The **Commercial Division**

of The State of New York

Law Report - JULY 2004

THE LAW REPORT

A report on leading decisions issued by the Justices of the Commercial Division of the Supreme Court of the State of New York

Arbitration; FAA; AAA International Rules; Article 31; review; legal fees; FAA versus New York Law. Motions to confirm and vacate an arbitration award consisting of a declaration in respondent's favor that a Collateral Manager Event had not occurred and a monetary award of $466,000 in legal fees. Respondent was plaintiff in an action arising from a $1.5 billion transaction governed by a Warehousing Agreement with a New York choice-of-law provision. The Agreement required plaintiff, as Collateral Manager, to identify bonds for defendant's purchase which defendant would "warehouse," then use as security for bonds sold to sophisticated investors. A year into the Agreement defendant had given notice that a Collateral Manager Event had occurred, allowing the Agreement to be terminated, and plaintiff had commenced the underlying action claiming breach of contract. The parties had agreed to arbitration to resolve the issue of whether a CME had taken place. The court stayed the action pending the arbitration on the basis that the FAA, not New York law, "governed" the proceeding as it concerned commerce. Subsequently, the arbitration had been conducted under the auspices of the AAA - International Centre for Dispute Resolution, under the rules of which (Article 31) plaintiff had also sought attorneys' fees. In this motion, defendant contended that the arbitration panel had manifestly disregarded the evidence in declaring that no CME had occurred, although defendant's position, analysis revealed, was actually that the arbitrators had misinterpreted contractual provisions. It is axiomatic, the court stated, that a reviewing court may not second guess an arbitrator's resolution of a contract dispute. It had properly been for the arbitrators to decide based on the divergent evidence, which had included evidence that defendant itself had stopped working toward a transaction. The court confirmed the arbitrators' declaration. Defendant contended that the arbitrators had manifestly disregarded evidence and law in awarding the fees. The award had been made "in accordance with New York law and [Article] 31 of the International Dispute Resolution Procedures" but, defendant argued, New York does not permit such fees in the absence of malice or agreement, and the Warehousing Agreement did not mention such fees. The court declined to find that there had been malice. Plaintiff argued that defendant had consented to the fees' arbitration and that the arbitrators had not exceeded their power by awarding them. But the court distinguished the case to which plaintiff pointed for support. True, the court had confirmed a fees award on the basis that in agreeing to international arbitration the parties had also agreed to Article 31, thus satisfying the New York requirement as to agreement. But in that case, the parties had agreed to arbitrate "all disputes." Here, the parties had agreed to arbitrate only the CME issue. Thus, in view of the Warehousing Agreement's New York choice-of-law provision, the federal rule permitting award of attorneys' fees under FAA did not trump New York's requirement. Plaintiff's contention that defendants had consented to the arbitration regarding the fees in that they had allegedly omitted to take two early opportunities to object to it did not avail, either. Objection had come in time, in defendant's post-hearing e-mail submission. The e-mail had also ensured that the arbitrator was aware of the New York law and its applicability, required to establish manifest disregard. The court vacated the fees award. CIT Project Finance, L.L.C. v. Credit Suisse First Boston, Index

VOL.7, NO. 3
JULY 2004

Division Website:
www.courts.state.ny.us/comdiv

Decisions discussed were issued **May-June 2004**
An asterix marks discussions of decisions posted in PDF; all other decisions are in HTML.

No. 600847/2003, 6/17/04 (Fried, J.).

Arbitration; Rule 600(a) of the Rules of the New York Stock Exchange; shareholders' derivative action; breach of fiduciary duty; fraud; third-party action. Procedure; release; reargument. Plaintiffs, preferred shareholders of defendant securities firm, alleged fraud and a shareholders' derivative claim. Third-party defendants moved to dismiss third-party plaintiffs' claim of breach of fiduciary duty and to stay the action and compel arbitration of remaining third-party plaintiffs' claims. Defendants moved to reargue the court's decision of June 30, 2003 which denied their motion to dismiss. The third-party defendants claimed that under rule 600(a) of the Rules of the New York Stock Exchange the third-party plaintiffs must submit their claim to arbitration. Defendants contended that they were entitled to demand arbitration because defendant was a member of the New York Stock Exchange and the controversy arose out of defendant's business and because third-party plaintiffs were "associated persons" with defendant. The third-party plaintiffs argued that their claims were not subject to arbitration because they did not arise out of defendant's business. The court determined that the third-party complaint, having been directed to non-members of the New York Stock Exchange, was not related to Exchange business and thus did not fall within Rule 600(a). The court granted the motion to dismiss third-party plaintiffs' claim for breach of fiduciary duty pointing to a previously - signed settlement which expressly released third-party defendants from further liability for claims arising out of their status as minority shareholders. The court denied defendants' motion to reargue, stating that the derivative action was an appropriate means for relief as against corporate officials, as well as any third-parties who had benefitted from their misconduct. Steinberg v. W.J. Nolan & Co., Index No. 119177/2002, 5/20/04 (Lowe, J.).

Arbitration; statement of reasons for award; manifest disregard of law. Employment agreement; breach; shares as compensation. **Promissory estoppel. Res judicata; collateral estoppel.** Motions concerning an arbitration award that included $1.16 million in total to the individual plaintiff, and $2000 to his former employer, defendant. Defendant had terminated the parties' employment agreement without stating a reason. Its letter had informed plaintiff of his severance payment and provided that in exchange for signing a separation agreement with a release, he would receive an additional $434,000, representing the value of 24.3% of certain shares in defendant that had been part of his compensation under the employment agreement. The letter had stated that plaintiff had forfeited the remaining shares. Plaintiff had brought suit seeking recovery for breach of contract. In dismissing a promissory estoppel claim asserted by the second plaintiff here, a company that plaintiff had established to negotiate post-termination with defendant to form a consulting agreement, the court had found that neither a post-termination contract nor oral agreement had been entered into. The court had thus also dismissed plaintiff's claims of tortious interference. Now, in moving to vacate the award, defendant contended that the arbitrators had not applied the doctrine of judicial estoppel in awarding plaintiff $39,000 for post-termination work for defendant. It further contended that in allowing plaintiff to amend his complaint to assert an individual promissory estoppel claim the arbitrators had contradicted the court's decisions, and that the doctrines of res judicata or collateral estoppel precluded such amendment. The court stated, however, that it had implied that the individual plaintiff might well have a claim based on promissory estoppel, that it would be part of the employment agreement and subject to arbitration. Defendant argued that the elements of promissory estoppel were lacking and that the arbitrators had ignored the express terms of the employment agreement. Plaintiff had received $168,000 severance pay, even though the agreement provided for such pay only if he returned all proprietary information, and he had erased his laptop's contents. The arbitrators had not required the pay to be returned, merely that defendant receive $2000 to restore the laptop. This, however, was consistent with evidence of cost presented at trial and otherwise rational, the court said. Claims that the arbitrators disregarded an agreement that provided for forfeiture of the shares if plaintiff were terminated for "poor performance" did not avail since over seven days of hearings the arbitrators could have determined that plaintiff's performance had been exemplary, and characterization of it as "poor" not based on objective or fair criteria. The arbitrators had not given their reasons for the award, but its basis was not obscure. Award confirmed. Palowitch v. Cap Gemini Ernst & Young, US., LLC, Index No. 114312/2001, 6/3/04 (Freedman, J.).

