

**Matter of Hearst Mags. v Five Star Fragrance Co.,
Inc.**

2018 NY Slip Op 30744(U)

April 24, 2018

Supreme Court, New York County

Docket Number: 159620/2017

Judge: Carol R. Edmead

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 35

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In the matter of the Petition of

HEARST MAGAZINES, a Division of Hearst
Communications, Inc.,

DECISION/ORDER

Petitioner,

Index No.: 159620/2017

For a Judgment Pursuant to
CPLR 5225(b) and/or CPLR 5227

-against-

Mot. Seq. 001

FIVE STAR FRAGRANCE COMPANY, INC,
A Party in Possession of Property of Cloudbreak
Holdings, LLC and/or Cloudbreak Group, LLC,
Judgment Debtors of Petitioner,

Respondent.

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HON. CAROL R. EDMEAD, J.S.C.:

MEMORANDUM DECISION

Petitioner, Hearst Magazines (“Petitioner”), brings a notice of petition seeking judgment on its first, second, third, fourth, and fifth causes of action, which seek pursuant to CPLR §§ 5225(b) and 5227, to set aside as fraudulent the conveyance by judgment debtors Cloudbreak Holdings, LLC and/or Cloudbreak Group (collectively “Debtors”) to respondent, Five Star Fragrance Company, Inc. (“Respondent”), of certain assets.¹

¹ CPLR § 5227 states, in relevant part, that:

“Upon 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,”

Here, there is no evidence suggesting that Respondent is or will become indebted to Debtors herein, and thus, CPLR § 5227 is inapplicable.

Respondent cross-moves pursuant to CPLR § 3211 to dismiss the Petition. Specifically, Respondent argues that there was no fraudulent conveyance, as the subject transfer was made with fair consideration.

The Petition

According to the Petition, between December 2012 and February 2013, Debtors purchased print and digital advertisements for Isaac Mizrahi fragrances in several of Petitioner's magazines, resulting in the total charges in the amount of \$259,450 (Petition, ¶¶ 9, 10). Petitioner further alleges that Debtors failed to pay for the advertisements (*id.*, ¶ 12). On July 23, 2013, Petitioner commenced an action in this Court against Cloudbreak to recover the costs of the advertisements (*Hearst Magazines v. Cloudbreak Holdings, LLC, et. al.*, 652567/13). In the underlying action, Petitioner moved for summary judgment on November 17, 2013, which was granted on June 12, 2014. On July 10, 2014 Judgment was entered in Petitioner's favor and against Debtors for \$295,673.50. Petitioner claims that with post-judgment interest and credit for \$53,131.55, the balance due on the Judgment is \$330,320.53 (*id.*, ¶ 19).

On September 26, 2011, Debtors entered into a five-year Trademark License Agreement with a company known as Xcel Brands² ("Licensor"), under which Debtors acquired licenses to use the trademarks, manufacture, market and sell Isaac Mizrahi fragrances ("License Agreement"). On May 1, 2014, while Petitioner's motion for summary judgment was pending, Debtors, Respondent and Licensor entered into the Termination Agreement, wherein, Petitioner alleges that, *inter alia*, Debtors transferred all of its assets to Respondent (Yudin Aff., Ex. C, Termination Agreement).

² Petitioner indicates that "IM Brands" succeeded Xcel Brands.

Petitioner thereafter filed the instant turnover proceeding alleging that the transfer of assets from Debtors to Respondent was a fraudulent conveyance under Debtor and Creditor Law (“DCL”) §§ 273, 273-a, 274, 275, and 276. Petitioner requests, *inter alia*, that: (1) the subject transfer be set aside in amount no less than the Judgment, or in the alternative, awarding Petitioner damages against Respondent or permitting Petitioner to disregard the transfer and attach or levy execution upon the property transferred; and (2) attorney’s fees pursuant to DCL § 276-a.

