STATE OF NEW YORK
SUPREME COURT : COUNTY OF ERIE

YELLOWSTONE CAPITAL LLC,

Plaintiff,

DECISION AND ORDER
Index No: 811837/2017

v.

CENTRAL USA WIRELESS LLC d/b/a CENTRAL USA WIRELESS AND CHRISTOPHER R. HILDENBRANT,

Defendants.

BEFORE: **HON. TIMOTHY J. WALKER, Presiding Justice**

APPEARANCES: **HODGSON RUSS, LLP**
Steven W. Wells, Esq., Of Counsel
Christopher Castro, Esq., Of Counsel
Attorneys for Plaintiff

LAW OFFICE OF LEWIS A. BARTELL
Lewis A. Bartell, Esq., Of Counsel
Attorneys for Defendant

WALKER, J.

Defendants have moved, pursuant to CPLR 5015, to vacate a certain Confession of Judgment, void certain merchant agreements, and enjoin any prosecution thereon. Defendants' arguments (that the transactions effectuated by the merchant agreements at issue are actually loans) have been submitted time and time again to a plethora of New York Courts, and have almost uniformly been rejected. Indeed, as this Court has previously determined in similar matters, the merchant agreements are, in fact, business contracts that are entered into between sophisticated business parties, which clearly reflect the purchase of a certain percentage of a

merchant's total future accounts receivable, up to a certain amount, for a specified purchase price. The terms of these merchant agreements are abundantly clear and, in most cases, these arrangements allow merchants to survive a period of cashflow shortage.

Equally important, every posited argument in support of Defendants' motion has already been considered and rejected numerous times by the trial courts of the State of New York. Additionally, there is clear Appellate Division case law determining that judgment debtors (such as Defendants) cannot challenge judgments entered against them by confession unless they are defective on their face, were entered without authority or in violation of its terms, were procured in violation of any due process requirements, or were the result of fraud - none of which are present in this case (*see Summerour, Inc. v. Bradhil Industries Inc.*, 91 AD2d 902, 902 [1st Dept. 1983]).

Courts across the state have considered almost identical arguments and agreements, and have (almost uniformly) denied motions to vacate on the grounds that (1) a judgment debtor must commence a plenary action, rather than a motion, if it seeks to challenge the merchant agreement and the confession of judgment that was entered against it; and/or (2) that the merchant agreements do not constitute loans subject to the usury laws (*see, e.g., EBF Partners, LLC v. Kevin R. Hackenberg d/b/a Nu Wave Botanicals and Kevin Hackenberg*, Index No. 802383/2017 [Erie Co. June 30, 2017]; *Yellowstone Capital, LLC v. Jevin*, Index No. 802457/2017 [October 6, 2017]).

There have been over twenty-eight (28) recent cases where New York State Courts considered substantially similar motions, involving substantially similar merchant agreements, and almost all of those courts denied the relief, at least in part, because a judgment debtor may

not seek to invalidate a confession of judgment entered against the judgment debtor on the grounds that it resulted from a usurious loan by way of motion (*see* NYSCEF DOC. NO. 30). In no less than thirty-eight (38) recent decisions, New York Courts have determined that the merchant agreements at issue (which are all substantially or exactly the same as the merchant agreement at issue here) do not constitute loans (*see* NYSCEF DOC. NO. 30; *see also Champion Auto Sales, LLC et al. V. Pearl Beta Funding, LLC*, 159 AD 2d 507 [1st Dept. 2018] [wherein the court determined that "the underlying agreement lending to the judgment by confession was not a usurious transaction"]). The merchant agreement at issue in *Champion Auto* is substantially similar to the merchant agreement in this case. Because there are no other Appellate Division decisions directly on point, the *Champion Auto* decision is binding on this Court (*Phelps v. Phelps* 128 AD 3d 1545, 1547 [4th Dept. 2015]).

In addition, CPLR 3218(a) provides that: "a judgment by confession may be entered, without an action, either for money due or to become due...upon an affidavit executed by the [confessing party]." The affidavit of confession "is sufficient if it adequately sets out the facts giving rise to the underlying debt..." (*Spires v. Mihou*, 273 AD 2d 844 [4th Dept. 2000]). This sufficiency requirement exists to protect third parties, i.e., creditors of the confessing party, who would be injured by a collusively obtained confession (*Eurofactors Int'l, Inc. v. Jacobowitz*, 21 AD 2d 443, 445 [2nd Dept. 2005]). Furthermore, courts will enforce a confession of judgment supported by consideration "irrespective of the alleged manner in which the underlying guarantee was procured" (*Demchuk v. North Fork Bank & Trust Co.*, 121 AD 2d 680, 680 [2nd Dept. 1986]). Courts will set aside a judgment by confession only where the party challenging the confession demonstrates "by a preponderance of clear, positive and satisfactory evidence... fraud,

misconduct or other [similar] circumstances..." (*City of Poughkeepsie v. Albano*, 122 AD 2d 14, 14-15 [2nd Dept. 1986]). Critically, "only a third-party judgment creditor has standing to question *on motion* the validity of a judgment by confession ... [whereas] a defendant debtor who seeks to attack such a judgment must proceed by plenary action" (*Id.* at 14) emphasis added; *see also Bufkor, Inc. v. Wasson & Fried, Inc.*, 33 AD 2d 636, 636 [4th Dept. 1969] [reversing the Trial Court's decision to vacate a judgment by confession on motion and holding that a plenary trial was required]).

