Brooklyn Indus. LLC v Hudson 500 LLC
2018 NY Slip Op 32714(U)
October 10, 2018
Supreme Court, New York County
Docket Number: 651378/2018
Judge: Gerald Lebovits

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: HON. GERALD LEBOVITS **PART** IAS MOTION 7EFM

Justice

----------X **INDEX NO.** 651378/2018

BROOKLYN INDUSTRIES LLC, **MOTION SEQ. NO.** 001

Plaintiff,

- v -

HUDSON 500 LLC, KANO REAL ESTATE INVESTORS INC., DAVID SHEMEL, NOAM SHEMEL **DECISION AND ORDER**

Defendants.

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The following e-filed documents, listed by NYSCEF document number (Motion 001) 12, 13, 14, 15, 16, 17, 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 30, 31, 32, 33, 34, 35, 36

were read on this motion to/for SUMMARY JUDGMENT (AFTER JOINDER).

BACKGROUND

Plaintiff, Brooklyn Industries LLC, a Delaware limited-liability company, maintains its principal office in New York. Defendant Hudson 500 LLC (Hudson) is a New York limited-liability company. Defendant KANO Real Estate Investors Inc. (KANO) is a New York business corporation. Defendants David Shemel and Naom Shemel reside and conduct business in New York. They are principals in Hudson and in KANO. On March 20, 2018, plaintiff commenced this action to recover its security deposit, asserting three causes of action: (1) breach of fiduciary duty (against all defendants), (2) conversion (against all defendants), and (3) breach of lease (only against Hudson.)

On March 29, 2006, plaintiff (tenant) and defendant Hudson, plaintiff's landlord, entered into a lease for a retail store at 500 Hudson Street. Plaintiff paid defendant Hudson a security deposit equal to three times the-then monthly rent of $17,000 for the first lease year. In November 2008, after a rent increase, plaintiff paid $4160.60 additional security deposit. On March 4, 2009, Lexy Funk, president and owner of the plaintiff, asked for "a 30% reduction in rent through the end of 2009 effective on April 1." (NYSCEF #36.) On March 18, 2009, David Shemel granted Funk's request partly and sent an email stating that "[t]his is to confirm that a rent concession will take effect on April 1, 2009 – December 31, 2009. [t]he rent reduction is equal to 20% or $3677.44 [t]he new rent will be 14,709.76 for those mentioned 9 months." (NYSCEF #15.)

After lease ended on August 31, 2017, plaintiff asked defendant David Shemel to return the security deposits and all interest. On January 29, 2018, David Shemel sent an email to plaintiff stating that $45,996.96 will be deducted from the total security deposit 51,000.00:

$12,900 as construction costs after plaintiff's move-out to bring the premises back to rentable condition and $33,096.96 in connection with a rent reduction for the period of nine months. (NYSCEF #3.) Plaintiff argues that it learned for the first time on January 29, 2018, that its security deposit was not placed in a segregated interest-bearing account. (NYSCEF #17, 18.) Plaintiff argues that it is entitled to the immediate return of its security deposits plus interest from April 1, 2018. (NYSCEF #17, 49.)

Plaintiff now moves for summary judgment on its causes of action for breach of fiduciary duty, conversion, and breach of lease. Plaintiff also moves to dismiss defendants' counterclaims and affirmative defenses. Defendants oppose the motion.

DISCUSSION

I. Plaintiff's Motion for Summary Judgment for Breach of Fiduciary Duty and Conversion

Plaintiff alleges that defendants breached their fiduciary duty as trustees by failing to place plaintiff's security deposits in a segregated interest-bearing account at a banking organization. (NYSCEF #17, 41.) Plaintiff asserts that David and Noam Shemel are jointly and severally liable with the landlord, Hudson, for breaching this fiduciary duty. (NYSCEF #17, 45.) Plaintiff also asserts a cause of action for conversion. (NYSCEF #17, 47.)

Under CPLR 3212 (b), to obtain summary judgement, "the proponent of summary judgment must make prima facie showing of entitlement to judgment as a matter of law, tendering sufficient evidence to demonstrate the absence of any material issues of fact." (*Alvarez v Prospect Hosp.*, 68 NY2d, 320, 324 [1986].) "Once this showing has been made, however, the burden shifts to party opposing the motion for summary judgment to produce evidentiary proof in admissible from sufficient to establish the existence of material issues of fact." (*Id.*)

General Obligations Law § 7 -103 provides that a landlord "receiving money deposited or advanced shall deposit such money in a banking organization." Accordingly, the landlord "shall notify in writing each of the persons making such deposit, giving the name and address of the banking organization in which, the deposit of security money is made, and the amount of such deposit." (GOL § 7-103 [2-a].) Failure to comply with the GOL § 7-103 notice provision constitutes a rebuttable presumption that the funds commingled. (*Dan Klores Assocs. v Abramoff.* 288 AD2d 121, 121 [1st Dept 2001].) When a defendant fails to rebut a showing of noncompliance with requirements of GOL § 7-103, a plaintiff is entitled to summary judgment. (*Leroy v Sayers,* 217 AD2d 63, 69 [1st Dept 1995].)

