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Back to Article

First Department Allows Class Actions to Proceed

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This past Thursday, the Appellate Division, First Department, released three decisions, all of which held that tenants can waive treble damages in *Roberts*-style class action cases so as to avoid the prohibition in the class action statute against seeking penalties. The cases were *Downing v. First Lenox Terrace Assocs.*, *Gudz v. Jemrock Realty*, and *Borden v. 400 East 55th Street Assocs*. (The authors' firm represented the owner in *Borden.)*

Background

The three cases arose in the wake of *Roberts v. Tishman Speyer Props.*, 62 A.D.3d 71, 874 N.Y.S.2d 97 (1st Dept. 2009), aff'd 13 N.Y.3d 270, 890 N.Y.S.2d 388 (2009). There, the New York State Court of Appeals ruled that an owner's receipt of J-51 benefits barred the owner from luxury deregulating apartments while such benefits were in effect.

Following *Roberts*, tenants in various buildings commenced putative class action lawsuits, seeking rent rollbacks and rent overcharge awards in J-51 buildings with respect to apartments that the owners had, in light of *Roberts*, incorrectly treated as luxury deregulated. The possibility that tenants could obtain treble damages in such cases raised an issue as to the very viability of proceeding as a class action. CPLR 901(b) states in its entirety:

Unless a statute creating or imposing a penalty, or a minimum measure of recovery specifically authorizes the recovery thereof in a class action, an action to recover a penalty, or minimum measure of recovery created or imposed by statute *may not be maintained as a class action*. (Italics supplied).

It is well settled that treble damages under the Rent Stabilization Law (RSL) constitute a penalty. See *H.O. Realty v. New York State Div. of Housing & Community Renewal*, 46 A.D.3d 103, 844 N.Y.S.2d 204 (1st Dept. 2007). It is also undisputed that the RSL does not specifically authorize tenants seeking a rent overcharge award to maintain a class action proceeding.

The named tenants in various class action complaints, acknowledging the CPLR 901(b) bar against maintaining class actions in cases where penalties are sought, purported to "waive" their right to treble damages on behalf of the entire class. This tactic, however, appeared to be at odds with Court of Appeals authority holding that tenants cannot waive their rights under the RSL. See *Riverside Syndicate v. Munroe*, 10 N.Y.3d 18, 853 N.Y.S.2d 263 (2008). In *Drucker v. Mauro*, 30 A.D.3d 37, 41, 814 N.Y.S.2d 43 (1st Dept. 2006), the First Department memorably held:

[t]he prohibition against avoiding, by agreement, protection by the rent stabilization scheme could not be stated more plainly…a tenant may not avail himself of the advantages of the statute when it furthers his interest and decline to be bound by the statutory scheme when it proves detrimental to those interests.

Thus, the question before the First Department in all three cases was whether tenants could waive their right to treble damages under the RSL in order to avoid the prohibition in CPLR 901(b) against seeking penalties in a class action proceeding. The First Department held that tenants could indeed waive their right to treble damages without running afoul of the RSL or CPLR 901(b).

'Downing'

In *Downing*, Justice Richard T. Andrias, writing for the court, held that penalty waivers in prior class action litigations had been found to be permissible:

However, even where a statute creates or imposes a penalty, the restriction of CPLR 901(b) is inapplicable where

the class representative seeks to recover only actual damages and waives the penalty on behalf of the class, and individual class members are allowed to opt out of the class to pursue their punitive damage claims (see *Cox v. Microsoft*, 8 AD3d 39 [1st Dept. 2004]…).

Addressing the ability of tenants to waive their rights under the RSL, Andrias wrote:

Rent Stabilization Code (9 NYCRR) §2520.13, which states that '[a]n agreement by the tenant to waive the benefit of any provision of the RSL or this Code is void,' does not require a different result. '[P]laintiffs are seeking to waive their entitlement to treble damages unilaterally, not through agreement. Thus, allowing the class action to proceed would not frustrate the RSC's purpose of [avoiding] situations whereby the landlord attempts to circumvent the [RSC's] benefits' (internal citations omitted).

