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RENT REGULATION

How Grim Is 'Grimm'?


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In *Grimm v. New York State Div. of Hous. and Community Renewal*, 15 NY3d 358 (2010), the Court of Appeals ruled that the four-year look-back period for determining a stabilized rent can be breached where a tenant establishes that the base rent was tainted by fraud; at the very least, where a tenant raises a colorable claim of fraud, the tribunal "has an obligation to ascertain whether the rent on the base date is a lawful rent."[1] The court wrote:

> 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 protection 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.[2]

This article will examine recent case law interpreting and applying *Grimm*.

Look-Back Period Intact

In *Boyd v. New York State Div. of Hous. and Community Renewal*, *110 AD3d 594* (1st Dept. 2013), rev'd 23 NY3d 999 (2014), the First Department, by a 3-2 margin, found that the tenant "had made a sufficient showing of fraud to require DHCR to investigate the legality of the base rent."[3] In her dissent, Justice Judith J. Gische, wrote:

> Petitioner's subjective belief that the [individual apartment improvements] could not have cost more than $5,000 does not satisfy her initial burden of showing that the fraud exception to the four-year statute of limitations should be applied, requiring DHCR to review a rent charged more than four years before her overcharge complaint. A conclusory claim, without more, is insufficient for the agency to disregard the four-year look back period established in the Rent Stabilization Law…
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> The majority's conclusions that the petitioner's letter triggered an inquiry eviscerates the four-year statutory rule whenever a tenant alleges fraud, even without any particularity. I do not believe that *Grimm* has such wide ranging implications.[4]

A unanimous Court of Appeals agreed with Gische. The court reversed the First Department and held that the "tenant failed to set forth sufficient indicia of fraud to warrant consideration of the rental

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history before the four-year statutory period."[5]

Not surprisingly, allegations of a fraudulent scheme to deregulate an apartment frequently arise in post-Roberts J-51 cases, where owners—who relied on DHCR's advice that luxury deregulation was available in buildings receiving J-51 benefits—decontrolled apartments, raised rents to market, offered non-stabilized leases, and stop registering units. In such circumstances, courts have been reluctant to follow *Grimm*.

Thus, in *Todres v. W7879*, 137 AD3d 597 (1st Dept. 2016), the First Department upheld the trial court's finding that "defendants did not engage in 'a fraudulent deregulation scheme to remove an apartment from the protection of rent stabilization.'" The First Department, ruling that the trial court "should not have looked at 'the rental history of the housing accommodation prior to the four-year period immediately preceding the commencement of the action,'" eliminated treble damages, and reduced the overcharge award from $131,042 to $2,618.

In revoking treble damages in *Todres*, the First Department relied on *Borden v. 400 E. 55th St. Assoc.*, 24 NY3d 382 (2014). There, the Court of Appeals held that tenants could waive treble damages in J-51 cases in order to maintain those cases as class actions. In so holding, the court held that the waiver of treble damages was of little moment, because in post-Roberts cases, landlords "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."[6] Under such logic, it would be difficult to make a finding that such erroneous deregulation was the product of a fraudulent scheme.

In *Gomez v. Rossrock*, 2016 WL 94579 (Sup. Ct. NY Co.), another J-51 case, the tenant asked the court to go beyond the statutory four-year look back period preceding his occupancy based on the landlord's alleged fraudulent scheme to deregulate the unit. The Supreme Court (Mendez, J.), disagreed, writing:

> There is no proof that defendants attempted to circumvent the RSL. Rather, the defendants relied on DHCR's regulations when they deregulated the premises pursuant to renovations and vacancy. After the Roberts decision the defendant re-stabilized the premises and provided plaintiff with a rent-stabilized lease.

A survey of post-Grimm cases establishes that courts are still struggling to determine when a tenant has raised a colorable claim of fraud, or has established a fraudulent scheme to deregulate.

See also *Cohen v. 305 Riverside Corp.*, 2014 WL 1314822 (Sup. Ct. NY Co.) ("the evidence and allegations made in regard to defendant's J-51 benefits do not constitute sufficient evidence of a fraudulent scheme to destabilize").

