Flintlock Constr. Servs., LLC v HPH Servs., Inc.
2014 NY Slip Op 33025(U)
November 20, 2014
Sup Ct, NY County
Docket Number: 653920/2012
Judge: Marcy S. Friedman
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK – PART 60

PRESENT: HON. MARCY S. FRIEDMAN, J.S.C.

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FLINTLOCK CONSTRUCTION SERVICES, LLC, as subrogee on behalf of all those persons who are beneficiaries of New York Lien Law Article 3-A trust funds arising from a subcontract for labor and materials supplied for the project at 218-222 West 50th Street, New York, New York,

Plaintiff,

- against -

HPH SERVICES, INC., MORRIS MILLER, SHALLAN HADDAD, JOHN DOE No. 1 through 5, being fictitious names representing persons participating in or causing the diversion of trust assets, and LAW OFFICES OF WEINER & WEINER, LLC, as escrowee,

Defendants.

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Index No.: 653920/2012

DECISION/ORDER

Motion Seq. 002

This is an action for breach of contract and diversion of trust assets under Lien Law Article 3-A, brought by plaintiff Flintlock Construction Services, LLC (Flintlock), the general contractor of a private improvement project, against defendant subcontractor HPH Services, Inc. and its principals, defendants Miller and Haddad (collectively HPH). HPH moves, pursuant to CPLR 3211 (a) (3) and (7), to dismiss plaintiff's second cause of action for diversion of trust assets, based on lack of standing and failure to state a cause of action. Flintlock cross-moves to amend the complaint to add allegations in support of its claim of standing.

The relevant facts are largely undisputed. Flintlock was hired as the general contractor for a new hotel construction project in Manhattan. (Weiss Aff., ¶ 3; Ex. A [construction

contract].) In November 2011, Flintlock entered into a subcontract with HPH for heating, ventilation, and air conditioning services. (Weiss Aff., ¶ 4, Ex. B [sub-contract]; Complaint, ¶¶ 8-9.) Flintlock agreed to pay HPH $3.75 million as a lump sum for the services provided. (Weiss Aff., ¶ 6; sub-contract at 17.) As of October 2012, HPH was no longer a subcontractor on the project. (Complaint, ¶ 18.) Flintlock alleges that, although it advanced HPH $1,116,966 during the project, HPH did not pay all of its suppliers. (Weiss Aff., ¶ 6.) Flintlock commenced this action by summons with notice on November 14, 2012. Flintlock also sought a preliminary injunction against defendants HPH, Miller, Haddad, and Weiner &Weiner, LLC, defendants' escrow agent, to prevent them from, among other things, disbursing monies that were then being held in escrow pursuant to an agreement of the parties. By decision and order dated January 18, 2013, this court denied that motion. Flintlock filed the complaint on February 1, 2013.

Flintlock alleges, and submits evidence, that after the complaint was filed, Flintlock paid $669,654.44 to HPH's suppliers. (Weiss Aff., ¶ 9; Ex. G [cancelled checks].) In exchange, the HPH suppliers that Flintlock paid assigned their claims against HPH for payment to Flintlock. (Id., ¶ 10; Ex. F [assignments].)

HPH moves to dismiss Flintlock's second cause of action on the ground that plaintiff lacks standing. Although HPH claims that the second cause of action should be dismissed for failure to state a cause of action, this claim is also based on plaintiff's alleged lack of standing.[1]

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[1]In seeking dismissal of the second cause of action, HPH uses the terms standing and lack of capacity to sue interchangeably. As the Court of Appeals has explained, "[c]apacity to sue is a threshold matter allied with, but conceptually distinct from, the question of standing. As a general matter, capacity concerns a litigant's power to appear and bring its grievance before the court. Capacity may depend on a litigant's status or . . . on authority to sue or be sued." (Silver v Pataki, 96 NY2d 532, 537 [2001], rearg denied 96 NY2d 938 [2001] [internal quotation marks and citations omitted].) In contrast, "'standing involves a determination of whether the party seeking relief has a sufficiently cognizable stake in the

Flintlock cross-moves to amend the complaint to assert allegations regarding its post-commencement payment of HPH's suppliers and their assignment of claims to Flintlock. Flintlock contends that these allegations establish its standing, either as a subrogee of the claims of HPH's suppliers as trust fund beneficiaries under the Lien Law, or as the assignee of the suppliers' claims.

