

**SUPREME COURT-STATE OF NEW YORK
SHORT FORM ORDER**

Present:

HON. TIMOTHY S. DRISCOLL
Justice Supreme Court

-----X
EVELYN AND ANTHONY IPPOLITO,
on behalf of themselves and on behalf of all
persons entitled to share in the funds received by
TJC DEVELOPMENT LLC., in connection with a
project identified as the renovation of the residence
located at 273 Park Avenue,
Babylon, New York 11702,

Plaintiffs,

-against-

TJC DEVELOPMENT, LLC, GERALD POINTING
and JOSEPH TORTO,

Defendants.

TRIAL/IAS PART: 25
NASSAU COUNTY

Index No: 18898-07
Motion Seq. Nos: 1 and 2
Submission Date: 8/17/09

The following papers having been read on these motions:

Notice of Cross Motion (Opposition to Class Certification),
Affirmation in Opposition and Exhibits.....X
Notice of Motion, Affidavit in Support and Exhibits.....X
Affirmation in Further Support/Opposition and Exhibit.....X
Plaintiffs' Memorandum of Law.....X
Defendants' Supplemental Memorandum of Law.....X

This matter is before the Court for decision on 1) the cross motion filed by Defendants on February 13, 2009 ("Cross Motion"),¹ and 2) the motion filed by Plaintiffs on February 17, 2009 ("Plaintiffs' Motion"). By Order dated June 17, 2009 ("Prior Order"), the

¹ Defendants' Cross Motion is assigned Motion Sequence #1, although it appears to be responsive to Plaintiffs' Motion, designated Motion Sequence #2.

Court directed oral argument on these motions. Pursuant to that Prior Order, the Court conducted oral argument on these motions and the motions were submitted on August 17, 2009.

For the reasons set forth below, the Court: 1) grants Defendants' Cross Motion to dismiss the Verified Complaint, but grants Plaintiffs leave to file an Amended Verified Complaint against Defendants Gerald Pointing and Joseph Torto, but not against Defendant TJC Development, LLC, for any viable cause(s) of action, other than a cause of action pursuant to Article 3-A of the Lien Law; and 2) denies Plaintiffs' Motion as moot.

BACKGROUND

A. Relief Sought

Plaintiffs move for an Order, pursuant to CPLR § 902 and Lien Law § 77(1), 1) permitting the claim in the Complaint to be maintained as a class action; 2) defining the class as all beneficiaries of Lien Law Article 3-A trust funds received by TJC Development, LLC ("TJC") in conjunction with the project known as the renovation of 273 Park Avenue, Babylon, New York; 3) directing Defendants to provide a list of all Lien Law Article 3-A trust beneficiaries to Plaintiffs; and 4) determining the method of notice to the members of the class.

Defendants move to dismiss the verified complaint ("Complaint"), pursuant to CPLR §§ 3211(a)(1) and (5), on the grounds that 1) Plaintiffs failed to move for the certification of a class within sixty (60) days of commencing the action, in violation of CPLR § 902(a) and New York Lien Law ("Lien Law") § 77(1); and 2) the action is barred by the principles of collateral estoppel and *res judicata*, in light of the arbitration of similar claims. Alternatively, Defendants move, pursuant to CPLR § 3025(b), to amend their verified answer ("Answer") to the Complaint to add the defenses of *res judicata* and collateral estoppel. Plaintiffs oppose Defendants' Motion.

B. The Parties' History

Plaintiffs have filed this class action lawsuit, pursuant to Article 3-A of the Lien Law, to recover damages and costs they allegedly incurred as a result of Defendants' diversion of trust assets, and for punitive damages. Defendant TJC Development, LLC ("TJC") is the general contractor for a home improvement project or renovation of property located at 273 Park Avenue, Babylon, New York ("Premises"), owned by Plaintiffs Evelyn and Anthony Ippolito ("Plaintiffs" or "Ippolitos"). Defendants Gerald Pointing ("Pointing") and Joseph Torto ("Torto") are principals of TJC.

The factual allegations of the Complaint are as follows: By agreement dated August 12, 2004 (“Agreement”), Plaintiffs retained TJC to perform substantial renovations to the Premises for an agreed-upon price of \$300,000. Plaintiffs allege that TJC failed to 1) provide adequate labor; 2) provide the material required; and 3) pay sub-contractors and material suppliers during construction. Plaintiffs terminated TJC and arranged for other contractors to complete the project, and to correct non-conforming and sub-standard work that TJC performed.

