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Inside

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How Assignment Restrictions in Leases Apply to Corporate Transactions

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I. Introduction

In any corporate merger, acquisition, or other change in ownership, the target company's space leases[1] will often prohibit[2] assignment and potentially other similar transactions. These restrictions may create issues for and impede a corporate transaction. In extreme cases, they may entirely prevent a transaction from closing. Whether any of these problems arise will depend primarily on the exact words of the leases and what those words mean.

Therefore, if a target company holds important leases,[3] the assignment restrictions in those leases may require substantial and very focused early attention in due diligence and contract negotiations. And any participant in a corporate transaction of this type will care very much about the answers to these questions:[4]

- What should counsel look for when reviewing assignment restrictions in space leases?
- What do the more common assignment restrictions mean?
- How do assignment restrictions affect mergers or other particular types of corporate transaction?
- Do similar principles apply to restrictions on subletting?[5]

This article tries to answer those questions. After summarizing the basic legal principles that govern this area, this article defines some important categories, then analyzes how courts treat certain transfer restrictions that commonly appear in space leases.

This article considers both New York law and general American "common law" principles. It also discusses whether a landlord must be reasonable when giving or denying consent to an assignment or sublease (if the lease requires landlord consent to a particular transaction), and, if so, what "reasonable" means.

II. Overview and Some Definitions

These general common law principles form the basic foundation and starting point for the present discussion:

- **Restraints on Alienation**—Restrictions against assignment and subletting are regarded as restraints on alienation, which the courts generally disfavor. The courts therefore construe these restrictions "strictly," in favor of free alienability.[6]
- **Forms of Alienation**—A covenant against one form of alienation does not prohibit another form.[7] For example, a covenant against assigning does not preclude subletting, pledging, or mortgaging.[8]

Starting from those general principles, these defined terms will apply throughout the discussion:

- **"Basic Assignment Restriction"** refers to an ordinary generic provision in a lease that generally prohibits a lease assignment (or requires landlord consent for such an assignment). Any such restriction does not single out particular types of assignments or specify other types of transfers that are prohibited. It merely says the tenant may not assign the lease.
- **"Advanced Assignment Restriction"** refers to provisions in a lease that prohibit particular types of assignments. For example, restrictions on the transfer of control of a corporation or assignments "by operation of law"[9] are Advanced Assignment Restrictions.
- **"Assignment Restriction"** refers to Basic Assignment Restrictions and Advanced Assignment Restrictions together.
- **"Subletting Restriction"** refers to an ordinary generic provision that generally prohibits all subletting of all or part of the leased property without landlord consent.
- **"Transfer Restriction"** refers to Assignment Restrictions and Subletting Restrictions together.

This article addresses the following four issues of law and reaches the conclusions summarized below.[10] For any individual transaction, of course, the conclusions in this article will need to be confirmed, taking into account the specific facts, circumstances, and leasing documents at issue.

A. Stock Transfers

Q: Do Basic Assignment Restrictions prohibit stock transfers of a corporate tenant?

A: No, unless the lease contains an Advanced Assignment Restriction that specifically prohibits such transfers.

B. Assignments "By Operation of Law"

Q: Do Basic Assignment Restrictions prohibit assignments "by operation of law"?

A: No. An assignment "by operation of law" will not violate the lease unless the lease contains an Advanced Assignment Restriction that specifically prohibits such assignments.

C. Mergers

Q: Do Basic Assignment Restrictions prohibit mergers of a corporate tenant?

A: No. A corporate merger will not violate the lease unless it contains an Advanced Assignment Restriction that specifically prohibits mergers—either explicitly or as assignments or transfers "by operation of law."

D. Reasonableness in Denying Consent

Q: If a Transfer Restriction sets no standard for the landlord's consent, must the landlord act reasonably in refusing consent? If so, what standard of "reasonableness" must the landlord satisfy?

A: Only a minority of jurisdictions require landlords to be reasonable. Even where the courts require it, no single standard defines "reasonableness." The cases, and there are many of them, offer some clues.

Important Note: While the above answers represent majority viewpoints, there are exceptions and minority viewpoints (some of which amount to "emerging trends") relating to most of the above issues. Moreover, any individual judge can usually find some basis to decide any particular case in whatever way the judge sees fit. Any potential participant in a transaction should therefore consult current case law in each applicable jurisdiction. Moreover, in negotiating leases and corporate transactional documents, the parties should not leave these issues for a court to decide.

III. Stock Transfers

Under general legal principles, the sale or transfer of a corporate tenant's stock does not violate a Basic Assignment Restriction.[11] This is because a corporation exists separately from its stockholders. Thus, while the owners of a corporation may transfer the company's stock, this does not change the actual tenant under the lease, which was, is, and remains exactly the same corporation.[12] Courts have applied this rule even where a landlord has previously disapproved a proposed lease assignment, and the rejected assignee then proceeded to purchase the stock of the corporate tenant[13]—a transparent and brazen attempt to "get around" the assignment prohibition. New York courts have (in a few cases on point) generally followed the precedent of other jurisdictions on this question.[14]

A landlord may, if it wants, try to prohibit a de facto assignment of the lease through a stock transfer. To do this, the landlord must draft an Advanced Assignment Restriction that specifically forbids transfer of control of the tenant corporation.[15] Although such provisions have been enforced,[16] they restrict alienation of property and courts will construe them strictly against the landlord.[17] For example, a clause whose language bars the transfer of existing stock may be held to allow the creation and sale of new stock, the issuance of which is enough to change control of the corporation.[18] Although New York courts have not considered Advanced Assignment Restrictions that specifically prohibit the transfer of a corporate tenant's stock, one case suggests that such clauses would be enforceable under New York law.[19] In any event, such restrictions may be of unreliable enforceability or value where a corporation has many shareholders. In one case, for example, a court disregarded these restrictions where, when the lease was signed, 40 percent or more of the corporation's stock was owned by over a dozen shareholders.[20]

If the tenant is a limited liability company ("LLC"), but the lease prohibits stock transfers or partnership transfers and says nothing about transfers of LLC membership interests, the courts would probably allow a transfer of the LLC interests. Courts dislike Assignment Restrictions and will construe them strictly. Therefore, courts would probably say that if the landlord wanted to prohibit transfer of LLC interests, the landlord should have said so in the lease.

IV. Assignments by "Operation of Law"

Many commercial leases prohibit assignments by "operation of law." To understand these restrictions, one must first define an assignment by "operation of law." *Black's Law Dictionary* defines "operation of law" as follows:

> The manner in which rights, and sometimes liabilities, devolve upon a person by the mere application to the particular transaction of the established rules of law, without the act or cooperation of the party himself.[21]
>
> The means by which a right or a liability is created for a party regardless of the party's actual intent.[22]

"Operation of law" thus refers to the transfer of rights or liabilities by court order, statute, or the like—as opposed to a voluntary and express transfer made by a party. Assignments "by operation of law" would include the transition of a tenant's lease rights to the executor of the estate of a deceased tenant,[23] to a legatee,[24] to a tenant's trustee in bankruptcy[25] or receiver,[26] or through a judicial sale.[27] The passage of a corporate tenant's lease to a successor tenant through a merger of the corporate tenant is also regarded as being "by operation of law."[28]

Like transfers of leases through the sale of stock, assignments by operation of law do not violate Basic Assignment Restrictions. This is because Basic Assignment Restrictions are said to bar only affirmative voluntary acts by the tenant.[29] Because assignments by operation of law are not voluntary acts by the assignor, Basic Assignment Restrictions do not prohibit them.[30] As one potential exception to this rule, courts might not allow assignments by operation of law that have demon-

strably been arranged for the specific purpose of circumventing a Basic Assignment Restriction.[31] Even then, courts would not necessarily interfere, as they are often quite willing to endorse transactions that brazenly seek to "get around" Basic Assignment Restrictions.

As would be the case with other types of assignments, a landlord can prohibit assignments by operation of law by using Advanced Assignment Restrictions.[32] Again, such restrictions must be drafted with extreme specificity and clarity because most courts disfavor them and will construe them strictly against the landlord.[33]

Absent an Advanced Assignment Restriction that specifically refers to transfers "by operation of law," tenants can generally take comfort that such transfers will not run afoul of any Basic Assignment Restrictions in their lease.

V. Mergers

Few courts have considered whether the merger of a corporate tenant violates a Basic Assignment Restriction.[34] The courts that have considered the question have typically treated these transactions as constituting transfers by operation of law, not voluntary assignments.[35] As a result, such transfers do not violate Basic Assignment Restrictions.[36] One New York court reasoned:

> [T]he merger of the subsidiary corporation into its parent corporation did not constitute an assignment for purposes of violating the nonassignment covenant in the lease. The merger did not change the beneficial ownership, possession, or control of [the subsidiary's] property or leasehold estate. Only [the subsidiary's] corporate form was affected, not the corporate property. Therefore, no assignment or similar transfer of the lease occurred.[37]

Although most jurisdictions agree that Basic Assignment Restrictions do not prohibit mergers of corporate tenants, courts disagree over whether the change of ownership of a leasehold estate through a merger should be classified as an actual "assignment" of the lease, or as a mere "transfer by operation of law." The wording of the restriction in any particular lease is therefore quite important. The wording of the merger closing documents may also play a role.

Under a strict construction of Basic Assignment Restrictions, they would prohibit mergers only if mergers pass rights through "assignments" rather than mere "transfers by operation of law." This question of construction becomes quite important given that most modern Assignment Restrictions specifically prohibit "assignments by operation of law." It seems that the majority answer to this question of construction is that clauses that specifically prohibit "assignments by operation of law" do prohibit mergers.[38] For example, an Oregon Court stated:

> Although there is "meager authority" addressing the effect on a nonassignment clause of mergers by corporate tenants, where such clauses prohibit transfers "by operation of law," such mergers are a breach of the nonassignment clause "if the effect is to transfer the lease to an entity other than that of the original tenant" *even though no interest in property is impaired by the merger*.[39]

Other courts, however, have held that mergers, although "transfers" by operation of law, are not "assignments" of any kind, and are therefore not covered by such clauses.[40] Given most courts' hostility toward restraints on alienation, it is unclear whether courts will continue to follow the majority rule or adopt the second, more permissive view. Landlords wishing to prohibit mergers of their corporate tenants should therefore do so specifically, prohibiting both "mergers" in particular and "all transfers, subleases, or assignments made by operation of law" in general, in order to prohibit mergers under either reading.

Because of this disagreement, a corporate tenant planning a merger might not want to execute a document entitled "Assignment Agreement" or in any other way suggest in the merger documentation that any lease was ever "assigned." The tenant may later wish to claim that the transaction was merely a change in the identity of the tenant but in no way an assignment of the lease or a violation of a prohibition against "assignments by operation of law." This might be difficult to argue if the parties executed an "Assignment Agreement." Therefore, it may be advisable to title the document "Transfer of Lease" or "Succession of Lease," or to let the merger speak for itself (a reasonable position if, in fact, the parties intend to take the position that the lease was never transferred and the merger did whatever it did without an assignment of the lease).

A careful purchaser should, however, consider the possibility that any merger may well be deemed a prohibited "assignment by operation of law"—even if the closing documents try to portray the transaction as something else—and should proceed accordingly.

VI. Reasonableness in Denying Consent

A. Whether Required

In most states, including New York, the rule remains that where a lease prohibits assignment or subletting without the landlord's consent, the landlord may refuse consent arbitrarily and for any or no reason at all (and may even extract payment as a condition for consent), unless the lease specifically requires any refusal of consent to be reasonable.[41] Under the traditional majority rule, a

landlord bears no obligation to act "reasonably" or "in good faith" in considering a request for such consent.

A small but growing minority of jurisdictions hold, however, that a landlord must be reasonable in withholding consent even if the lease does not require reasonableness.[42] California codified this presumption of reasonableness for purposes of Assignment Restrictions, but placed the burden of proof on the tenant.[43] The California statute still allows the parties to contract around this presumption by setting express standards in the lease agreement.[44] A 2005 California federal court case[45] restated this rule by holding that when the contract unambiguously grants one party an unqualified right, "in its sole discretion, to terminate the negotiations with any prospective [s]ubtenant or assignee at any time and to refuse to enter into any sublease or with any prospective subtenant,"[46] that party can not only refuse to enter into any sublease proposals, but can refuse to even consider any and all proposed sublease agreements.[47]

As in so many other areas, New York diverges from California, follows the majority rule, and tends to prefer private negotiations over judicial improvement (and often rewriting) of privately negotiated agreements. If a New York lease contains a Transfer Restriction, the landlord need not be reasonable in refusing consent unless the lease language specifically so requires.[48] Unless a landlord has agreed otherwise, a New York landlord may impose conditions, including payment of additional rent or other consideration, on the tenant as a prerequisite to consent.[49] (One court, however, held that such conditions may amount to economic duress,[50] demonstrating yet again how these outcomes often depend on the particular judge rather than the consistent application of predictable legal principles, even in New York.) Like other restrictions on alienation of property, though, Transfer Restrictions are disfavored. Therefore, courts will construe such clauses strictly against any restrictions on alienation.[51]

B. What Constitutes Reasonableness

Even where a Transfer Restriction or governing law requires a landlord to act "reasonably" or "not unreasonably" in withholding consent, it is not at all clear what "reasonable" means. Although landlords cannot seize upon absolutely any creative excuse to withhold consent, no single rule or set of rules for defining "reasonableness" exists.

The question of "reasonableness" is therefore generally left to the trier of fact to decide,[52] with the result that consistent legal principles—or predictable results —are quite hard to find in this area. Randolph and Friedman wrote: "What is 'reasonable' at one time may not be at another."[53] This standard requires the fact finder to consider whether a reasonably prudent person in the landlord's position would have withheld consent.[54] Considerations of mere personal taste and convenience—personal idiosyncrasies of the landlord—are probably not reasonable.[55] The test of "reasonableness" is an objective one, based on the standard of "a reasonable prudent man," without considering "the personal taste and convenience of the landlord."[56]

Despite the nebulous nature of the "reasonableness" standard, the court in *American Book Co. v. Yeshiva University Development Foundation, Inc*. set forth a non-exhaustive list of "objective" standards for determining reasonableness. Other courts have followed them.[57] These standards, described as "readily measurable criteria of a proposed subtenant's or assignee's acceptability, from the point of view of *any* landlord," are:

- Financial responsibility of the proposed subtenant,
- The "identity" or "business character" of the subtenant—i.e., the subtenant's suitability for the particular building,
- The legality of the proposed use,[58] and
- The nature of the occupancy—i.e., office, factory, clinic, or whatever.[59]

Starting with the first criterion suggested above, a landlord is probably reasonable in refusing consent unless the tenant gives the landlord reasonable evidence that the proposed assignee is ready, willing, and able to perform the lease agreement.[60] A reasonable belief supported by evidence that a proposed assignee is unable to pay should almost always give a landlord reasonable grounds to deny consent.[61] A landlord should also almost always be deemed "reasonable" in refusing consent if the proposed assignee does not deliver adequate financial information in a timely manner so that the landlord can ascertain whether the proposed assignee would be financially responsible.[62]

Other considerations can, however, sometimes outweigh financial responsibility. For example, a landlord's refusal to allow financially responsible parties as multiple subtenants was upheld where subdivision of the leased space would have been undesirable in a "prestige building."[63]

Although the second factor listed above, the "identity" or "business character" of the subtenant/assignee, may be used as a reasonable basis for a landlord to reject an assignment, landlords that assert this argument bear a heavy burden of proof.[64]

One New York case involved an Assignment Restriction that required the landlord to be reasonable, but stated that the landlord could consider the "business reputation of the proposed assignee or subtenant," as well as "the effect that the proposed assignee or subtenant's occupancy or use of the demised premises would have upon the operation and maintenance of the building and the landlord's investment therein." Although the court in that case did begin by analyzing the factors listed above, it rejected the landlord's substantial evidence that assignment to a financially responsible bank with an alleged

"bad business reputation" would lower the value of the property.[65] This case reflects judicial skepticism of landlords who turn down assignments based on allegedly bad characteristics of the assignee.

Courts have, however, held that a landlord may "reasonably" deny consent under these circumstances, for example:

- If a landlord is unaware of the assignee's proposed use,[66]
- If a proposed subtenant would compete with other businesses in the same shopping center, prejudicing the landlord's relationship with other tenants,[67]
- If gross sales, and thus percentage rents, would be reduced,[68] and
- Where the mix of tenants is critical to the success of the landlord, such as in a shopping center.[69]

"Unreasonable" grounds for denial have included these circumstances as examples:

- If a proposed subtenant would compete with the landlord's business,[70]
- The fact that a tenant would make a profit from the assignment or sublease,[71]
- A landlord's philosophical objections to the proposed tenant's business,[72]
- A landlord's dislike of a particular business or method of doing business,[73]
- The mere fact that the prospective assignee is already an existing tenant,[74] and
- A landlord's attempt to extract an economic concession or to improve its financial position.[75]

The above hardly represents a complete list of all factors that courts have considered in determining reasonableness. Potential assignors and assignees should consult case law regarding "reasonableness" in each applicable jurisdiction and should remember that courts may rule differently on the same grounds for rejection, depending on the facts of the particular case. And, perhaps, what the judge had for breakfast. Landlords, in turn, should plan carefully and consult counsel before taking any action or imposing any condition on a tenant that could create an appearance of substantive unfairness or economic duress.

C. "Withholding Consent " vs. "Refusing Consent"

One Colorado case purported to distinguish between a landlord's "withholding" and "refusing" consent to a proposed assignment.[76] In *Parr v. Triple L&J Corp.*, the lease allowed the tenant to assign with the landlord's prior consent, and also said the landlord could not unreasonably "withhold" that consent.[77]

The tenant told the landlord it wanted to assign. The landlord asked for certain information. The tenant provided all that information. Then the landlord did nothing. The landlord deferred making any decision at all, even though the tenant told the landlord that timing was crucial.[78] The tenant turned out to be right, and "lost the deal."

The court concluded that when the lease said the landlord could not "withhold" consent, this meant the landlord could not silently let an unreasonable amount of time go by without response. The court suggested that if the lease had said the landlord could not "refuse" consent, then the landlord might violate the lease only if the landlord took some affirmative action, or made some affirmative statement of rejection, but mere inaction might be just fine.[79] Because the lease prohibited unreasonable withholding of consent (not "refusal" of consent), the landlord's delaying consent amounted to a withholding of consent.[80] In contrast, if the lease had said the landlord could not "unreasonably refuse" consent, then mere silence might have been acceptable.

No court in any other case reviewed for this article drew any similar distinction between a landlord's decision to "withhold" consent or "refuse" consent. Nevertheless, if this distinction actually exists, then landlords' counsel might want any lease to say that the landlord will not "unreasonably refuse" consent. Correspondingly, tenant's counsel might want to use the words "unreasonably withhold" consent. The case is hardly persuasive in any event.

VII. Lessons for a Landlord

A landlord should consider these suggestions when writing or reviewing Transfer Restrictions in leases:

- *Uphill Battle*. Courts dislike restrictions on alienation and will strictly construe them. It is important to be very precise when drafting the language of such restrictions.
- *Prohibit Equity Transfers*. Include specific language that prohibits the transfer of control of a corporation. This language should also prohibit the creation and sale of new stock. The language should be broad enough to refer to all present and future entity types and equity types.
- *Change of Control?* Prohibitions against the transfer of control are probably only appropriate when dealing with corporations that have a small number of shareholders.
- *Operation of Law*. Include language prohibiting transfers, subleases or assignments by "operation of law."
- *Murkiness on Mergers*. A landlord should specifically prohibit mergers or, more generally, prohibit a whole laundry list of possible transactions—"all transfers, subleases, mergers, consolidations, or assignments by operation of law."

- *Consent Standards*. Explicit standards regarding consent tend to prevail over the presumed "reasonableness" standard, so it is better to state what the parties consider "reasonable." Without a specific standard, the outcome is unpredictable, although that may concern a tenant more than a landlord.
- *Idiosyncratic Tastes.* If the landlord wants the right to withhold consent for reasons specific to that particular landlord—religious beliefs, personal tastes, the landlord's own activities—the lease should expressly say so or, better yet, give the landlord an absolute discretionary right to withhold consent.
- *Liability for Unreasonableness*. If a landlord agrees to be "reasonable," the landlord should disclaim any liability for failing to be reasonable. The lease should provide that the tenant's only remedy in that case would be to obtain equitable relief deeming the landlord's consent granted.

VIII. Lessons for a Tenant

A tenant should consider these suggestions to mitigate the risks of Transfer Restrictions:

- *Cut Them Back*. Try to limit Transfer Restrictions as much as possible. If possible, avoid Advanced Assignment Restrictions entirely. If it is not possible, at least try to obtain the landlord's preapproval of certain likely corporate transactions that would obviously not constitute devices to evade the Assignment Restrictions (e.g., bona fide corporate transactions or transactions affecting multiple sites). State that the landlord will not unreasonably "withhold" consent as opposed to unreasonably "refuse" consent. Consider adding a statement that any transaction not expressly banned shall be deemed permitted.
- *Early Attention*. Particularly for a real-estate-intensive company with high value leases, consider the effect of Assignment Restrictions in the earliest stages of structuring the transaction. Treat them as fundamental business issues.
- *Identify and Use Leverage*. If the landlord ever requests any accommodation or amendment related to any lease, try to use it as an opportunity to trim back any Assignment Restrictions in the lease.

Assignment Restrictions can create unpleasant surprises for both landlords and tenants. As the first step toward preventing those surprises, parties to commercial leases first need to understand what the various Assignment Restrictions mean, and then confirm that they reflect the parties' expectations. This article seeks to provide that starting point.

Endnotes

1. A "space lease" usually means a lease of space the tenant uses for actual business operations, where the tenant is not in the development or real estate investment business. Space leases typically include office leases, with an original term of 5 to 15 years, and retail leases, which can go much longer (at least for large spaces) after taking into account multiple extension options. The longer the lease term and the more limited the landlord's responsibilities, the closer the transaction gets to a "ground lease," where the tenant regards its leasehold as a real estate investment. A "ground lease" will typically allow the tenant much more flexibility than a "space lease," and will be less likely to contain burdensome provisions of the type this article analyzes.
2. This article treats a requirement to obtain the landlord's consent as equivalent to a prohibition, because one should assume both roads will usually lead to the same place. In some states, however, a consent requirement may imply a "reasonableness" qualification, whereas an outright prohibition will not. These distinctions are, however, quite subtle, fact-specific, unpredictable, and unreliable. This article discusses all these issues below.
3. If the company has only a few leases, or if it has generic space requirements (so it could easily replace any lost leases), or if most of its leases are at or above market, the parties may make a "business decision" not to worry about leases at all. As a practical matter, the likelihood of trouble under these circumstances seems fairly low, especially if the company has good relations with its landlords and those landlords are widely dispersed. On the other hand, if the company's value lies in its leases and their below-market rents (e.g., a typical supermarket chain), the risk of claims by opportunistic landlords may turn these legal issues into the most important business issues in the deal. Exactly how to approach all this represents a strategic decision to be discussed with the client early in the transaction and confirmed in writing.
4. Similar issues arise for valuable contracts. There is no reason to think the answers would be dramatically different.
5. When faced with strict prohibitions on assignment, the parties can sometimes, depending on the larger deal structure, instead create a sublease to give the subtenant nearly the functional equivalent of an assignment. The question then becomes whether the lease prohibits—or requires the landlord's consent to—subleasing of this type.
6. *See Riggs v. Pursell*, 66 N.Y. 193, 201 (1876).
7. *See* PATRICK A. RANDOLPH, JR. & MILTON R. FRIEDMAN, FRIEDMAN ON LEASES § 7:3.3 (5th ed. 2005).
8. *See id*. If, however, the mortgagee or pledgee exercises its rights and remedies to bring about an absolute transfer, then at that point the transaction will usually—and should—be deemed an assignment or transfer. In most cases, therefore, the "safe harbor" for a "mortgage" or "pledge" will usually not give a lender much comfort, as the lender will usually want to know that it can safely realize on its collateral. On the other hand, if the lender merely wanted to achieve "secured" status for bankruptcy purposes, the lender might not care about this problem.
9. This article includes a discussion of what "operation of law" means. See Section IV.
10. The discussion refers only to corporate tenants. It is believed that limited liability company tenants and partnership tenants would be treated the same as corporations for this purpose. That conclusion has not been tested or researched for the present discussion.
11. *See In re Ames Dep't Store*, 127 B.R. 744, 748-49 (Bankr. S.D.N.Y. 1991) ("In Illinois, it is settled that the transfer of all of the stock issued by a tenant corporation does not effect an assignment of the tenant's lease unless the lease so provides."); *Ser-Bye Corp. v. C. P. & G. Markets*, 179 P.2d 342, 345 (Cal. Dist. Ct. App. 1947) ("The inhibitions against assignment run as to the lease itself and not to the stock in the lessee corporation by one or more stockholders. When, therefore, it was covenanted that the lessee should not 'assign the leasehold estate,' the lease as an entirety was meant, and not merely shares of stock in the lessee corporation."). *See also U.S. Cellular Inv. Co. v. GTE Mobilnet, Inc.*, 281 F.3d 929, 934-36 (9th Cir. 2002) (limited partnership agreement restriction on

a corporation's sale of its general partnership interest does not restrict sale of stock by stockholders of that partner); *Richardson v. La Rancherita La Jolla*, 159 Cal. Rptr. 285 (Ct. App. 1978) (sale of all shares of stock in lessee corporation does not violate antiassignment clause); *Posner v. Air Brakes & Equipment Corp.*, 62 A.2d 711, 713 (N.J. Super. Ct. Ch. Div. 1948) (fact that tenant corporation became wholly owned by or a subsidiary of another corporation "does not under the circumstances of this case constitute an assignment of the lease or an underletting of the premises by the lessee"); *Burrows Motor Co. v. Davis*, 76 A.2d 163, 165 (D.C. 1950) (transfer of majority of stock in lessee corporation producing change in control does not violate antiassignment clause).

12. *See Branmar Theatre Co. v. Branmar, Inc.*, 264 A.2d 526, 529 (Del. Ch. 1970) ("The rule that precludes a person from doing indirectly what he cannot do directly has no application to the present case. The attempted assignment was . . . by plaintiff corporation, the sale of stock by its stockholders."). Although courts refuse to treat a stock sale as an implied lease assignment, the New York state and city tax rules take a different approach. They treat the transfer of a "controlling interest" in an entity that owns real estate as an implied transfer of the real estate. N.Y. Tax Law § 1401(b), (e); N.Y.C. Admin. Code § 11-2101(6) through (9); § 11-2102(a).

13. *See Ames Dept. Stores*, 127 B.R. at 749. *See also Burrows Motor Co.*, 76 A.2d at 164.

14. *See Rubinstein Bros. v. Ole of 34th St., Inc.*, 421 N.Y.S.2d 534, 538 (Civ. Ct. 1979) ("The rule of [the cases previously cited] makes sense. A landlord entering a lease with a corporate tenant should be presumed to know that it is an artificial entity with a life distinct from the individuals who may from time to time be its owners."). *See also Gasparre v. 88-36 Elmhurst Ave. Realty Corp.*, 464 N.Y.S.2d 106 (Sup. Ct. 1983) (extending *Rubinstein* to hold that transfer of stock of corporate property owner does not constitute sale of property under "due on sale" clause).

15. *See U.S. Cellular*, 281 F.3d at 936 ("Had the partners intended that the sale of stock of a corporate partner be restricted, such intent could easily have been stated.").

16. *See Associated Cotton Shops, Inc. v. Evergreen Park Shopping Plaza*, 170 N.E.2d 35 (Ill. App. Ct. 1960).

17. *See Lipsker v. Billings Boot Shop*, 288 P.2d 660 (Mont. 1955). *See also, e.g.*, N.Y. Gen. Oblig. Law § 13-101 ("Any claim or demand can be transferred" with very limited exceptions.).

18. *See* Randolph & Friedman, *supra* note 7, § 7:3.3[C][1]. To avoid ambiguity when attempting to prevent changes in corporate control, Randolph and Friedman recommend that landlords draft nonassignment clauses in the following form (which may require updating or modification in particular cases):

> An assignment, forbidden within the meaning of this Article, shall be deemed to include one or more sales or transfers, by operation of law or otherwise, or creation of new stock, by which an aggregate of more than 50% of Tenant's stock shall be vested in a party or parties who are nonstockholders as of the date hereof. This paragraph shall not apply if Tenant's stock is listed on a recognized security exchange. For the purpose of this paragraph, stock ownership shall be determined in accordance with the principles set forth in Section 544 of the Internal Revenue Code of 1954 as the same existed on August 16, 1954.

19. *See Rubinstein Bros.*, 421 N.Y.S.2d at 538 ("If a landlord wished to protect itself against such vicissitude [of corporate ownership], it could easily write into the lease a condition subsequent. One can certainly not be implied, however."). *See also Dennis' Natural Mini-Meals, Inc. v. 91 Fifth Ave. Corp.*, 568 N.Y.S.2d 740 (App. Div. 1991).

