Ambase Corp. v ACREFI Mtge. Lending, LLC
2019 NY Slip Op 33148(U)
October 22, 2019
Supreme Court, New York County
Docket Number: 653251/2018
Judge: O. Peter Sherwood
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**SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 49**
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AMBASE CORPORATION, 111 WEST 57TH MANAGER FUNDING LLC, and 111 WEST 57TH INVESTMENT LLC,

Plaintiffs,

-against-

ACREFI MORTGAGE LENDING, LLC, APOLLO CREDIT OPPORTUNITY FUND III AIV I LP, AGRE DEBT 1 – 111 W 57, LLC, and APOLLO COMMERCIAL REAL ESTATE FINANCE, INC.,

Defendants.
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**DECISION AND ORDER
Index No.: 653251/2018**

Motion Sequence No.: 001

O. PETER SHERWOOD, J.:

Under motion sequence number 001, defendants move to dismiss the complaint in its entirety pursuant to CPLR 3211(a)(1), 3211(a)(7), and 3016 (b). The motion shall be granted.

I. FACTS

This case arises out of the financing agreements for the construction of a super slender residential skyscraper at 111 57th Street in Manhattan. Plaintiffs are investors in a joint venture with Michael Stern ("Stern') and Kevin Maloney ("Maloney") to acquire and develop the building (complaint ¶ 1). Plaintiffs 111 West 57th Investment LLC ("Investment") and 111 West 57th Manager Funding LLC ("Manager Funding") are both wholly owned subsidiaries of plaintiff AmBase Corporation ("AmBase") (*id.* ¶¶ 9-11). Investment joined with non-party 111 West 57th Sponsor LLC ("Sponsor"), an entity controlled by Stern and Maloney, to form non-party 111 West 57th Partners LLC (the "Company") as part of the joint venture (*id.* ¶ 20). Stern and Maloney also control the entities that are the developer and construction manager for the project (*id.* ¶ 29). Defendants are all affiliated entities operating under the umbrella of Apollo Commercial Real Estate Finance, Inc. ("Apollo"), a real estate investment trust (*id.* ¶¶ 1, 15).

Sponsor, Investment, and nonparty Atlantic 57, LLC, entered into the Amended and Restated Limited Liability Company Agreement (the "Joint Venture Agreement" or "JVA") (Mennitt affirmation, exhibit B [NYSCEF Doc No 13]) on December 17, 2013. Under the JVA, Sponsor – controlled by Stern and Maloney – manages the "day-today" affairs of the Company (complaint ¶ 24; JVA § 7.2). Sponsor's authority is, however, tempered by Investment's right to

approve decisions regarding, *inter alia*, budgets, "any sale, transfer or other disposition…any financing or refinancing", and certain agreement modifications ("Major Decision rights") (complaint ¶ 25; JVA § 7.2[a]). Sponsor must provide Investment with budget updates, subject to Investment's approval, within 60 days of the end of each fiscal year, at a minimum (complaint ¶ 27; JVA § 8.2[b]). The JVA also provides that "if, any time after the closing of the construction loan, Investment declines to approve a proposed budget in which the hard costs exceed an amount equal to at least 110% of the hard costs set forth in the prior approved budget," Investment may demand that Sponsor purchase its equity for an amount that would equal a 20% return on its investment ("Equity Put Right") (complaint ¶ 28; JVA § 11.5).

The joint venture obtained $725 million in financing in June 2015, comprised of a $400 million senior mortgage loan made by non-parties and a $375 million mezzanine loan made by defendants ACREFI and Apollo to 111 West 57th Holdings, LLC ("Original Mezzanine Borrower") (complaint ¶¶ 30-31). The mezzanine loan has since been split into senior and junior mezzanine loans as will be discussed below.