Andrias next distinguished *Asher v. Abbott Labs.*, 290 A.D.2d 208, 737 N.Y.S.2d 4 (1st Dept. 2012), a case involving the Donnelly Act (GBL §340[5]), wherein the First Department rejected the plaintiffs' attempt to preserve class action status by waiving treble damages:

However, under General Business Law §340(5), treble damages are awarded upon a finding of liability; the statute does not require a finding of willfulness or bad faith. In contrast, Rent Stabilization Law §26-516(a) only requires treble damages where the landlord cannot demonstrate that it did not act willfully….

The court then addressed the issue of whether interest and attorney fees in connection with an overcharge claim, which claims the tenants in *Downing* did not waive, constitute a penalty under CPLR 901(b):

…an award of interest is simply the means of indemnifying an aggrieved person. It represents the cost of having the use of another person's money for the specified period. Thus, while treble damages under the Rent Stabilization Law §26-516(a) is a true penalty, allowable only where the overcharge is willful, the award of interest on the overcharge is compensatory in nature in that a tenant is only getting a return on the actual amount he or she was overcharged, which would correspond to the landlord's reasonable use of the money while it was in the landlord's possession. (Internal quotation marks and citations omitted).

'Gudz'

The courts in *Gudz* and *Borden*, citing *Downing*, also held that the representative tenants therein could waive their claim for treble damages so as to proceed as a class action. In *Gudz*, however, Justice Sallie Manzanet-Daniels authored a sharp dissent, in which Justice Karla Moskowitz joined. Manzanet-Daniels first addressed the issue of whether the legislative intent of CPLR 901(b) and the RSL itself allowed tenants to waive treble damages in order to preserve class action status:

The majority finds CPLR 901(b) inapplicable in this case because the plaintiff class representatives waived the right to seek treble damages under RSL §26-516(a). However, to permit such a waiver would be to circumvent the clear intent of CPLR 901(b), which is to preclude the maintenance of a class action suit seeking a penalty. Plaintiff's waiver of treble damages is moreover void under Rent Stabilization Code (9 NYCRR) §2520.13, which provides that "[a]n agreement by the tenant to waive the benefit of any provisions of the RSL or this Code is void." (Citations omitted).

The dissent continued:

We have previously held that an agreement "which waives the benefit of a statutory protection *is unenforceable as a matter of public policy, even if it benefits the tenant*" (*Drucker,* 30 AD3d at 38 [emphasis added]). Since the effect of the waiver is to vitiate a provision integral to the RSL—the exaction of excessive rents by the landlord—I am compelled to conclude that it is void under 9 NYCRR §2520.13.

The dissent also challenged the majority's holding that there is no RSL violation because tenants who want treble damages can simply "opt out" of the class action litigation:

I am similarly unpersuaded by the majority's reasoning that there is no statutory violation because an individual class member may opt out of the class to pursue his or her treble damages claim. By allowing a class action to proceed seeking only actual damages, we permit the class to effectively rewrite RSL 26-516(a) and undermine the Legislature's purpose in enacting the statute. Further, allowing waiver under these circumstances arguably does not satisfy due process. …Since an award of treble damages pursuant to RSL 26-516(a) unequivocally constitutes a "penalty," no rational class member would presume that a class representative would have had the right to waive these claims, and, more importantly, that he or she would be bound by any such waiver and unable to pursue a treble damages claim that he or she, like most absent class members, neglected to opt out.

The dissent next observed a class representative who purports to waive two thirds of his or her damage award cannot constitute an "adequate" class representative under the class action statute:

Finally, the unilateral waiver of a statutorily imposed penalty by a class representative adversely affects his or her ability to act as an adequate class representative (see *Small v. Lorillard Tobacco*, 94 NY2d 43, 54 [1999] [affirming finding that plaintiffs were not adequate class representatives where they limited their theory of recovery in 'significant ways' and limited their claim for damages 'in order to shape a legally de minimis theory of the case']). …Since the statute authorizes both actual (in the event the landlord rebuts the presumption of willfulness) and punitive damages, the named representative must seek both in order to adequately represent the interests of the proposed class…" (citation omitted).

The owners in the *Downing*, *Gudz* and *Borden* cases will all be moving the First Department for leave to appeal to the Court of Appeals. In *Roberts*, the Court of Appeals observed that its ruling left undecided "among other

things…retroactivity, class certification, statute of limitations, and other defenses that may be applicable to particular tenants." 13 N.Y.3d at 287. The question thus remains as to whether the First Department will allow the Court of Appeals to rule on the issue of whether rent stabilized tenants may waive their right to treble damages in order to maintain a class action.

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