STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

NEWPORT, SC. **SUPERIOR COURT**

(FILED: May 29, 2013)

EMOND PLUMBING AND HEATING INC.; TECTA AMERICA NEW ENGLAND, LLC, Plaintiffs	:	
v.	:	**C.A. No. NB 2011-0569**
BANKNEWPORT, Defendant	:	

DECISION

STERN, J. Before this Court for decision are cross-motions for summary judgment filed by Plaintiffs Emond Plumbing and Heating Inc. (Emond) and Tecta America New England, LLC (Tecta) (collectively Plaintiffs), and Defendant BankNewport (Bank). Plaintiffs individually brought unjust enrichment claims against Bank. Bank now seeks summary judgment against Plaintiffs' claims I and II. Conversely, Plaintiffs ask this Court to deny summary judgment and grant their own motion for summary judgment on Counts I and II. This Court has reviewed the evidence and the applicable law, together with the parties' legal memoranda and oral arguments, and now issues this written Decision.

I

Facts and Travel

In May 2010, AIDG Properties, LLC (AIDG), a real estate holding company, purchased an office and industrial building located at 184 John Clarke Road in Middletown for $4,300,000. See Pls.' Ex. K at 1. Anjan Dutta-Gupta (Dutta-Gupta), AIDG's main decision-maker, was also

the principal for Advanced Solutions For Tomorrow, Inc. (ASFT), a defense contractor. Dutta-Gupta decided to use the building as a headquarter and administrative office for ASFT. See McNamara Aff. at 6-7. Bank financed this purchase with two loans in the total original amount of $4,500,000. The first loan was in the amount of $2,516,000; the second loan was for $1,984,000. The second loan was to provide proceeds for necessary construction improvements estimated to cost $675,000. See Pls.' Ex. A. After closing, AIDG re-assessed the condition of the building and determined that an increase in the construction budget was necessary in order to replace the mechanical systems, an undertaking estimated to cost $400,000, as well as a complete roof replacement, estimated to cost $357,000. Id. Bank agreed to increase its funding to provide for the new construction budget totaling $927,800. Id. On October 6, 2010, a loan modification was executed, bringing both notes to $4,727,520. McNamara Aff. at 10. Replacement of the mechanical systems and roof were critical improvements and were to be concluded before the building could be reasonably used; therefore, they were scheduled first in the improvement process. Payment for these improvements was to be made in a similar manner as an ordinary construction loan. The improvements were to be completed by February 2011, whereupon the whole of the second loan would be converted to permanent financing through facilities offered by the Small Business Administration. See Pls.' Ex. A; Pls.' Ex. V at 20-25, Pls.' Ex. G.

AIDG engaged ABC Building Corp. (ABC) to serve as general contractor for the first phase of improvements, including HVAC and roof work. AIDG and ABC opened a competitive bidding process and solicited interested subcontractors. Pls.' Ex. T at 15, 17. Emond was the lowest bidder for HVAC work. The agreed upon compensation for Emond's work was

originally $400,000. This contract was later increased by change orders by $13,428.21, bringing the total compensation for the HVAC improvements to $413,428.21. Pls.' Ex. B.

Tecta won the bid for the roof replacement contract. The original price for the roof replacement was $206,570. There was a change order in the amount of $480, bringing the total compensation for the roof replacement to $207,230. Pls.' Ex. C.

On or about September 1, 2010, work began. Both Emond and Tecta submitted monthly payment applications to ABC with statements of the work completed. ABC, in turn, forwarded to AIDG a monthly consolidated payment application reflecting all work. AIDG submitted this paperwork to Bank for its review, inspection of the completed work and the approval of construction loan disbursements. Pls.' Ex. U at 60-62. Bank engaged its own inspector who confirmed that all work set forth in each payment application had actually been completed before Bank disbursed the funds to AIDG, so AIDG could compensate the subcontractors for their efforts. Id. at 60-61. This process would normally take 30 days. Pls.' Ex. U at 60-63; Pls.' Ex. D. The subcontractors submitted the following payment applications:

Emond, Pls.' Ex. E.:

Application #:	**Date:**	**Amount:**
1	09/30/2010	$ 28,440.00
2	10/31/2010	$ 76,728.03
3	11/30/2010	$ 155,572.77
4	12/31/2010	$ 35,473.50
5	01/31/2011	$ 73,486.09
6	02/01/2011	$ 2,385.00
7	02/01/2011	$ 41,342.82
	Total:	**$ 413,428.21**

Tecta, Pls.' Ex. H.:

Application #:	**Date:**	**Amount:**
1	10/31/2010	$ 11,191.50
2	11/30/2010	$ 138,996.00
3	12/31/2010	$ 35,887.50
4	02/22/2011	$ 432.00
	Total:	**$ 186,507.00**

Emond was paid a total amount of $94,668.02. See Pls.' Exs. F, Y. Tecta, meanwhile, received only $11,191.50. See Pls.' Ex. I. The transmission of the November pay applications were delayed until the time of the December pay applications. See Pls.' Ex. U at 63-64, 66-67. Both these applications were sent to Bank at the same time later in the year. See Pls.' Ex. J. At that time, Emond was owed the total amount of $191,046.27 for payment applications 3 and 4; while Tecta was owed $174,883.50 for payment applications 2 and 3.[1] See Pls.' Exs. E, H, J. Emond and Tecta substantially completed their remaining work on the project in January 2011. See Pls.' Ex. T at 25-33; Pls.' Ex. U at 71.