On December 9, 2016, Sponsor sent a letter to Investment seeking approval of a new proposed budget and additional financing to cover additional costs in the proposed budget (*id.* ¶ 41). After requesting further information, Investment determined that "(1) a significant portion of the portion of the budget overruns Stern and Maloney sought to cover with the proposed financing should be considered Manager Overruns for which Stern and Maloney were responsible under the Joint Venture Agreement § 3.2[e], and (2) Stern and Maloney had manipulated the December Proposed Budget in a fraudulent effort to avoid triggering Investment's Equity Put Right" (*id.* ¶ 45). Properly calculated, the new proposed budget met the requirements for Investment to be eligible to exercise its Equity Put Right (*id.* ¶ 46). Investment disapproved the proposed budget and elected to exercise its Equity Put Right, which Sponsor has refused to honor to date (*id.* ¶¶ 47-49).

On January 3, 2017, Apollo issued a notice to Original Mezzanine Borrower, which was also provided to plaintiffs, indicating that due to budget overruns the loan has been and continues to be "out of balance" (*id.* ¶¶ 52-53). On January 25, 2017, Apollo demanded by letter that the Original Mezzanine Borrower pay a Borrower's Shortfall Contribution pursuant to the Mezzanine Loan Agreement that included remaining construction costs that would have triggered Investment's Equity Put Right had those costs been calculated as part of Sponsor's prior proposed

budget (*id.* ¶¶ 54-55). To protect itself from having to buy out Investment's interest, "Apollo, colluding with Stern and Maloney, withdrew its First Borrower's Shortfall Contribution Notice and replaced it with another out of balance letter dated February 1, 2017, this time lowering the out of balance condition to help reinforce Stern and Maloney's... position that 10 percent threshold was not surpassed" (*id.* ¶ 57; exhibit C).

Defendants then continued with their efforts to frustrate Investment's Equity Put Right through two separate efforts designed to "wipe out" plaintiffs, maintain Stern and Maloney as project and development managers, and secure $100 million in new capital for them, so that defendants would not ultimately lose any of the original $325 million loan (*id.* ¶¶ 58-61). Under Plan A, "a new subordinated lender... would purchase the last $25 million of the Apollo loan. It would then loan an additional $60 million to cover immediate budget overruns, plus up to $40 million more, as needed for future overruns" all at an interest rate of more than 20 percent, which would "for all practical purposes" wipe out plaintiffs' equity interests (*id.* ¶ 62). Defendants Stern and Maloney plotted to help to fund the prospective new lender by assisting Stern in refinancing another building project in such a way that the prospective new lender would receive a large cash infusion that could be reinvested in 111 West 57th Street (*id.* ¶¶ 64, 66). Defendants attempted to coerce Investment into consenting to the transaction by "threatening to immediately conduct its own non-judicial mezzanine foreclosure sale", but Investment was not swayed and did not approve the transaction (*id.* ¶¶ 69-72).

Under Plan B, Apollo attempted to circumvent Investment's approval rights by getting investor Spruce Capital to purchase $25 million "of Defendants' debt stack and conduct [a] strict foreclosure" (*id.* ¶¶ 73, 75). That portion of the debt did not exist in a separate note, but defendants restructured it as such by entering into the Junior Mezzanine Construction Loan Agreement with the Borrower, Original Mezzanine Borrower, Stern, and Maloney to break the Original Mezzanine Loan into a $300 million Senior Mezzanine Loan and $25 million Junior Mezzanine Loan (*id.* ¶¶ 31, 76). Stern and Maloney would agree to hand over the keys to Spruce Capital in exchange for "a developer-fee backdoor deal including a share of the upside, to the exclusion of Plaintiffs" (*id.* ¶ 74). In order to circumvent the prohibition in the Intercreditor Agreement ("ICA") barring a lender holding a note in the debt stack from partnering with principals of the borrowers, defendants modified the ICA so that Spruce Capital, through 111 W57 Mezz Investor LLC, could buy the loan and enter into a backdoor arrangement with Stern and Maloney (*id.* ¶¶ 80, 82).