The Complaint asserts a single class action claim under Article 3-A on behalf of Plaintiffs and all trust beneficiaries. Plaintiffs aver that they paid TJC approximately \$296,883.00, which payment was impressed with an Article 3-A trust to be held and applied for payment of the costs of the project including materials, labor and equipment. Plaintiffs allege, upon information and belief, that TJC 1) received and diverted trust assets; 2) consented to the diversion of trust assets; and 3) knowingly diverted trust assets, all in violation of Article 3-A of the Lien Law. They make the identical allegations against Defendants Pointing and Torto.

Plaintiffs allege that Defendants never completed the renovation project and, upon information and belief, did not maintain proper accounting records reflecting the establishment of a trust fund. They aver that the failure to keep the appropriate records is presumptive evidence of a diversion of trust funds, and that the diversion of those funds constitutes a larceny under the Penal Law. They allege, further, that the foregoing acts constitute a public as well as a private harm, and that Defendants acted with malice and/or reckless or wilful disregard for the Plaintiffs' rights. Plaintiffs seek compensatory damages in the amount of \$150,000, plus attorney's fees and “exemplary and punitive” damages in the amount of \$1,000,000,000 (one million dollars).

As the Agreement required, Plaintiffs previously submitted their claim for breach of contract against TJC to arbitration. The Claimants in the arbitration are Anthony and Evelyn Ippolito and the Respondent in the arbitration is TJC Development LLC. Arbitrator Thomas J. Rossi, in a decision dated December 7, 2008, concluded that TJC breached the Agreement “by failing to adequately prosecute the project and not completing the project in a reasonably timely fashion” and that the Ippolitos were “justified in terminating the contract and retaining others to complete the project.” With respect to damages, Arbitrator Rossi (“Rossi”) held that the Ippolitos were “entitled to an award equal to the reasonable costs to complete the work under the

contract, and the reasonable value of the work needed to correct any deficient work performed by [TJC], less the amount remaining to be paid under [TJC's] contract.” Rossi declined to base an award of damages solely on the amount that the replacement contractor charged, in light of Rossi’s conclusion that the replacement contractor performed additional work not provided for under the original contract. Instead, Rossi relied on the estimate of Olympic Siding & Window Co., Inc., concluding that it was a “more reliable measure” of reasonable completion costs because it made reference to “the deficient work as noted by the architect and the original plans for the project.” Rossi thus awarded Plaintiffs a total of \$121,155.32, representing damages (\$102,674) plus interest (\$18,481.32).

Plaintiffs have been unable to recover from TJC on the arbitration award. As Defendants’ counsel affirms in his Order to Show Cause, TJC is no longer an ongoing business. Plaintiffs now seek to hold TJC principals Pointing and Torto liable for a diversion of trust funds under Lien Law Article 3-A.

By Order dated June 17, 2009 (“Prior Order”), the Court directed oral argument on these motions to address the issue of whether the Lien Law was intended to create a trust relationship between a homeowner and a contractor, which is the relationship between the parties in the matter *sub judice*. Counsel for the parties addressed this issue at the oral argument.

C. The Parties’ Positions

Plaintiffs submit that they have met the requirements for certification of this action as a class action, in light of language in the Lien Law that permits beneficiaries of trust funds held by a home improvement contractor to sue to enforce that trust. Plaintiffs argue, further, that class certification is necessary because the Lien law requires Plaintiffs to assert their claim against Defendants in a representative capacity. Plaintiffs submit that the Court’s denial of Plaintiffs’ certification application would effectively eliminate Plaintiffs’ right to seek a remedy pursuant to the Lien Law. Finally, Plaintiffs ask the Court to waive the requirements regarding class certification set forth in CPLR §§ 901 and 902. Plaintiffs submit that the Court should liberally construe these provisions and, further, that the Court has discretion in determining whether to grant class action certification.

Defendants move to dismiss the Complaint, submitting that Plaintiff’s application for class certification is untimely. Defendants argue, further, that the claims in the Complaint are

“unquestionably within the scope of the claims” subject to arbitration pursuant to the Agreement, and, therefore, Plaintiffs waived their right to sue TJC by failing to arbitrate their trust diversion claim during the arbitration. Thus, Defendants submit, Plaintiffs’ instant action is barred by the principles of collateral estoppel and res judicata.