Attorney and client; DR-5-105; attorney disqualification; conflict of interest; motion to dismiss. On third-party defendants' motion to dismiss, the court on its own initiative raised the issue under DR 5-105 of the Code of Professional Responsibility of whether plaintiffs' attorneys should be disqualified from representing third-party defendants due to a possible conflict of interest. The court had been informed during a conference that counsel for plaintiffs had also been retained to defend the third-party defendants in the third party action. The crux of the potential conflict was that if the third-party plaintiffs prevailed in their complaint, plaintiffs might have an independent cause of action against the third-party defendant. Although plaintiffs' counsel submitted three consents to representation and waivers of conflict, the court nonetheless determined that the circumstances presented a situation where the potential conflict was non-waivable. The court further rejected plaintiffs' suggestion that granting the third-party defendants' motion to dismiss would eliminate the need for the court to address the disqualification issue, stating that the granting of such motion might lead to an appeal which would again require counsel to represent the third-party defendants, thus raising the same conflict. Franklin High Income Trust v. APP Global, Index No. 602567/2002, 6/23/04 (Cahn, J.).

Comity; foreign bankruptcy proceedings; motion to dismiss. When defendant, an Israeli citizen, defaulted on a loan contract, plaintiff brought the instant motion for summary judgment in lieu of complaint. Defendant had previously filed for bankruptcy in an Israeli court. Plaintiff had also filed an additional claim against defendant in the Israeli bankruptcy proceeding with regard to a different loan. The Israeli Bankruptcy court issued a Receiving Order, which had the effect of staying all proceedings, including those for execution against defendant. Defendant cross-moved to dismiss, arguing that comity required American courts to recognize the Israeli bankruptcy proceeding. Plaintiff contended that the principles of comity would not be violated by maintaining the instant action. Plaintiff argued that it had not asserted the instant claim in the Israeli Bankruptcy court. Moreover, the bankruptcy process in the Israeli courts was substantially different from proceedings under Title 11 of the United States Code. Plaintiff further argued that defendant should have instituted a proceeding to stay in the New York Bankruptcy court pursuant to Section 304 of the Bankruptcy Code. The court found that comity should be extended to the Israeli bankruptcy proceeding and granted defendant's cross-motion to dismiss. The court explained that plaintiff would not be prejudiced by the Israeli bankruptcy proceeding because he had been aware of it and had in fact submitted himself to the jurisdiction of the Israeli Bankruptcy court when he had filed a claim there. The court also pointed out that Israel's liquidation procedures are comparable to those under the United States Bankruptcy Code. The court further found that plaintiff had had ample opportunity to pursue the instant claim in the Israeli bankruptcy proceeding and that allowing plaintiff to pursue an additional claim in New York would run counter to the purposes of comity as applied to foreign bankruptcy proceedings. Finally, the court found that although Section 304 of the Bankruptcy Code permits commencement of bankruptcy proceedings ancillary to those brought in foreign jurisdictions, it is not an exclusive remedy. Bertisch v. Drory, Index No. 603049/2003, 6/21/04 (Fried, J.).

Construction contracts; "no damages for delay" clause. Indemnification. Contribution; tort versus breach of contract; CPLR 1401. Oral agreement; parol evidence. Consolidation of related actions. Action stemming from a problem-plagued $90 million New York City Transportation Authority (NYCTA) project to build a bus depot. Plaintiff, a steel subcontractor, brought a $4.5 million breach of contract claim against defendant, the prime contractor, for change orders that included additional work plaintiff had done and charges for delay damages. The contractor brought a third-party action against the project's design professional. The court denied plaintiff's motion to sever the third-party action because the cases arose from a common nucleus of facts, the same witnesses would likely be involved, and plaintiff had failed to demonstrate prejudice to a substantial right if the third party action was not severed. Plaintiff moved for partial summary judgment on the contractor's liability for a group of change orders that it alleged were undisputed. The court denied the motion. It was entirely based on the pleadings, and the boilerplate allegations in the complaint examined beside the answer showed that although the contractor did not dispute that changes had been made, it denied plaintiff's categorization of the work and that it had directed it to do it. Material issues of fact also existed; neither the complaint nor moving papers addressed contractual conditions precedent to plaintiff's right to payment. Additionally, the subcontract contained a "no damages for delay" clause. Plaintiff had not shown that the damages it claimed for delay had arisen from the contractor's willful misconduct or gross negligence, as needed to prevail on the claim. Finally, plaintiff's motion did not even address issues of fact the contractor raised in its affirmative defenses, e.g. whether the claims were subject to the subcontract's release and waiver of claims provision limiting the contractor's liability to the extent of additional compensation it collected from NYCTA. In the third-party action, the contractor sought damages of over $11 million. Six of eight of its causes of action expressly or impliedly sought relief based on indemnification and contribution. The court granted third-party defendant's motion for partial summary judgment. Although the parties' subcontract gave the contractor an express right to indemnification, it was limited to claims for personal injury or property damages, and plaintiff's claim for contract damages did not trigger it. Implied indemnity is predicated on vicarious liability without actual fault. To recover damages the party seeking indemnity must have delegated to the party from whom it seeks indemnification exclusive responsibility for the duties that gave rise to the loss. Here, the court noted, the agreement between the contractor and third-party defendant gave the contractor exclusive control over construction and the unfettered right to approve, reject, or direct the third-party defendant's designs. In addition, defendant had exercised its right to control; e.g., third-party defendant was required to and did attend regular Design Review meetings with the contractor. Plaintiff did not allege that third-party defendant had assigned any of the contractor's contract obligations, either; its allegations were all claimed breaches of the contractor's duty for which third-party defendant could not have been responsible. The contractor contended that the complaint was not just a breach claim and that the third-party defendant was liable for damages that could be attributable to plaintiff's delay claims. However, the contractor's contract with NYCTA, and subcontract with the plaintiff, both had exculpatory provisions precluding delay damages, on one of which the contractor admittedly relied as a defense to plaintiff's delay claim. Thus, third-party defendant was insulated from an indemnity claim because plaintiff did not allege that it was guilty of willful misconduct or gross negligence. The claims based on indemnification were dismissed. As for contribution, it distributes a loss among joint tortfeasors. Here, the plaintiff sought economic damages for breach, for which contribution is unavailable, the court stated. Even where tort has been alleged, whether contribution is available is determined by the measure of damages sought, and the plaintiff sought only benefit of its contractual bargain. The contractor attempted to transform the underlying action into one that sounded in tort by suggesting that the court look to the professional negligence claims it had interposed, rather than to plaintiff's claims. But the only case it offered in support was irrelevant. The cause of action based on contribution was dismissed. The contractor also claimed breach of an oral agreement that pre-dated the written subcontract. The parol evidence rule barred the assertion of an oral agreement inconsistent with the written contract. The contractor alleged, in its response to the summary judgment motion–and for the first time–that the oral agreement had been a "Teaming Agreement," independent and wholly separate, and that the written merger clause did not bar a separate claim for breach. But its affidavits lacked details about who allegedly had reached an oral agreement and certain written memos purportedly in evidence of the agreement lacked language indicating a meeting of the minds and were signed only by the contractor. A breach of warranty claim against third-party defendant was dismissed since the warranties could only be triggered by the NYCTA alleging breach against the contractor, which did not occur here. The court granted the contractor's cross-motion to consolidate a second action it had started in Westchester against a subcontractor. Plaintiff argued that the cases lacked common issues, but its own claims for "inefficiencies" that had cost it man-hours constituted delay claims, the court found. Moreover, its complaint unequivocally alleged delay. The argument of defendant in the second action opposing consolidation also failed as it ignored the temporal link between the subcontractors' work. Nor could the forum selection clause in its subcontract bar consolidation. The prime contract incorporated by reference into the subcontract provided for commencement in or transfer to New York County, and courts have found that an otherwise valid forum selection clause must give way when it would contravene the public policy that favors consolidating similar actions. Metropolitan Steel Industries, Inc. v. Perini Corp., Index No. 104341/2002, 6/14/04 (Cahn, J.).