20. *See* Randolph & Friedman, *supra* note 7, § 7:3.3[C][1].

21. *See Black's Law Dictionary* 1092 (6th ed. 1990).

22. *See Black's Law Dictionary* 1119 (7th ed. 1999).

23. *See Francis v. Ferguson*, 159 N.E. 416 (N.Y. 1927). *See also Second Realty Corp. v. Fiore*, 65 A.2d 926 (D.C. 1949); *Swan v. Bill*, 59 A.2d 346 (N.H. 1948).

24. *See Burns v. McGraw*, 171 P.2d 148 (Cal. Dist. Ct. App. 1946). *See also Charcowsky v. Stahl*, 189 N.Y.S.2d 384 (App. Div. 1959); *Squire v. Learned*, 81 N.E. 880 (Mass. 1907); *Buddon Realty Co. v. Wallace*, 189 S.W.2d 1002 (Mo. Ct. App. 1945).

25. *See Gazlay v. Williams*, 210 U.S. 41 (1907*). See also Miller v. Fredeking*, 133 S.E. 375 (W.Va. 1926); *Standard Operations, Inc. v. Montague*, 758 S.W.2d 442 (Mo. 1988).

26. *See In re Prudential Lithograph Co.*, 265 F. 869 (S.D.N.Y. 1920). *See also Standard Operations*, 758 S.W.2d at 442.

27. *See* Randolph & Friedman, *supra* note 7, § 7:3.3[D].

28. Section V covers mergers in some depth.

29. *See* Randolph & Friedman, *supra* note 7, § 7:3.3[D].

30. *See In re Childs Co.*, 64 F. Supp. 282, 284 (S.D.N.Y. 1944) ("It is well settled under the cases that an involuntary assignment by operation of law, as we have here, does not constitute a breach of a covenant in a lease against an assignment thereof by the tenant without the consent of the landlord."). *See also Francis*, 159 N.E. at 416; *Burrows Motor Co.*, 76 A.2d at 165; *Milmoe v. Sapienza*, 142 A. 360 (N.J. Ch. 1928).

31. *See Swan*, 95 N.H. at 158 ("A transfer by operation of law is not, in the absence of an express stipulation in that regard, within a provision against assignment, unless it is procured by the tenant merely for the purpose of avoiding the restriction."). *See also Francis*, 159 N.E. at 417.

32. *See Pacific First Bank v. New Morgan Park Corp.*, 876 P.2d 761, 765 (Or. 1994) ("If a covenant not to assign a lease expressly prohibits transfers by operation of law, then transfers by operation of law breach the covenant not to assign."); *In re Georgalas Bros.*, 245 F. 129 (N. D. Ohio 1917). *See also Clifford v. Androscoggin & K. R. Co.*, 115 A. 511 (Me. 1921).

33. *See Morris v. Canadian Four State Holdings, Ltd.*, 678 N.Y.S.2d 214 (App. Div. 1998) (general language prohibiting assignment "whether by operation of law or otherwise" did not contain "very special" language needed to treat devolution to executors as being a prohibited assignment). *See also Francis*, 159 N.E. at 417.

34. *See* Randolph & Friedman, *supra* note 7, § 7:3.3[E][2].

35. *See Middendorf v. Fuqua Indus., Inc.*, 623 F.2d 13, 16 (6th Cir. Ohio 1980) ("The effect under Ohio law of the merger of [two corporations] was to transfer the leasehold by operation of law and not by assignment.").

36. *See Segal v. Greater Valley Terminal Corp.*, 199 A.2d 48, 50 (N.J. Super. Ct. App. Div. 1964) ("In authorizing a corporate merger, the Legislature provided that the rights, privileges, powers, franchises 'and all and every other interest' of each component corporation shall vest in the successor corporation. N.J. Rev. Stat. § 14:12-5. The passage of such interests under the statute, whether labeled an assignment, sublease, or transfer, is by operation of law, and it will not operate as a breach of a covenant barring assignment."); *Dodier Realty & Inv. Co. v. St. Louis Nat'l Baseball Club*, 238 S.W.2d 321, 325 (Mo. 1951) ("The merged corporation having succeeded to the rights of the original lessee by operation of law, it follows that there was no assignment within the prohibition of the covenant in question").

37. *Brentsun Realty Corp. v. D'Urso Supermarkets, Inc.*, 582 N.Y.S.2d 216, 217 (App. Div. 1992).

38. *See Citizens Bank & Trust Co. v. Barlow Corp.*, 456 A.2d 1283, 1289 (Md. 1983) ("The nonassignment clause used . . . in the lease of the subject premises may be characterized as of the strict type. Its inclusion of assignments by operation of law embraces transfers by merger.").

39. *Pacific First Bank*, 876 P.2d at 765.

40. *See Sante Fe Energy Res., Inc. v. Manners*, 635 A.2d 648 (Pa. Super. Ct. 1993) (transfer of rights of action and property pursuant to merger properly characterized as succession, not assignment); *Albermarle, Inc. v. Eaton Corp*., 357 S.E.2d 887 (Ga. Ct. App. 1987) (surviving corporation following merger more accurately described as successor than assignee); *Standard Operations*, 758 S.W.2d at 443 ("The present lease makes use of the phrase, 'operation of law,' which was used in the Dodier opinion to describe the transaction we found not to be covered, but continues to use the term, 'assignment,' which we there found to be an inappropriate description of the effect of a merger."). The *Standard Operations* court justifies this conclusion under the theory that forfeitures must be viewed with disfavor and read as strictly as possible.

41. Courts (although not necessarily all courts) in the following jurisdictions have adopted this majority rule: Colorado, Connecticut, Delaware, Georgia, Indiana, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Nebraska, New Hampshire, New Jersey, New York, North Dakota, Ohio, Pennsylvania, South Carolina, Vermont, and Washington. Because of the frequency with which this issue arises and the likelihood of changes in the law, the preceding list (which was based on minimal research) should not be relied upon. For a description of cases in some of these jurisdictions, *see* James C. McLoughlin, Annotation, *When Lessor May Withhold Consent Under Unqualified Provision in Lease Prohibiting Assignment or Subletting of Leased Premises Without Lessor's Consent*, 21 A.L.R.4th 188, § 3 (2004).

42. Courts, though not necessarily all courts, in the following jurisdictions have adopted this minority rule: Alabama, Arizona, Arkansas, California, Colorado, Connecticut, District of Columbia, Florida, Georgia, Idaho, Illinois, Louisiana, Maryland, Massachusetts, Nebraska, New Mexico, North Carolina, Ohio, Oregon, and Tennessee. (But see the caveats in the preceding footnote.) *See also Pacific First Bank*, 876 P.2d at 762 (applying contractual duty of good faith to lease agreements, which requires adherence to reasonable expectations of parties—a standard that may in practice leave it all up to the judge, potentially many years after the fact).

43. *See* Cal. Civ. Code §§ 1995.010-.340 (2004).

44. Well-represented landlords will presumably do so. Hence, each lease may now contain yet another state-specific paragraph, probably in all capital letters and requiring the parties to add their initials to prove they were awake. And leases will grow a little bit longer yet again.

45. *Turkus v. Egreetings Network, Inc*., No. C 05-1091 MJJ, 2005 WL 2333834 (N.D. Cal. Sept. 19, 2005). The court also restated the rule that "where a discretionary right in a contract i[s] unambiguous, a party may not invoke the implied covenant of good faith and fair dealing." This case involved a real-estate-related consent right other than the typical landlord's right to consent a sublease, but there is no reason to think different principles would apply.

46. *Id*. at *4.

47. *See id.* at *4.

48. *See Mann Theatres Corp. v. Mid-Island Shopping Plaza Co*., 464 N.Y.S.2d 793, 797-98 (App. Div. 1983) ("[W]here the lease contains an express provision restricting assignment or subletting without the landlord's consent, the landlord may arbitrarily refuse consent for any or for no reason, unless the provision requires that consent not be unreasonably withheld."), *aff'd*, 468 N.E.2d 51 (1983). *See also Caridi v. Markey*, 539 N.Y.S.2d 404, 405 (App. Div. 1989) (recognizing need to protect landlord's substantial interest in controlling assignability of leases in New York); *Arlu Assocs., Inc. v. Rosner*, 220 N.Y.S.2d 288 (App. Div. 1961), *aff'd*, 185 N.E.2d 913 (1962); *Kruger*, 432 N.Y.S.2d at 295 (which includes subletting in the majority rule).

49. *See Durand v. Lipman*, 1 N.Y.S.2d 468, 473-74 (Mun. Ct. 1937) ("The landlord . . . could withhold such consent, even arbitrarily. Hence the landlord was at liberty to impose such conditions as he deemed proper as a prerequisite to his consent to the assignment."). *See also Herlou Card Shop, Inc. v. Prudential Ins. Co*., 422 N.Y.S.2d 708 (App. Div. 1979). Note, however, that Randolph and Friedman write that such practices by landlords are not viewed favorably by courts and may be the motivating force behind the change of many jurisdictions to the minority rule. ("It may be noted that the minority cases generally involve a demand by landlord from tenant for something in excess of the tenant's lease obligations, usually a rent increase or equivalent, which one court called 'blood money' . . . . A few more 'blood money' cases could provoke a change [in other jurisdictions to requiring reasonableness in withholding consent]." RANDOLPH & FRIEDMAN, *supra* note 7, § 7:3.4[A].)

50. *See Equity Funding Corp. v. Carol Mgmt. Corp*., 322 N.Y.S.2d 965 (Sup. Ct. 1971), *aff'd*, 326 N.Y.S.2d 384 (App. Div. 1971).

51. *See Kruger*, 432 N.Y.S.2d at 295. *See also Chanslor-Western Oil & Dev. Co. v. Metro. Sanitary Dist*., 266 N.E.2d 405 (Ill. App. Ct. 1970); *Ring v. Mpath Interactive*, 302 F. Supp. 2d 301, 306 (S.D.N.Y. 2004).

52. *See Worcester-Tatnuck Square CVS, Inc. v. Kaplan*, 601 N.E.2d 485, 488 (Mass. App. Ct. 1992) ("Whether a lessor acts reasonably in withholding his consent to a sublease, therefore, is a question for the finder of fact."); *Am. Book Co. v. Yeshiva Univ. Dev. Found., Inc*., 297 N.Y.S.2d 156, 159 (1969) ("The standards of 'reasonableness' have not heretofore been clearly delineated by any single New York case, but are left to the trial court to determine in accordance with the particular factual patterns before it, and the conceptual boundaries may be only faintly discerned in the few reported cases."). *See also* Cal. Civ. Code § 1995.260 (2004).

53. RANDOLPH & FRIEDMAN, *supra* note 7, § 7:3.4[D][3].

54. *See Ernst Home Ctr. v. John Y. Sato*, 910 P.2d 486, 492 (1996); *Ringwood Assocs., Ltd. v. Jack's of Route 23, Inc*., 379 A.2d 508, 511 (N.J. Super. Ct. Law Div. 1977); *Ramco-Gershenson Props., L.P. v. Serv. Merchandise Co., Inc*., 293 B.R. 169 (M.D. Tenn. 2003) (applying commercial reasonableness standard to landlord's withholding of consent).

55. *See Worcester*, 601 N.E.2d at 488-489. *See also Chanslor-Western*, 266 N.E.2d at 405; *Broad & Branford Place Corp. v. J. J. Hockenjos* Co., 39 A.2d 80 (N.J. Sup. Ct. 1944).

56. *See Tenet v. Jefferson Parish Medical Center*, 2005 U.S. App. LEXIS 20283 (5th Cir. 9/21/05). In this well reasoned Fifth Circuit case, a real estate investor leased space to a tenant for a medical use. The lease said the landlord would not unreasonably withhold consent to an assignment. The original landlord sold the property to a hospital. The original tenant proposed to assign to a different type of medical use, one that the lease would allow but that would compete with the hospital in ways that the previous tenant would not have. The hospital withheld consent on that basis. The hospital argued that "reasonableness" depends in part on the identity and circumstances of the landlord at the moment the tenant requests the landlord's consent, and that if the current landlord wants to protect itself from competition, that constitutes a "reasonable" basis to withhold approval. The court disagreed, stating: "In determining whether a landlord's refusal to consent was reasonable in a commercial context, only factors that relate to the landlord's interest in preserving the leased property or in having the terms of [the] prime lease performed should be considered." The court also reasoned that if a future landlord can tighten the scope of permitted assignments based on circumstances peculiar to that landlord, this would amount to an expansion of the landlord's rights under the lease without the tenant's consent. (Of course, this court would not even have allowed the original landlord to assert its own personal circumstances, either, so the argument carries little additional weight.)

57. 297 N.Y.S.2d at 160. *See also Ernst Home Ctr*., 910 P.2d at 493 (discussing the factors that a landlord can reasonably consider); *Fernandez v. Vazquez*, 397 So. 2d 1171 (Fla. Dist. Ct. App. 1981).

58. If the proposed assignee or subtenant would or might use the premises in violation of the lease (whether the use clause, an obligation to comply with law, or any other lease terms), why shouldn't the landlord be relegated to its rights and remedies if

and when a violation actually occurs? Why should this discussion be a component of "reasonableness" at all? The answer may be that the courts cannot be relied upon to enforce the landlord's rights and remedies for a nonmonetary breach and therefore the landlord should be able to point to the likelihood of such a breach as a "reason" to withhold consent.

59. *See Am. Book Co.*, 297 N.Y.S.2d at 156.

60. *See Golf Mgmt. Co. v. Evening Tides Waterbeds, Inc.*, 571 N.E.2d 1000 (Ill. App. Ct. 1991).

61. *But see Ring*, 302 F. Supp. 2d at 306 (landlord's unsubstantiated assertion that some unspecified documents showed subtenant to be a financial risk constitutes an unreasonable refusal of consent). *See also* RANDOLPH & FRIEDMAN, *supra* note 7, § 7:3.4[D][3]. Randolph and Friedman point out that "inasmuch as neither assignment nor subletting releases the original tenant from his lease obligations, it may be argued that landlord has all he bargained for regardless of the wealth or skill of the assignee or subtenant." They note, however, that the little relevant authority on the issue has held that the landlord is entitled to a responsible assignee. In practice landlords prefer a financially responsible assignee or subtenant to minimize the likelihood of default and litigation against the tenant, even though the tenant will remain liable on the lease. That preference is generally accepted and taken seriously in the real estate industry.

62. *See 200 Eighth Ave. Rest. Corp. v. Daytona Holding Corp.*, 740 N.Y.S.2d 330, 331 (App. Div. 2002) (noting that financial information later submitted by proposed assignee showed proposed assignee was not financially capable of assuming lease obligations).

63. *See Time, Inc. v. Tager*, 260 N.Y.S.2d 413 (Civ. Ct. 1965).

64. *See Ernst Home Ctr.*, 910 P.2d at 493 (while "tone" and "image" are valid considerations, landlord must be able not only to express [concoct?] appropriate concerns, but also to produce evidence that a trier of fact could examine objectively).

65. *Chase Manhattan Bank, N.A. v. Lincoln Plaza Assocs.*, 201 (5) N.Y.L.J. 22, col. B (Jan. 9, 1989). Here, Chase Manhattan wanted to assign its lease to Bank Leumi. The landlord rejected the assignment, saying Bank Leumi had a "bad business reputation," was plagued by "image problems," and was "simply not a Chase Manhattan." As evidence, the landlord introduced (among other things) news articles on indictments of several of the bank's low-level officers and economic problems and stock scandals in Israel, Bank Leumi's home country. The landlord also presented affidavits by real estate attorneys and appraisers that a Bank Leumi tenancy would lower the value of the building. Presumably the tenant offered competing affidavits from other attorneys and appraisers.

66. *See Kroger Co. v. Rossford Indus. Corp.*, 261 N.E.2d 355 (Ohio C.P. 1969).

67. *See Norville v. Carr-Gottstein Foods Co.*, 84 P.3d 996, 1002 (Alaska 2004).

68. *See id. See also Worcester-Tatnuck Square CVS, Inc.*, 601 N.E.2d at 489 ("[Landlord] could reasonably insist upon a subtenancy that would be likely to generate at least a reasonable amount of percentage rent.").

69. *See Warmack v. Merchants Nat'l Bank*, 612 S.W.2d 733 (Ark. 1981) (upholding landlord's refusal to consent to assignment from bank to savings and loan, where savings and loan would not draw the same nor as many customers as bank). *See also Ramco-Gershenson Props.*, 293 B.R. at 174-75 ("[T]he tenant mix in a shopping center may be as important to the lessor as the actual promised rental payments" (quoting H.R. Rep. No. 595, 95th Cong., 1st Sess. 348-49 (1977), *reprinted in* 1978 U.S. Code Cong. & Ad. News 5963, 6305)).

70. *See Tenet*, 426 F.3d at 744, which found a landlord's withholding of consent unreasonable when premised on concern that the assignee would compete with the landlord's business. The court held that the landlord's refusal must relate to the ownership and operation of the leased property, not to its general economic interest. *See also Edelman v. F. W. Woolworth Co.*, 252 Ill. App. 142 (App. Ct. 1929), held that such denial was unreasonable where the landlord's business was located a block away from the potential competitor's business.

71. *See Stauffer Chemical Co. v. Fisher-Park Lane Co.*, 312 N.Y.S.2d 243 (Sup. Ct. 1970). *See also Carter v. Safeway Stores*, 744 P.2d 458 (Ariz. Ct. App. 1987).

72. *See Am. Book Co.*, 297 N.Y.S.2d at 156 (refusal to consent to assignment was unreasonable where landlord, a religious university, objected to tenant's sublease to a Planned Parenthood office). A landlord with special sensitivities of this type may wish to build appropriate restrictions into the lease or insist on an absolutely "discretionary" right of approval.

73. *See Broad & Branford Place*, 39 A.2d at 80 (refusal to consent to assignment was unreasonable where proposed assignee was a dressed poultry store). *See also Roundup Tavern, Inc. v. Pardini*, 413 P.2d 820 (Wash. 1966) (involving a tavern).

74. *See Catalina, Inc. v. Biscayne Northeast Corp.*, 296 So. 2d 580, 582-83 (Fla. Dist. Ct. App. 1974) (such a refusal to consent would be reasonable if proposed sublease would have destroyed or adversely affected preexisting lease).

75. *See Worcester*, 601 N.E.2d at 489. *See also Campbell v. Westdahl*, 715 P.2d 288 (Ariz. Ct. App. 1985); *Giordano v. Miller*, 733 N.Y.S.2d 94, 95 (App. Div. 2001) (landlord's demand that tenant pay landlord fee as a condition precedent to landlord's granting of consent is unreasonable). Note, however, that while a landlord's demanding of a fee as a condition precedent to granting consent is permitted under New York law if the lease is silent, the lease in *Giordano* specified that the landlord could not withhold its consent unreasonably and the lease did not provide for such a fee. Hence the landlord's request for such a fee was unreasonable.

76. *See Farr v. Triple L&J Corp.*, 107 P.3d 1104 (Colo. Ct. App. 2004).

77. *Id.* at 1107.

78. *Id.* at 1107.

79. *Id.* at 1108.

80. *Id.* at 1108.

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Nonprimary-Residence Holdover Proceedings

By Gerald Lebovits and Matthias W. Li

I. Introduction

New York City's rent-control and rent-stabilization laws were established in a time of housing shortages to protect tenants from evictions without good cause and to regulate the amount of rent tenants pay. So long as rent-regulated tenants pay rent, their landlords may not evict them[1] unless an eviction is premised on a narrowly enumerated ground. One of these grounds emerged from § 55 of the Omnibus Housing Act, which took effect on June 30, 1983. It requires rent-regulated tenants to maintain their apartments as their primary residence or face eviction.[2]

When a tenant does not use a rent-regulated apartment as a primary residence, the "[p]ublic policy is not advanced by permitting housing units to be held, partly or wholly unutilized, by tenants whose interest is pecuniary gain rather than affordable housing."[3] The legislature intended rent regulation to "alleviate the housing shortage, not to permit tenants to use apartments for convenience or storage."[4] The goal is to return underused apartments to the marketplace. The legislature has therefore exempted from rent-regulation protection apartments that tenants do not use as their primary residence.[5] As a result, a landlord may bring a summary holdover proceeding against a tenant who violates the primary-residence requirement. This article explores the contours of primary-residence holdovers.

II. Commencing Nonprimary Residence Summary Holdover Proceedings

A. Predicate Notices

Before a landlord may commence a holdover proceeding for nonprimary residence, the landlord must serve the tenant with predicate notices. If the tenant resides in a rent-stabilized or a rent-controlled apartment, the landlord must serve on the tenant a termination notice under Real Property Law ("RPL") § 232-a, giving the tenant 30 days' notice "that the landlord elects to terminate the tenancy and that unless the tenant removes from such premises on the day on which his term expires the landlord will commence summary proceedings under the statute to remove such tenant therefrom."[6] RPL § 232-a also provides that "no monthly tenant, or tenant from month to month, shall hereafter be removed from any lands or buildings in the city of New York on the grounds of holding over his term unless at least thirty days before the expiration of the term the landlord or his agent serve upon the tenant, in the same manner in which a notice of petition in summary proceedings is now allowed to be served by law." Because these requirements are statutory, a court is without subject-matter jurisdiction to proceed if a landlord fails to serve on a tenant a termination notice within the time provided by RPL § 232-a. A service defect may not be cured.[7]

For rent-stabilized tenants, the landlord must offer a renewal lease to a tenant not more than 150 and not less than 90 days before the existing lease expires.[8] This offer remains open to the tenant for 60 days. A landlord that chooses not to renew the lease must give the tenant a nonrenewal notice, known as a "Golub notice,"[9] in addition to a termination notice. Notice of the landlord's intention not to renew the tenant's rent-stabilized lease for non primary residence must be given to the tenant not more than 150 and not less than 90 days before the existing lease expires. This window is known as the "Golub period."[10] The Golub notice must state the grounds to evict the tenant, the facts necessary to establish the existence of the grounds, and the date when the tenant is required to surrender possession.[11]

Rent Stabilization Code (RSC) § 2524.4(c) provides that a nonrenewal notice and a termination notice may be served together in one notice.[12]

The RSC dictates the proper service method for a Golub notice. If a Golub notice is served untimely or not at all, the refusal to renew the lease on nonprimary-residence grounds will not have been preserved, and the tenant will be entitled to a renewal lease.[13] The RSC and the Rent Stabilization Law (RSL) dictate the mailing methods that are sufficient to communicate the Golub notice to a tenant. Lease provisions requiring stricter mailing requirements are unenforceable.[14] Serving a Golub notice by ordinary mail only, even though a lease requires service by certified mail, is proper because the first-class mailing requirement is specifically provided for in the RSC and RSL. An incorrect address on a mailing must, however, lead to dismissal.[15] Copies of the notice must also be mailed to any alternative addresses of the tenant known to a landlord who has written information about the alternative addresses. Failure to comply with these service requirements requires dismissal.[16]

Facts in a Golub notice that support the landlord's claim of nonprimary residence may include the alternate addresses where the tenant is alleged to reside or other evidence (such as public records) that the tenant does not use the subject premises as the primary residence.[17] This

requirement ensures that tenants will be informed of the factual and legal claims they will need to meet and enables them to interpose available defenses.[18] A Golub notice that alleges only the legal ground for eviction and not the facts on which the proceeding is based is "insufficient and cannot serve as a predicate for an eviction proceeding."[19] When assessing the sufficiency of a termination notice, the test is one of reasonableness in view of all the particular circumstances.[20]

B. Rent-Controlled Tenants and Rent-Stabilized Tenants

Unlike rent-stabilized tenants, statutory rent-controlled tenants often have no leases, or the leases are so old they are lost. These tenancies have neither a lease nor a finite term. Rent-controlled tenants are afforded an additional layer of protection.[21]

The New York City Rent Control Law (RCL) provides that no tenant shall be evicted on other than seven stated grounds unless, on the landlord's application, the city rent agency, now the Division of Housing and Community Renewal (DHCR), shall issue an order granting a certificate of eviction according to its rules and regulations.[22] A certificate of eviction is a jurisdictional prerequisite to commencing a summary holdover proceeding to obtain a final judgment of possession, and "in those cases where a month-to-month tenancy has the protection of rent control legislation, the certificate of eviction removes such protection and permits termination of the month-to-month tenancy by the service of a thirty-day notice."[23] The issuance of the DHCR's certificate of eviction permits a landlord to serve the tenant with a notice terminating the tenancy and, thereafter, to commence a holdover proceeding for nonprimary residence.[24]

Rent-stabilized tenants, unlike statutory rent-controlled tenants, have renewable leases. A landlord that wishes to begin a nonprimary-residence holdover proceeding must first serve the appropriate predicate notices and then wait for the stabilized lease to expire before commencing the holdover proceeding.[25] An owner may terminate the tenancy of a tenant who sublets contrary to the RSC's terms[26] or who assigns a lease without the owner's written consent,[27] but no action or proceeding to terminate a stabilized tenancy for nonprimary residence may be commenced before the tenant's lease expires.[28] The landlord of a rent-stabilized tenant need not obtain a certificate of eviction from the DHCR.[29]

C. Declaratory Judgments

A landlord of a rent-stabilized tenant may proceed on nonprimary-residence grounds by two distinct methods. The landlord may seek either a declaratory-judgment that a particular rental unit is no longer the tenant's primary residence or begin a summary proceeding to recover possession of the rental unit, claiming that a primary-residence violation forfeited the tenant's renewal rights. It does not matter whether a landlord chooses to litigate a nonprimary residency issue by a declaratory-judgment action or by summary eviction proceeding. As one court explained, "Whether the landlord seeks a declaration of nonprimary residency, or directly seeks possession claiming that renewal rights have been forfeited because of nonprimary residency, the ultimate objective is the same, namely, termination of the rent-stabilized tenancy."[30]

III. Landlord's Burden of Proof in Nonprimary-Residence Proceedings

The landlord bears the burden of proof to evict a rent-regulated tenant. The tenant can be evicted if the landlord can show that a tenant did not use the rent-stabilized apartment as a primary residence[31] for the preceding lease term up to the point at which the Golub nonrenewal notice was served. For a rent-controlled apartment, for which there is no existing lease, the preceding lease term is irrelevant. What counts is whether the rent-controlled tenant maintained the apartment as a primary residence for the preceding two years. These time frames are called the "relevant period."

The inquiry is fact-sensitive. To prove its case, a landlord must establish by a preponderance of the evidence that the tenant does not have an ongoing, substantial physical nexus with the premises for actual living purposes.[32] If a landlord establishes that the tenant does not use the rental unit as the primary residence, the burden shifts to the tenant. The tenant must then show an ongoing, substantial, physical nexus with the controlled premises for actual living purposes—which is best demonstrated by objective, empirical evidence.[33] A landlord that cannot establish that the tenant does not use a rent-stabilized apartment as a primary residence must offer the tenant a renewal lease.