Commingling constitutes conversion and a breach of fiduciary duty. (*Id.* at 68-70.) In this lawsuit, plaintiff asserts causes of action for breach of fiduciary duty and conversion, both arising from defendants' alleged violation of GOL § 7-103. Because both causes of actions arise from violations of GOL § 7-103, this court will analyze them together.

Defendants do not dispute that they did not notify plaintiff of the name and address of the bank that held plaintiff's deposit. Therefore, defendant's failure to comply with the statute

constitutes a rebuttable presumption against defendants. Bank statements can refute this presumption. (*Harlem Capital Ctr., LLC v Rosen & Gordon, LLC*, 145 AD3d 579, 558 [1st Dept 2016].) It is a defendant's burden to prove that the security deposit was not commingled with other funds. (*Id.*) Bank statements that reflect amounts slightly more than the security deposit and lists the account name with an identifier raise triable issues of fact with respect to whether there was commingling. (*Id.*)

Defendants provide four bank statements that list the account name as "[t]enant [s]ecurity [m]aster [a]ccount." The amount listed on the bank statement is $22,817.12.

Plaintiff argues that the bank statements are not enough to rebut the presumption of commingling. Plaintiff states that the amount should be $55,160.60, its two security deposits. Plaintiff further argues that this case is distinguishable from *Urban Soccer Inc. v Royal Wine Corp.*, in which a bank statement refuted the allegation of commingling because the amount in the bank statement was equal to the security deposit. (53 Misc 3d 448 [Sup Ct, NY County 2016].) Plaintiff argues that the amount in defendants' bank statements is substantially less than the aggregate amount of its security deposits, 41.37% of the security deposits. (NYSCEF #34.)

Defendants argue the amount in the bank statement, $22,817.12, represents the difference between the $55,160.60 security deposits and the $33,086.96 rent concession plus $752.48 previously accrued interest on the account. (NYSCEF # 31, 6.)

Plaintiff argues that no evidence exists of the $752.48 interest and that the reason defendants allege that the bank account earned $752.48 in interest is that defendants want the numbers to be precise. (NYSCEF #34.)

An issue of fact exists for trial. The amount in the bank statements need not reflect the exact amount of the security deposits to raise triable issues of fact. Amount in a bank statement can be slightly more than the aggregate amount of security deposits. (*See Harlem Capital Ctr.*, 145 AD3d at 558.) Whether the amount in the account is substantially less than the two security deposits, as plaintiff suggests, depends on whether the parties agreed that the rent concession would be repaid from the security deposits.

Defendants state that plaintiff agreed to have the rent concession subtracted from the security deposits. Plaintiff denies this.

Also, the court cannot tell whether the account previously accrued interest of $752.48. The parties disagree about this amount.

Giving the defendants, the nonparty party, all reasonable inferences in their favor, defendants have demonstrated enough at this phase to rebut the presumption of commingling.

Furthermore, although plaintiff argues that no link exists between the submitted bank statements and plaintiff, the name of the bank statements that defendants provide show that bank account is for tenancy purposes.

Plaintiff's motion for summary judgment is denied on the breach of fiduciary duty and conversion claims, its first and second causes of actions.

II. Plaintiff's Summary Judgment for Breach of Lease

On the third cause of action against Hudson, plaintiff alleges that "[l]andlord's failure to deposit and maintain [t]enant's security deposit in a segregated interest-bearing account held at commercial bank constitutes material breach of the lease." (NYSCEF #17, 52.) Defendant assert that KANO maintains an interest-bearing account. (NYSCEF #22, 52) Article 5.7 of the Rider to the Store Lease provides that "[l]andlord agrees to deposit the security interest in an interest-bearing account in a bank located in New York State." (NYSCEF #2.)

When considering a motion for summary judgment, the court's duty is not to resolve issues of fact but merely to determine whether issues exist. (*Meridian Mgt. Corp. v Cristi Cleaning Serv. Corp.*, 70 AD3d 508, 510 [1st Dept 2010].) Here, plaintiff argues that defendant failed to deposit money in an interest-bearing account; defendant Hudson argues that it placed plaintiff's deposits in an interest-bearing account and that $752.48 interest accrued. Material triable issues of fact exist. Plaintiff's summary judgment on its breach of lease cause of action is denied.