Other cases have turned on landlord errors or missteps that fall short of a fraudulent scheme to deregulate. In *B-U Realty Corp. v. Kiebert-Boss*, 50 Misc.3d 1220(A) (NYC Civ. Ct. 2016), the tenant alleged fraud based on, inter alia, erroneous registration statements that overstated the rent. The court (Kraus J.), declining to invoke *Grimm*, held:

> While the original registrations were improper and listed inflated amounts, petitioner never sought to collect these amounts, and cured the impropriety by the amended filing. This does not establish the colorable fraud required to go back ten years to 2006 as respondent argues.[7]

Other cases have turned on the tenant's burden of proving a fraudulent scheme to deregulate. In *245 Owner LLC v. Yaghoobian*, 2015 WL 4366191 (NYC Civ. Ct.), the tenant submitted the affidavit of an architect who claimed that the owner, when establishing the legal rent for the apartment, had overstated the amount of individual apartment improvements.

The court held that the architect had failed to establish any particular expertise with respect to such matters, and that a "non-expert assessment is…. insufficient to raise an issue of material fact that petitioner has engaged in fraudulent conduct."

In *Grimm*, the Court of Appeals held that a mere "bump" in the rent is not sufficient to establish fraud. In *IWC 879 Dekalb, LLC v. Walsh*, 46 Misc.3d 1227 (A) (NYC Civ. Ct. 2015), Judge Andrew Lehrer found no indicia of fraud where the tenants merely alleged that "there was a rent increase in 2003 (or 2004) that exceeded the amount permitted by the Rent Guidelines Board."

Look-Back Period Breached

In *Conason v. Megan Holding*, 109 AD3d 724 (1st Dept. 2013), aff'd as modified 25 NY3d 1 (2015), the trial court found that the landlord had fraudulently listed a non-existent tenant as the prior occupant of the unit, and had claimed non-existent improvements to the apartments to inflate the rent. The First Department affirmed the trial court's finding of a fraudulent scheme to deregulate. The Court of Appeals thereafter affirmed. The Court of Appeals held that the tenants had "alleged substantial evidence pointing to the setting of an illegal rent in connection with a stratagem devised by Megan to remove tenants' apartments from the protection of rent stabilization."[8] Indeed, it would be hard to imagine a more blatant attempt to fraudulently deregulate an apartment than the use of a non-existent tenant and phantom improvements.

In *Altschuler v. Jobman, 478/480*, 135 AD3d 439 (1st Dept. 2016), the First Department applied *Grimm* based on a finding that the landlord engaged in a fraudulent scheme to deregulate by "executing market rent leases during a time it was receiving J-51 benefits, failing to provide [tenant] with a lease rider, and failing to file the required annual registrations with DHCR during his tenancy."[9]

It is often the case that there is insufficient evidence in the record to determine whether the tenant has raised a colorable claim of fraud, or whether the landlord has engaged in a fraudulent scheme to deregulate the apartment.

Further Discovery Required

It is often the case that there is insufficient evidence in the record to determine whether the tenant has raised a colorable claim of fraud, or whether the landlord has engaged in a fraudulent scheme to deregulate the apartment. In *Meyers v. Four Thirty Realty*, 127 AD3d 501 (1st Dept. 2015), a substantial increase in the apartment's rent was based on "unspecified improvements," and various leases and other documents relating to the rental history were not in the record. The First Department held that the issue of whether *Grimm* applied would have to await further discovery "'for the limited purpose of determining whether a fraudulent scheme to destabilize the apartment tainted the reliability of the rent on the base date.'"[10] See also *Tabak Assoc. v. Vargas*, 48 Misc.3d 143(A) (App. Term 1st Dept. 2015).

A survey of post-Grimm cases thus establishes that courts are still struggling to determine when a tenant has raised a colorable claim of fraud, or has established a fraudulent scheme to deregulate. *Boyd* and *Conason* demonstrate that the Court of Appeals requires real proof, but will not hesitate to breach the four-year look back period where such proof has been supplied.

1. 15 NY3d at 366.
2. Id. at 367.
3. 110 AD3d at 595.
4. Id. at 598.
5. 23 NY3d at 1001.
6. 24 NY3d at 398.
7. 2016 WL 94579 at *2.
8. 25 NY3d at 17.
9. 135 AD3d at 440.
10. 127 AD3d at 502.