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Stabilization Issue

First Department Splits on Waiver of Benefits
Warren A. Estis, a founding partner at Rosenberg Estis, and Jeffrey Turkel, a partner at the firm, write that landlords and tenants frequently enter into stipulations to settle their disputes. Enforcing such stipulations can be problematic, because both the Rent and Eviction Regulations and the Rent Stabilization Code contain provisions that generally bar tenants from waiving statutory benefits.

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Landlords and tenants frequently enter into stipulations to settle their disputes. In many of these stipulations, the tenant waives a right under rent control or rent stabilization in exchange for valuable consideration.

Enforcing such stipulations can be problematic, because both the Rent and Eviction Regulations[1] (rent control) and the Rent Stabilization Code[2] contain provisions that generally bar tenants from waiving statutory benefits. Section 2200.15 of the Rent and Eviction Regulations provides:

An agreement by the tenant to waive the benefit of any provisions of the Rent Law or these regulations is void.

Similarly, Section 2520.13 of the Rent Stabilization Code states in relevant part:

An agreement by the tenant to waive the benefit of any provision of the RSL or this Code is void; provided, however, that based upon a negotiated settlement between the parties and with the approval of the DHCR or a court of competent jurisdiction where a tenant is represented by counsel, a tenant may withdraw, with prejudice, any complaint pending before the DHCR.

In our column of May 2, 2001, we explored the question of when courts will or will not enforce such stipulations. The case law, however, took a new turn on April 20, 2006, when the Appellate Division, First Department, issued its determination in *Drucker v. Mauro*, 2006 WL 1028965. By a 3-2 margin, the Court ¿ ruling against the tenants and reversing Supreme Court ¿ held that "an agreement in purported or actual settlement of a landlord-tenant dispute which waives the benefit of a statutory protection is unenforceable as a matter of public policy, even if it benefits the tenant."

The Facts

In November 1981, John and Jacquelin Drucker moved into a rent-stabilized apartment at 432 East 58th Street in Manhattan. The lease was periodically renewed through Oct. 31, 1992.

For reasons not clear from the record, the owner failed to renew the lease in 1992, resulting in extensive negotiations between the parties concerning not only the renewal lease, but "the rent regulated status of the building . . . repairs and renovations that had been made; and the right to certain personal property in the Apartment."

The parties settled their differences years later in a renewal lease and rider commencing March 1, 1995. The rider to the renewal lease provided, inter alia, that the tenant would be entitled to perpetual two-year renewal leases at increases

equal to the current Rent Guidelines Board percentages. The rent was increased to $1,700 per month, which was higher, but not substantially higher, than it would have been had the parties simply renewed the 1992 lease. That lease stipulated a monthly rent of $1,529.

Notably, the rider to the renewal lease settled the owner's claim concerning approximately $6,675 in costs and expenses relating to various renovations made to the apartment in 1992. Assuming that all $6,675 was spent on new equipment and improvements (as opposed to ordinary repairs), and further assuming that the tenants were willing to pay a rent increase for such equipment and improvements (as the rider appears to suggest), the owner would have been able to increase the rent for the apartment by $166.88 per month, i.e., 1/40th of $6,675. The $166.88 figure alone virtually bridges the gap between the existing 1992 monthly rent ($1,529) and the monthly rent to which the parties agreed in 1995 ($1,700).

In February 1996, DHCR, in response to the owner's application, issued an order finding that the apartment in question was indeed rent stabilized. Thus, the apartment was subject to rent regulation at the time the parties entered into the 1995 lease and rider.

The 1995 lease was periodically extended through Novemberf 2000. In April 2002, when the rent was over $2,000 per month, the owner sought to luxury deregulate the apartment. DHCR ultimately issued an order deregulating the apartment in October 2003, on the ground that the tenants' income exceeded the $175,000 statutory threshold.

Once the owner began the deregulation process, however, the tenants commenced a Supreme Court action seeking (1) a declaration that the 1995 lease and rider were fully enforceable, particularly the perpetual renewal provision therein, and (2) an order permanently enjoining the landlord from deregulating the apartment or raising the rent beyond the rent level to which the parties agreed. The owner, inter alia, sought a declaration that the contested provision of the rider was void as against public policy.

In a Feb. 18, 2004 decision and order, Supreme Court (Kapnick, J.) refused to enjoin the luxury deregulation process, but held that the perpetual renewal provision was fully enforceable, notwithstanding the deregulation of the apartment in October 2003. Justice Kapnick held:

. . . defendant has not citied any authority for the proposition that the parties are barred under the Rent Stabilization Code from contractually agreeing to abide by certain provisions of the Code even if the premises are not otherwise subject to regulation or, as in the instant case, the premises became de-regulated through 'regular, officially authorized means.' This Court finds that no public policy is implicated in the enforcement of such a contract.

Supreme Court held, in essence, that landlords and tenants are free to agree that an apartment, upon lawful deregulation, may be treated as if it were rent stabilized with respect to renewals and rent increases. Supreme Court did not address the issue, however, of whether the parties were free to so contract while the apartment was still rent stabilized.

