IN THE COURT OF COMMON PLEAS OF PHILADELPHIA COUNTY

FIRST JUDICIAL DISTRICT OF PENNSYLVANIA

CIVIL TRIAL DIVISION

USCLAIMS, INC. and USCLAIMS OF AMERICA, INC.	:	
Plaintiffs,	:	SEPTEMBER TERM, 2007
	:	
v.	:	No. 2629
	:	
MICHAEL FLOMENHAFT, ESQUIRE,	:	
FLOMENHAFT & CANNATA, LLP,	:	(Commerce Program)
STILLWATER ASSET-BACKED FUND,	:	
LP, THE OXBRIDGE GROUP, LLC, and	:	Control No. 102349
BRIAN SPIRA	:	
Defendants.	:	

O R D E R

AND NOW, this 14th day of May 2008, upon consideration of the Motion for Partial Judgment on the Pleadings of defendants (Stillwater Asset-Backed Fund, LP, The Oxbridge Group, LLC, and Brian Spira) the response in opposition, all other matters of record, and in accord with the Opinion being contemporaneously filed, it is **ORDERED** that the Motion is **DENIED**.

BY THE COURT:

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ALBERT W. SHEPPARD, JR., J.

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<u>O P I N I O N</u>

Albert W. Sheppard, Jr., J. ……………………………………………… May 14, 2008

Presently before the court is the Motion for Partial Judgment on the Pleadings of defendants (Stillwater Asset-Backed Fund, LP, The Oxbridge Group, LLC, and Brian Spira). For the reasons discussed, the Motion is denied.

BACKGROUND

Plaintiffs, USClaims, Inc. and USClaims of America ("plaintiffs"), allege that from November 2001 to July 2003, they entered into a series of purchase agreements ("Purchase Agreements" or "Flomenhaft Purchase Agreements") with defendants, Michael Flomenhaft, Esquire and Flomenhaft & Cannata, LLP (the "Law Firm Defendants"). Pursuant to these agreements the Law Firm Defendants sold and assigned to plaintiffs their interests in future attorneys' fees that they would earn in various personal injury claims. Specifically, each Purchase Agreement set forth a list of claimants who had retained the Law Firm Defendants in their personal injury matters. The Purchase Agreements recited that the Law Firm Defendants had entered into fee agreements with each claimant on the attached list pursuant to which the Law Firm Defendants' fees were based on a percentage of the claimants' recovery. The Purchase Agreements further stated that the Law Firm Defendants were selling to plaintiffs an "interest" in the fees (the "Flomenhaft Interests"). The amount of this "interest" was to vary, depending on the date of payment by the Law Firm Defendants to plaintiffs and whether plaintiffs incurred any costs and expenses in enforcing their rights under the Purchase Agreements. In addition, under the terms of the Purchase Agreements, plaintiffs were entitled to one hundred percent (100%) of the Law Firm Defendants' fees from the proceeds of each named claimants' case until the aggregate amount received by the plaintiffs equaled their interest, as quantified in the Purchase Agreements.[1]

The Purchase Agreements further provided that if any of the claimants hired new counsel or if a claim resulted in no recovery, the Law Firm Defendants were required to transfer to plaintiffs "makeup fees" from other claims in an amount at least equal to the estimated fees for any such claim for which no fee was payable.[2] The Law Firm Defendants also represented that they would not sell, transfer, assign, and/or convey the fees in the future.[3] Further, the Law Firm Defendants promised that they would not allow

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[1] See Third Amended Complaint, at Exh., A, § 1(d).
[2] Id. at § 5.
[3] Id. at § 3(c).

any other party to take funds away from the fees and would not sell any rights in the fees.[4]

In their Third Amended Complaint, plaintiffs allege that defendant Brian Spira ("Spira") served as plaintiffs' Vice-President of Business Development and Finance from June 2001 to March 2004.[5] In this capacity, Spira was responsible for procuring, representing, and protecting plaintiffs' interests in the Flomenhaft Purchase Agreements, and thus, was intimately aware of the provisions of and the parties' rights and obligations under the Flomenhaft Purchase Agreements.[6]