In support of the Petition, counsel for Petitioner submits an affirmation arguing, first, that Respondent has the burden of establishing that the subject transfer was not a fraudulent conveyance. Petitioner further contends the transfer: was not supported by fair consideration; divested Debtors of all its assets, rendering Debtors insolvent; and resulted in an unreasonably small capital remaining in Debtors. Petitioner also argues that Debtors should have been aware that it would incur debts beyond its ability to pay as the debts mature. Additionally, Petitioner argues that the subject transfer was fraudulent to DCL § 276, since the circumstances associated with the subject transfer give rise to an inference of fraudulent intent.

Respondent’s Opposition and Cross-Motion

In opposition and in support of the cross-motion to dismiss, Respondent argues that Petitioner may not utilize a turnover proceeding pursuant to CPLR § 5225(b) because Debtors have no interest in the assets transferred, as it surrendered all of its assets and collateral to a secured creditor. Respondent contends that the secured creditors have a blanket lien over the interests that were transferred or surrendered by Debtors as of December 1, 2014. Moreover, Respondent argues that a blanket lien held by the secured

creditors, requiring that the secured creditors be paid first. Respondent further contends that since there is not enough money to satisfy the secured creditors, Petitioner may not recover. Next, Respondent argues that there was no constructive fraudulent conveyance, as the subject transfer was made with fair consideration. Respondent submits the affidavit of Michael W. Katz, Chief Executive Officer of Respondent, wherein he affirms that the transfer was completed because Cloudbreak Group was no longer being funded and was indebted to its secured lenders. Respondent further argues that Petitioner fails to provide the necessary details to give rise to an inference of fraudulent intent and relies on unsupported allegations.

Petitioner's Reply

In reply, Petitioner first argues that Respondent failed to meet its burden to come forward with evidence demonstrating that the fairness of the consideration. Additionally, Petitioner argues that it has adequately plead constructive and actual fraud.

Petitioner also submits evidence, submitted for the first time in its reply, in support of its claim that fair consideration was not exchanged as part of the subject transfer. First, Petitioner argues that the Isaac Mizrahi sales data indicates that the sales of fragrance products from October 2014 and February 2016 were \$1,141,803. Second, Petitioner argues that the deposition testimony of Michael Anderson, Chief Financial Officer of Debtors and the 2013 federal tax returns for Cloudbreak Holdings establish that Glenn Nussdorf ("Nussdorf") owns a majority of Cloudbreak Holdings. Third, Petitioner contends that the Termination Agreement was prepared and structured by a single lawyer, who is general counsel for a corporation owned and controlled by members of the Nussdorf family.

Discussion

CPLR 5225(b)

CPLR 5225(b) states in relevant part:

“Upon a special proceeding commenced by the judgment creditor, against a person in possession of custody of money or other personal property in which the judgment debtor has an interest, or *against a person who is a transferee of money or other personal property from the judgment debtor*, where it is shown that the judgment debtor is entitled to possession of such property or that the judgment creditor's rights are superior to those of the transferee, the court shall require such person to pay the money, or so much of it as is sufficient to satisfy the judgment”

“A special proceeding under Section 5225 may serve as the means by which the Court sets aside a transfer made by a judgment debtor to defraud his or her creditors if the Court finds that the transfer at issue is fraudulent” (*Interpool Ltd. v. Patterson*, 890 F. Supp. 259, 269 [S.D.N.Y. 1995]; *Hotel 71 Mezz Lender, LLC v. Rosenblatt*, 64 A.D.3d 431, 432 [1st Dept 2009]). Accordingly, CPLR § 5225(b) authorizes a turnover proceeding to be initiated against a transferee, such as Respondent (*see WBP Cent. Assocs., LLC v. DeCola*, 50 A.D.3d 693, 693 [2d Dept 2008]; *F.D.I.C. v. Conte*, 204 A.D.2d 845, 846, [3d Dept 1994]; *Gelbard v. Esses*, 96 A.D.2d 573, 575 [2d Dept 1983]; *Siemens & Halske GmbH v. Gres*, 32 A.D.2d 624, 624 [1st Dept 1969]).

