IN THE SUPERIOR COURT OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

AIRPORT BUSINESS CENTER V LLLP, R. CLAYTON EMORY, ROBERT H. HILL and CARMEN J. FACCIOLO, JR. Plaintiffs, v. SUN NATIONAL BANK, and SPF 2011 OWNER, LLC Defendant.	)))))))))))	C.A. No.: N11C-10-200 PLA

On DEFENDANT SUN NATIONAL BANK'S MOTION TO DISMISS
GRANTED IN PART AND DENIED IN PART

Submitted: December 19, 2011
Decided: March 6, 2012

I. Introduction

In December 2004, a group of commercial real estate developers entered into a loan agreement with Sun National Bank ("Sun") to purchase an office building in Wilmington, Delaware. At the time, Sun was the anchor tenant of the property. Seven years later, the borrower and guarantors of the loan filed this lawsuit seeking damages for fraud and negligent misrepresentation in transacting the loan, and for breach of the lease by Sun when it vacated its retail space in the building. The guarantors of the loan also seek declaratory relief that their obligations have automatically terminated pursuant to an alleged modification of the loan agreement

that occurred in November 2009. The defendants have filed a Motion to Dismiss pursuant to Superior Court 12(b)(6), alleging that the plaintiffs' fraud, negligent misrepresentation, and breach-of-lease claims are barred by the statute of limitations. The defendants also assert that the plaintiffs have failed to state a claim under which declaratory relief can be granted, contending that there was no modification of the guaranty agreement as alleged by the plaintiffs and that the plaintiffs have alleged no facts that could support such a claim.

Upon review of the Complaint and the supporting documents, as well as the parties' arguments, the Court concludes that the defendants' motion should be GRANTED in part and DENIED in part. The Court agrees that the plaintiffs' claims for fraud, negligent misrepresentation, and breach of lease are barred by the statute of limitations and those claims will therefore be dismissed with prejudice. The Court finds, however, that the plaintiffs have sufficiently alleged a dispute regarding the modification of the guaranty agreement to allow their claim for declaratory relief to proceed.

II. Facts[1]

a. December 2004: Sun Lends $3.995 Million to ABC

In 2004, R. Clayton Emory, Robert H. Hill, and Carmen J. Facciolo, Jr. (collectively, "the Guarantors"), who are experienced commercial real estate developers in Delaware, approached Sun about the possibility of purchasing an office building located at 1300 North Market Street in Wilmington, Delaware ("the Property"). At the time, Sun was the anchor tenant in the building and occupied 24 percent of the Property, including a retail branch operation on the main floor. Sun offered to lend Plaintiffs the funds to purchase the Property. Before agreeing to underwrite the loan, Sun commissioned an appraisal of the property to determine its value (the "Appraisal"). Sun provided its appraiser with its Commercial Lending Appraisal Standards, which required that the Appraisal, among other things:

- Document actual income, vacancy, expenses, and net income for the two year period subsequent to the date of valuation;
- Analyze and report on trends that will affect projected income including increasing vacancy rates;
- Identify and report on any negative trends that affect the collateral;
- Not be based on unrealistic assumptions about the future;
- Contain all information necessary for the reviewer to understand the appraiser's opinion; and
- Clearly state any assumptions and conclusions.

[1] The facts in this opinion, which must be treated as true for the purposes of a motion to dismiss, are drawn from the well-pleaded allegations of the Complaint and the documents incorporated in the Complaint. *See, e.g.*, *Latesco, L.P. v. Wayport, Inc.*, 2009 WL 2246973, at *1, n.1 (Del. Ch. July 24, 2009).

The Appraisal estimated the value of the Property to be $5,300,000. It did not make any adjustment for the possibility that Sun would not renew its lease when it expired in 2006.