Contracts; construction; Lein Law 34; "pay when paid"; public policy. Subcontractor sued GC for almost $3 million for work and materials. Defendant refused to pay, citing a clause making payments contingent on its receipt of payment from the owner, now insolvent. Plaintiff relied upon Lein Law § 34, which declares provisions waiving the right to enforce a lien against public policy. The court held that this law and a Court of Appeals decision interpreting it rendered the clause at issue in this case unenforceable. Summary judgment for defendant denied; affirmative defense stricken. Hugh O'Kane Electric Co. v. Mastec North America, Inc., Index No. 600391/2002, 5/6/04 (Ramos, J.).

Contracts; interpretation. Summary judgment; unjust enrichment; equitable estoppel; unclean hands; Rule 19-a of the Commercial Division. Plaintiff moved for summary judgment in litigation relating to a settlement agreement entered into by defendant, actress Elizabeth Taylor, following a 1985 agreement between the parties to market Taylor's name. Plaintiff contended that it was entitled to 12.5% of the total compensation under the 1985 agreement; that defendant's refusal to pay plaintiff as assignee was an actual and anticipatory breach of the 1985 agreement; and that the 12.5% of the total compensation was owing under the theory of unjust enrichment. Defendant counterclaimed for contribution and setoff against any amount plaintiff was to receive in the instant action and further counterclaimed for breach of contract for plaintiff's alleged failure to pay legal costs incurred in the underlying litigation. Plaintiff argued that the 1985 agreement contained an irrevocable grant, tantamount to a gift, to its assignor of the 12.5% interest as the agreement lacked contractual formalities. Defendant countered that the 12.5% was in fact a bargained-for exchange between the parties and that the amount was contingent on plaintiff's future performance. Defendant further contended, *inter alia,* that summary judgment should be denied because plaintiff had failed to comply with Rule 19-a of the Commercial Division, which requires parties moving for summary judgment to provide a statement of material facts not in dispute. The court granted plaintiff's motion only to the extent of dismissing the affirmative defense that plaintiff's assignor had violated the Code of Professional Conduct in its representation of Taylor and the Elizabeth Taylor Cosmetic Company, finding that the defendant lacked standing to assert that claim. The court further found that the language of the 1985 agreement lacked the elements necessary for the 12.5% interest to have been considered an irrevocable transfer and that questions of fact remained about the intent of the parties which might be resolved by examination of the parties' prior course of conduct. The court determined next that a letter sent by plaintiff's assignor to defendant regarding payment of the legal fees constituted an offer to make a unilateral contract and that questions of fact remained as to whether defendant had acted upon that offer, and, if so, whether plaintiff's assignor had opted out. The court further denied plaintiff's motion because it had failed to comply with Rule 19-a of the Commercial Division, explaining that in addition to seeking dismissal of the counterclaims and affirmative defenses, plaintiff sought summary judgment on the first two causes of action and was thereby required to comply with the rule. The court then denied dismissal of the remaining affirmative defenses, finding that the defenses of both equitable estoppel and unclean hands were appropriate since the third cause of action for unjust enrichment was an equitable claim. U&B Properties v. Aries Design Management, Inc., Index No. 101460/2003, 6/3/04 (Cahn, J.).

Contracts; interpretation; termination provision. Plaintiff, a limited liability company, marketed and sold motivational products. Plaintiff and defendant entered into an agreement whereby stores selling plaintiff's products would be operated inside defendant's locations in return for which plaintiff was to make revenue share payments. The parties also negotiated a termination provision by which either party could terminate the contract. When plaintiff had failed to make timely payments for several months, defendant had sent plaintiff a letter terminating the agreement. Plaintiff brought this action and moved for summary judgment, claiming that defendant's termination where the agreement without notice and opportunity to cure was a breach of contract. The case turned on the interpretation of the agreement's termination clause, specifically whether a provision authorizing termination where the agreement was "demonstrably injurious" was exclusive such that plaintiff would have had, as set forth therein, a 60-day opportunity to cure. Defendant contended that the agreement's termination clause was not exclusive and that plaintiff's material breaches allowed for termination without notice and opportunity to cure. The court concluded that the termination clause was not exclusive, explaining that the disputed term, "demonstrably injurious," was not unequivocally the equivalent of a material breach. Plaintiff's motion for summary judgment was denied. Inspire Someone, LLC, v. Kinko's Inc., Index No. 603105/2003, 5/5/04 (Ramos, J.).

Contracts; negotiations. Art; auction house. John Doe; cause of action; identity revelation. Procedure; service of OSC. Agency. Plaintiff's president, in search of a painting from Andy Warhol's 1981 "Mickey Mouse" series, had contacted defendant auction house and learned that defendant John Doe was offering such a painting in the $1 million price range. The president and the defendant auction house had negotiated for three days, after which the house had e-mailed the president that the painting's price would be $660,000. The president had allegedly responded asking the house to reserve the painting at that price for two weeks. At the end of nearly two weeks, the president had e-mailed to tell the house "your offer of $660,000 is accepted" conditioned on his personally confirming that the work was in good condition and signed. The house had phoned the president a few days later to say that the painting was no longer available; allegedly, it said in a phone conversation later that day that the painting was available but would cost $1.4 million. The plaintiff brought this suit and moved by OSC for an order directing the defendant auction house to reveal John Doe or accept service of all papers on his behalf. The plaintiff also sought to enjoin the defendants from selling the painting and to appoint a receiver for it. John Doe argued that the service of the OSC upon him was untimely. The argument failed. The defendant auction house had been timely served, the OSC provided that the auction house would accept service for John Doe, and the house had punctually faxed him the papers and delivered them to him personally the next day. The court agreed, however, that the plaintiff failed to state a cause of action against John Doe. The plaintiff did not allege any facts that demonstrated that it had an agreement with John Doe, or that the auction house had entered into a definitive agreement to sell the painting as Doe's agent. The plaintiff's allegations showed that efforts had been made to create a contractual relationship between the plaintiff and the house, or between the plaintiff, the house and John Doe, but not that the relationship had actually been created. The plaintiff's motion was denied in its entirety. Sands & Co., Inc. v. Christie's Inc., Index No. 600268/2004, 5/28/04 (Ramos, J.).

Contracts; real property purchase; readiness to close. Plaintiff moved to renew and reargue its opposition to defendants' motion for summary judgment in a contract action. The action arose out of plaintiff's alleged default on a contract to purchase a supermarket from defendants. Defendants alleged that on the day before the scheduled closing, plaintiff had requested an extension of time which defendants refused to grant and that on the following day plaintiff showed up unprepared to close. Plaintiff contended that it had come to the closing ready, willing and able to close but that defendants had failed to tender a properly executed deed so plaintiff refused to tender payment. The court noted that the contract between the parties could not be modified absent a signed writing. Moreover, plaintiff's letter, which included a final "time of the essence" extension of the closing, provided for no further extensions. The letter indicated that if purchaser defaulted and failed to close, seller had the right to retain the remaining down payment. After reviewing the terms of the contract of sale, the court concluded that the defendants' documentary evidence supported their right to judgment as a matter of law, and that plaintiff had failed to establish that it had been ready, willing and able to perform at the closing or raise triable issues of fact on that issue. Summary judgment granted; complaint dismissed. Realty Equities, Inc. v. Waldbaum, Inc., Index No. 5697/2003, 5/19/04 (Rudolph, J.).

