Short Form Order

NEW YORK SUPREME COURT - QUEENS COUNTY

PRESENT: HON. ORIN R. KITZES **PART 17**
Justice

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NATIONAL ENVIRONMENTAL SAFETY COMPANY, INC.

Plaintiff,

-against- **Index No.: 121/11**
Motion Date: 7/13/11

AZHAR SHABBIR and AZHAR SHABBIR d/b/a TSC CONSTRUCTION, **Mot. Cal. No: 36**

Defendants,

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The following papers numbered 1 to 10 read on this motion by plaintiff **NATIONAL ENVIRONMENTAL SAFETY COMPANY, INC. (NESCO)**, and counterclaim defendant DOMINICK FERTITTA (collectively referred to as NESCO), to dismiss defendants **AZHAR SHABBIR AND AZHAR SHABBIR d/b/a TSC CONSTRUCTION'S (TSC),** (collectively referred to herein as defendants) counterclaims pursuant to CPLR 3211 (a)(1) and (7); to dismiss defendants' claims for reasonable attorneys' fees and costs; and to dismiss the said defendants' affirmative defenses.

	PAPERS NUMBERED
Notice of Motion - Affidavits - Exhibits.....	1-5
Answering Affidavits - Exhibits.....	6-7
Reply Affidavits.....	8-10

Upon the foregoing papers it is ordered that the motion is decided as follows:

Plaintiff general contractor brings this lien law action alleging, *inter alia*, breach of contract and trust fund diversion. Plaintiff seeks damages for alleged poor work, labor and services performed by defendant TSC in the performance of a subcontract. The subcontractor filed counterclaims for, *inter alia*, breach of contract and trust fund diversion.

The causes of action asserted by plaintiff NESCO, and the counterclaims asserted by TSC all arise out of work TSC performed in connection with two school construction projects commissioned by the New York City School Construction Authority (SCA). NESCO was the general contractor and TSC was a subcontractor for the projects, which were located at PS 224K in Brooklyn, and Walton High School in the Bronx. The work performed by TSC included, *inter*

alia, concrete and masonry restoration work and sheet metal work. It is alleged that, TSC provided defective and unacceptable work and failed to provide the necessary labor and materials to progress and complete the subcontract work; and that TSC terminated and stopped all work prior to completing its subcontract work. In response, TSC submits that, despite TSC's repeated demands for payment, NESCO failed to pay for the work valued at approximately $484,742.99. In January of 2011, TSC filed two public improvement mechanic's liens with respect to the work with the SCA.

It is noted that the motion does not seek dismissal of TSC's second counterclaim for breach of contract arising out of the failure to pay TSC for the work performed. The remaining counterclaims seek damages arising out of the two SCA projects described above, but seek different damages and are alleged upon different legal theories of recovery: Enforcement of a Lien Law Article 3-A trust claim (First Counterclaim); breach of contract for damages other than those set forth in the Second Counterclaim (Third and Fourth Counterclaims); Unjust Enrichment (Fifth Counterclaim); Defamation (Sixth Counterclaim). NESCO seeks to dismiss the first, fifth and sixth counterclaims on the ground that they fail to state a claim pursuant to CPLR 3211 (a)(7), and as to the third and fourth counterclaims, based upon documentary evidence pursuant to CPLR 3211 (a)(1).

Trust Fund Diversion (First Counterclaim)

"Article 3–A of the Lien Law creates trust funds out of certain construction payments or funds to assure payment of subcontractors, suppliers, architects, engineers, laborers, as well as specified taxes and expenses of construction' " (Aspro Mech. Contr. v Fleet Bank, 1 NY3d 324, 328 [2004], quoting Caristo Constr. Corp. v Diners Fin. Corp., 21 NY2d 507, 512 [1968]; *see* Lien Law §§70, 71). "[T]he primary purpose of article 3–A and its predecessors [is] to ensure that those who have directly expended labor and materials to improve real property [or a public improvement] at the direction of the owner or a general contractor receive payment for the work actually performed" (Aspro Mech. Contr. v Fleet Bank, 1 NY3d at 328 [internal quotation marks omitted]; *see* Matter of RLI Ins. Co., Sur. Div. v New York State Dept. of Labor, 97 NY2d 256, 264 [2002]).