Emory, Hill, and Facciolo decided to proceed with the transaction. On December 9, 2004, their entity, Airport Business Center V ("ABC"),[2] borrowed $3,995,000 from Sun and used the proceeds to purchase the Property. Under the Loan Agreement and the Note, the loan was to be a non-revolving bridge/permanent loan. Section 2(a) of the Note provided for an initial term of 12 months with a Borrower's option to extend the initial term for several additional 12-month periods (the "Bridge Term") for no additional fee upon written notice to the Lender. At the Borrower's sole discretion, the loan could be extended for five years (the "Permanent Term") upon expiration of the Bridge Term provided that: (i) the Property achieved and maintained a "Debt Service Coverage Ratio" of at least 1.20 to 1.0, to be tested by the Lender on an annual basis (the "DSC Covenant"); and (ii) the Borrower was not in default of any obligations under the Loan Documents.

During the Bridge Term, the Note had a fixed interest rate of 7.25% per annum. Monthly installments of accrued interest on the outstanding principal balance of the loan were due and payable on the first day of each month during the

[2] Collectively, ABC and Emory, Hill, and Facciolo will be referred to hereinafter as "Plaintiffs."

Bridge Term. If the Borrower chose to extend the loan, the interest rate on the outstanding principal balance of the Note during the Permanent Term was to be equal to the fixed rate of the five-year rate of the Federal Home Loan Bank of New York as of the first day of the Permanent Term plus 200 basis points per annum. Assuming the Borrower extended the loan for the Permanent Term, the loan would be amortized over a 25-year period during the Permanent Term. The entire outstanding principal balance of the Loan, together with any and all accrued interest thereon, was to become due and payable, in full, upon expiration of the Permanent Term.

In connection with this transaction, Sun also required Hill, Emory, and Facciolo to sign a Guaranty Agreement as security for the loan. The guarantees were purportedly "unlimited," joint and several, and included all present and future written agreements between the Borrower and the Lender. Paragraph 21, which contained an important limitation on the duration of the Guaranty Agreement, provided that the Guaranty Agreement would cease automatically "at such time as the Property maintains a Debt Service Coverage Ratio (as defined in the Loan Agreement) of at least 1.20 to 1.0 throughout a continuous twelve (12) month period, provided that there is no Event of Default at the time of such termination."

The corresponding provision of the Loan Agreement, Section 4.1(k), defined the Debt Service Coverage Ratio as follows:

> "Debt Service Coverage Ratio" is defined as the ratio of Borrower's total net earnings before interest expense, taxes, depreciation, amortization and Leasing and Capital Cost, for a twelve (12) month period, divided by Borrower's annual Debt Service for such period. As used herein, "Leasing and Capital Cost" is defined as the average stabilized amount per net leasable square foot per year, which comprises tenant improvements, leasing commissions and capital reserves, for the applicable twelve (12) month period that is stated in Borrower's pro forma "Argus Model" financial projections that have been received and approved by Lender prior hereto (initially, $2.28 per net leasable square foot). Borrower's initial repairs to the Property's roof and other planned repairs to the building during the first year of the Permanent Term in excess of $2.28 per net leasable square foot will not be included in calculating the Leasing and Capital Cost. As used herein, the term "Debt Service" is defined as the annual payments of interest and principal due under the Loan (and under any other debt obligations secured by all or any portion of the Property) plus, as of the end of Borrower's last completed fiscal year, current matured long-term debt plus current capitalized lease obligations.

ABC notified Sun in writing on February 2, 2005 that it was electing to extend the Bridge Term for twenty-four months, *i.e.*, through December 9, 2006.

b. March 2006: Sun Vacates the Property

Approximately six months after issuing the loan, on June 30, 2005, Sun's Senior Vice President Larry Kramil advised ABC in writing that Sun had decided not to renew the lease upon its expiration on March 31, 2006. Kramil explained that Sun had determined that the Property's location did not present optimal potential for the growth of Sun's business. Plaintiffs allege that prior to June 30, 2005, Sun had never advised them that it did not consider the Property to be a good location for its business, and in fact, they submit that Sun had led them to believe that it intended to renew its lease.

