SUPREME COURT OF THE STATE OF NEW YORK, COUNTY OF KINGS

Index No 522397/2024

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ITRIA VENTURES LLC,

Plaintiff,

-against-

SOTATX, LLC DBA GOOSEHEAD INSURANCE, BSS FINANCIAL, LLC and SHAUN COLIN WILLIAM SEXTON, BRITTANY MARTINEZ SEXTON,

Defendants.

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ANSWER

Defendants by their attorney retained solely therefor answer the complaint:

1. Admit that plaintiff (a foreign limited liability company) is authorized to do business in New York. Deny that it has offices in New York.

2. Admit paragraph 2.

3. Admit paragraph 3.

4. Admit paragraph 4.

5. Admit paragraph 5.

1. Deny paragraph 1. Plaintiff is a LENDER.

2. Paragraph 2: Admit the date of the contract, the payback sum, and that the parties' transaction was for the amount stated, but otherwise denies. The contract had nothing to do with any purchase.

3. Deny paragraph 3. The contract had a fixed weekly payment regardless of receipts.

4. Paragraph 4: Admit the date of the contract, the payback sum and that the parties' transaction was for the amount stated, but otherwise denies. The contract had nothing to do with any purchase.

5. Deny paragraph 5. The contract had a fixed weekly payment regardless of receipts.

6. Paragraph 6: Admit that the subject contract states what this paragraph alleges it states. Denies if anything more is alleged.

7. Paragraph 7: Admit that the subject contract states what this paragraph alleges it states. Denies if anything more is alleged.

8. Paragraph 8: Admit that the subject document states what this paragraph alleges it states. Denies if anything more is alleged.

9. Admit paragraph 9 as to personal jurisdiction but deny as to subject matter jurisdiction.

10. Denies the First Claim for Relief and each and every paragraph therein and every other allegation of the complaint not expressly admitted above.

First Affirmative Defense: Illusory Contract. No Risk

11. To find as a matter of law that the contract was a genuine purchase, and not a loan, the transaction must be "sufficiently risky" for the funder. Strategic Funding Source, Inc. v. Takeastrole, LLC, 2023 NY Slip Op 33062(U), 4; LG Funding, LLC v United Senior Props. of Olathe, LLC, 181 A.D.3d 664 [2020]: "These provisions suggest that the plaintiff did not assume the risk that United would have less-than-expected or no revenues."

12. Plaintiff's contract eliminated the risk.

13. **Feb. 28, 2023** Contract: The plaintiff's funding/loan started at a 37% annual rate of interest. 37% is 1.47 times the 25% maximum under the criminal usury statute.

14. **Calculation of Interest**: Under the Agreement, the total paid to Defendant was $73,000, less startup fees, for which Defendant had to pay plaintiff back $93,750, by a weekly payment of $2,343.75 per week. Defendant getting gross proceeds from plaintiff of $73,000, and having to pay back $93,750, the difference, of $20,750, was the interest that Defendant had to pay on the $73,000. $20,750 interest on $73,000, if it had to be paid back over a year, would have been 28.4% interest. The agreement required weekly payments of $2,343.75 per week, which meant 40 payments of $2,343.75 each, to pay the $93,750. 40 weeks is 77% of a year. Since 28.4% interest had to be paid back in 77% of a year, that was an annual interest rate of 37%.

15. The weekly receipts of defendant needed for the $2,343.75 fixed weekly payment under the contract, at the specified percentage of 6.13%, equaled $38,234.09 (6.13% of $38,234.09 = $2,343.75).

16. The initial 37% interest rate was 1.47 times the 25% criminal usury cap. 25 times 1.47 = 37%.

17. By the 25% criminal usury cap, the Legislature determined that any higher rate was utterly unaffordable and took criminal advantage of a borrower.

18. If the fixed weekly payment was reduced so that 6.13% of receipts equaled the 25% maximum criminal usury rate rather than the 37% criminal rate, the receipts needed would only be $25,867.37. Calculation: The 37 interest rate divided by 25 =1.47. The $38,234.09 receipts needed under the contract to cover the 6.13% Specified Percentage divided by 1.47 = $25,867.37.

19. Therefore, until the plaintiff granted a reconciliation taking 6.13% of only $25,867.37 of receipts, the funding was criminally usurious.

20. If $93,750.00 has to be paid back after receipt of $73,000.00 with fixed weekly payments each week and an annual interest rate

of 25%, each weekly payment would equal $1575,66 which at 6.13% of weekly receipts would equal $25,867.37 of receipts.

21. Until receipts dropped to $25,867.37, the 6.13% specified percentage was criminally usurious.

22. If the defendant's receipts diminished from $38,234.09 to $25,867.37, it would have to cut back on everything.

23. **May 17, 2023 Contract**: The plaintiff's funding/loan started at a 48.5% annual rate of interest. 48.5% is 1.93 times the 25% maximum under the criminal usury statute.

24. **Calculation of Interest**: Under the Agreement, the total paid to Defendant was $73,000, less startup fees, for which Defendant had to pay plaintiff back $97,500, by a weekly payment of $2,708.33 per week. Defendant getting gross proceeds from plaintiff of $73,000, and having to pay back $97,500, the difference, of $24,500, was the interest that Defendant had to pay on the $73,000. $24,500 interest on $73,000, if it had to be paid back over a year, would have been 33% interest. The agreement required weekly payments of $2,708.33 per week, which meant 33 payments of $2,708.33 each, to pay the $97,500. 33 weeks is 69% of a year. Since 33% interest had to be paid back in 69% of a year, that was an annual interest rate of 48.5%.