On June 28, 2017, Defendants assigned the Junior Mezzanine Loan to Spruce Capital, and on June 30, 2017, Spruce recalled the Junior Mezzanine Loan based on Borrower's failure to make the Shortfall Contribution required in the second notice (*id.* ¶ 83). The Borrower did not make the payment, and Spruce sent Borrower a proposal to collect the collateral in full satisfaction of the loan pursuant to UCC § 9-620 (*id.* ¶ 85). Plaintiff's position is that the UCC requires the borrower and all interested parties to consent to a "strict foreclosure", and, in any event, such an approval is a "Major Decision" subject to its approval (*id.* ¶ 92). Investor notified Sponsor it intended to disapprove the decision (*id.*). Sponsor's position is that "whether to assert an objection" would not constitute a "Major Decision" and declined to deliver Investment's objection (*id.* ¶¶ 95, 97). Investment then delivered a notice of objection in its own name as an interested party (*id.* ¶ 98). Spruce, however, went forward with the strict foreclosure, resulting in separate litigation against Spruce[1] (*id.* ¶ 99).

In this action, plaintiffs assert claims against defendants for 1) tortious interference with the Put Equity Right and 2) aiding and abetting Sponsor's breach of fiduciary duty.

II. STANDARD

On a motion to dismiss a plaintiff's claim pursuant to CPLR § 3211 (a) (7) for failure to state a cause of action, the court is not called upon to determine the truth of the allegations (*see, Campaign for Fiscal Equity v State,* 86 NY2d 307, 317 [1995]; *219 Broadway Corp. v Alexander's, Inc.,* 46 NY2d 506, 509 [1979]). Rather, the court is required to "afford the pleadings a liberal construction, take the allegations of the complaint as true and provide plaintiff the benefit of every possible inference [citation omitted]. Whether a plaintiff can ultimately establish its allegations is not part of the calculus in determining a motion to dismiss" (*EBC I v Goldman, Sachs & Co.,* 5 NY3d 11, 19 [2005]). The court's role is limited to determining whether the pleading states a cause of action, not whether there is evidentiary support to establish a meritorious cause of action (*see Guggenheimer v Ginzburg,* 43 NY2d 268, 275 [1977]; *Sokol v Leader,* 74 AD3d 1180 [2d Dept 2010]).

To succeed on a motion to dismiss pursuant to CPLR § 3211 (a) (1), the documentary evidence submitted that forms the basis of a defense must resolve all factual issues and definitively dispose of the plaintiff's claims (*see, 511 W. 232nd Owners Corp. v Jennifer Realty Co.,* 98 NY2d 144, 152 [2002]; *Blonder & Co., Inc. v Citibank, N.A.,* 28 AD3d 180, 182 [1st Dept 2006]). A

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[1] *AmBase Corp. et al. v Spruce Capital Partners LLC, et al.*, Index No. 655031/2017

motion to dismiss pursuant to CPLR § 3211 (a) (1) "may be appropriately granted only where the documentary evidence utterly refutes plaintiff's factual allegations, conclusively establishing a defense as a matter of law" (*McCully v. Jersey Partners, Inc.*, 60 AD3d 562, 562 [1st Dept. 2009]). The facts as alleged in the complaint are regarded as true, and the plaintiff is afforded the benefit of every favorable inference (*see Leon v Martinez,* 84 NY2d 83, 87-88 [1994]). Allegations consisting of bare legal conclusions as well as factual claims flatly contradicted by documentary evidence are not entitled to any such consideration (*see e.g. Nisari v Ramjohn,* 85 AD3d 987, 989 [2nd Dept 2011]).

CPLR § 3211 (a) (1) does not explicitly define "documentary evidence." As used in this statutory provision, "'documentary evidence' is a 'fuzzy term', and what is documentary evidence for one purpose, might not be documentary evidence for another" (*Fontanetta v John Doe 1,* 73 AD3d 78, 84 [2nd Dept 2010]). "[T]o be considered 'documentary,' evidence must be unambiguous and of undisputed authenticity" (*id.* at 86, citing Siegel, Practice Commentaries, McKinney's Cons. Laws of N.Y., Book 7B, CPLR 3211:10, at 21-22). Typically that means "judicial records, as well as documents reflecting out-of-court transactions such as mortgages, deeds, contracts, and any other papers, the contents of which are 'essentially undeniable,' " (*id.* at 84-85).