III. Plaintiff's Motion to Dismiss Defendants' Counterclaims and Affirmative Defenses

Defendants have asserted four affirmative defenses: (1) plaintiff's representative agreed that the rent reduction would be repaid out of the security deposit, (2) the statute of limitations bars all or portion of plaintiff's claim, (3) security deposits were placed into an interest-bearing account, and (4) defendants are entitled to set off for all or part of any amounts that may be adjudged due to plaintiff. (NYSCEF #22.) Defendants also assert two counterclaims in their answer: (1) breach of lease and (2) breach of the alteration terms of the lease. (NYSCEF #22.) Plaintiff moves to dismiss defendants' counterclaims and affirmative defenses under CPLR 3211 (a) (1) and (7).

As to all counterclaims and affirmative defenses, plaintiff argues that defendants may not assert any right to set off for any purpose because they forfeited the right to avail themselves of the security deposit by violating GOL § 7-103. Because this court found that a triable issue of fact exists about whether defendants commingled funds, plaintiff's argument that defendants' counterclaims and affirmative defenses are barred by GOL § 7-103 is unpersuasive.

Defendants allege in their first affirmative defense that plaintiff's representative agreed that the rent reduction would be repaid out of the security deposit: "Plaintiff's representative agreed that so-called rent reduction would be repaid out of the security deposit." (NYSCEF #22, 50.) Plaintiff argues that it agreed with defendant to a rent concession and that it was a permanent forgiveness of rent. (NYSCEF #34.) Plaintiff argues that no evidence exists that the concession would be deducted from plaintiff's security deposits either in the March 4, 2009, letter requesting a rent reduction or the March 18, 2009, letter. (NYSCEF #34.) Defendants' allegation is sufficient to withstand plaintiff's summary-judgment motion. Whether the parties

had another agreement is a question of fact. Plaintiff's motion to dismiss defendants' first affirmative defense is denied.

Defendants assert in their second affirmative defense that the statute of limitations bars all or a portion of plaintiff's claim. Plaintiff does not set forth the reasons to dismiss defendant's statute of limitations defense. Therefore, plaintiff's motion to dismiss the second affirmative defense is denied.

In their third affirmative defense, defendants assert that they placed plaintiff's security deposits in an interest-bearing account that earned $752.48 interest. (NYSCEF #31.) Bank statements submitted by defendants show that no interest has been credited to the account from June 18, 2015, to date. (NYSCEF #31.) Plaintiff argues that defendants failed to provide relevant records showing $752.48 interest paid on plaintiff's security deposits. (NYSCEF #34.) Issues of fact exist that precludes this court from granting plaintiff's motion. Plaintiff's motion to dismiss defendants' third affirmative defense is denied.

In their fourth affirmative defense, defendants assert four set-offs: (1) $33,096.96 in connection with the rent reduction, (2) $12,900 for expenses to remove rubbish and make repairs to restore the premises to rentable condition, (3) $9000 for expenses incurred to replace the front door to the premises, and (4) $15,000 for expenses defendant expected to incur from issued Department of Buildings (DOB) violation.

The first set-off claim is based on the same argument as the first affirmative defense; therefore, the motion to dismiss is denied.

The second and third set-off claims are based on the same ground as the first counterclaim and the fourth set-off claim is based on the same ground as the second counterclaim. Therefore, this court will analyze them under the related counterclaim.

In their first counterclaim, defendants argue that plaintiff violated section 21 of the lease by failing to remove rubbish, severely damaging an interior wall, and failing to restore the electrical system. Defendants claim that they incurred $12,900 in expenses to remove rubbish and make repairs to the premises to restore it to rentable condition. (NYSCEF #22.) Plaintiff does not explain why this court should grant its motion to dismiss. The motion to dismiss is denied for the section 21 violation claim. In their first counterclaim, defendants also argue that they expect to incur $9000 expenses to replace the front doors to the premises. Plaintiff argues future expenditure of $9000 was not mentioned in the January 28, 2018, letter and therefore that this expenditure contradicts the documentary evidence. (NYSCEF #13). Defendants do not dispute this in their opposition papers. Plaintiff's motion to dismiss the counterclaim for $9000 future expenditure is granted. Therefore, plaintiff's motion to dismiss defendants' first counterclaim is granted in part and denied in part: the $9000 set off, is denied.

In their second counterclaim, defendants argue that plaintiff breached the alteration terms of the lease. As a result of plaintiff's failure to comply with government regulations, defendants expect to incur $15,000 to fix and file the appropriate paper work. (NYSCEF #10.) Plaintiff argues that these future expenditures of $15,000 were not mentioned in the January 28, 2018,

letter and therefore that this contradicts the documentary evidence. (NYSCEF #13.) Defendants do not dispute this in their opposition papers. Plaintiff's motion to dismiss defendants' second counterclaim is granted.

Therefore, plaintiff's motion is granted in part and denied in part.

Accordingly, it is

ORDERED that plaintiff's motion is granted in part and denied in part: part of the first counterclaim, the $9000 setoff, is dismissed; defendants' second counterclaim is dismissed; and the motion is otherwise denied.

10/10/2018
DATE

GERALD LEBOVITS, J.S.C.

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