Corporations; de facto merger doctrine; continuity of ownership; lease versus acquisition. Subsidiary as alter ego. Unjust enrichment. Quantum meruit. Plaintiff was a medical supply company that had obtained a default judgment of $1.2 million against a hospital in a breach of contract suit. Plaintiff alleged that one defendant, a medical center that had leased the hospital's property to run its own operations, was liable for the debts of the hospital as its successor under the de facto merger doctrine. Plaintiff contended that the medical center had first controlled the hospital through its co-defendant, its subsidiary, which had been formed to manage the hospital for a fee. Plaintiff further contended that after the hospital had developed financial problems and formed a settlement agreement with a State creditor, the medical center had taken the hospital over directly by leasing its premises and conducting hospital operations there. However, documentary evidence refuted plaintiff's de facto merger allegations. Co-defendant subsidiary's management agreement with the hospital stated, among other things, that neither party was the other's guarantor and the hospital alone was responsible for its operating costs. The hospital's agreement with its State creditor had required the hospital to deposit rents and receipts into a pledge fund and assign all rights to the creditor, and put its assets in a lock box operated by the creditor. That the medical center had had no rights in regard to the lock box, pledge fund, or settlement agreement was expressly stated in a funding agreement between the defendant and the State creditor that had governed the defendant's operations on the hospital's premises. The court determined that the medical center had not purchased or acquired the hospital's assets. There had been no continuity of ownership, and the hospital had not dissolved; thus, two requisite criteria of de facto merger were not met. Plaintiff asserted that more discovery was needed but failed to show it was likely to lead to evidence of triable issues of fact. Plaintiff's claims of unjust enrichment and for quantum meruit also failed. Based on the terms of the relevant contracts, plaintiff's goods and services had been supplied to and accepted by the hospital, not defendants. Further, the court stated, unjust enrichment and quantum meruit claims are precluded where an express agreement governs the subject matter, and an express contract had existed between the hospital and plaintiff, its supplier. Claims were dismissed. Micro Bio-Medics, Inc. v. Westchester Medical Center, Index No. 9578/2003, 6/18/04 (Rudolph, J.).

Corporations; de facto merger doctrine; criteria; tort versus contract. Employer-employee relationship. Joinder of predecessor in interest. Plaintiff sought to recover a default judgment of over $23 million based on the de facto merger doctrine, alleging that defendant mortgage corporation was successor in interest to the liabilities of a mortgage bank against which default judgments had been obtained in South Carolina and New York. Plaintiff alleged that three days before the bank had had to surrender its license due to involvement in certain lending schemes, it had entered into a Regional Manager Employment Agreement with defendant whereby the bank's CEO, a 50% shareholder in the bank, would operate a mortgage-related division of defendant using the bank's essential operating assets. In a motion to dismiss, the court found that one of four criteria for de facto merger, continuity of ownership, was lacking because there had been no stock transfer between the bank and defendant. Defendant cited a case in which the Second Department had held that de facto merger was relevant to product liability but not in an action seeking to collect on a promissory note. The court found that more recent authority held that the doctrine was and should be applied in the context of contractual obligation, but in that context continuity of ownership is a prerequisite. Plaintiff relied on various cases to argue that it was not. But there was stockholder, and thus ownership, continuity in those cases. In another, the deciding court distinguished between applying the doctrine in contexts of tort liability and commercial obligation, based on policy considerations; commercial entities generally consider business failure and loss allocation when drafting a contract, while such provisions are beyond someone buying a retail product. Plaintiff further argued that in any case it had alleged facts showing continuity of ownership, that the employment agreement between defendant and the bank CEO allowed the CEO a salary of zero and all of the division's profits, and that this demonstrated that the CEO should be treated as an owner or shareholder of defendant. The court noted that an employer-employee relationship may exist despite the fact that the employee's compensation is based upon the success of her/his efforts. Here the agreement's terms concerning reimbursement to a manager advancing his own funds for branch expenses evidenced defendant's strict control over the division. The agreement also included classic indicia of an employer-employee relationship, and the CEO did not assume risks in loan delivery or liability for bad loans. Plaintiff pointed to the agreement's addendum, which stated that the CEO would acquire the division's trade name when the agreement ended, to suggest that the CEO had acquired an ownership interest in defendant. The CEO was precluded from removing any material related to the branch's business, however. And absent continuity of ownership, that the branch office was in the same site that the mortgage bank had occupied, and employed some of its employees, did not establish a de facto merger. The court also found that the fourth criterion for de facto merger, assumption by the purchaser of the acquired corporation's liabilities, had not been met. Finally, the court noted that although the employment agreement had been executed well before the start of the actions that had led to default judgments against the bank, in neither had the current defendant been made party. That it had been plaintiff's predecessor in interest's failure to join defendant, when it had already employed the CEO, did not alter the failure's effect. Complaint dismissed. Washington Mutual Bank, FA v. SIB Mortgage Corp., Index No. 1281/2004, 6/18/04 (Demarest, J.).

Discovery; subpoena to non-party foreign entity; Hague Convention. Motion to quash subpoena directed to non-party foreign bank. Movant had no responsive documents in New York, nor any employees with knowledge of the facts. The court held that the subpoena was improper because China, like a civil law nation, would regard non-judicial taking of evidence as an affront to its sovereignty. The procedures of the Hague Convention are virtually compulsory and necessary here. A United States-based arm of a corporation is not required to produce documents not located here. Motion granted. Nam Tai Electronics, Inc. v. UBS Painewebber, Inc., Index No. 602976/2003, 5/18/04 (Ramos, J.).

Executive Law § 12; Indian Gaming Regulatory Act; New York State Constitution Art. III § 1, and Art. IV § 1; ripeness; Seneca Nation Land Claims Settlement Act; standing; State Finance law § 123-b; summary judgment. All parties moved for summary judgment in an action which arose out of a memorandum of understanding and a Tribal-State Compact which was to authorize the establishment of three gaming casinos by the Seneca Nation on Indian Lands in New York. Plaintiffs claimed that certain language in the compact authorizing the Seneca Nation to locate a casino anywhere in Erie County outside of the City of Buffalo negated the legislative intent behind Exec. Law § 12 and violated the separation of powers under the New York State Constitution, and should be severed from the compact. Plaintiffs further sought a permanent injunction barring defendants from transferring certain property to the Seneca Nation, and from carrying out, assisting in or authorizing the placement of a Seneca Nation casino anywhere in Erie County outside the City of Buffalo. Defendants, the Governor and the State, argued that plaintiffs lacked standing to sue, that the action was prematurely brought and that the Seneca Nation was an indispensable party. Defendants argued that the compact was consistent with the memorandum of understanding and that a provision in the compact permitted the Seneca Nation to operate a casino, with the Governor's consent, anywhere in Erie County. The defendants further contended that the relief sought by plaintiffs would require reformation of the compact, a remedy they maintained was barred by the compact's severability clause; by the absence of the Seneca Nation as a party; and by the doctrine of Federal preemption. The court granted summary judgment to the plaintiffs, determining first that State Finance Law §123-b provided standing to certain plaintiffs to challenge allegedly unconstitutional or illegal expenditures of State funds under the memorandum of understanding, Exec. Law § 12, and the compact. The court next determined that the action had not been prematurely initiated by plaintiffs, pointing out that numerous steps had been taken towards the establishment of a third casino by the Seneca Nation in Western New York, among them: the execution of the memorandum of understanding by the Governor and the Seneca Nation; the passage of enabling legislation; execution of the compact authorizing Class III gaming; and a letter of intent entered into for the transfer of property. Moreover, the fact that the Secretary of the Interior had tacitly approved the compact, as well as the lack of indication that any municipal or Federal action would be taken during the comment period provided for in the Seneca Nation Land Claim Settlement Act, left open the possibility that the Seneca Nation might purchase the land with Settlement Act funds. Such purchase would have had the effect of foreclosing the State Courts's jurisdiction over the land and rendering unreviewable the relevant State Constitutional issues involved. The court next addressed defendants' allegation that the Seneca Nation was an indispensable party, citing the Court of Appeals decision in *Saratoga III*, and finding that this case involved the court's interpretation of portions of the memorandum of understanding, Exec. Law § 12, and the compact, along with constitutional provisions so that the nonjoinder of the Seneca Nation was excused. The court, citing *Saratoga I* and *III,* found that there was no Federal preemption over the questions raised. The court explained that although the Indian Gaming Regulatory Act completely preempts the area of regulation of gaming on Indian lands, such preemption would not negate State Constitutional and statutory law regarding issues relevant to the execution of a Tribal-State Compact because the Federal Act seeks to facilitate relationships where tribes might seek extension of State jurisdiction and the application of State laws to activities conducted on Indian land. The court determined that the issue of the location of the Erie County casino was a matter properly within the ambit of the New York State Legislature in the exercise of its policy-making power. The court next found that while the Seneca Nation had the authority to propose an alternate site for the casino, it could not select or choose the site unless permitted to do so by the memorandum of understanding and by Exec. Law § 12. The court elaborated that use of the words "select" or "choose" would divest the Legislature of its sovereign policy-making authority under Art. III § 1 of the New York State Constitution. The court concluded that the memorandum of understanding and subparagraph 11(a)(2) of the compact were inconsistent on the issue of the Seneca Nation's authority to determine the municipal location of the casino in Erie County outside of the city of Buffalo. The court concurred with plaintiffs that it had been the Legislature's intent in enacting Exec. Law § 12 that the two agreements be consistent with each other on that issue. The court further found that the inconsistent language contained in the same subparagraph which allowed the Seneca Nation to determine an alternate site for the casino was also unconstitutional under Art. III § 1 of the Constitution. The court determined that the inconsistent language was to be severed from the compact with all remaining provisions of the compact to be given full force and effect. The court stated that this would not constitute a reformation of the compact. The court enjoined the sale and transfer of property to the Seneca Nation for the purposes of development or construction of a class III gaming facility. Finally, the court denied defendant's cross-motions to dismiss. Huron Group, Inc., v. Pataki, Index No. 4425/2004, 6/16/04 (Makowski, J).

