COUNSEL'S CORNER

By Kenneth J. Finger, Esq.,
Carl L. Finger, Esq., and
Daniel S. Finger, Esq.
Finger & Finger, Chief Counsel,
Building & Realty Institute (BRI)

Courts Continue to Uphold Business Judgment Rule On Subletting Routines and On Additional Key Issues

WHITE PLAINS—In the recent case of Bregman v. 111 Tenants Corp., 943 N.Y.S.2d 100 (App. Div. 2012), the Appellate Division First Department reached three important conclusions pertaining to the right of a Cooperative's Board of Directors to dictate subletting rules.

The Court concluded that the Plaintiff had not provided adequate documentation to prove her case, that the Cooperative could not create classes of shares where certain shareholders possessed unfettered rights not granted to others, and third, that the Cooperative's Board of Directors business judgment was entitled to deference.

Plaintiff sought to sublet the apartment without the permission of the Board based on a purported agreement with the prior holder of unsold shares. The court concluded that the Plaintiff, who sought to sublet her apartment, had not provided any documentation that would support her claim that she maintained an unfettered right to sublet her apartment. There are numerous cases relating to the rights of "holders of unsold shares" which, of late, have dealt with the issues of documentation, or the lack thereof, and the impact on claims of status as "holders of unsold shares."

Though not cited by the Court, these cases are consistent with the concept that in order to sustain such a claim, that status must be documented and that the claim is a contractual issue requiring such documentation.

An Important Matter

The second and much more fundamental holding of the Court requires attention. The Court held that "even if plaintiff had been granted such preferential unfettered sublet rights, Business Corporations Law § 501(c)—which provides that "each share [issued by a corporation] shall be equal to every other share of the same class"—precludes any such special subletting rights (see Wapnick v. Seven Park Ave. Corp., 240 A.D.2d 245, 658 N.Y.S.2d 604 [1997]; see also Krakauer v. Stuyvesant Owners, 301 A.D.2d 450, 753 N.Y.S.2d 367 [2003])."

The Court went on to find that "we view the directive of Business Corporations Law § 501(c) as not limited to unequal treatment in proprietary leases or bylaws. It precludes the proposition, advanced by plaintiff, that a shareholder purchasing common shares may, by contract with the cooperative, obtain special rights that could not be granted in the corporate documents themselves."

Interestingly, in this section of the decision, the Court essentially limited the authority of the Board by interpretation of the Business Corporations Law.

Finally, in a sweeping view of the Board's authority, subject no doubt to the above references, the Court held that "the board here was prompted by a legitimate interest in the welfare of the cooperative: maximizing owner residency and therefore the value of the shares. It is therefore authorized to adopt a resolution in furtherance of that interest… Moreover, while a board may not deliberately single out individuals for harmful treatment (Levandusky, 75 N.Y.2d at 538, 554 N.Y.S.2d 807, 553 N.E.2d 1317), if a board of directors becomes aware of a situation or conduct of a particular shareholder that it considers contrary to the interests of the cooperative generally, there is no prohibition against the board's adoption of a policy protective of those broader interests, even if the policy is responsive to a single shareholder's situation or conduct."

Similarly, the District Court in Nassau County recently upheld a Cooperative's Board of Directors' refusal to approve a sublet. The Court stated that: "the Court rejects Respondent's claims that Petitioner acted arbitrarily or committed fraud. Respondents purchased the cooperative in 2004. There is no mandatory obligation in the Proprietary Lease for the Petitioner to approve a sublet. Paragraph 14 in the Proprietary Lease is clear that subletting is subject to the approval of the Board subject to "which consent shall not be unreasonably withheld." The Court finds that the Petitioner acted appropriately in not approving the sublet and there is no violation of the business judgment rule. The actions of the Board were appropriate and subject to the business judgment rule which this Court finds no reason to vacate. See Matter of Levandusky v. One Fifth Avenue Apartment Corp., 75 N.Y.2d 530, 554 N.Y.S.2d 807 (1990).

In the case at bar, Petitioner acted for the legitimate welfare of the cooperative and thus its actions were reasonable. See also Chambers v. 15 Beach Owners, Inc., 221 A.D.2d 400, 633 N.Y.S.2d 1016 (2nd Dept 1995). First Buckingham Owners Corp. v. Tamburo, 32 Misc. 3d 1238(A), 938 N.Y.S.2d 226 (Dist. Ct. 2011)."

Factors

The recent spate of cases relative to subletting and otherwise challenging the Board's authority may be linked to the economic forces at work today. With shareholders "under water" yet with expanding families and other issues, the need to sublet has increased. Conversely, the tightening of bank requirements regarding rentals and sublets when financing cooperatives may be causing Boards to take more care in the implementation of their sublet policies and to adhere to strict limits.

Nonetheless, it appears that the Boards are well within their business judgment to implement such policies and should take comfort as they go forward that Courts will respect their judgment in such matters.

Other Issues

The Courts continue to uphold the business judgment rule in other ways, as well. In another case, the Supreme Court of New York County upheld the Board's authority to finance a window replacement project. In that case, the Court particularly upheld the Board's decision where it was alleged that the project could have been done for no cost via a grant, but was, instead, the subject of borrowing and an anticipated assessment. The Court held that:

Defendant's decisions regarding the window replacement project are protected by the business judgment rule, which provides that the court should defer to a cooperative board's determination [s] "so long as the board acts for the purposes of the cooperative, within the scope of its authority and in good faith." Levandusky v. One Fifth Avenue Apartment Corp, 75 N.Y.2d 530, 538 (1990); Accord 40 West 67th Street Corp v. Pullman, 100 N.Y.2d 147, 153 (2003); Pelton v. 77 Park Avenue Condominium, 38 AD3d 1, 7–9 (1st Dept 2006). Under the business judgment rule, the court will not inquire as to

Continued on page 9