The RSC offers factors to ascertain whether a rent-stabilized tenant uses the subject apartment as a primary residence.[34] These factors include (1) a tenant's use of an address other than the housing accommodation as a place of residence on any tax return,[35] motor vehicle registration, driver's license, or other document filed with a public agency; (2) a tenant's use of another address for voting; (3) a tenant's occupancy of the housing accommodation for fewer than 183 days in the most recent calendar year, except for temporary periods of relocation permitted by the RSC; and (4) a tenant's subletting of the housing accommodation.[36] These factors must be viewed in their totality; no single factor is determinative.[37]

Although the factors listed above represent the standard indicia, no fixed criteria determine primary residence,[38] a test that differs from domicile. Courts have often looked to a number of other factors in determining whether a tenant occupies a rent-regulated apartment as the primary residence. Some courts give more consideration to the address the tenant lists on income-tax returns, driver's license, motor vehicle registration, voter registration, or other documents filed with public agencies.[39] Other courts will consider factors like the address the tenant uses for telephone billing as well as the amount of telephone or electrical usage to determine a tenant's primary residence.[40]

In *Toa Constr. Co. v. Tsitsires*,[41] the tenant chose homelessness over living in the apartment, possibly due to mental illness, drugs, or alcohol. The tenant argued that the landlord failed to prove that tenant had an alternative address that he used as his primary residence.[42] The court found that proof of an alternative address is but one factor in determining primary residence. The court listed several other factors that help determine primary residence, including the tenant's telephone usage, the tenant's utility usage, video surveillance, and a landlord's employee's testimony about a tenant's absence from a rent-regulated unit.[43] The court ultimately ruled in the landlord's favor but not before noting that a tenant's under-use of a rent-regulated premises "may not alone suffice for a finding of nonprimary residence, at least in circumstances where the tenant's absence is attributable to a credible, excusable reason."[44]

In another case, the Appellate Division found that a tenant was entitled to a renewal lease even though the tenant owned a condominium in Florida, registered her car there, and had a restricted Florida driver's license.[45] The court evaluated the tenancy's entire history and concluded that the New York apartment was the tenant's primary residence.[46] That court found that the tenant maintained her primary residence in New York because she voted in New York, paid New York income taxes, possessed a New York State driver's license, received ongoing care from medical professionals in New York, and kept her clothing in her New York apartment.[47]

IV. Special Considerations for Certain Tenants

Some tenants are entitled to special considerations in the context of a primary-residence analysis. Those most identified to receive modified treatment under the primary-residence rule are individuals in the military, the elderly, the disabled, full-time students, and those temporarily absent from their rent-regulated apartments for employment or medical purposes.[48]

The two common factors in inquiring whether tenants present excusable reasons for their absences are whether they will live in the subject premises when they are able to do so and whether the reason for their absence will end so as to allow them to use the subject premises as a conventional primary residence.[49]

One court has elaborated on the policies behind this exception: "If a senior citizen chooses to retain her rent-controlled apartment as her primary residence and pays her rent monthly while confined in a geriatric facility or a nursing home, it should be her right to do so."[50] This court further explained that "[t]he primary residence law was not intended and should not apply to a senior citizen who . . . has no intention of abandoning her rent-regulated apartment."[51] The court found that a landlord could not repossess a rent-controlled apartment from an 84-year-old tenant suffering from Alzheimer's disease who resided in a nursing home and could not immediately return to her apartment.[52] The court found that the tenant did not voluntarily relinquish her rights to the apartment, would be able to function at home with a full-time attendant, had all her furniture and belongings in the apartment, and would be at the nursing home for nursing care until the family arranged for in-home care. The court explained that the primary-residence law is directed against tenants who have established primary residence elsewhere while continuing to retain rent-regulated apartments for convenience and monetary benefits.[53]

In one Appellate Term case, a rent-stabilized tenant with a family of 10 was forced to vacate her apartment after a fire destroyed it.[54] After living in a shelter with her family for three months, the tenant bought a one-family home under the DHCR guidelines. The mortgage on the house was conditioned on her living there for one year as a primary residence. Despite her commitment to this mortgage condition, the court found that a "temporary relocation to another dwelling place does not, by itself . . . establish that the premises is not her primary residence."[55] Under these circumstances, therefore, the tenant's temporary housing excused her absence from the primary residence.

Courts are less likely to find that a tenant has an "ongoing physical nexus" with the premises if the tenant is incarcerated for an indeterminate period of time. One court found that a landlord was entitled to possession of a rent-controlled apartment because the statutory tenant had been convicted of second-degree murder and sentenced to an indefinite term of 15 years to life.[56] That court stated that a tenant who will be absent from the premises for the foreseeable future is not a person who will have an "ongoing, substantial, physical nexus with the controlled premises for actual living purposes."[57]

Courts use a similar analysis when determining whether a tenant who spends a significant amount of time away from the regulated apartment for employment reasons uses it as a primary residence. In one nonprimary-residence holdover proceeding, the tenant acknowledged that she had slept in the apartment no more than once or twice a week and that she ran a business at another apartment where she worked 17 hours a day, six days a week, including nights.[58] The court found that these facts did not by themselves show that she did not use the apartment as her primary residence.[59] All her documentary evidence showed that the apartment was her residence, and almost all her furniture and possessions were maintained there. In another nonprimary holdover case, the court held for the tenant, a singer with a busy tour schedule who occupied a regulated apartment only three days a month.[60] The court noted that "the ordinary meaning of the word 'primary' is 'first in rank or importance: chief, principal.'"[61] The court found that her apartment was more central than the houses, hotels, and dormitories she lived in while on tour, that she kept her piano and personal possessions in her apartment, and that she intended to stay there when her professional life allowed.[62]

V. Primary-Residence Requirement: Courts Look To Subletting

To determine whether a rent-regulated tenant maintains an apartment as a primary residence, courts often consider whether the tenant has sublet the rental unit.[63] However, proceedings based on illegal subletting and nonprimary-residence grounds have different requirements. A landlord should carefully choose its theory of the case—subletting or nonprimary residence. The procedure to begin an illegal-sublet summary proceeding bears some similarity to the procedure to begin a nonprimary-residence proceeding. Both require a termination notice; both place a heavy factual burden on the landlord. To succeed on an illegal-sublet claim, a landlord must prove that the prime tenant no longer resides at the subject premises and that the prime tenant sublet the premises to a subtenant without the landlord's consent.[64]

Although the burden rests on the landlord to prove illegal subletting, the nonrenewal notice need satisfy only RSC § 2524.2(b) and state the grounds for the proceeding and the facts on which the grounds are based. In one case, the tenant argued that the nonrenewal notice lacked the requisite factual information under RSC § 2524.2(b).[65] The landlord claimed that the notice was sufficient because it alleged not only that the tenant had sublet the subject premises without the landlord's permission but also that the landlord believed that the tenant's principal residence was in Florida. The court found that "[e]ither allegation by itself would not constitute the 'facts necessary to establish the existence' of the nonprimary residence ground. However, the allegations together provide sufficient facts to place the respondent on notice of the petitioner's claims against her. . . . [E]nlightenment can be achieved under the liberal discovery allowed in primary residence cases."[66] In another case, the landlord began a summary-eviction proceeding for alleged illegal subletting.[67] The tenant claimed that the landlord's notice to cure and termination notice failed to include the necessary factual statements in that they did not name the record tenant's new primary address. The record tenant moved to dismiss. The court found under RSC § 2524.2(b) that a landlord must provide only the facts necessary to establish a ground for eviction. The landlord's notices were sufficient because they alleged that the record tenant sublet the premises to a named individual without the landlord's permission and that the tenant no longer resided at the premises. The court concluded that the notices did not have to specify the record tenant's new primary residence.[68]

A lease silent on a tenant's right to assign or sublet does not confer greater rights on a tenant than what the RPL and the RSC require. In *Sherry House Assocs. v. Kaye*, the landlord filed an illegal-sublet proceeding against the tenant.[69] The Civil Court dismissed the proceeding because the tenant's original lease did not contain a clause restricting subletting. The Appellate Term, First Department, reversed; it held that unless an affirmative agreement (such as a lease provision permitting the tenant to sublet at will) expanded the tenant's right to sublet, the right to sublet is governed by RPL § 226-b and RSC § 2525.6. The Appellate Term found that the tenant's failure to obtain the landlord's written consent before subletting is a substantial breach of lease or tenancy under RPL § 226-b(5) and thus that the tenancy terminated under RSC § 2525.6(f).[70]

A landlord may not use disclosure to convert a subletting case into a nonprimary case.[71] In *Metropolitan Life Ins. Co. v. Butler*, the court denied the landlord's motion for disclosure in its illegal-sublet proceeding.[72] The landlord claimed that the record tenants no longer occupied the premises. One of the tenants claimed that she primarily resided in the subject apartment with her son. The court stated that the landlord's claims that the record tenants no longer used the premises as their primary residence was appropriate in a nonprimary-residence case but not in an illegal-sublet case, because a landlord may not bootstrap a nonprimary-residence claim onto an illegal-sublet proceeding. The court wrote in the context of this illegal-sublet proceeding that the discovery the landlord sought is a prohibited "fishing expedition." The court noted that in contrast with nonprimary-residence proceedings, no presumption of disclosure arises in sublet cases.[73]

Another main difference between illegal-sublet and nonprimary proceedings is the notice-to-cure requirement. A tenant may cure an illegal sublet but not a primary-residence violation.[74] Additionally, a court lacks jurisdiction in a landlord's proceeding to recover possession of a rent-stabilized apartment if the tenant cures both an illegal sublet and a rent overcharge within the time set forth in landlord's notice to cure.[75] After a landlord gives the tenant a cure notice, no ground exists to terminate the tenancy, and the termination notice is deemed ineffective, once the tenant has timely cured the violations.

VI. Illusory Tenancy

An "illusory tenant" is someone who, while assuming the guise of a prime tenant, enters into a sublease arrangement intended, directly or indirectly, to evade rent-stabilization requirements. Courts may find an illusory tenancy when the prime tenant subleases the apartment for profit or deprives the subtenant of stabilization rights.[76] A court that finds an illusory tenancy will accord the subtenant full rent-stabilization protection.[77]

Determining whether an illusory tenancy exists involves assessing the parties' good faith.[78] Courts will determine whether a subtenancy allowed the prime tenant or the landlord to profit by violating the rent-stabilization laws, which were designed to prevent unjust, oppressive rents and to avoid profiteering, speculation, and other disruptive practices.[79]

VII. Roommates and the Primary-Residence Rule

When a prime tenant vacates a rent-regulated apartment or dies, the landlord may attempt to evict any occupants living in the apartment. But RPL § 235-f, known as the Roommate Law, and RSC § 2204.6(d)[80] protect occupants who qualify as family members. Under the RSC, the term "family member" includes the primary tenant's husband, wife, son, daughter, stepson, stepdaughter, father, mother, stepfather, stepmother, brother, sister, grandfather, grandmother, grandson, granddaughter, father-in-law, mother-in-law, son-in-law, and daughter-in-law.[81] In the Roommate Law's context, the primary residence of a tenant or a tenant's spouse is treated interchangeably with the prime tenant's. The RSC also protects other persons residing with the vacating tenant in the housing accommodation as a primary or principal residence if they can prove that they are non-traditional family members who had an emotional commitment and financial interdependence with the record tenant.[82]

Under the RSC, when the record tenant dies, family members who resided in the unit for at least two years are entitled to succeed to the tenancy.[83] The Appellate Term has interpreted the succession-rights rule broadly to find that a granddaughter who forged her grandmother's signature on the renewal leases was nevertheless entitled to succession rights.[84] The court found the granddaughter's succession rights "firmly established"[85] and not forfeited even though she had concealed her occupancy from the landlord.

The RSC allows an occupant to raise a succession-rights defense in a nonprimary-residence proceeding against a record tenant. This defense is "rationally related to the legitimate governmental interest in preventing loss of housing by apartment inhabitants upon the death of the tenant of record."[86] A record tenant's family member may acquire "independent possessory rights" to the rental unit if the family member had lived with the record tenant since the "inception of the tenancy"[87] or for two years before the tenant departs or dies.

A. Non-traditional Family Members

The *Braschi* court was the first to protect non-traditional family members from being evicted from a rent-regulated apartment upon the record tenant's death. In *Braschi*, the Court of Appeals held that RSC § 2204.6(d) extended to a gay life partner upon the statutory tenant's death.[88] In so finding, the court pointed out that the men had lived together as permanent life partners for more than 10 years; that they regarded one another, and were regarded by friends and family, as spouses; that they regularly visited each other's families and attended family functions together as a couple; that the partner considered the apartment his home and listed it as his address on his driver's license and passport and received his mail at the apartment; that the partner's occupancy was known to the building's superintendent and doormen, who viewed the two men as a couple; that financially, the two men shared all obligations, including a household budget; that they were authorized signatories of three safe-deposit boxes and maintained joint checking and savings accounts and joint credit cards; that the rent was often paid with checks from their joint checking account; that one of the men executed a power of attorney in the remaining tenant's favor so that the remaining tenant could make necessary decisions—financial, medical, and personal—for him during his illness; and that the life partner who sought succession rights was the named beneficiary of his partner's life insurance policy as well as the primary legatee and co-executor of his estate.[89]

RPL § 235-f has also been interpreted to include non-traditional family members. Practitioners should note, however, that the Roommate Law applies only to an apartment occupied as a primary residence.[90] The Court of Appeals has held that the Roommate Law does not apply to tenants "living temporarily in student housing";[91] student housing is not considered a primary residence.

In another case, the Appellate Division found that the evidence established the deceased tenant's roommate's entitlement to succeed as a non-traditional family member to the rent-controlled tenancy.[92] The court found that the primary-residence requirement was satisfied because the occupant lived with the record tenant for eight years before the tenant died.[93]

B. Special Considerations for Succession Rights

The rules for succession rights are modified for disabled or elderly persons. To succeed to a tenancy, an individual must live in the rental unit with the record tenant for either two years before the tenant's permanent vacatur or since the tenancy began.[94] Senior citizens (someone over 62) and disabled persons must prove only one year of cohabitation with the record tenant to establish succession rights.[95] As with most special statutory considerations, this rule serves an important public policy. The one-year allowance gives the elderly and disabled the opportunity to establish their succession rights despite any temporary absences from the rent-regulated apartment.[96]

Additionally, the RSC allows for interruptions in the two-year residency requirement for certain reasons.[97] As explained above, these exceptions include active military duty, enrollment as a full-time student, employment requiring temporary relocation, hospitalization, and other reasonable grounds.[98]

VIII. Landlord May Not Contract Away the Right to Claim Nonprimary Residence

Rent regulation often overrides contractual agreements between the landlords and their tenants and subtenants. By way of example, the right to sublet a rent-stabilized apartment is not a private right between two parties and is therefore not subject to the defenses of estoppel, laches, waiver, reliance, or the passing of the statute of limitations in bringing an action or proceeding for violating a lease. The right to do so is a matter of public policy.[99]

A landlord's attempt to waive the right to bring a nonprimary-residence holdover proceeding is void: a landlord may not contract away the right to claim nonprimary residence.[100] Rent-regulatory laws are frustrated when tenants tie up rent-stabilized apartments, and "such occupancies should be discouraged."[101] In one Appellate Term case, a landlord agreed to waive her right to object to the tenant's occupancy on the ground of nonprimary residence. Refusing to enforce that agreement, the court found that "when a tenant does not maintain the apartment as a primary residence, she is not entitled to protection under the rent regulation laws."[102]

In *270 Riverside Drive, Inc. v. Wilson*,[103] the landlord allowed the tenant to sublease the premises. After the sublease expired, the subtenant, with the record tenant's cooperation, allowed another subtenant to move in and concealed their continued subtenancy from the landlord. The court found that the tenant violated RSL § 26-511(c)(12)(f). The court rejected the subtenants' claim that the landlord created an implied tenancy with them and thus waived its right to contest the subtenants' occupancy, because the tenant never surrendered the premises to the landlord. The illusory-tenancy defense also failed because there was no evidence that the sublet, which the landlord had approved, was designed to profiteer or to deprive the subtenants of RSL rights.[104]

IX. Estoppel, Waiver, and Fraud

An occupant may raise estoppel, waiver, or fraud as defenses to a holdover proceeding for nonprimary residence. Waiver is the voluntary abandonment or relinquishment of a known right.[105] Estoppel precludes a moving party from alleging or denying a fact because of a previous action, inaction, allegation, or denial.[106] Fraud is an artifice that deceives another.[107] These three categories are often grouped together, and determining whether an act should be viewed as estoppel, waiver, or fraud requires analyzing the facts carefully.[108]

Waiver may be inferred from a landlord's accepting rent in some circumstances.[109] But accepting a few rent payment checks in combination with other acts that show that the landlord has not chosen to waive its rights under the lease may belie the waiver defense.[110] In *Herald Towers LLC v. Sun Lord Int'l, Inc.*, the landlord brought a nonprimary-residence holdover against a corporate tenant and moved for summary judgment. The court refused to grant the motion. The court noted that it was necessary to examine at trial the tenant's claim that he was a lawful tenant and forced to create the "fictitious" entity, which was formed solely in response to the prior landlord's "bad faith" insistence that a "lease could only be given in a corporate name." The court also found it necessary to examine at trial whether the landlord had waived its right to claim that the tenant was not the lawful tenant due to the landlord's acceptance of the tenant's personal checks for over 20 years.[111]

Waiver or estoppel cannot create rent-stabilized status.[112] In once case, the tenant moved into a rent-stabilized apartment after the death of his mother, the previous tenant.[113] Contending that the owners of the premises represented that the tenant would be entitled to a rent-stabilized lease renewal, the tenant brought a declaratory-judgment action to declare the apartment rent stabilized. On appeal, the court found that a tenant who does not reside with the nonpurchasing tenant for at least two years

may not be named as a tenant on the renewal lease and that waiver or equitable estoppel may not create rent-regulation coverage.[114]

X. Husband and Wife Maintaining Separate Dwellings as Their Primary Residences

A husband and wife may maintain two different primary residences without being subject to eviction for a primary-residence violation.[115] In one case, a husband and wife bought a condominium in Florida with their son. The husband adopted the Florida condominium as his primary residence while the wife maintained a rent-stabilized apartment in New York City as her primary residence. The landlord of the New York apartment refused to offer the couple a renewal lease and sought to evict them because only the wife regarded the apartment as a primary residence. The Court of Appeals noted that it was not unusual for an older couple to purchase property for use during the winter and for specific vacations. The landlord had argued that the wife treated the Florida condominium as her primary residence because she filed joint tax returns listing the condominium as a primary residence. The court reasoned that the address on her tax return was only one factor to consider in discerning her primary residence.[116]

XI. Landlord's Right to Investigate a Suspected Primary Residence Violation

Landlords that suspect that a tenant is violating the primary-residence rule have the right to investigate. Because it is difficult to prove a nonprimary-residence case, a landlord may elect to hire a private investigator to gather relevant information about a tenant's presence at the subject apartment.[117] A landlord seeking to establish the necessary factual showing of a primary-residence violation may also seek access to various databases, including those containing addresses, registrations, and debt collection information. One Civil Court opinion explained the concept this way: "Just as primary residence may be found despite the tenant's absence, nonprimary residence may be found despite some presence by the tenant."[118] Therefore, some investigation might be necessary for a landlord to meet its burden in court. Practitioners should be mindful that once "a landlord's evidence justifies the conclusion" that the tenant no longer maintains the apartment at issue as a primary residence, "the tenant's credibility will be of particular importance to the court in determining this largely subjective question."[119]

Toa Construction illustrates how a landlord can prove that a tenant does not use the subject premises as the primary residence—through video surveillance, telephone bills showing that the tenant did not use the telephone during the relevant two-year lease period, and testimony from an employee of the landlord that he did not see the tenant during that period.[120]

XII. Disclosure Motions

Nonprimary-residence cases are fact-driven. It is important for the landlord to obtain disclosure. Summary proceedings, however, are "entirely creatures of statute," created to provide an efficient remedy in routine contexts.[121] Disclosure is therefore inconsistent with the speedy determination of rights that summary proceedings seek to resolve.[122] Leave of court is required for disclosure in a summary proceeding[123] because litigants sometimes abuse disclosure to stall litigation or to secure disclosure for a case different from the one being litigated. But disclosure is not always inherently "hostile to the nature of a summary proceeding."[124] Sometimes disclosure protects tenants; a landlord might move to dismiss a proceeding, without forcing a tenant to endure a trial, if the tenant can show during disclosure that the proceeding is not meritorious. Disclosure also allows a party to move for summary judgment if what is discovered shows an absence of material facts. In this regard, a tenant's summary-judgment motion in a nonprimary-residence holdover best awaits the conclusion of disclosure.[125]

To prevail on a motion for disclosure, a party must meet the "ample need" requirement.[126] Factors to determine whether this requirement is met include whether the moving party has asserted sufficient facts to establish a cause of action, whether gathering additional information is necessary and directly related to the proceeding, whether the requested disclosure is appropriately narrow and likely to clarify disputed facts, whether any potential prejudice may be reduced or eliminated by a court's conditional grant, whether the information sought is known only to the other side, and whether disclosure can be structured to protect tenants from any adverse effect of disclosure.[127] These factors are important for pro se tenants, who are likely unaware of the consequences related to disclosure. They also help prevent landlords and tenants from engaging in fishing expeditions.[128] The "ample need" requirement and its detailed analysis may dissuade a landlord from asserting non-meritorious reasons to support a disclosure motion and may dissuade a tenant from asserting irrelevant or unrelated defenses.[129]

Although the presumption was previously against disclosure in the nonprimary-residence summary-proceeding context,[130] courts now apply a presumption that disclosure is necessary to ensure that all relevant information is obtained and considered when a motion for leave to disclose is made in a nonprimary-residence proceeding.[131] When facts concerning the tenant's residence and the use made of the leased premises are peculiarly within

the tenant's knowledge, the law recognizes a presumption favoring disclosure. If "the requests are palpably overbroad, the court will not prune the requests to 'cull the good from the bad.'"[132] Production of documents must also be limited in time to correspond to the relevant period and may not seek confidential information, like personal or financial information unrelated to the address.

XIII. Attorney Fees

A prevailing party is entitled to attorney fees from the losing party if the parties' agreement or a statute or court rule authorizes the fees.[133] If the lease contains a standard attorney fee provision, attorney fees may be awarded to the prevailing party in a summary proceeding based on nonprimary residence. If the proceeding is commenced at the expiration of a lease term, the ultimate issue in that proceeding is whether the tenant fulfilled the contractual duty to vacate the premises. This attorney fee allowance exists because of its contractual basis.[134]

Many leases with attorney fee provisions allow only landlords to recover attorneys' fees based on tenant's default. RPL § 234 provides that in every lease in which that provision exists, the landlord reciprocally covenants that a tenant who prevails in a plenary action or summary proceeding may recover attorney fees.[135]

XIV. Conclusion

Tenants in rent-regulated units must maintain that home as their primary residence. Failing to do so might result in the landlord's bringing an action or proceeding to terminate the tenancy. The policies behind rent regulation are well documented and well grounded: "The Legislature has made clear its intention that regulatory protection should not be available where the tenant's claim to the subject premises is based on less than the need for a place to call home," and "[t]his intent is entirely consonant with the public policy sought to be advanced, which is to promote the availability of affordable housing units."[136]

It is equally important that the landlords be held to strict rules about how and when they may bring nonprimary-residence holdover proceedings. These rules have been promulgated to ensure that landlords properly notify tenants that they are in danger of losing their homes and to give tenants the safeguards necessary to protect their rights.

Endnotes

1. 9 N.Y.C.R.R. §§ 2204.1(a); 2524.1(a).
2. Omnibus Housing Act, ch. 403, (1983), N.Y. Rent Stab. Code, N.Y.C. Admin. Code § YY51-6.0, 26-504(a)(1).
3. *Park S. Assocs. v. Mason*, 123 Misc. 2d 750, 753, 474 N.Y.S.2d 672, 675 (Hous. Part Civ. Ct., N.Y. Co. 1984), *aff'd*, 126 Misc. 2d 945, 488 N.Y.S.2d 1020 (App. Term 1st Dep't 1984) (*per curiam*).
4. *Nussbaum Resources I LLC v. Gilmartin*, 195 Misc. 2d 145, 148-49, 756 N.Y.S.2d 408, 411 (Hous. Part Civ. Ct., Bronx Co. 2003).
5. *See, e.g., Emay Props., Inc. v. Norton*, 136 Misc. 2d 127, 128, 519 N.Y.S.2d 90 (App. Term 1st Dep't 1987) (*per curiam*); *In re LJM Venture No. 1 v. Joy*, 105 Misc. 2d 291, 296, 432 N.Y.S.2d 58, 61 (1980) (holding that move to nursing home by tenant was a change in primary residence).
6. RPL § 232-a; *Hughes v. Lenox Hill Hosp.*, 226 A.D.2d 4, 6, 651 N.Y.S.2d 418, 421 (1st Dep't 1996).
7. *Rosen v. Wade*, 99 Misc. 2d 1114, 1115, 418 N.Y.S.2d 258, 259 (Civ. Ct., N.Y. Co. 1979).
8. 9 N.Y.C.R.R. § 2523.5(a); *Golub v. Frank*, 65 N.Y.2d 900, 901, 493 N.Y.S.2d 451, 451, 483 N.E.2d 126, 126 (1985) (mem.).
9. 9 N.Y.C.R.R. § 2524.2(c)(2).
10. *Id.*; Warren A. Estis & William J. Robbins, *Notices to Tenant—When Do They Become Effective?*, N.Y.L.J., Feb 2, 2005, p. 5, col. 1.
11. 9 N.Y.C.R.R. § 2524.2(b).
12. 9 N.Y.C.R.R. § 2524.4(c); *Glenbriar Co. v. Nesbitt*, N.Y.L.J., Aug. 12, 1998, p. 21, col. 5 (Hous. Part Civ. Ct. Bronx Co.) ("[B]efore commencing a holdover proceeding to remove a tenant from an apartment on [nonprimary-residence] grounds, the landlord must give the tenant notice at least 30 days before commencement of the proceeding of its intention to [bring] eviction proceedings. The two notices may be combined, as they were in this case, in a single document.") (citing 9 N.Y.C.R.R. § 2524.4(c)).
13. *Herman v. Meryn*, 159 Misc. 2d 851, 853, 607 N.Y.S.2d 216, 217 (Hous. Part Civ. Ct., N.Y. Co. 1993).
14. *390 W. End Assocs. v. Atkins*, N.Y.L.J., June 3, 1998, p. 26, col. 3 (Hous. Part Civ. Ct., N.Y. Co.) (citing *340 E. 57th St. Assoc. v. Comras*, N.Y.L.J., Nov. 30, 1994, p. 25, col. 6 (App. Term 1st Dep't) (*per curiam*)).
15. *Regency Towers LLC v. Landou*, 10 Misc. 3d 994, 996, 807 N.Y.S.2d 863, 864 (Hous. Part Civ. Ct., N.Y. Co. 2006) (Gerald Lebovits, J.).
16. *See* RPAPL § 735; *390 West End Assocs.*, N.Y.L.J., June 3, 1998, p. 26, col. 3.
17. 9 N.Y.C.R.R. § 2524.2(b); *Berkeley Assocs. Co. v. Camlakides*, 173 A.D.2d 193, 196, 569 N.Y.S.2d 629, 631 (1st Dep't 1991) (mem.).
18. 9 N.Y.C.R.R. § 2524.2(b); *MSG Pomp Corp. v. Doe*, 185 A.D.2d 798, 800, 586 N.Y.S.2d 965, 967 (1st Dep't 1992) (mem.).
19. *Bellstell 140 E. 56th St., LLC. v. Layton*, 180 Misc. 2d 25, 27, 687 N.Y.S.2d 536, 539 (Hous. Part Civ. Ct., N.Y. Co. 1999).
20. *E.g.*, *First Sterling Corp. v. Zurkowsk*i, 142 Misc. 2d 978, 978, 542 N.Y.S.2d 899, 900 (App. Term 1st Dep't 1989) (*per curiam*); *Nussbaum Resources I LLC*, 195 Misc. 2d at 147, 756 N.Y.S.2d at 410.
21. *Fisher v. Velasquez*, 126 Misc. 2d 24, 26, 480 N.Y.S.2d 992, 994 (Hous. Part Civ. Ct., Kings Co. 1984).
22. Emergency Housing Rent Control Law, N.Y. Unconsol. Law § 8585.2(b); N.Y.C. Admin. Code § 26-408(b)(2); *Quiles v. Term Equities*, 22 A.D.3d 417, 420, 802 N.Y.S.2d 679, 681-82 (1st Dep't 2005) (mem).
23. *Fisher*, 126 Misc. 2d at 25, 480 N.Y.S.2d at 993.
24. *Quiles*, 22 A.D.3d at 420, 802 N.Y.S.2d at 682.
25. 9 N.Y.C.R.R. § 2524.2 (c).
26. *Id.*; § 2520.1.
27. *Id.*; § 2525.6(f).