Section 70 of the Lien Law defines trusts created thereunder. That section provides, in pertinent part,

> "The funds described in this section ... received by a contractor under or in connection with a contract for an improvement of real property, or home improvement, or a contract for a public improvement in this state, or received by a subcontractor under or in connection with a subcontract made with the contractor for such improvement of real property including a home improvement contract or public improvement or made with any

> subcontractor under any such contract, and any right of action for any such funds due or earned or to become due or earned, shall constitute assets of a trust for the purposes provided in section seventy-one of this chapter."

Lien Law § 70[1]). "An article 3–A trust commences 'when any asset thereof comes into existence' and continues until all trust claims have been paid or discharged, or all assets have been applied for trust purposes" (Matter of RLI Ins. Co., Sur. Div. v New York State Dept. of Labor, 97 N.Y.2d at 262, quoting Lien Law § 70[3]).

> "Under a home improvement contract, payments received from an owner by a home improvement contractor prior to the substantial completion of work under the contract shall be deposited within five business days thereafter by the recipient in an escrow account in a bank, trust company, savings bank, or state or federal savings and loan association, located in this state.... Such deposit or deposits shall remain the property of such owner except as otherwise provided herein" (Lien Law § 71–a[4][a]).

Such deposit or deposits shall remain the property of the owner or such bond or contract of indemnity or irrevocable letter of credit continued in effect until (i) the proper payment, transfer or application of such deposits by the contractor to the purposes of the home improvement contract under the schedule of payments provided therein; or (ii) the default or breach of the owner excusing the recipient's performance of the terms of the home improvement contract, but only to the extent of any reasonable liquidated damage amount as defined in section 2–718 of the uniform commercial code and set forth in the contract, and only after seven days prior written notice to the owner; or (iii) substantial performance of the contract" (Lien Law § 71–a[4][d]).

Synthesizing the foregoing sections of the Lien Law,

> "contractors who receive money in advance for the construction of home improvements are required to place the money in a bank account and hold the money as the property of the owner until the money is paid for purposes of the home improvement. The funds deposited remain the property of the owner until: (1) the proper payment by the contractor for the purposes of the home improvement project; or (2) default or breach by the owner which excuses the contractor's performance, but only to the extent of any reasonable liquidated damage amount and only after 7 days prior written notice to the owner; or (3)

substantial performance of the contract" (Stern v H. DiMarzo, Inc., 19 Misc.3d 1144[A], 2008 N.Y. Slip Op. 51163[U], [2008 WL 2369749] [2008] [citations omitted]).

"The trust assets of which a contractor or subcontractor is trustee shall be held and applied for the following expenditures arising out of the improvement of real property, including home improvement or public improvement and incurred in the performance of his contract or subcontract, as the case may be: ... (f) payment to which the owner is entitled pursuant to the provisions of section seventy-one-a of this chapter" (Lien Law § 71[2][f]).

"Any transaction by which any trust asset is paid, transferred or applied for any purpose other than a purpose of the trust as stated in subdivision one or subdivision two of section seventy-one, before payment or discharge of all trust claims with respect to the trust, is a diversion of trust assets, whether or not there are trust claims in existence at the time of the transaction, and if the diversion occurs by the voluntary act of the trustee or by his consent such act or consent is a breach of trust" (Lien Law § 72[1]).

