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

PRESENT: BARBARA R. KAPNICK Justice PART 39

Index Number : 650607/2009
BELLAS, MICHAEL L.
vs.
KRELL INDUSTRIES LLC
SEQUENCE NUMBER : 001
SUMMARY JUDGMENT

INDEX NO. 650607/09
MOTION DATE
MOTION SEQ. NO. 001
MOTION CAL. NO.

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 ACCOMPANYING MEMORANDUM DECISION

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

Dated: 1/18/11

BARBARA R. KAPNICK J.S.C.

Check one: ☐ FINAL DISPOSITION ☐ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

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

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IA PART 39

----------X

MICHAEL L. BELLAS

Plaintiffs,

- against -

KRELL INDUSTRIES, LLC

Defendants.

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DECISION/ORDER
Index No. 650607/09
Motion Seq. No. 001

BARBARA R. KAPNICK, J.:

This is an action to collect monies allegedly owed to plaintiff Michael L. Bellas ("Bellas") on a promissory note executed by the parties on April 3, 2009.

Background

On or about January 13, 2009, Bellas loaned Krell Industries, Inc. ("Old Krell") $404,000.00, which was secured by a promissory note that was executed by Rondi D'Agostino, as President of Old Krell and Daniel D'Agostino (collectively, the "D'Agostinos"). The promissory note provided that all payments were to be made to Bellas at the initial interest rate of 5.25% per annum.

On or about April 3, 2009, defendant Krell Industries, LLC ("New Krell") was formed pursuant to the terms of a Limited Liability Company Agreement (the "April 2009 Transaction"), which provided that New Krell assumed certain liabilities of Old Krell, including repayment of the $404,000.00 plus interest.

[* 3]

As of April 3, 2009 New Krell owed Bellas $460,807.00. Bellas allowed New Krell to retain $200,000.00 of the $460,807.00 owed to him as a new loan. Bellas was paid $260,807.00. The terms of the "new" $200,000.00 loan to New Krell were set forth in a promissory note (the "Note") dated April 3, 2009, which was executed by Bellas and by Rondi D'Agostino on behalf of New Krell. The Note provides that interest would be charged at 6% per annum and that all payments of principal and interest were due to Bellas on October 3, 2009.

On April 3, 2009, New Krell also entered into an Accounts Receivable Financing Agreement (the "Financing Agreement") with Wells Fargo Trade Capital Services, Inc. ("Wells Fargo"). Rondi D'Agostino executed the Financing Agreement on behalf of New Krell as President.[1] There is no dispute that Bellas is not a signatory to the Financing Agreement.

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[1] The Schedule to the Financing Agreement provides, in relevant part:

> 6. ADDITIONAL PROVISIONS.
>
> * * *
>
> (b) Conditions for Repayment of Current Indebtedness:
> (i) On the six-month anniversary of the date hereof, and provided that no Default exists hereunder, and Client is not otherwise in default of any of its obligations, then Client shall be permitted to make the following payments to the following persons on account of the respective debts owed to them:
> (A) Michael Bellas: $200,000, (plus accrued interest at the rate of 6% per annum); . . . .

Bellas, however, is a signatory to a General Subordination Agreement ("Subordination Agreement"), which was also executed by defendant on April 3, 2009 and is addressed to Wells Fargo. The Subordination Agreement provides, in relevant part:

> the undersigned hereby agrees to make subject and subordinate, and does hereby make subject and subordinate, the payment of the aforementioned indebtedness and any and all other present or future indebtedness of Debtor to the undersigned together with any and all other present or future indebtedness of Debtor to the undersigned together with any and all interest accrued or to accrue thereon (all hereinafter referred to as "secondary obligations") to the payment of **any and all debts, obligations and liabilities of Debtor to you [Wells Fargo], whether absolute or contingent, due or to become due, now existing or hereafter arising and whether direct or acquired by you by transfer, assignment or otherwise (all hereinafter referred to as 'primary obligations')** and the undersigned agrees not to ask, demand, sue for, take or receive payment or security for all or any part of said secondary obligations until and unless all and every part of said primary obligations shall have been fully paid and discharged, except as expressly set forth on Exhibit A, and subject to the conditions provided therein, and the undersigned further agrees to and does hereby transfer and assign to you and grant to you a security interest in said secondary obligations and any and all collateral security for such secondary obligations as collateral security for the payment and discharge in full of any and all of said primary obligations. The undersigned agrees to deliver to you endorsed in blank any note or other instrument which may now or in the future evidence said secondary obligations.

