Stipulations

Undone by Material Misrepresentations
Warren A. Estis, a founding partner at Rosenberg & Estis, and William J. Robbins, a partner at the firm, write that many landlord-tenant cases are resolved by a stipulation of settlement. The courts welcome stipulations of settlement as an efficient method of resolving litigation. Given the volume of cases in the trial courts, without stipulations of settlement, court calendars would be overwhelmed.

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Many landlord-tenant cases are resolved by a stipulation of settlement. The courts welcome stipulations of settlement as an efficient method of resolving litigation. Given the volume of cases in the trial courts, without stipulations of settlement, court calendars would be overwhelmed. In order to promote the use of such stipulations, they need to be accorded finality and not be easily avoided once entered into ¿ and that, indeed, is a basic principle which courts have applied to stipulations of settlement.

Nevertheless, there are circumstances, albeit rare, where courts find it proper to set aside a stipulation of settlement. A recent decision by New York County Supreme Court Justice Edward H. Lehner in *Century Realty Inc. v. Hyatt*[1] is an example of a situation where the court concluded that a consent judgment issued pursuant to a stipulation of settlement should be vacated and set aside. The court granted the motion by four tenants seeking such relief and denied the landlord's cross-motion for an order directing the Sheriff to turn over possession of the tenants' premises to it. The decision includes a discussion of various cases relevant to the issue of vacating stipulations of settlement and consent judgments based on such stipulations.

The case concerned the building at 142 Fulton Street in Manhattan. According to the tenants, since 1983, the building has contained at least six dwelling units, but admittedly none of the loft units was ever legalized for residential use by the tenants. In the early 1990's there were disputes between the tenants and the landlord concerning the tenants' right to remain in occupancy under the Rent Stabilization Law.

The controversy was resolved by a stipulation which the tenants, represented by counsel, entered into in June 1996. Pursuant to the stipulation, the tenants consented to entry of a judgment in an action to be commenced declaring that the various units they occupied are not subject to the Rent Stabilization Law, but allowing the tenants to remain in possession until June 30, 2006.

In relevant part, the stipulation stated that the tenants claimed to be subject to the Rent Stabilization Law; that the landlord would not issue renewal leases without first obtaining a declaration that the units are not subject to the Rent Stabilization Law; and that the building was "substantially rehabilitated for residential use after January 1, 1974 and the tenants did not complete the substantial rehabilitation."

Justice Lehner commented as follows concerning the reason for including in the stipulation the provision about substantial rehabilitation of the building:

> It appears that such provision was contained in the Stipulation in order to form a basis to exempt the Building from the RSL [Rent Stabilization Law] in light of the Appellate Division decision in *Wilson v. One Ten Duane Street Realty Co* . . . . In that case, where the tenants had in fact legalized their units for residential use, the court noted the statutory provision exempting from regulation any building that was 'substantially rehabilitated as family units on or after January 1, 1974.'[2]

Following the stipulation, the landlord served a complaint dated Aug. 29, 1996, which, as relevant here, alleged that the building was substantially rehabilitated subsequent to Jan. 1, 1974, with the tenants not having performed such work. Pursuant to the stipulation, a consent judgment, dated Oct. 24, 1996, was issued by Justice Paula J. Omansky. That judgment contained a declaration that the building was substantially rehabilitated for residential use after Jan. 1, 1974.

In 2004, a proceeding was commenced against one of the tenants, Richard Hyatt, on the grounds that he allegedly sublet his unit in violation of the stipulation. In defense, he argued that the stipulation was an impermissible waiver of rights under the Rent Stabilization Law and thus invalid. By decision dated Feb. 23, 2004, Justice Omansky rejected that defense.

In his recent decision, Justice Lehner stated that he agreed with the legal principle upon which Justice Omansky, in what he described as "an exhaustive opinion discussing the various cases," had rejected Hyatt's waiver defense. He summarized that legal principle as follows:

> . . . [A] court could enforce a stipulation with respect to coverage if parties, who were all represented by counsel, present a stipulation setting forth facts that raise a bona fide dispute as to whether a tenant, whose occupancy had never been acknowledged by the landlord or determined by a court or administrative agency as subject to the RSL, was entitled to its protection, with the caveat that the Rent Stabilization Code ('Code') §2523.3 specifically prohibits a landlord from requiring a 'prospective tenant' to agree that the apartment will not be the tenant's primary residence.[3]

The court commented that if that principle were not applied, then "any bona fide dispute on a question of coverage could never be resolved by the parties and would mandate that such disputes always be litigated."