As a threshold matter, the court rejects HPH's contention that the court is bound by its finding on Flintlock's prior motion for a preliminary injunction that Flintlock's single payment of $5,000 to one vendor of HPH, after this action was commenced, sufficed to make Flintlock a subrogee of all of HPH's Lien Law trust fund beneficiaries. (See HPH Memo. In Support at 2-3; Jan. 18, 2013 Decision at 5-6.) It is well settled that "[t]he granting or refusal of a temporary injunction does not constitute the law of the case or an adjudication on the merits. . . ." (J.A. Preston Corp. v Fabrication Enters., Inc., 68 NY2d 397, 402 [1986] [quoting Walker Mem. Baptist Church v Saunders, 285 NY 462, 474 [1941]; Coinmach Corp. v Fordham Hill Owners Corp., 3 AD3d 312, 314 [1st Dept 2004].)

The court accordingly turns to the merits of the motions to dismiss and to amend. It is undisputed that an Article 3-A trust was established in connection with the development project at issue. The Lien Law provides that all funds paid to a contractor in connection with the improvement of real property constitute assets of a trust to ensure the payment of trust

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outcome so as to cast the dispute in a form traditionally capable of resolution.'" (People ex rel Spitzer v Grasso, 54 AD3d 180, 190 n 4 [2008] [quoting Matter of Graziano v County of Albany, 3 NY3d 475, 479 [2004] [brackets omitted].)

In order to resolve the instant motions, the court need not determine whether HPH's objection to Flintlock's maintenance of the diversion claim is properly characterized as one based on standing or on capacity to sue. The court will assume that the objection goes to standing and will therefore reach the further issue of whether the asserted defect in standing is curable. (See infra at 7-8.)

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beneficiaries, including subcontractors, laborers, and materialmen, and the payment of taxes and other specified expenses. (Lien Law §§ 70 [1], [2]; 71 [2] [a], [b].) The "primary purpose of the Lien Law 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." (Canron Corp. v City of New York, 89 NY2d 147, 155 [1996] [quoting West-Fair Elec. Contrs. v Aetna Cas. & Sur. Co., 87 NY2d 148, 157 [1995]].) "[O]nce a trust comes into existence, its funds may not be diverted for non-trust purposes [and] [u]se of trust assets for any purpose other than the expenditures authorized [by statute] . . . constitutes an improper diversion of trust assets, regardless of the propriety of the trustee's intentions." (Mount Vernon City Sch. Dist. v Nova Cas. Co., 19 NY3d 28, 37 [2012] [internal quotation marks and citations omitted].) "Certainly money paid by the owner to anyone in satisfaction of the contract would be impressed with this broadly inclusive trust." (City of New York v Cross Bay Contr. Corp., 93 NY2d 14, 19 [1999] [internal quotation marks and citation omitted] [emphasis in original].)

Sections 77 (1) and (3) of the Lien Law provide that the "holder of any trust claim, including any person subrogated to the right of a beneficiary of the trust holding a trust claim," may maintain a cause of action for, among other things, enforcement of the trust, an accounting, recovery of diverted trust assets, and money damages. "The equitable doctrine of subrogation 'is applicable to cases where a party is compelled to pay the debt of a third person to protect his own rights, or to save his own property.'" (Broadway Houston Mack Dev., LLC v Kohl, 71 AD3d at 937, 937 [2d Dept 2010] [quoting Gerseta Corp. v Equitable Trust Co. of N.Y., 241 NY 418, 426 (1926)] [other internal citations omitted].) Although subrogation is a "broad" doctrine, "it cannot

be invoked where the payments sought to be recovered are voluntary." (Broadway Houston Mack Dev., LLC, 71 AD3d at 937.) The involuntary nature of payment can be established by the party seeking subrogation "either by pointing to a contractual obligation or to the need to protect its own legal or economic interests. When invoking the latter ground, however, the party seeking subrogation must show that the act is not merely helpful but necessary to the protection of its interests." (Id. [internal citations omitted].)

