Sterling Natl. Bank v Travelers Cas.& Surety Co.
2010 NY Slip Op 33864(U)
December 3, 2010
Sup Ct, New York County
Docket Number: 601543/04
Judge: Shirley Werner Kornreich
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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: JUSTICE SHIRLEY WERNER KORNREICH PART 54

Index Number : 601543/2004

STERLING NATIONAL BANK

vs

TRAVELERS CASUALTY & SURETY

Sequence Number : 005

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 Summary Judgment

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	27 — 41
Answering Affidavits — Exhibits _____	
Replying Affidavits _____	

Cross-Motion: ☐ Yes ☐ No

Upon the foregoing papers, it is ordered that this motion

MEMORANDUM DECISION AND ORDER.

RECEIVED
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NYS SUPREME COURT-CIVIL

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

Dated: 12/3/10 JUSTICE SHIRLEY WERNER KORNREICH 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: IAS PART 54

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STERLING NATIONAL BANK,

Index No. 601543/04

Plaintiff,

-against-

DECISION and ORDER

TRAVELERS CASUALTY & SURETY CO. of AMERICA,

Defendant.

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SHIRLEY WERNER KORNREICH, J.:

In this coverage action on a Financial Institution Bond (Bond), plaintiff Sterling National Bank (Sterling) moves: for an order granting summary judgment (CPLR 3212) against defendant Travelers Casualty and Surety Company of America (Travelers); a declaration that Sterling's loss by way of extending credit, on the faith of a certain Bill of Lading, is a loss insured by Travelers; and an award of money damages. Motion Seq. 004. Travelers cross-moves (CPLR 3212) for an order granting summary judgment and dismissing the complaint. Motion Seq. 005. The motions are consolidated for disposition. For the reasons stated below, Travelers' motion for summary judgment is granted and the complaint dismissed, and Sterling's motion is denied.

I. Background

In July 1999, Sterling purchased a portfolio of loans from Park Avenue Bank. The portfolio included loans made to Allied Deals, Inc.(ADI). After purchase of these loans, Sterling extended a $6,000,000 credit facility to ADI, based upon Sterling's claimed reliance on certification of ADI's financial statements by Ernst & Young (E&Y). ADI, however, was a fraudulent operation which inflated its sales and receivables by creating sham customers and

005

obtaining loans from lender banks based upon these fictitious receivables. The last nine of forty-one loans on the ADI credit facility were not repaid. Eventually, ADI was placed in bankruptcy, and its principals and a number of its employees were criminally prosecuted.[1]

One of the outstanding transactions not repaid involved Sterling's extension of $904,625.00 in credit, on June 26, 2001, to ADI in connection with a June 7, 2001 Bill of Lading (Bill of Lading). The transaction purportedly arose from a purchase of metal from Century Industries (Century) by BR Brothers that was allegedly arranged by ADI as broker. The transaction involved: a June 22, 2001 application for a letter of credit by ADI, naming Century as the beneficiary; Sterling's approval of the application and issuance of a letter of credit on June 26, 2001; and a Bill of Lading sent to Sterling on June 27, 2001. The Bill of Lading: was on China National Foreign Trade Transportation Corp. (Sinotrans) letterhead; listed Century as the beneficiary; was executed (stamped/signed) by Zhang Zhen Hui on behalf of K-Line Hong Kong Ltd. (K-Line); and noted the place and date of issuance as Guangzhou, June 7, 2001. On July 2, 2001, Sterling paid Century $911,500.27, as guaranteed by the Letter of Credit. Scheller Aff., ¶¶ 7-13, Sterling Mot. The Letter of Credit required presentation of the original invoice and the Bill of Lading. Ex. 7, Travelers Mot. Sterling alleges that, on its face, the Bill of Lading appeared to be in "regular form." Complaint, ¶ 6.

Previously, on October 5, 2000, Travelers had issued a Certificate of Insurance to non-party Sterling Bancorp and its affiliates, which included plaintiff Sterling. Pursuant to the Certificate of Insurance, Travelers agreed to provide insurance to Sterling under the terms of a

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[1]In addition to this action against Travelers, Sterling brought actions against Park Avenue Bank and Ernst & Young both of which have been settle.

