El Ad US Holding Group, Inc. v American Intl. Group, Inc.
2020 NY Slip Op 33819(U)
November 17, 2020
Supreme Court, New York County
Docket Number: 158426/2020
Judge: Arthur F. Engoron

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: **HON. ARTHUR F. ENGORON** **PART** **IAS MOTION 37EFM**

Justice

----------X

EL AD US HOLDING GROUP, INC. A/K/A EL AD US HOLDING, INC.,RIVERSIDE CENTER SITE 5 OWNER LLC A/K/A RIVERSIDE CENTER 5 HOLDING CO.,

Plaintiff,

- v -

AMERICAN INTERNATIONAL GROUP, INC.,NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PA., THE INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA, NEW HAMPSHIRE INSURANCE COMPANY, LEXINGTON INSURANCE COMPANY, ISRAEL DISCOUNT BANK OF NEW YORK

Defendant.

----------X

INDEX NO. 158426/2020

MOTION DATE N/A

MOTION SEQ. NO. 001

DECISION + ORDER ON MOTION

The following e-filed documents, listed by NYSCEF document number (Motion 001) 2, 20, 21, 22, 23, 25, 26, 27, 28, 29, 30, 31, 32, 33, 34, 35, 36, 37, 38, 39, 40, 41, 42, 43, 44, 48, 49

were read on this motion to/for PRELIMINARY INJUNCTION.

Upon the foregoing documents, petitioners' motion for a preliminary injunction is denied.

Background

On October 12, 2020, petitioners, El Ad US Holding Group, Inc. a/k/a El Ad US Holding, Inc. ("El Ad") and Riverside Center Site 5 Owner LLC a/k/a Riverside Center 5 Holding Co. ("Riverside"; collectively with El Ad, "Petitioners"), commenced this special proceeding, by way of an Order to Show Cause, to enjoin respondents, American International Group, Inc. ("AIG"); National Union Fire Insurance Company of Pittsburgh, PA ("National Union"); The Insurance Company of the State of Pennsylvania ("ICOP"); New Hampshire Insurance Company ("NHIC"); Lexington Insurance Company ("Lexington"); and Israel Discount Bank of New York ("IDB"; collectively with AIG, National Union, ICOP, NHIC, and Lexington, "Respondents"), from drawing down or releasing any funds on a letter of credit until a related arbitration proceeding is concluded.

The Insurance Programs at Play

El Ad is a real estate developer and the parent company of Riverside. Riverside is the owner of a real estate development project known as Riverside Center Site 5, located at 1 West End Avenue, New York, New York ("the Project"). Sometime in 2014, Riverside procured an Owner Controlled Insurance Program ("OCIP" or "the Insurance Program") for the Project from

National Union. The Insurance Program consists of general liability, workers' compensation, and employer's liability policies.

The parties describe the Insurance Program as being a "loss sensitive program," meaning that the cost of insurance is based on the insured's actual loss experience, as well as the amount of payroll required to compensate the contractors working on the Project. National Union also describes the Insurance Program as being a "depleting cash collateral program," meaning that Petitioners fund cash collateral, which National Union draws upon to pay losses as they occur.

In conjunction with the Insurance Program, Riverside and National Union entered into a "Payment Agreement" that governs many of the parties' respective obligations and rights. Pursuant thereto, Riverside agreed to pay "Your [i.e., Riverside's] Payment Obligation," defined as follows:

> the amounts that [Riverside] must pay [National Union] for the insurance and services in accordance with the terms of the *Policies*, this Agreement … . Such amounts shall include, but are not limited to, any of the following … :
>
> - the premiums and premium surcharges, taxes and assessments,
>
> * * *
>
> - any amount that [National Union] may have paid on [Riverside's] behalf because of any occurrence, accident, offense, claim or suit with respect to which [Riverside] [is] a self-insurer,
>
> * * *
>
> - any other fees, charges, or obligations as shown in the *Schedule* or as may arise as [Riverside] and [National Union] may agree from time to time,
>
> * * *

Riverside also agreed to post several forms of collateral to secure the "Your Payment Obligation," including a letter of credit issued by IDB for the benefit of National Union in the amount of $5,500,000.00 ("the LOC").

Under the Payment Agreement, National Union has the right to adjust claims; conduct payroll audits; and demand additional premiums and collateral from Riverside as a reserve for future losses. The Payment Agreement provides that all payments covered by the "Your Payment Obligation" are due within thirty days of the later of the invoice, notice or bill date. If, as a result of any review, National Union determined that it required additional collateral, then Riverside was to post the additional collateral within thirty days of National Union's written request and worksheet illustrating National Union's calculations. Riverside's failure to remit payment of additional premium or additional collateral within five days after its due date would constitute a default under the Payment Agreement.