A party that makes payment to trust beneficiaries will be held to have standing to enforce Article 3-A of the Lien Law where it has already made payment to a contractor and is required to pay the contractor's suppliers or subcontractors after the contractor fails to do so. (See e.g. Wallkill Med. Dev., LLC v Sweet Constructors, LLC, 83 AD3d 695, 695-696 [2d Dept 2011] [holding that where plaintiff paid funds to general contractor for architectural subcontractor and was required by financing contract to deposit funds into escrow to secure payment of same architectural subcontractor, plaintiff acted to protect its own economic interest and had standing as subrogee to bring Lien Law claim]; J. Petrocelli Constr., Inc. v Realm Electric Contrs., Inc., 15 AD3d 444, 446 [2d Dept 2005] [holding that plaintiff general contractor could maintain action under Lien Law article 3-A as a subrogee, where it "was required to make payments totaling $687,066.81" to its subcontractor's vendors after terminating its contract with subcontractor]. Compare Broadway Houston Mack Dev., LLC, 71 AD3d at 937-938, affg 22 Misc 3d 1001, 1008-1010 [upholding trial court's determination that where ground lessee made payments to subcontractors of general contractor that ground lessee had paid in full, such payments were helpful but not necessary to protect ground lessee's interests, because the payments were made to avoid placement of mechanics liens on the premises which could have been discharged or bonded

at a fraction of cost]; See Caristo Constr. Corp. v Diners Fin. Corp., 21 NY2d 507, 510 [1968] [upholding general contractors' claim as subrogee under Lien Law of unpaid subcontractors and suppliers "whom it had paid pursuant to its obligation under a payment bond"]; Matter of RLI Ins. Co. v New York State Dept. of Labor, 97 NY2d 256, 265 [2002] [characterizing Caristo as case which "determined that a contractor/co-obligor who satisfied the claims of unpaid subcontractors and suppliers under a payment bond succeeded to the Lien Law article 3-A rights of those trust beneficiaries and, thus, could maintain an action to recover diverted trust funds"].)

Here, Flintlock contends that by virtue of its payments of $669,654 to HPH's suppliers, Flintlock is subrogated to the trust beneficiaries and has standing to sue. (Weiss Aff., ¶¶ 8, 10.) Flintlock further alleges that these payments were involuntary and were necessary to ensure Flintlock's performance as the general contractor under the construction contract, and otherwise to protect Flintlock's economic interests. Specifically, Flintlock asserts that the payments were required to prevent the construction project "from shutting down due to HPH's suppliers' refusal to deliver their materials to the [construction project] until payment was made"; to complete the work allegedly abandoned by HPH; to avoid delay of completion of the construction project or the work of other subcontractors; to "prevent the owner from imposing liquidated damages on Flintlock in the amount of $3,000 per day for any resulting delays"; to "prevent the owner from holding Flintlock in default" of the construction contract; to prevent the filing of mechanic's liens against the property "which would have resulted in the owner withholding progress payments to Flintlock until the lien claims were bonded by Flintlock"; and to prevent HPH's suppliers from making claims against Flintlock's payment bond. (Id., ¶ 9; Proposed Amended Complaint, ¶¶ 30-42.) Flintlock also asserts that it has standing to maintain this action on the independent ground

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that HPH's suppliers assigned their claims to Flintlock after the commencement of the action.