In a summary proceeding such as a turnover proceeding pursuant to CPLR § 5225(b), “a court is authorized to ‘make a summary determination upon the pleadings, papers and admissions to the extent that no triable issues of fact are raised’ ” (*Matter of TNT Petroleum, Inc. v. Sea Petroleum, Inc.*, 72 A.D.3d 694, 695 [2d Dept 2010], quoting CPLR 409 [b]). A court in a turnover proceeding “will apply summary judgment analysis and[,] absent a factual issue requiring a trial,” the matter will be summarily determined on the papers presented (*Matter of Trustco Bank, N.A. v. Strong*, 261 A.D.2d 25, 27 [3d

Dept 1999]; see *Winston Capital, LLC v. Abadiam*, 70 A.D.3d 414 [1st Dept 2010]; *Hotel 71 Mezz Lender*, 64 A.D.3d at 432). Thus, a petition in a special proceeding must be accompanied by competent evidence raising a material issue of fact (*Thompson v. Cooper*, 91 A.D.3d 461, 462 [1st Dept 2012]; *WBP Cent. Assocs.*, 50 A.D.3d at 694).

The burden of proof in a turnover proceeding rests with the judgment creditor to establish that contested transfer was made without fair consideration (*Petrocelli v. Petrocelli Elec. Co.*, 121 A.D.3d 596 [1st Dept 2014]; *CIT Group/Commercial Services, Inc. v. 160-09 Jamaica Ave. Ltd.*, 25 A.D.3d 301, 306 [1st Dept 2006]). However, there is some authority for the view that “where the evidentiary facts as to the nature and value of the consideration are within the transferee’s control, the burden of coming forward with evidence on the fairness of the consideration shifts to the transferee[,]” (*ACLI Gov’t Sec. v. Rhoades*, 653 F.Supp. 1388, 1391 (S.D.N.Y.1987), *aff’d mem.*, 842 F.2d 1287 [2d Cir. 1988]), “and the [burden of proving the] fairness of the consideration therefor, should be cast upon the transferees” (*Gelbard*, 96 A.D.2d 573, 576 [2d Dept 1983]; see *U.S. v. McCombs*, 30 F.3d 310 [2nd Cir. 1994]).

Here, the burden of demonstrating whether fair consideration was exchanged as part of the subject transfer remains with the Petitioner. In the cases where the burden of demonstrating fair consideration was shifted to the transferee, including those cases cited by Petitioner, the conveyance at issue was made between family members and was for no consideration, or the nature of the consideration was concealed. For instance, in *Gelbard*, the judgment debtors transferred assets under a complex agreement involving the exchange of, *inter alia*, stock interests in corporations pursuant to security agreements made between family members (*Gelbard*, 96 A.D.2d 573). The court in *Gelbard*

determined that “[w]here the creditor asserts that the transferees paid insufficient consideration and the evidentiary facts as to the nature and value of the consideration are within the transferees’ control, the burden of coming forward with evidence disclosing the nature and value of the [consideration] furnished by the corporation . . . and the fairness of the consideration therefor, should be cast upon the transferees” (*id.* at 576). The court further indicated that “[t]his is particularly so here because the Bankruptcy Court did not authorize the creation of a security interest in the assets of the corporation” (*id.*).

In *Greystone v. Neuberg* (US Dist Ct, ED NY, 10-CV-5225 Seybert, J., 2011), another case cited by Petitioner, the plaintiff alleged that co-defendant submitted a financial statement falsely indicating that he owned a property, when in fact co-defendant transferred the subject property to his wife two weeks earlier for no consideration (*see also ACLI Gov't Sec., Inc. v. Rhoades*, 653 F. Supp. 1388, 1390 [S.D.N.Y. 1987] [consideration consisted of \$1.00 and unspecified “other good consideration”]).

Here, there is no such complex agreement that concealed the nature and value of the consideration exchanged. The Termination Agreement, which was furnished to Petitioner, addresses the consideration exchanged. Petitioner neither presents any evidence suggesting that evidence of the nature and value of the consideration exchanged in the subject transfer is in the Respondent’s control, nor identify what evidence is exclusively in its possession. Further, it is undisputed that tangible consideration was exchanged as part of the subject transfer. Additionally, other than Petitioner’s self-serving claim that the subject transaction was made between entities controlled by

Nussdorf or members of his family, Petitioner does not present any evidence suggesting that the subject transfer was intra-family. Accordingly, Petitioner's claims do not warrant the shift in the burden of establishing fair consideration from Petitioner to Respondent.