In March 2004, Spira left his position with plaintiffs and began to work for defendant Oxbridge Group, LLC ("Oxbridge").[7] Subsequently, the Law Firm Defendants allegedly sold and assigned the Flomenhaft Interests to defendant Stillwater. Specifically, it is alleged that Spira and Oxbridge (collectively, the "Broker Defendants") brokered the sale of the Flomenhaft Interests from the Law Firm Defendants to Stillwater despite their knowledge that the plaintiffs had already acquired the same interests in the attorneys' fees in the underlying personal injury claims.[8] The Third Amended Complaint states that Stillwater filed a UCC-1 Financing Statement in New York in January 2005, purporting to perfect a security interest in the Flomenhaft Interests that had previously been sold to plaintiffs.[9] No such financing statements were ever filed by plaintiffs with respect to any of the Purchase Agreements. Plaintiffs assert that the sum of

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[4] Id. at § 4a.
[5] See Third Amended Complaint, at ¶ 18.
[6] Id. at ¶ 22.
[7] Id. at ¶ 26.
[8] Id. at ¶¶ 27, 29.
[9] Id. at ¶ 28.

$3,086,546.10, plus interest and attorneys' fees, is due and owing to them from the Law Firm Defendants.[10]

Plaintiffs have brought the following counts in their Third Amended Complaint: breach of contract against the Law Firm Defendants (Count I); conversion against all defendants (Count II); tortious interference against Stillwater and the Broker Defendants (Count III); breach of fiduciary duty against the Law Firm Defendants (Count IV); aiding and abetting against Stillwater and the Broker Defendants (Count V); declaratory relief against all defendants (Count VI); accounting against the Law Firm Defendants (Count VII); and specific performance and injunctive relief against all defendants (Count VIII). Defendants Stillwater, Oxbridge, and Spira subsequently filed Answers to plaintiffs' Third Amended Complaint on July 11, 2007.

This case was originally filed in the United States District Court for the Eastern District of Pennsylvania. In that court the Honorable Legrome D. Davis rendered three memoranda opinions in the case. Plaintiffs had asserted that federal jurisdiction was proper on the basis of the diversity of citizenship of the parties. However, it was later discovered that there was not complete diversity of citizenship between the parties and thus, federal jurisdiction was lacking. As a result the three Judge Davis opinions were void.

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[10] Id. at ¶ 42.

The parties stipulated to the dismissal of the action in federal court on September 18, 2007. Pursuant to 42 Pa.C.S.A. § 5103(b),[11] the case was transferred to this court on September 25, 2007. On October 25, 2007, defendants Stillwater, Oxbridge, and Spira filed the present motion for partial judgment on the pleadings, requesting that judgment be entered in their favor on Counts II, III, V, VI, and VIII of plaintiffs' Third Amended Complaint.

DISCUSSION

I. Legal Standard

Pa. R.C.P. 1034 provides that "[a]fter the relevant pleadings are closed, but within such time as not to unreasonably delay the trial, any party may move for judgment on the pleadings." A motion for judgment on the pleadings is similar to a demurrer. It may be entered where there are no disputed issues of fact and the moving party is entitled to judgment as a matter of law. In determining if there is a dispute as to facts, the court must confine its consideration to the pleadings and relevant documents.[12] Further, neither party may be deemed to have admitted conclusions of law.[13]

[11] 42 Pa.C.S.A. § 5103(b) ("Transfer of erroneously filed matters") provides, in relevant part: "(1)…Where a matter is filed in any United States court for a district embracing any part of this Commonwealth and the matter is dismissed by the United States court for lack of jurisdiction, any litigant in the matter filed may transfer the matter to a court or magisterial district of this Commonwealth by complying with the transfer provisions set forth in paragraph (2).
(2) Except as otherwise prescribed by general rules, or by order of the United States court, such transfer may be effected by filing a certified transcript of the final judgment of the United States court and the related pleadings in a court or magisterial district of this Commonwealth. The pleadings shall have the same effect as under the practice in the United States court, but the transferee court or magisterial district judge may require that they be amended to conform to the practice in this Commonwealth…."