Sun vacated the Property on or before March 31, 2006. When it did so, it left behind two oversized vault doors that had been used in its banking operations. Article 18 of the lease required Sun to remove trade fixtures, equipment, and furniture at the request of the Landlord. After Sun's departure, the property manager wrote to Sun on behalf of the landlord requesting that Sun remove and dispose of the vault doors or remit to ABC the cost of their removal. Sun had previously estimated that it would cost $79,760.15 to remove the doors. Despite repeated requests from ABC to remove the vault doors, Sun refused to do so. Sun likewise refused to remit the cost of their removal to ABC as requested and as required under the lease, leaving ABC to pay the cost and undertake the removal and disposal of the vault doors.

After Sun vacated the Property, ABC's rental income plummeted as Plaintiffs were unable to find a suitable tenant at a comparable rent. Unable to repay the principal balance of the loan at the end of the Bridge Term, and unable to find replacement financing to satisfy Sun's loan, ABC extended the Bridge Term for another six months through June 1, 2007.

c. August 2007: The Parties Modify the Loan

On August 27, 2007, Plaintiffs executed a formal Loan Modification Agreement (the "Modification Agreement") effective retroactively to June 1, 2007. Pursuant to the Modification Agreement, the parties extended the Bridge Term yet

again, from June 1, 2007 through August 31, 2008, at which time the Borrower could extend the loan for the five-year Permanent Term, if specific conditions were met as provided in the Note and Loan Agreement.

Section 1 of the Modification Agreement deleted Section 2(a) of the Note in its entirety and replaced it with the following language:

> The term of this Note shall be from the date hereof through August 31, 2008 (the "Bridge Term"). Notwithstanding the foregoing, the term of this Note may be extended for the period beginning immediately upon the end of the Bridge Term and ending on the date five (5) years thereafter (the "Permanent Term"), at the option of Borrower provided that (i) the Property [...] achieves a Debt Service Coverage Ratio (as defined in the Loan Agreement) of at least 1.20 to 1.0, and (ii) there is no uncured Event of Default [...] as of the end of the Bridge Term.

On June 16, 2008, Sun notified the Borrower that it was in default of the Debt Service Coverage Ratio requirement in the Loan Agreement (the "DSC Covenant"). According to Sun, the Borrower's Debt Service Coverage Ratio was "negative" for the fiscal period ending December 31, 2007. Sun "agreed to delay invoking its default provision and waive the event of default on [that] one occasion."

In late 2008, a disproportionate share of Sun's loan portfolio defaulted or was about to default. Because of systematic problems with its credit risk management and loan review practices, Sun was forced to enter into a memorandum of agreement (the "MOA") with the Office of the Comptroller of the Currency ("OCC") on April 15, 2010, providing the OCC with, among other things, broad

oversight over Sun's capital reserve strategies, lending practices, and loan management functions. The MOA, signed by the OCC and Sun's Board of Directors, acknowledged that the MOA was necessary for Sun to operate "safely and soundly" as a result of "unsafe and unsound banking practices, including inadequate credit risk management and loan review practices in the commercial lending area."

d. November 2009: The Parties Negotiate a Liquidity Covenant

On August 31, 2008, the Bridge Term expired pursuant to the Modification Agreement, but ABC was still unable to pay the outstanding principal balance of the loan or find replacement financing, due in large part to Sun's failure to renew its lease. Although Sun had claimed that ABC was in default due to a negative Debt Service Coverage Ratio, Sun did not declare an event of default as of the maturity date of the loan (August 31, 2008). Instead, Sun extended the Bridge Term through December 31, 2008 rather than call the debt and add another non-performing loan to its balance sheet.

Though the parties never executed another formal modification to the Loan Documents after August 2007, Sun continued to accept interest-only payments for another four (4) months after the loan matured until January 2009. In January 2009, rather than call the matured loan, which would have presented a significant risk of default, Sun ignored the claimed DSC Covenant default and began

amortizing the loan and billing ABC a fixed amount which included interest and principal. This change in billing by Sun to ABC increased debt service to an amount greater than the interest amounts billed by Sun to ABC prior to January 2009.