Under the provision of the Payment Agreement titled "What May We Do in Case of Default?" the parties agreed that National Union could take "reasonable and appropriate steps" necessary to protect its interest.

The Payment Agreement also includes an arbitration provision, which provides as follows:

What if we disagree about payment due?
If [Riverside] disagree[s] with [National Union] about any amount of *Your Payment Obligation* that [National Union has] asked [Riverside] to pay, within the time allowed for payment [Riverside] must:

- give [National Union] written particulars about the items with which [it] disagree[s]; and
- pay those items with which [Riverside] do[es] not disagree.

[National Union] will review the disputed items promptly and provide [Riverside] with further explanations, details, or corrections. [Riverside] must pay [National Union] the correct amounts for the disputed items within 10 days of agreement between [Riverside] and [National Union] about their [sic?] correct amounts. Any disputed items not resolved within 60 days after [National Union's] response to [Riverside's] written particulars must immediately be submitted to arbitration … So long as [Riverside] [is] not otherwise in default under this Agreement, [National Union] will not exercise [its] rights set forth under "What May We Do in Case of Default?", pending the outcome of the arbitration on the disputed amount of *Your Payment Obligation*.
What about disputes other than disputes about payment due?
Any other unresolved dispute arising out of this Agreement must be submitted to arbitration.

The Disputed Demand for Additional Premiums and Collateral
On March 6, 2019, based on a payroll audit of contractors working on the Project, National Union issued an invoice to Riverside for $1,840,800.00 in additional premium due. Also, on March 15, 2019, National Union issued an invoice for $8,214,978.00 in additional cash collateral due.

On April 9, 2019, Riverside sent AIG a written dispute of the aforesaid payroll audit, including particulars about the items with which it disagreed, stating that Riverside was willing "to place in escrow the undisputed additional premium amount or, alternatively, pay half and place the other half in escrow." Additionally, Riverside requested a meeting with AIG to review the additional collateral demand.

On September 16, 2019, Riverside again disputed the payroll audit and demanded that AIG re-audit the payroll for the Project and abstain from collecting the additional premium pending the results of the audit review.

As a result of this payroll audit review, National Union adjusted the additional premium due down to $1,827,960.00 and on December 4, 2019 sent an invoice in that amount. The revised audit was also sent to Riverside's insurance broker, Willis of New York, Inc., for review. In an email dated December 18, 2019, Riverside's broker stated "[t]he audit adjustment is acceptable to us. We agree with the changes and final outcome. It has been sent to the insured … ."

Petitioners allege that on January 6, 2020, AIG advised that its credit department was awaiting the actuary review for losses for the revised collateral demand amount and that in the interim,

AIG agreed to schedule a meeting to discuss payment terms, subject to Riverside's making an immediate $250,000.00 deposit towards the latest premium invoice. Riverside thus paid $250,000.00 towards the revised additional premium demand, bringing the outstanding balance down to $1,577,960.00.

On June 17, 2020, Riverside's broker advised that AIG had expressed confidence in its calculations of the additional premium and collateral demand amounts, and that AIG demanded that Riverside immediately pay the additional premium of $1,577,960.00 and commence installment payments of additional collateral totaling $7,742,289.00.

The parties agree that Petitioners have not paid the balance of alleged additional premium due in the amount of $1,577,960.00, and that Petitioners have not addressed the alleged collateral shortfall, which National Union claims has now grown to $17,924,830.00.

On or about October 7, 2020, National Union initiated a request with IDB to draw down on the LOC. On or about that same day, National Union commenced arbitration against Petitioners by serving them with a demand for arbitration. The demand alleges that Petitioners breached the Payment Agreement by failing to pay $1,577,960.00 due for additional premiums and failing to deposit $17,924,830.00 in additional collateral. On October 9, 2020, IDB notified Petitioners of National Union's intent to draw on the LOC.

On October 12, 2020, Petitioners commenced the instant special proceeding, seeking to enjoin Respondents from drawing down or releasing any funds on the LOC until the subject arbitration proceeding concludes. On October 13, 2020, this Court issued a temporary restraining order against any draw-down of the LOC.

On October 13, 2020, National Union sent Petitioners three additional invoices for unpaid losses from July – September 2020 in the total amount of $4,021,335.78. National Union alleges that Riverside provided cash collateral in the amount of $7,362,962.10, which National Union has drawn upon to pay losses as they occurred. However, due to loss payments, the cash collateral has been reduced to $142,194.71, and Petitioners' account has incurred further losses totaling $4,021,336.00.

