Rent Gouging

Courts Unsympathetic to Tenants Who Overcharge
Warren A. Estis, a founding partner at Rosenberg Estis, and Jeffrey Turkel, a partner at the firm, write that the Rent Stabilization Law is intended to protect tenants from "unjust, unreasonable and oppressive rents." But what happens, they ask, when a tenant overcharges his or her subtenant?

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The Rent Stabilization Law is intended to protect tenants from "unjust, unreasonable and oppressive rents."[1] But what happens when a tenant overcharges his or her subtenant? The answer, as clarified in the recent cases of *30-40 Assocs. Corp. v. Cuervo*, N.Y.L.J., June 26, 2007, at 28, col. 1 (App. T. 1st Dep't) and *643 Realty, LLC v. Thadal*, N.Y.L.J., Apr. 18, 2007, at 30, col. 2 (App. T. 2d Dep't), is that the tenant may well be evicted.

Before discussing the recent Appellate Term decisions, some history is in order.

'Continental'

The seminal subleasing overcharge case is *Continental Towers Ltd. Partnership v. Freidman*, 128 Misc.2d 680, 494 N.Y.S.2d 595 (App. T. 1st Dep't 1985). In *Continental*, the tenant obtained his landlord's consent to sublease his apartment for $724.56 per month, i.e., 10 percent above the rent recited in the prime lease. Notwithstanding a written sublease agreement setting forth that rent, the tenant actually charged his subtenant $1,500 per month. When the landlord found out, it sued to evict the tenant. Civil Court (Brandveen, J.) held that the tenant had substantially violated the lease, but in view of his purported "cure," declined to order his eviction.

Appellate Term pointedly reversed, holding:

> *We disagree with so much of the decision below as permanently stayed issuance of the warrant. The cure provision contained in subdivision 4 of RPAPL § 753 is not to be rotely applied in all cases [citation omitted], and we think a cure in these circumstances would not be in furtherance of the public interest. The Rent Stabilization Law was enacted, in part, 'in order to prevent exactions of unjust, unreasonable and oppressive rents and rental agreements and to forestall profiteering, speculation and other disruptive practices. . .' which were then prevailing due to an acute shortage of dwelling space [citation omitted]. The integrity of the rent stabilization scheme is obviously undermined if tenants, who themselves are the beneficiaries of regulated rents, are free to sublease their apartments at market levels and thereby collect the profits which are denied the main landlord.*
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> *This practice, which the Rent Stabilization Law was designed to prevent, is not to be condoned by permitting the tenant to remain after the fraud has been found out.*[2]

Rent Stabilization Code

In May of 1987, DHCR promulgated an amended Rent Stabilization Code. Section 2525.6(b) of the Code provides that "[t]he rental charged to the subtenant by the tenant shall not exceed the legal regulated rent plus no more than a ten percent surcharge payable to the tenant if the housing accommodation is sublet fully furnished." Section 2625.6(f) provides that a landlord "may terminate the tenancy of a tenant who sublets contrary to the terms of this section. . . ."

A Nuanced View

The position staked out by Appellate Term in *Continental* - that rent gouging equals eviction - proved too draconian for other courts facing different fact patterns. In *Husda Realty Corp. v. Padien*, 136 Misc.2d 92, 518 N.Y.S.2d 99 (N.Y.C. Civ. Ct. 1987), the tenant sublet her stabilized apartment without permission, and charged her subtenant more than twice the legal rent. Upon receiving a notice to cure, however, the tenant refunded the overcharge to the subtenant, who promptly vacated. Judge - now Justice - Peter Tom held that the court had no jurisdictional basis to evict the tenant. Judge Tom reasoned that once the tenant cured, the landlord had no right to terminate the tenancy, such that the notice of termination was without any effect.

In *Alverjan Holding Corp. v. Weiss*, N.Y.L.J., May 19, 1994, at 27, col. 4 (App. T. 1st Dep't), Appellate Term declined to evict an overcharging tenant, citing the "short-lived and unintended rent overcharge by the tenant against her authorized subtenant," which was "summarily resolved by and between those parties." The liberalizing trend continued in *Ariel Assocs., L.L.C. v. Brown*, 271 A.D.2d 369, 706 N.Y.S.2d 116 (1st Dep't 2000), wherein the Appellate Division, affirming Appellate Term, held that the landlord's "claim that respondents should be evicted for profiteering was properly rejected on the ground that the summer subletting complained of did not rise to a level of profiteering warranting termination of respondents' 20-year tenancy without giving them an opportunity to cure [citations omitted]."[3] The Appellate Division also observed that "respondents properly refunded all sums to the subtenants and notified petitioner of the cure prior to the commencement of holdover proceedings [citations omitted]."[4]