The court contrasted a stipulation in the context of such a bona fide coverage dispute, on the one hand, with a stipulation whereby a tenant "covered by the rent laws" waived a right the tenant possessed under those laws, on the other hand. Citing *Drucker v. Mauro*,[4] *Draper v. Georgia Properties, Inc.*[5] and *Delano Village Company v. New York State Division of Housing and Community Renewal,*[6] the court pointed out that in the latter situation, a stipulation waiving rights would be void and unenforceable as against public policy because it attempted to circumvent the rent laws.

The court in *Century Realty Inc. v. Hyatt* emphasized that there was a significant difference between what had been raised before Justice Omansky and what was now before the court. Specifically, it was now "acknowledged by the Landlord that it did not substantially rehabilitate the building." The stipulated "fact" that the landlord had substantially rehabilitated the building for residential use after Jan. 1, 1974 was now admitted to be false, making it evident that the judgment had been "procured by a misrepresentation to the court of a material fact." This information, none of which had been before Justice Omansky, was of determinative significance to Justice Lehner.

Notwithstanding the misrepresentation, the landlord still wanted the court to enforce the judgment. The landlord's attorney asserted that since the judgment had been signed by Justice Omansky, the landlord was now entitled to evict the tenants. The court had a "major problem" with the landlord's position, namely:

> Even though the Stipulation contains both benefits and detriments to the Landlord and to the Tenants, the submission of a stipulation containing intentional misrepresentations as to an essential fact is, in essence, a fraud upon the court.
>
> Notwithstanding that misrepresentation, the Landlord now wants this court to enforce the Judgment. This I will not do as the integrity of the judicial system is at stake when judicial mandates are procured by the submission of fraudulent representations.[7]

Justice Lehner discussed three cases where courts had been faced with what he referred to as "a fraudulent scheme" concerning the rent laws, namely, *390 West End Associates v. Baron,*[8] *Thornton v. Baron*[9] and *390 West End Avenue Associates v. Youngstein.*[10] In *390 West End Associates v. Baron*, the landlord and tenant entered into a settlement agreement in which the tenant acknowledged that the apartment was not his primary residence and, therefore, exempt from the Rent Stabilization Law. As characterized by the court in *Century Realty*, this settlement agreement was:

> . . . part of a scheme whereby the tenant would then sublet the premises to others who would be required to state that they

also would not occupy the premises as a primary resident, with the result that the owner and prime tenant earned profits well above that authorized by the RSL.[11]

A consent judgment was entered declaring the exemption from the Rent Stabilization Law to which the tenant had agreed in the settlement agreement. The tenant subleased the apartment pursuant to a sublease that provided the subtenants would not use the apartment as their primary residence. However, they did use it as their primary residence, and subsequently suspended payment of rent and brought a rent overcharge action against the tenant. The landlord moved to vacate the consent judgment and rescind the tenant's lease so that it could offer a rent-stabilized lease to the subtenants.

The Appellate Division reversed the trial court and granted the motion to vacate the consent judgment, holding that "Rent Stabilization Code (9 NYCRR) §2520.13 states that an agreement to waive the benefit of any provision of the Rent Stabilization Law or Code is void." The court continued, however, that although it was "constrained to acknowledge that the lease is void," it was concerned that the landlord "may have benefited unjustly at the [subtenants'] expense." The appellate court, therefore, stated that its granting of the landlord's motion was without prejudice to the assertion of any claims among the parties and/or the subtenants "with respect to profits obtained in violation of the Rent Stabilization Law."

Thornton v. Baron was the rent overcharge action the subtenants brought against the tenant. The case reached the Court of Appeals where, in a decision by Chief Judge Judith Kaye, the court considered the issue of "establish[ing] the legal regulated rent for an apartment improperly removed from rent stabilization." The rent numbers recited in the decision reflect the extent to which "both the owner and the prime tenants earned profits far above what the Rent Stabilization Law allowed" as a result of what the Court of Appeals described as "defendants' fraudulent conduct."

In the 1992 lease, Baron agreed to rent a four-room apartment, for which the previous tenant had paid a stabilized rent of $507.85 per month, for an initial monthly rent of $2,400, with increases beginning after three years. Baron then subleased the apartment to the Thorntons for $3,250 per month, increasing to $3,500 after two years and then to $3,750 after three.

