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

PRESENT: HON. JUDITH J. GISCHE PART 10

Justice

CAPITAL ONE, N.A., ET AL. INDEX NO. 115534/08

MOTION DATE

- v -

MOTION SEQ. NO. 4

174 STREET, LLC, ET AL. MOTION CAL. NO.

The following papers, numbered 1 to _____ were read on this motion to/for _____

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
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 THE ACCOMPANYING MEMORANDUM DECISION.

Dated: NOV 28 2011

HON. JUDITH J. GISCHE J.S.C.

Check one: ☐ FINAL DISPOSITION ☐ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

☐ SUBMIT ORDER/ JUDG. ☐ SETTLE ORDER/ JUDG.

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 10

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CAPITAL ONE, N.A., successor by merger to NORTH FORK BANK, a Division of Capital One, N.A.,

- against -

Plaintiff,

174 STREET, LLC, NEW YORK CITY ENVIRONMENTAL CONTROL BOARD, NEW YORK STATE DEPARTMENT OF TAXATION AND FINANCE, and NEW YORK CITY DEPARTMENT OF FINANCE,

Defendants.

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Decision/ Order
Index No. 115534/08
Seq. No.: 00

Present:
Hon. Judith J. Gische, JSC

Recitation, as required by CPLR § 2219 [a] of the papers considered in the review of this (these) motion(s):

Papers	**Numbered**
Def 174 OSC (vacate) w/MW affirm, exhs	1
Pltf Third Bronx opp w/HZ affirm, exhs	2
Reply w/DM affirm, exhs	3
Transcript 8/4/11	4

Upon the foregoing papers, the decision and order of the court is as follows:

GISCHE, J.:

This action is to foreclose a mortgage in the amount of $2.3 million. Upon the retirement of the Hon. Nicolas Figueroa, this action was randomly reassigned to this court. By order to show cause dated May 19, 2011, defendant 174 Street, LLC ("defendant") moves to vacate or modify the Judgment of Foreclosure dated July 21, 2009 by Judge Figueroa. Pending the court's decision, the court issued a temporary restraining order, the court stayed foreclosure on condition the defendant pay the prospective sums due under the mortgage, interest on the note and escrow

sums for utilities. That TRO was modified by the court July 14, 2011 and remains in effect at this time.

This motion is brought pursuant to CPLR 317, 2004, 5015 (a) (1), (2), and (3), 5019, 5240, and Real Property Tax Law (RPTL) Article 11. Defendant claims that the publication of the foreclosure sale was not in compliance with applicable law, the default interest rate is a disguised penalty and the mortgage demands a criminally usurious rate of interest. The motion is opposed by Third Bronx, LLC (Third Bronx), the plaintiff by assignment as of September 11, 2009. The assignment was recorded in the Register's Office in New York County on October 13, 2009. Hereinafter, references to "plaintiff" shall mean either the assignor of the mortgage (Capital) or the assignee (Third Bronx).

Facts and Arguments

At the time the mortgage was executed, on October 25, 2007, defendant was leasing the building located at 553 West 174th Street, New York, New York ("premises") to AFB Housing in its entirety. In turn, AFB Housing sublet the premises to the New York City Department of Homeless Services (Homeless Services). During 2008, Homeless Services abandoned its sublease with AFB and AFB, in turn, stopped paying rent to defendant. As a result of losing rents, starting in June 2008, defendant stopped making its mortgage payments to the bank. Efforts by the parties at resolving this problem were unsuccessful and the bank continued to charge defendant the default interest rate of 24% on the mortgage. Thereafter, on November 19, 2008, plaintiff commenced the instant action to foreclose the mortgage.

Plaintiff has provided proof that on November 24, 2008, plaintiff served defendant by delivering two copies of the summons, complaint, and notice of pendency to the Secretary of

State. Despite such service, defendant did not answer the complaint. According to defendant's managing member, Steven Kaufman (Kaufman), he and his prior attorney, Eli Fixler, Esq., had extensive discussions with Capital about modifying the mortgage.[1] On January 15, 2009, Kaufman offered to buy the mortgage for $1,650,000. Allegedly, Capital repeatedly represented that it was interested in this offer and requested an appraisal of the property to determine the economic feasability of such an arrangement. Defendant allowed the appraisal. However, without informing defendant, Capital sold the mortgage to Third Bronx for $50,000 less than defendant had been willing to pay. In September 2009, Capital assigned the mortgage, all the related loan documents, and the rights in this foreclosure action to Third Bronx, the party opposing defendant's motion.

