IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

GENERAL ELECTRIC CAPITAL CORPORATION	:	**CIVIL ACTION**
	:	
v.	:	
	:	
ELLIOT STONE	:	**NO. 04-1691**

MEMORANDUM

Padova, J. **February 4, 2005**

Plaintiff, General Electric Capital Corporation ("GECC"), has brought this action in confession of judgment seeking payment by Defendant, Elliot Stone, on a guarantee executed by Stone in connection with a loan agreement entered into between GECC and Sorbee International, Ltd. ("Sorbee"). This Court entered Judgment by Confession in favor of GECC and against Stone on May 24, 2004. Before the Court is Defendant's Motion to Open Judgment by Confession. For the reasons which follow, Defendant's Motion is denied and the Stay of Execution upon the Judgment is vacated.

I. BACKGROUND

This action arises from a loan agreement entered into by GECC and Sorbee on February 1, 2002. (Compl. ¶ 6.) The parties to the loan executed the following relevant loan documents: a Loan and Security Agreement dated February 1, 2002 (the "Loan Agreement") and a Revolving Credit Note dated February 1, 2002, in the maximum principal amount of $8,000,000, as amended by the First Allonge to Revolving Credit Note which reduced the maximum principal amount to $5,000,000 (the "Revolving Note"). (Compl. Exs. A & B.) On

February 1, 2002, Stone, the President and Chief Executive Officer of Sorbee, executed a Guarantee and Suretyship pursuant to which he unconditionally guaranteed the repayment of all obligations of Sorbee under the Loan Agreement and Revolving Note (the "Guarantee"). (Compl. Ex. C.)

Sorbee defaulted on its obligations to GECC pursuant to the Loan Documents by filing a petition for bankruptcy relief, failing to account for significant cash collections, refusing to permit GECC's auditors to inspect Sorbee's books and records, and failing to perform various financial covenants. (Compl. ¶ 11.) As a result of these defaults, a total of $3,045,574.69 was due and payable from Stone to GECC pursuant to the Guarantee as of April 19, 2004. (Compl. ¶ 12.) Although GECC sent Stone a demand letter on April 14, 2004, he did not make any payments to GECC. Judgment by Confession was entered against Stone on May 24, 2004 in the amount of $3,045,574.69, with interest at the per diem rate of $666.80 from April 13, 2004. (May 24, 2004 Order.)

Sorbee has brought an adversary proceeding against GECC in its bankruptcy proceeding. See Sorbee Int'l, Ltd., Individually, and as Assignee of the Claims of Elliot Stone and Melvin Feinberg v. General Electric Capital Corp., Bankr. No. 04-15255-KJC, Adv. Proc. No. 04-515 (Bankr. E.D. Pa.) (the "Adversary Action"). Sorbee asserts, in the Adversary Action, that:

> GECC engaged in a course of conduct relating to letters of credit, reserves and charges

> against Sorbee's revolving line of credit, that Sorbee questioned GECC about the practice, that GECC confirmed that the practice was proper and that Sorbee could rely upon it, and that the parties actually performed consistently therewith for a period exceeding seven (7) months. At the conclusion of the seven months, GECC abruptly terminated the practice that had become the parties' established course of performance, threw Sorbee's finances into a turmoil and ultimately forced it to file for protection under Chapter 11 of the United States Bankruptcy Code.

(Def.'s Supp. Mem. at 2-3.)

II. LEGAL STANDARD

Motions to open confessed judgment are procedurally governed by Rule 60 of the Federal Rules of Civil Procedure. FDIC v. Deglau, 207 F.3d 153, 161 (3d Cir. 2000). "The proper inquiry for relief under Rule 60(b) is whether vacating the judgment will visit prejudice on the plaintiff and whether the defendant has a meritorious defense." Id. at 165 (citation omitted). State law "governs the substantive aspects of motions to open or strike confessed judgments." Id. at 166.

The parties agree that Pennsylvania law governs the substantive aspects of the instant Motion in accordance with paragraph 16 of the Guarantee, which states that the "GUARANTOR SPECIFICALLY CONSENTS TO THE APPLICABILITY OF PENNSYLVANIA LAW (WITHOUT REGARD TO PENNSYLVANIA CONFLICTS OF LAWS PRINCIPLES) WITH RESPECT TO LENDER'S EXERCISE AND ENFORCEMENT OF THE REMEDY OF CONFESSION OF JUDGMENT. . . ." (Compl. Ex. C ¶ 16, emphasis in

