Rent Overcharge: Supreme Court Tackles Four-Year Rule

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The four-year statute of limitations on rent overcharge claims—originally intended as a bright line rule to simplify the calculation of a tenant's legal rent—has been altered over the years to the point where application depends on the peculiar facts of each case. In the landmark decision of *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 where there is evidence of "fraud," DHCR may examine the rental history prior to the four-year look-back period. If fraud is found, DHCR can utilize the so-called "default rent formula" to establish the tenant's rent, a formula that will undoubtedly reduce the tenant's rent substantially.

What constitutes proof of fraud, however, is not wholly clear. In *Grimm*, the Court of Appeals addressed the issue as follows:

DHCR…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 (see Rent Stabilization Law §26 511[c][13])—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. As in *Thornton*, the rental history may be examined for the limited purpose of determining whether a fraudulent scheme to destabilize the apartment tainted the reliability of the rent on the base date.[1]

Following *Grimm*, tenants and tenant advocates have liberally claimed that any real or imagined irregularity in an apartment's rental history—whether a typographical error in a lease or a mistake in a rent registration—constitutes "fraud." In the recent case of *White v. New York State Division of Housing and Community Renewal*, 2013 WL 753516 (Sup. Ct. N.Y. Co.), DHCR, as affirmed by New York County Supreme Court (Schlesinger, J.), held that the tenant had failed to prove fraud, and dismissed the tenant's overcharge complaint.

'White'

In 2010, tenant Donavin White moved into an apartment at 511 W. 143rd St. in Manhattan. The tenant signed a one-year lease at $1,800 per month, and a one-year renewal at $1,880 per month. The leases stated that the apartment was not rent stabilized.

The tenant filed a rent overcharge complaint with DHCR on June 17, 2011. The owner answered that the apartment was deregulated based on high rent luxury decontrol. The owner explained that the apartment became vacant in 2005, when the lawful rent exceeded $2,000 per month. The owner also argued that the apartment had thereafter been re-rented at $2,300 per month between 2005 and 2007, and at $2,400 per month between 2007 and 2010. White then moved into the apartment at $1,800 per month.

The tenant responded by submitting a copy of the registration history for the apartment dating back to 2004. The 2004 registration showed that the apartment was rented to one "Kimberly Butter" at a monthly rent of $1,166.00; the 2005 registration showed the apartment to be permanently exempt due to luxury deregulation.

On Feb. 21, 2012, DHCR's rent administrator issued a determination stating in relevant part:

In response to the complaint, the owner stated that the subject apartment was deregulated as of 03/01/2005 because the legal regulated rent exceeded $2000.00. A copy of the vacancy lease with a begin date of 03/01/2005 that reflected a legal regulated rent of $2300.00 per month was attached to the owner's response. A copy of the owner's submission was forwarded to the tenant on 02/08/2012. The tenant did not dispute the owner's statements/submission.

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Based on the above and the DHCR database, the legal rent as of 03/01/2005 exceeded $2000.00. Therefore, the apartment became deregulated and is no longer protected by the Rent Stabilization Law and Code.

The Tenant's PAR

The tenant thereafter filed a petition for administrative review with DHCR asserting that the $2,300 per month rent in the 2005 lease was fraudulent because it represented an unlawful increase above the $1,166.00 monthly rent paid by the prior tenant. Citing *Grimm*, the tenant demanded that DHCR examine the entire rental history, based on what the tenant alleged was evidence of fraud.

DHCR, in turn, examined the rental history all the way back to 1984 and found a variety of inconsistencies, which the Supreme Court described as follows:

The 2002 registration reported a regulated rent of $400 for "Kimberly Butler." The 2003 registration reported a rent of $1,166 for "Kimberly Buffer." The 2004 registration was for the same amount, but the tenant's name was "Kimberly Butter." While surmising that the tenant was the same throughout that period and that the different names were mere typographical errors, the agency did note some inconsistencies between the leases described in 2002 and 2003. Specifically, both of those leases were described in the rent history as having commenced on September 1, 2002, yet one was a one-year lease and the other was a two-year lease.

