permits a judgment creditor to seek satisfaction of the debtor's obligation by commencing a special proceeding against a third person in possession of money or personalty in which the debtor has an interest" (*National Union Fire Insurance Company of Pittsburgh, PA v Eland Motor Car Company, Inc.*, 85 NY2d 725, 729 [1995], clarification denied 87 NY2d 1002 [1996]). However, petitioner fares no better under this statute, since it has not shown that either Candor is entitled to the money at issue (see *Irving & William H. Stark, Inc. v Milberg Factors, Inc.*, 38 AD2d 526 [1st Dept 1971]) or that petitioner's right to that money is superior to Chase's (see *Lang v State of New York*, 258 AD2d 165, 169 [1st Dept 1999]; see also *Key Lease Corp. v Manufacturers Hanover Trust Co.*, 117 AD2d 560, 561-562 [1st Dept 1986]).

Accordingly, it is ORDERED that the petition is granted only to the extent that the unresolved factual issues identified herein shall be tried (CPLR 410); because the items in question are the equivalent of a long account, the trial shall be referred to a referee to hear and determine; and it is further

ORDERED that the remaining issues are referred to a Special Referee to hear and determine; and it is further

ORDERED that, the Clerk shall enter judgment against defendant in accordance with the report of the Special Referee without any further application to the Court.

DATED: December 7, 2009
New York, NY

FILED
DEC 16 2009
NEW YORK
COUNTY CLERK'S OFFICE



J.S.C.

MICHAEL D. STALLMAN
J.S.C.