Financial Institution Bond (Bond). Among other things, Travelers agreed to insure Sterling for losses "resulting directly from the insured [Sterling] having, in good faith ... (1) acquired, sold or delivered, or given value, extended credit or assumed liability, on the faith of, any original... Document of Title" bearing a forged signature or that is counterfeit. Bond, (E) Securities. The Bond also provided, "Actual physical possession of the [Document of Title] by the insured, its correspondent bank or other authorized representative, is a condition precedent to the insured's having relied on the faith of such items." *Id.*

As defined in the Bond, the term "Document of Title" included a bill of lading. Sec. 1, Definitions (f). "Counterfeit" was defined as "an imitation which is intended to deceive and to be taken as an original" [*Id.* at (e)], and "counterfeiting, except when covered" by the above definition, was excluded. Sec. 2, Exclusions (p). "Forgery" was defined as "the signing of the name of another person or organization with intent to deceive." Sec. 1, Definitions (I). The Bond further stated that a forgery "does not mean a signature which consists in whole or in part of one's own name signed with or without authority, in any capacity, for any purpose." *Id.* Moreover, the Bond specifically excluded "loss resulting directly or indirectly from forgery..., except when covered under" the above definition [Sec. 2, Exclusions at (a)] and loss resulting from "trick, artifice, fraud or false pretense" not previously explicitly included.

In addition, the Bond provided, *inter alia*, that "[l]egal proceedings for the recovery of any loss hereunder shall not be brought...after the expiration of 24 months from the discovery of such loss." Sec. 5 (d)Notice. And, it specified that "[d]iscovery occurs when a Senior Vice President or above, or General Counsel of the Insured first become aware of the facts which would cause a reasonable person to assume that a loss of a type covered by this bond has been or

will be incurred, regardless of when the act or acts causing or contributing to such loss occurred, even though the exact amount or details of loss may not then be known." Sec. 3, Discovery, as amended by RSC 301 of the Bond.

On May 9, 2002, Jerrold Gilbert, an Executive Vice President and General Counsel at Sterling, sent Travelers a letter providing "notice of the discovery of a loss" under the Bond. The letter stated that "the loss involves the possible forgery, alteration and counterfeiting of documents used as a basis of extending credit" to ADI. In addition, it stated that "[i]nvestigation is currently being conducted to determine the extent of loss." Then, in a letter dated January 28, 2003, Sterling's executive Vice President, Howard Applebaum, provided Travelers with a form titled "Proof of Loss" in connection with a "[l]oss resulting from reliance on loan documents which were forged or which were counterfeit." The form set forth that Sterling had learned of the loss in May of 2002 and had reported the loss to Travelers on May 9, 2002. Exs. 17, 21, 24-26, Travelers Mot.; Exs. 1-2, 6-8. Sterling Mot.

An attachment to the form stated that, in May of 2002, Sterling had obtained reports about certain of ADI's customers which revealed that those companies were either closed, did not exist or were in a different line of business. The attachment also stated that one of Sterling's officers, Michael Scheller, had contacted various shipping companies which had allegedly issued bills of lading, and was informed that those companies had not issued such bills. Principals and certain employees of ADI were indicted for bank fraud in June 2002, in the Southern District of New York.

Meantime, in April 2003, the parties executed a Non-Waiver Agreement stating that any actions taken by either party "shall not be construed to waive or modify any of the terms,

conditions, limitations, exclusions or provisions of the Bond ... [and] shall not constitute an estoppel or waiver of any kind, nor waive, invalidate, forfeit or modify any of the rights, remedies, liabilities or defenses which Travelers may have..." Then, in June of 2003, Sterling requested from Travelers an extension of time for commencing suit under the Bond. In a letter dated June 17, 2003, Travelers agreed that "any suit filed in this matter on or before January 1, 2004, will have the same force and effect, insofar as timeliness is concerned, as though filed on June 10, 2003."

ADI principals, including the chief executive officer and the chief financial officer, eventually pled guilty to bank fraud. Exs. 6-7 (plea allocutions), Phillips Affirm., Sterling Mot. The deposition testimony of ADI principals and testimony at the criminal trials of ADI employees establish that the Bill of Lading was not genuine, that the sale of metal by Century to ADI was fictitious and that the stamped signature on the Bill of Lading had not been authorized.

Sterling commenced the instant action on May 21, 2004. Sterling's first cause of action seeks a declaration that Sterling's loss, by reason of extending credit to ADI on the basis of the Bill of Lading, is a loss insured by Travelers under the Bond. The second cause of action alleges that Travelers is in breach of its obligation to indemnify Sterling for its loss by reason of extending credit to ADI on the basis of the Bill of Lading. Specifically, Sterling contends that, under the terms of the Bond, Sterling is entitled to recover $904,625 plus interest and costs, minus any applicable deductible from Travelers.

I. *Motions*

Sterling moves for summary judgment on the ground that the loss it incurred, by "providing value and extending credit" to ADI and Century is a covered loss under the Bond

because the loss was incurred "on the faith" of the Bill of Lading and the Bill of Lading both was "forged" and "counterfeit." Travelers opposes and moves for dismissal on several grounds.

