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

PRESENT: MARCY S. FRIEDMAN PART 60
Justice

412 WEST 12th STREET 1N LLC,

Plaintiff,

-against-

C AND A CAPITAL LLC,

Defendant.

INDEX NO. 652656/2012

MOTION DATE _____

MOTION SEQ. NO. 001

The following papers, numbered 1 to ____ were read on this motion to dismiss.

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	No (s). _____
Answering Affidavits — Exhibits _____	No (s). _____
Replying Affidavits _____	No (s). _____

Cross-Motion: ☐ Yes ☒ No

Defendant's motion to dismiss is decided in accordance with the attached decision/order, dated December 6, 2013.

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

Dated: 12-6-13

J.S.C.

MARCY S. FRIEDMAN, J.S.C.

1. Check one: ..... ☐ CASE DISPOSED ☒ NON-FINAL DISPOSITION

2. Check as appropriate:.....Motion is: ☐ GRANTED ☐ DENIED ☐ GRANTED IN PART ☐ OTHER

3. Check if appropriate:..... ☐ SETTLE ORDER ☐ SUBMIT ORDER

☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK – PART 60

PRESENT: HON. MARCY S. FRIEDMAN, J.S.C.

412 WEST12th STREET 1N LLC,

Plaintiff,

- against -

C AND A CAPITAL LLC,

Defendant.

Index No.: 652656/2012

Motion Seq. 001

DECISION/ORDER

In this action, plaintiff-borrower 412 West 12th Street 1N LLC (412 West), sues defendant-lender C and A Capital LLC (C&A) to recover sums paid under allegedly unenforceable penalty clauses. C&A alleges that 412 West freely entered into the contract and that both West 412 and C&A performed under it. C&A now moves to dismiss the complaint based on documentary evidence pursuant to CPLR 3211(a)(1), and for failure to state a claim pursuant to CPLR 3211(a)(7).

The relevant facts are undisputed. On May 10, 2010, the parties executed a Mortgage Note evidencing that 412 West borrowed $2,016,789.64 from C&A. (Complaint, ¶ 3; Ex. A.) On the same date, the parties executed a Consolidated, Restated and Extended Mortgage Note in the amount of $4.5 million that superseded and replaced the $2,016,789.64 Mortgage Note, among other notes. (Complaint, ¶ 4; Ex. B.) Also on May 10, 2010, the parties entered into a Mortgage Consolidation, Modification and Extension Agreement (And Assignment of Lease and Rents and Security Agreement) (Mortgage Agreement). (Complaint, ¶ 5; Ex. C.)

Under the terms of the Mortgage Agreement, the failure to make any "payments of interest

or principal that may at any time be due under the Note or this Mortgage, including the principal balance at such time as it may be or become payable in full" constituted a default, which entitled C&A, upon expiration of any notice or cure period, "to immediately exercise any and all of its rights provided under this Mortgage or by law or in equity for default." (Mortgage Agreement, §§ 1[c], 16[a], [b].) The Mortgage Agreement provided for the acceleration of all principal, accrued interest, and "any late payment charge, liquidated damages or interest charge that may be assessed under this Mortgage." (Id., §§ 1[a], 17[a].) Once an event of default occurred, the rate of interest increased to the Default Rate, defined as "a rate of interest equal to the lesser of 24% per annum or the maximum legal rate at the time any such interest is to be calculated." (Id., §§ 1[d], 12[a].) Further, if a payment was not made by 5:00 p.m. on the seventh day after it was due, "a late charge of 4¢ for each $1 so overdue" became immediately due and payable "as liquidated damages for failure to make prompt payment." (Id., § 12[b].)