[12] Cole v. Lawrence, 701 A.2d 987, 988 (Pa. Super. 1997) (citations omitted).

[13] Mellon Bank, N. A. v. National Union Fire Ins. Co., 768 A.2d 865, 868 (Pa. Super. 2001).

II. Superiority of the Competing Security Interests

A.

The issue before the court is whether Stillwater's security interest in the attorneys' fees is superior to plaintiffs' interest. Stillwater argues that its security interest in the fees is superior to plaintiffs' interest because it perfected its interest by filing a financing statement in accordance with Article 9 of the Uniform Commercial Code, while plaintiffs did not file a financing statement. Plaintiffs, however, contend that their security interest in the fees was automatically perfected when it attached and thus, they were not required to file a financing statement.[14]

A security interest "attaches" to the collateral of a debtor when it becomes enforceable against the debtor.[15] Typically, this requires that the debtor own the collateral in which it is conveying an interest, that the creditor make a loan, and that the debtor sign a security agreement.[16] Once the security interest has "attached," it is effective between the debtor and the creditor.[17] In order to compete effectively with third parties, the secured interest must then be "perfected."[18]

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[14] Both parties agree that New York law under Revised Article 9 of the Uniform Commercial Code governs this dispute. Section 9-301 of the U.C.C. provides the general rule that "while a debtor is located in a jurisdiction, the local law of that jurisdiction governs perfection, the effect of perfection or nonperfection, and the priority of a security interest in collateral." Since the debtors, i.e., the Law Firm Defendants, are located in New York, New York law governs perfection, the effect of perfection or nonperfection, and the priority of the security interest at issue.

[15] White & Summers, Uniform Commercial Code, Sec. 30-1(b) (5th ed., 2002).

[16] Id.

[17] Id.

[18] Id.

The general rule is that a financing statement must be filed in order to perfect all security interests.[19] When there is more than one perfected security interest, the security interests rank according to priority in time of filing or perfection.[20] "Filing" refers to the filing of an effective financing statement, whereas "perfection" refers to the acquisition of a perfected security interest, i.e., one that has attached and as to which any required perfection step has been taken.[21] A perfected security interest has priority over a conflicting unperfected security interest.[22] Further, a secured creditor's knowledge of another's security interest in the same collateral is irrelevant. "Whichever secured party first perfects its security interest…takes priority. It makes no difference whether that secured party knows of the other security interest at the time it perfects its own."[23]

Although the general rule is that a financing statement must be filed in order to perfect a security interest, there are certain exceptions in which perfection is automatic.[24] One such exception is that perfection is automatic upon attachment for the sale of a "payment intangible."[25] Plaintiffs assert that the interest that they acquired under the Purchase Agreements constituted a "payment intangible" and thus perfection was automatic upon attachment. Stillwater, on the other hand, contends that the interest that plaintiffs obtained was considered an "account" for which the filing of a financing statement was necessary. Thus, the issue of priority hinges on the characterization of the interest that plaintiffs obtained under the Purchase Agreements - - that is, a "payment intangible" or an "account."

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[19] N.Y. U.C.C. § 9-310(a).
[20] N.Y. U.C.C. § 9-322(a)(1).
[21] N.Y. U.C.C. § 9-322, cmt. 4.
[22] N.Y. U.C.C. § 9-322(a)(2).
[23] N.Y. U.C.C. § 9-322, cmt. 4, ex. 2.
[24] See N.Y. U.C.C. § 9-310(b).
[25] N.Y. U.C.C. § 9-309(3).