25. The weekly receipts of defendant needed for the $2,708.33 fixed weekly payment under the contract, at the specified percentage of 6.09%, equaled $44,471.76 (6.09% of $44,471.76 = $2,708.33).

26. The initial 48.5% interest rate was 1.93 times the 25% criminal usury cap. 25 times 1.93 = 48.5%.

27. By the 25% criminal usury cap, the Legislature determined that any higher rate was utterly unaffordable and took criminal advantage of a borrower.

28. If the fixed weekly payment was reduced so that 6.09% of receipts equaled the 25% maximum criminal usury rate rather than the 48.5% criminal rate, the receipts needed would only be $22,934.05. Calculation: The 48.5% interest rate divided by 25 =1.93. The $44,471.76 receipts needed under the contract to cover the 6.09% Specified Percentage divided by 1.93 = $22,934.05.

29. Therefore, until the plaintiff granted a reconciliation taking 6.09% of only $22,934.05 of receipts, the funding was criminally usurious.

30. If $97,500.00 has to be paid back after receipt of $73,000.00 with fixed weekly payments each week and an annual interest rate

of 25%, each weekly payment would equal $1396.68 which at 6.09% of weekly receipts would equal $22,934.05 of receipts.

31. Until receipts dropped to $22,934.05, the 6.09% specified percentage was criminally usurious.

32. If the defendant's receipts diminished from $44,471.76 to $22,934.05, it would obviously be utterly unable to run its business with insufficient funds to pay employees, landlord, tax, materials, work expense, etc. Assuming that someone in business for themselves, like the individual defendant, needed some kind of draw from his business to live on, his family was going hungry and homeless.

33. It is as if the $210,900 salary of a New York Supreme Court justice was reduced $109,274.61.

34. For plaintiff to then use a reconciliation to deduct a fixed weekly payment of 6.09% of the $22,934.05 could not reasonably be contemplated under the parties' contract since the debtor would be forced to block plaintiff's 6.09% debit if receipts dropped to $22,934.05.

35. This would enable plaintiff to declare a default.

36. In sum, taking the position that a debtor whose receipts stayed the same has no excuse not to suffer this $2,708.33 fixed weekly payment is enforcing criminal usury.

37. Taking the position that a debtor who has not requested a reconciliation has no excuse not to pay this $2,708.33 fixed weekly payment is enforcing criminal usury.

38. The entire premise of the contracts was false and illusory because each contemplated that about 6% was the affordable payback but the combination of the two resulted in over 12%.

39. The entire premise of the contract was false and illusory because it purported to restrict defendants from any personal use of the business account (quoted in subsequent affirmative defense) when, to the contrary, it was obvious from the inception that the said account would be the source of the individual defendant's livelihood. People do not form a company in order to serve as its unpaid volunteer director/officer but, instead, to draw their livelihood from it. People's livelihood includes not only basics but other expenses such as children's college tuition, annual vacations, etc.

40. The entire premise of the contract was illusory because it purported to be a purchase of receivables, or receipts, payable from future sales, but if there was a default, the entire purchase price for such future sales was immediately due and payable even though such sales perforce did not exist.

41. It has already been established that there is no such thing as a purchase of future receivables. Stathos v. Murphy, 26 A.D.2d 500 First Dept. [1966] "(affirmed *** upon the opinion at the Appellate Division" 19 N.Y.2d 883, 885 [1967]):

> "The confusion in this area of the law arises primarily from a failure to distinguish between the assignment of future rights, such as future wages, revenues on contracts yet to be made, and the like, regarded as after-acquired property, and the assignment of present rights, typically choses in action, which have yet to ripen into deliverable assets, particularly money. * * *
> There is no doubt that the assignment of a truly future claim or interest does not work a present transfer of property. It does not because it cannot; no property yet exists."

42. The contract was full of promised benefits and rights which were illusory and false, having been taken away or made impossible by other provisions.

43. The contract indicated that payments made to plaintiff would be conditioned upon defendant's sale of products and services, and the payment therefore by defendant's customers: "Purchaser's right to receive remittances under this Agreement is contingent on your receipt of Receivables."

44. This benefit was illusory because under the contract, plaintiff intended to ACH-debit the fixed daily payment each business day regardless of receipts:

> This is the periodic amount ("Periodic Amount") to be remitted to Purchaser every week
>
> 4(1) You hereby authorize Purchaser to debit the designated amount from your Approved Account(s) on the periodic basis specified above,

45. The reconciliation provision was illusory (see, more specific defense below).

46. The notice provision stated:

> (c) Notices. All communications between the parties with respect of, or notices, requests, directions, consents or other information sent under, this Agreement shall be in writing and delivered by email (with proof of transmission) to an email address of the other party at which such party normally and customarily receives email communications as of the time the notice is sent or, at the request of any party, by Federal Express or other internationally recognized courier (with signature). All such communications and notices shall be effective upon receipt or sending with proof of transmission.

47. This made any right of defendant to demand anything under the agreement illusory because the benefit of allowing requests could be delayed and rejected at plaintiff's whim by refusing to sign for or claim the dispatch.