In the meantime, on January 21, 2009, Capital filed a motion for a default judgment and an order of reference. Plaintiff presents an affidavit showing that it served defendant with the motion. In his affidavit, Kaufman states that it was in January 2009 that he first learned that plaintiff had commenced this action. In addition, Kaufman states that he was never personally serve with the complaint and his prior attorney informed him that he was never served with notice of the motion for a default judgment.

On April 6, 2009, the motion for a default judgment and reference was granted by Judge Figueroa and, thereafter, on April 28, 2009, defendant's former attorney, Fixler, filed a notice of appearance. On April 29, 2009, the referee issued his report fixing the principal and interest due

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[1] The allegations concerning the negotiations are taken from a November 6, 2009 affidavit by defendant's managing member, made pursuant to a previous motion to vacate the default judgment. The affidavit is not attached to defendant's moving papers, but to plaintiff's opposing papers. Defendant's attorney affirmation for the instant motion makes the same allegations; however, the attorney does not claim personal knowledge of the facts.

on the mortgage. On May 14, 2009, plaintiff served defendant's attorney with the notice of entry of the order granting the default judgment. On June 8, 2009, plaintiff moved for a judgment of foreclosure and sale and for confirmation of the referee's report, and served defendant's attorney with the motion. Thereafter, defendant and plaintiff stipulated, on two occasions, to adjourn the return date of the motion. Defendant opposed the motion, only to the extent of challenging the legal fees being sought by plaintiff. Defendant did not otherwise oppose the referee's report. On July 21, 2009, plaintiff's motion for a judgment of foreclosure and confirmation of the referee's report was granted, although the court reduced plaintiff's legal fees to $11,000 from the amount originally sought ($24,405.75).

Notice of entry of the order granting the motion was served upon defendant on September 29, 2009. On September 30, 2009, plaintiff served defendant with a notice of sale of the premises notifying defendant that the sale was scheduled for November 12, 2009. On November 9, 2009, defendant filed an order to show cause to vacate the default judgment and the judgment of foreclosure. On November 10, 2009, defendant filed for bankruptcy in the United States District Court, Eastern District of New York. On November 23, 2009, the order to show cause was apparently declined by Judge Figueroa as "moot due to the fact that movant informed the court of defendant's bankruptcy filing." Defendant sought to to challenge the judgment of foreclosure in the bankruptcy action by way of an "Objection to Claim." The bankruptcy court judge indicated that he would not nor could he alter a final order of the state court.

In April 2010, defendant obtained a tenant for the premises and on April 21, 2010, the bankruptcy court ordered that defendant pay the monthly sum of $15,991 to plaintiff until further order. Plaintiff moved for relief from the automatic stay imposed in a bankruptcy action. By

stipulation and order dated April 29, 2011, the bankruptcy court vacated the automatic stay to permit the debtor (174 LLC) and the applicant (plaintiff herein) to pursue their rights under state law. On May 3, 2011, plaintiff served defendant with a second notice of sale of the mortgaged premises. On May 19, 2011, defendant filed the instant motion. The court granted the instant motion to the extent of issuing a TRO staying any foreclosure sale pending a decision and on the condition that defendant pay the mortgage on a monthly basis.

Discussion

Defendant moves pursuant to CPLR 317, 2004, 5015 (a) (1), (2), and (3), 5019, 5240, and Real Property Tax Law (RPTL) Article 11. Default judgments may be vacated pursuant to CPLR 317 and 5015 (a) (1). Four requirements must be met for CPLR 317 to apply (Alexander, Practice Commentary, McKinney's Cons Laws of NY, CPLR C317:1). One, the defendant must show that service was not made by personal delivery. Two, the defendant must show that it did not receive actual notice of the process in time to defend the action. Three, the defendant must show a meritorious defense. Four, the defendant must make the CPLR 317 motion within one year from learning that the default judgment was entered. CPLR 317 applies to a defendant "who does not appear." Presumably that means one who did not appear in time to prevent the granting of a default judgment. Under CPLR 317, the defendant need not demonstrate a reasonable excuse for the default.

Under CPLR 5015 (a) (1), a defendant must show a meritorious defense and an excusable default, and make the motion within one year after service on defendant of a copy of the judgment or order with written notice of its entry (*Caba v Rai*, 63 AD3d 578, 580 [1st Dept 2009]). A CPLR 5015 motion does not consider the manner in which the defendant was served

(*id.*).

Under CPLR 2004, the court has the inherent power to consider applications seeking relief from a default judgment made more than one year after entry of the default judgment, upon good cause and the showing of a meritorious defense (*Hunter v Enquirer/Star, Inc.*, 210 AD2d 32, 33 [1st Dept 1994]).