The Court of Appeals "agree[d] with Supreme Court and the Appellate Division majority" that, given these circumstances, "the default formula used by DHCR to set the rent where no reliable rent records are available was the appropriate vehicle for fixing the base rent Lease." The Court of Appeals refused to establish the legal regulated rent by reference to the annual registration statement that had been filed listing the rent charged to Baron. The court explained that the Baron lease "was void at its inception" since it reflected "an attempt to circumvent the Rent Stabilization Law in violation of the public policy of New York." Since the rent that lease "purported to establish was therefore illegal," the rent registration statement "listing this illegal rent was also a nullity."

The Court of Appeals recognized that its holding meant that the subtenants would benefit by having a lower legal regulated rent. They would benefit even though they "themselves had unclean hands," having participated with the prime tenant and owner of the building in falsely representing that they did not intend to use the apartment as their primary residence. Judge Kaye explained, however, that "the principle we establish here will apply equally to innocent renters looking to succeed illusory tenancies" and that the court had reached its conclusion "so that no wrongdoer may benefit at the expense of the public."

As described by Justice Lehner in *Century Realty*, the third case, *390 West End Avenue Associates v. Youngstein,* involved "a similar set of facts" as *390 West End Associates v. Baron.* There, too, a consent judgment was issued decontrolling the apartment on the basis that the named tenants would not be occupying the apartment as their primary residence. There, too, the actual occupants of the apartment (who were the daughter and granddaughter of the named tenants) did use it as their primary residence.

When the landlord subsequently commenced a lawsuit seeking relief against the actual occupants of the apartment, the Appellate Division affirmed the Supreme Court's dismissal of the lawsuit, commenting that:

> . . . [I]t is now apparent that the parties may have attempted to evade the Rent Stabilization Law and create an 'illusory tenancy' . . . Thus, plaintiff's [landlord's] status as a wrongdoer, in pari delicto, justifies the equitable denial of any affirmative relief to it in this action . . . The prior judgment which plaintiff obtained operates as a bar to this action. This disposition by us is without prejudice to the commencement of a proceeding to obtain a vacatur of that declaratory judgment before Justice McCooe [who had issued the consent judgment].[12]

In *Century Realty*, Justice Lehner noted that the case before him was different from the three cases just discussed. He stated that those three cases were cases "where the parties devised a fraudulent scheme in an effort to obtain rents in excess of that permitted by law." By contrast, Justice Lehner characterized what had occurred in *Century Realty* as follows:

[T]he parties in apparent good faith came to an agreement with respect to the subject loft units at a time when it was not absolutely clear that the occupancy would be protected by the RSL. To insure that the agreement would be approved by a court and be enforceable, they included the aforesaid misrepresentation of fact."[13]

Still, there had been misrepresentation of an essential fact which amounted "in essence" to "a fraud upon the court." Therefore, the court granted the tenants' motion to the extent of vacating and setting aside the consent judgment, and denied the landlord's cross-motion for an order directing the Sheriff to turn over possession of the tenants' premises to it. The court commented that this occurrence placed the parties "back into the positions that they occupied prior to the submission of the [consent] judgment" and allowed them to "now litigate based on facts, not fiction".

In short, this case shows that stipulations of settlement do not always put an end to litigation. There are considerations, such as the sanctity of the courts and the judicial process, that outweigh the interest in finality and case resolution.

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1. NYLJ, July 19, 2006, p. 22, col. 1 (Sup. Ct. N.Y. Co.).

2. Id. The case cited in the quoted passage, Wilson v. One Ten Duane Street Realty Co., is at 123 A.D.2d 198, 510 N.Y.S.2d 603 ((1st Dep't 1987). The statutory provision referred to is Unconsolidated Laws §8625(a)(5).

3. Id., at col. 2.

4. 814 N.Y.S.2d 43 (1st Dep't 2006).

5. 94 N.Y.2d 809, 701 N.Y.S.2d 322 (1999).

6. 245 A.D.2d 196, 666 N.Y.S.2d 617 (1st Dep't 1997).

7. NYLJ, July 19, 2006, p. 22, at cols. 2, 4.

8. 274 A.D.2d 330, 711 N.Y.S.2d 176 (1st Dep't 2000).

9. 5 N.Y. 3d 175, 800 N.Y.S. 2d 118 (2005).

10. 221 A.D.2d 292, 634 N.Y.S.2d 112 (1st Dep't 1995).

11. NYLJ, July 19, 2006, p. 22, at col. 2.

12. 221A.D.2d at 294.

13. NYLJ, July 19, 2006, p. 22, at col. 4.