48. Section 4.3 further made any benefit or right of defendant to notify plaintiff or demand anything of plaintiff illusory, there being no email or other address of plaintiff stated in the contract and anything outside of the contract was invalid.

49. The contract did not expressly make bankruptcy a default and appeared to permit bankruptcy without a default.

50. The individual guarantor, under the contract, guaranteed the performance of the "merchant" defendant. This guaranty of performance did not cease upon a bankruptcy.

51. Bankruptcy was effectively barred by the parties' agreement, among others, because the plaintiff's contract prohibited defendants from changing the approved bank account or depositing receipts into any other account:

> (v) Closing of Accounts. Merchant shall not close any Approved Account provided to Purchaser without Purchaser's express prior written approval.

52. A bankrupt or debtor in possession violates Federal Law by failing to open a debtor-in-possession account or failing to deposit receipts into the debtor-in-possession account.

> Rushton v. American Pac. Wood Prods. (In re Americana Expressways), 133 F.3d 752, 756-757 [1997]:
> "The United States Trustee has the responsibility for supervising Chapter 11 debtors in possession. The trustee's Operating Guidelines and Reporting Requirements mandate that the debtor in possession close prepetition bank accounts and open new accounts that include the words "Debtor in Possession." See Appellees' Supp. App. 91. 4 The debtor in possession is an officer of the court and subject to the bankruptcy court's power and control. See Chmil v. Rulisa Operating Co. (In re Tudor Assocs. Ltd. II), 64 B.R. 656, 661 (E.D.N.C. 1986)."

> C.C Canal Realty Trust v. Harrington, (In re Spenlinhauer), 2017 WL 1098820; 2017 U.S. Dist. LEXIS 42336, *9:
> "Debtors-in-possession are also required to deposit post-petition funds into designated debtor-in-possession bank accounts. See In re Sieber, 489 B.R. 531, 548-49 (Bankr. D. Md. 2013)."
>
> Jackson v. GSO Bus. Mgmt., LLC (In re Jackson), 643 B.R. 664, 699 [2022]:
> "The unauthorized withdrawal of funds from a debtor-in-possession bank account is an affront to the integrity of the bankruptcy process."

53. Bankruptcy was prohibited by these provisions which are inimical and antithetical to bankruptcy:

> 1 * * * you will continue to operate the Merchant business in good faith.
>
> B 2 *** (i) Good Faith. Merchant will at all times conduct its business in good faith and consistent with past practice as disclosed to Purchaser, and agrees that it will not take any action designed to impair or frustrate Purchaser's ability to collect Receivables.

54. This made the entire contract illusory.

55. The contracts stated:

> 2c *** "Receivables" also includes the Receivables of Merchants subsidiaries and affiliated companies and, upon a Material Breach, of any (x) new or existing company owned or controlled by Merchant or any Guarantor (collectively, an "Other Business"), (y) any new or existing company, whether owned or controlled by Merchant or Guarantor or any third party, to which all or a material portion of the business or assets of Merchant are

> sold or otherwise transferred (collectively, a "Successor Company") or (z) any affiliate of any of the foregoing, in each case without the express prior written consent of Purchaser.

56. This provision prevented the guarantor from forming or participating in or becoming employed in any other entity.

57. This eliminated any genuine risk.

58. The contracts stated:

> (d) Rights of Purchaser. Without any prior notice to you, Purchaser may: (1) compromise or settle any claim, liability or obligation of Merchant under this Agreement or of any customer owing a Receivable purchased hereunder; (2) contact any credit card processor of Merchant in order to place a "hold" on all account funds upon the occurrence of a Material

59. This eliminated any risk and made the contract illusory, it enabling plaintiff to grab all receipts or potential receipts of defendant at any time for any reason or no reason at all and put defendant in default.

60. The contract purported to be a purchase. This was illusory. Plymouth Venture Partners, II, L.P. v. GTR Source, LLC, 37 N.Y.3d 591, [Now Chief Justice] Rowan Wilson Diss. Op. (4-3 majority held that a CPLR 5240 motion is required, not a tort action, to attack the illegal enforcement method of a judgment):

> "Although the GTR and CMS agreements are described as "factoring" agreements, they do not bear several of the hallmarks of traditional factoring arrangements, in that

> FutureNet did not sell any identifiable receivable to GTR or CMS; GTR and CMS did not collect any receivables; GTR and CMS received fixed daily withdrawals from FutureNet's bank account regardless of whether or how much FutureNet collected from or billed to its clients; and GTR and CMS did not bear the risk of nonpayment by any specific customer of FutureNet. The arrangements FutureNet entered with GTR and CMS appear less like factoring agreements and more like high-interest loans that might trigger usury concerns (*see Adar Bays, LLC v GeneSYS ID*, — NY3d —, 2021 NY Slip Op 05616 [2021])"

Home Bond Co. v. McChesney, 239 U.S. 568, 575-576 [1916]:

> "[A]ppellant, by virtue of the contracts between it and the bankrupts *** did not become the purchaser or owner of the accounts receivable in question, and *** the transactions were really loans, with the accounts receivable transferred as collateral security. *** To quote from the opinion of the District Court: "The considerations which support this conclusion are that the bankrupts were to and did collect the accounts and bear all expense in connection with their collection * * * In so far as the contracts in question here use words fit for a contract of purchase they are mere shams and devices to cover loans of money at usurious rates of interest."