original.) Under Pennsylvania law, a motion to open a confessed judgment will be granted "[i]f evidence is produced which in a jury trial would require the issues to be submitted to the jury. . . ." Pa. R. Civ. P. 2959(e); see also First Seneca Bank v. Laurel Mt. Dev. Corp., 485 A.2d 1086, 1088 (Pa. 1984) ("A judgment taken by confession will be opened in only a limited number of circumstances, and only when the person seeking to have it opened acts promptly, alleges a meritorious defense and presents sufficient evidence of that defense to require submission of the issues to the jury."). The standard is that of a directed verdict. Deglau, 207 F.3d at 168 (citing Suburban Mechan. Contractors, Inc. v. Leo, 502 A.2d 230, 232 (Pa. Super. Ct. 1985)). Consequently, the district court considers the evidence in the light most favorable to the petitioner and accepts as true all evidence and proper inferences from it which support the defense while rejecting adverse allegations of the party obtaining the judgment. Id. Moreover, "[t]he Pennsylvania rules regarding challenges to confessed judgment require the petitioner to offer clear, direct, precise and believable evidence of his meritorious defenses." Id. (citation omitted).

III. DISCUSSION

A. Motion to Open Judgment

Stone argues that the confessed judgment should be opened because he has meritorious defenses to the judgment. These

defenses arise from the lending practices of GECC in connection with letters of credit ("L/Cs") issued to Sorbee's vendors which are the same lending practices which are the subject of the Adversary Action. (Def.'s Supp. Mem. at 3.)

Stone alleges that GECC and Sorbee originally agreed that, when Sorbee ordered goods from a vendor and a L/C was opened in favor of a vendor, 50% of the amount of the L/C was reserved by GECC, reducing Sorbee's credit availability by that amount. (Mot. ¶ 10.) Once a bill of lading was presented to GECC, GECC would reserve 100% of amount of the L/C, reducing availability under the Revolving Note by 100% of the amount of the L/C. (Id.) In May 2003, GECC altered its procedures as follows: once goods were ordered and a L/C was opened in favor of a vendor, GECC would reserve 35% of the amount of the L/C; upon presentation of the bill of lading to GECC, GECC would reverse the reserve for the L/C, thereby increasing Sorbee's borrowing availability under the Revolving Note; GECC would charge the full amount of the L/C against Sorbee's credit availability under the Revolving Note when either the L/C was drawn by the vendor or when Sorbee's credit terms from the vendors expired (30-120 days). (Mot. ¶¶ 11-12.) In reliance on GECC's change in its lending practices, Stone, on behalf of Sorbee, purchased substantial additional inventory from foreign vendors on greatly extended payment terms. (Mot. ¶ 15.) This L/C lending practice became critical to Sorbee's financial

well being and, in reliance on this lending practice, Sorbee increased its credit availability with GECC by at least $3,000,000 between September 2003 and January 2004 and used this credit availability to purchase substantially greater amounts of inventory. (Mot. ¶¶ 18-19.)

Stone further alleges that GECC terminated this lending practice on January 22, 2004 and, without notice to Sorbee, began to reserve 100% on all L/Cs for which a bill of lading had been presented, reducing Sorbee's credit availability by nearly $700,000 overnight. (Mot. ¶ 20.) As a result, Sorbee bounced checks to trade in the amount of $265,576.38, bounced its entire payroll, laid off half of its staff, ceased work on 25 new products, cancelled raw materials lines, ceased shipping to strategic customers, including Walmart and BJs, and notified valued customers that it may not be able to continue in the sugar-free business. (Mot. ¶ 23.) As a result, Sorbee was forced to file for Chapter 11 bankruptcy protection on April 13, 2004. (Mot. ¶ 24.) On May 18, 2004, Sorbee, individually and as assignee of the claims of Stone and Mel Feinberg, filed an adversary complaint against GECC in the bankruptcy proceeding. (Mot. ¶ 25.)

Stone argues that the confessed judgment should be opened because Sorbee has meritorious claims against GE Capital, based upon these facts, which, if successful, would render the confessed judgment against him void. He asserts that Sorbee has asserted

meritorious claims against GE Capital for breach of contract, breach of the duty of good faith and fair dealing, negligent misrepresentation, avoidable preference, equitable subordination, and economic duress. (Mot. ¶ 27.) He has submitted, in support of this argument, evidence relating to GECC's lending practices with respect to the L/Cs. This evidence consists of spreadsheets summarizing L/Cs issued on behalf of Sorbee which show the amount reserved by GECC with respect to each L/C. (Def.'s Ex. D.) Stone also argues that his application to open the judgment was timely filed and that GECC would not be prejudiced if the judgment were opened and it was required to litigate its claims.