First, it contends that Sterling extended the $904,625 in credit to ADI before Sterling received the Bill of Lading, based upon E&Y's audits, not "on the faith of" the Bill of Lading. It argues that credit was not extended based upon the Bill of Lading and that the condition precedent that Sterling have physical possession of the Bill of Lading was not met. Second, Travelers claims that Sterling has not proved that the loss arose from a forged or counterfeit Bill of Lading, as defined in the Bond, but that the loss arose, instead, from the underlying fraud. Third, it contends that this action is untimely, since it was filed more than twenty-four months after discovery of the loss. Further, it contends that Sterling cannot prove damages since it recovered a portion of its damages from BR Brothers and settled its suit against Park Avenue Bank, recovering the claimed damages. Finally, it alleges that Sterling's claim for attorneys' fees is without merit. Sterling opposes.

III. *Discussion*

It is well established that summary judgment may be granted only when it is clear that no triable issue of fact exists. *Alvarez v Prospect Hosp.*, 68 NY2d 320, 325 (1986). The burden is upon the moving party to make a *prima facie* showing of entitlement to summary judgment as a matter of law. *Zuckerman v City of New York*, 49 NY2d 557, 562 (1980); *Friends of Animals, Inc. v Associated Fur Mfrs., Inc.*, 46 NY2d 1065, 1067 (1979). A failure to make such a *prima facie* showing requires a denial of the summary judgment motion, regardless of the sufficiency of the opposing papers. *Ayotte v Gervasio*, 81 NY2d 1062, 1063 (1993). If a *prima facie* showing has been made, the burden shifts to the opposing party to produce evidentiary proof sufficient to

establish the existence of material issues of fact. *Alvarez, supra*, 68 NY2d at 324; *Zuckerman, supra*, 49 NY2d at 562. The papers submitted in support of and in opposition to a summary judgment motion are examined in the light most favorable to the party opposing the motion. *Martin v Briggs*, 235 AD2d 192, 196 (1st Dept 1997). Mere conclusions, unsubstantiated allegations, or expressions of hope are insufficient to defeat a summary judgment motion. *Zuckerman, supra*, 49 NY2d, at 562. Upon the completion of the court's examination of all the documents submitted in connection with a summary judgment motion, the motion must be denied if there is any doubt as to the existence of a triable issue of fact. *Rotuba Extruders, Inc. v Ceppos*, 46 NY2d 223, 231 (1978).

A. *Coverage Under the Bond*

Both motions require the court to determine whether there is coverage for any loss incurred by Sterling under the Bond. For Sterling to establish liability as a matter of law, it must show that the Bill of Lading it received was in fact "counterfeit" or that it bore a "forged" signature, as those terms are used in the Bond. Sterling also must show that the Bill of Lading was in its "physical possession" when it "[gave] value, [or] extended credit ... on the faith of" it. Bond, (E) Securities. Here, the Bill of Lading purported to represent a transaction that never occurred. The entire transaction was a sham.

Travelers asserts lack of coverage under the Bond for the loss, arguing that: (1) Sterling extended credit before receiving the Bill of Lading, so the "on the faith of"and "actual possession" conditions were not met; (2) The signature on the Bill of Lading is not forged; and (3) The Bill of Lading is not counterfeit. Travelers reasons that Sterling's loss falls squarely within the Bond's express exclusions because it resulted,

> directly or indirectly from the complete or partial nonpayment of, or default upon, any Loan or transaction involving the insured as a lender or borrower, or extension of credit ..., whether such Loan, transaction or extension was procured in good faith or through trick, artifice, fraud or false pretenses, except when covered under Insuring Agreements (A), (D) or (E).

Bond, 2(e) Exclusions. Simply put, Travelers contends that Sterling lost the claimed money because the entire underlying transaction was fraudulent and not because it relied on a Bill of Lading that was counterfeit or contained a forged signature.

Sterling has a different view. It argues that coverage exists because it suffered a loss by reason of its providing value and extending credit to ADI and Century, on the faith of a counterfeit Bill of Lading that contained a forged signature. The court agrees in part. Sterling, "gave value," in the form of payment to Century, on the faith that the Bill of Lading it received was valid. Indeed, Sterling properly honored the Bill of Lading, which on its face, appeared to comply with the terms and conditions of the letter of credit. *See* UCC 5-109. As for the extension of credit, Sterling could not have "relied on the faith of" the Bill of Lading, which it received later. The issue of whether the Bill of Lading was counterfeit or the signature forged is more complicated.