(emphasis added).

Additionally, Exhibit A to the Subordination Agreement provides, in relevant part:

> Repayment on Account of Secondary Obligations
>
> * * *
>
> 1. On the sixth-month anniversary of the Closing Date (*i.e.*, the date of the General Subordination Agreement), provided that **no Event of Default exists under the Accounts Receivable Financing Agreement and Debtor is not otherwise in default of any of its Primary Obligations**, then Debtor shall be permitted to make the following payments to the following persons on account of their respective Secondary Obligations:
>
> (a) Michael Bellas: $200,000 (plus accrued interest at the rate of 6% per annum); . . . .

(emphasis added).

By letter dated October 2, 2009, one day before New Krell was required to repay Bellas, New Krell informed Bellas that it would not repay him because, according to New Krell:

> . . . repayment of our indebtedness to you is expressly prohibited if a Default would result from such repayment. As the repayment of our indebtedness to you at this time would result in a material adverse change in our financial condition, we are precluded by the agreements with Wells Fargo from repaying our indebtedness to you at this time and until our financial condition improves sufficiently to allow that repayment.

Bellas filed the instant Verified Complaint, dated October 15, 2009, asserting a single cause of action for repayment on the

promissory note in the amount of $200,000.00, plus pre-judgment interest in the amount of 6% per annum, attorneys' fees, disbursements and costs in accordance with the terms of the Note.

Plaintiff now moves pursuant to CPLR 3212 for an Order granting him summary judgment.

Plaintiff argues that the documentary proof establishes the following undisputed facts: (1) New Krell executed the unambiguous Note; (2) New Krell was obligated under the Note to repay Bellas $200,000.00 plus any accrued interest at 6% per annum; and (3) New Krell defaulted under the Note.

Defendant opposes the motion and argues that plaintiff has failed to establish as a matter of law that payment on the Note is permitted under the Subordination Agreement because two Events of Default, as defined by the Financing Agreement, existed at the time the Note became due and preclude it from repaying Bellas.

Defendant also argues that granting summary judgment is inappropriate because there has been no discovery in this case and because it has viable claims pending against Bellas in a related action pending before this Court.[2]

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[2] *Krell Investor LLC et. al. v. KI, Inc. f/k/a Krell Industries, Inc., Daniel D'Agostino, Rondi D'Agostino, Michael L. Bellas and Petra Wilde* (Index No. 650652/2009).

Plaintiff responds that defendant's claims are contradicted by the explanation offered by New Krell in its letter dated October 2, 2009, which stated that repayment of the loan was prohibited by the Subordination Agreement because repayment would cause a *future* material adverse change to its business condition.[3] Plaintiff argues that the mere possibility of a future change to New Krell's business condition is not one of the prescribed Events of Default which could relieve New Krell of its obligation to Bellas. Moreover, plaintiff contends that there is no proof that an event of default occurred under either the Financing Agreement or the Subordination Agreement.

Discussion

Plaintiff asserts that he has established his right to summary judgment on his sole cause of action because he has shown the existence of the Note and the defendant's default in making payment. *Alard, LLC v. Weiss*, 1 AD3d 131 (1st Dep't 2003).

Defendant contends that payment of the Note may only be made if no Event of Default exists under the Financing Agreement and New

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[3] The Court notes that the final sentence of the October 2, 2009 states as follows:

> This [sic] letter is written without prejudice to other bases that may exist for not paying the subject amounts.

Krell is not otherwise in default of any of its Primary Obligations.[4] According to defendant, two Events of Default existed at the time that payment of the Note was due: (1) there was a "material adverse change to its business or financial condition after the execution of the April 2009 Transaction;" when it discovered costs and liabilities that it argues were concealed by Old Krell prior to April 2009; and (2) "[New] Krell has been unable, and is still unable, generally to pay its debts as they come due."

To support its contention that there were two Events of Default, Krell submits the affidavit of Ling Kwok ("Kwok"), who is a member of New Krell's Board of Managers.