The term "account" is defined under Article 9 as "a right to payment of a monetary obligation, whether or not earned by performance,…for services rendered or to be rendered."[26] Pursuant to N.Y. U.C.C. § 9-102, cmt. 5(a), if "accounts" are sold, a financing statement must be filed to perfect the buyer's interest in them. In contrast, a "payment intangible" is considered a type of "general intangible." A "general intangible" means "any personal property, including things in action, *other than accounts*, chattel paper, commercial tort claims, deposit accounts, documents, goods, instruments, investment property, letter-of-credit rights, letters of credit, money, and oil, gas, or other minerals before extraction. The term includes payment intangibles and software."[27] The Official Comment to N.Y. U.C.C. § 9-102 states that the "general intangible" category is the residual category of personal property that is not included in the other defined types of collateral.[28] A "payment intangible" is defined as "a general intangible under which the account debtor's principal obligation is a monetary obligation."[29] As noted, perfection is automatic for the sale of a "payment intangible."

Plaintiffs contend, pursuant to New York law, that when they purchased the interest in the fees they acquired not only contractual rights under the Purchase Agreements, but also liens on, as well as property and equitable ownership interests in, the underlying personal injury claims. In support, plaintiffs cite N.Y. Judiciary Law § 475, which states, in relevant part: "From the commencement of an action…the attorney who appears for a party has a lien upon his client's cause of action, claim or counterclaim, which attaches to a verdict, report, determination, decision, judgment or

[26] N.Y. U.C.C. § 9-102(a)(2)(ii).
[27] N.Y. U.C.C. § 9-102(a)(42) (emphasis added).
[28] See N.Y. U.C.C. § 9-102, cmt. 5(d).
[29] N.Y. U.C.C. § 9-102(a)(61).

final order in his client's favor, and the proceeds thereof in whatever hands they may come." Plaintiffs also cite LMWT Realty Corp. v. Davis Agency, 85 N.Y.2d 462, 467 (1995) for the proposition that this statutory lien gives the attorney a "vested property interest" and an "equitable ownership interest" in the client's cause of action. Thus, plaintiffs maintain that the interests purchased from the Law Firm Defendants were vested property interests and equitable ownership interests in the underlying personal injury claims, rather than merely a right to payment for services rendered or to be rendered under a contract. They argue that these are interests in "things in action" and thus are "payment intangibles" rather than "accounts."

The District Court found that the interest that plaintiffs obtained under the Purchase Agreements was an "account." This court agrees. As the District Court noted, the proper Article 9 characterization of interests like the ones at issue in this case has not been frequently litigated. However, at least one court has held that an unmatured contingency fee contract was an "account" under Article 9. In PNC Bank v. Berg, 1997 Del. Super. LEXIS 19 (1997), the issue was whether a lender can take a security interest in a law firm's contingency fee contracts. Both parties agreed that a matured contingency fee claim (where the fee has been earned and the money is owed) is an account receivable under the U.C.C. However, they disagreed as to whether an unmatured contingency fee contract was considered an account receivable under the U.C.C. The Delaware Superior Court found that an unmatured contingency fee contract was an "account" under Article 9 of the U.C.C. because the lender's security interest included "contract rights" in the contingency fee contracts which were encompassed within the meaning of an "account."

Similarly, here, the interest that plaintiffs were purchasing under the Purchase Agreements was not an interest in the underlying personal injury claims, but rather an interest in the legal fees to be received from the specified cases. The Purchase Agreements set forth that the Law Firm Defendants were conveying to plaintiffs an interest in their attorneys' fees that was payable by the specified personal injury claimants. The attorneys' fee contracts between the Law Firm Defendants and the claimants created "a right to payment of a monetary obligation, whether or not earned by performance for services rendered or to be rendered" to the Law Firm Defendants. Thus, the Purchase Agreements between the Law Firm Defendants and plaintiffs constituted sales of "accounts" under Article 9 and not "payment intangibles."

B.

Plaintiffs argue alternatively that even if the assets transferred by the Purchase Agreements are considered "accounts," the assignments were nevertheless subject to automatic perfection under N.Y. U.C.C. § 9-309(2) because they did not transfer a significant part of the Law Firm Defendants' outstanding accounts or payment intangibles. Section 9-309(2) of Article 9 provides a second exception to the general rule that a financing statement must be filed in order to perfect a security interest. That section provides that "an assignment of accounts or payment intangibles which does not by itself or in conjunction with other assignments to the same assignee transfer a significant part of the assignor's outstanding accounts or payment intangibles" perfects automatically when it attaches.[30] The official comment to § 9-309(2) provides that the purpose of this particular exception is "to save from *ex post facto* invalidation casual or isolated assignments – assignments which no one would think of filing. Any person who

