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RENT REGULATION

Grimm Case Sows More Confusion


By **Warren A. Estis** And **Jeffrey Turkel**

In its 4-3 ruling in *Grimm v. New York State Division of Housing and Community Renewal*, 15 N.Y.3d 358, 912 N.Y.S.2d 491 (2010), the Court of Appeals held that the Division of Housing and Community Renewal (DHCR) or a court can ignore the four-year look-back period for rent overcharge claims where the tenant raises a "colorable" claim of fraud. In response to DHCR's argument that chaos would ensue if it were required to evaluate claims of fraud on a case-by-case basis, Judge Carmen B. Ciparick, who authored the majority opinion, wrote:

> DHCR also argues that, under the Appellate Division's holding, any "bump" in an apartment's rent—even those authorized without prior DHCR approval, such as rent increases upon installation of improvements to an apartment—will establish a colorable claim of fraud requiring DHCR investigation. Again, we disagree. Generally, an increase in the rent alone will not be sufficient to establish a "colorable claim of fraud," and a mere allegation of fraud alone, without more, will not be sufficient to require DHCR to inquire further. What is required is evidence of a landlord's fraudulent deregulation scheme to remove an apartment from the protections of rent stabilization.[1]

Judge Robert S. Smith, writing for the dissent, sympathized with DHCR's dilemma:

> The majority opinion can be read to mean either that the four-year limitation has largely ceased to exist, or that any case to which the limit applies on its face must lead to a mini-litigation, in which DHCR tries to figure out whether the overcharge was "fraudulent" enough to escape the time limit. If the former, the majority has simply tossed aside the Legislature's command. If the latter, I do not envy DHCR its task.[2]

Judge Smith's warning provides an apt introduction to the Appellate Division, First Department's Oct. 29, 2013 split decision in *Boyd v. New York State Division of Housing and Community Renewal*, 110 A.D.3d 594, 973 N.Y.S.2d 609 (1st Dept. 2013). There, the majority held that the tenant had raised a "colorable" claim of fraud, which DHCR had failed to properly investigate.

'Boyd'

In 2007, tenant Kelley Boyd moved into an apartment at 240 Cabrini Blvd. at a stabilized rent of over $2,000 per month. (Because the building was receiving J-51 benefits, the apartment remained rent stabilized.) On April 7, 2009, she filed a complaint of rent overcharge with DHCR.

The rental history revealed that the registered rent for the apartment was $572 in 2004, at which time a long-time tenant vacated the apartment. The landlord then performed work in the unit, and in October of 2004 raised the stabilized rent to $1,750 per month.

The tenant alleged in her overcharge complaint that the $1,750 rent could not be justified based on individual apartment improvements (IAIs) because (1) the landlord would have needed to spend $39,000 to justify that rent, and (2) she estimated that, based on her research and calculations, the improvements could not have cost more than $5,000. The landlord, in turn, did not specifically rebut the tenant's allegations or provide details as to the work performed.

Critically, the work in question took place in mid-2004, i.e., more than four years before the tenant filed her overcharge complaint. Thus, the question arose as to whether, under *Grimm*, the tenant raised a "colorable" claim of fraud, such that DHCR was required to investigate whether the IAIs justified the $1,750 rent.

DHCR's Ruling

In its July 19, 2011 final order, DHCR ruled that the tenant had not raised a "colorable" claim of fraud. DHCR ruled that the three-part test of factors set forth in *Grimm* were (1) a combination of circumstances alleged by the tenant that point to other violations of the Rent Stabilization Law; (2) a fraudulent deregulation scheme; and (3) a variance in the registration history from the lease history. DHCR found that the first criterion had not been satisfied, and, as to the second criterion, observed that the owner consistently registered the apartment as rent stabilized. The agency also ascribed a variance in the registration history to a clerical error.

On the central issue of the alleged IAIs, DHCR's commissioner noted that, in contrast to the circumstances set forth in *Grimm*, the rent increase at issue occurred after the building owner renovated the apartment for the first time in 32 years, and that "it would not be difficult for anyone with

WARREN A. ESTIS *is a founding partner at Rosenberg & Estis.* JEFFREY TURKEL *is a partner at the firm.*

any experience in this industry to believe that it could have taken $39,000" to do so.