Bank's inspector confirmed that all work noted in the subcontractor's November and December payment applications was complete and Bank disbursed $497,327.66 in loan proceeds to pay for the completed work. On February 4, 2011, Bank deposited construction loan proceeds in the amount of $497,327.66 into AIDG's account. Pls.' Ex. D at 2. Shortly after the deposit was made, Bank learned that Dutta-Gupta was arrested on allegations of bribing a government official with certain contracts between ASFT and the U.S. Navy. Pls.' Ex. K at 1. Subsequently, ASFT laid off all its employees and was closed. On February 8, 2011, Bank reversed the disbursement made on February 4. Bank declared AIDG in default and review and inspection of

[1] Emond also was owed $10,500 from payment application 2 which was not fully paid.

January and subsequent pay applications were cancelled. See Pls.' Ex. U at 71, 76. Bank obtained court approval to take control of the real property. Pls.' Ex. V at 65. At this point, having received no payment since the October pay application, Emond was owed $318,760.19 for work and material; while Tecta was owed $196, 038.50. See Pls.' Exs. F, I, X, Y.

The two subcontractors commenced mechanic's lien proceedings which were stayed when AIDG filed for bankruptcy.

On July 18 and July 29, 2011, respectively, Bank obtained permission from the Bankruptcy Court and the Rhode Island Superior Court to foreclose on the property. Bank refused demands to release the undistributed loan proceeds and refused to allow Emond to retrieve its installed rooftop HVAC units. On September 15, 2011, Emond notified Bank of its equitable lien claims against any foreclosure proceeds. See Pls.' Ex. N.

On September 16, 2011, Bank submitted a bid of $1 million, foreclosing only on the outstanding second mortgage. Pls.' Ex. V at 89. Bank acquired title subject only to its own first mortgage. Subsequently, Bank closed out and set off its loans to AIDG. Id. at 87-89. Bank plans to use the former AIDG building as its own new headquarters.

On November 15, 2011, Plaintiffs filed the Complaint in Docket Number C.A. NC11-569 against Bank. On December 12, 2011, Bank filed an Answer. On September 17, 2012, Bank filed a Motion for Summary Judgment, followed by Plaintiffs' Cross-Motion for Summary Judgment on October 24, 2012. The matter was placed on the business calendar on September 19, 2012. This Court heard oral argument on December 4, 2012.

II

Standard of Review

Summary judgment is proper when "no genuine issue of material fact is evident from the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, and the motion justice finds that the moving party is entitled to prevail as a matter of law." Smiler v. Napolitano, 911 A.2d 1035, 1038 (R.I. 2006) (quoting Rule 56(c)). When considering a motion for summary judgment, this Court must draw '"all reasonable inferences in the light most favorable to the nonmoving party."' Hill v. Nat'l Grid, 11 A.3d 110, 113 (R.I. 2011) (quoting Fiorenzano v. Lima, 982 A.2d 585, 589 (R.I. 2009)). The burden lies on the nonmoving party to "prove the existence of a disputed issue of material fact by competent evidence," rather than resting on the pleadings or mere legal opinions and conclusions. Hill, 11 A.3d at 113. Where it is concluded '"that no genuine issue of material fact exists and that the moving party is entitled to judgment as a matter of law,'" summary judgment shall enter. Malinou v. Miriam Hosp., 24 A.3d 497, 508 (R.I. 2011) (quoting Poulin v. Custom Craft, Inc., 996 A.2d 654, 658 (R.I. 2010)). However, "if the record evinces a genuine issue of material fact, summary judgment is improper." Shelter Harbor Conservation Soc'y, Inc. v. Rogers, 21 A.3d 337, 343 (R.I. 2011) (citations omitted). Finally, '"[s]ummary judgment is an extreme remedy that should be applied cautiously.'" Hill, 11 A.3d at 113 (quoting Plainfield Pike Gas & Convenience, LLC v. 1889 Plainfield Pike Realty Corp., 994 A.2d 54, 57 (R.I. 2010)).