Insurance; joint loss; business income loss calculation; extra expenses. Equitable estoppel. Post-trial decision. Defendant insurance company had paid one plaintiff $793,000 following a fire that had destroyed its premises. Plaintiffs were a laminate counter-top manufacturer at whose premises the fire had occurred, and its subsidiary, a granite counter-top manufacturer that operated entirely from separate facilities except for certain bookkeeping. Both were named insureds. Plaintiffs alleged that defendant had undervalued the claimed loss of business income that they had suffered due to the fire. Plaintiffs contended that defendant should be estopped from disclaiming coverage to the granite-top plaintiff because, they argued, up until trial defendant had treated the loss as a joint loss except in one initial report. That report had subsequently been recalculated to reflect joint losses, after the laminate-top plaintiff had told defendant that some of the granite-top business had been conducted from its premises and defendant's review of certain ledgers had indeed shown granite-top sales from the facility. But records defendant had later received showed that the granite-top sales had only reflected orders that the laminate-top plaintiff had outsourced before its subsidiary had acquired a granite-top manufacturer. Plaintiff, having been aware of facts corroborating defendant's original method of calculation, was not entitled to the protection of equitable estoppel, the court found. The granite-top plaintiff's claim for loss of business income also failed on the merits, because, except for some bookkeeping, all granite-related operations had been moved to its separate facility before the fire loss. Despite plaintiffs' vice president's "vacillating and unsure" testimony attempting to connect the granite operations to the fire losses, he and a manager of the granite-top facility both also testified that granite operations had continued uninterrupted after the fire. Not only did plaintiffs fail to establish that the granite-top plaintiff had suffered direct physical loss or damage or that its business had been interrupted due to the fire, it was also clear that a decline in its revenues did not result from the fire. According to the granite-top plaintiff's manager, the plaintiff had not sustained the customer base of the manufacturer it had bought, and there had been poor quality control. Even if the granite-top plaintiff's income was included in the insurance coverage, defendant had not undervalued the claimed loss of business income. Plaintiffs' assumption of a 28% growth rate for the businesses if not for the fire ignored their poor performance for several months up to the fire, and was based on the laminate-top plaintiff's growth during the anomalous period of its launching its granite out-sourcing activities. Moreover, defendant's expert had arbitrarily added $200,000 to the figure derived from the 28% rate. And, to obtain the total business loss, he had added another $471,000, which he indicated was a deferred receivable from sales when in fact it was a deferred asset due under the insurance policy. More reliable, the court found, was defendant's analysis and finding of a 2.56% sales growth factor for the businesses; applying that rate resulted in a total loss of business income equal to defendant's payment. Plaintiffs also claimed, without success, extra expenses that defendant had rejected. Given defendant's direct payments to the laminate-top plaintiff of $300,000 without use restrictions, and payments to its vendor, within months of the fire, plaintiffs failed to establish that interest paid on a revolving line of credit had been an expense incurred to minimize business interruption. A claim for labor inefficiencies related to the plaintiff's move to a temporary site was not supported by documentary or expert proof. Nor was it clear whether estimates of the inefficiency took into account that the plaintiff had been compensated for its entire payroll for the first 90 days after the loss. Miscellaneous expenses did not meet the insurance policy's category definition. Case dismissed. Arcy Plastic Laminates v. Travelers Indemnity Co. Of Illinois, Index No. 5400/2001, 6/4/04 (Benza, J.).

Insurance; property damage; advance approval of repairs; estoppel; timeliness of disclaimer. Plaintiff, a construction company, alleged breach of contract. Defendants, insurance companies, sought summary judgment declaring that they had no obligation to reimburse plaintiff for repair costs. Plaintiff had subcontracted with a roofing company to construct the roof of a hotel, which had subsequently leaked, causing significant damage. Prior to notifying the insurance company of any claim, plaintiff hired a new roofing company to repair the defective roof and hired another company to repair the hotel's interior. Plaintiff first sought compensation for the repairs necessitated by the subcontractor's defective work from that subcontractor's insurance company, but the claim was denied. Plaintiff then submitted the claim to its insurance company, which disclaimed coverage because the repairs had not been pre-approved in accordance with the terms of the policy. The court agreed and found that plaintiff could not be reimbursed for the repair costs because it had failed to comply with the terms of the policy. Plaintiff further argued that defendants should be estopped from disclaiming coverage under the policy as they had failed to provide timely notice that they would disclaim. The court determined that there were no grounds for estoppel. The court explained that the eight-month period which had transpired after plaintiff had submitted the notice of claim to the insurer and before coverage was disclaimed was timely, given that defendants had sent plaintiff a letter containing a reservation of rights while the carrier investigated the claim. The court further pointed out that there had been correspondence and documents exchanged between plaintiff and defendants spanning the eight-month period, and the insurer disclaimed within nine days of receiving all the documents from plaintiff. The court held that plaintiff's reliance on Insurance Law § 3420 was inappropriate as that statutory provision applies to coverage for death and bodily injury, not to claims for property damage. The court further explained that, notwithstanding the statute's inapplicability, the Court of Appeals has determined that the length of time for a disclaimer should depend on all the facts and circumstances and the reasons for the delay. Summary judgment to defendants; complaint dismissed. Spoleta Construction Corp. v. CNA Insurance Co. Index No. 08918/2002, 5/21/04 (Stander, J.).