The Current Motion

In support of the instant motion, Petitioners argue that under the terms of the Payment Agreement, National Union is not currently entitled to draw down on the LOC. As stated above, pursuant to the provision of the Payment Agreement entitled "What May We Do in Case of Default?", the parties agreed that in the event of default, National Union could take "reasonable and appropriate steps" necessary to protect its interest. As relevant here, the Payment Agreement states:

> [National Union] may draw upon, liquidate, or take ownership of any or all collateral we hold regardless of the form, and hold or apply such amounts to any of *Your Payment Obligation* under this Agreement or any other premium, surcharge or deductible financing agreement between [Riverside] and [National Union], or under any *Policies*. However, [National Union] will not draw upon,

> liquidate, or take ownership of more collateral than is reasonably necessary to protect [its] interest.

Petitioners argue that "Your Payment Obligation" only includes National Union's request for additional premium, not additional collateral. As such, National Union cannot draw down the LOC to satisfy its demand for additional collateral; it may only be used to satisfy Riverside's obligation to pay additional premium (which is currently in dispute and the subject of the parties' arbitration proceeding). Petitioners also cite to the fact that National Union agreed that it would not draw down on more of the LOC than was reasonably necessary to protect its interest. Petitioners argue that National Union has only claimed that the current amount of "Your Payment Obligation" owed by Riverside is $1,577,960.00, which is far less than the $5.5 million LOC. In addition, pursuant to the arbitration provision within the Payment Agreement, if the parties disagree about the amount of "Your Payment Obligation," and if the parties proceed to arbitration, then "[s]o long as [Riverside] [is] not otherwise in default under this Agreement, [National Union] will not exercise [its] rights set forth under "What May We Do in Case of Default?," pending the outcome of the arbitration. Petitioners argue that they are not "otherwise in default," and, therefore, Respondents are not permitted to exercise their default remedies pending the outcome of the arbitration. Thus, in seeking to draw down on the LOC during the pendency of arbitration, National Union has knowingly and intentionally misrepresented to IDB the terms of the Payment Agreement. Petitioners also argue that they will be irreparably harmed absent injunctive relief.

Respondents assert that Petitioners' motion must be denied for a number of reasons. First, Petitioners failed to show the fraud required to enjoin a draw-down of a letter of credit, a requirement under "the doctrine of separate contracts." Second, Petitioners failed to demonstrate their entitlement to a preliminary injunction; more specifically, that on the merits, the Payment Agreement permits National Union to draw down the LOC in the instant situation; that Petitioners cannot establish irreparable harm, as their claims are nothing more than assertions of economic hardship; and that the balance of equities tips in Respondents' favor, as enjoining Respondents from drawing down on the LOC will undermine the most basic purpose of letters of credit.

Discussion

"Under the doctrine of separate contracts, a letter of credit is independent of disputes concerning the underlying contract." 410 Sixth Ave. Foods v 410 Sixth Ave., 197AD2d 435, 436 (1st Dept. 1993). UCC § 5-109(b) provides that

> [i]f an applicant claims that a required document is forged or materially fraudulent or that honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant, a court of competent jurisdiction may temporarily or permanently enjoin the issuer from honoring a presentation or grant similar relief against the issuer or other persons only if the court finds that:
> (1) The relief is not prohibited under the law applicable to an accepted draft or deferred obligation incurred by the issuer;

(2) A beneficiary, issuer, or nominated person who may be adversely affected is adequately protected against loss that it may suffer because the relief is granted;
(3) All of the conditions to entitle a person to the relief under the law of this state have been met; and
(4) On the basis of the information submitted to the court, the applicant is more likely than not to succeed under its claim of forgery or material fraud and the person demanding honor does not qualify for protection under paragraph (1) of subsection (a) of this section.

"The only way for the purchaser of a letter of credit to succeed on an action to defeat payment on that letter of credit is to demonstrate fraud in the transaction or presentment of the letter." 410 Sixth Ave. Foods, 197 AD2d at 436. Thus, "[t]he purchaser of a letter of credit 'may apply to enjoin the issuer from paying drafts down under the letter of credit' where 'fraud in the transaction has been shown and the holder has not taken the draft in circumstances that would make it a holder in due course.'" Lenox Hill Hosp. v Am. Intl. Group, Inc., 873 NYS2d 512, 512 (Sup Ct, NY County 2008) (quoting United Bank, Ltd. v Cambridge Sporting Goods Corp., 41 NY2d 254, 259 (1976)). As stated in the official commentary to UCC § 5-109,

> fraud must be found either in the documents or must have been committed by the beneficiary on the issuer or applicant. Secondly, it makes clear that fraud must be 'material.' Necessarily courts must decide the breadth and width of 'materiality.' The use of the word requires that the fraudulent aspect of a document be material to a purchaser of that document or that the fraudulent act be significant to the participations in the underlying transaction … . The courts must examine the underlying transaction when there is an allegation of material fraud, for only by examining that transaction can one determine whether a document is fraudulent or the beneficiary has committed fraud and, if so, whether the fraud was material. Material fraud by the beneficiary occurs only when the beneficiary has no colorable right to expect honor and where there is no basis in fact to support such a right to honor …

(internal citations omitted). Petitioners' argument that National Union is engaged in "fraud" proves too much; if that were the case, every contract dispute would amount to fraud, which is not the law.