In this case, the Confession of Judgment unequivocally complies with CPLR § 3218: (1) It states the sum for which judgment may be entered; (2) It authorizes the entry of judgment in Erie County and others; (3) It states concisely the facts out of which the debt arose and showed that the sum confessed is justly due, and (4) It is supported by an affidavit setting forth the default that was the basis for filing the Confession of Judgment.

Counsel for merchants filing these types of motions have previously, almost exclusively, cited the decision in *Merchant Funding Services, LLC v. Volunteer Pharmacy, Inc.*, 55 Misc.3d 316 [Westchester Co. Dec. 30, 2016] as the basis for attempting to use motion practice to vacate confessions of judgment. *Volunteer Pharmacy* is a decision from a trial court in Westchester County that not only represents the quintessential outlier, but is ***not*** controlling or precedential case law, and is not even ***settled*** case law (as it is the subject of an appeal to the Second Department). Indeed, the Second Department has consistently held that a confession of judgment can only be vacated by a plenary action (*see Regency Club at Wallkill, LLC v. Bienish,* 95 AD 3d 879 [2nd Dept. 2012]; *Estate of Zelman v. Scibelli*, 157 AD 2d 705 [2nd Dept. 1990]; *A.B.J.M. Corp. v. Prudenti,* 270 AD 2d 219 [2nd Dept. 2000]; and *City of Poughkeepsie*, 122 AD 2d at 14).

Hence, the decision in *Volunteer Pharmacy,* is a ruling on a procedural issue, and is no more "binding" on Plaintiff than it is on this Court.

Moreover, in *Merchant Funding Services, LLC v. Micromanos Corporation et al.,* (Index No. EF000598-2017), this Court analyzed the same merchant agreement as did the court in *Volunteer Pharmacy,* and came to a completely opposite conclusion: "Defendants' position is grounded on a dubious misreading of the [Merchant] Agreement." This Court dismissed the defendants' bases for claiming that the merchant agreement resulted in a loan (which are substantially the same bases asserted in the Motion for Defendants' claim that the YSC Merchant Agreement creates a loan), and ruled as follows:

> Therefore, the Secured Merchant Agreement is not on its face and as a matter of law a criminally usurious loan. Consequently, Defendants have failed to establish an exception to the general requirement that relief from a judgment entered against them upon the filing of an affidavit of confession of judgment must be sought by way of a separate plenary action.

Micromanos at p. 5.

Thus, Defendants lack standing to challenge the Judgment by way of motion practice and may only seek to have it vacated in a plenary action. There is no such action pending in Erie County, or anywhere else in New York. Defendants' Motion is denied for this threshold reason.

Assuming *arguendo*, if Defendants had standing, the merchant agreement does not create a usurious loan. Instead, as expressly provided in the agreement, the transaction is a purchase of a specified percentage of all future receipts generated by the merchant's accounts receivable, up to the "Purchased Amount".

"Usury is an affirmative defense, and a heavy burden rests upon the party seeking to impeach a transaction based upon usury" (*Hochman v. Larea*, 14 AD 3d 653, 654 [2nd Dept. 2005] [internal citations omitted]). "Thus, usury must be proved by clear and convincing

evidence as to all its elements and usury will not be presumed" (*Id.*) "There is a strong presumption against the finding of usury" (*Transmedia Rest. Co., Inc. v. 33 E. 61 Street Rest. Corp.*, 184 Misc.2d 706, 710, 710 [Sup. Ct. N.Y. Co. 2000]). The only "proof" that Defendants submit in support of their usury claim are self-serving misconstructions of cherry-picked provisions of the merchant agreement, and an outright disregard for contrary provisions contained in that document.

Criminal usury requires a loan. Pursuant to New York Penal Law § 190.40, the statute relied upon by Defendants, a person commits criminal usury where he "knowingly charges, takes or receives ... interest on a loan or forbearance of any money or other property, at a rate exceeding twenty-five percent per annum." Thus, the statute requires a "loan," payment of "interest," and intent (*Accord, Seidel v. E. 17th Street Owners, Inc.*, 79 NY 2d 735, 744 [1992] ["If the transaction is not a loan, there can be no usury, however unconscionable the contract may be"]). "In order for a transaction to constitute a loan, there must be a borrower and a lender; and it must appear that the real purpose of the transaction was, on the one side, to lend money at usurious interest reserved in some form by the contract and, on the other side, to borrow money upon the usurious terms dictated by the lender" (*Donatelli v. Siskind*, 170 AD 2d 433, 434 [2nd Dept. 1991]).