Insurance; terrorism risk; "all risk"; "force-placement" of coverage; reasonableness of premiums. Mortgage loan agreement. Plaintiff borrower sought a declaration that the terms of a commercial mortgage agreement did not obligate it to obtain and maintain terrorism insurance and to pay a $2.1 million premium for the insurance that defendants had purchased. Defendants, trustee for holders of $500 million in mortgage certificates that the lender had sold to secure the mortgage loan, and a mortgage company servicing the loan, counter-claimed for a declaration that plaintiff was obligated to maintain the insurance and pay the premium. The parties moved for summary judgment. The subject property was land and a building on Park Avenue near Grand Central Station allegedly worth $900 million. On execution of the mortgage agreement plaintiff had become a named "insured" on an "all risk" blanket policy for $6 billion, the "2000 Policy," that covered the property and that did not exclude the risk of terrorism. The 2000 Policy expired in October 2001. Plaintiff's related corporate entity had allegedly had difficulties in finding an insurer not excluding terrorism coverage from its "all risk" policies after "9/11." It had acquired a $1 billion policy for its portfolio of properties, including the subject property, that contained a sub-limit of $1 million for losses due to terrorism. Defendant mortgage company had then demanded from plaintiff evidence within 10 days of "insurance coverage for terrorist acts in an amount not less than the unpaid principal balance of the Loan." The parties had exchanged various communications regarding whether plaintiff would be in default if it did not obtain at least $500 million of insurance coverage for terrorist acts for the property, and about the defendant's continuing inquiries into the insurance market, which the plaintiff alleged interfered with its own interests in seeking additional coverage. After the plaintiff's related entity had gotten a blanket terrorism policy that covered its portfolio of properties for up to $200 million on each property, a defendant had made its own inquiries regarding an additional $300 million of terrorism insurance for the property. It had gotten quotes of premiums of $350,000 and $3 million. Concurrently, the defendant had learned from rating agencies that the mortgage certificate ratings risked downgrade due to the terrorism coverage issue; subsequently, the agencies had indicated that coverage of $350 million, rather than $500, would suffice. At that point, the defendant had contacted plaintiff that it intended, by the close of business, to bind $150 million in additional terrorism coverage for the property at a $2.1 million premium. Without hearing from plaintiff the defendant had "force-placed" the coverage and sent plaintiff the invoice. Among plaintiff's complaints were that the new policy was flawed and far overpriced, and that the defendant had been aware that plaintiff itself had been negotiating at the same time with the new insurer to obtain more coverage. Although the mortgage agreement did not include the words "terrorism" or "terrorist acts," it provided that plaintiff would obtain and maintain insurance "insuring against any peril now or hereafter included within the classification 'All Risk'...in an amount equal to 100% of the 'Full Replacement Cost.'" The court noted that New York courts have found that, prior to 9/11, "all risk" policies included losses caused by acts of terrorism since terrorism was not specifically excluded. The 2000 Policy had thus covered risk of terrorism. The court found that the mortgage agreement language made clear that the parties had considered the fact that "all risk" policies would vary over time, and that they had intended to expressly cover all perils as of the agreement's date, including risk of terrorism. It distinguished a recent case in which the parties' agreement had used different wording. Plaintiff's argument that this interpretation made a later "other insurance" clause meaningless failed. That clause required "such other insurance...as Lender...may reasonably request against such other insurable hazards which at the time are commonly insured against for other first class properties... comparable to the Property." Had terrorism been excluded from the 2000 Policy, and the risk had subsequently become commonly insured against for comparable properties, defendants could have requested terrorism risk coverage under this clause, in which case the reasonable amount and price of the insurance would present questions of fact. The court accordingly granted defendants' motion for summary judgment that plaintiff was obligated to obtain and maintain $500 million in terrorism insurance through the term of the mortgage. The court further ruled that, pursuant to another clause in the agreement, defendants had the right to force-place terrorism insurance up to $500 million. However, the court was unable to determine whether the $2.1 million premium for the force-placed coverage was reasonable. It denied summary judgment to either side on that issue and declined to release $2.1 million in an escrow account plaintiff had established at the outset of litigation. BFP 245 Park Co. LLC v. GMAC Commercial Mortgage Corp., Index No. 601937/2002, 5/13/04 (Lowe, J.).

Intentional infliction of emotional distress; negligent misrepresentation; fraudulent misrepresentation; negligence; Public Health Law 2442. Action arose after a Columbia University professor as part of a study wrote admittedly false letters to a number of New York City restaurants claiming that his wife had suffered food poisoning after dining at their establishments. While the case was still in the pre-answer stage, plaintiffs made a motion for leave to file a second amended complaint. The court found first that plaintiffs had corrected defects in their previous pleadings and now pled with specificity their claims for intentional infliction of emotional distress. The court next determined that plaintiffs' claims for negligent misrepresentation and fraudulent misrepresentation could stand, citing to previous decisions by Justice Gammerman and the First Department rendered in this case. The court also ruled that these claims would not doom the intentional infliction claim since the claims sought different damages. The court, however, dismissed plaintiffs' negligence claim, stating that in order to allege negligent supervision, there must be, but was not, an allegation that the professor's employers "knew or should have known" that he was conducting such a potentially harmful study. The court further dismissed as insufficient plaintiffs' allegation under Public Health Law 2442, stating that the statute refers to human research conducted in institutions or agencies under the ambit of the Commissioner of Health of the State of New York and here it had not been alleged that Columbia University or its business school qualified as such agencies or institutions. Chez Josephine v. Columbia University, Index No. 101362/2002, 6/29/04 (Fried, J.).

Limited liability company law; Partnership Law § 62; dissolution. Petitioner, an aggrieved business partner, sought to dissolve a limited liability company pursuant to Partnership Law § 69(1), or the Limited Liability Company Law. Petitioner's chief argument for pursuing dissolution pursuant to Partnership Law was that the company's members had never adopted an operating agreement. The court determined that the argument was meritless, explaining that the Limited Liability Company Law has no provision which would create a penalty for failure to adopt an operating statement and that neither statutes nor common law support a conclusion that failure to adopt an operating agreement transforms a limited liability company into a partnership. The court pointed out that articles of organization were filed designating the entity as a limited liability company; thus, it was governed by the Limited Liability Company Law. Respondents argued that their certification of authority, LLC operating agreement amendment and an interim voting agreement were sufficient to have qualified as an operating agreement under the statute. The court found that the certification of authority did not qualify as an operating agreement as it had only been signed by the company's president and was not a written agreement of the members. The court next determined that while the operating agreement amendment was sufficient in its form to qualify as an operating agreement, it had expired in June 2002 and was thus no longer effective. The court next examined the company's interim voting agreement and found that it was sufficient to qualify as an operating agreement only to the extent of voting issues. The court explained that in the absence of a formal operating agreement, the statute provides default provisions applicable to the conduct of limited liability companies. On an application for judicial dissolution, the court must determine the issue of whether or not it is reasonably practicable to carry on the business in light of the statutory default provisions. The court decreed judicial dissolution of the company, finding that when the members locked petitioner out of the business by changing the locks and computer passwords, they removed him from the LLC and thus activated the dissolution and winding up process. Finally, the court directed the winding up of the company's affairs pursuant to the Limited Liability Company Law § 703 and § 704, and directed the company's remaining members to provide a full accounting of the business to the court. Spires v. Lighthouse Solutions, LLC, Index No. 12560/2003, 5/2004 (Stander, J.).

Negligence; fiduciary duty; insurance brokers. Misrepresentation; reliance; parole evidence. Procedure; statute of limitations; continuous representation. The court dismissed plaintiff's claims of professional negligence, fraud, and breach of fiduciary duty. Plaintiff had been 60 when she bought two "Life-Paid-up at Age 98" life insurance policies and a variable annuity from the defendant company. She alleged that the defendant broker had orally represented that the premiums would "vanish" and the policies meet her specific financial needs after seven years. The court agreed with defendants that the three-year statute of limitations barred the claims for professional negligence and breach of fiduciary duty. The continuous representation doctrine did not change the tolling of the statute, as insurance brokers are not "professionals," and plaintiff did not describe a long-term advisory relationship unrelated to the policies' issue. The negligence claim failed. Although insurance brokers are licensed, they are not required to have specialized education and training and are not bound by a code of conduct imposing standards beyond those of the marketplace. Generally, brokers owe no fiduciary duty. In an exceptional situation where a broker comes to owe a fiduciary duty to an insured, it is the latter's burden to show that the broker undertook specific obligations exceeding those fixed in the common law that would warrant imposing the duty. Plaintiff made no specific allegations that the defendant broker had ever advised her about any other "investments." Her allegations that the broker had held himself out as having financial expertise, and that after buying the policies she had received advice from defendants while continuing to pay premiums for approximately four years, did not themselves establish the special relationship necessary to retroactively impose a fiduciary duty with respect to the policies. The court cited a case in which the significant circumstances in the broker-insured relationship did not impose a greater duty even though the circumstances had continued for several decades. The court also distinguished a case in which similar claims had survived dismissal based on documentary evidence. Here plaintiff neither elucidated her allegations of a fiduciary relationship, nor offered evidentiary proof such as an affidavit in response to defendants' evidence and arguments. Plaintiff thus failed to establish an "exceptional situation" that had differed in any material respect from "practice of the art of salesmanship" on the broker's part. As to the fraud claim, the representations alleged were too speculative to be actionable, except that the premiums would "vanish" after seven years. This, though, was directly contradicted by the premium schedule that stated that premiums were payable for 38 years based on plaintiff's age of 60. The parole evidence rule barred plaintiff's claim of relying on the broker's oral representation in the face of a complete written agreement, and although the policies' merger clause would not have excluded parol evidence in establishing fraud in the inducement, plaintiff failed to set forth with enough particularity even fraud's most rudimentary elements. In ruling that there were no cognizable causes of action, the court also noted that although plaintiff complained that the policies were not self-sustaining after seven years, seven years had not elapsed since their purchase, so the claims were either premature or insufficiently articulated. Tesoriero v. Metlife, Index No. 46200/2003, 5/13/04 (Demarest, J.).