Regarding the timeliness of this motion, the default judgment was granted on April 6, 2009. Defendant was served with the notice of entry of the default judgment on May 14, 2009. Although the instant motion was made in May 2011, two years after those events, the motion is timely if the bankruptcy stay applies, which the court finds it does. The stay began on November 10, 2009 and was lifted on April 29, 2011.

As defendant was not personally served, the first requirement of CPLR 317 is met. Service by delivering process to the Secretary of State is not personal delivery (*Eugene Di Lorenzo, Inc. v A.C. Dutton Lbr. Co.*, 67 NY2d 138, 142 [1986]; *Franklin v 172 Aububon Corp.*, 32 AD3d 454, 455 [2d Dept 2006]).

Concerning the second requirement of CPLR 317, defendant fails to show that it did not receive actual notice of the process in time to defend the action. Plaintiff submits an affidavit of service via the Secretary of State. Said affidavit is prima facie proof that defendant was served (*see Del Priore v Furnival Mach. Co.*, 124 AD2d 695, 696 [2d Dept 1986]). Defendant's "mere denial of receipt of the summons and complaint [is] insufficient to rebut the presumption of proper service created by the affidavit of service" (*General Motors Acceptance Corp. v Grade A Auto Body, Inc.*, 21 AD3d 447, 447 [2d Dept 2005]) and does not constitute a reasonable excuse for defendant's failure to answer the pleading (*KPG Inc. v Salinas Group Ltd.*, 11 AD3d 338,

338 [1st Dept 2004]).

Defendant's managing member claims that Fixler, his attorney, reportedly told him that he was never sent any notice of the default judgment motion. However, plaintiff submits an affidavit showing service of that motion on defendant at the address named in the mortgage. Moreover, defendant does not deny receiving notice of the order granting the default judgment and notice of the motion for judgment of foreclosure, sale, and a reference, and notice of the granting of the latter motion. A motion to vacate a default judgment will be denied where the defendant received the motion for a default judgment (*see Gainey v Anorzej*, 25 AD3d 650, 651 [2d Dept 2006]; *Matter of Brittany J.*, 235 AD2d 310, 311 [1st Dept 1997] [motion to vacate default denied where defendant had actual knowledge of proceeding and of the default judgment against her]).

Defendant's managing member alleges that he learned of this action in January 2009. Plaintiff's motion for a default judgment was made on January 21, 2009, and defendant was notified. Defendant's allegations do not constitute an excuse for failing to answer the complaint, oppose the motion for a default judgment, or make a more comprehensive response to the motion to confirm the referee's report. In opposing the motion to confirm the referee's report, defendant raised only the issue of attorney's fees and costs, successfully convincing Judge Figueroa that the legal fees needed to adjusted downward. There is no excusable default under CPLR 5015.

Turning now to the requirement of a meritorious defense, defendant claims that the mortgage agreement is usurious. Usury constitutes the voluntary taking or reservation of a greater interest or compensation for the loan or forbearance of money than that allowed by law (*Freitas v Geddes Sav. & Loan Assn.*, 63 NY2d 254, 262 [1984]). With one exception, that does

not apply to this case, the defense of civil usury is not available to limited liability companies (Limited Liability Company Law § 1104). This action, therefore, is concerned with criminal usury, which is interest at a rate exceeding 25% per annum or the equivalent rate for a longer or shorter period (Penal Law § 190.40; General Obligations Law [GOL] § 5-521). Penal usury laws apply to loans that are less than $2.5 million (GOL § 5-501 [6]). Here, the loan was for $2.3 million.

Defendant was to repay the principal sum with interest at the rate of 5.875% per annum. Interest and principal would be repaid in equal monthly installments of $13,605, based on a 30-year amortization, commencing December 1, 2007, and thereafter on the first day of each month to and including November 1, 2012, when the balance of the principal, with interest, would become due and payable (Mortgage Agreement, ¶ III, at 3). Any installment not paid within 10 days after the date on which it is due, will bear a late fee of 4% of the installment (*id.*, ¶ 20, at 12). Upon a default in payment ,and upon the mortgagee exercising its option to declare the debt immediately due and payable, the interest rate would increase to 24% per annum (*id.*, ¶ 18 [q], at 12).