[30] N.Y. U.C.C. § 9-309(2).

regularly takes assignments of any debtor's accounts or payment intangibles should file."[31]

The appropriate tests to be applied in interpreting U.C.C. § 9-309(2) are the "percentage test" and the "casual and isolated transaction test."[32] The casual and isolated transaction test requires the Court to examine the circumstances surrounding the transaction, including the status of the assignee, to determine whether the assignment was, in fact, casual and isolated.[33] The underlying rationale behind this test is that it would not be unreasonable to require a secured creditor to file if he regularly takes assignments of a debtor's accounts, but it would be unreasonable if this was not a usual practice.[34] In contrast, the percentage test focuses on the size of the assignment in relation to the size of the outstanding accounts or payment intangibles of the assignor.[35] Both tests need to be reviewed in conjunction with all of the facts and circumstances involved in the relationship between the parties and the transactions in which they are engaged.[36]

Plaintiffs' Third Amended Complaint alleges that since the commencement of its business in 1998, USClaims was primarily in the business of purchasing directly from plaintiffs their interests in the potential proceeds of their personal injury claims.[37] Specifically, plaintiffs' Third Amended Complaint states that more than 97% of plaintiffs' customer relationships involved the purchase of these proceeds, for which

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[31]N.Y. U.C.C. § 9-309, cmt. 4.
[32] In re Wood, 67 B.R. 321, 323 (W.D.N.Y. 1986).
[33] Id. at 324.
[34] Id.
[35] See, e.g., In re B. Hollis Knight Co., 605 F.2d 397, 401 (8th Cir. 1979).
[36] In re Wood, 67 B.R. at 323.
[37] See Third Amended Complaint, at ¶¶ 12, 13.

perfection was automatic.[38] In contrast, plaintiffs contend that only approximately 1% of their customer relationships involved purchasing directly from attorneys a portion of their fee interests in their clients' non-settled personal injury claims, which are the type of interests at issue in this litigation.[39] Plaintiffs further allege that the value of the Flomenhaft Interests when purchased represented only approximately 10% of the total fees anticipated to be earned in connection with the cases at issue.[40] Lastly, plaintiffs assert that the percentage of their purchase of the Flomenhaft Interests, as compared to the Law Firm Defendants' total portfolio of cases, was significantly less than 10%.[41]

At this stage, there are questions of fact as to whether the interest assigned by the Law Firm Defendants to plaintiffs constituted a "significant part" of the Law Firm Defendants' outstanding accounts and payments intangibles. Under the "percentage test" and the "casual and isolated transaction test," the court must examine all of the facts and circumstances involved in the relationship between the parties and the transactions in which they are engaged. Here, there are issues of fact at to the various percentages alleged by plaintiffs and whether plaintiffs regularly took assignments of accounts or payment intangibles. While plaintiffs allege that the majority of their business consisted of *purchasing* directly from the injured claimants, themselves, their interests in the potential proceeds of their personal injury claims (for which perfection was automatic), plaintiffs contend that they did not regularly take *assignments* of accounts or payment intangibles. At this juncture, the court cannot assume that plaintiffs regularly took

[38] Id., at ¶¶ 13, 34.
[39] Id., at ¶¶ 14-16.
[40] Id., at ¶ 17.
[41] Id.

assignments of accounts or payment intangibles.[42] Since there are disputed issues of fact, judgment on the pleadings cannot be entered with respect to this issue.

III. Conversion (Count II)

Stillwater next moves for judgment on the pleadings on plaintiffs' claim for conversion. In support of their conversion claim, plaintiffs allege that "[n]otwithstanding Plaintiffs' superior rights and interests in and to the Flomenhaft Interests, Stillwater has taken and retained Plaintiffs' property (i.e., the fees paid on account of the Flomenhaft Interests), and Stillwater has advised that it plans to continue to take and retain Plaintiffs' property (i.e., the future fees to be paid on account of the Flomenhaft Interests)."[43] Stillwater contends that since plaintiffs' rights in the attorneys' fees are not superior to Stillwater's rights, plaintiffs' claim for conversion must fail.