HPH contends that Flintlock lacks standing to maintain the diversion of trust assets cause of action because it had not made any payments to any of HPH's trust fund beneficiaries and therefore was not their subrogee or assignee at the time it commenced this action. (HPH Memo. In Support at 6.) Now that Flintlock has made substantial payments to HPH's suppliers and their claims against HPH have been assigned to Flintlock, HPH appears to concede that Flintlock has an actual legal stake in the litigation and could bring a second timely action based on those allegations, even if HPH's partial motion to dismiss were granted. (See OA Tr. at 8.) HPH argues, however, that the second cause of action should be dismissed because Flintlock's lack of standing at the outset of the litigation cannot be corrected through an amended complaint. (HPH Memo. In Support at 3-5.)

Standing is "an aspect of justiciability which, when challenged, must be considered at the outset of any litigation." (Socy of the Plastics Indus., Inc. v County of Suffolk, 77 NY2d 761, 769 [1991].) In Cortlandt Street Recovery Corp. v Hellas Telecommunications, S.A.R.L, 2014 NY Slip Op 24268, 2014 WL 4650231 [Sept. 16, 2014], this court discussed the extensive conflicting appellate authority on the issue of whether a defect in standing is curable. The court incorporates that discussion here. The Cortlandt decision held, in accordance with the predominant and more persuasive authority, that a defect in standing is curable where it is not so fundamental as to implicate the court's subject matter jurisdiction or power to hear an action. (See Lacks v Lacks, 41 NY2d 71, 74 [1976], rearg denied 41 NY2d 862 [1977]; Cortlandt, 2014 WL 4650231 at * 6-8 [and authorities cited therein].)

HPH does not argue that this court ever lacked subject matter jurisdiction to hear an action

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for breach of contract or diversion of trust assets. Nor could it persuasively do so. As this Department has reasoned: "The question of subject matter jurisdiction is a question of judicial power: whether the court has the power conferred by the Constitution or statute, to entertain the case before it. Because New York's Supreme Court is a court of original, unlimited and unqualified jurisdiction, it is competent to entertain all causes of action." (Security Pacific Natl. Bank v Evans, 31 AD3d 278, 283 [1st Dept 2006], appeal dismissed 8 NY3d 837 [2007].) The court accordingly holds that although Flintlock lacked standing to maintain the diversion cause of action at the time the action was commenced, this defect in standing was not so fundamental as to implicate the court's subject matter jurisdiction to hear that cause of action.

The court turns, finally, to Flintlock's motion to amend the complaint to plead standing to maintain the diversion cause of action. It is well settled that leave to amend should be freely granted absent prejudice or surprise. (CPLR 3025 [b]; Thomas Crimmins Contr. Co. v City of New York, 74 NY2d 166, 170 [1989].) Although the party seeking leave "need not establish the merit of the proposed new allegations," it must "show that the proffered amendment is not palpably insufficient or clearly devoid of merit." (MBIA Ins. Corp. v Greystone & Co., Inc., 74 AD3d 499, 500 [1st Dept 2010]; accord Miller v Cohen, 93 AD3d 424, 425 [1st Dept 2012].) Applying this standard, the court holds that the motion to amend should be granted, as HPH fails to claim prejudice as a result of the amendment, and the proposed amended pleading alleges sufficient facts to support Flintlock's claim to standing as the subrogee or assignee of Lien Law trust fund beneficiaries.

The court has considered the defendants' remaining contentions and finds them to be without merit.

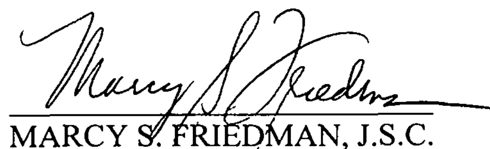
It is accordingly hereby ORDERED that Flintlock's cross-motion for leave to amend the complaint is granted, and the amended complaint in the proposed form annexed to the moving papers shall be deemed served upon service of a copy of this order with notice of entry; and it is further

ORDERED that defendants shall serve an answer to the amended complaint or otherwise respond thereto within 20 days from the date of said service; and it is further

ORDERED that defendants' motion to dismiss is denied.

This constitutes the decision and order of the court.

Dated: New York, New York
November 20, 2014



MARCY S. FRIEDMAN, J.S.C.