Under New York law, contractual provisions providing for an increased interest rate on default or maturity are enforceable and do not, as defendant contends, constitute a penalty or usury (*Hicki v Choice Capital Corp.*, 264 AD2d 710, 711 [2d Dept 1999]; *Nextbridge Arc Fund, LLC v Vadodra Prop., LLC,* 31 Misc 3d 1202[A], 2011 NY Slip Op 50466[U], *3 [Sup Ct, Queens County 2011]; *Eastern Sav. Bank, FSB v Aguirre,* 30 Misc 3d 1230[A], 2011 NY Slip Op 50285[U], *8 [Sup Ct, Queens County 2011]; *Emigrant Funding Corp. v 7021 LLC,* 25 Misc 3d 1220[A], 2009 NY Slip Op 52199[U], *4 [Sup Ct, Queens County 2009]; *In re Vargas*

Realty Enters., Inc., 440 BR 224, 234 [SD NY 2010]; *In re Gas Reclamation, Inc. Sec. Litig.*, 741 F Supp 1094, 1098 [SD NY 1990]). Late fees may also be charged upon defaults in payment (*Nextbridge Arc*, 2011 NY Slip Op 50466[U], *5-6; *1st Bridge LLC v 682 Jamaica Ave., LLC*, 2010 WL 4608326, *4, 6, 2010 US Dist LEXIS 118327, *12, 17 [ED NY 2010]).

Defendant argues that it is required to pay late fees in addition to the accelerated debt and that plaintiff should not be allowed to recover both these charges. The mortgagee is not entitled to recover late charges in a foreclosure proceeding where the mortgagee seeks to recover the full accelerated principal debt (2 Mortgages and Mortgage Foreclosure in NY § 36:3; *see also Beal Bank, S.S.B. v Scelza*, 1997 WL 244350, *3, 1997 US App LEXIS 11092, *7 [2d Cir 1997]; *4 B's Realty 1530 CR39, LLC v Toscano*, --- F Supp 2d ----, 2011 WL 4908385, *7, 2011 US Dist LEXIS 118265, *17-18 [ED NY 2011]). This mortgage agreement does not indicate that the parties intended that both late charges and a higher rate of interest should apply after a default under the mortgage (*see Resolution Trust Corp. v 12A Assoc.*, 782 F Supp 270, 271 [SD NY 1992]). Consequently, defendant has raised a valid defense and that is one aspect of the referee's calculations that is incorrect and should be changed. There are other errors in the calculations which both sides agree should be corrected. This recalculation, however, does not change the fact that defendant has defaulted on the underlying mortgage. CPLR 5019, which is aimed at correcting such things as mistakes, defects and irregularities that do not affect the substantial rights of parties, applies to this situation (*Kiker v Nassau County*, 85 NY2d 879, 881 [1995]). The matter is re-referred to the Referee who shall recompute the sums due in accordance with this decision.

Defendant complains that the late fee amounts to compound interest. The late fee is

demanded on top of the installment payment, which is made up of principal and interest. Such interest, defined as the "accruing of interest upon unpaid interest, irrespective of whether such unpaid interest is added to the principal debt" is allowed by law (GOL § 5-527 [1]; *Elliott Assoc., L.P. v Banco de la Nacion,* 194 FRD 116, 121-122 [SD NY 2000]). The word "compound" need not be included in the agreement, so long as it provides for the compounding of interest by adding interest to payments that include interest, as does this mortgage agreement (*see 4 B's Realty,* 2011 WL 4908385, *5, 2011 US Dist LEXIS 118265, *12-14). Therefore, the late fee is not improper.

Section 5 of the mortgage agreement requires the borrower to pay an amount sufficient to pay the taxes on the property into an interest-free escrow fund. Defendant complains that this requirement is actually "a device by which the lender is to receive a benefit in addition to the highest permitted interest for the consideration of the loan," thus, rendering the loan usurious (9 Lord, Williston on Contracts § 20:9 [4th ed] [Williston]). The laws prescribing a minimum rate of interest on mortgage escrow accounts do not apply to commercial mortgages (Banking Law § 14-b [1]; GOL § 5-601; 2 Mortgages and Mortgage Foreclosure in NY § 36:5). A mortgagor's obligation to make installment payments to the mortgagee on account of real estate taxes on the mortgaged premises which are held in an account do not entitle the mortgagor to interest on the payments so held, absent an express agreement between parties (*Matter of Surrey Strathmore Corp. v Dollar Sav. Bank of N.Y.*, 36 NY2d 173, 177 [1975]). In addition, defendant's contention that plaintiff's retention of the escrow fund increased the effective rate of interest to more than 25% per annum is conclusory, unsubstantiated, and insufficient to raise a meritorious defense (*see Beube v English*, 206 AD2d 339, 339 [2d Dept 1994]; *Bankers Trust Co. of Cal.,*

N.A. v Sciarpelletti, NYLJ, Mar. 20, 2002, at 25, col 4 [Sup Ct, Westchester County, Lefkowitz, J.]). The payment of real estate taxes may be a condition in the loan agreement but the payments are for an entirely separate obligation.

