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

PRESENT: James A. Yates PART 49

Index Number : 601860/2009
ING REAL ESTATE FINANCE
vs.
PARK AVE HOTEL ACQUISITION, LLC
SEQUENCE NUMBER : 001
DISMISS

INDEX NO. _____
MOTION DATE _____
MOTION SEQ. NO. _____
MOTION CAL. NO. _____

n this motion to/for _____

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
Answering Affidavits — Exhibits	
Replying Affidavits	

Cross-Motion: ☐ Yes ☑ No

Upon the foregoing papers, it is ordered that this motion

is decided in accordance with the attached Decision and Order, dated February 24, 2010.

RECEIVED
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Dated: FEB 24 2010

James A. Yates
J.S.C.

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

Check one: ☐ FINAL DISPOSITION ☑ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 49

ING REAL ESTATE FINANCE (USA) LLC and SWEDBANK AB, NEW YORK BRANCH, by and through their Administrative Agent, ING Real Estate Finance (USA) LLC, pursuant to that certain Co-Lending Agreement, dated August 1, 2007, Plaintiffs, -against- PARK AVENUE HOTEL ACQUISITION LLC, NEW YORK CITY ENVIRONMENTAL CONTROL BOARD, NEW YORK STATE DEPARTMENT OF TAXATION AND FINANCE, ABY ROSEN, MICHAEL FUCHS, HHC LEXINGTON AVENUE, INC., SHANGRI-LA ASIA LIMITED, AND JOHN DOE #1 through 50, said John Doe defendants being fictitious and unknown to plaintiff, it being intended to name all other parties who may have some interest in or lien upon the premises sought to be foreclosed, Defendants.	:	Decision and Order Index No. 601860-2009 Motion Seq. 001

Morrison & Foerster LLP, New York City (*Rachel M. Wertheimer* of counsel), for ING Real Estate Finance (USA) LLC and Swedbank AB, New York Branch, Plaintiffs.

Fried, Frank, Harris, Shriver & Jacobson LLP, New York City (*Gregg L. Weiner* of counsel), for Park Avenue Hotel Acquisition LLC, Aby Rosen, Michael Fuchs, Defendants.

Patton Boggs LLP, New York City (*Patrick F. McManemin* of counsel), for HHC Lexington Avenue, Inc., Defendant.

Baker & McKenzie LLP, New York City (*David Zaslowsky* of counsel), for Shangri-La Asia, Limited, Defendant.

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Hon. James A. Yates, J.S.C.

Defendant Park Avenue Hotel Acquisition LLC (the "Borrower"), and defendants Aby Rosen, Michael Fuchs, HHC Lexington Avenue, Inc., and Shangri-La Asia Limited (the "Guarantors") (together with the Borrower, "moving defendants") move to dismiss the deficiency claims (the "Full Recourse Claims") of the Verified Amended Complaint filed by ING Real Estate Finance (USA) LLC ("ING") and Swedbank AB, New York Branch (collectively, "plaintiffs"), pursuant to CPLR 3211 (a) (1) and (7).

Plaintiffs' claims arise in connection with plaintiffs' attempt to foreclose on real property at 610 Lexington Avenue, based on the Borrower's alleged failure to pay the outstanding principal balance due on the loans made to finance the acquisition of the property, the demolition of the structure on the property, and certain construction costs and pre-development costs on the property (collectively, the "debt"). The debt is non-recourse meaning, absent certain limited acts by the Borrower, plaintiffs agreed to limit recovery on the debt to the proceeds of the sale of the property through foreclosure. Plaintiffs, here, however, seek full recourse, following foreclosure, from moving defendants. For the following reasons, the claims of personal liability are dismissed.

