Profiteering

Split Panel Finds Code Does Not Allow Eviction

BY WARREN A. ESTIS AND JEFFREY TURKEL

In *First Hudson Capital, LLC v. Seaborn*, NYLJ, Aug. 7, 2008, at 35, col. 1 (1st Dept.), a bare majority of the Appellate Division, First Department held that §2525.7(b) of the Rent Stabilization Code does not permit a landlord to evict a tenant who has charged his roommates a disproportionate share of the stabilized rent. The ruling, in turn, reversed an earlier split decision by the Appellate Term, First Department.[1]

Facts

Ron Seaborn is the rent stabilized tenant of an apartment at 208 West 30th Street in Manhattan. It appears that for a period of three years, the tenant advertised in the Village Voice for a roommate. He charged one of his roommates virtually the entire stabilized rent. Once, when he had two roommates simultaneously, he collected almost twice the rent.

Seaborn moved into the apartment in 1976, when it was commercial space. He invested thousands of dollars in the apartment to legalize it (including plumbing and legal work) and to obtain stabilization status.

Civil Court

The landlord, upon discovering the tenant's actions, commenced a summary holdover proceeding against Seaborn under §2525.7(b) of the Rent Stabilization Code. That section, added to the Code in December of 2000, states in relevant part:

> The rental amount that a tenant may charge a person in occupancy pursuant to section 235-f of the Real Property Law [the so-called "Roommate Law"] shall not exceed such occupant's proportionate share of the legal regulated rent charged to and paid by the tenant for the subject housing accommodation (material in brackets supplied).

A trial was held before Civil Court Judge Gerald Lebovits, who issued a judgment of eviction in favor of the landlord. The court found that the tenant had "lied and recanted his testimony" both at trial and at a post-trial hearing, and concluded that the tenant had engaged in profiteering in connection with his stabilized apartment. The tenant thereafter appealed.

Appellate Term

On March 30, 2007, the Appellate Term, First Department, by a 2-1 margin, affirmed Civil Court. The majority, consisting of Justices Douglas McKeon and Martin Schoenfeld, credited Civil Court's factual findings, and held that "the tenant's commercial exploitation of his stabilized apartment required eviction...."[2] In so holding, Appellate Term favorably cited *West 148 LLC v. Yonke*, 11 Misc.3d 40, 812 N.Y.S.2d 735 (1st Dept. 2006), one of several Appellate Term decisions affirming an owner's right under §2525.7(b) to evict a tenant found to have engaged in profiteering at the expense of a roommate.

Justice William P. McCooe dissented, observing that while §2525.7(b) prohibited a tenant from overcharging a roommate, it did not authorize a landlord to evict such a tenant. Justice McCooe favorably cited *SBR Assocs. LLC v. Diederich*,[3] a 2003 determination of the Appellate Term for the Ninth and Tenth Judicial Districts, wherein that court noted that DHCR had taken the position that the code provision in question was intended to vest the roommate with the right to file a complaint against the tenant, but not to create an independent cause of action for eviction.

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RENT REGULATION

The dissent argued that if a tenant could not be evicted for violating §2525.7(b), the section had little or no point.... The dissent then wrote that its interpretation of §2525.7(b) would not only give the section meaning, but would actively discourage the conduct the Code drafters sought to prohibit.

The Appellate Division

The case then moved to the Appellate Division, First Department. In a per curiam opinion joined by Justices Angela M. Mazzerelli, Richard T. Andrias and John W. Sweeny, Jr., the majority reversed Appellate Term and found for the tenant. The majority, echoing Justice McCooe's analysis, wrote:

> Since it became effective December 20, 2000, Rent Stabilization Code §2525.7(b) makes it a violation to charge a roommate more than a proportional share of the rent. However, unlike RSC §2525.6(f), which permits an owner to terminate the tenancy of the tenant who charges his subtenant more than the legal regulated rent plus no more than 10 percent if the apartment is sublet fully furnished, RSC §2525.7(b) does not provide for termination of the lease. Prior to enactment of RSC §2525.7, it was the firm rule in this Department that '[t]here is no cause of action for rent profiteering with respect to a roommate' (*Handwerker v. Ensley*, 261 AD2d 190, 191 [1999])" (internal citations omitted).