The Bond defined "counterfeit" as "an imitation which is intended to deceive and to be taken as an original." (e) Definitions. The Court of Appeals, in *Iselin & Co. v Fireman's Fund Ins. Co.*, 69 NY2d 908 (1987), addressed similar language in a Banker's Blanket Bond. The Court modified the Appellate Division opinion based on the dissent of Justice Sandler, *Iselin & Co. v Fireman's Fund Ins. Co.*, 117 AD2d 86, 93 (1st Dept 1986). In *Iselin*, the bills of lading bore an unauthorized printed, stamped signature, as occurred here. The majority below held that the unauthorized use of a stamped, printed signature constituted a forged signature. The dissent

agreed with the majority on this point, but, unlike the majority found that the document was not counterfeit. In doing so, Justice Sandler, and subsequently the Court of Appeals, relied upon the construction given the word "counterfeit" in like documents, by the Second Circuit Court of Appeals in *Exchange Natl. Bank of Olean v Insurance Co. of N. Am.*, 341 F2d 673, *cert denied* 382 US 816 (1965). There, the court held:

> A document or writing is counterfeit if it is an imitation, if it attempts to simulate another document or writing which is authentic. The deceptive and fraudulent quality of these invoices, however, arose, not from the effort to imitate or simulate authentic invoices, but from falsity of the implicit and explicit representations of fact, to wit, that certain goods had already been shipped to a customer. To hold that these [fraudulent] invoices are counterfeit would obliterate elementary distinctions among the techniques of deception.

Id. at 676. *See French American Banking Corp. v Flota Mercante Grancolombiana, S.A.*, 925 F2d 603 (2d Cir 1991).

Here, the Bill of Lading was not genuine, the sale of metal by Century to ADI was fictitious, and the stamped signature on the Bill of Lading had not been authorized. Based on the decision in *Iselin*, 117 AD2d 93, the court finds that the Bill of Lading was not a counterfeit. However, the signature was "forged" and the claimed loss is covered. *Id.*

Similarly, the court does not accept Travelers' position that Sterling failed to establish it relied on the forgery and that its reliance directly caused the loss. Travelers asserts that Exclusion (e) applies as Sterling's loss resulted from its making a bad loan to a "fraudster," and not from its reliance on a forged or counterfeit Bill of Lading. Sterling has shown, as a matter of law and undisputed material fact, that it paid Century because the Bill of Lading appeared to be valid. If Sterling had known that the signature was forged, it would not have paid. The case law that Travelers recites and analyzes is not controlling because the opinions are not from New York and

are not directly on point. The covered "loss" here is Sterling's giving value, not extending credit, to ADI.

B. Timeliness

Sterling commenced this action on May 21, 2004. The parties dispute whether this was timely under the terms of the Bond. As set forth above, the Bond provides that legal proceedings for the recovery of any loss could not be commenced more than 24 months from discovery of such loss. *See* Bond, § 5 (d). Section 3 of the Bond defines discovery as "when a Senior Vice President or above, or General Counsel of the Insured first become aware of the facts which would cause a reasonable person to assume that a loss of a type covered by this bond has been or will be incurred, regardless of when the act or acts causing or contributing to such loss occurred, even though the exact amount or details of loss may not then be known." Travelers argues that Sterling discovered the loss by at least May 9, 2002, which was the date of Sterling's letter to Travelers providing notice of a loss arising from "the possible forgery, alteration and counterfeiting of documents used as a basis of extending credit" to Allied Deals. The letter was sent by Jerrold Gilbert, who was Executive Vice President and General Counsel of Sterling.

Sterling, however, contends that it did not discover the loss until June of 2002 at the earliest, when Michael Scheller contacted Sinotrans and K-Line and was informed that they had not issued the Bill of Lading. Sterling further argues that it did not know specific facts about the forgery and counterfeiting until May of 2004, when it reviewed transcripts from the criminal trial of certain ADI employees.

The court finds that Sterling's own documents demonstrate that by May 9, 2002, Sterling had enough information to cause a reasonable person to assume that a loss had been incurred or

would be incurred. The May 9 letter explicitly states that Sterling had discovered a loss under the Bond and that the loss involved "the possible forgery, alteration and counterfeiting of documents." Additionally, the letter states that Sterling was already conducting an investigation to determine the extent of the loss. Given that Sterling sent the letter, it is clear that by May 9, 2002, Sterling was aware of facts which caused it to believe: 1) that a loss had occurred involving the extension of credit to ADI; 2) that the loss might have arisen from forged or counterfeited documents upon which Sterling relied in extending such credit; and 3) that the loss might be covered by the terms of the Bond. *See Culinary Inst. of Am. v Aetna Cas. & Sur. Co.*, 151 AD2d 638 (2d Dept 1989).