On June 1, 2011, 412 West failed to make an installment payment of the mortgage. (Complaint, ¶ 10.) C&A sent 412 West a default notice, dated June 2, 2011, by which C&A (a) notified 412 West that it was in default "for failure to pay the monthly installment of interest due on June 1, 2011," (b) accelerated "the obligations secured by the Mortgage," © imposed the Default Rate of interest from the date the payment was due to the time the payment was made, (d) imposed a late charge of 4¢ on every $1 overdue as liquidated damages, and (e) notified 412 West of its liability for C&A's expenses incurred as a result of the default, including reasonable attorney's fees. (Complaint, ¶ 14; Ex. D.) At 412 West's request, allegedly made before the missed installment payment, C&A sent 412 West a pay-off letter, dated June 6, 2011, demanding payment of $4.5 million in principal, $1,500 in regular interest, $42,000 in default interest, and

$53,104.09 for reimbursement of legal fees per an indemnification agreement.[1] (Xu Aff., Ex. A.) On or about June 9, 2011, C&A sent 412 West a second pay-off letter, demanding payment of $4.5 million in principal, $1,500 in regular interest, $45,000 in default interest, $180,000 as a "late payment charge," and $53,104.09 for legal fee reimbursement.[2] (Complaint, ¶ 15; Ex. E.) On or about June 16, 2011, 412 West paid C&A $4,787,439.23 in full satisfaction of the mortgage, consisting of $4,599,607.09 in principal and interest, $180,000 as a late charge, and $7,832.14 in legal fees. (Complaint, ¶ 17; Ex. F.) Although the Mortgage Agreement provided for up to 24% in default interest, 412 West admits that it paid only approximately 1% of the outstanding principal, or $45,000, as the default interest rate. (March 7, 2013 Tr. at 9-10.) 412 West now seeks to recover from C&A damages consisting of the $180,000 late charge and the $45,000 paid in default interest.

It is well settled that on a motion to dismiss addressed to the face of the pleading, "the pleading is to be afforded a liberal construction (see, CPLR 3026). [The court must] accept the facts as alleged in the complaint as true, accord plaintiffs the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory." (Leon v Martinez, 84 NY2d 83, 87-88 [1994]. See also 511 W. 232nd Owners Corp. v Jennifer Realty Co., 98 NY2d 144 [2002].) However, "the court is not required to accept factual allegations that are plainly contradicted by the documentary evidence or legal conclusions that are

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[1]Liquidated damages in the form of the late charge were not demanded in the June 6, 2011 letter as they did not become due until the expiration of a seven-day grace period. (March 7, 2013 Tr. at 9; Mortgage Agreement, § 12[b].)

[2]The approximately $50,000 in legal fees were paid pursuant to an indemnification agreement, which is not before the court in this action. These fees were paid "for an unrelated case." (March 7, 2013 Tr. at 10.)

unsupportable based upon the undisputed facts." (Robinson v Robinson, 303 AD2d 234, 235 [1st Dept 2003]; see also Water St. Leasehold LLC v Deloitte & Touche LLP, 19 AD3d 183 [1st Dept 2005], lv denied 6 NY3d 706 [2006].) When documentary evidence under CPLR 3211(a)(1) is considered, "a dismissal is warranted only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law." (Leon, 84 NY2d at 88; see also Arnav Indus., Inc. Retirement Trust v Brown, Raysman, Millstein, Felder & Steiner, L.L.P., 96 NY2d 300 [2001].)

In moving to dismiss, C&A contends that 412 West's first cause of action alleging an adhesion contract and second cause of action alleging an unenforceable liquidated damages clause or penalty may be asserted only as affirmative defenses to an action by C&A on the mortgage. (Memo. In Supp. at 9, 13.) This contention is plainly without merit. 412 West in effect seeks a declaratory judgment that the contract at issue contains unenforceable terms. A declaratory judgment "may be an appropriate vehicle for settling justiciable disputes as to contract rights and obligations." (Kalisch-Jarcho, Inc. v City of New York, 72 NY2d 727, 731 [1988]; see CPLR 3013.)

412 West contends that the default interest rate provision and the late charge provision of the Mortgage Agreement are unenforceable penalties and are unconscionable. In particular, 412 West alleges that the late charge is, in fact, a penalty clause and is "disproportionate to the actual loss that C&A suffered." (Complaint, ¶ 27.) 412 West also alleges that C&A was "aware of the dire financial situation and constraints that 412 West was under at the time of the Mortgage Note" (Complaint, ¶ 7), and that "with [412 West's] precarious financial position, they had little choice but to sign the documents," although they did have an attorney review them. (Complaint, ¶ 20.)

According to 412 West, its "precarious" financial position, coupled with the "extreme" default interest rate, the "obscenely large" late charge, and the "extremely short" grace periods, render the Mortgage Note and related documents contracts of adhesion. (Complaint, ¶¶ 20-23.)