The majority then addressed an Appellate Term decision, *West 148 LLC v. Yonke*, supra, which stated outright that a tenant's violation of §2525.7(b) was grounds for eviction, as well as an Appellate Division, First Department case, *54 Green St. Realty Corp. v. Shook*,[4] which seemed to imply such a result.

> While the 20-year tenant, who originally moved into commercial space and invested thousands of dollars in improvements in order to gain rent stabilized status, concededly advertised for roommates in the Village Voice and charged them more than their proportional share of the rent, this is not a case like *West 148 LLC v. Yonke*, where the tenant rented a portion of the stabilized apartment at double the regulated rent to a series of guests or 'roommates' and described the apartment, in both an Internet listing for 'Affordable Hotels' and on her business card, as the 'Chez Sylvie Bed & Breakfast.' It is closer to *54 Green St. Realty Corp. v. Shook*, where the tenant erroneously, but not unreasonably, believed that he was entitled to some compensation for the improvements he made to the former loft space. In any event, to the extent that those cases presuppose a cause of action for eviction by the landlord, they should not be followed."

The dissenting opinion was authored by Justice David B. Saxe, and joined by Justice Luis A. Gonzalez. The dissent argued that if a tenant could not be evicted for violating §2525.7(b), the section had little or no point:

> The provision of the Rent Stabilization Code applicable to overcharging roommates, 9 NYCRR 2525.7(b), was enacted in 2000. Unlike the section's counterpart regarding overcharging subtenants, 9 NYCRR 2525.6, which authorizes both an award of treble damages to the overcharged tenant (RSC §2525.6[b]) and the termination of the lease of the prime tenant (RSC §2525.6[f]), the enactment regarding overcharging roommates contains no specific provision

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for how it may be enforced, or by whom.

Although RSC §2525.7 contains no enforcement provision, it cannot seriously be suggested that it was intended to stand merely as an empty prohibition with no means of enforcement. Since enactment of the provision, Appellate Term, First Department has considered the issue in several cases and has concluded that RSC §2525.7 supports a judgment of eviction in appropriate roommate-profiteering cases. Indeed, in two of those cases this Court has denied leave to appeal, which, although not a determination on the merits, indicates that we perceive no grave error in the rule enunciated in those cases" (internal citations omitted).

The dissent then wrote that its interpretation of §2525.7(b) would not only give that section meaning, but would actively discourage the conduct the Code drafters sought to prohibit:

I add that there is a significant policy rationale for permitting eviction of a rent stabilized tenant who profiteered from roommates. When a tenant sublets, the landlord is entitled to demand an array of information, including a copy of the sublease, whereas the landlord has no right to any such information with respect to a roommate beyond the name of the new occupant (Real Property Law §235-f[5]). With so little oversight over roommate arrangements, the possibility of profiteering from roommates will be better kept in check where tenants have reason to know that forming such an arrangement in violation of the Rent Stabilization Code may result in the serious penalty of eviction rather than merely having to pay back rent overcharges.

The dissent concluded:

I therefore reject the suggestion that eviction of tenants for overcharging roommates is never permitted because the regulation does not specifically authorize such a cause of action. Rather, I would adopt the rule stated by the Appellate Term, First Department, and implied in this Court's previously discussed cases: RSC §2525.7 must be read to permit a cause of action to evict a rent-stabilized tenant who overcharges roommates, where overcharges have been found to constitute the commercial exploitation of the tenant's rent-stabilized apartment through the use of intentional profiteering.

Because there were two dissents in the Appellate Division, the defeated landlord would have an appeal as of right to the Court of Appeals. It remains to be seen whether the landlord will prosecute that appeal, or how the Court of Appeals might rule.

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1 *First Hudson Capital, LLC v. Seaborn*, 15 Misc.3d 40, 833 N.Y.S.2d 834 (App. T. 1st Dep't 2007).

2 15 Misc.3d at 41.

3 *SBR Assocs., LLC v. Diederich*, 2003 N.Y. Slip. Op. 51057 [U], 2003 WL 21513200 (App. T. 9th & 10th Jud. Dists.).

4 8 A.D.3d 168, 779 N.Y.S.2d 77 (1st Dep't 2004), lv. denied 4 N.Y.3d 704, 792 N.Y.S.2d 1 (2005).