28. *Id.*
29. Id. § 2524(c).
30. *Park House Partners, Ltd. v. De Irazabal*, 140 A.D.2d 84, 88, 532 N.Y.S.2d 249, 252 (1st Dep't 1988).
31. 9 N.Y.C.R.R. § 2524.4(c).
32. *See E. End Temple v. Silverman*, 199 A.D.2d 94, 94, 605 N.Y.S.2d 56, 56 (1st Dep't 1993) (mem.).
33. Daniel Finkelstein & Lucas A. Ferrara, *Landlord Tenant Practice in New York* § 15:46, at 15-49 (2006 ed.); Andrew Scherer, *Residential Landlord-Tenant Law in New York* § 8:207, at 585 (2006 ed.).
34. 9 N.Y.C.R.R. § 2520.6(u).
35. http://www.tenant.net/DHCR_info/Fact_Sheets/fact07a.html ("A tenant may be required to submit proof in court that he or she filed a New York City Resident Income Tax Return specifying the address of the subject apartment as his or her residence for the most recent taxable year for which such return should be filed.") (last visited Apr. 24, 2006).
36. 9 N.Y.C.R.R. § 2200.3.
37. *Chelsmore Apts. v. Garcia*, 189 Misc. 2d 542, 544, 733 N.Y.S.2d 329, 330 (Hous. Part Civ. Ct., N.Y. Co. 2001).
38. Scherer, *supra* note 33, at § 8:208, at 586-88.
39. *Hart Future Co. v. Rose*, N.Y.L.J., May 10, 2000, p. 31, col. 2 (Hous. Part Civ. Ct., N.Y. Co.).
40. *See Janco Realty Corp. v. Lee*, N.Y.L.J., June 16, 1987, p. 11, col. 1 (App. Term, 1st Dep't) (*per curiam*).
41. 9 Misc. 3d 469, 798 N.Y.S.2d 674 (Hous. Part Civ. Ct., N.Y. Co. 2005) (Gerald Lebovits, J.). *Toa Construction* is currently on appeal before the Appellate Term, First Department. Judge Lebovits did not write the portions in this article about this case. These portions were written entirely by Mr. Li.
42. *Id.* at 470, 798 N.Y.S.2d at 676.
43. *Id.* at 474, 798 N.Y.S.2d at 679.
44. *Id.* at 490, 798 N.Y.S.2d at 690 (quoting *Emel Realty Corp. v. Carey*, 188 Misc. 2d 280, 282, 729 N.Y.S.2d 228 (App. Term 1st Dep't) (*per curiam*), *aff'd*, 288 A.D.2d 163, 733 N.Y.S.2d 188 (1st Dep't 2001) (mem.).
45. *Four Winds Assocs. v. Rachlin*, 248 A.D.2d 352, 353, 669 N.Y.S.2d 650, 651 (2d Dep't. 1998) (mem.).
46. *Id.*; *see also* Finkelstein & Ferrara, *supra* note 33, at § 13:115, at 13-58.
47. *Four Winds Assocs.*, 248 A.D.2d at 353, 669 N.Y.S.2d at 651.
48. *See, e.g.*, 9 N.Y.C.R.R. § 2523.5(b); *Soybel v. Gruber*, 136 Misc. 2d 430, 518 N.Y.S.2d 920 (Hous. Part Civ. Ct., N.Y. Co. 1987).
49. *See Toa Const.*, 9 Misc. 3d at 492, 798 N.Y.S.2d at 691-92.
50. *Soybel*, 136 Misc. 2d at 435, 518 N.Y.S.2d at 923-24.
51. *Id.* at 433, 518 N.Y.S.2d at 922.
52. *Id.* at 437, 518 N.Y.S.2d at 924.
53. *Id.* at 434, 518 N.Y.S.2d at 923.
54. *Corona Apts. v. Benitez*, 1 Misc. 3d 79, 81, 769 N.Y.S.2d 349, 350 (App. Term 2d Dep't, 2d & 11th Jud. Dists. 2003) (mem.).
55. *Id.* at 80.
56. *Emay Props. Corp. v. Norton*, 136 Misc. 2d 127, 129, 519 N.Y.S.2d 90, 92 (App. Term 1st Dep't 1987) (*per curiam*).
57. *Id.*
58. *Sarraf v. Szunics*, 132 Misc. 2d 97, 98, 503 N.Y.S.2d 513, 515 (Hous. Part Civ. Ct., N.Y. Co. 1986).
59. *Id.* at 100, 503 N.Y.S.2d at 516.
60. *Coronet Props. Co. v. Brychova*, 122 Misc. 2d 212, 213, 469 N.Y.S.2d 911, 912 (Hous. Part Civ. Ct., N.Y. Co. 1983).
61. *Id.*
62. *Id.*
63. *See, e.g.*, 9 N.Y.C.R.R. § 2200.3(j); *Toa Const.*, 9 Misc. 3d at 489, 798 N.Y.S.2d at 694.
64. *Bellstell 140 East 56th St.*, 180 Misc. 2d at 29, 687 N.Y.S.2d at 540.
65. *London Terrace Gardens v. Sacks*, 149 Misc. 2d 292, 292, 563 N.Y.S.2d 1017, 1018 (Hous. Part Civ. Ct., N.Y. Co. 1990).
66. *Id.* at 294, 563 N.Y.S.2d at 1019.
67. *Bellstell 140 E. 56th St*, 180 Misc. 2d at 29, 687 N.Y.S.2d at 539.
68. *Id.*, 687 N.Y.S.2d at 539.
69. *Sherry House Assocs. v. Kaye*, 167 Misc. 2d 729, 730, 643 N.Y.S.2d 881, 881 (App. Term 1st Dep't 1996) (*per curiam*).
70. *Id.*, 643 N.Y.S.2d at 881.
71. *See Renwick Realty v. Molina*, N.Y.L.J., Nov. 20, 2002, p. 26, col. 1 (Hous. Part Civ. Ct., N.Y. Co.).
72. N.Y.L.J., Dec. 19, 2001, p. 17, col. 1 (Hous. Part Civ. Ct., N.Y. Co.) ("At oral argument on the motion, petitioner claimed discovery was necessary because the facts regarding respondents' alleged cure were known only to respondent. If petitioner submitted a properly tailored request for discovery on this issue, perhaps ample need could have been demonstrated.").
73. *Id.*
74. *See Pamela Equities Corp. v. Camp*, 127 Misc. 2d 395, 397, 486 N.Y.S.2d 149, 152 (Hous. Part Civ. Ct., N.Y. Co. 1985); *Lufkin v. Drago*, 126 Misc. 2d 177, 179, 481 N.Y.S.2d 850, 852 (Hous. Part Civ. Ct., N.Y. Co. 1984); Finkelstein & Ferrara, *supra* note 33, at § 11:447, at 11-220.
75. *Husda Realty Corp. v. Padien*, 136 Misc. 2d 92, 518 N.Y.S.2d 99 (Hous. Part Civ. Ct., N.Y. Co. 1987).
76. RPL § 226-b; N.Y.C. Admin. Code, § 26-511(c)(12)(f); *270 Riverside Drive, Inc. v. Wilson*, 195 Misc. 2d 44, 755 N.Y.S.2d 215 (Hous. Part Civ. Ct., N.Y. Co. 2003).
77. *Primrose Mgmt. Co. v. Donahue*, 253 A.D.2d 404, 676 N.Y.S.2d 585 (1st Dep't 1998) (mem.) (holding that subtenancy established from beginning to allow prime tenant improperly to profit in violation of rent regulations was an illusory tenancy, entitling subtenant protection under rent laws, especially where former building superintendent's knowledge or presumed knowledge of improper activities could be imputed to landlord).
78. RPL § 226-b; N.Y.C. Admin. Code § 26-511(c)(12)(f); *270 Riverside Dr.*, 195 Misc. 2d at 49, 755 N.Y.S.2d at 220.
79. RPL § 226-b; N.Y.C. Admin. Code § 26-511(c)(12)(f); *270 Riverside Dr.*, 195 Misc. 2d at 50, 755 N.Y.S.2d at 220.
80. 9 N.Y.C.R.R. § 2204.6(d) ("No occupant of housing accommodations shall be evicted under this section where the occupant is either the surviving spouse of the deceased tenant or some other member of the deceased tenant's family who has been living with the tenant.").
81. *Id.*, § 2520.6(o)(1).
82. *Id.*, § 2520.6(o)(2).
83. *Id.*, § 2523.5(b); *Riverton Assocs. v. Knibb*, 3 Misc. 3d 193, 194, 772 N.Y.S.2d 494, 495 (Hous. Part Civ. Ct., N.Y. Co. 2004), *rev'd*, 2005

N.Y. Slip Op. 25552, at *1, 2005 WL 3542476, at *1, 2005 N.Y. Misc. LEXIS 2933, *2 (App. Term 1st Dep't 2005) (*per curiam*).

84. 2005 N.Y. Slip Op. 25552, at *1, 2005 WL 3542476, at *1, 2005 N.Y. Misc. LEXIS 2933, at *2.
85. *Id*. 2005 WL 3542476, at *1, 2005 N.Y. Misc. LEXIS 2933, at *2.
86. *See* 9 N.Y.C.R.R. § 2523.5(b); *Black v. New York*, 13 F. Supp. 2d 538, 542 (S.D.N.Y. 1998).
87. *Id*.; *accord Stanford Realty Assocs. v. Rollins*, 161 Misc. 2d 754, 756, 615 N.Y.S.2d 229, 230 (Hous. Part Civ. Ct., N.Y., Co. 1994).
88. *Braschi v. Stahl Assocs. Co.*, 74 N.Y.2d 201, 211, 544 N.Y.S.2d 784, 794, 543 N.E.2d 49, 59 (1989).
89. *Id.* at 213, 544 N.Y.S.2d at 790, 543 N.E.2d at 55.
90. *Levin v. Yeshiva Univ.*, 96 N.Y.3d 484, 730 N.Y.S.2d 15, 754 N.E.2d 1099 (2001).
91. *Id*. at 498, 730 N.Y.S.2d at 24, 754 N.E.2d at 1107.
92. *Arnie Realty Corp. v. Torres*, 294 A.D.2d 193, 194, 742 N.Y.S.2d 240, 241 (1st Dep't 2002) (mem.).
93. *Id.*, 742 N.Y.S.2d at 241.
94. 9 N.Y.C.R.R. § 2523.5(b).
95. *Id.*; *Stanford Realty Assocs.*, 161 Misc. 2d at 756, 615 N.Y.S.2d at 230.
96. *Stanford Realty Assocs.*, 161 Misc. 2d at 755, 615 N.Y.S.2d at 230.
97. 9 N.Y.C.R.R. 2523.5(2).
98. *Id.*
99. RPL § 226-b; *270 Riverside Drive, Inc.*, 195 Misc. 2d at 47, 755 N.Y.S.2d at 218.
100. *Park Towers Co. v. Universal Attractions*, 274 A.D.2d 312, 313, 710 N.Y.S.2d 571, 572 (1st Dep't 2000) (mem.); *see* Finkelstein & Ferrara, *supra* note 33, at § 11:101, at 11-56.
101. *Park Towers*, 274 A.D.2d at 313, 710 N.Y.S.2d at 572.
102. *Rocky 116 LLC v. Weston*, 186 Misc. 2d 251, 253, 717 N.Y.S.2d 823, 825 (App. Term 1st Dep't 2000) (*per curiam*).
103. 195 Misc. 2d 44, 755 N.Y.S.2d 215 (Hous. Part Civ. Ct., N.Y. Co. 2003).
104. *Id*. at 51, 755 N.Y.S.2d at 221.
105. *Jefpaul Garage Corp. v. Presbyterian Hosp. in N.Y.*, 61 N.Y.2d 442, 459, 474 N.Y.S.2d 458, 446, 459 N.E.2d 1176, 1177 (1984).
106. Henry Campbell Black., *Black's Dictionary of Law* 648 (rev. 4th ed. 1968); s*ee Doubledown Realty Corp. v. Gibbs*, 122 Misc. 2d 32, 35, 469 N.Y.S.2d 887, 889 (Hous. Part Civ. Ct., N.Y. Co. 1983) (stating that although waiver issue focuses on landlord's intent, estoppel looks to effect landlord's conduct has on tenant).
107. *Goldstein v. Equitable Life Assurance Soc.*, 160 Misc. 364, 366, 289 N.Y.S. 1064, 1067 (Civ. Ct., N.Y. Co. 1936).
108. Dov Treiman, *Succession: "If At First You Don't Succeed, Die, Die, Again" Part III*, 4 Finkelstein, Ferrara, and Treiman's Landlord-Tenant Monthly 11 (Apr. 2006).
109. *Jefpaul Garage*, 61 N.Y.2d at 446, 474 N.Y.S.2d at 1178, 462 N.E.2d at 1178.
110. *Herald Towers LLC v. Sun Lord Int'l, Inc.*, 2002 N.Y. Slip Op. 50239(U), *3, 2002 N.Y. Misc. LEXIS 740, at *3 (App. Term 1st Dep't 2002) (*per curiam*).
111. *Id.*, N.Y. Misc. LEXIS 740, at *3.
112. *Mazda Realty Assocs., LLP v. Green*, 187 Misc. 2d 419, 420, 723 N.Y.S.2d 812, 814 (App. Term 1st Dep't 2000) (*per curiam*).
113. *Gregory v. Colonial DPC Corp. III*, 234 A.D.2d 419, 651 N.Y.S.2d 150 (2d Dep't 1996) (mem.).
114. *Id*, at 419, 651 N.Y.S.2d at 151.
115. *Glenbriar v. Lipsman*, 5 N.Y.3d 388, 394, 804 N.Y.S.2d 719, 723, 838 N.E.2d 635, 639 (2005); *see* Finkelstein & Ferrara, *supra* note 33, at § 15:476, at 15-277.
116. *Glenbriar*, 5 N.Y.3d at 392, 804 N.Y.S.2d at 722, 838 N.E.2d at 639.
117. *See, e.g., Tabak v. Steele*, 8 Misc. 3d 78, 82, 798 N.Y.S.2d 835, 838 (App. Term 1st Dep't 2005) (*per curiam*); *PLWJ Realty, Inc. v. Gonzalez*, 187 Misc. 2d 241, 242, 721 N.Y.S.2d 458, 459 (App. Term 1st Dep't 2000) (*per curiam*); *Tuckahoe Rd. Partnership v. Giananti*, 135 Misc. 2d 780, 785, 516 N.Y.S.2d 838, 842 (Yonkers City Ct. 1987).
118. *Tuckahoe Road Partnership.*, 135 Misc. 2d at 785, 516 N.Y.S.2d at 842.
119. *Id.*, 516 N.Y.S.2d at 842.
120. 9 Misc. 3d at 474, 798 N.Y.S.2d at 679.
121. *MSG Pomp Corp. v. Doe*, 185 A.D.2d 798, 799-800, 586 N.Y.S.2d 965, 966 (1st Dep't 1992) (mem.); *Berkeley Assocs.*, 122 A.D.2d at 705, 505 N.Y.S.2d at 632.
122. *See, e.g., N.Y. Univ. v. Farkas*, 121 Misc. 2d 643, 644, 468 N.Y.S.2d 808, 810 (Hous. Part Civ. Ct., N.Y. Co. 1983).
123. CPLR 408.
124. *See, e.g., 42 W. 15th St. Corp. v. Friedman*, 208 Misc. 123, 125, 143 N.Y.S.2d 159 (App. Term 1st Dep't 1955) (*per curiam*).
125. *See, e.g., Uptown Realty Group, L.P. v. Buffaloe*, 2005 N.Y. Slip Op. 50164, *2, 2005 N.Y. Misc. LEXIS 253.
126. *Antilean Holding Co. v. Lindley*, 76 Misc. 2d 1044, 1047, 352 N.Y.S.2d 557, 561 (Hous. Part Civ. Ct., N.Y. Co. 1973).
127. *See N.Y. Univ.*, 121 Misc. 2d at 647, 468 N.Y.S.2d at 811-12.
128. *Id.*, 468 N.Y.S.2d at 811-12.
129. *Id.*, 468 N.Y.S.2d at 811-12.
130. *See Dubowsky v. Goldsmith*, 202 A.D. 818, 818, 195 N.Y.S. 67, 67 (2d Dep't 1922) (mem.).
131. *See Profile Enters. LP v. Sanzo*, N.Y.L.J., July 13, 2005, p. 21, col. 1 (Hous. Part Civ. Ct., N.Y. Co.); *N.Y. Univ.*, 121 Misc. 2d at 646, 468 N.Y.S.2d at 811.
132. *W. 16th Realty Co. v. Ali*, 176 Misc. 2d 978, 979, 676 N.Y.S.2d 401, 403 (Hous. Part Civ. Ct., N.Y. Co. 1998).
133. *See In re A.G. Ship Maintenance Corp. v. Lezak*, 69 N.Y.2d 1, 5, 511 N.Y.S.2d 216, 218, 503 N.E.2d 681, 683 (1986); *Mighty Midgets v. Centennial Ins. Co.*, 47 N.Y.2d 12, 21-22, 416 N.Y.S.2d 559, 564, 389 N.E.2d 1080, 1085 (1979).
134. *See Cier Indus. Co. v. Hessen*, 136 A.D.2d 145, 148, 526 N.Y.S.2d 77, 79 (1st Dep't 1988).
135. RPL § 234.
136. *Park S. Assocs.*, 123 Misc. 2d at 753, 474 N.Y.S.2d at 675.

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Roommates in New York Law

By Gerald Lebovits

I. The Roommate Law: Origins and Purpose

The Roommate Law is the popular name for New York's Unlawful Restrictions on Occupancy Law, codified at Real Property Law (RPL) § 235-f. It was enacted as part of the Omnibus Housing Act (OHA) of 1983 in response to courts that "refus[ed] to extend the protection of the human rights law to unrelated persons sharing a dwelling."[1] The New York Legislature recognized that countless households were composed of unrelated persons who lived together for reasons of economy, safety, and companionship. The Legislature reasoned that unless corrective action was taken, these households would be in jeopardy. The Roommate Law is designed to prevent evictions of residential tenants who had nontraditional living arrangements. The law permits a tenant to share a rental unit with additional occupants and be afforded the same protections as a traditional family.

A traditional family enjoys the most protection under the law, but New York's Roommate Law also allows for nontraditional living arrangements. A tenant is granted a number of rights, including the right to privacy and the right to live with anyone, subject to some exceptions. This article explores the protections, and their limitations, afforded to tenants and roommates under the Roommate Law.

II. Definition of Roommate

Despite its popular name, the Roommate Law fails to define the term "roommate." The law refers to a roommate as an "occupant": "a person, other than a tenant or member of a tenant's immediate family, occupying premises with the consent of the tenant or tenants."[2] The term "tenant" refers to every individual with a lease, including all those living in rent-stabilized or rent-controlled apartments.[3]

These definitions neither answer nor address the problems that arise in disputes involving landlords and roommates. In the context of the Roommate Law, landlord-tenant rights and obligations depend on a number of factors, including a tenant's relationship with a co-habitant and whether a co-habitant is a party to the lease.[4] Different levels of liability, legal remedies, and protections apply to those who share space. Each definition becomes significant when disagreements can no longer be resolved in the living room and must be resolved in the courtroom.

III. Tenancy Relationships

A co-tenancy relationship exists when two or more individuals rent a unit and sign the same lease. This occurs either when a unit is initially rented or when a new tenant is added to an existing lease sometime later. Each co-tenant is independently liable for all the rent for a unit. Each co-tenant has equal tenancy responsibilities and is in privity of contract with the landlord.

A subtenant, on the other hand, enters into a sublease agreement and pays rent to the primary tenant—the tenant named on the lease. This creates a subtenancy relationship. A sublease is a "transfer of the tenant's interest in all or part of the leased property with reservation of a reversionary interest."[5] With an agreement to sublease, the primary tenant "retains privity of contract with the landlord and remains responsible for all obligations under the lease."[6]

If an occupant lives with the tenant but is not a member of a tenant's immediate family and does not execute a lease with the landlord or a sublease with the tenant, the occupant is a roommate whom the Roommate Law protects. A roommate, unlike a tenant or co-tenant, is "neither in privity of contract nor privity of estate with the landlord."[7] A landlord "cannot hold a roommate liable for the rent nor can the roommate bind the landlord to the benefits of the lease."[8]

A roommate is different from a guest, "who is temporarily received and entertained at one's home but who is not a regular occupant."[9]

IV. A Landlord's Right to Know

Tenants do not need a landlord's consent before an immediate family member or an additional occupant moves into a unit. The Roommate Law protects tenants from a landlord that attempts to reduce apartment-sharing rights, even when the landlord attempts to diminish these rights in a lease. Any clause in a tenant's lease that purports to waive or modify a tenant's right to share rental space is "unenforceable as against public policy."[10]

A landlord has the right to know about any occupant in the rental unit. A tenant must inform the landlord, upon the landlord's request, of the name of any occupant within 30 days after the occupancy begins.[11] A landlord's request need not be made in writing. Both the landlord and the Division of Housing and Community Renewal (DHCR) are authorized under the New York City Housing Maintenance Code (HMC) to demand that

a tenant provide a sworn affidavit containing information about all occupants residing in the rental unit, including the name, relationship, and age of any minor children.[12]

V. The Limitation on the Number of Occupants

Although landlords may not unlawfully place occupancy restrictions on a tenant, they have the right, at least initially on lease signing, to limit the number of occupants living in the rental unit. Under the Roommate Law, the number of occupants allowed to share living space depends on the number of tenants who signed the lease.[13] When one tenant is named in a lease, the law provides that "[a]ny lease or rental agreement for residential premises entered into by one tenant is construed to permit occupancy by the tenant, tenant's immediate family, and one additional occupant and occupant's dependent children. . . ."[14] When two or more tenants are named in a lease, the law provides that "the total number of tenants and occupants . . . may not exceed the number of tenants specified in the current lease or rental agreement. . . ."[15] The occupants' immediate family and dependent children are excluded from this calculation. The Roommate Law further requires that the apartment be the primary residence of either the tenant or the tenant's spouse.

Other limits also affect the number of occupants who may live in a rental unit. The Roommate Law does not inhibit a landlord's ability to restrict occupancy to comply with federal, state, or local laws, regulations, ordinances, or codes.[16] For example, the HMC provides a formula to determine the maximum number of persons who may occupy an apartment. According to the HMC, each person, including tenants and occupants, must have at least 80 square feet of livable space.[17] To determine the number of occupants allowed in a rental unit, the square footage of the livable space is divided by 80. In addition, for every two persons who may lawfully occupy the space, one child under four may reside there. The HMC does not distinguish between tenants, immediate family, and occupants.

If a family member or roommate resides in a rental unit according to the Roommate Law, the landlord may still restrict occupancy if the HMC's standard is not satisfied. But a landlord may not use the federal or state restrictions, including the proscription Multiple Dwelling Law § 31(6),[18] to evict a tenant in violation of the Roommate Law, unless an overcrowding violation has been placed against the premises. In one case of alleged overcrowding, a court held that the landlord was not permitted to evict absent dangerous conditions. The court noted that the HMC was not intended "as a sword by a landlord who seeks to evict low rent tenants who have not been proven to be a danger to the building."[19] One court held in 1949 that violations of the then-extant Department of Housing and Buildings does not require evicting a tenant if the violation can be cured through other means.[20] In another case, the court found that to evict a tenant for "so-called single-room violations" would be against the legislative intent manifested in § 6 of the Federal Rent Regulation for Housing in the New York City Defense-Rental Area and § 261 of the Multiple Dwelling Law.[21] Nevertheless, the Department of Housing Preservation and Development or the Department of Buildings can order the unit vacated if occupancy rules are violated and if there is a genuine safety or fire hazard not curable except by evicting the tenants.

VI. Immediate Family

The Roommate Law protects a tenant's right to have immediate family members living in the unit, but the Roommate Law does not define "immediate family." Case law provides some guidance. In one case involving an apartment subject to the Rent Stabilization Law (RSL), the court found that the tenant's mother qualified as a member of the tenant's immediate family.[22] Little controversy arises when a court finds that a tenant's mother is a member of the tenant's immediate family, because the Rent Stabilization Code (RSC) defines the phrase "immediate family" to include a "parent, grandparent, child, stepchild, grandchild, brother or sister of the tenant or of the tenant's spouse or the spouse of any of the foregoing."[23] The controversies lie elsewhere.

Defining the phrase "immediate family" gets more complicated when shareholders of cooperative apartments share living space with family members. The relationship between a cooperative corporation and a shareholder-proprietary lessee is that of a landlord and tenant. A proprietary lease into which a stockholder of a cooperative corporation enters is a lease by a tenant for residential rental premises.[24] A proprietary lessee of a cooperative apartment may invoke RPL § 235-f as a defense when a landlord improperly restricts occupancy. Using this rationale, one court declined to enforce a proprietary lease that restricted occupancy to the shareholder and his immediate family.[25]

In *Mitchell Gardens No. 1 Co-op. Corp. v. Cataldo*, a case involving a cooperative apartment, the court found it improper to use the RSC's definition of immediate family because cooperatives are excluded from the RSL.[26] In *Cataldo*, the court looked to the parties' cooperative agreement for the meaning of "immediate family." The cooperative rules and regulations defined the phrase to mean "those members of the Stockholder's family who lived with the Stockholder on the date he first took occupancy of his apartment and lived with the Stockholder continuously from that date."[27] Finding that a stepdaughter does not qualify as an immediate family member, the court

held that the cooperative corporation, acting as landlord, did not unlawfully restrict occupancy by denying the stepdaughter protection as an immediate family member.

The Roommate Law's ambiguous definitions can work to a tenant's benefit. In cases not involving cooperative apartments with restrictive proprietary leases, uncles, aunts, nephews, and nieces may still move in as a roommate even if they do not qualify as an immediate family member as the RSC defines them.

VII. Profiteering from Roommates

Until RSC § 2525.7(b) went into effect on December 20, 2000, the Appellate Division, First Department, found "no cause of action for rent profiteering with respect to a roommate."[28] Section 2525.7(b) now protects roommates from primary tenants who profiteer. It prohibits a rent-stabilized tenant from charging a roommate anything more than a proportionate share of the legal regulated rent. To calculate the roommate's proportionate share, the legal regulated rent is divided by the number of tenants named on the lease and the total number of occupants living in the unit.[29] The formula does not cover the tenant's spouse and family members or the occupant's dependent children[30] or account for a situation in which one roommate invests much more into the rental unit than the other occupant, thus imposing an equal share division, unlike that of a subletting situation.[31] Thus, a court may take into account the apartment's furnishings, utilities, and other services when determining the proportionate rent.[32] The proportionate share requirement under RSC § 2525.7 represents a reasonable approximation of the individual's fair share of the apartment's expenses, including rent.[33]

A roommate's "remedy for a violation of § 2525.7 is not set forth in the code."[34] The DHCR, the agency that supervises rent-stabilized apartments, provides a remedy by allowing the overcharged roommate to file a rent overcharge complaint with the agency,[35] and courts have held the roommate has an implied cause of action and can sue the tenant for actual damages.[36] Unlike a rent-stabilized tenant whom a landlord overcharges, a roommate is not entitled to treble damages.[37]

Section 2525.7(b) of the RSC prohibits a tenant from charging the roommate more than a proportionate share of the apartment's rent.[38] If the tenant violates this provision, the overcharged roommate can sue the tenant, and a successful roommate will be refunded any rent paid over the apartment's proportionate share.[39] RSC § 2525.7(b) defines proportionate share as the registered rent of the apartment divided evenly by the number of tenants and occupants living therein, excluding tenant's family members and the occupant's dependent children.[40] If the tenant charges the roommate more rent than the tenant is paying the landlord (the authentic rent share), this is known as profiteering. No *prima facie* case of profiteering exists in a plenary action if the tenant has refunded the overcharge[41]; the tenant may move to dismiss for failure to state a cause of action.

In addition to the roommate's plenary action, a landlord may also start a holdover proceeding against a tenant charging the roommate more than the proportionate share of the legal rent.[42] Landlords will not always be successful in evicting a tenant for rent profiteering. Even if the tenant violates RSC § 2525.7 by unlawfully charging the roommate more than half the monthly stabilized rent, the landlord may not prevail if the overcharge was small and there was no evidence of bad faith or intent to profit.[43] Courts do not always allow a tenant's cure to alleviate a violation under the cure provision of Real Property Actions and Proceedings Law 753. One court that examined the amount of rent charged over the proportionate share held that preventing a landlord from evicting a tenant based on the cure is inconsistent with the law.[44] The court held that the cure provision "is not to be rotely applied"[45] to all cases. If the tenant collects grossly excessive rent, for example, no cure is allowed for the profiteering tenant in a holdover proceeding,[46] although the court will allow a cure if "the surcharge amounts, though not insubstantial, do not reflect commercial exploitation of the regulated tenancy."[47] Ultimately, courts are much more likely to allow cures when a roommate as opposed to a subtenant is overcharged.

A landlord may also move for injunctive relief. One court enjoined a rent-controlled tenant from leasing or subleasing the apartment to roommates, occupants, and subtenants for the duration of her tenancy.[48]

Courts have not extended the same protection to roommates sharing living space regulated by the Rent Control Law and the Loft Law. RSC § 2525.7 prohibits only rent-stabilized tenants from charging roommates more than a proportionate share of the legal rent. The Appellate Term, First Department, has held that RSC § 2525.7 does not allow a rent-controlled tenant to be evicted for overcharging a roommate.[49] The court found no rent-control regulation that parallels RSC § 2525.7; no rent-control provision authorizes evicting rent-controlled tenants for rent profiteering. Similarly, a landlord has no cause of action to evict a loft tenant who charges a roommate more than a proportionate share of the legal rent.[50] Nothing in the Loft Law or its regulations prohibit tenants from overcharging roommates more than the proportionate share of the legal rent, and the Loft Law does not give the landlord a cause of action to evict a tenant for that conduct.[51] A landlord may bring an eviction proceeding

against a tenant subleasing a rent-controlled apartment for profit, but the restrictions in sublet situations do not apply to situations involving roommates.[52]

VIII. Succession Rights

After *Braschi v. Stahl*,[53] a 1989 Court of Appeals decision, the DHCR amended its rent regulations, now set out in RSC § 2204.6(d), to provide for leasehold succession rights in accordance with *Braschi*'s broad definition of the term "family." The Court of Appeals in *Braschi* held that a family includes "two lifetime partners whose relationship is long term and characterized by an emotional and financial commitment and interdependence."[54]

A person claiming succession rights to a rent-stabilized apartment must (1) be a member of the tenant's family; (2) use the premises as a primary residence; and (3) live in the apartment with the primary tenant for two years immediately before the primary tenant's move or death (unless the family member is a senior citizen or disabled). The preceding Code narrowly defined "family"[55] and excluded non-traditional family members from the right to succeed.