In support of their position that the Lien Law is not applicable to the matter before the Court, Defendants cite, *inter alia*, *Langston v. Triboro Contracting*, 44 A.D.3d 365 (1st Dept. 2007) and *Select Construction Corp. v. 502 Old Country Road LLC*, 11 Misc. 3d 1078A (Sup. Ct. Nassau Cty. 2006). In support of their position that the Lien Law is applicable to this matter, Plaintiffs cite, *inter alia*, *People v. Hollowell*, 168 A.D.2d 970 (4th Dept. 1990) and *Stern v. DiMarzo*, 2008 NY Slip Op. 51163U (Sup. Ct. Westchester Cty. 2008).

RULING OF THE COURT

A. Effect of Arbitration Award

The principles of *res judicata* clearly apply to arbitration awards. *Simpson v. County of Westchester*, 5 A.D.3d 780, 781 (2d Dept. 2004), *lv. app. den.* 3 N.Y.3d 602 (2004), citing, *inter alia*, *Matter of Ranni [Ross]*, 58 N.Y.2d 715, 717. Rossi’s arbitration award was based on the Ippolitos’ allegation that TJC did not complete certain work contemplated by the Agreement. The Ippolitos now seek similar relief in the action *sub judice*, *i.e.*, to recover trust funds held for work that TJC did not complete.

Under the “transactional analysis” applicable here, once a claim is brought to a final conclusion “all other claims arising out of the same transaction . . . are barred even if based upon different theories or if seeking different remedies.” *Simpson*, 5 A.D.3d at 782. Both the breach of contract and trust claims arise out of nonperformance of the Agreement, and the difference between the claims asserted during the arbitration, and those asserted in the Complaint, lies solely in the legal theory that Plaintiffs propound and the remedy they seek. Accordingly, the Ippolitos may not seek to recover trust funds against TJC. However, assuming that the action were not otherwise foreclosed, the prior arbitration does not foreclose the Plaintiffs’ pursuit of this action against Defendants Pointing and Torto, who are not parties to the Agreement, and, absent circumstances not alleged here, could not be compelled to participate in arbitration. *TNS Holdings v. MKI Securities Corp.*, 92 N.Y.2d 335 (1998) (court may require “alter ego” of signatory to arbitrate).

Defendants Pointing and Torto were not parties to the contract or the arbitration proceeding, and thus are neither bound by Rossi's conclusion that TJC breached the contract, nor protected by the defense of *res judicata* with respect to any of Rossi's findings.

B. Applicability of Lien Law to Defendants

The starting point for the Court's analysis regarding the applicability of the Lien Law is *South Carolina Steel v. Miller and Nationwide Steel*, 170 A.D.2d 592 (2d Dept. 1991). There, the Court held:

Lien Law [A]rticle 3-A was designed and enacted to create trust funds out of certain construction payments and thus ensure, or at least make more certain, that those whose skill, labor, and materials create an improvement are paid for their services [citations omitted]. The Lien Law provisions which create a statutory trust do not, however, preclude an unpaid contractor from pursuing recovery under the parties' contract. Rather, the statutory trust provisions are intended to provide aggrieved subcontractors or materialmen with additional remedies by enabling them to recover diverted trust funds from third parties who are not in privity with the parties to the contract [citations omitted].

The language in *South Carolina Steel* strongly suggests that, while the Plaintiffs in the matter *sub judice* may have a cause of action against the Defendants for breach of contract or other claims, which they have not alleged in the Complaint, their Lien Law claims against the Defendants may not be viable.