III

Analysis

1

Unjust Enrichment

"Recovery for unjust enrichment is predicated upon the equitable principle that one shall not be permitted to enrich himself at the expense of another by receiving property or benefits without making compensation for them." Narragansett Elec. Co. v. Carbone, 898 A.2d 87, 99 (R.I. 2006) (citing R & B Elec. Co. v. Amco Constr. Co., 471 A.2d 1351, 1355 (R.I. 1984)). To recover for unjust enrichment, the "plaintiff must prove three elements: that a benefit was conferred upon the defendant by the plaintiff; that the defendant appreciated this benefit; and that acceptance of this benefit by the defendant under the existing circumstances would be inequitable unless the defendant pays for the value of this benefit." Narragansett Elec. Co., 898 A.2d at 99 (quoting Bouchard v. Price, 694 A.2d 670, 673 (1997)). "[A] benefit is conferred when improvements are made to property, materials are furnished, or services are rendered without payment." Narragansett Elec. Co., 898 A.2d at 99. The second element—appreciation of the benefit conferred—is satisfied if the defendant profited from the benefit. See id. at 100. The third element—that retention of the benefit without payment would be inequitable—is the "most significant" of the three requirements and is satisfied "if the plaintiff can prove the reasonable value of services rendered without payment." Id. at 99 ((quoting R & B Elec. Co, 471 A.2d at 1356) (citing Best v. McAuslan, 27 R.I. 107, 60 A. 774, 774-75 (1905))).

Plaintiffs contend that all three elements of the doctrine have been fulfilled because 1) Plaintiffs' unpaid labor and materials furnished conferred a benefit on Bank; 2) Bank appreciated such a benefit by not paying for improvements on the building, improvements Bank had

approved of; and 3) Retention of the benefit by Bank would be unjust. In short, Plaintiffs argue that Bank received an un-bargained for windfall because it retains loan proceeds while contractors remain unpaid after performing their work.

In response, Bank argues that it has not received such a benefit and asks this Court to find that it has not been unjustly enriched for a variety of reasons. First, Bank submits that any benefit it received in this case was acquired by virtue of its status as a secured creditor and its participation in the liquidation of the property. Second, even though Bank disbursed the loan proceeds and subsequently set off the account, it argues that it was clearly allowed to set off the account based on its deposit agreement with AIDG. Third, Bank contends that Plaintiffs failed to oppose Bank's effort to foreclose its mortgage even though they were aware that such failure would have a detrimental effect on Plaintiffs' efforts to assert any mechanic liens. Finally, Bank avers that there will be a chilling effect on the standard practice of commercial and construction lending if this Court were to find unjust enrichment in this matter and furnished equitable relief by shielding Plaintiffs from losses brought forth under their business judgment.

A

Creditor priority hierarchy

Here, the main dispute is whether a creditor obtained a benefit. In this case, it is undisputed that Bank holds a perfected security interest in the collateral. However, it needs to be determined whether Bank can be held liable to unsecured creditors, via unjust enrichment, for the benefits given by the unsecured creditors that resulted in an increase of the collateral's value. This Court must decide whether the facts of this case should allow equitable principles, like unjust enrichment, to overcome the creditor priority system set forth in the Uniform Commercial Code (UCC). In commercial law, there exist three "priority principles" that can be summarized as

follows: (1) unsecured creditors share pro rata; (2) a later creditor enjoys priority over an earlier one only when the later alone is secured; and (3) an earlier secured creditor generally has priority over later creditors. Alan Schwartz & Robert E. Scott, Commercial Transactions: Principles and Policies 609 (2d ed. 1991). To quote our High Court: "In the world of debtors and creditors, first in time is often first in right." McFarland v. Brier, 850 A.2d 965, 973 (R.I. 2004).

Bank held a perfected security interest and both Emond and Tecta were unsecured creditors. Were this Court to find that these unsecured creditors conferred a benefit on the secured creditor by enhancing the collateral and subsequently grant a claim for unjust enrichment against the secured creditor, the result would amount to a loss of the secured creditor's priority status. This would translate into a substantial impairment of the effectiveness and reliability set forth by the UCC. A review of Rhode Island decisions provided no clear guidance on this issue. However, one federal case, although distinguishable in some respects, provides some direction.