Endico Potatoes v. CIT Group/Factoring, 67 F.3d 1063, 1069, 2d Cir. Ct. of App. N.Y. [1995]:

> "Where the lender has purchased the accounts receivable, the borrower's debt is extinguished and the lender's risk with regard to the performance of the accounts is direct, that is, the lender and not the borrower bears the risk of non-performance by the account debtor. If the lender holds only a security interest, however, the lender's risk is derivative or secondary, that is, the borrower remains liable for the debt and 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 borrower unable to satisfy the loan."

61. None of these defects constituted invented or theoretical defenses. Crystal Springs Capital v Big Thicket Coin, 220 AD3d 745, 747, 748 [2023] held that the language in the merchant funding agreement, alone, will establish these defenses.

> "Here, the defendants established that the agreement constituted a criminally usurious loan. *** [T]he defendants conclusively established through the submission of the agreement that it constituted a criminally usurious loan (see Adar Bays, LLC v GeneSYS ID, Inc., 37 NY3d at 332; LG Funding, LLC v United Senior Props. of Olathe, LLC, 181 AD3d at 666)."

62. The foregoing has reasonably placed the plaintiff on notice of the defense that the contract was illusory, nor need the defendants enumerate every manner in which the contract could be found illusory.

Second Affirmative Defense: Appellate Division Opinion of Nov. 28, 2023, Guiding Whether Transaction Is a Loan

63. Kapitus Servicing, Inc. v Point Blank Constr., Inc., 221 A.D.3d 532 [2023]:

> "Further, although the presence in an agreement of a right to reconciliation may be an indication of whether an agreement constitutes a loan, the agreement here does not make clear on its face whether it conferred that right (see Davis v Richmond Capital Group, LLC, 194 AD3d 516, 517 [1st Dept 2021])."

64. The plaintiff's contract had a seeming reconciliation provision but other provisions that abridged any right to a reconciliation. The contract had a seeming reconciliation at section 5.5 Merchant's Right of Reconciliation.

65. The provision did not provide any manner of calculating a reconciliation.

66. No time period over which any reconciliation is to be calculated provided other than maximum 90 days prior.

67. No deadline was set forth for any calculation or implementation "promptly calculate the excess and provide a credit or refund to your Merchant account, as you may specify;".

68. A reconciliation could be immediately rescinded, the contracts stating:

> 5 *** You agree that, during each month a Forward Adjustment reconciliation is in effect, you are still required to provide additional documentation covering such period as we may reasonably request. We will then review such documentation in good faith in order to determine whether it is appropriate to continue the Forward Adjustment or return to the original Purchase and Sale Terms. You further agree to promptly notify us in the event any Forward Adjustment reconciliation covering future periods is no longer required or if your Receivables increase to levels estimated in the Purchase and Sale

69. At no time in its existence has the plaintiff ever refunded to any "merchant" any amount previously ACH-debited from the merchant because a reconciliation found that the total previously ACH-debited exceeded the Specified Percentage of the prior sales, receipts, revenue, or receivables.

70. At no time in its existence has the plaintiff ever credited to any "merchant" any amount previously ACH-debited from the merchant because a reconciliation found that the total previously ACH-debited exceeded the Specified Percentage of prior sales, receipts, or revenue, receivables.

Third Affirmative Defense: Criminal Usury.

71. Oakshire Props., LLC v Argus Capital Funding, LLC, ___ AD3d ___, 2024 NY Slip Op 03943, Fourth Dept. Appellate Division, held that:

A. "although there is a reconciliation provision in the agreement, the provision appears illusory inasmuch as Argus may not be subject to any consequences for failing to comply with its terms"

Here, while not stating that failure to reconcile would constitute a breach, the contract eliminated any remedy or consequences to plaintiff in the event that plaintiff failed to reconcile ("12. Limitation of Liability"), and permitted plaintiff to continue to ACH-debit the automatic payments even if it did not reconcile.

B. "Argus has sole discretion to adjust the amount of the daily payments."

This was present here (above).

C. "a default on the part of Oakshire would occur where, inter alia, "two or more [automatic withdrawal] transactions attempted by [Argus] within one calendar month are rejected by [the] bank," immediately accelerating the entire amount"

As the complaint admitted, nonpayment was a default:

> Complaint: 6. The RSA sets forth certain actions which would result in a material breach of the RSA, one of which is Merchant Defendant's failure to timely remit to Plaintiff the Remittance Amount (the "Material Breach")

D. "there was an implied finite term in the agreement inasmuch as plaintiffs allege that the daily payment amount was set to ensure that Argus's targeted return would be met in a predetermined period of time as opposed to having been set based on the specified percentage of Oakshire's sales"

It has already been demonstrated, above, that the fixed payment was to be ACH-debited by plaintiff regardless of any receipts, and not as a percentage of any receipts.

E. "the agreement allowed Argus, in its sole discretion, to continue making daily payment withdrawals even if the daily payment amount exceeded Oakshire's sales, thereby providing Argus with a means to compel an event of "default" upon which it could then immediately accelerate the entire debt".

It has already been demonstrated, above, that the fixed payment was to be ACH-debited by plaintiff regardless of any receipts at all, and not as a percentage of any receipts, providing plaintiff with a means to compel a default upon which it could immediately accelerate the entire debt.

72. For the reasons outlined in this answer, the transaction was criminally usurious, the interest rate being above the maximum legal threshold of 25%.