One of the cases that Plaintiffs cite in support of their position is *People v. Hollowell*, 168 A.D.2d 970 (4th Dept. 1990). *Hollowell* is a criminal case in which the defendant was charged, *inter alia*, with two counts of grand larceny under Lien Law § 79-a in connection with funds that the defendant received to construct a deck for the complainant. On May 22, 1988, the complainant paid defendant money to construct a deck for the complainant's home before July 4. The defendant never returned to construct the desk, instead depositing the money into his business checking account and spending it for his business and personal expenses. As a result, defendant had no money with which to purchase supplies to perform the work. At the time that he spent the money, defendant owed over \$18,000 and had filed for bankruptcy a month previously. The lower court dismissed the two counts of larceny under the Lien law, concluding that defendant lacked the requisite intent to commit larceny. The Second Department reversed, concluding that, under the circumstances presented, a jury could infer that defendant, when he misappropriated trust funds, intended to deprive complainant of the trust funds or appropriate

them to himself. *Id.* at 970-971.²

The Court in *Hollowell* held that, as a result of the amendment of Lien Law § 71(2) by the addition of paragraph (f), applicable to contracts entered into after March 1, 1988, trust claims were extended to include owners' claims to funds that the owners advanced to contractors for the construction of home improvements. The Second Department concluded that, because the complainant contracted with defendant after the effective date of the new amendment, he had a valid trust claim against the moneys he advanced for his home improvement. The Court held, further, that defendant's alleged misappropriation of the money and failure to pay the complainant's trust claim may constitute the crime of larceny under Lien Law § 79-a. 168 A.D. 2d at 971.

The Court in *Hollowell* concluded that the evidence was sufficient to establish a violation of Lien Law § 79-a(1)(b) which provides:

1. Any trustee of a trust arising under this article, and any officer, director or agent of such trustee, who applies or consents to the application of trust funds received by the trustee as money or an instrument for the payment of money for any purpose other than the purposes of that trust, as defined in section seventy-one, is guilty of larceny and punishable as provided in the penal law if

(b) such funds were received by the trustee as contractor or subcontractor, as such terms are used in article three-a of this chapter, and the trustee fails to pay, within thirty-one days of the time it is due, any trust claim arising at any time; provided, however, that if the trustee who received such funds as contractor or sub-contractor disputes in good faith the existence, validity or amount of a trust claim or disputes that it is due, the application of trust funds for a purpose other than a trust purpose, or the consent to such application, shall not be deemed larceny by reason of failure to pay the disputed claim within thirty-one days of the date when it is due if the trustee pays such claim within thirty-one days after the final determination of such dispute.

The defendant in *Hollowell* never performed any of the work contracted for and essentially disappeared with the complainant's money. Defendants in the matter *sub judice*, on the other hand, performed extensive work. Moreover, they disputed the claim which was addressed at the arbitration and resulted in an award to Plaintiffs, albeit for less than they demanded. Under the

² The Court held that the other larceny count based on the Lien Law was properly dismissed because the transaction in question predated the amendment that, the Court held, extended trust claims to include claims of owners who advanced funds to contractors for the construction of home improvements. *Hollowell*, 168 A.D.2d at 971.

circumstances, the Court is not persuaded that the decision in *Hollowell*, which addressed the validity of criminal charges against a contractor who took money from the complainant and never performed any work, establishes the Plaintiff's right to assert a Lien Law claim in the matter *sub judice*.

Plaintiffs also cite *Stern v. DiMarzo*, 2008 NY Slip Op. 51163U (Sup. Ct. Westchester Cty. 2008) in support of their claimed right to assert a Lien Law claim against Defendants. *Stern* involved plaintiff-homeowners who entered into an agreement with defendant contractors to renovate their home. The plaintiffs claimed that 1) they paid defendants well in excess of the value of the services defendants provided; 2) defendants charged plaintiffs for work on other, unrelated projects; 3) intentionally inflated their costs to cover the alleged diversion of funds; and 4) took substantially more profit than they deserved. *Id.* at p. 3. The plaintiffs also alleged that they deposited money into a separate account that the defendant contractor corporation maintained for each project in which it was involved. *Id.* at p.4.

The plaintiffs' verified complaint in *Stern* contained a cause of action based on plaintiffs' allegation that, once they deposited money into the account, a statutory trust was created by operation of the New York State Lien Law. The plaintiffs asserted, further, that defendants were statutory trustees who diverted funds to other, unrelated projects, and that this diversion was a violation of the Lien Law. The plaintiffs also alleged that, as a result of this diversion, certain subcontractors remained unpaid. *Id.* at 19.

In addressing defendants' contention that plaintiffs lacked standing to maintain an action based on breach of trust provisions in that statute, the *Stern* Court discussed the amendments to the Lien Law, to which the *Hollowell* Court also referred, stating as follows:

Under the amended statute, 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 [citation omitted]. 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.