In addition to a showing of fraud, the applicant must also establish that "[a]ll of the conditions to entitle a person to the relief under the law of this state have been met." UCC § 5-109(b)(3). Thus, "[f]or an injunction to issue, the requesting party must demonstrate a likelihood of success on the merits, irreparable harm, and that a balancing of the equities tips in that party's favor." 410 Sixth Ave. Foods, 197 AD2d at 436 (citing to Albini v Solork Associates, 326 NYS2d 150 (2nd Dept. 1971).

Essentially, Petitioners argue that National Union's failure to abide by the terms of the Payment Agreement (specially, that part of the Payment Agreement in which National Union agreed not to draw down on the LOC during pendency of arbitration) constitutes intentional fraud by

Respondents, such that allowing IDB to honor the draw-down would facilitate multiple acts of material fraud by Respondents.

Respondents argue that Petitioners failed to establish the elements for injunctive relief (likelihood of success on the merits, irreparable harm, and a balancing of the equities in their favor), as the Payment Agreement allows National Union to exercise its default remedies during the pendency of arbitration so long as Petitioners are "otherwise in default." Respondents contend that Petitioners are "otherwise in default" because they failed to satisfy the additional collateral demand and never tendered a formal dispute over that particular demand, and because Petitioners failed to pay the balance due for the adjusted premium demand despite the fact that Petitioners' broker accepted the adjusted premium amount, such that there is no longer a dispute as to the amount due.

In reply, Petitioners contend that they have disputed the adjusted premium and additional collateral demands despite the unauthorized and non-binding acceptance of the amount owed by its broker.

This Court finds that Petitioners have failed to demonstrate fraud in the transaction sufficient to succeed on this action to defeat payment on the LOC. Petitioners' allegations that National Union's failure to abide by the Payment Agreement provisions constitutes active intentional fraud is, at best, an assertion that National Union breached the Payment Agreement, not an assertion of fraud. See Lenox Hill Hosp. v American Intl. Group Inc., 1 Misc 3d 1123(A), *1123(A) (Sup Ct NY Cty 2008) ("The fact that [plaintiff] believes these numbers to be fabricated is evidence of a contract dispute between [plaintiff] and defendants about an unexpectedly high premium, but it does not tend to show active, intentional fraud."); 410 Sixth Ave. Foods v 410 Sixth Ave., 197 AD2d 435, 437 (1st Dept. 1993) (denying preliminary injunction because, inter alia, "[a]t best, the evidence supports solely mutual allegations of breach of contract, not fraud"); Chiat/Day Inc. v Kalimian, 105 AD2d 94, 97 (1st Dept. 1984) ("payment of a [LOC] may be enjoined only where 'active intentional fraud' is shown. In addition, the case law distinguishes between mere disputes about performance of a contract or breach of warranty and the active intentional fraud which rises to the level of fraud in the transaction.").

Furthermore, although the Payment Agreement has a broad arbitration provision, petitioners have not requested arbitration about an LOC draw-down.

Moreover, Petitioners have failed to demonstrate entitlement to a preliminary injunction, as they have failed to establish irreparable harm. Petitioners' allegations of irreparable harm are merely conclusory assertions of economic hardship, which are insufficient to satisfy their burden. See 410 Sixth Ave. Foods v 410 Sixth Ave. 197 AD2d at 437 ("[D]amages would appear to be an adequate remedy if [Tenants'] rights have been interfered with in any way. There is thus no ground for an injunction.") (internal citations omitted). Although Petitioners claim that they will be irreparably harmed, they have failed to provide this Court with any proof that this monetary loss will force them into bankruptcy; they don't even make such a claim. Furthermore, Petitioners' allegations illustrate a possibility, not a definite likelihood, that they will suffer irreparable harm.

As Petitioners have failed to establish irreparable harm, this Court need not and does not reach the issues of likelihood of success on the merits and balance of equities in its favor.

Conclusion

Petitioners' motion for a preliminary injunction is hereby denied, and the Clerk is hereby directed to enter judgment denying and dismissing the petition.

11/17/2020
DATE

ARTHUR F. ENGORON, J.S.C.

CHECK ONE:	[X]	CASE DISPOSED		[ ]	NON-FINAL DISPOSITION		
	[ ]	GRANTED	[X] DENIED	[ ]	GRANTED IN PART	[ ]	OTHER
APPLICATION:	[ ]	SETTLE ORDER		[ ]	SUBMIT ORDER		
CHECK IF APPROPRIATE:	[ ]	INCLUDES TRANSFER/REASSIGN		[ ]	FIDUCIARY APPOINTMENT	[ ]	REFERENCE