73. The idea that a reconciliation provision creates risk that precludes usury is absurd. The initial interest far exceeded the 25% interest rate above which the Legislature has determined a loan is criminally usurious. By stating that an interest rate above 25% is criminally usurious, the Legislature believed that any higher rate was utterly unaffordable and took criminal advantage of a borrower. Therefore if receipts stayed exactly the same, the funding was already deemed utterly unaffordable. The idea that such

a borrower could be faulted for not seeking a reconciliation if receipts plummeted even further endorses the criminally usurious funding. Criminal usury has been rebuked by the Court of Appeals in the strongest possible terms. Adar Bays, LLC v. GeneSYS ID, Inc., 37 NY3d 320 [2021].

74. The interest rate was ridiculously higher than the 25% legal limit.

75. Crystal Springs Capital v Big Thicket Coin, 220 AD3d 745, 747, 748 [2023] held that criminal usury was demonstrated by "in the event of the [ ] defendants' default by changing their payment processing arrangements or declaring bankruptcy."

76. The plaintiff's contract prohibited any change of the payment processing arrangements.

77. The plaintiff's contract effectively made bankruptcy a default (above).

78. Crystal Springs Capital v Big Thicket Coin, 220 AD3d 745, 747, 748 [2023] found that the agreement was a criminally usurious loan because "the plaintiff was "under no obligation" to reconcile the payments to a percentage amount of the [ ] defendants' sales rather than the fixed daily amount".

79. Here, while the contract did not expressly state that plaintiff was "under no obligation" to provide a reconciliation, the contract effectively permitted plaintiff to avoid any reconciliation.

80. Nothing in the plaintiff's contract enabled defendants to stop the fixed daily or weekly payment without being in default, nor did anything in plaintiff's contract force plaintiff to stop its ACH-debit of the fixed daily or weekly payment.

81. Nothing in the contract avoided the fixed daily or weekly payment if defendants had no receipts.

82. The contract eliminated all risk (provisions quoted herein).

83. While the initial interest rate could have been theoretically reduced by a reconciliation, this would not negate the usury:

> Band Realty Co. v. North Brewster, Inc., 37 N.Y.2d 460 [1975] (quoting Feldman v Kings Highway Sav. Bank (278 App Div 589, 590, affd 303 NY 675) "[So] long as all payments on account of interest did not aggregate a sum greater than the aggregate of interest that could lawfully have been earned had the debt continued to the earliest maturity date, there would be no usury."); Canal v Munassar, 144 A.D.3d 1663 [2016]; Norstar Bank v. Pickard & Anderson, 140 A.D.2d 1002, [1988]; DeStaso v Bottiglieri, 25 Misc. 3d 1213(A), 2009 NY Slip Op 52082(U); Fremont Inv. & Loan v. Haley, 23 Misc. 3d 1138(A), 2009 NY Slip Op 51186(U).
>
> Canal v Munassar, 144 A.D.3d 1663, 1664 [2016]:
> In determining whether the interest charged exceeded the usury limit, courts must apply the traditional method for calculating the effective interest rate as set forth in *Band Realty Co. v North Brewster, Inc*. (37 NY2d 460, 462 [1975], *rearg denied* 37 NY2d 937 [1975]) (*see Oliveto*

Holdings, Inc. v Rattenni, 110 AD3d 969, 972 [2013]). According to that method, "[s]o long as all payments on account of interest did not aggregate a sum greater than the aggregate of interest that could lawfully have been earned had the debt continued to the earliest maturity date, there would be no usury" (*Band Realty Co.*, 37 NY2d at 464 [internal quotation marks omitted]).

Norstar Bank v. Pickard & Anderson, 140 A.D.2d 1002, [1988]: "[T]he bank contended that the variable rate of interest charged on the loan should be averaged over the term of the loan for the purpose of determining whether the interest rate was usurious. ***. Although there is a conflict in authority (see, Annotation, Usury in Connection with Loan Calling for Variable Interest Rate, 18 ALR4th 1068), we believe the better rule is that, in the case of a loan at a variable rate of interest, the interest charged should not be averaged over the term of the loan in determining whether a usurious rate has been charged [citations] * * * If defendants were compelled to average the rate of interest charged over the full term of the loan, they would not know whether a usurious rate was being charged until the end of the term. Thus, they would be compelled to make excessive interest payments for a substantial period and would not be able to seek relief from the usurious payments until the expiration of the loan. On the other hand, the bank could have readily avoided charging usurious interest on its loan by placing a cap on the charges for interest so that no payment would exceed the variable legal rate".

American Express Natl. Bank v. Ellis, 2023 NY Slip Op 51428(U), 2 That the initial interest rate of 0% is legal under GOL § 5-501 would not save the agreement, given the contemplated increase to rates that exceed New York's 16% cap.1 (*See Fremont Inv. & Loan v Haley*, 23 Misc. 3d 1138[A], 889 N.Y.S.2d 505, 2009 NY Slip Op 51186[U], at *7 [Sup Ct, Queens County 2009]; *accord Norstar Bank v Pickard & Anderson*, 140 AD2d 1002, 1002-1003, 529 N.Y.S.2d 667 [4th Dept 1988] [holding that "in the case of a loan at a variable rate of interest, the interest charged should not be averaged over the term of the loan in determining whether a usurious rate has been charged"].)