The January 8, 2003 "Proof of Loss" form further demonstrates that Sterling had sufficiently discovered the loss by May 9, 2002, so as to trigger the 24-month time limitation. That form, which was prepared after Scheller contacted Sinotrans and K-Line and learned that they had not prepared the Bill of Lading, once again states that Sterling learned of the loss in May of 2002, and had reported the loss to Travelers on May 9, 2002.

Sterling, however, contends that it did not learn certain specific facts about the forgery and counterfeiting until May of 2004. The terms of the Bond provide that discovery of a loss occurs when enough facts are known to cause a reasonable person to assume a loss has occurred, even though the exact amount or details of the loss are not known at that point. Sterling's lack of knowledge on May 9, 2002 as to certain details of the forgery and counterfeiting does not mean that discovery did not occur as of that date.

Sterling commenced this action on May 21, 2004, more than 24 months after discovery of the loss. The action was not timely commenced under the terms of the Bond.

C. Tolling of Limitations Period

Sterling argues that this action is timely, in any event, because the contractual limitations period of 24 months was tolled pursuant to the June 17, 2003 letter from Travelers. As set forth above, in June of 2003, Sterling requested an extension of time for commencing suit under the Bond. On June 17, 2003, Travelers agreed that any suit filed on or before January 1, 2004, would have the same force and effect as though it had been filed on June 10, 2003. Sterling argues that the agreement tolled the limitations period from June 10, 2003 to January 1, 2004 and, thereby, extended the time period in which suit had to be commenced. It contends that the action is timely because it was commenced within the extended time period.

Sterling's argument is unpersuasive. The June 17 letter agreement, by its plain terms, merely states that "any suit filed in this matter on or before January 1, 2004, will have the same force and effect, insofar as timeliness is concerned, as though filed on June 10, 2003." Nothing in the agreement suggests that the letter tolled the contractual limitation period.[2]

Nor has Travelers waived its rights with respect to the contractual time limitation. "Waiver is the intentional relinquishment of a known right." [citation omitted]. *Enright v Nationwide Ins.*, 295 AD2d 980, 981 (4th Dept 2002); *See Carnegie Hill 90th St., Inc. v Greater N.Y. Mut. Ins. Co.*, 271 AD2d 333, 334 (1st Dept 2000) (plaintiff failed to offer evidence from which clear manifestation of intent to relinquish contractual limitation period could be reasonably inferred). Plaintiffs have not established intent by Travelers to relinquish the contractual limitation period beyond January 1, 2004. Instead, the June letter made clear that the

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[2] The court will not speculate why the June 10, 2003 date cited in the letter, was chosen. However, it is striking that the letter of credit was issued, the Bill of Lading presented and the money was paid in June 2002.

limitation period existed and was extended only to the January 1st date. *See Carat Diamond Corp. v Underwriters at Lloyd's, London*, 123 AD2d 544 (1st Dept 1986) (time limitation in insurance contract enforced where insurer did not mislead insured into believing limitation would not be invoked); *see also Beekman Regent Condominium Assn. v Greater N.Y. Mut. Ins. Co.*, 45 AD3d 311 (1st Dept 2007) (insurer under no obligation to call insured's attention to limitation clause and settlement negotiations, without more, insufficient to prove waiver or estoppel). Moreover, in April 2003, the parties had executed a Non-Waiver Agreement preserving the parties' rights under the Bond.

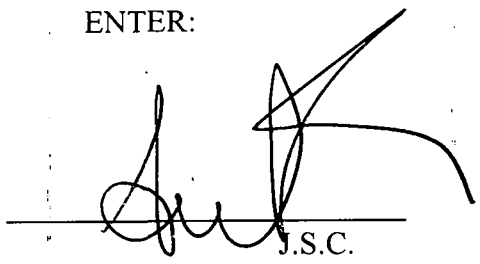
Finally, the court has considered the remaining contentions of the parties and finds it unnecessary to the court's determination. Accordingly, it is

ORDERED that plaintiff Sterling National Bank's motion for summary judgment is denied; and it is further

ORDERED that defendant Travelers Casualty and Surety Company of America's motion for summary judgment dismissing the complaint is granted, and the complaint is dismissed with costs and disbursements to defendant as taxed by the Clerk upon the submission of an appropriate bill of costs; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

ENTER:



J.S.C.

DATED: December 3, 2010
New York, N.Y.