The DHCR amendments broadened the definition of family members entitled to succession rights as the *Braschi* court required. The current definition includes those who can prove that the apartment was their primary residence and that an emotional and financial commitment demonstrates interdependence between that individual and the record tenant. Courts consider eight factors in determining whether the requisite emotional and financial commitments exist: (1) the length of the relationship; (2) sharing of expenses; (3) intermingling of finances; (4) engaging in family-type activities; (5) the parties' formalized legal obligations and responsibilities; (6) holding themselves out as family members through words or acts; (7) regularly performing family functions; and (8) any other pattern of behavior that evidences an intent to create a long-term, emotionally committed relationship. No single determining factor preponderates. Courts will look at the totality of the evidence.[56] These factors give roommates who are non-traditional family members an opportunity to show their right to continue residing in the apartment.

Courts will grant succession rights to occupants who can prove that they were more than the deceased tenant's roommate—that they are a non-traditional family member. The occupant must meet the burden of proving the necessary emotional and financial commitment.[57] In one case when a landlord tried to evict a deceased tenant's alleged roommate, the court was particularly persuaded by the facts that the roommate lived with the tenant for 15 years without paying rent, took care of the tenant while battling cancer, and used the apartment's address on a W-2 form, bank statement, and voter registration card. The court acknowledged that "while the statute considers intermingling of finances, the absence of this factor here does not negate the conclusion that she is in fact a non-traditional family member."[58]

Another court held that an occupant was not subject to eviction after the record tenant died. In that case, the occupant could not establish through documentary evidence a financial interdependence between the occupant and the tenant. The landlord proved that the occupant and tenant maintained separate checking accounts and credit cards, but the court found that the occupant had a valid succession claim because the "totality of the circumstances evince[d] a long-term relationship characterized by emotional and financial commitment."[59]

Tenants living in rent-controlled and rent-stabilized apartments can protect their roommate's succession rights. A tenant may complete a DHCR form entitled "Notice to Owner of Family Members Residing with the Named Tenant in the Apartment Who May Be Entitled to Succession Rights/Protection from Eviction." This form informs landlords about those people living in the tenant's apartment as their primary residence. Assuming that a roommate is ready to accept the liabilities and responsibilities of tenancy, the roommate may also list the roommate as a co-tenant on the lease. A roommate's right to remain in the apartment is contingent on the tenant's continued occupancy unless succession rights accrue.

IX. Liability for Roommate's Conduct

A tenant may be held liable for a roommate's conduct that rises to the level of a nuisance.[60] A nuisance is a condition that threatens the comfort and safety of others in the building.[61]

A landlord seeking to evict a tenant must give a tenant sufficient notice to cure the nuisance if the nuisance is curable and cite the specific lease prohibition or law allegedly violated.[62] The landlord must also prove more than one isolated instance of nuisance. The conduct must be recurring, frequent, or continuous.[63] To qualify as a nuisance, therefore, the conduct must "import[] a continuous invasion of rights—'a pattern of continuity or recurrence of objectionable conduct.'"[64]

In one leading case, an uncle allowed his sister and his schizophrenic nephew to share his apartment.[65] The court found that the tenant-uncle "permitted and condoned the nuisance and whose tenancy itself, in all likelihood will encourage the nuisance to continue unabated."[66] As a result, the court held that evicting the tenant-uncle was appropriate to protect the other tenants in the building.

X. Increasing the Rent

The DHCR sets the approval guidelines for situations when a landlord may increase rent.[67] A landlord may be entitled to increase the rent for a rent-controlled apartment when a tenant takes a roommate. The landlord may not increase the rent if the additional occupant is a member of the tenant's immediate family. The landlord must first apply to the DHCR, and the agency's administrator may grant the appropriate adjustment only during the period "of subletting or increase in the number of occupants."[68] The total rent can be increased by as much as 10 percent when a tenant shares the apartment with roommates.

Landlords of rent-stabilized apartments are not entitled to increase the tenant's rent when the tenant shares an apartment with roommates. But when roommates decide to change their status to co-tenants by placing their names on the lease, the DHCR allows the landlord to increase the rent at lease renewal. By adding a new co-tenant to the renewal lease, the landlord may issue a vacancy rent increase.[69]

XI. Acceptance of Rent

A roommate may get mixed signals from a landlord who accepts rent even when a roommate has no succession rights to the apartment. A landlord who accepts rent from a tenant's roommate "does not in and of itself, create a tenancy when the tenant has vacated the apartment."[70] The landlord's intent will determine whether the acceptance of rent will create a tenancy. According to dozens of cases, the tenant must establish that the landlord "knowingly and purposefully accepted" the rent.[71] This rationale is consistent with the policies behind waiver in landlord-tenant law. In the context of a holdover proceeding, for example, a tenant may assert the defense that the landlord waived the default by accepting rent even if a "no waiver" clause is in the lease. This defense applies only if the tenant can prove that the landlord intended to enter or maintain the landlord-tenant relationship.[72] A landlord's waiver is inferred from accepting rent, but the acceptance of rent with knowledge of a breach, and without a diligent effort to terminate the lease, triggers an inference that the landlord has elected to ignore the noncompliance and hold the tenant to the parties' agreement.[73]

XII. Conclusion

New York has made a legislative determination that tenants may have roommates, at least during the tenancy, and sometimes beyond the tenancy. But tenants may not abuse their right to live with roommates, and limitations affect the roommates' number and behavior and the rent a tenant may charge them.

Endnotes

1. L. 1983, ch. 403, § 1.
2. RPL § 235-f(1)(b).
3. *Id.* § 235-f(1)(a).
4. For an overview of the rent regulatory system, see Andrew Scherer, *Residential Landlord and Tenant Law in New York* § 4:1, at 150 (2006 ed.).
5. Daniel Finkelstein & Lucas A. Ferrara, *Landlord and Tenant Practice in New York* § 3:39, at 17 (2006 ed.).
6. Scherer, *supra* note 4, at § 2:44, at 36.
7. Finkelstein & Ferrara, *supra* note 5, at § 3:38, at 16-17.
8. *Id.*
9. *Id.* § 3:40, at 17-18.
10. RPL § 235-f(2).
11. *Id.* § 235-f(5).
12. N.Y.C. Admin. Code § 27-2075(2)(c).
13. RPL § 235-f(3), (4).
14. *Id.* § 235-f(3).
15. *Id.* § 235-f(4).
16. RPL § 235-f(8); Scherer, *supra* note 4, at § 2:42, at 35-36.
17. N.Y.C. Admin. Code § 27- 2075(a)(1).
18. *Sima Realty LLC v. Philips*, 282 AD2d 394, 395, 724 N.Y.S.2d 51, 52 (1st Dep't 2001) (mem.) (noting that Multiple Dwelling Law "was enacted to protect tenants of multiple dwellings against unsafe living conditions, not to provide a vehicle for landlords to evict tenants on the ground that premises are unsafe"); *Porto v. Watts*, 2006 N.Y. Slip Op. 50436(U), at *4 (Hous. Part. Civ. Ct., N.Y. Co., Feb. 26, 2006) ("[A] landlord may not maintain a proceeding for overcrowding under MDL § 31(6)(a) unless an overcrowding violation has been placed against the building by reason of the tenant's occupancy.") (citing *210 W. 94 LLC v. Concepcion*, 2003 N.Y. Slip Op. 50612(U), *3, 2003 WL 1873768, at *1 (App Term 1st Dept, Mar. 3, 2003) (*per curiam*)).
19. *338 W. 17th St. Assoc. v. Katehis*, N.Y.L.J., Oct. 5, 1994, p. 22, col. 2 (Hous. Part Civ. Ct., N.Y. Co.).
20. *Kirschenbaum v. Finkelstein*, 275 App. Div. 683, 683, 86 N.Y.S.2d 428, 428 (2d Dep't 1949) (mem.).
21. *2025 Broadway, Inc. v. Wolf*, 187 Misc. 1065, 1066, 66 N.Y.S. 2d 17, 17 (App. Term 1st Dep't 1946) (*per curiam*).
22. *38th Astoria Assocs. v. Chavez*, 126 Misc. 2d 811, 813, 484 N.Y.S.2d 467, 469 (Hous. Part Civ. Ct., Queens Co. 1985).
23. RSC § 2520.6(n).
24. *Silverman v. Alcoa Plaza Assocs.*, 37 A.D.2d 166, 172, 323 N.Y.S.2d 39, 45 (1st Dep't 1971) (quoting *Susskind v. 1136 Tenants Corp.*, 43 Misc. 2d 588, 590 (Civ. Ct., N.Y. Co. 1964)); *Suarez v. Rivercross Tenants' Corp.*, 107 Misc. 2d 135, 137, 438 N.Y.S.2d 164, 166 (App. Term 1st Dep't 1988) (*per curiam*); *Sherwood Village Cooperative A, Inc. v. Slovik*, 134 Misc. 2d 922, 924, 513 N.Y.S.2d 577, 578 (Hous. Part Civ. Ct., Queens Co. 1986).
25. *Southridge Cooperative Section No. 3, Inc. v. Menendez*, 141 Misc. 2d 823, 826, 535 N.Y.S.2d 299, 302 (Hous. Part Civ. Ct., Queens Co. 1988).
26. 175 Misc. 2d 493, 494, 670 N.Y.S.2d 190, 191 (App. Term 2d Dep't 2d & 11th Jud. Dists. 1997) (mem.) (citing RSC § 2520.6(n)).
27. *Id.* at 496, 670 N.Y.S.2d at 192.

28. *Handwerker v. Ensley*, 261 A.D.2d 190, 191, 690 N.Y.S.2d 54, 55 (1st Dep't 1999) (mem.).
29. RSC § 2525.7(b).
30. *Id.*
31. *Bryant v. Carey*, 196 Misc. 2d 412, 414, 765 N.Y.S.2d 146, 148 (Civ. Ct., N.Y. Co. 2003).
32. *719 W. 180th St. LLC v. Gonzalez*, 193 Misc. 2d 736, 739, 752 N.Y.S.2d 214, 217 (Hous. Part Civ. Ct., N.Y. Co. 2002).
33. *Id.* at 740, 752 N.Y.S.2d at 217.
34. *Bryant*, 196 Misc. 2d at 414, 765 N.Y.S.2d at 148-49.
35. *Scherer, supra* note 4, at § 8:163, at 571.
36. *Bryant*, 196 Misc. 2d at 414, 765 N.Y.S.2d at 149.
37. *Compare* RSC § 2526.1 *with Bryant*, 196 Misc. 2d at 416, 765 N.Y.S.2d at 150.
38. RSC § 2525.7.
39. *Bryant*, 196 Misc. 2d at 416, 765 N.Y.S.2d at 150.
40. RSC § 2525.7(b).
41. *Ariel Assoc., L.L.C. v. Brown*, 271 A.D.2d 369, 370, 706 N.Y.S.2d 116, 117 (1st Dep't) (mem.), *appeal dismissed*, 95 N.Y.2d 844, 713 N.Y.S.2d 517, 735 N.E.2d 1282 (2000); *Alverjan Holding Corp. v. Weiss*, N.Y. L.J., May 19, 1994, p. 27, col. 1 (App. Term 1st Dep't 1994) (*per curiam*); *L.E.S.P.M.H.A., Inc. v. Nunez*, N.Y. L.J., Dec. 18, 2002, p. 23, col. 4 (Hous. Part Civ. Ct., N.Y. Co. 2002).
42. *See, e.g.*, *W. 148 LLC, v. Yonke*, N.Y. Slip Op. 23068(U), at *1 (App. Term 1st Dep't Feb. 8, 2006) (*per curiam*) (evicting tenant who charged series of roommates nearly double monthly stabilized rent and advertised the apartment under Internet listing for "Affordable Hotels"); *Ram 1 L.L.C. v. Mazzola*, 2001 N.Y. Slip Op. 50073(U), at *1, 2001 WL 1682829, at *1 (App. Term 1st Dep't 2001) (*per curiam*).
43. *See, e.g.*, *54 Greene St. Realty Corp. v. Shook*, 8 A.D.3d 168, 168, 779 N.Y.S.2d 77, 77 (1st Dep't 2004) (mem.), *lv. denied*, 4 N.Y.3d 704, 792 N.Y.S.2d 1, 825 N.E.2d 133 (2005).
44. *Continental Towers v. Freuman*, 128 Misc. 2d 680, 681, 494 N.Y.S.2d 595, 596 (App. Term 1st Dep't 1985) (*per curiam*).
45. *Id.*, 494 N.Y.S.2d at 596 (citing *Beekman Estate v. Hanson*, N.Y. L.J., Dec 5, 1984, p. 6, col. 2 (App. Term 1st Dep't) (*per curiam*)).
46. *Id.*
47. *Roxborough Apts. Corp. v. Becker*, __ Misc. 3d __, 2006 N.Y. Slip Op. 26120, at *2 (App. Term 1st Dep't, Mar. 29, 2006) (*per curiam*) (citing *54 Greene St. Realty*, 8 A.D.3d 168, 779 N.Y.S.2d; *Ariel Assoc., L.L.C. v. Brown*, 271 A.D.2d 369, 706 N.Y.S.2d 116 (1st Dep't), *lv. dismissed*, 95 N.Y.2d 844, 713 N.Y.S.2d 517, 735 N.E.2d 1282 (2000); *270 Riverside Dr., Inc. v. Braun*, 4 Misc. 3d 77, 79, 781 N.Y.S.2d 551, 551 (App. Term 1st Dep't 2004) (*per curiam*) (finding violation curable because tenant collected $1,270 in rent from two roommates when legal regulated rent was $1,192); *W. 148 LLC*, 2006 N.Y. Slip Op. 26038).
48. *Leonori Assoc. v. Sultan*, N.Y.L.J., Mar. 23, 2005, p. 18, col. 1 (Sup. Ct., N.Y. Co. 2005).
49. *270 Riverside*, 4 Misc. 3d at 77, 781 N.Y.S.2d at 551; *see also Porto*, 2006 N.Y. Slip Op. 50436(U), at **1-3 (collecting cases).
50. *Giachino Enters. v. Inokuchi*, 7 Misc. 3d 738, 740, 791 N.Y.S.2d 814, 815-16 (Hous. Part Civ. Ct., N.Y. Co. 2005); *cf. BLF Realty Holding Corp. v. Kasher*, 299 A.D.2d 87, 747 N.Y.S.2d 457 (1st Dep't 2002) (sublets under Loft Law), *appeal dismissed*, 100 N.Y.2d 535, 762 N.Y.S.2d 876, 793 N.E.2d 413 (2003).
51. *Giachino Enters.*, 7 Misc. 3d at 740, 791 N.Y.S.2d at 816.
52. *See BLF Realty Holding*, 299 A.D.2d at 91, 747 N.Y.S.2d at 461 (citing *Hurst v. Miske*, 133 Misc. 2d 362, 365, 505 N.Y.S.2d 984, 986 (Hous. Part Civ. Ct., N.Y. Co. 1986)).
53. *Braschi v. Stahl*, 74 N.Y.2d 201, 544 N.Y.S.2d 784, 544 N.E.2d 784 (1989).
54. *Id.* at 211-12, 544 N.Y.S.2d at 789-90, 544 N.E.2d at 789.
55. *See* RSC § 2204.6.
56. *RHM Estates v. Hampshire*, 18 A.D.3d 326, 327, 795 N.Y.S.2d 214, 215 (1st Dep't 2005) (mem.).
57. *Riverview Develop. Holding Corp. v. Doe*, 8 Misc. 3d 132(A), 803 N.Y.S.2d 20, 2005 N.Y. Slip Op. 51140(U), *1, 2005 WL 1704431, at *1 (App. Term 1st Dep't 2005) (*per curiam*).
58. *RHM Estates*, 18 A.D.3d at 327, 795 N.Y.S.2d at 215; *accord* RSC § 2520.6(o)(2).
59. *St. Marks Assets, Inc. v. Herzog*, 196 Misc. 2d 112,113, 760 N.Y.S.2d 608, 609 (App. Term 1st Dep't 2003) (*per curiam*).
60. *Acorn Realty v. Torres*, 169 Misc. 2d 670, 671, 652 N.Y.S.2d 472, 473 (App. Term 1st Dep't 1996) (*per curiam*).
61. *Novak v. Fischbein, Olivieri, Rozenholc & Badillo*, 151 A.D.2d 296, 298, 542 N.Y.S.2d 568, 570 (1st Dep't 1989) (mem.).
62. *Chinatown Apts. v. Chu Cho Lam*, 51 N.Y.2d 786, 786, 433 N.Y.S.2d 86, 86, 412 N.E.2d 1312, 1313 (1980).
63. *Domen Holding Co. v. Aranovich*, 1 N.Y.3d 117, 124, 769 N.Y.S.2d 785, 789, 802 N.E.2d 135, 139 (2003).
64. *Id.* 769 N.Y.S.2d at 789, 802 N.E.2d at 139 (quoting *Frank v. Park Summit Realty Corp.*, 175 A.D.2d 33, 35, 573 N.Y.S.2d 655, 657 (1st Dep't 1991), *modified on other grounds*, 79 N.Y.2d 789, 579 N.Y.S.2d 649, 587 N.E.2d 287 (1991)); *accord Goodhue Residential Co. v. Lazansky*, 1 Misc. 3d 907(A), 781 N.Y.S.2d 624, 2003 N.Y. Slip Op. 51559(U), 2003 WL 23148836 (Hous. Part Civ. Ct., N.Y. Co., Dec. 29, 2003) (Gerald Lebovits, J.).
65. *Frank*, 175 A.D.2d at 34, 573 N.Y.S.2d at 656.
66. *Id.*
67. RSC § 2522.4.
68. *Id.* § 2522.4(a)(2).
69. *See In re 427 Senator St.*, DHCR Admin. Rev. Dkt. No. GG 210085-RO (Mar. 19, 1993).
70. *171 W. Fourth LLC v. Fennell*, N.Y.L.J., Feb. 24, 1999, p. 29, col. 1 (App. Term 1st Dep't 1999) (*per curiam*).
71. *E.g., Park Holding Co. v. Power*, N.Y.L.J., Jan 17, 1992, p. 26, col. 1 (App. Term 1st Dep't) (*per curiam*).
72. *E.g.*, *Pollack v. J. A. Green Const. Corp.*, 40 A.D.2d 996, 996, 338 N.Y.S.2d 486, 487 (2d Dep't 1972), *aff'd*, 32 N.Y.2d 720, 722, 344 N.Y.S.2d 363, 363, 297 N.E.2d 99, 99 (1973).
73. Scherer, *supra* note 4, at 11:4-11:12, at 664-68.

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Subletting in New York Law

By Gerald Lebovits

I. Introduction

Residential tenants are permitted to sublease an apartment if they follow the procedures outlined in New York Real Property Law (RPL) § 226-b, frequently referred to as New York's "Sublet Law." This article explores the common illegal sublet scenarios, the steps a landlord must follow to commence an alleged illegal-sublet holdover proceeding, the holdover proceeding itself along with motion practice and disclosure, and a tenant's opportunity to cure an illegal sublet.

A sublease is "a lease by a lessee to a third party, conveying some or all of the leased property for a shorter term than that of the lessee, who retains a reversion in the lease."[1] In a sublease, the tenant is the "prime tenant" and the sublessee is the "subtenant" for the duration of the sublease. The main characteristic of a sublease is that the tenant conveys less than the entire interest in the property and retains either a reversionary interest in the whole property or a possessory interest in part of the property. The prime tenant conveys the rights to occupy and enjoy the rental unit for the sublease term and regains possession when the term ends.

Sublets are different from assignments. An assignment is "the transfer of rights or property."[2] The main characteristic of an assignment in this context is that the tenant conveys his entire interest in the property, either possessory or reversionary, and retains nothing. An assignment may or may not be coupled with a release of the original tenant from all obligations under the original lease, depending on the original lease's provisions.

Courts distinguish between roommates and subtenants. When the prime tenant shows that an occupant is merely a roommate and not a subtenant in possession of the rental unit for a specified duration, the landlord cannot maintain a cause of action premised on an illegal sublet.[3]

In the past, rent-regulated tenants were allowed to sublet or assign a rental unit without limitation.[4] Today, that view is contrary to public policy and void as illegal. Rent regulation is not served by lenient alienability.[5]

A tenant's right to sublet is governed by RPL § 226-b and, when applicable, New York's Rent Stabilization Code § 2525.6,[6] but the parties may affirmatively agree to expand a tenant's right to sublet. Examples of affirmative agreements include a lease provision or a stipulation of the parties permitting the tenant to sublet at will. When a tenant's lease is silent about the right to sublet or assign, the silence may not be construed as conferring greater rights on the tenant than those a statute affords.[7]

The following are the most common illegal-sublet scenarios. First, a tenant may sublet a rental unit without complying with relevant statutory provisions like RPL § 226-b.[8] Second, a tenant may choose to sublease a rental unit without asking for the landlord's consent. Third, a tenant may ask for the landlord's consent and then sublease the unit, even though the landlord had withheld consent. Fourth, a tenant may sublet without meeting a primary-residence requirement. Fifth, a tenant may attempt to sublet continuously, called "piggybacking."

II. Common Illegal Sublet Scenarios

A. RPL § 226-b Requirements

If a lease or a regulation requires it, tenants must obtain the landlord's consent before they sublet an apartment. Once a tenant informs the landlord of the proposed sublease, the landlord may not withhold consent unreasonably.[9] RPL § 226-b gives tenants who have an "existing lease in a dwelling having four or more residential units" the right to sublease an apartment after a tenant has obtained the landlord's written consent.[10] The Sublet Law does not protect all tenants. It exempts from its coverage tenants in buildings with fewer than four units; tenants with periodic rental agreements, such as month-to-month tenants; and rent-controlled tenants without current leases, because a current lease governs a tenant's right to sublease.

To obtain consent, a tenant must mail a notice of intent to the landlord by certified mail, return receipt requested.[11] The notice of intent must include the term of the proposed sublet; the tenant's reason for subletting; the proposed sublessee's name, business address, and permanent home address; and a copy of the proposed sublease.[12] A landlord has several choices once a sublet request is made. The landlord may choose to accept or reject the sublet request within 30 days of either the mailing of the tenant's request or the mailing of the additional information requested by the landlord, whichever is later. [13] A landlord that does not do so is deemed to consent, and the tenant may proceed with the proposed sublease.[14] The landlord may also ask for additional information about the sublet within 10 days, or reject the sublet request as defective within 10 days.[15] The landlord may request additional information from the tenant so long as this request is not unduly burdensome. The landlord that wants to request additional information must do so within 10 days of the tenant's mailing the notice of intent.[16]

Because landlords owning rent-regulated units may not unreasonably withhold consent to sublet,[17] case law

has interpreted reasonable and unreasonable grounds for rejection. Tenants seeking to sublet their rent-stabilized apartments should be mindful of the various inquiries landlords are permitted to make of prime tenants regarding a proposed sublet despite the unreasonable consent rule being in their favor.[18]

B. Landlord's Consent Unnecessary

A rent-regulated tenant may sublet an apartment to statutorily defined family members without a landlord's consent.[19] Family members and roommates are not characterized as illegal subtenants but rather as additional "occupants."[20] New York's Rent Stabilization Code (RSC) contains a list of family members who qualify for no-consent sublets.[21] The RSC further provides that other individuals who use the housing accommodation as a primary residence may qualify if they can show emotional and financial commitment and interdependence between themselves and the tenant.[22] The RSC lists several factors to determine the existence of emotional and financial commitment and interdependence, including (1) the relationship's longevity; (2) the intermingling of funds with the tenant; (3) holding themselves out as family members; and (4) regularly performing family functions.[23] Although no factor is determinative, courts have interpreted this provision by emphasizing an individual's long-standing connection to the rental unit.[24]

C. Landlord Withholds Consent

When a tenant alleges that a landlord unreasonably withholds consent to sublet a unit, courts must determine whether the landlord's actions were unreasonable.[25] Absent this determination, the proposed sublease does not by itself confer any occupancy to a subtenant.[26] This lack of entitlement means that a subtenant has no "peaceable" or "constructive" possession required to maintain an action for possession and treble damages.[27]

Under New York's rent-regulatory scheme, a landlord may not unreasonably withhold consent to sublet.[28] In a recent case, the court was faced with a landlord who had rejected a prime tenant's sublet request for three reasons: (1) the prime tenant would have been away from the country for the entire proposed sublease term; (2) the proposed subtenant had insufficient means of income or support; and (3) the proposed sublease term would extend beyond the current lease term.[29] The prime tenant had complied with all subletting requirements RPL § 226-b. The court held that none of the landlord's reasons constituted a reasonable withholding of consent. The court went on to hold that nothing requires a prime tenant to reside in the same country during the sublease period. The court also found that the proposed subtenant provided proof of sufficient income or support to fund rent and utility obligations. Finally, the court found that New York's Rent Stabilization Code allows a sublease to extend beyond the term of the prime tenant's lease and prohibits withholding consent solely on that ground.[30]

A sublease or an assignment undertaken without the landlord's prior consent is a ground for eviction. Approval of the New York State Division of Housing and Community Renewal (DHCR) is not required for rent-regulated tenancies.[31] When a landlord reasonably withholds consent to sublet or assign a rental unit, the tenant has no remedy. A distinction between subleases and assignments arises when a landlord unreasonably withholds consent. If a landlord unreasonably withholds consent to assign an apartment, a tenant's remedy is to request to be released from the lease; the landlord must comply with this request within 30 days' notice.[32] In contrast, a landlord may not unreasonably withhold consent to sublet.[33]

D. The Primary-Residence Requirement

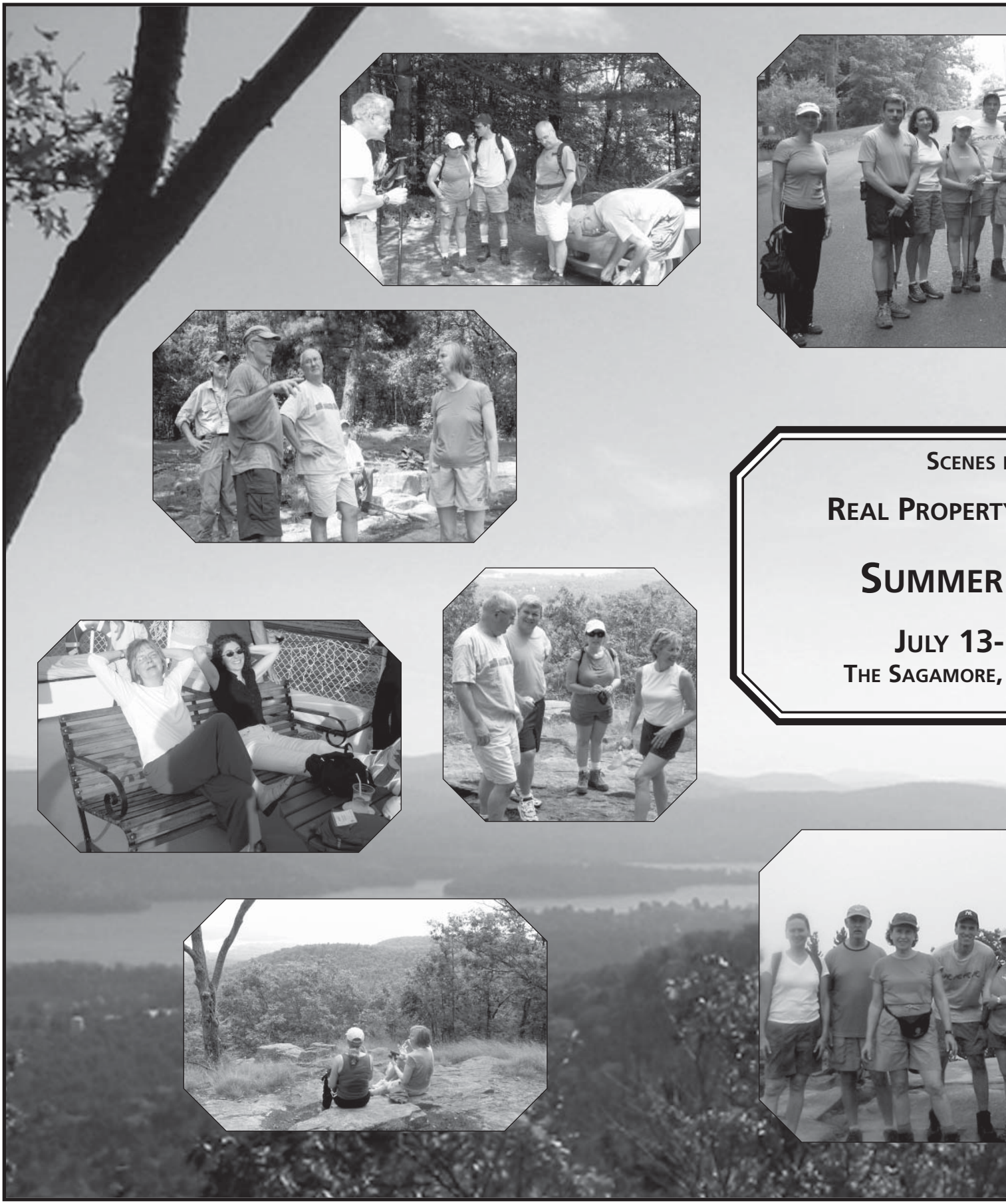
A rent-stabilized tenant must comply with the requirements in RPL § 226-b as well as with the primary-residence requirement.[34] The tenant's housing accommodation must be maintained as a primary residence at all times, and the tenant must intend to occupy the unit as a primary residence at the termination of the sublease.[35] An agreement to sublease may still be illegal even if the tenant maintains the housing accommodation as a primary residence.[36] For example, when a tenant is permitted to have a roommate who contributes to rent payments,[37] a tenant may not reconfigure and rent separate parts of the apartment.[38] An illegal sublease also arises when the prime tenant conveys an interest in the roommate's space but retains an interest in the remainder of the apartment.[39]