84. The above and foregoing has reasonably placed the plaintiff on notice of the defense of criminal usury.

Fourth Affirmative Defense: Opinion Granting Summary Judgment in Case Brought By Letitia James, New York State Attorney General, Requires Dismissal

85. Under People v. Richmond Capital Group LLC, 2023 NY Slip Op 50975(U), 3 (Andrew Borrok, J.) the plaintiff's MCA agreement was a predatory, illegal, criminally usurious loan, because [the plaintiff knew from the very beginning of the MCA transaction that the defendant was going to be in default of the agreement,

86. Here, plaintiff knew from the outset that defendants would be in default because the agreement forbade the individual defendant from earning a livelihood from the proceeds of the business:

> 1 * * * you will use the funded amount solely for working capital purposes in the operation of your business;
>
> A *** (i) Use of Proceeds for Business Purposes. Merchant agrees that it will use all proceeds funded by Purchaser solely for business purposes, namely for working capital or other bona fide use in the operation of its business, and not for any personal, consumer or household purposes.

87. People v. Richmond Capital Group LLC, 2023 NY Slip Op 50975(U), 3 (Andrew Borrok, J.), held that the reconciliation provision was "a total sham" because "[a]lthough the MCAs provided for mandatory reconciliation of the daily amounts collected with the amounts of accounts

receivable actually received" "the Borrowers were required to send bank statements to the Predatory Lenders".

88. Similarly, here, the plaintiff's MCA contract provided that, at all times, defendant was required to provide its bank statements to plaintiff:

> 2 *** You understand and agree that Purchaser shall have full read-only access to all Approved Accounts while this Agreement is in effect.
> 4 *** You will provide Purchaser and/or its authorized agents with all information, authorizations and passwords that are necessary for and/or Service Provider (as defined) to verify Merchant's receivables, receipts, and deposits.

Fifth Affirmative Defense: Violations Found in Action by the New York State Attorney General

89. Her Honor, Letitia James, Attorney General, filed an action against a host of merchant cash advance lenders on March 5, 2024, People v Yellowstone et al., Supreme Court, Albany County, Index No. 450750/2024, for $1.3B.

90. This action was based upon an investigation by the New York Attorney General and proves that none of the defenses recited in this answer were invented by defense counsel.

91. At paragraph 384 of her petition, Attorney General noted that the "Agreements also require full, immediate payment of the entire Payback Amount in the event of default—discarding altogether the notion of payments tied to the merchants' revenue." The same provision is in plaintiff's contract.

92. Plaintiff's contracts stated:

> 8 (c) Purchaser may withdraw funds from any of Merchants bank accounts, including any Approved Account, by ACH, up to an amount equal any Amount Sold, plus unpaid fees and charges under this Agreement, if any, and Purchaser's costs and expenses relating to this Agreement (including without limitation, all Costs of Collection).

93. This provision showed that plaintiff's right to defendant's money was unrelated to merchants' revenue.

94. The Attorney General stated in her petition, paragraph 210: "By Reconciling merchants' payments against a made-up, inflated Specified Percentage number that bore no relation to the Daily Amount actually negotiated by the Parties, Yellowstone, Delta bridge, and their Funders made it virtually impossible for merchants to qualify for any Reconciliation refund. As one merchant explained, "I cannot imagine that [my business] would have taken advantage of this reconciliation process, since reconciling [my business's] payments based on this 15% 'Specified Percentage' likely would have caused its payment amount not to decrease but to increase."

95. Here, the duplication of contracts doubled the Specified Percentage of each.

96. At paragraph 387 of her petition (NYSCEF Doc. No. 1), the Attorney General noted that "These secured interests give Respondents

priority status in the event of a merchant's bankruptcy, ensuring that they can still recover in full against the merchant's assets—even if the merchant has collected zero dollars in revenue".

97. The contract of plaintiff had a similar secured interest:

> 9. Sale of Receivables. (a) Security Interest. To evidence the purchase and sale of Receivables hereunder and to secure Mer chant's obligations to remit the Periodic Amount until the Amount Sold is received by Purchaser out of Receivables, Merchant and Guarantor hereby grant to Purchaser, in the nameof Purchaser or its duly authorized representative, a first priority, continuing security interest (unless a third-party lien has been consented to by Purchaser in writing prior to the Effective Date) in and to: (i) the Receivables of Merchant (or any person or entity whose accounts are included in Receivables) up to the Amount Sold; (ii) all equipment and inventory as those terms are defined in Article 9 of the UCC, as amended, whether now or hereafter owned or acquired by Merchant (and/or any subsidiary or other person or entity whose accounts are included in Receivables) and wherever located; (iii) all "proceeds" of such property described in clause fi) and/or clause (ii), as that term is defined in Article 9 of the UCC;

98. The Attorney General noted that a reconciliation was blocked, under the same provision as here: Petition page 91, paragraph 262 and 263:

> "262*** Reconciliation was not available at all to merchants whose declining revenues left insufficient funds in their bank accounts to accommodate debits of the Daily Amounts *** 263. Respondents accomplished this through contractual language barring merchants from Reconciliation if the merchant was "in default" of its Agreement, and by deeming a "default" to include four bounced payments.

99. Here, any reconciliation was blocked by any alleged default:

> 5 *** Company may decline a reconciliation request where a documented Material Breach by Merchant, as specified in Section 7, is in effect.