The First Department Majority

The owner, aggrieved by the enforcement of the lease and rider, appealed. In a majority opinion authored by Justice Peter Tom (and joined by Justices Angela M. Mazzarelli and Luis A. Gonzalez), the First Department reversed Justice Kapnick's order. The majority focused on the rent increase ¿ from $1,529 to $1,700 per month ¿ as a basis for voiding the contested provision:

To permit a landlord to exceed the legal regulated rent on the flimsy premise that a negotiated lease represents the settlement of a dispute with a tenant would invite ready circumvention of the regulatory scheme through selective invalidation of provisions of the Rent Stabilization Law, severely compromising the protection it was intended to afford and eventually eviscerating the entire Rent Stabilization scheme.

Central to the statutory scheme is preventing the exaction of excessive rents by landlords (*Estro Chem. Co. v. Falk*, 303 N.Y. 83, 87 [1951] ['The obtaining of excessive rents strikes at the very purpose of the act']).

The majority then focused on two additional factors. First, the rent increase ¿ even if agreed to by the owner and the tenant ¿ would prejudice future tenants of the apartment. Second, the Court looked at the issue of luxury deregulation:

The result of the enhanced rent paid by plaintiffs herein has been to prematurely subject the premises to luxury decontrol. Anomalously, the intended effect of the lease rider is to permanently remove the apartment from the operation of the Rent Stabilization Law's luxury decontrol provision, in violation of express statutory language deregulating affected units [citation omitted]. Simply, the enforcement of the lease and rider would preclude luxury decontrol of the unit, even after the rent exceeds $2,000, because landlord can only charge the rent provided in the agreement, not fair market value, in perpetuity.

The majority's ruling in this regard can be questioned in two respects. First, luxury deregulation based on high income is never guaranteed; here, it so happened that the tenants exceeded the income threshold (although that probably explains

why they wanted the perpetual renewal clause). Second, the contested provision did not prevent the apartment from being luxury deregulated ¿ DHCR in fact deregulated the apartment. It merely deprived the owner of the full benefits of luxury deregulation, such as the right to a market rent and the right to recover the space. It is not clear how the owner's waiver of such rights violates the spirit of the rent laws or adversely affects other renters.

The majority concluded by ruling that the policy of the Rent Stabilization Law was to protect tenants, and that tenants could not evade stabilization provisions even if they ultimately gained an advantage in doing so. The majority wrote:

Were the intent of Rent Stabilization Code §2520.13 to permit the tenant to avoid an agreement waiving statutory protection at his option, the regulatory language would undoubtedly so state. Instead, it simply provides that such agreements are 'void' as a matter of public policy [citation omitted].

The Dissent

The dissenting opinion, authored by Justice Richard T. Andrias, and joined by Justice David Friedman, began with the premise that settlements are to be encouraged unless public policy is violated. The dissent concluded that no such violation had occurred.

The dissent first observed that, in fact, there had been no agreement to deregulate the apartment:

Although it is well established that landlords and tenants are prohibited, on public policy grounds, from making private agreements to effectively deregulate rent-stabilized housing units . . . as the motion court correctly found, no violation of public policy is implicated in the enforcement of the parties' agreement, inasmuch as nothing in the agreement explicitly or implicitly deregulated the apartment in question. The motion court specifically found that the issue of whether the apartment should be luxury decontrolled is a question for DHCR, and, in fact, while the cross motions were pending before the court, DHCR granted defendant's application and luxury decontrolled the apartment on Oct. 31, 2003.

The dissent next addressed the issue of whether public policy was violated by the post-deregulation enforcement of the perpetual lease renewal and rent limiting provisions in the lease rider:

Thus, the apartment having been deregulated, not by the parties' agreement but by DHCR, the only question remaining before the motion court was whether the landlord of a previously rent-stabilized apartment may agree to offer his or her tenant renewal leases in perpetuity with rent increases that coincide with the amount of rent increases set by the Rent Guidelines Board for apartments that are still subject to rent stabilization.

Contrary to the majority's opinion, there is simply nothing in the rider to the parties' lease that indicates a waiver by the plaintiffs of any protection offered by the lawful stabilized rent for the apartment and their right to timely renewal of their lease.

The dissent then addressed the majority's argument that the lease and rider prejudiced future tenants of the subject apartment:

Likewise, the majority's fear that the higher rent presently paid by plaintiff may result in a future tenant having to pay more than the legal stabilized rent for this unit is totally unfounded. There is simply no question that the apartment in question has been luxury decontrolled by DHCR. Any future tenant will, as plaintiffs have already done, negotiate a fair market rent for the unit without recourse to the rent stabilization laws.

Because of the 3-2 split in the Appellate Division, the unsuccessful tenants have an as of right appeal to the Court of Appeals. Edward Cohn, the tenants' attorney, reports that the tenants have not yet decided whether to appeal.

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Endnotes:

1. 9 NYCRR 2200 et seq.

2. 9 NYCRR 2520 et seq.

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