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LANDLORD-TENANT LAW

Court of Appeals Facilitates Class Actions in J-51 Suits

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In three cases decided on Nov. 24, 2014, *Gudz v. Jemrock Realty*, *Downing v. First Lenox Terrace Assoc.*, and *Borden v. 400 East 55th Street Assoc.*, the New York State Court of Appeals held that tenants can waive their right to seek treble damages so as to bring class action proceedings for rent overcharge. These decisions were the latest in a series of setbacks for landlords before New York State's highest court. (Co-author Jeffrey Turkel represented the landlord in *Borden* before the Court of Appeals.).

'Roberts'

The three cases arise from the Court of Appeals' Oct. 22, 2009 decision in *Roberts v. Tishman Speyer Properties*, 13 NY3d 270 (2009). There, the court, by a 4-2 margin, held that landlords whose stabilized buildings were receiving J-51 tax benefits could not seek luxury deregulation while those tax benefits remained in effect.

In *Roberts*, the majority acknowledged that its decision left open a number of critical issues that would have to be determined by lower courts:

> Defendants predict dire financial consequences from our ruling, for themselves and the New York City real estate industry generally. These predictions may not come true; they depend, among other things, on issues yet to be decided, including retroactivity, class certification, the statute of limitations, and other defenses that may be applicable to particular tenants. If the statute imposes unacceptable burdens, defendants' remedy is to seek legislative relief.[1]

Those dire consequences have now largely come to pass. In *Gersten v. 56 7th Ave.*, 88 AD3d 189 (1st Dept. 2011), the First Department ruled that *Roberts* would be given retroactive effect. In *Borden*, *Gudz*, and *Downing*, the Court of Appeals itself, as detailed below, has facilitated class action proceedings arising from *Roberts*. Certainly, "legislative relief" has not been forthcoming.

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'Borden,' 'Gudz' and 'Downing'

Following the *Roberts* decision, various plaintiffs in J-51 buildings commenced putative class actions against their landlords, seeking, inter alia, (1) a declaration that apartments that had been luxury deregulated prior to *Roberts* were in fact rent stabilized, and (2) damages for overcharges that landlords had collected under the misimpression that luxury deregulation had been available.

In the Borden, Gudz and Downing cases, the plaintiffs initially sought treble damages in their complaints. Section 26-516(a) of the Rent Stabilization Law (RSL) authorizes an award of treble damages where overcharges have been willful, and states in relevant part:

> Subject to the conditions and limitations of this subdivision, any owner of housing accommodations who, upon complaint of a tenant…is found by the state division of housing and community renewal, after a reasonable opportunity to be heard, to have collected an overcharge above the rent authorized for a housing accommodation subject to this chapter shall be liable to the tenant for a penalty equal to three times the amount of such overcharge.
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> If the owner establishes by a preponderance of the evidence that the overcharge was not willful, the state division of housing and community renewal shall establish the penalty as the amount of the overcharge plus interest.

By seeking treble damages, however, the plaintiffs endangered the viability of their class actions. Class action litigation is governed by Article 9 of the CPLR. CPLR 901(b) bars a plaintiff from seeking a "penalty" in a class action and states in its entirety:

> Unless the 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

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by statute may not be maintained as a class action.

It was well settled that treble damages under the RSL constituted a penalty under law. As the First Department wrote in *H.O. Realty v. New York State Division of Housing and Community Renewal*, 46 AD3d 103, 108 (1st Dept. 2007):

> By any reasonable measure, treble damages amount to a substantial penalty. It is punitive in nature and obviously designed to severely punish owners who deliberately and systematically charge tenants unlawful rents, while deterring other owners of stabilized premises who might be similarly inclined (citation omitted).

To avoid the proscription in CPLR 901(b), the plaintiffs in *Borden*, *Gudz*, and *Downing* all subsequently "waived" their claims for treble damages, and instead sought compensatory damages, attorney fees and interest. The issue then arose as to whether such waiver was void as against public policy, contrary to the RSL, or contrary to section 2520.13 of the Rent Stabilization Code, which 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, or where a tenant is represented by counsel, a tenant may withdraw, with prejudice, any complaint pending before the DHCR.