Background

On April 17, 2007, Lehman Brothers Holding, Inc. ("LBHI") agreed to loan $145 million to the Borrower, secured by mortgages on the property. The Master Credit Agreement ("Credit Agreement") sets forth the rights and duties of the Borrower and LBHI under the Loan Documents.[1] Pursuant to Section 9.1 (a) of the Credit Agreement, the debt is non-recourse. In an event of default, plaintiffs may bring a foreclosure action, but may "not sue for, seek or demand any deficiency judgment against Borrower or any other Person" (affirmation of Adam R. Adler [Sept. 15, 2009], exhibit 2 [Credit Agreement] § 9.1 [a], at 59). Plaintiffs may bring a foreclosure action "provided no money judgment is

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[1] The Credit Agreement and the Guaranty Agreement, along with the Acquisition Loan, Project Loan, Building Loan, Acquisition Loan Note, Acquisition Loan Mortgage, Assignment of Leases, Project Loan Notes, Project Loan Notes, Project Loan Agreement, Project Loan Mortgage, Building Loan Note, Building Loan Agreement, and Building Loan Mortgage, as those terms are defined in the Credit Agreement, are collectively referred to as the "Loan Documents."

sought" (*id.* § 9.1 [b]).

Concurrently with the Credit Agreement, the Guarantors executed the Guaranty of Recourse Obligations (the "Guaranty Agreement"), whereby they undertook certain limited obligations with respect to the Loan Documents. Those obligations are only triggered in the event of a "Partial Recourse Event" or "Full Recourse Event" as defined under Sections 9.2 and 9.3 of the Credit Agreement. Section 9.3 of the Credit Agreement sets forth four provisions constituting Full Recourse Events, where moving defendants are jointly and severally liable for the debt:

> "**Section 9.3** Full Recourse. In addition to the rights of the Lender set forth in Section 9.2 (and not in limitation thereof), the Debt shall be fully recourse to Borrower and the Guarantors jointly and severally, and the provisions of Section 9.1(a) shall be wholly inapplicable *ab initio*, and Borrower and the Guarantors shall be fully personally liable, jointly and severally, for all of the Debt upon the occurrence of any of the following (collectively, the "**Full Recourse Events**", and individually, a "**Full Recourse Event**"): (a) any voluntary action by Borrower or any Borrower Party which result in a violation, breach or failure to comply with Section 5.22; (b) any of the events described in Section 7.1(a)(vi) shall occur; (c) if Borrower incurs any Indebtedness in violation of the express restrictions or prohibitions contained in the Loan Documents and such violation is not cured within thirty (30) days after receipt of notice from Lender; or (d) breach of Borrower of the provisions of Section 4.1(s) (with the exception of 4.1(s)(v) and 4.1(s)(x))."

(*Id.* § 9.3, at 60.)

Section 4.1 (s) (iii) of the Credit Agreement can trigger Section 9.3 (d). Section 4.1 (s) (iii) states:

> "Borrower hereby represents and warrants . . . :
>
> (iii) Borrower has not incurred and will not incur any Indebtedness, secured or unsecured, direct or indirect, absolute or contingent (including guaranteeing any obligation), other than (A) the Debt or (B) unsecured trade debt none of which is or shall be at any time more than ninety (90) days past due (unless same is being contested in accordance with applicable Legal Requirements and the Loan Documents and Lender has been notified in writing of the same) and does not and shall not exceed in the aggregate at any time the Maximum Permitted Trade Payables . . . No Indebtedness other than the Debt may be secured (superior, subordinate or pari passu) by the Property or any portion thereof."

(*Id.* § 4.1 [s] [iii], at 12.)

The Credit Agreement defines "Indebtedness" as the "sum (without duplication) at such date of (a) all indebtedness or liability for borrowed money; (b) obligations evidenced by bonds, debentures, notes, or other similar instruments; (c) obligations for the deferred purchase price of property or services (including trade obligations); (d) obligations under letters of credit; (e) obligations under acceptance facilities; (f) all guaranties, endorsements (other than for collection or deposit in the ordinary course of business) and other contingent obligations to purchase, to provide funds for payment, to supply funds, to invest in any Person, or otherwise to assure a creditor against loss; and (g) *obligations secured by any Liens, whether or not the obligations have been assumed*" (*id.*, Schedule I, at I-8 [emphasis added]).