Notwithstanding, DHCR ruled in its July 12, 2012 order that these inconsistencies did not amount to proof of fraud:

The Commissioner notes that the inconsistencies in the three Kimberly Butler registrations cannot be reconciled based on the record herein. However, comparing the Butler rent with the Cornelius rent [immediately before it], there is only about $100.00 increase which needs to be explained over and above the applicable statutory vacancy allowance and the lower of the two possibly applicable Guidelines increases. That gap could be explained by $4,000.00 worth of Individual Apartment Improvements…The Commissioner also notes that the increase in rent from $1,166.00 (reported as Kimberly Butler's last rent) to the [free market] rent of $2,300.00 in the exit registration is not explained in this record. After the applicable 20% vacancy allowance, there is a gap of $900.80 that could be filled with something like $36,032.00 worth of [Individual Apartment Increase] costs.

The commissioner then observed that notwithstanding these inconsistencies, the tenant had failed to produce evidence—such as information from prior tenants in the building—to support his claim of fraud. Thus, DHCR ruled that it could not look beyond the four-year look back period, and determined that there had been no rent overcharge.

The Article 78 Proceeding

In the subsequent Article 78 proceeding, the tenant submitted affidavits from current and former tenants of the building, all attesting to the fact that no one named "Kimberly Butler" ever lived in the subject apartment. The Supreme Court (Schlesinger, J.) held that the court could not consider these affidavits, which had not been submitted before DHCR. The court added, however, that the affidavits "lack credibility and do not constitute proof of fraud under *Grimm*."

The landlord, in turn, had submitted documentation which appeared to explain the "inconsistencies" that DHCR found in the rental history. As the Supreme Court wrote:

Specifically, he has offered leases, letters, a copy of a check and detailed billing records relating to Kimberly Butler. These documents confirm a lease in the name of Kimberly Butler from September 1, 2001 through August 31, 2002 at a monthly rent of $1,100.00 and a two-year renewal through August 31, 2004 at a monthly rental of $1,166.00, after which Ms. Butler wrote to the owner indicating her intent to vacate the apartment. The owner has also supplied copies of the registration statements relating to Ms. Butler that are consistent with the leases; the $400.00 figure listed in the rental history… appears to be a data entry error. This detailed evidence is far more persuasive than the vague letters submitted by the tenant.

The Supreme Court then addressed DHCR's speculation, in the challenged order, that individual apartment improvements may well have justified significant rent increases during the course of the apartment's rental history:

The tenant next argues that the Commissioner erred in justifying various rent increases by speculating that Individual Apartment Improvements (IAI) had been completed, when no evidence of those improvements had been offered by the owner. While it is true that the owner did not establish (nor even claim) that the rents charged were justified by an IAI, he was not required to do so because the increases at issue were outside the four-year period. The Commissioner properly distinguished Mr. White's case from *Grimm* on the ground that the tenant had not offered any evidence of a fraudulent scheme; the inconsistencies in the rent registration statements, which for the most part were typographical errors, did not constitute proof of fraud justifying a look-back beyond the four-year period. Thus, actual proof of IAI increases that predate the four-year period was not required.

Based upon the evidence of record, the Supreme Court determined that DHCR had correctly determined that the instant case was distinguishable from *Grimm*, such that the default rent formula should not be used:

In *Grimm*, ample evidence of fraud existed. For example, there was no base date lease. Further, the owner offered to charge the tenant a lower rent if the tenant made repairs himself. The lease did not include a rent stabilized lease rider, and the owner ceased filing registration statements. None of that evidence, nor anything similar, is present here to suggest a fraudulent scheme.

Based upon the peculiar facts of *White*, it is difficult to arrive at any hard and fast rule regarding *Grimm* or its application. Justice Alice Schlesinger, however, has made clear that the burden of proving "fraud" is squarely on the tenant, and that mere unexplained increases in rent, or seeming irregularities in prior registration statements, will not be enough.

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Endnote:

1. 15 N.Y.3d at 367.