Thus, "Lien Law article 3–A mandates that once a trust comes into existence, its funds may not be diverted for non-trust purposes" (Matter of RLI Ins. Co., Sur. Div. v New York State Dept. of Labor, 97 NY2d at 263). "Use of trust assets for any purpose other than the expenditures authorized in Lien Law § 71 before all trust claims have been paid or discharged constitutes an improper diversion of trust assets, regardless of the propriety of the trustee's intentions" (*id.*). "Only after all trust claims have been paid or discharged does a beneficial interest in the remaining balance vest in the trustee owner or contractor" (id.).

In the posture of NESCO'S CPLR 3211 motion to dismiss, the court's task is to determine whether defendants' counterclaims state causes of action. The motion must be denied if, from the counterclaims' four corners, "factual allegations are discerned which taken together manifest any cause of action cognizable at law" (Polonetsky v Better Homes Depot, 97 NY2d 46, 54 [2001], quoting Guggenheimer v Ginzburg, 43 NY2d 268, 275 [1977]). In furtherance of this task, the court must liberally construe the counterclaims (*see e.g.* Leon v Martinez, 84 NY2d 83, 87 [1994]; CPLR 3026), and accept as true the facts alleged therein and any submissions in opposition to the dismissal motion (*see* Sokoloff v Harriman Estates Dev. Corp., 96 NY2d 409, 414 [2001] [collecting cases]; Wieder v Skala, 80 NY2d 628, 631 [1992]). The court must also accord defendants the benefit of every possible favorable inference (*see* Sokoloff, 96 NY2d at 414).

On a motion to dismiss under Section 3211(a)(7), "the sole criterion is whether the pleading states a cause of action, and if from its four corners factual allegations are discerned which taken together manifest any cause of action cognizable at law" (Guggenheimer v Ginsburg, 43 NY2d 268, 275 [1976]). Dismissal under CPLR 3211(a)(1) is warranted "only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law" (Leon, 84 NY2d at 88; *see generally* Siegel, NY Prac § 269, at 428 [3d ed]). Based on the foregoing principles, the court concludes that the first counterclaim adequately states a cause of action to recover damages for the plaintiff's alleged wrongful conduct.

The first counterclaim states that NESCO received funds that "were and are part of the fruits of the performance by TSC under the Subcontracts . . . and were and are statutory trust funds and were required by law to be first expended and applied to the payment of the costs of the subcontracts entered into between TSC, the other beneficiary defendants and NESCO. The first counterclaim specifies the funds at issue: "NESCO has failed to pay an outstanding balance of $160,310.94, owed to TSC for the work performed in connection with the PS224-K Subcontract and an outstanding balance of $324,432.05, owed to TSC for the work performed in connection with the Walton subcontract. The first counterclaim additionally describes the funds as those particularized in the mechanic's liens filed in January 2011, and served on NESCO. Finally, the first counterclaim alleges that these payments were required to be made to TSC under the Lien Law and that the failure of NESCO to make these payments in accordance with the Lien Law constituted a diversion of trust funds. Accordingly, a legally sufficient counterclaim for diversion of trust funds has been asserted (*see* Martirano Constr. Corp. v Briar Contracting Corp., 104 AD2d 1028 [1984]; *see also* Forest Elec. Corp. v Karco-Davis, Inc., 259 AD2d 303 [1999]).

Furthermore, the first counterclaim properly asserts a claim against Fertitta individually. An officer of a corporate trustee may be individually liable for diversion or breach of the trust if it is found that the individual was "actively participating" in the wrong of the corporation or had knowledge of use of trust monies in the corporate business" (*see* Ippolito v TJC Development, LLC, 83 AD3d 57 [2011]; Medco Plumbing, Inc. v Sparrow Const. Corp., 22 AD3d 647 [2005]. In order to find participation or knowledge, "[i]t is not essential that the misuse of the trust funds should be for the exclusive benefit of the person making such unlawful use, although benefit to the corporation is inseparable from the benefit to those financially interested in the corporation (Schwadron v Freund, 69 Misc2d 342 [Sup. Ct. Rockland Co., 1972]). Individual participation may be shown by a variety of methods, including receipt of a salary from the trustee corporation (Id.). Here, the counterclaim alleges that Fertitta was the Chairman and CEO of NESCO; that he made "unauthorized, illegal, unjustified and improper payments . . . with notice and knowledge of the source and origin thereof, and with notice and knowledge of the claims of TSC. As such, a claim for diversion of trust funds is properly stated against Fertitta.