Defendant's next argument suffers from the same deficiency. As a condition of acquiring the mortgage, defendant was obligated to maintain its operating accounts with plaintiff in interest free accounts. Again, there is no showing that any benefit plaintiff derived from this enabled it to obtain an illegally high rate of interest.

The per diem interest rate is calculated using a 360-day year. Defendant complains that this device brings the rate of default interest over the usury ceiling of 25%. "Custom and convenience have prevailed over strict logic in the generally accepted rule that it is not usurious to calculate interest in accordance with the usual practice on the assumption that there are only 360 days in a year or 30 days in a month although the rate is the highest legally permissible" (Williston § 20:21; see also Restatement [First] of Contracts § 534 [c]). There exists precedence for the 360-day year in calculating interest (*4 B's Realty*, 2011 WL 4908385, *5, 2011 US Dist LEXIS 118265, *13-14; *Builders Bank v Rockaway Equities, LLC*, 2011 WL 4458851, *1, 2011 US Dist LEXIS 107409, *4 [ED NY 2011]; *1st Bridge*, 2010 WL 4608326, *2, 2010 US Dist LEXIS 118327, *4; *cf. In re Rosner*, 48 BR 538, 561 [ED NY 1985]). The court does not find that application of this the device results in a usurious interest.

Defendant argues that the terms of the mortgage are unconscionable and unreasonable. "An unconscionable contract has been defined as one which is so grossly unreasonable or unconscionable in the light of the mores and business practices of the time and place as to be unenforcible [*sic*] according to its literal terms" (*Gillman v Chase Manhattan Bank*, 73 NY2d 1,

10 [1988] [internal quotation marks and citation omitted]). Defendant alleges that the default interest rate, the 4% late fee for each installment ten days late, and the escrow fund payments allow plaintiff an unjust, one-sided, advantage. These allegations fall well short of meeting the demanding definition of an unconscionable contract. Nothing smacks of unusual or dishonest business practices. In addition, "[m]ere inequality in bargaining power does not render a contract unenforceable" (*Mickle v Christie's, Inc.*, 207 F Supp 2d 237, 253 [SD NY 2002] [internal marks and citation omitted]).

Defendant does not allege any fraudulent or immoral conduct on plaintiff's part, or that the mortgaged property was under appraised. That plaintiff and defendant negotiated after the complaint was filed, and that plaintiff sold the mortgage for less than the mortgaged amount or defendant's proffered price for the mortgage does not, without more, indicate dishonest conduct by the bank. Plaintiff had a right to pursue its contractual remedies. The court finds that defendant lacks a meritorious defense.

CPLR 5015 (a) (2) and (3) which, respectively, allow vacatur of a default judgment based on newly discovered evidence and fraud, do not apply. Clearly, defendant knew about the bank's claims against it for some time and it has alleged no fraud. Nor does CPLR 5240 apply. Pursuant to CPLR 5240, a court may issue a protective order "denying, limiting, conditioning, regulating, extending or modifying the use of any enforcement procedure." This provision "grants the courts broad discretionary power to control and regulate the enforcement of a money judgment under article 52 to prevent unreasonable annoyance, expense, embarrassment, disadvantage, or other prejudice to any person or the courts" (*Guardian Loan Co. v Early*, 47 NY2d 515, 519 [1979] [internal marks and citation omitted]). Defendant has not claimed

anything to show that the foreclosure should be prevented, except that it can now it can afford to pay the monthly installments.

RPTL Article 11 deals with the collection of delinquent taxes and does not apply in this case.

Defendant's motion is denied. The sum owing to plaintiff should be adjusted as indicated above and otherwise brought up to date.

In conclusion, it is

ORDERED that the motion by defendant 174 Street, LLC to vacate the default judgment is denied; and it is further

ORDERED that the matter is re-referred to Referee Gary Angioli, Esq. who shall recompute the sums due plaintiff in accordance herewith and that pending such new report and subsequent motion to confirm the report, and entry of a corrected judgment, the court hereby stays the sale of the property in foreclosure; and it is further

ORDERED that the temporary restraining order and conditions thereof are hereby vacated; and it is further

ORDERED that this constitutes the decision and order of the court.

Dated: New York, New York
November 28, 2011

SO ORDERED:

Hon. Judith J. Gische, J.S.C.