III. DISCUSSION

A. Tortious Interference with Contract

To prove a claim for tortious interference with contract, the plaintiff must show: (1) the existence of a valid contract; (2) defendant's knowledge of the contract; (3) defendants' intentional procurement of the third-party's breach without justification; (4) actual breach of the contract; and (5) damages caused by breach of the contract (*Lama Holding Co. v Smith Barney*, 88 NY2d 413, 424 [1996]); *Kronos, Inc. v AVX Corp.*, 81 NY2d 90 [1993]).

The question with regard to the tortious interference claim is whether plaintiff has adequately alleged "defendants' intentional procurement of the third-party's breach without justification". The first issue is whether plaintiff has alleged Sponsor was predisposed to breach. Defendants primarily rely on *Kansas State Bank*, where the court found on a motion for summary judgment that defendant did not procure a breach where the breaching party communicated its intent to breach before the alleged interfering conduct on the part of defendant (66 AD3d at 1411). While the standard here is different, "[o]nce a plaintiff alleges facts… establishing that the

breaching party was predisposed toward breaching its agreement, the claim for tortious interference must be dismissed for failure to plead 'but for' causation" (*Granite Partners, L.P. v. Bear, Stearns & Co. Inc.*, 17 F. Supp. 2d 275, 294 [SD NY 1998], citing *Rapp Boxx, Inc. v. MTV, Inc.,* 226 AD2d 324 [1st Dep't 1996]). Here, defendants contend the plaintiffs have alleged that Sponsor had previously rejected plaintiff Investment's first attempt to exercise the Equity Put Right (complaint ¶ 48), and Sponsor was therefore predisposed to breach, regardless of the effect of Apollo's notice. Plaintiffs, however, argue that Sponsor was not predisposed to breach – this case is distinguishable from *Kansas State Bank* because Sponsor did not communicate its intent to reject the Equity Put Right until February 24, 2017 (*id.*) after the defendants withdrew their first "out-of-balance" notice on February 1, 2017 (*id.* ¶ 57). Construing the facts such that plaintiffs receive the benefit of all possible inferences, plaintiffs' claim for tortious interference should not be dismissed at this time based on predisposition.

The second issue is whether defendants' issuance of the shortfall contribution notice could be the "but for" cause of the breach, since Apollo's notice could not have had an effect on triggering of the Equity Put Right. The JVA provides that:

> In the event that (i) prior to the closing of the Construction Loan, Investor declines to approve a proposed Budget that exceeds the Permitted Variance applicable to the prior approved Budget, (ii) after the closing of the Construction Loan, Investor declines to approve a proposed Budget in which the hard costs exceed an amount equal to one hundred ten percent (110%) of the hard costs set forth in the prior approved Budget, (iii) Manager has not obtained, within twenty-four (24) months of the date hereof, an "Alteration 1" or "New Building" permit…, or (iv) the amount of the Construction Loan is less than fifty percent (50%) of the applicable Budget for the development and construction of the Property…, Investor shall have the right, upon notice within sixty (60) days after the occurrence of the applicable event set forth in clauses (i), (ii) or (iii) above… to require Sponsor to purchase Investor's equity interest in the Company for a purchase price equal to an amount that would cause Investor to receive a 20% Priority Distribution…"

(NYSCEF Doc No 13 [JVA] § 11.5). Defendants contend the documentary evidence shows that "both of Apollo's subsequent notices in January and February 2017 all exceeded the 'total hard costs' in the prior approved June 2015 budget by more than the 110% threshold" and it would have been impossible for the reissued notice from Apollo to have had any effect on the numbers at issue (reply at 6, citing mem at 15 n 6).