When a prime tenant illegally sublets a rental unit to an immediate family member long connected to the apartment, the proper remedy is a nonprimary-residence claim, not an illegal-sublet claim.[40] Although proof of a prime tenant's violation of the nonprimary-residence rule alone is insufficient in an illegal-sublet holdover,[41] courts permit landlords to maintain illegal sublet proceedings against family members who have no long-term connection with the apartment.[42]

A landlord has the option of bringing either a nonprimary-residence claim or an illegal sublet claim. Under the Omnibus Housing Act,[43] the right to sublet requires a tenant currently to reside, and intend to return, as the rental unit's primary resident when the proposed sublease term expires.[44] But differences exist between a nonprimary-residence claim and an illegal sublet claim, including the items of proof necessary to support each claim and the availability of a tenant's right to cure.[45]

(Continued on page 85)

Photos by Harry Meyer and Ron Kahn



SCENES

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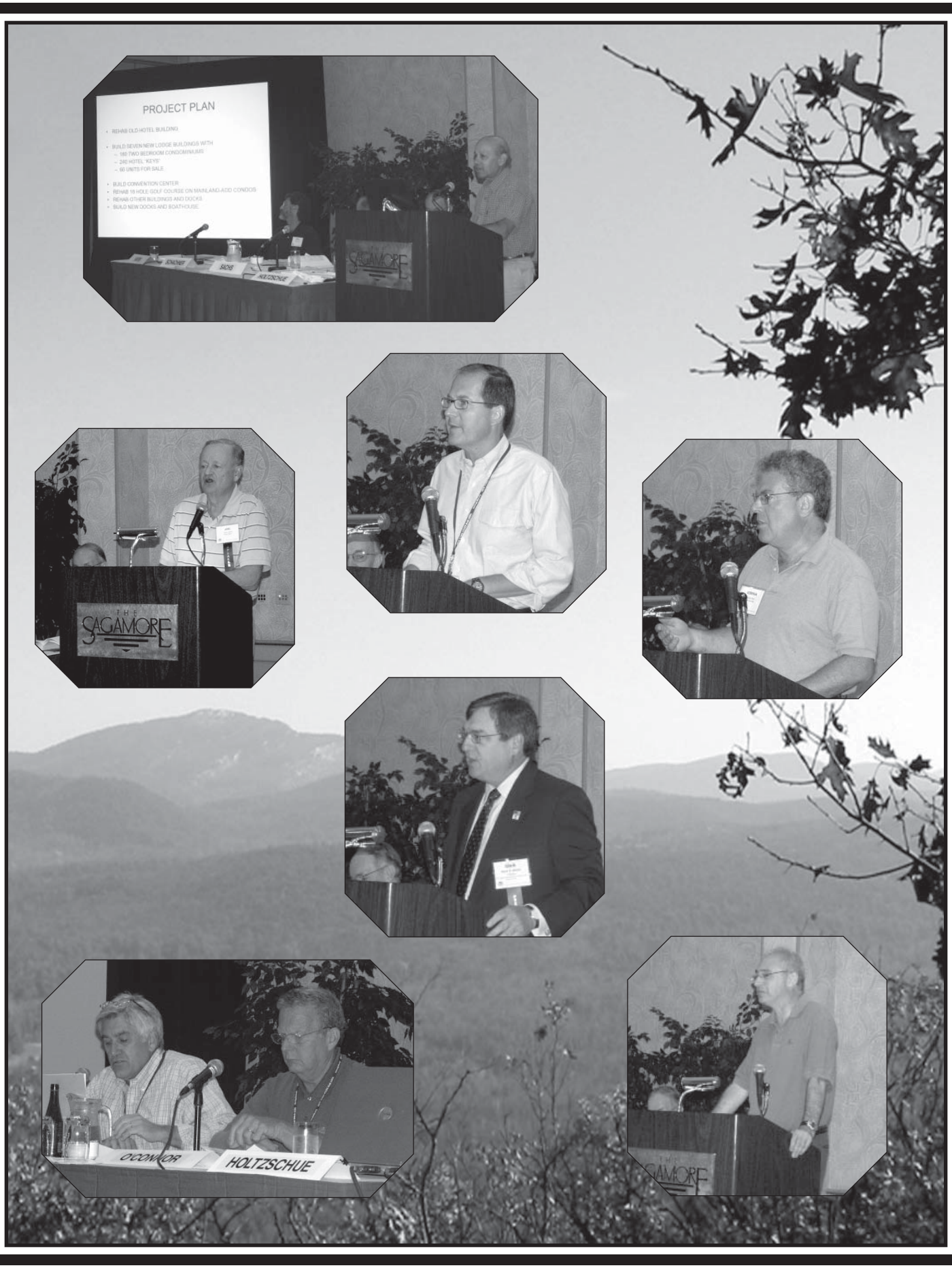
BOLTON LANDING


PROJECT PLAN
REHAB OLD HOTEL BUILDING
BUILD SEVEN NEW LODGE BUILDINGS WITH
– 180 TWO BEDROOM CONDOMINIUMS
– 240 HOTEL "KEYS"
– 60 UNITS FOR SALE
BUILD CONVENTION CENTER
REHAB 18 HOLE GOLF COURSE ON MAINLAND-ADD CONDOS
REHAB OTHER BUILDINGS AND DOCKS
BUILD NEW DOCKS AND BOATHOUSE
SAGAMORE
THE SAGAMORE
HOLTZSCHUE

(Continued from page 80)

E. Piggybacking

Tenants subject to New York's Sublet Law are prohibited from continuously subletting an apartment.[46] A rent-stabilized tenant is limited to subletting an apartment for a maximum of two years, including the term of the proposed sublease, out of the four years preceding the proposed sublease's termination date.[47] Violating this "no piggybacking" rule results in an illegal sublet.

III. Notice to Cure

To evict a rent-stabilized tenant, the landlord must first serve the tenant with a written notice to cure providing at least 10 days for the tenant to cure the wrongful acts or omissions.[48] This procedure also applies to loft tenants.[49] A landlord that gives a tenant an inadequate time to cure is unable to maintain a summary proceeding for an illegal sublet.[50]

The requirement to serve the tenant with a notice to cure does not apply if (1) the violation is continuous or recurrent and the landlord has previously served the tenant with a notice to cure within the last six months; or (2) the violation is a willful breach of an obligation that results in serious and substantial injury to the landlord or the property.[51]

IV. Notice to Terminate

Assuming that the landlord complies with the timing requirements of the notice to cure and that the tenant fails to cure the violation, the landlord may then serve the tenant with a termination notice requiring the tenant to vacate or surrender, subject to certain timing requirements before the intended termination date.[52] A landlord must serve the tenant at least seven days before the cited surrender date.[53] This termination notice may be combined with the notice to cure, such that the termination period includes the 10-day period specified in the notice to cure.[54] The notice to cure must state the grounds on which the owner relies for terminating the tenancy, the facts necessary to establish that ground, and the date by which the tenant is required to surrender possession.[55] A landlord will not establish a sufficient predicate notice to maintain an eviction proceeding if the notice of termination "merely recite[s] the legal ground for the eviction, but fail[s] to set forth any of the facts upon which the ensuing . . . proceeding would be based."[56] These requirements ensure that tenants are informed of the legal and factual claims asserted and provides them with the opportunity to "interpose any available defenses."[57] When a termination notice is deficient because it fails to contain all required information, the petition might be dismissed.[58] Strict compliance with these statutory provisions is mandated because a summary holdover proceeding is "entirely the creation of statute."[59]

At least for rent-stabilized tenants, a landlord must add five days to the combined cure notice and termination notice if the combined predicate notice is served by mail.[60] If the adequacy of the notice is material, courts will assess the adequacy of the notice in view of its reasonableness and all the attendant circumstances.[61]

V. The Eviction Proceeding

After a landlord serves a timely and sufficient predicate notice, the landlord's remedy is to commence a summary eviction proceeding based on an illegal sublet.[62] This proceeding can be instituted before a rent-stabilized lease expires.[63] The RSC further supports a landlord's right to evict a tenant for an illegal sublet by providing that a landlord may evict when the tenant sublets or assigns without obtaining prior written consent.[64] A landlord may not engage in a "self-help" eviction.[65]

Courts are split on whether a landlord or owner may assert in the petition alternative grounds for the tenant's removal from the rental unit. Some courts have permitted alternative pleadings in the context of an illegal sublet or assignment if the asserted theories are consistent.[66] Other courts have held that because the elements of each ground are "intrinsically different," the notices and pleadings may not combine theories.[67]

A landlord will not prevail on an illegal-sublet claim by asserting only that the prime tenant is no longer using the rental unit as a primary residence.[68] But a landlord need not allege a tenant's alternative residence to prevail.[69] A landlord may be successful by asserting one of the following: (1) breach of the lease; (2) statutory violation(s); (3) lack of consent for the sublet; (4) primary-residence violation.[70]

VI. Motion Practice and Disclosure

There is some debate, at least in the First Department, about when summary judgment is appropriate in an eviction proceeding based on an illegal sublet. A court might find that a tenant's summary-judgment motion seeking to dismiss a landlord's petition is premature and not grant it until the landlord has the opportunity to prove an illegal sublet at trial.[71] Courts debate over how much evidence a landlord must produce for an illegal sublet and how much rebuttal evidence a tenant must allege.[72] Most New York courts agree that when the only evidence a landlord offers is in terms of a primary-residence violation, a tenant's motion for summary judgment should be granted because the proper remedy is a nonprimary-residence holdover proceeding.[73]

Landlords and tenants must follow distinct processes when facing an alleged illegal-sublet proceeding.

Disclosure will be permitted, in limited circumstances, to ascertain the nature of the parties' relationship when the tenant asserts that the alleged illegal subtenant is a roommate.[74] When disclosure is more closely related to proof of nonprimary residence than to proof of an illegal sublet, however, the motion for leave for disclosure will be denied.[75] Courts will determine whether discovery is warranted by applying the ample-need requirement.[76]

When a tenant's defense to an illegal sublet claim is that the alleged illegal subtenant is a roommate, discovery may be permitted to ascertain the true nature of the parties' relationship.[77]

VII. Defenses

Once the tenant receives the notice to cure, the tenant may assert a defense alleging that there is no illegal sublet, that the landlord consented to the sublet, or that the alleged illegal subtenant is a family member or a roommate.

Tenants may also question whether a notice to cure was timely served or argue that the illegal sublet was cured.[78] After the landlord meets this burden and makes out a *prima facie* case of an illegal sublet, the summary proceeding may be maintained.[79]

VIII. Period to Cure

A landlord must give the tenant adequate notice and a specified amount of time to cure the illegal sublet, either by express agreement in the lease or by statute.[80] If the defect is not cured, the landlord may serve the tenant with a notice of termination, which ends the tenancy as of a particular date.[81] If the tenant does not vacate the premises as of that date, the landlord may institute a summary eviction proceeding.[82]

When a landlord proves its case and secures a final judgment on consent or after trial, courts will issue a stay of the execution of the warrant of eviction for 10 days to allow the tenant to cure the illegal sublet.[83] If the tenant does not cure, the court may stay the execution of the warrant for up to six months, in the court's discretion.[84]

A prime tenant may be able to cure both an illegal sublet and, unless grossly excessive, a rent overcharge or profiteering. One court found that a rent overcharge may be cured if the prime tenant cures the illegal sublet and returns all rent overpayments to the illegal subtenant.[85] This scenario is possible even if the lease is silent about rent overcharges. Landlords may assert that the overcharges caused a tenant to forfeit all rights to the rental unit because of unlawful profiteering.[86] Note that RSC § 2525.6 permits tenants to charge a subtenant a 10 percent surcharge over the legal rent when the apartment is fully furnished.

IX. Tenant's Options

The tenant has the option of affirmatively commencing an action seeking a declaratory judgment alleging that the landlord waived the written-consent requirement for subletting.[87] This type of declaratory relief will be granted only if the tenant can allege specific facts proving the waiver.[88] If the landlord properly served the notice to cure and the tenant had the opportunity to cure within the 10-day notice period, a court will likely deny injunctive relief.[89] If material issues of law or fact are present, Supreme Court may grant a Yellowstone injunction, temporarily tolling the time to cure the lease violation.[90]

X. Consequences of Illegal Sublets

A landlord may be entitled to increase a prime tenant's rent as a result of an illegal sublet if an illegal sublet exists and the tenant cures to avoid eviction. A rent increase is not automatic and will be analyzed factually on a case-by-case basis.[91]

XI. Conclusion

The law of subletting in New York has twists and turns that reflect the labyrinthian nature of landlord-tenant proceedings, especially for rent-regulated premises. But the rules make sense and comport the legislative will: to allow sublets of limited duration when a tenant does not abuse the right to sublet.

Endnotes

1. *Black's Law Dictionary* 600 (pocket ed. 1996).
2. *Id.* at 46.
3. *See, e.g.*, *Anoroc Realty, Inc. v. Rasmussen*, 4 Misc. 3d 135(A), 791 N.Y.S.2d 867, 867 (App. Term 2d Dep't 2d & 11th Jud. Dists. 2004) (mem.).
4. *Rima 106, L.P. v. Alvarez*, 257 A.D.2d 201, 205, 690 N.Y.S.2d 40, 43 (1st Dep't 1999) (mem.). The *Rima* court found that RPL § 226-b (5) and (6) provide that subleases and assignments must be in statutory compliance to avoid breaching the lease and being null and void. Any lease clause permitting a tenant to sublet and assign freely "confers benefits in direct violation" of the statute's constraints. It is not the purpose of New York's rent-regulation laws and codes "to create a class of mini-landlords who can profiteer in housing units placed under the law's protection." *Id.*
5. *Id.*; Daniel Finkelstein & Lucas A. Ferrara, *Landlord and Tenant Practice in New York* § 10:150, at 10-64 (2006 ed.).
6. *McDermott v. Pinto*, 101 A.D.2d 224, 229, 475 N.Y.S.2d 15, 18 (1st Dep't 1984) (mem.) (giving §§ 37 and 51 of the Emergency Tenant Protection Act retroactive effect).
7. *Sherry House Assocs. v. Kaye*, 167 Misc. 2d 729, 730, 643 N.Y.S.2d 881, 881 (App. Term 1st Dep't 1996) (*per curiam*).
8. *See, e.g.*, *Caniglia v. Perez*, 182 Misc. 2d 680, 682, 700 N.Y.S.2d 392, 393 (Hous. Part Civ. Ct., Queens Co. 1999).
9. RPL § 226-b(2)(a).
10. *Id.*
11. *Id.*

12. *Id.* § 226-b(2)(b).
13. *Id.* § 226-b(2)(c).
14. *Id.*
15. *Id.*
16. *Id.*
17. *Id.* § 226-b(2)(a).
18. *See* 9 N.Y.C.R.R. 2525.6.
19. RPL § 235-f(2).
20. *Id.*
21. *See* 9 N.Y.C.R.R. § 2204.6(d)(3)(i) (providing that family members include prime tenant's husband, wife, son, daughter, stepson, stepdaughter, father, mother, stepfather, stepmother, brother, sister, grandfather, grandmother, grandson, granddaughter, father-in-law, mother-in-law, son-in-law, or daughter-in-law).
22. *Id.*
23. *Id.*
24. *Id.*; *see 235 W. 71st St. LLC v. Chechak*, 4 Misc. 3d 114, 115, 782 N.Y.S.2d 498, 498-99 (App. Term 1st Dep't 2004) (*per curiam*) (characterizing over 20 years' occupancy as long-term tie with prime tenant and rental unit); *Arlin LLC v. Arnold*, 9 Misc. 3d 1114(A), __ N.Y.S.2d __ , 2005 WL 2384716, at *6 (Hous. Part Civ. Ct., N.Y. Co. 2005) (Gerald Lebovits, J.) ("A landlord may not maintain an illegal-sublet proceeding against a tenant's immediate family member with a long-standing connection to the apartment, even if the primary tenant no longer lives in the apartment."); *Ali Baba Hotel Corp. v. Seye*, 162 Misc. 2d 1006, 1008-09, 619 N.Y.S.2d 243, 245 (Hous. Part Civ. Ct., N.Y. Co. 1994) (holding that evidence of half-brothers living together for more than two years established valid sublet to family member); *see also* Robert L. Sweeney & Patricia Hart Nessler, *1994-95 Survey of New York Law*, 46 Syracuse L. Rev. 799, 817-18 (1995).
25. *Runquist v. Koeppel*, 146 Misc. 2d 569, 571, 551 N.Y.S.2d 765, 767 (Hous. Part Civ. Ct., N.Y. Co. 1990) ("Until such time as a court determines the withholding of consent to the sublet was unreasonable, as only a court may determine and not the parties, the sublease does not confer any right of occupancy.").
26. *Id*; *see* Finkelstein & Ferrara, *supra* note 5, at § 3:18, at 3-11.
27. *See* Finkelstein & Ferrara, *supra* note 5, at § 3:18, at 3-11; *see generally* 4 Robert F. Dolan, *Rasch's New York Landlord and Tenant—Including Summary Proceedings* § 36:10, at 564 (4th ed).
28. RPL § 226-b(2)(a).
29. *Baruch Hashem Yom Yom Corp. v. Gadbois*, 5 Misc. 3d 1023(A), 799 N.Y.S.2d 158, 2004 N.Y. Slip Op. 51512(U), 2004 WL 2805649, at **2-3, 2004 N.Y. Misc. LEXIS 2490, at *3-4 (Hous. Part Civ. Ct. N.Y. Co. 2004).
30. *See* 9 N.Y.C.R.R. § 2525.6(c).
31. 9 N.Y.C.R.R. §§ 2524.3(h), 2525.6(f); *see* Finkelstein & Ferrara, *supra* note 5, at § 18:197, at 18-89.
32. RPL § 226-b(1).
33. *Id.* at § 226-b(2)(a).
34. 9 N.Y.C.R.R. § 2505.7(a).
35. *Id.*
36. *See 2328 Uniave Corp. v. Beheler*, 2003 N.Y. Slip Op. 51135(U), at *4, 2003 WL 21709667, at *2, 2003 N.Y. Misc. LEXIS 956, at *3 (Civ. Ct., Bronx Co. 2003) (finding illegal sublet because tenant "took in various individuals as occupants . . . and maintained a revolving door operation to the subject apartment from which she gained financial renumeration [sic]").
37. RPL § 235 f).
38. *2328 Uniave*, 2003 N.Y. Slip Op. 51335(U), 2003 WL 21709667, at *2, 2003 N.Y. Misc. LEXIS 956, at *5-6.
39. *Id.*
40. *See Alta Apts., LLC v. Weisbond*, 10 Misc. 3d 40, 41, __ N.Y.S.2d __, 2005 WL 2997623, at *2 (App. Term 1st Dep't 2005) (*per curiam*) (Gangel-Jacob, J., dissenting) ("Once again we consider contentions of nonprimary residence brought in the guise of an illegal sublet to a family member, presumably to avoid the requirements of the 'Golub' notice or perhaps as a 'fishing expedition' in contemplation of future litigation."); *Hudson St. Equities Group, Inc. v. Escoffier*, 2003 WL 21994079, at *1 (App. Term 1st Dep't 2003) (*per curiam*); *Presbyterian Hosp. of City of N.Y. v. Melendez*, 2001 N.Y. Slip. Op. 40512(U), 2001 WL 1682762, at *1, 2001 N.Y. Misc. LEXIS 740, at *2 (App. Term 1st Dep't) (*per curiam*) (Gangel-Jacob, J., concurring).
41. *See PLWJ Realty, Inc. v. Gonzalez*, 285 A.D.2d 370, 370, 726 N.Y.S.2d 858, 858 (1st Dep't 2001) (mem.) (finding that landlord may not prevail in sublet holdover if it submits proof largely about the tenant's nonprimary residence and not about tenant's illegal sublet), *appeal dismissed*, 97 N.Y.2d 676, 738 N.Y.S.2d 287, 764 N.E.2d 391 (2001).
42. *See Arlin*, 9 Misc. 3d 1114(A), 2005 WL 2384716, at *7.
43. Omnibus Housing Act, L. 1983, ch. 403, *amd'g*, N.Y. Rent Stab. Code, N.Y.C. Admin. Code § YY51-6.0.
44. 9 N.Y.C.R.R. § 2525.6; *see* Andrew Scherer, *Residential Landlord and Tenant Law in New York* § 8:160, at 570 (2006 ed.).
45. *See Pamela Equities Corp. v. Camp*, 127 Misc. 2d 395, 396-97, 486 N.Y.S.2d 149, 150 (Hous. Part Civ. Ct. N.Y. Co. 1985) (noting that despite confusion between nonprimary residence and illegal sublet claims, "each ground is legally distinct and should not be confused due to certain common elements").
46. 9 N.Y.C.R.R. § 2505.7(c), 2525.6(c).
47. 9 N.Y.C.R.R. § 2505.7(c), 2525.6(c).
48. 9 N.Y.C.R.R. § 2504.1(d)(1)(i), 2524.3(a); *see* Finkelstein & Ferrara, *supra* note 5, at § 13:65, at 13-37-13:38.
49. *See Eichenbaum v. Kerpel*, N.Y.L.J., June 9, 1992, p. 24, col. 1 (Hous. Part Civ. Ct., N.Y. Co.) (finding that notice to cure is required before termination notice may be served on loft tenant for alleged illegal sublet).
50. *See 2215-75 Cruger Apts., Inc. v. Stovel*, 196 Misc. 2d 346, 347, 769 N.Y.S.2d 347, 348 (App. Term 1st Dep't 2003) (*per curium*) (finding that landlord's service of 10-day notice to cure that gave tenant less than 10 days to cure illegal sublet was insufficient predicate notice to permit landlord to terminate tenancy and commence holdover summary proceeding).
51. 9 N.Y.C.R.R. § 2504.1(d)(2).
52. 9 N.Y.C.R.R. § 2524.2(c); *see* Finkelstein & Ferrara, *supra* note 5, at § 13:65, at 13-38.
53. 9 N.Y.C.R.R. § 2524.3(a), 2524.2(c)(2), 2524.3(f); *see, e.g.*, *Hudson Assocs. v. Benoit*, 226 A.D.2d 196, 197, 640 N.Y.S.2d 540, 540 (1st Dep't 1996) (mem.); *see also* Finkelstein & Ferrara, *supra* note 5, at § 15:172, at 15-98-15-99; Scherer, *supra* note 44, at § 8:257, at 601.
54. 9 N.Y.C.R.R. § 2504.3 (Emergency Tenant Protection Regulations).
55. 9 N.Y.C.R.R. § 2524.2(b); *see Bellstell 140 E. 56th St., LLC v. Layton*, 180 Misc. 2d 25, 26-27, 687 N.Y.S.2d 536, 537-38 (Hous. Part Civ. Ct. N.Y. Co. 1999).
56. *See Bellstell*, 180 Misc. 2d at 26-27, 687 N.Y.S.2d at 537-38; *Berkeley Assocs. Co. v. Camlakides*, 173 A.D.2d 193, 194, 569 N.Y.S.2d 629, 630 (1st Dep't 1991) (mem.), *aff'd*, 78 N.Y.2d 1098, 1099, 578 N.Y.S.2d

872 , 872 (1991); *Kaycee W. 113th St. Corp. v. Diakoff*, 160 A.D.2d 573, 574, 554 N.Y.S.2d 216, 217 (1st Dep't 1990) (mem.); *First Sterling Corp. v. Zurkowski*, 142 Misc. 2d 978, 979, 542 N.Y.S.2d 899, 900 (App. Term 1st Dep't 1989) (*per curiam*).

57. *MSG Pomp Corp. v. Doe*, 185 A.D.2d 798, 800, 586 N.Y.S.2d 965, 966 (1st Dep't 1992) (mem.); *accord City of New York v. Valera*, 216 A.D.2d 237, 238, 628 N.Y.S.2d 695 (1st Dep't 1995) (mem.); *Giannini v. Stuart*, 6 A.D.2d 418, 420, 178 N.Y.S.2d 709, 711 (1st Dep't 1958) (*per curiam*); *Bellstell, 140 E. 56th St.*, 180 Misc. 2d at 27, 687 N.Y.S.2d at 538.

58. *Chinatown Apts. v. Chu Cho Lam*, 51 N.Y.2d 786, 788, 433 N.Y.S.2d 86, 88, 412 N.E.2d 1312, 1314 (1980) (mem.).

59. *In re Smith*, 204 A.D. 248, 249, 197 N.Y.S. 373, 374 (4th Dep't 1922); *Goldman Bros. v. Forester*, 62 Misc. 2d 812, 815, 309 N.Y.S.2d 694, 697 (Hous. Part Civ. Ct., N.Y. Co. 1970); *MSG Pomp*, 185 A.D.2d at 799-800, 586 N.Y.S.2d at 966; *Berkeley Assocs. Co. v. Di Nolfi*, 122 A.D.2d 703, 705, 505 N.Y.S.2d 630, 632 (1st Dep't 1986) (mem.).

60. *ATM One, LLC v. Landaverde*, 2 N.Y.3d 472, 472, 779 N.Y.S.2d 808, 808, 812 N.E.2d 298, 298 (2004) (dealing with notice to cure).

61. *See Hughes v. Lenox Hill Hosp.*, 226 A.D.2d 4, 17, 651 N.Y.S.2d 418, 427 (1st Dep't 1996).

62. 9 N.Y.C.R.R. §§ 2524.3(h), 2525.6(f); N.Y.C. Admin. Code §§ 26-511(c)(9)(e), 26-511(c)(12).

63. 9 N.Y.C.R.R. § 2524.3(h); *Arlin*, 2005 WL 2384716, 2005 N.Y. Slip Op. 51541(U), at *5.

64. *See* Finkelstein & Ferrara, *supra* note 5, at § 18:197, at 18-89, at 18-91.

65. *See, e.g.*, *Keenan v. Perreault*, N.Y.L.J., Oct. 22, 1998, p. 29, col. 5 (App. Term 1st Dep't) (*per curiam*) (noting that even if illegal sublet exists, landlord's remedy is to commence a summary eviction proceeding, not to resort to "self-help" tactics like changing locks).

66. *Peck v. Greene*, N.Y.L.J., May 11, 1994, p. 30, col. 4 (App. Term 1st Dep't) (*per curiam*) (permitting landlord alternatively to plead illegal sublet and nonprimary residence grounds for tenant's removal); *Carol Mgt. Corp. v. Britton*, N.Y.L.J., Oct. 26, 1992, p. 26, col. 5 (App. Term 2d Dep't 2d & 11th Jud. Dists.) (mem); *Turin Hous. Develop. Fund Co., Inc. v. Maor*, 1 Misc. 3d 907(A), 781 N.Y.S.2d 628, 2003 WL 23146010, at *2 (Hous. Part Civ. Ct., N.Y. Co. 2003) (Gerald Lebovits, J.) (finding that if alternative grounds are consistent, petitioner must plead both grounds or risk losing proceeding case and being estopped from moving on alternative theory).

67. *Cheung v. Li*, 148 Misc. 2d 55, 59, 559 N.Y.S.2d 425, 427 (Hous. Part Civ. Ct., Kings Co. 1989) ("The legal definitions and elements that the petitioner is required to prove to establish that respondents are licensees or squatters are intrinsically different. . . .").

68. *See PLWJ Realty*, 285 A.D.2d at 371, 726 N.Y.S.2d at 858.

69. *See Bellstell 140 E. 56th St.*, 180 Misc. 2d at 29, 687 N.Y.S.2d at 539; *see generally* Robert E. Parella, *1998-99 Survey of New York Law*, 50 Syracuse L. Rev. 863 (2000).

70. *Bellstell 140 E. 56th St.*, 180 Misc. 2d at 29, 687 N.Y.S.2d at 539.

71. *See, e.g.*, *445/86 Owners Corp. v. Haydon*, 300 A.D.2d 87, 88-89, 751 N.Y.S.2d 456, 456-57 (1st Dep't 2002) (mem.).

72. *See Alta Apts.*, 10 Misc. 3d 40, __ N.Y.S.2d __; *Hudson St. Equities Group*, 2003 WL 21994079, at *1 (discussing whether illegal-sublet claim was sufficiently rebutted by evidence of subletting family member's tenant's long-standing ties with apartment).