2008 NY Slip Op. 51163U at p.20.

Defendants in the matter at bar submit that *Stern* is readily distinguishable and not controlling. They contend that 1) the Stern court's extension of the Lien Law was not central to the Court's holding, which was that a homeowner may pursue a fraud claim against a contractor who inflates the costs that his company incurred; 2) the Ippolitos, unlike the plaintiffs in *Stern*, have paid nothing to the subcontractors, suppliers or other workers that TJC employed in connection with the Ippolitos' addition, and none of those subcontractors have filed mechanic's liens or asserted trust fund claims in connection with the Ippolitos' project; 3) the applicable laws do not require the general contractor to deposit the owner's advances into an escrow account or grant the homeowner rights in advances that the contractor has properly deposited into his general account; and 4) TJC properly deposited the Ippolitos' payments into its general business account, as authorized by Lien Law § 71-a(4)(a) and (g).

Defendants cite *Langston v. Triboro Contracting*, 44 A.D.3d 365 (1st Dept. 2007), in which the Court affirmed the lower court's denial of plaintiff-homeowner's motion for partial summary judgment on his causes of action against defendant contractor for diversion of Lien Law Article 3-A trust funds. *Id.* In affirming that decision, the Court rejected plaintiff's argument that he was entitled to the return of money that he paid to defendant, simply because the money, paid over time with checks, was never deposited into an escrow account. *Id.* The Court held that "the issue, in deciding whether there has been a diversion of trust funds, is not whether the funds have been deposited in a bank, but whether the funds have actually been used to pay subcontractors, suppliers and laborers [citation omitted]." *Id.* at 365-366.

The Court is persuaded that, at the very least, the precedents above do not establish the Ippolitos' right to assert a claim under the Lien Law under the facts of this case, and actually suggest that plaintiffs may not assert such a claim. Thus, plaintiffs' claims that are based on the Lien Law are not viable.

C. Amendment of Complaint

Pursuant to CPLR § 3025(c), the Court may permit pleadings to be amended before or after judgment to conform them to the evidence, upon such terms as may be just including the granting of costs and continuances. The decision whether to permit amendment of the pleadings is within the Court's discretion, and the Court should freely grant leave to amend pleadings, absent prejudice or surprise resulting directly from the delay. *Sanford v. Sanford*, 176 A.D.2d

932, 933 (2d Dept. 1991).

D. Standards for Dismissal

A complaint may be dismissed based upon documentary evidence pursuant to CPLR § 3211(a)(1) only if the factual allegations contained therein are definitively contradicted by the evidence submitted or a defense is conclusively established thereby. *Yew Prospect, LLC v. Szulman*, 305 A.D.2d 588 (2d Dept. 2003); *Sta-Bright Services, Inc. v Sutton*, 17 A.D.3d 570 (2d Dept. 2005).

Pursuant to CPLR § 3211(a)(5), a party may move for judgment dismissing one or more causes of action against him on the grounds, *inter alia*, that the action may not be maintained because of collateral estoppel or *res judicata*. Collateral estoppel requires that there be an identity of issue which has necessarily been decided in the prior action and is decisive of the present action, and a full and fair opportunity to contest the decision now said to be controlling. *Beuchel v. Bain*, 97 N.Y.2d 295, 303-304 (2001), *cert. den.* 535 U.S. 1096 (2002). Collateral estoppel is a flexible doctrine that must be applied on a case by case basis. *Id* at 304.

E. Conclusion

In light of the foregoing, the Court concludes that 1) Plaintiffs' action against TJC Development, LLC is barred, pursuant to the doctrine of *res judicata*, by the Arbitration Award; and 2) the Lien Law is not applicable to the matter at bar, but Plaintiffs may have other valid causes of action against Defendants Gerald Pointing and Joseph Torto. Accordingly, the Court 1) grants Defendants' Cross Motion to dismiss the Complaint, but grants Plaintiffs leave to file an Amended Verified Complaint against Defendants Gerald Pointing and Joseph Torto for any viable causes of action, other than a cause of action pursuant to Article 3-A of the Lien Law the Lien Law; and 2) denies Plaintiffs' Motion as moot.

DATED: Mineola, NY
October 16, 2009

ENTER

HON. TIMOTHY S. PRISCOLL
J.S.C.

ENTERED

OCT 21 2009

NASSAU COUNTY
COUNTY CLERK'S OFFICE