The various Supreme Courts, and the Appellate Division, First Department, all held in *Borden*, *Gudz*, and *Downing* that a waiver of treble damages, made to avoid the proscription in CPLR 901(b), was permissible.[2] The issue then reached the Court of Appeals, which affirmed in all three cases by a 4-2 margin.[3]

The landlords, citing such Court of Appeals authority as *Estro Chemical, v. Falk*, 303 NY 83 (1951), *Riverside Syndicate v. Munroe*, 10 NY3d 18 (2008), and *Jazilek v. Abart Holdings*, 10 NY3d 943 (2008), argued that, as a matter of law and public policy, rent-regulated tenants cannot waive their rights under any circumstances, even where such waiver benefits the tenants. The majority disagreed, holding that the anti-waiver case law only pertains to bilateral, collusive waivers between landlords and tenants:

> …tenants may waive a provision unilaterally (not through an agreement with the landlord), and still comply with the letter and spirit of the law. The code says as much when it allows tenants to withdraw claims through a negotiated settlement, or with the approval of the DHCR or a court, or where the tenant is represented by counsel. Where courts have denied a tenant's waiver, the evidence demonstrated that the landlord and tenant were either colluding to de-regulate apartments or that the tenants were being manipulated by contracts of adhesion"(citations omitted).

The court continued:

> Here, there is no evidence that tenants are being coerced to waive the treble damage provision or that there is any collusion between the landlords and the tenants. The tenants by themselves, and in opposition to the landlords' wishes, are opting to waive treble damages because they believe they will be more protected through a class action that finds that deregulation was illegal and gives them compensation for the overcharges. This protects tenants and preserves rent regulation, fulfilling the most significant purpose of the RSL. The tenant's waiver here is unilateral, supported by court order, and made with representation by counsel.

The majority also wrote that the plaintiffs' waiver of treble damages was permissible in that it was unlikely that any landlord found guilty of rent overcharge in a Roberts-type situation would be liable for treble damages, due to the absence of willfulness:

> As the lower courts noted, treble damages would be unavailable to the tenants because a finding of willfulness is generally not applicable to cases arising in the aftermath of *Roberts*. For Roberts cases, defendants followed the Division of Housing and Community Renewal's own guidance when deregulating the units, so there is little possibility of a finding of willfulness. Only after the Roberts decision did the DHCR's guidance become invalid (citation omitted).

The Dissent

Judge Robert S. Smith authored the dissent, and was joined by Judge Eugene F. Pigott. The dissent held that the damages the plaintiffs sought but did not waive—compensatory damages, attorney fees, and interest—were all "penalties" under the RSL, such that CPLR 901(b) barred the class action lawsuits:

> Defendants argue that these are actions 'to recover a penalty' because the treble damage remedy in Rent Stabilization Law (RSL) §26-516(a) is not waivable; because even if it were waivable under the statute that authorizes it, Rent Stabilization Code §2520.13 prohibits a waiver; and because in any event, even without trebling, the remedy provided in RSL §26-516(a) is a penalty. None of these arguments is without merit, but I will not stop to consider the first two, because I am satisfied that the third is correct. An action under CPLR [sic] 26-516(a) to recover a rent overcharge, whether trebled or not, is 'an action to recover a penalty…created or imposed by statute' and therefore 'may not be maintained in a class action'" (citations omitted).

In so holding, the dissent relied on the language of RSL 26-516(a), which states that "[i]f the owner establishes by a preponderance of the evidence that the overcharge was not willful, the state division of housing and community renewal shall establish the penalty as the amount of the overcharge plus interest" (italics supplied). As Smith concluded:

> It could hardly be said more plainly that the authors of the RSL considered 'the amount of the overcharge plus interest'—without trebling—to be a 'penalty.'

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1.13 NY3d at 287.

2. See, *Borden v. 400 East 55th Street Assoc.,* 105 AD3d 630 (1st Dept. 2013); *Gudz v. Jemrock Realty Co.*, 2011 WL 2516324 (Sup Ct New York County), aff'd 105 AD3d 625 (1st Dept 2013); *Downing v. First Lennox Terrace Assocs*., 107 AD3d 86 (1st Dept. 2013).

3. The majority opinion was authored by Chief Judge Jonathan Lippman, who was joined by Judges Victoria A. Graffeo and Jenny Rivera. Judge Susan Read concurred in the result.