Preliminary injunction; leases; res judicata; collateral estoppel. Plaintiff moved for a preliminary injunction in a dispute which arose from defendants' plans to construct a car wash in a shopping center. Plaintiff complained that the construction was encroaching on land leased to it and would also result in a loss of square footage in the common area of the shopping center. The court denied plaintiff's motion, finding that there were no provisions in the lease restricting the landlord from building on a portion of the common area. The construction in fact would not encroach on land leased to plaintiff. Moreover, defendants' proposed construction plan promised that additional common area would be added. The court pointed out that the lease contained no guarantees as to the amount of common area to be provided to tenants. The court further determined that neither the doctrine of res judicata nor collateral estoppel was applicable here as the facts in the previous Taco Bell litigation were dissimilar. The court explained that in Taco Bell the proposed taking from the common area was much greater and would have caused irreparable harm. Further, the construction here would bring updates and renovations to the center. The balance of equities, including plaintiff's delay in taking action, favored defendants. Century Liquors Inc., v. BMJ Properties, LLC, Index No. 02744/2004, 5/21/04 (Stander, J.).

Procedure; consent to jurisdiction; exclusivity; CPLR 3213; instrument for payment of money only; preferred stock subscription agreement. CPLR 3213 motion-action seeking recovery of $44 million pursuant to a subscription agreement for preferred stock and guaranty. With regard to a consent to jurisdiction by defendant Philippine corporations, defendants argued that it provided for an exclusive forum and plaintiff had already commenced a Federal action. The court held that the agreement and guaranty did not indicate that the forum selection was exclusive, although the word "or" appeared in the clause, and that there was jurisdiction. As to the availability of 3213, the court found that the agreement referred to redemption of shares and not reinstatement of a debt and that payment was made conditional on plaintiff's presentation of the shares. The same was true of the guaranty. Therefore, the court held, 3213 was unavailable. AIG Asian Infrastructure Fund, L.P. v. Bayan Telecommunications Holdings Corp., Index No. 600260/2003, 5/06/04 (Ramos, J.).

Procedure; CPLR 3213; promissory notes. Plaintiff moved for summary judgment in lieu of complaint on a promissory note and an unconditional guarantee. Defendants argued that plaintiff had been aware that the money loaned was to be used to start up a new business, that plaintiff had indicated it would work with defendants, and that they had been capable of making a payment which plaintiff had rejected. The court found defendants' arguments insufficient to defeat plaintiff's prima facie case, pointing out first that the money had been borrowed to purchase an existing restaurant, not for the opening of a new business. The court further found that the note specifically provided that the borrower could not use oral statements by the lender to contradict or alter the note's terms, thus precluding defendants from asserting such representations as a defense. The guarantee was unconditional and barred reliance on oral representations. Unity Bank v. Hot Diggity Doggies LLC, Index No. 17665/2003, 6/18/04 (Austin, J.).

Procedure; offset based on subordinated debt; discharge in bankruptcy. Plaintiffs moved to dismiss an affirmative defense of a defendant, former CEO. Plaintiffs sued claiming that defendant had paid himself excess compensation and unlawfully retained a bonus. Defendant alleged that plaintiffs had breached an agreement by refusing to buy back defendant's stock. Plaintiffs filed for Chapter II reorganization. Under the plan, plaintiffs argued, defendant would receive nothing from the bankruptcy estate and the affirmative defense should therefore be barred. The court noted that this case did not involve the automatic stay, at issue in certain cases cited. However, the principles of those cases applied: the law does not automatically bar an offset based on a subordinated claim. Nor does a discharge preclude a defendant from seeking an offset for debts. Plaintiffs' motion for summary judgment denied. Masterwear Corp. v. Bernard, Index No. 600766/1997, 6/22/04 (Ramos, J.).

Reinsurance; liquidation; offsets; Insurance Law § 7427. Procedure; reargument. Plaintiff insurance company had been assigned the right to collect monies owed to Citizens, a liquidated insurance company. Citizens and defendant, members of the same reinsurance pool, had reinsured one another. Plaintiff brought this action to collect from defendant sums defendant owed to Citizens. The court granted plaintiff's motion to reargue its cross-motion for summary judgment seeking to dismiss defendant's one remaining affirmative defense. Previously, the court had let stand defendant's assertion of a right to set off anything plaintiff might collect. Plaintiff alleged that there was nothing to set off. Pursuant to an expedited closing plan formulated by the liquidator, Citizens' reinsurance creditors, except for plaintiff, were to have been paid only for losses reflected on the liquidator's records as of a cut-off date that had passed. The debts had been paid, including debts due to defendant, and the plan clearly barred further payments.

Plaintiff's assignment had empowered it to collect two different classes of recoverables. The court now distinguished between the two. First, plaintiff was empowered to collect any recoverables due to Citizens as of the cut-off date which the liquidator had not collected one year later. The court now agreed that if the liquidator had intended debts owed to Citizens as of the cut-off date to be reduced by debts Citizens had owed, it would have disposed of the latter differently. But the liquidator's closing plan also assumed that debts owed to Citizens would continue to arise after the liquidation had closed: the pool manager would be notified of a loss incurred by a Citizens insured, Citizens would become liable for the loss, and Citizens' reinsurer would in turn become liable to Citizens–to plaintiff. Therefore, the second part of plaintiff's assignment allowed it to recover under reinsurance agreements running in Citizens' favor as of a date immediately following the first cut-off date. While the liquidator's plan had not allowed for offsets, it had not barred them. Plaintiff could collect from reinsurers what they would have owed Citizens if the liquidation had not ended, and the court did not accept that reinsurers could not set off what Citizens would have owed them. In addition to equity considerations, Insurance Law § 7427 is mandatory. Further, there was no language in plaintiff's assignment that supported plaintiff's contention that it had been assigned Citizens' rights but not the burden of its liabilities. The court adhered to its original decision allowing set offs, but only insofar as in regard to plaintiff's demands under the second part of the assignment. Defendant's failure to allege the existence of offsets in its answer did not constitute a waiver of that defense. Summary judgment denied. B.D. Cooke & Partners Ltd. v. Nationwide Mutual Insurance Company, Index No. 600655/2002, 6/28/04 (Lowe, J.).