In his affidavit, sworn to on October 29, 2010, Kwok states the following:

> 22. In October 2009, [New] Krell was unable generally to pay its debts as they came due. Indeed, from October 2009 through to the present day, [New] Krell owes significant amounts to vendors and others. [New] Krell

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[4] Section 7.1 of the Financing Agreement provides, in relevant part:

> ***7.1 Events of Default.*** The occurrence of any of the following events shall constitute an "Event of Default" under this Agreement . . . (k) Client shall generally not pay its debts as they become due . . . (l) there shall be a material adverse change in Client's business of financial condition.

> still has outstanding accounts payable of approximately $1.3 million, the vast majority of which has been outstanding for over 90 days. And, that sum does not include outstanding legal fees generated by the litigations with Plaintiff, his wife and others.

Kwok also asserts that he is "familiar with [New] Krell's financial condition" and attaches "copies of [New] Krell's internally generated Profit and Loss Statements for October 2009 and August 2010" to his Affidavit. (Kwok Aff. ¶ 21; *see also* Kwok Aff. Exs. B, C.) Kwok states that "[b]oth statements show that [New] Krell operated at a net loss for those months and year to date, and internal records indicate that Krell has not had a profitable month since at least October 2009." (Kwok Aff. ¶ 21.)

The Court finds that this evidence is sufficient to raise triable issues of material fact regarding whether New Krell experienced a "material adverse change" in its business condition and/or was unable to pay its debts as they become due. *See Rotuba Extruders, Inc. v. Ceppos,* 46 NY2d 223, 231 (1978).

In a letter dated June 9, 2011, after the instant motion had been argued and submitted, counsel for plaintiff informed this Court of the following:

> On May 5, 2011, Wells Fargo advised Krell Industries LLC that the Financing Agreement will terminate effective July 6, 2011. A copy of Wells Fargo's written notice of termination

> is annexed hereto as Exhibit "A." Because no Financing Agreement will exist as of July 6, 2011, Krell Industries LLC cannot commit any act of default thereunder. Krell Industries LLC thus has no viable defense and raises no issue of fact to defeat summary judgment. Therefore, Michael Bellas respectfully requests that the Court grant his motion for summary judgment.

By letter dated June 14, 2011, counsel for defendant responded, in pertinent part:

> Ms. Frommer's letter is premature. As plaintiff is aware, Krell is in the process of negotiating with potential new lenders to replace Wells Fargo. Under discussion is the assignment of the Wells Fargo loan to the new lender, which circumstance will not terminate the financing agreement as Ms. Frommer suggests. Wells Fargo has agreed that the Financing Agreement will remain in effect until at least July 6, 2011, when the proposed assignment will take place. Thus, the Financing Agreement remains binding and will continue to be binding after such an assignment. We submit that until the new financing is secured, the parties are unable to determine its impact, of any, on Mr. Bellas' pending motion.

In a subsequent conference call with the Court on July 20, 2011, counsel for defendant represented that the Wells Fargo line was still in place and that there was no new lender. Thereafter, in a letter to the Court dated September 14, 2011, defendant's counsel informed the Court of the following development:

> [T]he financing facility between our client, Krell Industries LLC, and Wells Fargo is no longer in effect. Krell Industries has obtained a new financing facility from Rosenthal & Rosenthal.

The Court then held two conference calls with the parties on October 11 and 14, 2011 to discuss this development. The parties were unable to agree how, if at all, the termination of the Wells Fargo line impacts the instant motion for summary judgment or whether supplemental briefing on the issue would be appropriate.[5]

Accordingly, based on the record as submitted to this Court prior to June 9, 2011, plaintiff's motion for summary judgment is denied without prejudice. Counsel shall appear for a preliminary conference on December 21, 2011 at 10:00AM in IA Part 39, 60 Centre Street, Room 208.

This constitutes the decision and order of this Court.

Date: November 18, 2011

Barbara R. Kapnick
J.S.C.

BARBARA R. KAPNICK
J.S.C.

[5] Also, counsel for defendant indicated that he may move for leave to amend the Answer to assert new factual allegations. However, as of the date of this Decision/Order, no such motion has been filed.