Sixth Affirmative Defense: Arbitration

100. The plaintiff's contract had an arbitration clause.

> (e) Arbitration. Except as expressly otherwise provided herein, each party agrees to confidential arbitration of ali disputes and claims arising out of or relating to this Agreement, including issues relating to the arbitrability of any dispute or claim (collectively, "claims"). If a party seeks to have a dispute settled by arbitration, that party must first send to the other party, by certified mail, a written Notice of Intent to Arbitrate (the "Notice"). If the parties do not reach an agreement to resolve the claim within thirty (30) days after the Notice is received, Purchaser and Merchant agree that the claim will be resolved by a final and binding arbitration proceeding with JAMS, Inc. ("JAMS") in New York County, State of New York, under the Optional Expedited Arbitration Procedures then in effect.

101. Defendants reserve the right to demand arbitration. De Sapio v. Kohlmeyer, 35 N.Y.2d 402, 405-406 [1974]: "[A] defendant's right to compel arbitration, and the concomitant right to stay an action, does not remain absolute regardless of the degree of his participation in the action. (Matter of Zimmerman v. Cohen, 236 N. Y. 15.) *** On the other hand, interposing an answer of itself does not work to waive a defendant's right to a stay. (Matter of Hosiery Mfrs. Corp. v. Goldston, 238 N. Y. 22, 27.) *** Of course, the

existence of an arbitration agreement is not a defense. (American Reserve Ins. Co. v. China Ins. Co., 297 N. Y. 322, 327; Aschkenasy v. Teichman, 12 A D 2d 904.)"

Seventh Affirmative Defense. Lack of Subject Matter Jurisdiction.

102. The plaintiff was formed in a state other than New York. The business defendant was formed in a state other than New York and was never registered or authorized to do business in New York. No party is a resident of New York. The parties' transaction was for less than $1,000,000. The object of the action does not affect the title of real property in New York.

103. Under Business Corporation Law §1314(b), the court lacks subject matter jurisdiction. Parkview Advance LLC v High Purity, 2023 NY Slip Op 32976(U); Pearl Beta Funding, LLC v Elegant, 2023 NY Slip Op 31936(U); Harper Advance LLC v Reynolds, 2023 NY Slip Op 31191(U).

104. Techo-TM, LLC v Fireaway, Inc., 123 A.D.3d 610 [2014], where the First Department dismissed for lack of subject matter jurisdiction an action by a limited liability company, confirmed that any type of forum selection clause could not confer subject matter jurisdiction: "However, while New York recognizes consent as a basis for personal jurisdiction (see CPLR 301 and Vincent C. Alexander, Practice Commentaries, McKinney's Cons Laws of NY, Book 7B, CPLR 301:1), it does not recognize consent as a basis for

long-arm jurisdiction (see Graham v New York City Hous. Auth., 224 AD2d 248 [1st Dept 1996]).”

105. Techo-TM, though a First Department opinion, is binding on all trial courts in New York, there being no contrary appellate division opinion from any other department. Mountain View Coach Lines, Inc. v. Storms, 102 A.D.2d 663, 665, Second Department. [1984].

106. Actions required to be dismissed under BCL §1314(b) are routinely dismissed against the foreign entity defendant as well as the individual defendant. Mobile Programming LLC v. Tallapureddy, 2021 NY Slip Op 50411(U); Pearl Beta Funding, LLC v Eleant, 2023 NY Slip Op 31936(U); Harper Advance, LLC v Reynolds, 2023 NY Slip Op 31191(U); Parkview Advance, LLC v High Purity, 2023 NY Slip Op 32976(U); Fox Capital Group Corp. v Tomassetti, Sup. Ct., Kings Cty. Index No. 523737/2021 (NYSCEF Doc. No. 60, Dec. 23, 2022).

107. The exception to BCL §1314(b) is if the transaction arose in New York. The test for this was established by Kapitus Servicing, Inc. v Point Blank Constr., Inc., 221 A.D.3d 532 [2023]:

> “We agree with Supreme Court's finding that it had subject matter jurisdiction over the action, but on grounds different from those that the court stated. An action against a foreign corporation may be maintained "where it is brought to recover damages for a breach of contract made within New York State" (Business Corporation Law §

> 1314[b][1]). Here, the agreement was made in New York. As this Court has held, the "place of making of [a] contract is established when the last act necessary for its formulation is done, and at the place where that final act is done" (Fremay, Inc. v Modern Plastic Mach. Corp., 15 AD2d 235, 237 [1st Dept 1961] [internal quotation marks omitted]). According to the affidavit of plaintiff's vice president, plaintiff performed the last necessary act in New York by sending funds to Point Blank's Florida bank account; the sending of those funds, not Point Blank's passive receipt of them in Florida, was the last act necessary for formulation of the agreement."

108. If plaintiff's funding was wired to defendant from a bank outside of New York there is no subject matter jurisdiction.

Eighth Affirmative Defense: Unconscionability/Adhesion Contract

109. By the very nature of their transaction, as more fully set forth below, the parties had completely unequal bargaining power, defendants were not in the least "sophisticated," and any review of plaintiff's contract by any counsel for defendants was known to be incongruous with the parties' transaction.

110. The parties' transaction was the very antithesis of two sophisticated parties hammering out the terms of a contract through experienced counsel.