Debt and Creditor Law

Under DCL §§ 273, 273-a, 274, and 275, a lack of fair consideration is a prerequisite to a finding of constructive fraud. Accordingly, in order for Petitioner to obtain the relief under the aforementioned sections of the DCL, it has the burden of proving, by clear and convincing evidence, that the transfer was lacking fair consideration. DCL § 272 states, in relevant portion, that “fair consideration” is given for property, or an obligation, “[w]hen in exchange for such property, or obligation, as a fair equivalent therefor, and in good faith, property is conveyed or an antecedent debt is satisfied”

Fair consideration requires that the exchange not only be for equivalent value, but also that the conveyance be made in good faith (DCL § 272; *Sardis v. Frankel*, 113 A.D.3d 135, 142 [1st Dept 2014]; *Ede v. Ede*, 193 A.D.2d 940, 941–942 [3d Dept 1993]). However, “fair consideration does not require dollar-for-dollar equivalence; consideration can be fair even if it is less than the value of the transferred property, as long as it is an amount that is not ‘disproportionately small’ as compared to the value of the transferred property” (*Lippe v. Bairnco Corp.*, 249 F.Supp.2d 357, 377 [S.D.N.Y. 2003]; *Abreu v. Barkin & Assocs. Real Estate, LLC*, 136 A.D.3d 600 [1st Dept 2016] [denying fraudulent conveyance claim inasmuch as it was premised on lack of fair consideration, since petitioner failed to show that \$20,000 was not a “fair equivalent” for the items sold]). Good faith “is lacking where there is a failure to deal honestly, fairly,

and openly” (*Sardis*, 113 A.D.3d at 143). Indications of lack of good faith include the close relationship between the debtor and transferee’s principals, the lack of consideration, representation by the same attorney, a series of transfers by the debtor after incurring its obligation to the creditor, and the debtor becoming an empty shell (*see Cadle Co. v. Organes Enters., Inc.*, 29 A.D.3d 927, 928 [2d Dept 2006]). Ultimately, “whether fair consideration is given for the property under Debtor and Creditor Law § 272 must ‘be determined upon the facts and circumstances of each particular case.’” (*Commodity Futures Trading Comm’n v. Walsh*, 17 N.Y.3d 162, 175 [2011], quoting *Halsey v. Winant*, 258 N.Y.512, 523 [1932]).

Here, Petitioner failed to provide evidence that the subject transfer lacked fair consideration. The Termination Agreement, entered into by Debtors, Respondent and Licensor, documented the subject transfer. The Termination Agreement indicates that in exchange for \$200,000³ and the transfer of Cloudbreak Group’s outstanding royalty payments to the Licensor in the amount of \$750,000 to Respondent, Debtors transferred to Respondent the: (1) license to use the trademarks and manufacture, market and sell Isaac Mizrahi fragrances; (2) unapplied royalty payments in the amount of \$300,000; (3) approximately 61,000 units of Isaac Mizrahi fragrance and products remaining in Debtors inventory; and (4) the custom molds and other equipment used to manufacture the fragrance line. Petitioner fails to demonstrate that the exchange of the above consideration by Respondent to Debtors, the amounts of which are not disputed by the parties, constitutes a disproportionately small value compared to the consideration

³ Katz affirms that under the Termination Agreement Respondent paid Cloudbreak Holdings \$100,000 for agreeing with Respondent and Licensor to terminate the original Licensing Agreement and paid Cloudbreak Group \$100,000 for inventory (Katz Aff., ¶ 25).

furnished by Debtors to Respondent. Other than its claim there was not a fair exchange of value, Petitioner does not submit any means by which the Court may evaluate the value of the consideration exchanged.