Supreme Court

The tenant then commenced an Article 78 proceeding, which was assigned to New York County Supreme Court Justice Barbara Jaffe. Jaffe denied the tenant's Article 78 petition, crediting the commissioner's finding that it was not illogical to assume that the landlord had spent at least $39,000 to improve the apartment. The court also focused on language in *Grimm* stating that, in order to go beyond the four-year look-back period, the tenant must provide "evidence of a landlord's fraudulent deregulation scheme to remove an apartment from the protections of rent stabilization." *Grimm*, 15 N.Y.3d at 367. The Supreme Court wrote:

> Here, in concluding that there were insufficient indicia of fraud to warrant examination of the rental history for petitioner's apartment beyond the four-year limitations period, the Deputy Commissioner… rationally distinguished the building owner's behavior from that of the landlords in *Grimm* and *Thornton v. Baron*. Whereas they engaged in fraudulent deregulation by, inter alia, requiring tenants to sign leases containing a provision that their apartments would not be their primary residences, increasing rent without providing rent stabilized lease riders, and threatening to raise rents if tenants failed to perform repairs at their own expense, the building owner here always registered the apartment as rent stabilized, even when the registered rent exceeded the $2,000 limit for rent stabilized apartments, and provided rent stabilized lease riders.[3]

The tenant then appealed to the Appellate Division, First Department.

The Majority

By a 3-2 margin, the First Department reversed the Supreme Court and remanded the matter to DHCR. The majority consisted of Justices Angela M. Mazzarelli, Helen E. Freedman, and Paul G. Feinman. Justice Judith J. Gische wrote the dissenting opinion, in which Justice John W. Sweeny joined.

The majority held that DHCR must go beyond the four-year look-back period where there is "'substantial indicia of fraud on the record.'"[4] The majority focused on what it claimed was DHCR's "disparate treatment of the parties' claims" regarding the renovation: the tenant's claim that the apartment renovation could not possibly have cost $39,000, and the landlord's relative silence on the issue. The majority wrote:

> While the agency made no attempt to evaluate the legitimacy of petitioner's claims despite their consistency and degree of detail, DHCR credited the owner's implicit claim that it spent $39,000 to renovate the apartment simply because "it would not be difficult for anyone with experience in this industry to believe it could have taken $39,000 in IAIs to update the appearance and equipment in an apartment which had not changed hands for thirty-two years."[5]

Judge Robert Smith's warning provides an apt introduction to the Appellate Division, First Department's split decision in 'Boyd,' where the majority held that the tenant had raised a "colorable" claim of fraud, which DHCR had failed to properly investigate.

The majority continued:

> This justification for the agency's determination is irrational. Finding that the owner "could have' spent $39,000 in IAIs, where the owner never submitted any evidence controverting petitioner's claims is not equivalent to finding that the owner actually made improvements costing that much."[6]

The dissent took a different approach, holding that the issue was not the competing claims of the tenant and landlord, but whether the tenant had met the threshold of raising a colorable claim of fraud. The dissent wrote:

> Petitioner's subjective belief that the IAIs could not have cost more than $5,000 does not satisfy her initial burden of showing that the fraud exception to the four-year statute of limitations should be applied, requiring DHCR to review a rent charged more than four years before her overcharge complaint. A conclusory claim, without more, is insufficient for the agency to disregard the four-year look back period established in the Rent Stabilization Law…requiring that an owner retain records relating to rents for housing accommodations for four years prior to the date of the most recent registration.[7]

The dissent concluded:

> The majority's conclusions that petitioner's letter triggered an inquiry eviscerates the four-year statutory rule whenever a tenant alleges fraud, even without any particularity. I do not believe that *Grimm* has such wide-ranging implications.[8]

Although the First Department's decision in *Boyd* had two dissents, the majority remanded the matter to DHCR "to give the parties the opportunity to present evidence in connection with the legality of the base rate rent."[9] As such, the matter cannot be appealed to the Court of Appeals as of right. However, the authors are informed that both DHCR and the landlord in *Boyd* have moved for leave to appeal. If leave is granted, the Court of Appeals will have an opportunity to clarify what constitutes a "colorable" allegation of fraud so as to justify going beyond the four-year look-back period.

1. 15 N.Y.3d at 367 (internal citations omitted).
2. Id. at 369.
3. 2012 WL 1834251.
4. 973 N.Y.S.2d at 610.
5. Id.
6. Id.
7. 973 N.Y.S.2d at 612-13 (citations omitted).
8. Id.
9. 973 N.Y.S.2d at 611.