Plaintiffs' position is merely that it is a question of fact that should not be decided on this motion to dismiss. The core of plaintiffs' allegation is that defendants' withdrawal "enabled" the breach:

> "Apollo, colluding with Stern and Maloney, withdrew its First Borrower's Shortfall Contribution Notice and replaced it with another out of balance letter dated February 1, 2017, this time lowering the out of balance condition to help reinforce Stern and Maloney's (still incorrect) position that the 10 percent put threshold was not surpassed... By withdrawing the notice, Defendants enabled Sponsor to argue that the Equity Put Right had not been in fact triggered, and Sponsor thereafter breached the Joint Venture Agreement by refusing to honor that right. But for Defendants' improper conduct of withdrawing and replacing that notice, Sponsor... would have been under vastly enhanced and more urgent pressure to fulfill its contractual obligations under the Joint Venture Agreement concerning the Equity Put Right"

Since the Sponsor's rejection came after the reissuance, it is unclear from the facts alleged whether Sponsor would have breached had defendants not reissued the notice. But if the notices reflect the arithmetic as defendants present it, that it would have been impossible for the notice to have any effect, then the claim may be defeated by the documentary evidence.

The third issue is whether defendants may be excused based on a justifiable economic purpose. "[F]or the interference to be deemed tortious, the [defendant] must have acted without justification and its action must not have been incidental to a lawful purpose... Where a defendant procures the breach of a contract in the exercise of an equal or superior right, it is acting with just cause or excuse and has justification for what would perhaps otherwise be an actionable wrong" (*Intern. Nut Alliance, LLC v Bank Leumi USA*, No. 650149/2016, 2016 WL 5791508, at *3 [N.Y. Sup. Ct. Sep. 30, 2016], citing *Torrenzano Group, LLC v. Burnham*, 26 AD3d 242, 243 [1st Dep't 2006]).

Defendants argue they merely exercised a contractual right to seek shortfall contributions in order to further their economic interest in the venture. Defendants submit the mezzanine loan agreement and the reissued shortfall contribution letter, which states it is "based solely upon the Borrower's original construction budget and Borrower's December 2016 updated construction budget" (Mennitt aff, exhibit G). Only in their moving papers do defendants state that the lower demand is an attempt to avoid a dispute and collect the payment (mem at 16-17). Plaintiffs concede defendants had a contractual right, but challenge the adequacy of the evidence that proves they did

so to serve an economic purpose. Plaintiffs believe defendants have failed to establish their motivation by "irrefutable evidence", but defendants believe they have done so by showing they exercised a contractual right.

As discussed in *Intern. Nut Alliance*, the exercise of a contractual right is a justifiable economic purpose. Defendants evidence the right by providing the Mezzanine Loan Agreement (NYSCEF Doc. No. 16), which is irrefutable, even if the other correspondence provided in support of the defense is not. The case that plaintiffs cite in support of the proposition that defendants cannot claim economic interest where they act for the benefit of other projects, involves facts not analogous to the instant case. *White Plains* answered a specific question about whether "a generalized economic interest in soliciting business for profit constitute[s] a defense to a claim of tortious interference with an existing contract for an alleged tortfeasor with no previous economic relationship with the breaching party" (8 NY3d at 425). Here, the mezzanine loan was part of the financing for the breaching party's project, and Apollo, having rights under that loan, exercised them. Finally, "economic interest is a defense to an action for tortious interference with a contract unless there is a showing of malice or illegality" (*Foster v Churchill*, 87 NY2d 744, 750 [1996]). Plaintiff may have alleged that defendants acted against their interests, but have not alleged that they were motivated by malice or that they acted illegally. Therefore, the claim for tortious interference may be dismissed based on the economic justification defense.

B. Aiding and Abetting Breach of Fiduciary Duty

To establish a claim for aiding and abetting a breach of fiduciary duty, plaintiff must demonstrate "a breach of fiduciary duty, that the defendant knowingly induced or participated in the breach, and damages resulting therefrom" (*Bullmore*, 45 AD3d at 464). "A person knowingly participates in a breach of fiduciary duty only when he or she provides 'substantial assistance' to the primary violator" (*Kaufman v Cohen*, 307 AD2d 113, 126 [1st Dept 2003]).