111. Under the circumstances, as more fully set forth below, unconscionability and adhesion contract is an available defense, notwithstanding that the one-person business defendant was filed as a

business entity. Gillman v Chase Manhattan, 135 A.D.2d 488, 491, Second Dept. [1987]:

> "[T]he doctrine of unconscionability has little applicability in the commercial setting because it is presumed that businessmen deal at arm's length with relative equality of bargaining power [string cite]. Apparently, the doctrine is primarily a means with which to protect the `commercially illiterate consumer beguiled into a grossly unfair bargain by a deceptive vendor or finance company' [citation]."
>
> Delphi-Delco Elecs. Sys. v. M/V Nedlloyd Europa, 324 F. Supp. 2d 403, 414, S.D.N.Y. [2004]:
>
> "Allied Chemical Intern. Corp. v. Companhia de Navegacao Lloyd Brasileiro, 775 F.2d 476, 482 (2d Cir. 1985) ("We bear in mind that bills of lading are contracts of adhesion and, as such, are strictly construed against the carrier.")."

112. Plaintiff advertised its funding/loan as being immediate funding/loan available in 24 hours.

113. Plaintiff knew that its borrowers came to it for immediate funding available in 24 hours/

114. Plaintiff knew that there was neither time, opportunity, nor ability to review the fine print of the documents that it submitted for DocuSigning by defendants for emailing to plaintiff and that the transaction was designed for no review of plaintiff's contract. *Cf*., Empery Asset Master, Ltd. v. AIT Therapeutics, Inc., 197 A.D.3d 1064, 1065 [2021]:

> "We cannot conclude, as a matter of law, that a reasonable person reviewing a 20-page warrant and a 42-plus-page Securities Purchase and Registration Rights Agreement would have realized that the word "sentence" (in "immediately preceding sentence") should have been "sentences." "

115. Plaintiff's lengthy contract is pre-printed in fine print and not available for negotiation by borrowers like defendant.

116. Plaintiff knew but failed to inform defendants of provisions of the agreement known by plaintiff to be intended and used by plaintiff to the detriment of defendants, such as:

- The exorbitant interest rate.
- That plaintiff would not routinely lower the interest rate after the first set of payments.
- The funding was unaffordable especially by a borrower needing instant cash financing.
- The fixed daily payment or fixed weekly payment was immutable with no way of defendants to avoid it and with no ability to obtain any immediate relief from the fixed payments.
- a secured interest provision under which plaintiff would and could send UCC lien notices to defendant's customers to cut off payments to defendant and disable defendant from any

further business with such customer with such UCC lien notices demanding inflated unjustified amounts.

- inclusion of additional guarantors other than the individual defendant.
- a reconciliation provision, never actually employed by plaintiff, but used by plaintiff to confuse a court into believing that its loan was an investment.
- the fact that plaintiff would not accord with the underlying assumption of defendants that plaintiff was *loaning monies* but that the transaction would be claimed by plaintiff not to be a loan at all but to be a purchase and sale in order to justify the criminally usurious rate of interest.
- a forum selection clause under which the defendants would be sued in New York in any random county.

117. There is no term in plaintiff's contract that should shield it from the defense of unconscionability of adhesion contract. *Cf.*, Danann Realty Corp. v. Harris, 5 N Y 2d 317 [1959].

118. The foregoing has reasonably placed the plaintiff on notice of the defense of unconscionability and adhesion contract.

Ninth Affirmative Defense: Unenforceable Default Fee

119. Plaintiff has no right to any default fee. Rubin v. Napoli Bern Ripka Shkolnik, LLP, 179 AD3d 495 [2020]:

> "Although the party challenging the liquidated damages provision has the burden to prove that the liquidated damages are, in fact, an unenforceable penalty (see JMD Holding Corp. v Congress Fin. Corp., 4 NY3d 373, 380 [2005]; Parker v Parker, 163 AD3d 405, 406 [1st Dept 2018]), the party seeking to enforce the provision must necessarily have been damaged in order for the provision to apply (see e.g. J. Weinstein & Sons, Inc. v City of New York, 264 App Div 398, 400 [1st Dept 1942]."

Trustees of Columbia Univ. in the City of N.Y. v D'Agostino Supermarkets, Inc., 36 N.Y.3d 69, 73, 74-77 [2020]:

> "(W)here the breach of contract was a failure to pay money, plaintiff should be limited to a recovery of the contract amounts plus appropriate interest] [citation omitted]; Cotheal v Talmage, 9 NY 551, 554, Seld. Notes 238 [1854] ["Where there is a contract to pay money, the damages for its breach are fixed and liquidated by law, and require no liquidation by the parties"]; 36 NY Jur 2d, Damages § 173 [stating that liquidated damages clauses in contracts for the payment of money are typically inappropriate because "for the nonpayment of money, the law awards interest as damages"]).

WHEREFORE, defendants respectfully demand judgment dismissing the complaint.

Dated: September 16, 2024

Amos Weinberg
Attorney for Defendants

Office and P.O. Address:
49 Somerset Drive South
Great Neck NY 11020-1821
Phone: (516) 829-3900.
Email: amos@AmosLegal.com

VERIFICATION: State of New York, County of Nassau, ss.: The undersigned attorney for defendants, duly admitted to practice in the courts of the State of New York, affirms under penalties of perjury: that he has read the foregoing answer, and knows the contents thereof; that it is true upon information and belief and I believe it to be true. This verification is made by me because defendants are not in the county where I have my office. The source of my information is privileged emails and discussions with the individual defendant and review of plaintiff's documents.

Dated: September 16, 2024

Amos Weinberg