Reinsurance; treaty and duty to disclose; access to records clause; facultative; "follow the fortunes." Residual value; gains v. losses policy. Ex gratia settlement. Discovery; attorney-client privilege. Rescission. Ratification. Procedure; statute of limitations. Plaintiff insurance company claimed that defendants had breached the parties' reinsurance treaties by failing to pay purported obligations arising from plaintiff's settlement of a lawsuit with an insured. Defendants, reinsurers, sought summary judgment on their counterclaims for breach of contract, based on plaintiff's breach of an Access to Records clause, and a declaration of rescission. They also moved to compel further discovery. The underlying insurance settlement had involved a residual lease policy for leased vehicles that provided for gains vs. losses calculation. Plaintiff and the insured had disputed gains calculations, leading to court and to mediation, where plaintiff's initial offer had been $35 million. The president of plaintiff's parent company, Travelers, which was then floating a $1.4 billion debt offering, had taken over negotiations, and, belying plaintiff's optimistic reports and prediction to defendants that the settlement would not be for more than $100 million, settled for $266 million. Defendants had requested plaintiff's records, but were not furnished with all they sought. The court denied their motions for summary judgment. Plaintiff argued that by providing basically all non-privileged documents regarding the underlying lawsuit, it had complied with the access clause. However, the court ruled, the clause did not limit the defendants' right to documents in any way. By failing to provide full access plaintiff had breached the agreement. The court rejected plaintiff's contention that defendants' anticipatory breach had relieved it of its duty to provide access. Hiring outside counsel to exercise defendants' right to access could not be considered equivalent to a breach, nor could counsel's writing letters voicing concern about delay. At the litigation's current stage it was not possible to tell whether plaintiff's breach of the Access clause had so greatly hindered defendants' ability to ascertain plaintiff's good faith and adherence to the treaties as to constitute a material breach. A trial was required. Plaintiff contended that the "follow the fortunes" doctrine, which binds a reinsurer to follow cedent's settlements of coverage disputes, relieved them of further obligation. But to be binding the settlement would have to have been made in good faith, and the court found that defendants had basis to seek further discovery on this. Another basis for further discovery was whether the gains vs. losses policy had been properly ceded to the treaties; a "Specimen Policy" in the treaties, which plaintiff had represented would be used with insureds, was not a gains vs. losses policy but the more common losses-only policy. The former was experimental, plaintiff said. It had a different time frame for loss notification, and with gains, unlike with losses, there is no objective basis for computation. Plaintiff's other arguments opposing further discovery failed. The court rejected plaintiff's argument that defendants could have, but did not, discover earlier a problem with the underlying policy. There was no statute of limitations issue nor any other basis whereby the delay would preclude defendants from obtaining discovery. In any case, plaintiff would have to have provided the information under the Access clause. Arguments about burden and the privacy rights of non-parties were of no avail. That certain documents might otherwise be deemed privileged did not narrow the Access clause, which was so expansive as to have no limit, the court noted. Plaintiffs contended that a reinsured need not produce documents to a reinsurer once the two are in adversarial positions, but in the cases it pointed to, reinsurers had invoked a cooperation clause intended to enable the parties to cooperate against an insurer bringing suit; here the Access clause was invoked and it was not tied to any limited underlying purpose, but gave defendants an expansive right. Plaintiff also argued that it could not provide material requested because of a confidentiality stipulation connected to the settlement. But if plaintiff had failed to take into account the rights of its reinsurers, it had to bear the resulting burden. The court granted the motion to compel discovery. Plaintiff moved to dismiss various claims made by one defendant, including a claim for rescission based on plaintiff's failure to disclose that the underlying policy was a gains vs. losses policy and on the underlying insured having submitted incomplete loss information. Plaintiff argued, among other things, that the defendant had ratified the treaties and was estopped from seeking rescission. However, the court declared the issue to be what information the defendant had needed to ascertain that it had basis to seek rescission, and when the information had been received. Plaintiff argued that this defendant's counterclaim was time-barred. But the six-year statute ran from date of breach, not the date of contract. Further, plaintiff allegedly had breached its obligations continuously by concealing staggering losses and a high volume of claims. The court denied plaintiff's motion to dismiss. Gulf Insurance Co. v. Transatlantic Reinsurance Co. Index No. 601602/2003, 5/21/04 (Lowe, J.).

UCC; conversion; bank check; cashier's check; teller's check; drawee; drawer. UCC § 4-102 (2). Agency; express; implied. Ordinary care. Plaintiff, a religious order, moved for summary judgment on a conversion claim against a defendant bank pertaining to a check for $414,000. The bank cross-moved to dismiss the complaint. Plaintiff had been beneficiary of an estate and the estate's attorney had asked to work with plaintiff's legal representative. It had later emerged that the attorney to whom plaintiff had directed the estate's lawyer had embezzled half a million dollars from previous clients and been disbarred in New York and New Jersey. This attorney, over the course of about a year, had received from the estate's lawyer two checks for a sum of $451,000, and had forwarded both to plaintiff and informed it that a third check would arrive in about nine months. That check had arrived and the attorney had endorsed it with a forged signature and deposited it into an escrow account he had opened. Plaintiff alleged that the defendant bank was drawee on the third check, and that, having paid it on a forged endorsement, was liable to plaintiff, the named payee, for its full amount. As a threshold issue, the court found that under the UCC, Maine laws governed the defendant's liability; plaintiff's argument that New Hampshire laws governed ignored the fact that the complaint concerned the check's payment over a forged endorsement, not its purchase. Based on the plain language of the check and other uncontradicted documentary evidence, the court agreed with the bank that it was not the drawee. Unlike the first two checks, the third had not been drawn on the estate's checking account at the bank. The estate's lawyer had requested a "bank check" and the instrument issued had borne pre-printed language of "Drawer Bank of New Hampshire," "OFFICIAL CHECK," and in the bottom left corner, the name of a different bank. The term "official check" has no legal meaning, the court noted, and the check was not a cashier's check, in which one bank is both drawer and drawee. It was akin to a teller's check, drawn by the bank on an account payable at or through another bank. Teller's checks are also known as bank checks, so the defendant bank had met the estate lawyer's reasonable expectation when she had requested one. The defendant bank having drawn the check, it had deposited funds to pay it into its general ledger account and then wired funds from the account to the drawee bank responsible for its payment, the bank named in the lower left corner. Defendant bank's involvement had ended there. The check had not been returned to it, as it would have been had it been the drawee. The court dismissed the conversion claim. However, even if the defendant bank had been the drawee bank, the court could not have granted plaintiff's motion for summary judgment. A payee cannot sustain a conversion claim against a drawee bank if the check was not delivered to the payee or its authorized agent. The bank's argument that neither plaintiff nor its agent had ever received the check raised issues of fact, as did its argument that plaintiff's failure to exercise ordinary care exempted it from liability under Maine law. In the first instance, the question was whether the disbarred lawyer was plaintiff's authorized agent. As to ordinary care, the court noted that, among other things, although plaintiff had known that a third check would be coming, it had let a year go by before asking about it, and then had only asked when it had learned of the attorney's disbarments. Plaintiff's motion for summary judgment denied; defendant's cross-motion granted. Dominican Fathers v. Chase Manhattan Bank USA, N.A., Index No. 120382/2002, 6/15/04 (Fried, J.).

The *Report* is issued five times per year by the Commercial Division. The complete texts of decisions discussed in the *Report* are available by hyperlink on the website of the Commercial Division at www.courts.state.ny.us/comdiv (under the "Law Report" section), and on the home page of the New York State Bar Association's Commercial and Federal

Litigation Section at www.nysba.org (and follow links). Members of the Commercial and Federal Litigation Section may sign up at the Section's home page to receive copies of the *Report* by e-mail automatically. The decisions as they appear on the home pages have not been edited and may differ from the final text published in the official reports by the State Reporter.

THE NEXT ISSUE WILL BE POSTED ON THE HOME PAGES OF THE COMMERCIAL DIVISION AND THE COMMERCIAL AND FEDERAL LITIGATION SECTION ON NOVEMBER 30, 2004 COVERING DECISIONS ISSUED JULY-SEPTEMBER 2004.

Please forward any comments on this website to the Webmaster at rboucher@courts.state.ny.us