It is well settled that "[w]hether a contractual provision represents an enforceable liquidation of damages or an unenforceable penalty is a question of law, giving due consideration to the nature of the contract and the circumstances." (Bates Adv. USA, Inc. v 498 Seventh, LLC, 7 NY3d 115, 120 [2006] [internal quotation marks omitted], rearg denied 7 NY3d 784, citing JMD Holding Corp. v Congress Fin. Corp., 4 NY3d 373, 379 [2005].) It is the burden of the party seeking to avoid liquidated damages to show that the stated liquidated damages are a penalty. (JMD Holding Corp., 4 NY3d at 380; Hunts Point Multi-Serv. Ctr., Inc. v Terra Firma Constr. Mgt. & Gen. Contr. LLC, 5 AD3d 183, 184 [1st Dept 2004].)

It is also well settled that "[a] contractual provision fixing damages in the event of breach will be sustained if the amount liquidated bears a reasonable proportion to the probable loss and the amount of actual loss is incapable or difficult of precise estimation. If, however, the amount fixed is plainly or grossly disproportionate to the probable loss, the provision calls for a penalty and will not be enforced." (Truck Rent-A-Center, Inc. v Puritan Farms 2nd, Inc., 41 NY2d 420, 425 [1977] [internal citations omitted].) The contract is to be interpreted as of the date of its making and not as of the date of its breach. (Id. at 425.) Liquidated damages are compensable and are "an estimate ... of the extent of the injury that would be sustained as a result of breach of the agreement." (Id. at 424.) As the Court of Appeals has noted, "[t]oday the trend favors freedom of contract through the enforcement of stipulated damage provisions as long as they do not clearly disregard the principle of compensation." (JMD Holding Corp., 4 NY3d at 380

[quoting 3 Farnsworth, Contracts § 12.18].)

On this motion, C&A fails to meet its burden of demonstrating both that the damages that would result from a default under the Mortgage Agreement were not readily ascertainable at the time the contract was entered into, and that the default interest rate provision, the late charge provision, or both in combination, are not grossly disproportionate to the probable damages.

The issue of what the default interest rate and the late charge were intended to compensate C&A for, and what its probable losses were at the time of contracting, cannot be resolved on the record of this motion to dismiss. The loan documents are silent on this point. C&A relies solely on the conclusory, non-probative statements made by its counsel in a memorandum of law that 412 West "was a substantial lending risk on the verge of defaulting upon a prior loan obligation," and that C&A could not "account for all possibilities at the time it agreed to the loan, including if and/or when [412 West] would default and for how long." (Memo. In Reply at 9.) The loan documents themselves reveal that C&A accounted for its risk, at least in part, by demanding that the loan be secured through a mortgage on real property.

C&A relies on cases that upheld liquidated damages in amounts far in excess of the percentage of the principal claimed here.[3] Disproportionately is, however, only one prong of the analysis. Significantly, also, the cases relied on by C&A were decided at a different procedural posture than the instant case or on a record which contained at least some probative evidence as to why damages were not ascertainable at the time of contracting. (See JMD Holding Corp., 4 NY3d at 382-383 [enforcing early termination fee on summary judgment where lender's commitment to

[3]The $45,000 in default interest paid represents approximately 1% of the then outstanding principal of $4.5 million and the $180,000 late charge represents approximately 4% of same for a combined total of approximately 5%.

a $40 million revolving loan agreement created costs and "diminished [lender's] capacity to make profitable loans to other entities"]; Walter E. Heller & Co., Inc. v American Flyers Airline Corp., 459 F2d 896 [2d Cir 1972] [enforcing liquidated damages on appeal after trial where lender had costs, among others, for procuring substitute borrower]; Axa Inv. Mgrs. UK Ltd. v Endeavor Capital Mgt. LLC, 890 F Supp 2d 373, 389-390 [SD NY 2012] [enforcing higher default interest rate of 25% per annum on summary judgment where rate "reflect[ed] the manifest intent to shield plaintiff from risk in partial consideration for the extension of the option period, which allowed defendants to temporarily forestall litigation of their default under the original contract," and opportunity costs were "unpredictable"]; Financial Center Assocs. of East Meadow L.P. v The Funding Corp., 140 BR 829, 836-837 [ED NY Bankr. 1992] [although involving a motion to dismiss in adversary proceeding, court enforced pre-payment charge based on U.S. Treasury Bond interest rates, after considering "the nature of the transaction and the amount involved," and applying factors including "the loss upon pre-payment of all of the interest to which the lender is entitled; the cost and expenses of procuring a substitute borrower and the attendant risk and delay involved; the applicable rate of return; ... the extent and realizability of the collateral"] [internal quotation marks omitted].)