Sun continued to bill ABC fixed monthly amounts for eleven (11) months until November 2009. At that time, Sun approached the Borrower and proposed replacing the DSC Covenant with a liquidity covenant requiring the Guarantors to maintain a minimum liquid asset position of $5,000,000 tested annually (the "Liquidity Covenant"). Plaintiffs allege that, by virtue of the substitution of the Liquidity Covenant, the Guaranty Agreement would terminate automatically if the Guarantors maintained a minimum liquidity position of $5,000,000 for twelve (12) months, consistent with Section 21 of the Guaranty Agreement, as modified.

On November 2, 2009, Jason Mellinger, on behalf of Sun, wrote to Chris Galligan, on behalf of ABC, confirming that "the financial covenant was changed to test guarantor liquidity on an annual basis. This covenant states that all guarantors (Bob, Carmen and Mr. Emory) must maintain a liquid position above $5,000,000." On November 11, 2009, Mellinger and Galligan again spoke, and confirmed that the DSC Covenant in the Loan Documents would be replaced with the Liquidity Covenant. In exchange for this crucial modification to the Loan Documents, Sun received authorization to bill ABC new and additional

consideration including, but not limited to, an additional interest payment on the principal balance of the loan and repayment of loan principal. The next day, November 12, 2009, Galligan wrote to Mellinger confirming their agreement. In his letter, Galligan wrote:

> This letter will serve to memorialize our conversation yesterday regarding the [DSC Covenant] of the above[-]referenced loan. As discussed, the DSC [C]ovenant does not apply during the term of the loan. Rather, the covenant requiring the three guarantors to maintain a liquid position above $5,000,000, tested annually, remains in force during the term of the loan.

Sun did not subsequently contest that the Liquidity Covenant had been substituted for the DSC Covenant.

Plaintiffs contend that the Guarantors satisfied the requirement under the Liquidity Covenant for all periods since the inception of the Note as evidenced by personal financial statements provided to Sun by the Guarantors each year. The personal financial statements of the Guarantors submitted to Sun indicate liquidity in excess of $5,000,000 as of June 30, 2008, June 30, 2009, and June 30, 2010. As such, the Guarantors "…maintain[ed] a liquid position above $5,000,000, tested annually…" for the years 2008, 2009, and 2010. Therefore, Plaintiffs argue, pursuant to Section 21 of the Guaranty Agreement, as modified, the Guaranty Agreement is terminated.

e. May 2011: Sun Sells the Loan to SPF

On May 18, 2011, Sun notified the Borrower that it had sold the loan to SPF. Plaintiffs allege upon information and belief that Sun sold the loan to SPF/Garrison in a pool of troubled loans for approximately 57 cents on the dollar. Plaintiffs further allege upon information and belief that SPF knew or should have known that, based on the November 2, 2009 modification to the Loan Documents, the Guaranty Agreement terminated automatically in 2010.

The Guarantors allege that Sun began circulating the Guarantors' personal financial statements among potential purchasers of the loan in the first quarter of 2011. The Guarantors assert that Sun did not request permission, nor did it have authorization to circulate the Guarantors' personal financial statements in such indiscriminate fashion. Furthermore, the Guarantors allege upon information and belief that Sun never disclosed the substitution of the Liquidity Covenant to the potential purchasers of the loan, nor did it disclose that the Liquidity Covenant had been satisfied and that the Guaranty Agreement had terminated while it was marketing the loan.

Upon learning of the use of their personal financial statements to market the loan, the Guarantors contacted, through both letters and telephone calls, Bruce Dansbury, then Executive Vice President, Chief Operating Officer and Chief Credit Officer of Sun, and demanded: (1) the identities of all persons and entities

to whom their personal financial statements had been provided, and (2) their personal financial statements be retrieved from all recipients. Plaintiffs allege that Sun has refused to take any steps to retrieve or otherwise protect the privacy of the Guarantors' personal financial statements.