Breach of Contract (Third and Fourth Counterclaims)

NESCO moves to dismiss the third and fourth counterclaims for consequential damages based upon alleged documentary evidence. A motion to dismiss a complaint pursuant to CPLR 3211 (a) (1) may be granted only if the documentary evidence submitted by the defendant utterly refutes the factual allegations of the complaint and conclusively establishes a defense to the claims as a matter of law (*see* Goshen v Mutual Life Ins. Co. of N.Y., 98 NY2d 314 [2002]; First Keystone Consultants, Inc. v DDR Constr. Servs., 74 AD3d 1135 [2010]). In order for evidence to qualify as "documentary," it must be unambiguous, authentic, and undeniable (Fontanetta v John Doe 1, 73 AD3d 78, 84-86 [2010]). Here, the material submitted by NESCO in support of their motion, namely, the Subcontract, fails to refute TSC's allegations as a matter of law (*see* Reiver v Burkhart Wexler & Hirschberg, LLP, 73 AD3d 1149 [2010]; Fontanetta v John Doe 1, 73 AD3d 78 [2010]). NESCO claims that the subcontract only allows for payment to be made for acceptable work in place, and not to exceed $484,472.99, as the total consideration of the contract. This does not appear to be the case, however. Section 10.02 of the General Conditions clearly allows for recovery for, *inter alia*, demobilization, unused material, and 5% of the residual value of the contract. The contract language relied upon by NESCO states that the "in no event . . . shall the contractor be entitled to compensation in excess of the total consideration of the contract." The total consideration of the PS244-K Subcontract, however, is $895,000.00, and the Walton High School Subcontract is $580,000.00. At a minimum, the provisions are ambiguous and thus cannot be the basis for dismissing the counterclaims (*see* Goshen v Mutual Life Ins. Co. Of New York, 98 NY2d 314 [2002]; Granada Condominium III Ass'n v Palomino, 78 AD3d 996 [2010]).

Unjust Enrichment (Fifth Counterclaim)

The branch of the motion which is to dismiss fifth counterclaim against NESCO, claiming unjust enrichment, is denied. "The existence of a valid and enforceable written contract governing a particular subject matter ordinarily precludes recovery in quasi contract for events arising out of the same subject matter.... [A] quasi contract' only applies in the absence of an express agreement, and is not really a contract at all, but rather a legal obligation imposed in order to prevent a party's unjust enrichment.' Unjust enrichment is a quasi contract claim barred by this principle. However, the counterclaims alleging breach of contract and unjust enrichment may be pleaded alternatively (*see*, CPLR 3014; Joseph Sternberg, Inc. v Walber 36th St. Assocs., 187 AD2d 225 [1993]; Strauss v Di Cicco, 64 AD2d 979 [1978]). Clearly, at trial TSC could not recover on both grounds for the same work. However, in the event the unjust enrichment claim

is dismissed and the underlying subcontract is found unenforceable, TSC would have no recourse to recover the fair and reasonable value of the work it performed.

Defamation (Sixth Counterclaim)

The branch of the motion which seeks to dismiss the sixth counterclaim is granted. The sixth counterclaim alleges that NESCO slandered and defamed NSC by reporting that NSC poorly and improperly performed the subcontract.

A cause of action sounding in defamation which fails to comply with the special pleading requirements contained in CPLR 3016 (a) that the complaint set forth "the particular words complained of," mandates dismissal (*see* Gill v Pathmark Stores, 237 AD2d 563 [1997]; Sirianni v Rafaloff, 284 AD2d 447 [2001]). Failure to state the particular person or persons to whom the allegedly defamatory statements were made also warrants dismissal (*see* Gill v Pathmark Stores, supra; Sirianni v Rafaloff, supra).

