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NEW YORK COURT HOLDS RECEIVABLES SALES ARE NOT USURIOUS LOANS

A New York court recently held that receivables sales were not loans subject to New York usury limitations in two separate cases.

Merchant Cash & Capital v. G&E Asian American Enterprise

In *Merchant Cash & Capital v. G&E Asian American Enterprise*, No. 605800-15 (N.Y. Sup. Ct. Aug. 2, 2016), Merchant Cash & Capital (MCC) allegedly purchased receivables from a corporation at a discount in exchange for a percentage of the corporation's daily business receipts until the entire amount of the purchased receivables were collected. The corporation's obligations were guaranteed by two individuals. Within 10 days of receiving the purchase price, the corporation terminated MCC's ability to withdraw the daily collection from the corporation's bank account. MCC sued claiming that the corporation defaulted on the contract and that the individuals breached their guarantees. After the defendants failed to appear, a default judgment was entered against the defendants.

The defendants moved to have the default judgment vacated on grounds that the agreement constituted a usurious and unenforceable loan. The Supreme Court for Nassau County disagreed. The court concluded that the agreement under consideration did not provide for a loan of money that was subject to New York's 25% criminal usury cap because MCC was entitled to payments based upon a percentage of daily receipts and thus took a risk that there could be no daily receipts. The defendants also took the risk that if the receipts were substantially greater than anticipated, repayment of the obligation could occur over an abbreviated period, with the sum over and above the amount advanced being more than 25%. The court declined to convert the agreement to a loan because to do so would require unwarranted speculation and would contradict the terms of the sale of future receivables in accordance with the agreement of the parties. In support of its holding, the court cited a decision in which the United States District Court for the Southern District of New York agreed with a federal magistrate that a similar transaction between MCC and another business was not a loan and thus not subject to New York usury laws. *Merchant Cash & Capital v. Edgewood Group*, No. 14 Cv. 3497 (JGK)(DCF), 2015 WL 4451057 (S.D.N.Y. July 20, 2015). When analyzing that transaction, the magistrate stated that although the transaction looked like a loan, the magistrate could not conclude as a matter of law that the

transaction was in fact a loan based on the contractual language and the fact that the defendant's waived their affirmative usury defense by failing to appear and defend the action.

Platinum Rapid Funding Group v. VIP Limousine Services

In *Platinum Rapid Funding Group v. VIP Limousine Services*, No. 604163-15 (N.Y. Sup. Ct. July 10, 2016), Platinum Rapid Funding Group, Inc. (PRFG) allegedly agreed to purchase future receivables from a corporation at a discount. After the corporation paid a certain amount of funds arising from the future receivables to PRFG, the corporation terminated PRFG's ability to electronically withdraw funds from the corporation's bank account. PRFG sued the corporation for breach of contract and breach of the representations and warranties in the parties' agreement. PRFG also sued an individual guarantor for breaching his personal guarantee in connection with the agreement. In response to the complaint, the defendants raised certain affirmative defenses, including a defense that PRFG committed civil and criminal usury.

PRFG filed a motion to dismiss the defendants' affirmative usury defense, which the Supreme Court for Nassau County granted for the following reasons. First, the court determined that under New York law, a corporation and an individual guarantor of a corporation's obligations are prohibited from asserting the defense of civil usury. Second, the court determined that the defendants failed to adequately allege a violation of New York's 25% criminal usury cap because usury laws are applicable only to loans or forbearances and the transaction under consideration was not a loan. According to the court, the transaction was not a loan because the agreement provided for the sale of future receivables with repayment based on a percentage of daily receipts over an indeterminate period, thus exposing PRFG to a risk of loss in the event there were no daily receipts. For these reasons, the court declined to conclude that the parties' agreement provided for a loan.

The above cases provide comfort to receivables purchasers operating under New York law. Of course, these cases would not be binding precedent with respect to transactions that are subject to the laws of other states. Consequently, receivables purchasers that operate under the laws of other states should be mindful of other relevant case law and be prepared to make program modifications to the extent required. □

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