On April 14, 2009, plaintiffs sent a notice of event of default to moving defendants claiming that the Borrower had breached the Loan Documents by failing to pay the outstanding principal balance on the debt as it came due on April 8, 2009.

On June 16, 2009, plaintiffs filed the instant foreclosure action against the Borrower, again claiming that the Borrower failed to pay the outstanding principal balance on the debt of $133,602,101.00, together with accrued interest thereon and other charges pursuant to the Loan Documents. The Verified Complaint did not name or seek recourse from the Guarantors. At the time of filing, however, the project was undeveloped and the anticipated value of the property was only a fraction of the outstanding debt.

A few months later, on July 14, 2009, plaintiffs amended their complaint by adding the Guarantors as defendants by claiming that the Borrower had failed to pay $278,759.20 of real estate taxes due as of July 1, 2009, and as a result, a tax lien in that amount existed on the property, which created an Indebtedness under Section 4.1 (s) (iii) and, in turn, Section 9.3 (d), leading to full recourse liability. At oral argument, it was claimed that the property, still undeveloped, is worth approximately $45 million to $65 million (transcript at 8 [Feb. 9, 2010]), leaving a balance on the loan of almost $70 million to $90 million, which plaintiffs seek to collect from moving defendants. On July 20, 2009, the Borrower paid all real property taxes due to the City of New York along with accrued interest, thereby extinguishing the alleged tax lien. The Verified Amended Complaint, however, still asserts that a Full Recourse Event occurred, however briefly, and seeks a deficiency judgment against moving defendants for "the debt remaining unsatisfied after the [foreclosure] sale of the Mortgaged Premises" (*id.*, exhibit 1 [Verified Amended Complaint] ¶ 4, at 14).

The question before the Court is whether, by the terms of the contract, the nineteen-day tardiness in paying less than $300,000 in property taxes triggers a full recourse obligation by the Guarantors of up to $90 million. The parties cite separate, facially inconsistent, provisions of the contract in support of their respective positions.

Discussion

When determining a motion to dismiss, the court must "accept the facts as alleged in the complaint as true, accord plaintiffs the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory" (*Arnav Indus., Inc. Retirement Trust v Brown, Raysman, Millstein, Felder & Steiner, L.L.P.*, 96 NY2d 300, 303 [2001]). The court will not accept as true factual and legal conclusions that are "either inherently incredible or flatly contradicted by documentary evidence" (*Ullmann v Norma Kamali, Inc.*, 207 AD2d

691, 692 [1st Dept 1994]).

"Interpretation of the contract is a legal matter for the court" and may be decided on a motion to dismiss (*805 Third Ave. Co. v M.W. Realty Assoc.*, 58 NY2d 447, 451 [1983]). "[W]hen parties set down their agreement in a clear, complete document, their writing should as a rule be enforced according to its terms" (*W.W.W. Assoc., Inc. v Giancontieri*, 77 NY2d 157, 162 [1990]). A contract claim must be dismissed under CPLR 3211 (a) (1) and (7) when the unambiguous terms of the contract establish that the plaintiff has not stated a claim for which relief can be granted (*see e.g. Surge Licensing, Inc. v Copyright Promotions Ltd.*, 258 AD2d 257, 257-258 [1st Dept 1999]).

The issue here is whether, under the Credit Agreement, the Borrower's nineteen-day delay in paying the real estate taxes falls under: (1) Section 9.3 (c) (allowing thirty-day cure period upon filing of lien before recourse may occur); or (2) Section 9.3 (d) (calling for full recourse immediately upon Indebtedness). The parties do not dispute that the tax lien falls within "the definition of [I]ndebtedness [which] includes liens secured by the property" (transcript at 32 [Feb. 9, 2010]; *see also* affirmation of Adam R. Adler [Sept. 15, 2009], exhibit 2 [Credit Agreement], Schedule I, at I-8 ["Indebtedness" ¶ [g]]). As well, both parties acknowledge that the lien, during the nineteen-day period, was unenforceable since the City of New York does not institute foreclosure actions until after a tax lien has existed on a property for at least one year (*see* Administrative Code of the City of New York § 11-404).