C&A's conclusory statements as to the risk of default, notwithstanding that the loan was secured by real property, fail to meet this standard. In order to prevail in this action, 412 West must ultimately demonstrate that the liquidated damages provisions are unenforceable and, even if successful on this claim, will still be liable to C&A for any actual damages C&A suffered as a result of 412 West's default. (See JMD Holding Corp., 4 NY3d at 380.) On this motion on which the burden is on C&A, however, it has not demonstrated that 412 West's second cause of action

should be dismissed. (Compare Ames v Ames, 61 AD3d 442, 443-444 [1st Dept 2009].)

412 West also pleads a first cause of action that the contract was one of adhesion. The allegations in support of this cause of action are that 412 West was in "precarious" financial condition and that it had "little choice but to sign the documents." (Complaint, ¶ 20.) These allegations are insufficient to state a cause of action for a contract of adhesion. Unconscionability "requires some showing of an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party." (Matter of State of New York v Avco Fin. Serv. of N.Y., 50 NY2d 383, 389 [1980]. See also Blumenthal v Tener, 227 AD2d 183, 184 [1st Dept 1996] ["Where one party establishes it entered into an agreement by means of a wrongful threat precluding the exercise of free will, the agreement is voidable on the grounds of duress"].) 412 West makes no allegations in support of such claims. Accordingly, 412 West's first cause of action should be dismissed.

412 West also alleges in the third cause of action that C&A breached the contract by sending 412 West a default notice when C&A knew 412 West "wanted to pay off the mortgage" and had requested a pay-off letter. (Complaint, ¶¶ 34-35.) By its own admission, 412 West "did miss" the June 1, 2011 payment, and C&A twice sent the requested pay-off letter. (Complaint, ¶¶ 10, 15, Ex. E.) 412 West fails to identify any provision in the contract that C&A breached by sending it sent a default letter following an admitted failure to pay an installment of the loan. Accordingly, 412 West's third cause of action should be dismissed.

412 West also pleads a fourth cause of action for unjust enrichment and a fifth cause of action for conversion based on C&A's receipt of the default interest payment of $45,000 and the late charge of $180,000. These claims are barred by the existence a written contract governing the

same subject matter. (See Clark-Fitzpatrick, Inc. v Long Is. R.R. Co., 70 NY2d 382, 388 [1987].) Accordingly, 412 West's fourth and fifth causes of action should be dismissed.

Finally, C&A seeks an award of counsel fees based on section 14(b) of the Mortgage Agreement which provides that 412 West shall pay "all costs, attorney's fees and disbursements" incurred by C&A "in any action or proceeding [in which C&A] is named as a party, or issues relating to the priority, enforceability or collectibility, of, or amounts secured by, this Mortgage are raised."[4] As this provision does not authorize an interim award of fees, the court does not reach the parties' other arguments as to its applicability.

The court has considered the parties' remaining contentions and finds them to be without merit.

It is accordingly hereby ORDERED that C&A's motion is granted to the extent of dismissing the first, third, fourth, and fifth causes of action; and it is further

ORDERED that the parties shall appear for the previously scheduled oral argument on 412 West's motion for leave to amend the complaint in Part 60, Room 248, 60 Centre Street, New York, New York on January 9, 2014 at 11:30 a.m.

This constitutes the decision and order of the court.

Dated: New York, New York
December 6, 2013

MARCY S. FRIEDMAN, J.S.C.

[4]The court notes that C&A failed to include this request for relief or a general prayer for relief in its notice of motion (see CPLR 2214[a]), but did so in its memorandum of law (Memo. In Support at 16). As 412 West both had an opportunity to oppose and did oppose this request (Memo. In Opp. at 11), the procedural defect is not fatal.