73. *See 235 W. 71st St. LLC v. Chechak*, 16 A.D.3d 242, 242, 790 N.Y.S.2d 871, 871 (1st Dep't 2005) (mem.); *PLWJ Realty*, 285 A.D.2d 370, 726 N.Y.S.2d 858; *Park Holding Co. v. Rosen*, 241 A.D.2d 304, 659 N.Y.S.2d 35 (1st Dep't 1997) (mem.) (affirming on dissent in Appellate Term); *S. Pierre Assocs. v. Baron*, 10 Misc.3d 143(A), 2006 WL 211708, 2006 N.Y. Slip Op. 50095(U) (App. Term 1st Dep't Jan. 27, 2006) (*per curiam*); *see also* Dolan, *supra* note 27, at § 11:9.

74. *See Hartsdale Realty Co. v. Santos*, 170 A.D.2d 260, 260, 565 N.Y.S.2d 527, 527-28 (1st Dep't 1991) (mem.) (limited discovery permitted to identify apartment's current occupants); *Houston Village Apt. Co. v. Zitin*, 2001 WL 1470310, at *1 (App. Term 1st Dep't) (*per curiam*) (finding that with presumption favoring discovery, landlord established "ample need" to depose the tenant's wife); *see also* Finkelstein & Ferrara, *supra* note 5, at § 15:530, at 15-312.

75. *E.g.*, *Tribeca Equity Partners, LP v. Ezcura*, N.Y.L.J., Mar. 27, 1996, p. 32, col. 4 (Hous. Part Civ. Ct. N.Y. Co.) (declining to grant discovery in illegal-sublet proceeding because landlord's request for disclosure related solely to documents indicating nonprimary residence).

76. *See Hartsdale,* 170 A.D.2d at 260, 565 N.Y.S.2d at 527-28 ("[A]mple need has been demonstrated for limited discovery into the identification of the present occupants of the apartment."); *see* Finkelstein & Ferrara, *supra* note 5, at § 15:530, at 15-312.

77. *See Hartsdale,* 170 A.D.2d at 260, 565 N.Y.S.2d at 527-28; *Houston Village Apt. Co. v. Zitin*, 2001 WL 1470310, at *1; *see also* Finkelstein & Ferrara, *supra* note 5, at § 15:530, at 15-312.

78. 9 N.Y.C.R.R. § 2524.3(a); *see Benoit*, 226 A.D.2d at 197, 640 N.Y.S.2d at 540 ("In a summary holdover proceeding to recover possession upon the ground of an illegal sublet, the landlord is required to prove as part of its *prima facie* case that a notice to cure was served and that the tenant has failed to cure.").

79. 9 N.Y.C.R.R. § 2504.1(d)(1)(ii).

80. Finkelstein & Ferrara, *supra* note 5, § 15:103, at 15-82.

81. *See* Mary Ann Hallenborg, *New York Tenants' Rights* 16/5 (2002).

82. *Id.* at 16/5-16/6.

83. RPL § 753(4).

84. *Id.* § 753(1).

85. *Husda Realty Corp. v. Padien*, 136 Misc. 2d 92, 93, 518 N.Y.S.2d 99, 100 (Hous. Part Civ. Ct. N.Y. Co. 1987).

86. *BLF Realty Holding Corp. v. Kasher*, 299 A.D.2d 87, 747 N.Y.S.2d 457 (1st Dep't 2002) (sublets under Loft Law), *appeal dismissed*, 100 N.Y.2d 535, 762 N.Y.S.2d 876, 793 N.E.2d 413 (2003); *see* Scherer, *supra* note 44, at § 8:164, at 572.

87. *See, e.g.*, *Excel Graphics Technologies, Inc. v. CFG/AGSCB 75 9th Ave., LLC*, 1 A.D.3d 65, 767 N.Y.S.2d 99 (1st Dep't 2003), *lv. dismissed*, 2 N.Y.3d 794, 781 N.Y.S.2d 292, 814 N.E.2d 464 (2004).

88. *Id.* at 102-03.

89. *Id.* at 102-03.

90. *Id.* at 104.

91. 9 N.Y.C.R.R. § 2202.6; *see generally* Guy McPherson, *It's the End of the World as We Know It (and I Feel Fine): Rent Regulation in New York City and the Unanswered Questions of Market and Society*, 72 Fordham L. Rev. 1125 (2004).

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Real Property Transfer Tax and Mortgage Tax Traps in Conveyance of Condominium Units in New York City

By Yosi (Joe) Benlevi

Introduction

As many new residential condominium projects are being offered to the public, it is not a rarity to see buyers purchasing two, three and sometimes four units and combining them into impressive residences. As the price tag of these condominium units are constantly raised, questions regarding transfer taxes affecting the sale of these units become more important. Furthermore, developers are transferring to the buyer various expenses, such as transfer taxes, which generally are the responsibility of the seller, making the transfer taxes part of the direct purchase costs that buyers have to deal with at closing. The objective of this article is to describe the current interpretation the taxing authorities have given to the rules affecting the New York City Real Property Transfer Tax ("RPTT") in conveyances of multiple condominium units from a single seller to a single purchaser. We will analyze the recent rulings related to the matter and suggest possible interpretations that may favor purchasers or developers of condominium units.

We have also dedicated part of this article to describe the special provisions of § 339-ee of the New York Real Property Law, which allows credit for mortgage tax paid by developers of condominium projects (the "339-ee Credit").

Residential v. Commercial Transfer Tax Rates

Section 11-2102(a) of the New York City Administrative Code (the "Code") applies the RPTT to each deed conveying an interest in real property located in New York City when the consideration is over $25,000. The RPTT rates depend on the amount of the consideration and the type of property being transferred.

For conveyances of "one, two or three family houses and individual residential condominium units," the applicable RPTT rates are 1% where the consideration does not exceed $500,000 and 1.425% where consideration is in excess of $500,000 (the "Residential Rate"). For "all other conveyances," the Code imposes a tax of 1.425% where the consideration does not exceed $500,000 and 2.625% where the consideration is in excess of $500,000 (the "Commercial Rate").[1]

It is important to begin our analysis by reminding readers that neither the Code nor The Rules of the City of New York (the "Rules") specifically address the proper tax rates to be applied in case of a transaction involving multiple residential condominium units.[2] The official position of the Commissioner of Finance for the City of New York (the "Commissioner") and the New York City Department of Finance (the "Department") is that where more than one residential condominium unit is being conveyed to a single buyer by a single seller, the Residential Rate does not apply. This policy, known as the "Bulk Sale Policy," is described and set forth in the Finance Memorandum 00-6 (the "00-6 Memo") published on June 19, 2000.[3]

The 00-6 Memo is very short, laconic in language, and does not provide any substantive explanation to the policy described therein.[4] In order to learn more about the reasoning behind this interpretation we must examine a number of Letter Rulings published in the course of recent years (and some even before the 00-6 Memo) and review briefs submitted by the Commissioner in three separate New York City Tax Appeals Tribunal cases decided in the last year dealing with the topic.[5]

The Commissioner's main argument to support its Bulk Sale Policy in the 00-6 Memo and in the abovementioned cases stands upon the basic interpretation rule requiring that every word in a statute must be interpreted to be given meaning and not to be ignored. Thus, according to the Commissioner the word "individual" in the phrase "individual residential condominium units" in Code § 11-2102.a(9)(i) cannot be ignored. The Commissioner asserts that the sole interpretation of this word is that the Residential Rate applies only to a sale of a single/individual condominium unit and any other interpretation of the Code will render meaningless the statutory use of the word "individual." In the recent cases that put to the test this interpretation of the Code, the Commissioner further claimed that by including the word "individual" the legislature intended to restrict the Residential Rate to transfer of title to a single residential unit only.[6]

However, the Administrative Law Judges, in all three recent cases that examined the proper interpretation of the Code, rejected the Commissioner's position and ruled against the Department. It is important to remember that the determinations of Administrative Law Judges are not considered binding precedent. However, due to the fact that the Department has indicated its intention to appeal in all three cases and clearly stated that pending the outcome of the appeal they will continue to apply the Bulk Sale Policy, it is inevitable that the rulings of the judges in all three cases are to be re-examined by the Appeals Division of the Tribunal and, pending the outcome of the appeals, may become the prevailing law.

To begin with, all three rulings indicate that there is no evidence to support the Commissioner's interpretation of the legislative intention giving the word "individual" a restrictive meaning. Analysis of the legislative history of the RPTT actually indicates that the legislature intended to allow a lower tax rate to all residential properties in comparison to all commercial properties that generally are income-producing and have more of an investment characteristic to them.[7]

With respect to the Commissioner's main argument asking that a meaning must be given to the word "individual" in the Code, Chief Administrative Law Judge Gombinski in *Cambridge Leasing Corporation* offers a different definition to the word "individual." Judge Gombinski reads the word "individual" to restrict the Residential Rate to transfers of units that contain single residences, in contrast to transfers of individual units that actually contain multiple residential units. The judge finds an illustration to this interpretation in conveyances of residential "condop" units, where the residential unit in the condominium actually contains numerous individual residences that in most of the cases are conveyed by the sponsor to a cooperative housing corporation.[8] Furthermore, the Commissioner's briefs in these cases indicate that in fact the Department's reading of the Code is the one altering the actual reading of the text, by adding to the text a singular meaning to the word "unit" as if the statute reads "**an** individual residential condominium unit" where the Code specifically reads "individual residential condominium unit**s**." (*emphasis added*).[9]

Finally, as for the analogy made in the past by the Commissioner, that between conveyances of multiple residential condominium units and conveyances of multiple cooperative apartments, the Courts have rejected this analogy.[10] The Court states that a transfer of multiple cooperative apartments is governed by The Rules of the City of New York that specifically require the imposition of the Commercial Rate for conveyances of multiple cooperative apartments, where for conveyances of multiple residential condominium units the statute is silent.[11]

Exception to the Bulk Sale Policy—Combined Residential Condominium Units

Even under the Bulk Sale Policy the Commissioner concedes that some exceptions are allowed. The 00-6 Memo states that the Department will not treat transfer of adjacent condominium units that have been physically combined into a single residence as a bulk sale. The 00-6 Memo does not indicate the way the Department will determine if a specific transaction qualifies for this exception. The practice in the industry is that a revised Certificate of Occupancy, a letter of completion from the Buildings Department or a revised tax lot designation reflecting the joining of two or more units will be acceptable evidence of such a combination.[12] However, the 00-6 Memo states that the combination of the units after the transfer will not be sufficient to permit the transaction to be treated at the Residential Rate. Therefore, the combination of the units must be finalized prior to transfer.

In the past the Department has interpreted this exception to the Bulk Sale Policy in a rather restrictive way. However, in a recent Letter Ruling, the Department accepted a more liberal interpretation of the exception.[13] In this Letter Ruling, the Department accepted the assertion of a seller of three separate residential condominium units, which were physically combined into one residential unit prior to their transfer, as a sale of a single condominium unit, subject to the Residential Rate.[14]

In that case, although the seller could not provide a new Certificate of Occupancy or letter of completion, pictures of the units showed portions of the combined units and staircases connecting them. The seller also represented that all the bedrooms were located on one specific floor, which originally was one unit and the living room was located on a separate floor, which was originally a different unit. The circumstances in this case clearly showed that at the time of transfer the units were physically combined.[15]

Until the Appeals Division of the Administrative Tax Tribunal reaches a final decision in the matter, the Department is standing behind its interpretation of the Code, and therefore the Bulk Sale Policy is in effect. However, following the recent interpretation given by the Department to the Bulk Sale Policy exception, it is recommended that parties contracting for the purchase of multiple residential condominium units that are to be combined to a single residential unit should plan in advance and conclude at least a major part of the physical combination of the units prior to their transfer.

Transfer Tax Paid by Buyer as "Additional Consideration"

As mentioned in the introduction, customarily developers tend to transfer the cost of RPTT and the New York State Real Property Transfer Tax ("TP-584") to the buyer of the condominium unit. Any transfer taxes paid by the buyer, instead of the seller, is considered "additional consideration" which must be added to the purchase price in computing the RPTT and TP-584 due on a specific conveyance.

The calculation of the RPTT and TP-584 is done in a two tier process. In first instance the RPTT and TP-584 are calculated in the regular manner, as if it is being paid by the seller. Then, both the RPTT and TP-584 amounts are added to the consideration, increasing it to include the "additional consideration" which is the transfer tax being paid by the buyer on behalf of the seller. Then, the RPTT and TP-584 are re-calculated, this time the consideration being the actual purchase price and the RPTT and TP-584 calculated in the first tier.[16]

Mortgage Recording Tax Rates and the 339-ee Credit

Section 339-ee of the RPT provides a credit for previously paid mortgage tax in the first conveyance of a condominium unit, which is known in the industry as the 339-ee Credit. In a nutshell, the statute allows a developer of a condominium project to get, at the time of the first sale of the condominium unit, a credit against the mortgage recording taxes (except the Special Additional Mortgage Tax) that would otherwise be payable on a new mortgage taken by the new owner. This credit can be a very substantive benefit that can allow the developer to recuperate almost all the mortgage tax paid for the mortgages taken for the entire project.

In order to claim the credit, the mortgage for which the developer had originally paid mortgage tax has to be either (i) a construction mortgage that was used for the construction of the structure; or (ii) a blanket mortgage whose proceeds were applied exclusively to the payment of a construction mortgage, or the purchase of the land or buildings. The statute doesn't define the term "Construction Mortgage," but it seems that the intention is to include any mortgage that was applied for construction expenses, including "Project Loan" mortgages and "In-Direct Costs Loan" mortgages that are very common in many current construction financing projects.

When credit for a blanket mortgage used for the acquisition of land is desired, the statute requires the acquisition to be no more than two years prior to the recording of the Declaration of Condominium.[17] It is important to note that this "two-year" limit applies only to acquisition mortgages and has to be distinguished from a different two-year test, described herein, affected by the sale date of the first condominium unit in the project. In other words, developers who wish to get credit for mortgage tax paid on acquisition mortgages must record the Declaration within two years from the actual acquisition of the property. It should be noted that the time period is measured from the date of purchase and not the date of recordation of the vesting deed.[18]

Moreover, the statute requires that the mortgage recording tax to be duly paid on such construction or blanket mortgage in accordance with Article 11 of the New York Tax Law.[19] The practical meaning of this requirement is that parties cannot circumvent the provisions of the statute limiting the time frame for claiming credit for past mortgage tax paid, by modifying the old mortgage or consolidating it with a new nominal mortgage, and by this act "bringing to date" the old mortgage and the old mortgage tax paid. Credit can be claimed only if the mortgage tax was actually paid within the recognized time frame.

In addition to the above-described restrictions, Section 339-ee also requires that the sale of the first condominium unit must be within two years of the recording of the mortgage for which the credit is claimed. This requirement, especially when the construction project is a multi-stage one that encompasses a prolonged construction process, can be a critical trap. In these projects, sometimes even when the construction for part of the project is finished, the developer cannot close on an individual unit due to Certificate of Occupancy issues. In order to get the benefit of the credit it is crucial that at least one condominium unit is sold prior to the lapse of the two-year time period.

The combination of the two different "two-year rules" is that in order to claim credit for mortgage tax paid for acquisition mortgages, the developer must record the Declaration and close on the sale of the first unit within two years from the recording of the blanket mortgage and payment of the tax. Although for construction mortgages the statute requires the developer only to close on the sale of the first unit within two years from the recording of the construction mortgage, essentially the requirements for this credit are the same as the requirements for acquisition mortgages. This is because the recording of the Declaration of Condominium is the actual act creating the real property called the condominium unit, without which the units do not legally exist, and therefore no developer can actually sell a unit before recording the Declaration.[20]

The credit to be claimed is in an amount resulting from the product of the purchaser's pro rata percentage of interest in the common elements and the mortgage tax already paid on the construction or blanket mortgage. For example, let's assume that in a specific condominium project the developer paid $50,000 for Basic New York State mortgage tax; $100,000 for New York City Mortgage Tax; $25,000 in Special Additional Mortgage Tax; and $30,000 in Additional Mortgage Tax (also known as the AMT surcharge). When transferring a unit together with a two percent interest in the common elements of the condominium, the developer will be entitled to claim a maximum credit of $1,000 for Basic New York State mortgage tax ($50,000*2%); $2,000 for New York City Mortgage Tax ($100,000*2%); no credit for Special Additional Mortgage Tax paid; and $600 for Additional Mortgage Tax ($30,000*2%). Even though the statute doesn't state who is entitled to the 339-ee Credit, the practice is that the developer almost always claims the credit and the purchaser ends up paying the full mortgage tax for the mortgage taken at the time of closing. The end result for the buyer will be that instead of paying the whole mortgage tax due to the state, part of it (in this example $3,600) will go to the developer as a credit claimed on his closing statement.

Endnotes

1. *See also* DAVID M. GOLDBERG, TRANSFER AND MORTGAGE RECORDING TAXES IN NEW YORK TITLE CLOSINGS § 1.06 (2006).
2. This is not the case when dealing with conveyances of Cooperative Apartments: *See* 19 RCNY § 23-03.

3. *Real Property Transfer Tax on Bulk Sales of Cooperative Apartments and Residential Condominium Units,* Finance Memorandum 00-6 (June 19, 2000) at www.nyc.gov/finance.
4. *Id.* (Furthermore, the 00-6 Memo specifically states that "Finance Memoranda are advisory in nature and . . . are not declaratory rulings or rules of the Department of Finance and do not have legal force or effect . . . ".)
5. *In re Cambridge Leasing Corporation*, TAT(H) 03-11(RP) (September 28, 2004); *In re Daniel and Sheila Rosenblum*, TAT(H) 01-31(RP) (November 9, 2004); and *In re David Gruber*, TAT(H) 03-7(RP); TAT(H) 03-8(RP); TAT(H) 03-9(RP) (May 5, 2005).
6. Letter Ruling, FLR No. 004761-021 (August 23, 2000); *In re David Gruber* at 8.
7. *See In re Cambridge Leasing Corp.*, at 7-8 & 11-12; *In re Daniel and Sheila Rosenblum* at 9-11; *In re David Gruber* at 12-16 (for an analysis of the legislative history).
8. *In re Cambridge Leasing Corp.*; *In re Daniel and Sheila Rosenblum* at 10.
9. *In re Cambridge Leasing Corp.; In re Daniel and Sheila Rosenblum* at 7.
10. Letter Ruling FLR 94-4496 (August 17, 1994) (An example for this analogy can be found where the Deputy Commissioner states that "as in the case with sale of multiple cooperative apartments, a sale of multiple condominium units . . . does not qualify for the lower rates applicable to a conveyance of an individual unit.").
11. 19 RCNY § 23-03, examples 3 & 4.
12. A letter of completion is issued under the Building Department's Technical Policy and Procedure Notice, *available at* http://www.ci.nyc.ny.us/html/dof/pdf/00pdf/fm00_6.pdf. *See also* "New York City Transfer Tax on Multiple Residential Cooperatives and Condominiums," Michael J. Berey, *NYSBA N.Y. Real Property Law Journal,* Spring 2004, Vol. 32, No. 2, page 44.
13. *See In re David Gruber*, TAT(H) 03-7(RP); TAT(H) 03-8(RP); TAT(H) 03-9(RP) (May 5, 2005) (where the purchaser entered into three separate contracts to purchase three units to be combined to a single unit. The architect for the purchaser prepared plans for the actual combination of the units into one residential unit prior to closing and the sponsor, in anticipation of the actual combination on the units, provided the units with the "minimum level of finish" needed to obtain the Certificate of Occupancy for the units and installed only a single complete bathroom and one kitchen containing a sink and stove for all three units conveyed).
14. Letter Ruling FLR No. 054831-021 (June 9, 2005).
15. See FLR No. 994756-021 (http://www.nyc.gov/html/dof/html/pub/pub_guidance_letterrulings_rptt.shtml).
16. Technically the additional consideration (i.e., the New York City RPTT and the New York State TP-584 calculated in the first tier calculation) is added on the NYC-RPT form in Schedule 1—Details of Consideration, Item 9 ("Amount of Real Property Tax and/or other taxes or expenses of the grantor which are paid by the grantee"), and on the TP-584 form on Schedule B—Real estate transfer tax return, Item 1 (as part of the total consideration).
17. RPT § 339-ee (2).
18. RPT § 339-ee (2) (stating that "provided that such purchase was no more than two years prior to the recording of the declaration of the condominium").
19. *Id.*
20. RPT § 339-s (1).

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RPLS Task Force on Attorney Escrows Current Practice, Alternatives and Improvements

I. Overview and Introduction

In November, 2005, the President of the New York State Bar Association, A. Vincent Buzard, wrote a letter to Joshua Stein, Chair of the Real Property Law Section ("RPLS"), asking the RPLS to determine what practical methods are available to prevent the theft of real property escrow funds by lawyers. Chair Stein appointed a Task Force on Attorney Escrows, chaired by Ira Goldenberg. Following is the report of the Task Force.

The Task Force was directed to accept as given that attorney escrows need to be replaced. To fulfill that mission, the Task Force suggests banks as alternative escrowees, and we developed a model form of escrow agreement—a Bank Escrow Deposit Agreement ("BEDA"). However, the Task Force prefers a less drastic solution. After considering several alternatives, discussed below, the Task Force concluded that (1) overall, the current practice downstate of attorney escrow of contract deposits works well; (2) the current system could be improved by requiring dual signatures and requesting that escrow account statements be distributed to all interested parties; and (3) bank escrowees may provide an alternative for attorneys who prefer not to be "in the escrow business" but should not replace attorneys when they or their clients prefer that counsel serve as escrow agent.

II. Some Issues We Considered

A. Interest on Lawyer Account Fund ("IOLA")

New York Judiciary Law Section 497 requires attorneys holding escrows of "qualified funds"—funds which in the attorney's judgment are too small in amount, or which are reasonably expected to be held for too short a time, to generate sufficient interest to justify maintaining a separate interest-bearing account—to deposit them into an interest-bearing IOLA account. IOLA uses the funds it receives through these accounts to provide grants to various low-income legal assistance programs in New York. IOLA has provided tens of millions of dollars in such assistance. IOLA receives no funds whatsoever from taxpayers or attorney registration fees. Its sole source of funding is the interest earned on funds held by attorneys in IOLA accounts.

Most Task Force members are concerned about the impact upon the poor if this source of funding for legal services is eliminated, and strongly believe that the use of IOLA should be preserved to continue support of this important program.

B. Who Else Might Hold Escrows

The Task Force considered title companies, real estate brokers and banks as possible alternative escrow agents. For the reasons discussed below, the Task Force has determined that only banks provide a viable alternative to attorneys.

C. Practicalities of the Closing Process

New York real estate purchase and sale closings usually involve multiple parties—the seller, the seller's attorney, the seller's lender (and if the property is a cooperative apartment, the seller's lender's attorney), the seller's real estate broker, the purchaser, the purchaser's attorney, the purchaser's lender, the purchaser's lender's attorney, the title company (unless the property is a cooperative apartment and no title insurance is being purchased) and, if the property is a cooperative apartment, the managing agent or attorney for the cooperative corporation. In residential transactions, it is common for both the seller and the purchaser to sell one home and buy another within the same time period or even on the same day. Accordingly, any alternative escrow agent needs to be ready, willing and able to disburse escrowed funds at a moment's notice, sometimes in the form of multiple bank or certified funds, to avoid delaying or adjourning the closing and inconveniencing or causing financial hardship to the parties.

D. Cost

The Task Force is concerned that an alternative escrow agent might charge fees which the parties to the transaction find cost prohibitive. Lawyers who act as escrow agents and charge a fixed fee do not charge their clients extra for providing escrow accounts.

E. Willingness of Banks to Cooperate

See discussion in Section III below.

F. Desire of Attorneys to Act as Escrow Agents

Most members of the Task Force agree that serving as escrow agent in a real estate transaction is a thankless task, and one some attorneys would just as soon avoid. However, it is a time-honored practice that facilitates closings and works well in most situations.

III. An Alternative to Attorney Escrows: The Bank Escrow Deposit Agreement

A. The BEDA Concept

The Task Force spent a great deal of time and effort exploring how to set up an alternative system for banks to hold escrow deposits instead of attorneys. Banks are

regulated and prepared to handle bookkeeping issues. In addition, banks often already serve as escrow agents in private placement transactions. With this scenario, a detailed, fair and bank-protective agreement governing the bank's holding and release of the funds would be required (BEDA).

B. Parties and Documentation

The parties to the BEDA would be the bank and either (1) the seller and the buyer, or (2) their respective attorneys. In addition to the BEDA, the parties presumably would need to sign a W-9 Form and possibly other routine documents normally required by the bank to open an account for the benefit of the parties, including those required to comply with the Patriot Act.

C. How it Would Work

When the contract of sale is signed, the parties would simultaneously sign the BEDA and other bank-required related documents. The check for the contract deposit would be payable to the bank, as escrow agent, and deposited by the bank into the BEDA account. The bank would advise the parties in writing where the funds are being held, either at the time the BEDA is signed, or shortly thereafter. The deposit would be disbursed at closing in accordance with the parties' joint written instructions to the bank. If the contract is terminated, the bank would pay the deposit to whoever is entitled to it under the contract, as directed by the parties in writing. If there is a dispute as to who is entitled to the deposit, the bank would either continue to hold it until the dispute is resolved by the parties or by legal action, or pay it into court.

D. The Model BEDA Agreement

Attached to this Report is a model BEDA. It reflects the Task Force's view as to standard, appropriate and protective escrow provisions acceptable to most lenders. It is purposely protective of the bank as escrow agent, containing industry standard provisions which confirm that (1) the bank is merely a stakeholder, with no duties or responsibilities other than holding and disbursing the escrowed funds; (2) the bank shall be held harmless from liability except for damages arising from its gross negligence or willful misconduct; and (3) the bank may resign at any time.

E. Voluntary or Mandatory? If Mandatory, How to Implement

A number of questions have been raised about how to implement the BEDA, including (1) changes in banking statutes and regulations; (2) changes in Disciplinary Rules; (3) changes in Ethical Considerations; (4) regulation of the Chief Judge; (5) administrative rule of the Presiding Judge for each Appellate Division or (6) suggested practice adopted by the RPLS, with changes to standard form contracts. Following is a sample contract provision which contemplates the use of the BEDA:

> "Notwithstanding paragraph 6 of the printed form contract of sale, the bank ("Escrowee") named in the bank escrow deposit agreement executed by the parties hereto ("BEDA") shall hold the Downpayment in escrow pursuant to the terms of the BEDA. To the extent of any conflict between the printed form contract and the BEDA, the BEDA shall prevail. Unless otherwise provided in the BEDA, interest on the Downpayment shall be paid as provided in the contract of sale."

The Task Force recommends that the Association present the BEDA as a voluntary rather than mandatory alternative to attorney escrows. The Task Force also recommends that the BEDA apply only to deposits in excess of $25,000. This would avoid the need of a BEDA for small deposits, which would most likely make the BEDA more palatable to banks. It also would make the BEDA inapplicable to most deposits upstate, where attorneys are less involved in initial contract drafting, and deposits are customarily so small that they are held by the real estate broker.

F. The Biggest Problem: Funding at Closing

The use of banks as escrow agents raises practical considerations such as fees, personnel to appear at closings, defining the bank's role, preparing escrow agreements acceptable to the banks, and procedures to release funds, especially if multiple checks are required. The model BEDA attempts to address these issues but may not solve all of them. In addition, opportunities for fraud would still exist. Finally, speed and efficiency are legitimate concerns. The potential benefit of utilizing banks as escrow agents will be undermined if closings are delayed for hours, or worse, adjourned, while the parties wait for the delivery of checks required for closing because certain seller expenses are not determined until the closing itself.

G. Are Banks Interested? Discussions with JP Morgan Chase

A representative of JP Morgan Chase's national escrow department advised RPLS Chair Joshua Stein that Chase would, in principle, have great interest in serving as a BEDA escrowee. The Chase representative did not seem to regard the task as particularly difficult, burdensome, complicated or controversial. Chase would be willing to use a NYSBA-approved form of BEDA, provided that Chase could sign off on the final document. Chase had no problem with our draft BEDA. If Chase were to participate in BEDA, this would of course require some internal review and implementation measures—which we did not ask Chase to pursue at this time. Chase potentially has online capacities sufficient to move the entire escrow account opening, administration, disbursing and closing process onto the Web, and expressed interest in doing

so, but no commitment. One major problem in moving the process online would be the need to figure out how Chase could comply with the "know your customer" regulations of the USA Patriot Act, but this seemed manageable. We discussed with Chase various possible mechanisms to disburse closing checks in a timely way, and we think that this will require further discussion. Chase has no problem working with IOLA. BEDA residential deposit transactions would be handled directly (via e-mail, mail and perhaps a website) with Chase national escrow, based in New York. Branches would not be involved. We were encouraged by Chase's interest. We fully expect that Chase will participate in any BEDA program should it be adopted. In any case, Chase seems to offer a good alternative to attorneys who would prefer not to act as escrow holders in residential transactions.