GECC argues that the instant Motion should be denied because Stone cannot meet his burden of establishing a meritorious defense pursuant to Fed. R. Civ. P. 60(b) since the Guarantee provides that Stone's guarantee of payment to GECC is unconditional:

> Guarantor understands and agrees that this Guarantee shall be construed as a continuing, absolute and **unconditional** guarantee of payment **without regard to** (a) the validity, regularity or enforceability of the Loan Agreement, or any other Loan Document, any of the Obligations or any other collateral security therefor or guarantee or right of offset with respect thereto at any time or from time to time held by Lender (b) **any defense, set-off or counterclaim (other than a defense of payment or performance) which may at any time be available to or be asserted by Borrower against Lender**, or (c) any other circumstance whatsoever (with or without notice or knowledge of Borrower or Guarantor) which constitutes, or might be construed to constitute, an equitable or legal discharge of

> Borrower for the Obligations, or of Guarantor under this Guarantee, in bankruptcy or in any other instance.

(Compl. Ex. C ¶ 5, emphasis added.) GECC maintains that, in accordance with this provision of the Guarantee, Defendant agreed that he would be absolutely liable for repayment of the loans made to Sorbee by GECC, notwithstanding the existence of any defense, set-off or counterclaim which could be asserted against GECC by Sorbee.

The parties agree that New York law applies to this issue, pursuant to paragraph 16 of the Guarantee, which provides that "THIS GUARANTEE SHALL BE GOVERNED BY, AND CONSTRUED AND INTERPRETED IN ACCORDANCE WITH, THE LAW OF THE STATE OF NEW YORK" except in connection with confession of judgment. (Mot. Ex. C ¶ 16, emphasis in original.) GECC maintains that absolute and unconditional guarantees, such as the one in this case, are consistently upheld under New York law. The seminal New York Court of Appeals case regarding the enforceability of waivers in guaranties is Citibank, N.A. v. Plapinger, 485 N.E.2d 974 (N.Y. 1985). See Nat'l Westminster Bank PLC v. Empire Energy Mgmt. Syst., Inc., No. 93 Civ. 5331(WK), 1998 WL 47830, at *2 (S.D.N.Y. Feb. 5, 1998) (noting that the United States Court of Appeals for the Second Circuit has "recognized Plapinger as the controlling expression of New York law"). In Plapinger, Citibank and four other banks brought an action to enforce the terms of a guarantee against the officers and

directors of a corporation, who had personally guaranteed a line of credit for that corporation, which had declared bankruptcy. Plapinger, 485 N.E.2d at 975. The defendant officers and directors asserted, as a defense, that they had been fraudulently induced to execute the guarantee. Id. The New York Court of Appeals found that the parties had negotiated an "absolute and unconditional" guarantee, which waived claims regarding the validity of the parties' "'Restated Loan Agreement * * * or any other agreement or instrument relating thereto', or '(vii) any other circumstance which might otherwise constitute a defense' to the guarantee" and held that the waiver foreclosed their reliance on that defense. Id. at 977; see also WestRM-West Risk Mkts., Ltd. v. Lumbermens Mut. Cas. Co., 314 F. Supp. 2d 229, 234 (S.D.N.Y. 2004).

Stone relies on Mfrs. Hanover Trust Co. v. Yanakas, 7 F.3d 310 (2d Cir. 1993), to argue that the waiver contained in the Guarantee should not be enforced against him in this proceeding. In Yanakas, the United States Court of Appeals for the Second Circuit recognized that the New York courts which had considered the matter have found that a boilerplate waiver contained in a guarantee agreement (as opposed to the specifically negotiated waiver in Plapinger) would not bar a defense of fraudulent inducement: "many state court decisions since Plapinger . . . have ruled that the mere general recitation that a guarantee is 'absolute and unconditional' is insufficient under Plapinger to bar a defense of

fraudulent inducement, and that the touchstone is specificity. Thus, where specificity has been lacking, dismissal of the fraud claim has been ruled inappropriate." Id. at 316 (collecting cases). Stone contends that the waiver contained in the Guarantee is not sufficiently specific to act as a waiver of claims for breach of contract, breach of the duty of good faith and fair dealing, negligent misrepresentation, avoidable preference, equitable subordination, and economic duress. However, Yanakas limits only boilerplate waivers and only with respect to claims that the guarantor was fraudulently induced to enter into the guarantee. Id.; see also Valley Nat'l Bank v. Greenwich Ins. Co., 254 F. Supp. 2d 448, 457 (S.D.N.Y. 2003) ("The Second Circuit, in Manufacturers Hanover Trust v. Yanakas, elaborated on Plapinger by noting that 'in order to be considered sufficiently specific to bar a defense of fraudulent inducement ... a guarantee must contain explicit disclaimers of the particular representations that form the basis of the fraud-in-the-inducement claim.'") (citing Yanakas, 7 F.3d at 316); Nat'l Westminster Bank, 1998 WL 47830, at *3 (listing cases decided after Plapinger that support the Yanakas determination that boilerplate waiver language is insufficient to waive claims of fraudulent inducement).