In Ostroff v. F.D.I.C., 847 F. Supp. 270 (D.R.I. 1994), the United States District Court for the District of Rhode Island addressed the issue of unjust enrichment after a bank, which held a preexisting mortgage on property and which had issued a commitment letter approving one purchaser's mortgage loan request, foreclosed on assets to which purchasers had made improvements. In this case, the purchasers had spent approximately $100,000 renovating the property in anticipation of the transfer and had initiated a lien against the premises under the provision of the Rhode Island Mechanic's Lien Law. R.I. Gen. Laws § 34–28–1 *et seq*. Subsequently, the bank learned of an IRS tax lien against the premises and, due to issues with conveying clear title, the closing did not go forward. A foreclosure sale took place and the bank purchased the premises. The purchasers brought an action in Rhode Island state court against the bank, which subsequently became insolvent. The FDIC was appointed and accepted as Receiver

and Liquidating Agent of the failed financial institution and removed the action to the District Court. The Court in Ostroff did not find that the bank had been unjustly enriched. It noted that the bank, as a secured creditor, had justifiably foreclosed on its collateral and emphasized the priority hierarchy that places secured creditors before unsecured creditors. Ostroff, 847 F. Supp. at 277. Like the bank in Ostroff, Bank was justified in foreclosing on AIDG's assets. AIDG was in default on the loans and Bank foreclosed on its collateral. Similarly, removing the secured creditor's priority by requiring it to pay the unsecured parties would render Bank's position as a secured creditor meaningless. Id. at 277. Also, both unsecured creditors could have taken measures to protect themselves against the eventuality of losing the value of the enhancements they added to the property.

While some courts have held that a claim of unjust enrichment should succeed when the secured party had a hand in bringing about the unjust enrichment or where the lender was aware of a general contractor's financial difficulties and did not inform subcontractors of these issues, however, this is not the case here.[2] Conversely, while Bank did send an investigator to ensure that work was completed as stated, it was not involved in hiring or directing the subcontractors. There was also no sign of AIDG going into default until Dutta-Gupta was arrested, so Bank did not neglect to inform the subcontractors of any potential financial difficulties. This Court is not

[2] See Ninth Dist. Prod. Credit Assoc. v. Ed Duggan, Inc.,821 P.2d 788, (Colo. 1991) (holding that because a secured creditor was "involved in the transaction by which the unsecured creditor supplied goods or services that enhanced the value of the secured collateral," trial court erred by failing to give jury instructions on unjust enrichment); see also Metric Constructors Inc. v. Bank of Tokyo-Mitsubishi Ltd., 72 Fed. Appx. 916 (4th Cir. 2003) (granting a claim of unjust enrichment against lender where lender was on notice regarding owner's financial problems and previous defaults on other projects and failed to notify plaintiff of these concerns).

inclined to follow the generous interpretations of equity set forth by the Colorado Supreme Court in Duggan and undermine the hierarchy of priorities set forth by the UCC.

B

Setoff

Furthermore, Bank did approve the final construction loan payment and transferred the funds into AIDG's account so AIDG could use these funds to compensate the subcontractors. In spite of this, AIDG never ensured that the funds reached the subcontractors.

Bank's subsequent setoff of the funds transferred to cover the final construction loan payment is not an issue. "'In Rhode Island, the rights and obligations of a bank and its depositors in regard to funds on deposit are governed by the terms of the contract entered into at the time the relationship is established."' Couture v. Pawtucket Credit Union, 765 A.2d 831, 834 (R.I. 2001) (quoting Paradis v. Greater Providence Deposit Corp., 651 A.2d 738, 740 (R.I. 1994)). Bank had contractual setoff rights without prior notice for any amounts AIDG owed to Bank as indicated in Bank's Deposit Agreement. See Ex. 21 and Ex. 10 section 9.2.1. There is no indication that AIDG's representatives did not give meaningful consent to the terms of this contract. Our Supreme Court has further stated that "[u]nder established contract law principles, when there is an unambiguous contract and no proof of duress or the like, the terms of the contract are to be applied as written." Gorman v. Gorman, 883 A.2d 732, 739 n.11 (R.I. 2005). This Court finds that Bank was within its contractual rights to set off the transferred funds.

C

Foreclosure

Finally, this Court is not convinced that Bank was unjustly enriched by purchasing the premises at foreclosure. It submitted a bid and became the winning bidder on the premises, which included the improvements made. Any other party could have submitted a bid larger than Bank's. Plaintiffs could have attempted to bid on the premises themselves. However, they did not.

IV

Conclusion

For the aforementioned reasons, this Court finds as a matter of law that Bank did not receive a benefit it was not entitled to by virtue of its status as secured creditor. Also, this Court finds as a matter of law that Bank was not unjustly enriched by any improvements the Plaintiffs made to the premises when it purchased these at foreclosure. Accordingly, this Court grants Defendant's motion for summary judgment on Counts I and II of the Complaint and denies Plaintiffs' cross-motion for summary judgment.

The parties shall present an appropriate order and judgment for entry.

RHODE ISLAND SUPERIOR COURT

Decision Addendum Sheet

TITLE OF CASE:	Emond Plumbing and Heating, Inc., et al. v. BankNewport
CASE NO:	NB 2011-0569
COURT:	Newport County Superior Court
DATE DECISION FILED:	May 29, 2013
JUSTICE/MAGISTRATE:	Stern, J.

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