Moving defendants argue that Section 9.3 (c) controls. That section provides that a Full Recourse Event occurs only when "any Indebtedness . . . violation is not cured within thirty (30) days after receipt of notice from Lender" (affirmation of Adam R. Adler [Sept. 15, 2009], exhibit 2 [Credit Agreement] § 9.3 [c], at 60). Since moving defendants paid all real property taxes on July 20, 2009, six days after plaintiffs amended their complaint to allege that moving defendants failed to pay the real estate taxes due as of July 1, 2009, moving defendants cured within the thirty-day window and full recourse is not available.

On the other hand, plaintiffs argue that Section 9.3 (d) is the applicable provision. They assert that any Indebtedness is an "automatic trigger of a Full Recourse Event" (plaintiffs' memorandum of law in opposition at 10 [Oct. 12, 2009]). Plaintiffs contend that the tax lien resulting from the Borrower's failure to timely pay the property taxes constitutes an impermissible Indebtedness under Section 4.1 (s) (iii) of the Credit Agreement, calling for full recourse liability under

Section 9.3 (d), which contains no opportunity to cure.

Plaintiffs' argument fails for the following reasons:

First, "[w]here a contract . . . employs contradictory language, specific provisions control over general provisions" (*Green Harbour Homeowners' Assn., Inc. v G.H. Dev. & Constr., Inc.*, 14 AD3d 963, 965 [3d Dept 2005]). Here, Section 9.3 (c) specifically and narrowly addresses the recourse consequences where the "Borrower incurs any Indebtedness in violation of . . . the Loan Documents" (affirmation of Adam R. Adler [Sept. 15, 2009], exhibit 2 [Credit Agreement] § 9.3 [a], at 60). In contrast, Section 9.3 (d) applies to a broad array of nearly twenty separately delineated covenants found in Section 4.1 (s) concerning the operations of the Borrower as a "Single Purpose" entity (*id.* § 4.1 [s], at 12), most of which do not relate to "Indebtedness" (*id.* § 4.1 [s] [iii], at 12). For example, among other things, Section 9.3 (d) would be triggered if the Borrower "commingle[s] its funds and other assets with those of any other Person" (*id.* § 4.1 [s] [xi], at 13), "engage[s] in any business other than the ownership, renovation, management, [and] leasing of the Property" (*id.* § 4.1 [s] [ii], at 12), or "amend[s] its original constituent documents" (*id.* § 4.1 [s] [xxi], at 14), none of which would trigger Section 9.3 (c). While Section 9.3 (d) by indirect incorporation might be read to include any Indebtedness, Section 9.3 (c) provides specific direction as to how Indebtedness should be treated. Plaintiffs' reading effectively reads Section 9.3 (c) out of the agreement.

Although, on the surface, both Section 9.3 (c) and Section 9.3 (d) might seem to apply to the tax lien, they must be read in conjunction with Section 9.4 (a), which provides that there can be no full recourse liability until any applicable notice and cure period has expired. It states: "Notwithstanding anything to the contrary in this Article IX, (a) if any of the actions constituting a Recourse Event are subject to a specified notice and cure period in the Loan Documents, the same shall not give rise to personal liability for the payment and performance of the Obligations until the expiration of any such notice and cure period" (*id.* § 9.4 [a], at 60).

There are other provisions of the contract which are inconsistent with plaintiffs' claim as well. Plaintiffs' reading would render multiple sections of the Credit Agreement meaningless. However, "a court should not adopt an interpretation which would leave any provision without force and effect" (*Sunrise Mall Assoc. v Import Alley of Sunrise Mall, Inc.*, 211 AD2d 711, 711 [2d Dept 1995]).