f. August 2011: SPF Prevents a Sale of the Property

Finally, in late July 2011, the Borrower received a bona fide, all cash offer, with no contingencies, to purchase the Property for $600,000 from Lenape Properties Management, Inc. ("Lenape"). On July 26, 2011, Galligan wrote to Eric Rosenthal at Garrison requesting its consent to the Lenape offer and that it accept the net proceeds of the sale in full satisfaction of the Note. Fearful that Lenape was losing interest in the deal, Galligan requested a response in writing from Garrison by the close of business on August 1, 2011. Garrison refused to consent to a sale of the Property on behalf of SPF, and he also refused to provide a written response as requested. On August 5, 2011, ABC's counsel wrote to Rosenthal requesting that Garrison consider the Borrower's proposal on behalf of SPF, in light of the termination of the Guaranty Agreement and the need to bring closure with Lenape. Garrison never responded directly to counsel's letter. Nearly three months later, by letter from counsel dated October 18, 2011, SPF rejected the offer to purchase the Property made in July 2011.

III. Contentions

Plaintiffs brought this action in Delaware Superior Court on October 24, 2011. Count I of the Complaint asks the Court to enter a declaratory judgment that the express terms of the Guaranty Agreement, as modified by the parties in writing in November 2009, terminated automatically no later than December 31, 2010. Plaintiffs also seek damages and rescission of the Loan Documents. Count II of the Complaint, alleging fraud, asserts that Sun, by and through its officers, agents and/or appraisers, led Plaintiffs to believe that it would renew its lease as the anchor tenant of the Property despite the fact that its management already knew that it had no intention of renewing its lease because Sun had already made its decision to close all retail branch operations in Wilmington, Delaware at the time Sun offered the loan to the Borrower. Count III of the Complaint, titled Negligent Misrepresentation, alleges that Sun led Plaintiffs to believe that it would renew its lease as anchor tenant when it already knew that it would not do so and failed to advise its appraiser of its true intentions. Plaintiffs allege that Sun should have reasonably foreseen that Plaintiffs would rely upon the statements and representations contained in Sun's Appraisal when deciding to purchase the Property and execute the Loan Documents. Finally, Count IV, Breach of Lease, alleges that Sun failed and refused to remove the vault doors from the Property or

remit payment for the cost of their removal as required under Article 18 of the Lease.

Defendants have filed the instant Motion to Dismiss. They contend first that Counts II, III, and IV of the Complaint are barred by the statute of limitations. Second, Defendants submit that Plaintiffs have failed to state a claim upon which declaratory relief can be granted with respect to their obligations under the Guaranty Agreement because they have presented no evidence of a written modification to the Guaranty Agreement, as expressly required by the terms of the contract itself.

IV. Discussion

a. Standard of Review

The standard of review when considering a motion to dismiss is well-settled: (1) all well-pleaded factual allegations are accepted as true; (2) even vague allegations are "well-pleaded" if they give the opposing party notice of the claim; (3) the Court must draw all reasonable inferences in favor of the non-moving party; and (4) dismissal is inappropriate unless the "plaintiff would not be able to recover under any reasonably conceivable set of circumstances susceptible of proof."[3]

[3] *Savor, Inc. v. FMR Corp.*, 812 A.2d 894, 896-97 (Del. 2002) (citations omitted).

b. Counts II, III, and IV of the Complaint are Time-Barred

Plaintiffs do not contest Defendants' argument that the claims for fraud, negligent misrepresentation, and breach of lease are time-barred. Under 10 *Del. C.* §8106, which prohibits bringing claims "arising from a promise" more than three years after the cause of action has accrued, Plaintiffs' claims for fraud, misrepresentation, and breach of lease are precluded.[4] The statute of limitations begins to run when a plaintiff's claim accrues, which occurs at the moment of the wrongful act and not when the effects of the act are felt.[5] Here, Plaintiffs' claims for fraud and negligent misrepresentation accrued as of the date the loan was executed, on December 9, 2004. As such, the statute of limitations expired on those claims on December 9, 2007. Similarly, Plaintiffs' claims for breach of lease accrued when Sun's lease expired on March 31, 2006. The statute of limitations on the breach of lease claim expired March 31, 2009. Counts II, III, and IV of the Complaint are time-barred and will therefore be dismissed with prejudice.

c. Plaintiffs Have Satisfactorily Alleged a Claim for Declaratory Relief

The only remaining issue before the Court is whether the plaintiffs have sufficiently alleged a claim for declaratory relief with respect to the alleged