Stone does not contend that he was fraudulently induced to enter into the Guarantee by GECC. Accordingly, the Court holds that the waiver clause of the Guarantee waives any defense which

Stone might otherwise possess to the judgment in this case which constitutes a "any defense, set-off or counterclaim (other than a defense of payment or performance) . . available to or . . . asserted by Borrower against Lender." (Compl. Ex. C ¶ 5.) As the only defenses asserted by Stone to the judgment confessed against him by GECC are defenses which have been asserted by Sorbee against GECC in the Adversary Action, the Court finds that these defenses have been waived by Stone. Consequently, the Court further finds that Stone has not alleged a meritorious defense to the confessed judgment and, therefore, Defendant's Motion to Open Judgment by Confession is denied.

B. Request for a Stay

On May 25, 2004, this Court stayed execution on the confessed judgment pending decision on the instant Motion to Open Confessed Judgment. (May 24, 2004 Order.) Stone has asked this Court to continue the stay of execution on the confessed judgment until the Adversary Action has been adjudicated by the Bankruptcy Court. Federal Rule of Civil Procedure 62, which governs stays of proceedings to enforce a judgment, provides as follows:

> In any state in which a judgment is a lien upon the property of the judgment debtor and in which the judgment debtor is entitled to a stay of execution, a judgment debtor is entitled, in the district court held therein, to such stay as would be accorded the judgment debtor had the action been maintained in the courts of that state.

Fed. R. Civ. P. 62(f). The parties agree that Stone's entitlement

to a stay is governed by Pennsylvania law. Pennsylvania Rule of Civil Procedure 3121(b) provides, in pertinent part, that: "[e]xecution may be stayed by the court as to all or any part of the property of the defendant upon its own motion or application of any party in interest showing . . . . (2) any other legal or equitable ground therefor." Pa. R. Civ. P. 3121(b)(2). The Superior Court of Pennsylvania has explained that: "A court, in exercising this power, should not stay an execution unless the facts warrant an exercise of judicial discretion. This entails a balancing of the rights of the debtor and creditor." Kronz v. Kronz, 574 A.2d 91, 94 (Pa. Super. Ct. 1990) (citing Sinking Fund Commissioners of Philadelphia v. Philadelphia, 188 A. 314 (Pa. 1936)). Moreover, "[i]n order to merit a stay of execution, the law and equities in the case of the party seeking relief must be plain and free from doubt or difficulty." Morgan Guar. Trust Co. of N.Y. v. Staats, 631 A.2d 631, 635 (Pa. Super. Ct. 1993) (citing Pennsylvania Co. for Ins. v. Scott, 198 A. 115 (Pa. 1938)).

Stone contends that the equities weigh in favor of a stay in this case because, if Sorbee is successful in its adversary proceeding against GECC, it will not owe any debt to GECC and Stone, as guarantor, would have been forced to pay a debt that does not exist. (Def.'s Supp. Mem. at 15.) However, the Guarantee executed by Stone states that he has guaranteed Sorbee's debt even if Sorbee is found to have no legal obligation to pay that debt to

GECC. The Guarantee states that Stone's guarantee is continuing, absolute and unconditional, without regard to:

> (b) any defense, set-off or counterclaim (other than a defense of payment or performance) which may at any time be available to or be asserted by Borrower against Lender, or (c) any other circumstance whatsoever (with or without notice to or knowledge of Borrower or Guarantor) which constitutes, or might be construed to constitute, an equitable or legal discharge of Borrower for the Obligations, or of Guarantor under this Guarantee, in bankruptcy or in any other instance.

(Guarantee ¶ 5.) Consequently, the Court finds that the law and equities do not favor continuing the stay of execution upon the confessed judgment. Moreover, continuing the stay until such a time as the Adversary Action has been completed in Bankruptcy Court would prejudice GECC because it would allow Stone to use assets which would otherwise be subject to GECC's judgment and may allow the claims of other creditors to obtain priority over GECC's claim to Stone's personal property. Therefore, Stone's request for a continuation of the stay of execution in this matter until the Adversary Action has concluded is denied.

An appropriate order follows.

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O R D E R

AND NOW, this 4th day of February, 2005, upon consideration of Defendant's Motion to Open Judgment by Confession and to Stay Enforcement of Judgment (Docket No. 5), all attendant and responsive briefing, and the hearings held on May 24, 2004 and September 9, 2004, **IT IS HEREBY ORDERED** that said Motion is **DENIED**. **IT IS FURTHER ORDERED** that the Stay of Execution upon the Judgment entered in this case is hereby **VACATED**.

BY THE COURT:

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John R. Padova, J.