For example, Section 7.1 (a) (ix) provides that a lien on the property becomes an event of default only when it remains undischarged "for a period of forty-five (45) days after Borrower shall have received notice of such Lien" (affirmation of Adam R. Adler [Sept. 15, 2009], exhibit 2 [Credit Agreement] § 7.1 [a] [ix], at 44). However, under plaintiffs' interpretation, a simple one day delay in paying a tax, or any debt for which a lien may be filed, no matter how small, immediately becomes a Full Recourse Event under Section 9.3 (d). That interpretation is plainly inconsistent with Section 7.1 (a) (ix).

Additionally, plaintiffs' interpretation cannot be reconciled with Section 5.4 of the Credit Agreement, which permits the Borrower to contest a tax lien on the property if, for one, "no Event of Default exists" (*id.* § 5.4, at 17). Under plaintiffs' proffer, however, the Borrower could never contest the tax lien because, to plaintiffs, a tax lien automatically triggers a Full Recourse Event and is automatically an event of default. Section 5.4 becomes meaningless verbiage under their interpretation.

In this case, the claimed Indebtedness falls under paragraph (g) of the definition of that term, that is, "obligations secured by any Liens, whether or not the obligations have been assumed" (*id.*, Schedule I, at I-8). There is no claim that the Borrower incurred an Indebtedness as defined in paragraphs (a) through (f). Although Sections 9.3 (c) and 9.3 (d) both apply upon the occurrence of an Indebtedness and thereby appear facially inconsistent, they can be reconciled. A reasonable interpretation of the drafters' intent is that Section 9.3 (d) was meant to invoke full recourse for all Indebtedness described in paragraphs (a) through (f) of the definition of Indebtedness, while Section 9.3 (c), Section 7.1 (a) and Section 5.4, read together, were intended to carve out an exception, a safe-harbor with a cure period, for liens.

Under New York law, "[t]he terms of the guaranty . . . are to be strictly construed in favor of a private guarantor" (*665-75 Eleventh Ave. Realty Corp. v Schlanger*, 265 AD2d 270, 271 [1st Dept 1999]). Because the Credit Agreement is incorporated into the Guaranty Agreement, and the Guaranty Agreement must be strictly construed in favor of the Guarantors, the facial inconsistency between Sections 9.3 (c) and (d) should be resolved in favor of the Guarantors, entitling the Guarantors to a thirty-day cure period.

Finally, "[a] commercial agreement, of course, should not be interpreted in a commercially unreasonable manner or contrary to the reasonable expectations of the parties" (*HGCD Retail Servs.*,

LLC v 44-45 Broadway Realty Co., 37 AD3d 43, 49-50 [1st Dept 2006]). Immediate liability for the entire debt is not a reasonable measure of any probable loss associated with the delinquent payment of a relatively small amount of taxes. Here, pursuant to Section 9.3 (d), plaintiffs would have moving defendants potentially liable for the entire debt of up to $145 million if the Borrower is just one day delinquent in paying a dollar in property taxes or any other debt for which a lien may be imposed. Such an unlikely outcome could not have been intended by the parties, sophisticated commercial borrowers and lenders aided by competent counsel at the time of the drafting, and is impermissible under New York law (*see Truck Rent-A-Center, Inc. v Puritan Farms 2nd, Inc.*, 41 NY2d 420, 425 [1977] ["The rule is now well established. A contractual provision fixing damages in the event of breach will be sustained if the amount liquidated bears a reasonable proportion to the probable loss and the amount of actual loss is incapable or difficult of precise estimation. If, however, the amount fixed is plainly or grossly disproportionate to the probable loss, the provision calls for a penalty and will not be enforced."] [internal citations omitted]).

Conclusion

For the reasons stated, it is hereby:

ORDERED, that the motion to dismiss is granted and the Full Recourse Claims of the Verified Amended Complaint are severed ad dismissed; and it is further

ORDERED, that the remainder of the action shall continue; and it is further

ORDERED, that the parties are to appear before the Court on March 9, 2010, at 10:00 A.M., for a preliminary conference;

ORDERED, that the Clerk is directed to enter judgment accordingly.

This constitutes the Decision and Order of the Court.

Dated: February 24, 2010

FEB 24 2010

ENTER:

James A. Yates, J.S.C.

James A. Yates