Under New York law, "conversion occurs when a defendant exercises unauthorized dominion over personal property in interference with a plaintiff's legal title or superior right of possession."[44] Here, the claim for conversion hinges on the determination of which party has superior rights in the interests at issue. Since the threshold inquiry of the relative priority of the competing interests has not been answered, the court cannot enter judgment on the conversion claim at this stage.

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[42] See In re B. Hollis Knight Co., 605 F.2d at 402. ("The relevant question is whether [the banking institution] regularly took assignments of accounts receivable. There is no evidence in the record that they did…While [the banking institution] may do so as a matter of fact, the assignment of accounts receivable is a specialized method of securing loans, and we are not willing to assume that it was a regular practice.")
[43] See Third Amended Complaint, at ¶ 40.
[44] Newbro v. Freed, 409 F. Supp. 2d 386, 394 (S.D.N.Y. 2006), quoting LoPresti v. Terwilliger, 126 F.3d 34, 41 (2d Cir. 1997).

IV. Tortious Interference (Count III)

Stillwater also moves for judgment on the pleadings on plaintiffs' claim for tortious interference. Under New York law, tortious interference with a contract requires: 1) the existence of a valid contract between the plaintiff and a third party; 2) defendant's knowledge of that contract; 3) defendant's intentional procurement of the third-party's breach of the contract without justification; 4) actual breach of the contract; and 5) damages resulting therefrom.[45]

In their Third Amended Complaint, plaintiffs allege that Stillwater and the Broker Defendants had knowledge of the Purchase Agreements between plaintiffs and the Law Firm Defendants and intentionally and improperly procured the Law Firm Defendants' breach of those agreements without privilege or lawful justification.[46] Stillwater, however, argues that it is entitled to judgment on this count because plaintiffs cannot prove, as a matter of law, that Stillwater acted without "justification." Specifically, Stillwater contends that it acted with justification because it acted with a lawful purpose under Article 9 in perfecting its security interest ahead of plaintiffs, regardless of its knowledge of plaintiffs' earlier transactions with the Law Firm Defendants.

At this stage, the court cannot determine whether Stillwater acted with "justification" because the basis of its alleged justification again turns upon the question of which party perfected their security interest first. Accordingly, Stillwater's motion for judgment on the pleadings on the tortious interference claim must fail.

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[45] Lama Holding Co. v. Smith Barney Inc., 668 N.E.2d 1370, 1375 (N.Y. 1996).
[46] See Third Amended Complaint, at ¶¶ 52-53.

V. Aiding and Abetting (Count V)

In Count V, plaintiffs allege that Stillwater and the Broker Defendants aided and abetted the other defendants in the following wrongful acts: 1) the breach of fiduciary duty owed to the plaintiffs by the Law Firm Defendants; 2) the conversion of plaintiffs' property; and 3) the tortious interference with plaintiffs' rights under the Purchase Agreements.[47]

In their Motion for Judgment on the Pleadings, moving defendants state that they "do not seek judgment on the pleadings at this point on the claim against Stillwater for aiding and abetting tortious interference by Oxbridge and Spira, and the claims against all Moving Defendants for aiding and abetting breach of fiduciary duty."[48] Therefore, the only remaining claims under this count are for aiding and abetting in the conversion of plaintiffs' property against Stillwater and the Broker Defendants and aiding and abetting in the tortious interference with plaintiffs' rights under the Purchase Agreements against the Broker Defendants. Since the underlying tort claims will survive at this point for the reasons set forth above, judgment cannot be entered on the aiding and abetting claims.

CONCLUSION

For the reasons discussed, the Motion for Partial Judgment on the Pleadings is denied.

BY THE COURT,

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ALBERT W. SHEPPARD, JR., J.

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[47] See Third Amended Complaint, at ¶¶ 60-61.
[48] See Motion for Partial Judgment on the Pleadings, at p. 33.