Evictions Authorized

In *BLF Realty Holding Corp. v. Kasher*, 299 A.D.2d 87, 747 N.Y.S.2d 457 (1st Dep't 2002), the Appellate Division, First Department, analyzing the history of tenant overcharge cases, noted in passing that "[w]here there has been a substantial surcharge, the tenant cannot cure the lease violation."[5] The Appellate Division, Second Department put that observation to use the following year in *151-155 Atlantic Ave, Inc. v. Pendry*, 308 A.D.2d 543, 764 N.Y.S.2d 852 (2d Dep't 2003). In *Pendry*, Civil Court authorized the eviction of the overcharging tenant, but Appellate Term permanently stayed the warrant of eviction based on the tenant's "cure." The Second Department reversed Appellate Term, holding:

> *Under RPAPL 753(4), a tenant has 10 days to cure the breach of a lease provision. While the statute authorizes the Civil Court to impose a permanent injunction in favor of the tenant, precluding forfeiture of the lease upon the tenant curing the breach within the 10-day period, RPAPL 753(4), is not to be mechanically applied to defeat the purpose of the rent stabilization provisions.*
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> *Where, as here, there has been a substantial surcharge by the tenant, the tenant should not be permitted to cure the lease violation. The conduct of a profiteering rent-stabilized tenant 'is not to be condoned by permitting the tenant to remain after the fraud has been found out'(internal citations omitted).*[6]

'Cuervo' and 'Thadal'

In 643 *Realty LLC v. Thadal*, decided this past April, the Appellate Term, Second Department affirmed Civil Court's eviction of a tenant who had substantially overcharged her subtenant:

> *In this holdover proceeding based, inter alia, on a claim that the tenant sublet her apartment for an amount in excess of that permitted under the Rent Stabilization Code. . . the record shows, contrary to tenant's contention, that the tenant's profiteering was not insubstantial, as she charged her subtenant far in excess of the $492.41 monthly rent. Such conduct was not subject to a post-judgment cure (see Matter of 151-155 Atlantic Ave., Inc. v. Pendry, 308 AD2d 543 [2003]), and service of a 10-day notice to cure, required by the lease for defaults thereunder, was not required, since this proceeding was based not upon a default under the lease but upon tenant's violation of RSC § 2525.6(b).*

In *30-40 Assoc., Corp. v. Cuervo*, decided on June 20, 2007, the Appellate Term, First Department held to similar effect:

The evidence, fairly interpreted, supports the trial court's finding that tenant substantially overcharged his subtenant in violation of RSC § 2525.6(b). We agree that tenant should not be permitted to cure the lease violation, inasmuch tenant collected nearly three times the stabilized rent and failed to refund the overcharge [citation omitted].

The case law makes clear that these cases will be decided on their individual facts; no court has clarified when an overcharge will or will not be deemed "substantial." In any event, practitioners representing tenants, if they hope to preserve their client's tenancy, should direct their client to "cure" the violation as soon as possible. Practitioners should also note that RSC §2525.6(f) calls for a penalty of treble damages against the overcharging tenant, irrespective of whether the overcharge is willful. See, *Gboizo v. New York State Division of Housing & Community Renewal*, 13 Misc.3d 714, 820 N.Y.S.2d 789 (Sup. Ct. N.Y. Co. 2006).

Roommates

It should be observed that RSC § 2525.7(b) prohibits a tenant from charging a roommate (as opposed to a subtenant) more than "such occupant's proportionate share of the legal regulated rent charged to and paid by the tenant." Cases interpreting this section establish that tenants who overcharge their roommates may or may not be subject to eviction, depending upon (1) whether they have commercially exploited their apartments, and (2) the amount of the overcharge. See, *54 Greene Street Realty Corp. v. Shook*, 8 A.D.3d 168, 779 N.Y.S.2d 77 (1st Dep't 2004); *Roxborough Apts. Corp. v. Becker*, 11 Misc.3d 99, 816 N.Y.S.2d 810 (App. T. 1st Dep't 2006); *West 148 LLC v. Yonke*, 11 Misc.3d 40, 812 N.Y.S.2d 735 (App. T. 1st Dep't 2006).

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Endnotes:

1. RSL § 26-501.

2. 128 Misc.2d at 681-82.

3. 271 A.D.2d at 369-70.

4. 271 A.D.2d at 370.

5. 299 A.D.2d at 91.

6. 308 A.D.2d at 543-44.