Even if Petitioner demonstrated that exchange of property was not a fair equivalent, it fails to present evidence that the subject transfer was not made in good faith. Petitioner contends that the transfer by Debtors to Respondent of the entirety of Debtors' assets was made in a non-arm's length transaction between affiliated entities controlled by Nussdorf or members of his family. Petitioner's sole support for its argument that good faith is lacking is the affirmation of its counsel, alleging "upon information and belief" that Nussdorf was the majority owner and manager of Cloudbreak, and Respondent was owned and/or controlled by Nussdorf and/or other members of the Nussdorf family. Such allegation is pure speculation and is insufficient to raise a question of fact to preclude summary judgment (*see Alvarez v. Prospect Hosp.*, 68 N.Y.2d at 327; *Winegrad v New York Univ. Med Ctr.*, 64 N.Y.2d 851, 853 [1985] [a motion for summary judgment cannot rest upon "information and belief but rather must be rooted in a prima facie showing of entitlement to judgment as a matter of law, tendering sufficient evidence to demonstrate the absence of any material issues of fact from the case"]]). Additionally, the evidence submitted by Petitioner for the first time in its reply in support of its argument that fair consideration was not exchanged as part of the subject transfer is not properly before the Court, as Petitioner cannot rely upon evidence which is submitted for the first time in its reply papers to satisfy its *prima facie* burden, or to remedy basic deficiencies in its *prima facie* showing (*see, e.g., Rengifo v. City of New York*, 7 A.D.3d 773, 773 [2d Dept 2004]; *Migdol v. City of New York*, 291

A.D.2d 201, 201 [1st Dept 2002]; *Ritt by Ritt v. Lenox Hill Hosp.*, 182 A.D.2d 560, 561–62 [1st Dept 1992]).

DCL § 276 provides that “[e]very conveyance made and every obligation incurred with actual intent, as distinguished from intent presumed in law, to hinder, delay, or defraud either present or future creditors, is fraudulent as to both present and future creditors” (*Wall St. Assocs. v. Brodsky*, 257 A.D.2d 526, 529 [1st Dept 1999]). A claim under DCL § 276 must be pleaded with particularity under CPLR § 3016(b) (*see RTN Networks, LLC v. Telco Group, Inc.*, 126 A.D.3d 477, 478 [1st Dept 2015]). However, “[d]ue to the difficulty of proving actual intent to hinder, delay, or defraud creditors, the pleader is allowed to rely on ‘badges of fraud’ to support his case, i.e., circumstances so commonly associated with fraudulent transfers ‘that their presence gives rise to an inference of intent’ ” (*Wall St. Assocs.*, 257 AD2d at 529 [citations omitted]; *see Ray v Ray*, 108 A.D.3d 449, 451 [1st Dept 2013]).

Badges of fraud include: “(1) the close relationship among the parties to the transaction, (2) the inadequacy of the consideration, (3) the transferor's knowledge of the creditor's claims or claims so likely to arise as to be certain, and the transferor's inability to pay them, and (4) the retention of control of property by the transferor after the conveyance” (*Dempster v. Overview Equities*, 4 A.D.3d 495, 498 [2d Dept 2004]).

As addressed in the discussion above, Petitioner fails to meet its *prima facie* burden, in that it failed to submit sufficient evidence demonstrating that, among other things, fair consideration was not exchanged as part of the subject transfer and that Respondent retained control of the property after the conveyance. Thus, Petitioner fails to establish that there was a fraudulent conveyance. Since Petitioner's claim under DCL §

276 was unsuccessful, summary judgment of its claim for attorney's fees under DCL § 276-a is unwarranted. Finally, as Respondent has shown that there was no fraudulent conveyance, it is entitled to dismissal of this special proceeding.

CONCLUSION

Accordingly, it is hereby

ORDERED and **ADJUDGED** that the relief sought in the Petition is denied. It is further

ORDERED that Respondent's cross-motion to dismiss the Petition is granted. It is further

ORDERED that counsel for Petitioner shall serve a copy of this order with notice of entry upon all parties within ten (10) days of entry.

This constitutes the decision and order of the Court.

Dated: April 24, 2018



Hon. Carol Robinson Edmead, J.S.C

HON. CAROL R. EDMEAD
J.S.C.