"[A] primary indicia of usury is repayment of the principal sum advanced absolutely" (*see Merchants Advance, LLC v. Tera K, LLC T/A Tribeca Frank Crabetta*, 2008 NY Misc. LEXIS 10889, at p. * 4 [Sup. Ct. N.Y. Co. Dec. 19, 2008]). This is a strict and inflexible requirement (*see Zoo Holdings, LLC v. Clinton*, 11 Misc.3d 1051(A), 814 NYS 2d 893, at p. * 4 [Sup. Ct. N.Y. Co. Jan. 24, 2006]). "Where payment or enforcement rests upon a contingency, the

agreement is valid even though it provides for a return in excess of the legal rate of interest" (*Prof'l Merch. Advance Capital, LLC v. Your Trading Room, LLC*, 2012 NY Misc. LEXIS 6757, at pp. *13-14 [Sup. Ct. Suffolk Co. Nov. 28, 2012]); *Kelly, Grossman & Flanagan, LLP v. Quick Cash, Inc.*, 35 Misc.3d 1205(A) [Sup. Ct., Suffolk Co., 2012]; *O'Farrell v. Martin*, 163 Misc.353 [City Ct., N.Y. 1936]). In this case, payment of the "Purchased Amount" is contingent upon the merchant generating sufficient accounts receivable such that the "Specified Percentage" of those receivables will support payment of the Purchased Amount over a reasonable period of time, and, therefore, the payment is not absolutely payable.

Numerous courts -- at least thirty-eight (38) -- have reviewed the provisions of merchant agreements structured almost exactly as the agreement at issue in this case, and uniformly held that such agreements are not usurious (*see* NYSCEF DOC. NO. 31).

Recently, my colleague (Hon. Henry Nowak, J.S.C.) issued a decision in *Yellowstone Capital,* involving a challenge to a merchant agreement on the grounds that it was criminally usurious. Justice Nowak's analysis focused on whether "the agreement was actually a purchase for accounts receivables [or] a loan with a usurious interest rate. . . ." Justice Nowak noted that:

> A distinguishing factor between a purchase of accounts receivable and a loan is the burden of risk and the contingency of repayment. In a purchase of accounts receivable, repayment is for an indefinite term, contingent on the amount of accounts receivable. Thus, the lender bares the risk that there could be no or low daily receipts. However, if the lender holds only a loan, repayment is absolute and the merchant bears the risk of non-payment by the account debtor; while the lender only bears the risk that the account debtor's non-payment will leave the merchant unable to satisfy the loan.

Recognizing that the agreement at issue had a reconciliation clause, Justice Nowak determined that New York Courts have found that the presence of a reconciliation provision such as the one in this matter is a significant factor in determining that the agreement should be characterized as a purchase of accounts receivables as opposed to a loan." He distinguished the

cases relied upon by the merchant there -- the same cases relied upon by Defendants in this case – *Merchant Funding Services, LLC v. Volunteer Pharmacy Inc.*, 55 Misc.3d 316, 318 [Sup. Ct. Westchester Co. 2016] and *Pearl Capital Rivis Ventures v. RDN Construction*, 54 Misc.3d 470, 474 [Sup. Ct. Westchester Co. 2016]), "because there was no evidence that the agreements at issue included reconciliation provisions. Accordingly, the court held that the merchants had "not demonstrated that the agreement is a usurious loan in violation of Penal Law § 190.40. (*Id.*)

Numerous New York Courts have reviewed the provisions of agreements structured almost exactly as the agreement at issue in this case, and have uniformly held that such agreements are not usurious. The reasoning of all of these cases applies equally to the present dispute. The merchant agreement is not a loan, and the usury statutes do not apply (*see also, Champion Auto Sales, LLC, supra.*

It is abundantly clear that the "Daily Payment," both in its initial calculation, based upon Plaintiff's review of Defendants' past performance, and any adjustment based upon the reconciliation provisions is directly based upon the Specified Percentage of accounts receivable Plaintiff purchased. That is clearly not how a loan is structured.

Defendants never requested that a reconciliation be conducted. Instead, Defendants ceased remitting Daily Payments after remitting only $20,982.00 of the $80,245.00 in accounts receivable Plaintiff purchased.

For the reasons set forth above, the Motion is denied as a matter of law. In addition, the Court determines, in light of the history of these litigated matters and known binding precedent, Plaintiff is entitled to recover reasonable attorneys' fees and costs incurred in defending the Motion, subject to the submission of an affirmation setting forth the time detail with narratives.

Dated: June 25, 2018
Buffalo, New York

HON. TIMOTHY J. WALKER, J.C.C.
Acting Supreme Court Justice
8th Judicial District