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[4] The Chancery Court has consistently held that the three-year bar on claims arising from a promise extends to claims for fraud. *See, e.g.*, *Vichi v. Koninklijke Phillips Elecs. N.V.*, 2009 WL 4345724, at *5 (Del. Ch. Dec. 1, 2009) (explaining that Delaware law sets a three year statute of limitations for claims for…fraud…and breach of fiduciary duty); *Sunrise Ventures LLC v. Rehoboth Canal Ventures, LLC*, 2010 WL 363845, at *6 (Del. Ch. Jan. 27, 2010).
[5] *Sunrise Ventures*, 2010 WL 363845 at *6.

modification of the Guaranty Agreement. In essence, Plaintiffs argue that the parties' substitution of a Liquidity Covenant for the DSC Covenant in Paragraph 21 of the Loan Agreement in November 2009 extended to the Guaranty Agreement, which originally provided that the Guaranty Agreement would automatically terminate when the Property had maintained a Debt Service Coverage Ratio of at least 1.20 to 1.0 throughout a continuous twelve-month period in the absence of default. The Guarantors submit that they satisfied the new Liquidity Covenant, thereby triggering termination of the Guaranty Agreement and releasing them from their obligation.

In response, Sun argues that the replacement of the Debt Service Coverage Ratio with a Liquidity Covenant has no bearing on the Guaranty Agreement. In particular, Defendants insist that the Guaranty Agreement is a separate and distinct document from the Loan Agreement and that the Guaranty Agreement expressly provided that "any extension, modification, renewal or change in the Note…or in any other of the Loan Documents […] shall not in any manner affect or impair this Guaranty."[6] Furthermore, it submits that the Guaranty Agreement expressly required written modification to take effect. Defendants contend that Plaintiffs can provide no evidence of written modification to the Guaranty Agreement, nor can they prove that Sun intended the changes to the debt service coverage ratio in the

[6] Guaranty Agreement, section 2(a).

Loan Agreement to apply to the Guaranty Agreement. As such, Defendants argue that dismissal of the case is required.

At this stage of the litigation, the dispute over the alleged modification of the Guaranty Agreement appears to center upon the parties' intent. Plaintiffs assert that the replacement of the debt service coverage ratio in the Loan Agreement with a liquidity test necessarily affects the Guaranty Agreement because the Guaranty Agreement provided that it would automatically terminate upon the satisfaction of the debt service coverage ratio requirements in the original Loan Agreement. Plaintiffs have alleged that they can prove this change by oral and written evidence and by the existence of additional consideration provided to Sun, in the form of increased interest payments.[7] Defendants, for their part, insist that the language of the Guaranty Agreement does not permit modification through amending the terms of the Loan Agreement and that Sun never intended such a change. Thus, a question of fact exists as to whether Sun understood that it was approving a change in the terms of the Guaranty Agreement when it agreed to replace the debt service coverage ratio with a liquidity test in the Loan Agreement. Dismissal is therefore

[7] An amendment to a contract relies upon the presence of mutual assent and new consideration. While Delaware courts strongly prefer a showing of mutual assent in writing, it is possible to demonstrate mutual assent orally where the party asserting a change can show sufficient specificity and directness. *See, e.g.*, *Continental Ins. Co. v. Rutledge & Co., Inc.*, 750 A.2d 1219, 1228-1230 (Del. Ch. 2000).

inappropriate on the record presently before the Court.[8] Defendants' motion to dismiss Count I of the Complaint must therefore be DENIED.

V. Conclusion

For the reasons set forth above, Defendants' Motion to Dismiss Counts II, III, and IV of the Complaint is GRANTED. Defendants' Motion to Dismiss Count I of the Complaint seeking declaratory relief is DENIED.

IT IS SO ORDERED.

/s/ Peggy L. Ableman
PEGGY L. ABLEMAN, JUDGE

Original to Prothonotary

[8] *See, e.g.*, *Brasby v. Morris*, 2007 WL 949485 (Del. Super. Mar. 29, 2007)