In any event, the allegedly defamatory statements enjoyed a qualified privilege. Protection from defamation is afforded where the person making the statements does so fairly in the discharge of a public or private duty in which the person has an interest and where the statement is made to a person or persons with a corresponding interest or duty (*see* Jung Hee Lee Han v State of New York, 186 AD2d 536 [1992]; *see also* Liberman v Gelstein, 80 NY2d 429 [1992]). Here, NESCO, as the SCA's prime contractor on two construction projects involving New York City public schools, had a duty to report to the SCA, as they had a common interest, regarding the quality of NSC's work on the projects and their performance under the Subcontract Agreements. Correspondingly, the SCA, as the agency responsible for all construction projects involving the New York City public schools, had an interest and a duty to be informed by NESCO about the subcontractors on the projects, the quality of the subcontractors' work and whether the subcontractors were properly performing their duties for the construction of schools in conformance with required plans and specifications. Thus, any statements made by NESCO regarding NSC's work on the project and performance under the Subcontract Agreements were done in the discharge of NESCO's duties to report to SCA. The plaintiffs failed to demonstrate malice to defeat this privilege (*see* Wyllie v District Attorney of County of Kings, 2 AD3d 714 [2003]). Thus, the allegedly defamatory statements were protected by a qualified privilege and the sixth counterclaim is properly dismissed for this reason as well.

Attorneys' Fees, Costs and Disbursements

The branch of the motion which seeks to dismiss NSC's claims for its reasonable attorneys' fees, costs and disbursements in the second, third, fourth, fifth and sixth counterclaim is granted. Under the general rule, attorney's fees are incidents of litigation and a prevailing party may not collect them from the loser unless an award is authorized by agreement between the parties, statute or court rule (*see* Hooper Assoc. v AGS Computers, 74 NY2d 487 [1989]; Matter of A. G. Ship Maintenance Corp. v Lezak, 69 NY2d 1 [1986]; Mighty Midgets v Centennial Ins. Co., 47 NY2d 12 [1979]). Here, NSC does not offer any basis to recover their attorneys' fees, costs and disbursements for successfully prosecuting or defending this action.

Affirmative Defenses

NESCO argues that every affirmative defense asserted by NSC should be dismissed because they are not supported by factual allegations. This argument is without merit in light of the factual allegations incorporated in the counterclaims accompanying the affirmative defenses in the Verified Answer with Counterclaims.

Furthermore, "[u]pon a motion to dismiss a defense, the defendant is entitled to the benefit of every reasonable intendment of its pleading, which is to be liberally construed. If there is any doubt as to the availability of a defense, it should not be dismissed" (Federici v Metropolis Night Club, Inc., 48 AD3d 741, 743 [2008]; *see* Amerada Hess Corp. v Town of Southold, 39 AD3d 442 [2007]; Warwick v Cruz, 270 AD2d 255 [2000]). The movants bear "the burden of demonstrating that those defenses [a]re without merit as a matter of law" (Vita v New York Waste Servs., LLC, 34 AD3d 559, 559 [2006]). Here, NESCO failed to make such a showing. Therefore, the branch of the motion which is to dismiss all of NSC's affirmative defenses, is denied.

Conclusion

The branch of the motion which is to dismiss NSC's sixth counter claim, which is for defamation is granted. The branches of the motion which seeks to dismiss NSC's remaining counterclaims, to wit, one, three, four and five, are denied.

The branch of the motion which is to dismiss NSC's claims for its reasonable attorneys' fees, costs and disbursements in the second, third, fourth, fifth and sixth counterclaim is granted.

Finally, the branch of the motion which is to dismiss all of NSC's affirmative defenses, is denied.

Dated: August 12, 2011

ORIN R. KITZES. J.S.C.