Because the Members, including Investment and Sponsor, waived their fiduciary duties to each other outside of those arising from (i) fraud or intentional misconduct, or (ii) an unauthorized transaction under which a personal benefit was derived, the first issue is whether plaintiff has adequately alleged an underlying breach sounding in fraud or intentional misconduct (JVA § 8.5). The JVA provides, in relevant part:

> "[N]one of the Members shall have any duties or liabilities to the Company or any other Member (including fiduciary duties),...and each Member hereby expressly waives any such duties or liabilities; provided, however, that this Section 8.5 shall

> not eliminate or limit the liability of such parties (i) for acts or omissions that involve fraud, intentional misconduct or a knowing and culpable violation of that law, or (ii) for any transaction not permitted or authorized under or pursuant to this Agreement from which such party derived a personal benefit"

(*id.*). Defendants' position is that plaintiff could not be damaged by Plan A because it never happened, and with respect to Plan B, the Mezzanine Loan Agreement permitted splitting of the debt. Plaintiffs believe they have a claim based on their allegations that Sponsor, Stern and Maloney colluded "to wipe out Investment and obtain a new infusion of capital" through two separate schemes (complaint 59-61).

Plaintiffs analogize this case to a Delaware case, in which the court found that the plaintiffs stated a claim for breach of fiduciary duty where a company's directors approved a transaction that "wiped out the value of the common equity and surrendered all of that value to the company's creditors" (*Blackmore Partners, L.P. v Link Energy LLC,* 864 A2d 80, 86 [Del. Ch. 2004]). Likewise, here, Investment alleges that its stake in the project was totally "wiped out" by the strict foreclosure, assisted by defendants' "backdoor" refinancing (complaint ¶ 74). While *Blackmore* is not controlling, defendants do not attempt distinguish it.

As far as defendants' substantial assistance in the breach is concerned, plaintiffs allege that defendants modified the Intercreditor Agreement to permit Spruce to partner with Stern and Maloney (complaint ¶¶ 82, 117, 118). Defendants had a contractual right to modify the ICA and the transaction was structured to facilitate additional mezzanine financing (NYSCEF Doc. No. 23 [Org. Chart]). The Mezzanine Loan Agreement also contradicts plaintiff's characterization of the restructuring since the agreement would expressly permit it under section 5.1.9: " If, after the date of this Agreement, Lender elects to modify, split, and/or sever any portion of the Loan as described in this Section… Borrower shall cooperate, and cause each Direct Borrower Party to cooperate, in each case" (Mennitt affirmation, exhibit E [NYSCEF Doc No. 16]). However, "even where one has an apparently unlimited right under a contract, that right may not be exercised solely for personal gain in such a way as to deprive the other party of the fruits of the contract" (*Richbell Info. Servs., Inc. v. Jupiter Partners, L.P.*, 309 AD2d 288, 302 [1st Dept 2003]). In *Richbell*, the First Department found that plaintiff adequately alleged a breach of fiduciary duty where "the allegations [went] beyond claiming only that [defendant] should be precluded from exercising a contractual right; they support a claim that [defendant] exercised a right malevolently, for its own

gain as part of a purposeful scheme designed to deprive plaintiffs of the benefits of the joint venture and of the value of their pre-existing holdings" (309 AD2d at 302).

Such is not alleged here and the claim of aiding and abetting breach of fiduciary duty must be dismissed.

C. Punitive Damages Request

Defendants argue that because the conduct at issue was taken pursuant to their contractual rights, for the protection of their economic interests, and without harm to the public, plaintiff's request for punitive damages is frivolous and should be stricken (mem at 22). As the complaint shall be dismissed, the request for punitive damages fails. Even if one or more of plaintiffs' claims were to survive, the punitive damages claim would be stricken because plaintiff has not alleged "evil or malicious conduct beyond any breach of professional duty", and thus the demand for punitive damages should be stricken from the complaint (*Dupree v Giugliano*, 20 NY3d 921, 924 [2012]).

It is hereby

ORDERED that the motion of defendants to dismiss the complaint is GRANTED in its entirety and the complaint is hereby dismissed; and it is further

ORDERED that the Clerk of the Court is directed to enter a judgment in favor of defendants and against plaintiffs dismissing the complaint together with costs to be taxed against plaintiffs in an amount to be fixed by the Clerk upon presentation of a proper bill of costs.

This constitutes the decision and order of the court.

DATED: October 22, 2019

ENTER,

O. PETER SHERWOOD J.S.C.