H. Possible Concerns about Other Banks' Willingness to Cooperate

Members of the Task Force have spoken with a number of banking institutions about the BEDA. As described above, so far Chase appears receptive. Other banks have expressed interest as well. The Task Force firmly believes that the BEDA should be presented as a viable alternative to attorney escrows only if multiple banks statewide are willing to act in this capacity. The Task Force has contacted the New York Bankers Association to gauge the breadth of institutional interest. We await response.

IV. The Current System Works Well and Should Not Be Replaced

A. Attorney Escrow of Contract Deposits Works Well

In the overwhelming majority of cases, the current practice of attorney escrow of contract deposits works well. Attorney escrow facilitates making payments at the closing. Seller expenses typically include brokerage commissions, transfer taxes, miscellaneous fees related to the satisfaction of an outstanding loan and, in the case of a cooperative apartment, "flip taxes" and other charges payable to the cooperative corporation or its agents. The recipients of these payments usually prefer bank or certified checks but will often accept uncertified attorney escrow account checks instead. Disbursements by seller's counsel from the escrowed contract deposit saves the need for the buyer to produce multiple certified or bank checks at closing. This is particularly helpful because the bank funding the buyer's loan often does not advise the buyer until less than 24 hours before closing (sometimes not until the closing itself) the amount of the buyer's loan being net funded (after the buyer's loan charges are deducted from the gross loan amount). In addition, banks often do not wire funds to the account of the attorney closing the loan until the morning of the closing. As a result, the closing often is delayed while the parties first wait to confirm that the funds have been received, and then wait for the bank's counsel to obtain certified or bank checks to disburse those funds. The fewer the number of checks requested from the buyer at closing, the less likely the closing will be delayed.

In addition, some payments required from the seller cannot be determined before closing. These include interest and penalties on unpaid real estate taxes or water and sewer charges disclosed in a continuation search run by the title company from the closing, as well as other matters that might be disclosed on such a continuation search (previously undisclosed judgments and liens, for example). If more than a minimal amount is owed, title companies typically will not accept a personal check from the seller. If the seller's attorney can pay these charges from the escrowed contract deposit, the closing proceeds more efficiently. Efficiency is crucial and use of attorneys as escrow agents maximizes efficiency.

Attorney escrows are also less costly. Lawyers who act as escrow agents do not charge their clients extra for providing escrow accounts. It is expected, though not certain, that banks will charge a fee, albeit a modest one, for their services.

The first printed form downstate to provide for the seller's attorney to hold the downpayment in escrow was a Rider to House Contract of Sale (Blumberg Form 316, rider to NYBTU 8041, Blumberg Form 125) drafted by a subcommittee of the Association of the Bar of the City of New York that Karl Holtzschue chaired in 1980.[1] The NYBTU standard form contract of sale (Form 8041) then in use did not provide for escrow of the down payment. It became common for contract riders prepared by seller's counsel downstate to include attorney escrow provisions. The standard downstate multibar residential contract of sale thereafter "institutionalized" and expanded these provisions to further delineate the responsibilities and liability of the escrow agent.

In a recent case, the judge held that the risk of a misappropriation of a down payment by the seller's attorney fell on the seller, ordered the parties to close, and directed the seller to apply to the Lawyers Fund for Client Protection ("the Fund") for reimbursement. *Chen Li v. Akhtar*, 800 N.Y.S.2d 344 (Supreme Court Queens County 2005). The current system works.

B. There are Very Few Instances of Attorney Escrow Theft and the Losses are Paid by the Lawyers Fund for Client Protection

The instances of attorney escrow theft are miniscule. The Lawyers Fund reports that since 1982 client losses of all types reimbursed by the Fund are attributable to substantially less than one-third of one percent of New York's 215,000 registered lawyers. In 2005, 729 claims were made, and 227 awards totaling $8.1 million were granted, 51% of which were real estate-related, and most of which arose from the Second Department. Only 56 lawyers (32 for the first time) were responsible for all the claims.

Unfortunately, they receive a great deal of attention in the press and disproportionately undermine public confidence in the legal profession.

Most importantly, the few thefts that do occur are fully reimbursed by the Lawyers' Fund. The Lawyers' Fund is itself funded solely by lawyers as part of their biennial registration fees.

V. Possible Changes to the Current System (In Lieu of BEDA)

A. Our Specific Suggestions for Change

The current system of attorney escrows could be strengthened by the following protections: (1) requiring dual signatures on escrow accounts by both attorneys; (2) asking banks to send monthly statements of the escrow account to both attorneys and both clients; and (3) amending the DRs and AD Rules to allow inclusion in suspension from practice orders an order of restraint on the suspended attorney's escrow accounts (as proposed by the New York County Lawyers' Association). We also considered recommending mandatory bonding, but determined that it is too cost prohibitive and unlikely to be implemented, for the reasons discussed below.

B. The Benefit of These Changes

1. *Requiring Dual Signatures*: This might reduce the vast majority, if not necessarily all, attorney escrow misappropriation in real estate transactions. In the case of sole practitioners, the second signatory could be the attorney for another party involved in the transaction, or the client for whom the funds are being held in escrow. The mere requirement for dual signatures could sufficiently chill inappropriate conduct.

This safeguard would require the cooperation of lenders to prohibit withdrawals without joint signatures. Banks should be willing to do so, because they routinely require multi-party signatures to disburse monies from trust accounts with more than one trustee, or estate accounts with more than one executor.

2. *Bank Delivery of Escrow Account Statements to All Interested Parties*: If banks were asked to deliver copies of monthly bank statements to the parties for whose benefit an attorney escrow account is being maintained, it might also have a chilling effect on unauthorized withdrawals from attorney escrow accounts. Banks and other commercial institutions (brokerage firms, mutual funds) currently have the ability to send duplicate statements to parties upon request. This safeguard should not impose an undue burden.

3. *Changes to the DRs and ADRs Regarding Escrows*: The New York County Lawyers' Association issued a press release on March 15, 2006 announcing the submission to Hon. Judith S. Kaye, Chief Judge of the Court of Appeals, of a series of proposed changes to the Disciplinary Rules and Appellate Department Rules to safeguard clients' funds in trust, escrow, special or IOLA accounts in cases where attorneys were disbarred, suspended or ceased to practice law by reason or resignation, retirement or abandonment of practice. At the end of 2005, nearly half of the attorneys against whom claims were filed were repeat offenders. If suspension of these accounts could eliminate repeat offenders, the claims would be cut in half. These proposed changes would take funds out of the control of disciplined attorneys.

4. *Bonding*: We considered recommending that attorneys be either encouraged or required to obtain surety bonds to secure their safe return of client funds, but concluded that it raises more issues than it solves. It would be inconvenient and viewed by some attorneys as overly intrusive and expensive to complete a bond application and pay for a bond each time an escrow account is opened, regardless of the amount of the escrow and the length of time that the escrow is to be maintained. Some attorneys might pass the cost to their clients. If bonding were required only for certain escrows—those in excess of a certain dollar amount, or those expected to generate interest above a certain amount—perhaps those issues would be less problematic. However, mandatory bonding would need to be implemented in a way that did not slow down the process of creating the escrow account (an issue in real estate transactions, where parties rush to sign contracts so as to bind the other parties as soon as possible), and the location and security of the funds until the escrow is "bonded" would have to be addressed. In addition, bonding companies with a poor track record for timely paying claims would need to be excluded, where possible, from the system. We also would want to explore how this might affect victims' recovery from the Lawyers Fund. Would victims be required to seek reimbursement from the bonding company first, then from the Lawyers Fund for any deficiency, or the other way around? Alternatively, would the Lawyers Fund be the recipient of bond proceeds, and the intermediary for the payment of claims? Would victims be precluded from seeking recovery from the Lawyers Fund even if a bond covers only part of a victim's loss?

C. Counter-Point: Nassau County Bar Association Task Force Report

A Report of the Escrow Task Force of the Nassau County Bar Association, dated October 11, 2005, considered the 2004 Annual Report of the Lawyers' Fund, particularly with regard to its comments that Long Island attorneys are responsible for a disproportionately high number of thefts of real estate escrow funds, and responded to proposals to address the issue. This Task Force concluded that no new regulatory measures are needed. They rejected dual signature arrangements and joint escrows, finding them largely unworkable for sole practitioners. They rejected a shift to title company escrows, noting that the title industry has experienced its own defalcations. They recommended that the Lawyers' Fund study and

report on the causes of lawyer misappropriations so that educational programs could be fashioned.

VI. Other Alternatives Are Not Viable

The Task Force also considered title insurance companies and real estate brokers as possible escrow agents. These alternatives were rejected for the reasons discussed below.

A. New York Title Companies are Apparently Unwilling to Hold Escrows

Though title companies already do hold some funds in escrow and are regulated by the Insurance Department, they are not equipped to handle so many small accounts. To cover the administrative cost of processing these accounts, they would have to charge substantial fees. They are not now involved in some transactions, such as co-op sales. There would be concern about title agent or abstract company defalcation and the liability of title underwriters for such theft. While title underwriters are licensed by the Insurance Department, title agents are not. Title underwriters' responsibility for claims settlement is limited to matters covered by the terms of the policy. Use of title agents instead of attorneys raises many of the same problems, but without the Lawyers Fund to pay claims.

Currently most underwriters impose a fee to establish an escrow account and a monthly charge to maintain the account, as well as a per-check charge and fees for wiring funds. Title underwriters are not in a position to issue and deliver numerous closing checks on short notice on a routine basis. If the title companies moved the closing in house, an unintended consequence might be to increase the pressure to transform New York from a table settlement state to a California-style escrow closing state. That would substantially reduce the role and ability of attorneys to serve their clients in residential real estate transactions.

B. Switching to Broker Escrows Downstate is Inadvisable

Upstate, brokers fill in Bar Association contracts, subject to approval of the attorneys, and hold the down payment in escrow. Sale prices upstate generally are much less than downstate, and the down payments are usually a fairly nominal amount—much less than the 10% that is customary downstate. Partly due to the smaller amounts, there are not many reported cases of brokers stealing the escrow deposits. Extending the practice of broker escrows downstate, where the deposits are typically substantially higher than they are upstate, would not reduce the risk of theft, and would eliminate the protection of the Lawyers Fund and the ethical rules by which attorneys are bound.

VII. Conclusion

Our Task Force does not believe there is anything fundamentally wrong with attorneys acting as escrow agents, a time-honored and efficient process that works extremely well. To the extent that problems exist, they can be mitigated by requiring dual signatures and requesting that escrow account statements be distributed to all interested parties, as well as freezing the escrow accounts held by attorneys who are disbarred, suspended or otherwise no longer practicing law.

We were asked to assume, however, that the escrow system needs to be replaced. That assumption led to a critical study of alternatives. As described above, we rejected most of them. However, the concept of banks acting as escrow agents has strong appeal to our Task Force. The BEDA, though not perfect, may ultimately present parties to real estate transactions, their counsel, and the public-at-large with a viable, workable and abuse-free way of escrowing contract deposits. The model BEDA is simple, short, fair and bank-protective. We believe that banks may become interested in acting as escrow agents on a widespread basis in New York, and we wish to explore further the extent of such interest. We believe that if the BEDA is introduced and implemented on a voluntary basis initially, it may obtain, over time, general acceptance. It may become the industry standard, or at least a widely used alternative, especially in residential transactions downstate.

Endnote

1. See "Holtzschue on Real Estate Contracts" at page 2-9, note 19; Holtzschue, "City Bar Panel Drafts Rider For Contracts in Home Sales," N.Y.L.J., Dec. 10, 1980.

Ira Goldenberg, Task Force Chair

Task Force Members: Marvin Bagwell, James Blose, John Blyth, Anne Reynolds Copps, Richard Fries, Eric Garcia, Karl Holtzschue, Melvyn Mitzner, Lucien Morin II, Mindy H. Stern, Samuel Tilton, Joseph Walsh and Howard Wieder.

Report drafted by Karl B. Holtzschue and Mindy H. Stern, with contributions from Marvin Bagwell, John Blose, Richard Fries, Melvyn Mitzner and Joshua Stein.

Report Date: July 7, 2006

Report approved by the Executive Committee of the Real Property Section of the New York State Bar Association: July 13, 2006

MODEL BANK ESCROW DEPOSIT AGREEMENT[1]

New York State Bar Association Real Property Law Section
Attorneys' Escrow Task Force

Form dated: July 7, 2006

Accompanying report of the Attorney Escrow Task Force, adopted by the Executive Committee of the Real Property Section of the New York State Bar Association on July 13, 2006.

In 2005-06, the New York State Bar Association ("NYSBA") asked its Real Property Law Section to suggest a possible alternative to having attorneys hold contract deposits ("downpayments") in escrow for residential contracts of sale. In response, a Section Task Force recommended having banks hold downpayments above $25,000 in escrow for the parties, using a streamlined bank escrow deposit agreement (a "BEDA").

The following model demonstrates how a BEDA might look. The parties and any bank ("Bank") can of course use any escrow agreement they want, or negotiate any other arrangements they want for downpayments. We anticipate and hope, however, that they will often want to use this model BEDA, because it reflects all the following:

- *Extensive Review.* This BEDA has been reviewed by all members of the Task Force, by other practicing attorneys, and by bank counsel. It reflects a wide range of comments.
- *Simplicity.* This BEDA is simple, straightforward, and self-contained, with no need for additional documents, certificates, notifications, or other deliverables. (As the one exception to the previous sentence, Bank will need to obtain a W-9 form from whichever party will report the interest earnings as income.)
- *Bank-Protective.* The Task Force recognizes that any escrow agreement will in large part protect the escrowee, in this case the bank, from liability. For example, if the buyer and seller have a dispute about the escrow, the escrowee does not want to be called upon to resolve it or face liability for failure to comply with one party's or another party's claims or instructions. This BEDA protects the bank escrowee in a manner that falls within the usual range of industry-standard escrow agreements.
- *Plain English.* In preparing this BEDA, the Task Force worked from a number of existing agreements, then "translated" the result from "legalese" into ordinary business English. By doing so, the Task Force sought to make this model document accessible to nonlawyers, while also demonstrating more generally the benefits and practicality of "Plain English" drafting.[2]

This model BEDA assumes a typical residential real estate transaction, with a substantial downpayment that would (at least downstate) traditionally have been held by an attorney. To the extent a transaction varies from that norm, this BEDA may require customization. The parties may also want to customize the BEDA as follows and take into account these points:

- *Account Type.* The BEDA requires use of a federally insured deposit account of Bank, allowing withdrawals on any banking day. The parties may wish to fine-tune the requirements for the account.
- *Lawyers or Clients?* Instead of having the buyer and seller act as parties to the BEDA, the lawyers could become the parties, if Bank will proceed on that basis. We believe many banks will do so.
- *Account Identification.* This model BEDA contemplates Bank will notify the other parties of the escrow account number and branch. Ideally, Bank might skip that step by identifying that data before signing the BEDA, and then filling it in below Bank's signature.
- *IOLA.* Under traditional practice, if a lawyer holds funds and anticipates interest earnings will not exceed $150, then instead of releasing them to any party to the transaction, the lawyer can allow them to go to a program to fund legal services to the poor (a so-called "interest on lawyers' accounts" or "IOLA" program)—a major source of revenue for legal services in New York. This model BEDA seeks to continue existing IOLA practice. The wisdom or appropriateness of IOLA in general (as opposed to funding legal services from general tax revenues) represents a policy decision beyond the scope of the Task Force. The use of IOLA also represents a business decision for the parties to the transaction.

Any attorney may download this model BEDA directly from the following Web address: www.nysba.org/BEDA. No registration, password, or other information of any kind, or NYSBA membership, is required.

NYSBA consents to any attorney's use of this model BEDA. NYSBA also consents to any attorney's or bar association's republication and reprinting of this BEDA (in print, online, or otherwise), provided only that it includes: (a) these cover notes in their entirety; (b) NYSBA's copyright notice; and (c) the entire model BEDA without change or editing. NYSBA does not consent to reproduction, reprinting, or use of this model BEDA by nonattorneys, and recommends the use of attorneys in any real estate transaction, whether residential or commercial.

Escrow Date: _____

Estimated Closing Date: _____

BANK ESCROW DEPOSIT AGREEMENT

This **BANK ESCROW DEPOSIT AGREEMENT** (the "Escrow Agreement") is entered into on the Escrow Date above, among Buyer and Seller (together, the "Transaction Parties") and Bank, all as defined in the signature blocks below.

The Transaction Parties have entered into a contract (the "Purchase and Sale Contract") dated as of _____, 20___ and identified as: _____.

The Purchase and Sale Contract relates to this real estate or cooperative apartment: _____ (the "Premises").

By signing below, Bank acknowledges that on the Escrow Date Bank received $_____ from Buyer, by check payable to Bank as escrow agent, or in such other form as Bank has approved (the "Initial Funds").

As compensation for its services under this Escrow Agreement, Bank shall receive this payment, due and payable on the Escrow Date: $_____ (the "Escrow Fee"). (A blank for Escrow Fee means $0.)

At Closing, the Transaction Parties shall complete and sign a Closing Confirmation in the form attached or in any other form upon which all parties agree, consistent with the Purchase and Sale Contract (a "Closing Confirmation"), and give it to Bank. Bank shall disburse the Escrow Funds in compliance with the Closing Confirmation and this Escrow Agreement.

The parties further agree as follows:

1. Appointment; Holding of Deposit.

The Transaction Parties appoint Bank as their escrow agent for the Purchase and Sale Contract. Bank accepts that appointment, subject to this Escrow Agreement. Bank shall hold the Initial Funds in escrow and not release them except in accordance with this Escrow Agreement.

2. Escrow Account; Escrow Funds.

Bank shall promptly deposit the Initial Funds in a federally insured deposit account of Bank (the "Escrow Account"). The Escrow Account shall permit withdrawals on any banking day and bear interest at Bank's highest available rate for accounts of this type and size. Any interest on the Escrow Funds shall be added to the Escrow Account, except as this Escrow Agreement otherwise expressly provides. Bank shall promptly notify the Transaction Parties or their counsel of the account number and branch of the Escrow Account. The "Escrow Funds" means the Initial Funds plus any interest earnings deposited into the Escrow Account. Notwithstanding anything to the contrary in this Escrow Agreement, Bank shall never be obligated to disburse any Escrow Funds unless Bank has determined that they have cleared and constitute good funds.

Notwithstanding anything to the contrary in this Escrow Agreement, when Bank establishes the Escrow Account, Bank shall estimate the Escrow Account interest earnings, assuming the same interest rate in effect on the Escrow Date and a Closing on the Estimated Closing Date. (The Estimated Closing Date does not bind the Transaction Parties.) Bank does not guarantee any such estimate. Bank shall have no liability for any error. If Bank estimates the Escrow Account will earn interest below $150, then instead of paying interest into the Escrow Account, Bank shall: (a) pay it to [IOLA] ("IOLA") at this wire transfer address: _____ _____; and (b) not report it as any Transaction Party's income.

3. Initial Deposit Defects.

If for any reason Bank cannot process the Initial Deposit (e.g., because it is incorrectly made out), then Bank shall promptly notify the Transaction Parties and their counsel; hold all checks and other documentation; and do nothing pending instructions. If any check evidencing the Initial Deposit is returned for insufficient funds, Bank shall promptly redeposit it and notify the Transaction Parties.

4. Disposition of Escrow.

A. **If Closing**. The Transaction Parties' counsel shall give Bank reasonable prior notice by telephone or email of the Closing. To facilitate Closing, Bank shall countersign any Closing Confirmation; deliver it by hand or by fax to Closing; and diligently endeavor to disburse funds from the Escrow Account at Closing. By signing a Closing Confirmation, Bank

agrees (and acknowledges that it is unconditionally obligated) to disburse the Escrow Funds in accordance with the Closing Confirmation. If a Closing Confirmation requests disbursements beyond the Escrow Funds, Bank shall not countersign the Closing Confirmation and shall notify the Transaction Parties. Bank shall otherwise have no responsibility for, and no obligation to verify, any Closing Confirmation.

B. **If No Closing**. If the Purchase and Sale Contract terminates, the Transaction Parties agree that no Closing shall occur, or a dispute arises between the Transaction Parties, then Bank shall not disburse the Escrow Funds except in accordance with a court's final and unappealable order (a "Final Order") or the Transaction Parties' joint written instructions ("Joint Instructions"). The Transaction Parties shall issue Joint Instructions when and as the Purchase and Sale Contract contemplates release of the Escrow Funds. If Bank receives conflicting claims or is unsure of its obligations, Bank need not act. With or without depositing the Escrow Funds in court, Bank may commence an interpleader action. In no event shall this Escrow Agreement ever obligate Bank to disburse more than the Escrow Funds.

5. Compensation.

Each Transaction Party shall: (a) pay half of any Escrow Fee; and (b) reimburse Bank for all reasonable expenses, including reasonable legal fees, Bank incurs in acting under this Escrow Agreement, including in any Dispute or interpleader action. Bank may reimburse itself for such expenses and the Escrow Fee from the Escrow Funds, without prejudice to the Transaction Parties' rights between themselves.

6. Limited Responsibility.

Bank acts only as a stakeholder. Bank need not act under this Escrow Agreement or otherwise, except to receive, hold, and release any Escrow Funds as this Escrow Agreement or a Final Order requires. Bank shall have no obligations, liabilities, responsibilities, or duties under this Escrow Agreement except those expressly stated in this Escrow Agreement, which the parties acknowledge are ministerial in nature.

7. Excluded Duties.

Bank shall have no duty or obligation to: (a) enforce collection of any check, draft, or other payment instrument; (b) determine, perfect, identify, ascertain, or file any financing statement for any security interest in any Escrow Funds; (c) know, interpret, apply, be bound by, have any responsibility for, or enforce the Purchase and Sale Contract; (d) invest any Escrow Funds except in a Bank account as this Escrow Agreement requires; (e) give the Escrow Funds any more care than Bank would give its own similar property; (f) confirm anyone's identity, authority, or rights in executing or performing under this Escrow Agreement or the Purchase and Sale Agreement; (g) preserve rights against anyone regarding any Escrow Funds, whether or not Bank has or is deemed to have knowledge or notice of such matters; (h) take any action that Bank believes may expose it to cost or liability; or (i) institute or defend any legal proceedings unless fully indemnified to its satisfaction. Bank has no responsibility for anyone else's (except its own affiliates') acts or omissions. Bank has no interest in any Escrow Funds. Bank merely acts as escrowee, holding the Escrow Funds for that limited purpose.

8. No Confirmation.

Bank need not determine the validity or sufficiency, in form or in substance, of the Escrow Funds. Bank need not determine the validity, sufficiency, genuineness, or accuracy of any instrument, document, certificate, statement, or notice related to this Escrow Agreement, including any disbursement request or default notice (an "Escrow Notice"). It shall be sufficient if any Escrow Notice purports on its face to be correct in form and executed by the party(ies) required to execute it under this Escrow Agreement. If Bank believes an Escrow Notice is genuine, Bank may rely (and shall be protected in acting or refraining from acting) upon it, not only as to its due execution, validity, and effectiveness, but also as to its truth and accuracy.

9. No Liability.

Bank shall not be liable for its actions (or any error of judgment, mistake of law or fact, error, or omission) in connection with this Escrow Agreement, including any release of Escrow Funds, except actions that result from Bank's own willful misconduct, gross negligence, or actual breach ("Wrongful Acts"). Bank shall incur no liability for nonperformance resulting from any occurrence beyond Bank's reasonable control, including any provision of any law or regulation or any act of any governmental authority, any act of God or war, or terrorism. Bank shall not be charged with knowledge or notice of any fact or circumstance not expressly stated in this Escrow Agreement. In no event shall Bank be liable for incidental, indirect, special, consequential, or punitive damages. If Bank disburses the Escrow Funds in accordance with this Escrow Agreement, then Bank shall be released and discharged of any further responsibility or obligation under this Escrow Agreement.

10. Attachments.

If any court or other authority attaches, garnishes, levies upon, or stays or enjoins disbursement of, any Escrow Funds, or enters any other order, writ, judgment, or decree on the Escrow Funds (any of the foregoing, an "Attachment"), Bank may, in its sole and absolute discretion and notwithstanding anything in this Escrow Agreement to the contrary, obey and comply with such Attachment. If Bank complies with any Attachment, Bank shall have no liability for doing so, even if the Attachment is later appealed, reversed, modified, annulled, set aside, or vacated.

11. Bank's Advisers.

Bank may employ agents, attorneys, and accountants in acting under this Escrow Agreement. Bank shall not be liable for any action taken, suffered, or omitted in good faith upon the advice of counsel, accountants, or other skilled persons. Bank may act through its directors, officers, subsidiaries, affiliates, representatives, agents, attorneys, employees, successors, and assigns (collectively, "Related Parties").

12. Indemnity.

The Transaction Parties shall indemnify and hold harmless Bank and its Related Parties from and against any and all actions, claims, costs, expenses, demands, judgments, losses, damages and liabilities (including reasonable attorneys' fees and expenses) of any nature or kind whatsoever, whether direct, indirect or consequential arising out of or in connection with the Escrow Funds or this Escrow Agreement, except to the extent arising from Bank's Wrongful Acts. Bank may, in its sole and absolute discretion, employ separate counsel in any such action and to participate in its defense.

13. Resignation.

Bank may in its sole and absolute discretion at any time resign for any reason (or for no reason) by notifying the Transaction Parties. Bank shall not be discharged from its duties under this Escrow Agreement until: (a) the Transaction Parties designate a successor escrowee; (b) such successor executes and delivers an escrow agreement in substantially the form of this one; and (c) Bank delivers all Escrow Funds to such successor. If, 30 days after Bank resigns, no successor escrow agent has been appointed, then Bank may petition any court of competent jurisdiction for such an appointment or other appropriate relief. Any such resulting appointment shall bind all parties. In no event, however, shall Bank's obligations under this Escrow Agreement continue more than 90 days after it resigns.

14. Notices.

Except as this Escrow Agreement expressly provides, all requests, demands, notices and other communications required or otherwise given under this Escrow Agreement (each, a "Notice") must be given in writing, and only in a manner this paragraph allows. Notices shall be delivered in each case to the recipient at the address stated in this Escrow Agreement, or at such other address as such party shall have furnished in writing, in accordance with this paragraph, to the other parties. If delivered by hand, a Notice shall be effective when received as evidenced by a written receipt. If forwarded by nationally recognized overnight courier requiring acknowledgment of receipt, a Notice shall be effective on the business day after dispatch. If mailed by registered or certified mail, return receipt requested, a Notice shall be effective three business days after mailing.

15. Successors and Assigns.

This Escrow Agreement shall bind and benefit the parties and their heirs, successors, and assigns. To the extent this Escrow Agreement limits Bank's liability or obligations, such limitations shall bind the Transaction Parties and their Related Parties. Nothing in this Escrow Agreement gives any nonparty any right, remedy, or claim under, in, or for this Escrow Agreement or any Escrow Funds.

16. Governing Law.

New York law shall govern this Escrow Agreement. The parties consent to jurisdiction of: (a) the Supreme Court of the State of New York in the county where the Premises are located; and (b) the federal court for the district that includes such county. Any dispute or proceeding relating to, arising from, under, or in connection with this Escrow Agreement, or arising out of the relationship among any parties or the Escrow Funds (any of the foregoing, a "Dispute") shall, to the extent law allows, be held in such county.

17. WAIVER OF JURY TRIAL.

TO THE FULLEST EXTENT LAW ALLOWS, EACH PARTY KNOWINGLY, VOLUNTARILY, INTENTIONALLY, UNCONDITIONALLY AND IRREVOCABLY WAIVES ANY RIGHT TO A TRIAL BY JURY IN RESPECT OF ANY DISPUTE. THIS PROVISION IS A MATERIAL INDUCEMENT FOR BANK TO ENTER INTO THIS ESCROW AGREEMENT.

18. Miscellaneous.

Bank represents and warrants it has the power and legal authority to enter into and perform this Escrow Agreement. This Escrow Agreement contains the parties' entire agreement. It supersedes all agreements, representations, warranties, statements, promises and understandings, whether oral or written, about the subject matter of this Escrow Agreement. This Escrow Agreement may be amended, modified and supplemented, and any provision of this Escrow Agreement may be waived, only by a writing signed by the party to be charged. If a Transaction Party validly assigns the Purchase and Sale Contract, such Transaction Party shall also assign this Escrow Agreement to the same assignee, and require the assignee to assume this Escrow Agreement. No Transaction Party may otherwise assign this Escrow Agreement without the express written consent of the other parties. In accordance with ordinary principles of contract law, any assignment shall not release the assignor. If anything in this Escrow Agreement is invalid, illegal, or unenforceable, that shall not affect the remainder. This Escrow Agreement shall be construed as if it never contained the invalid, illegal, or unenforceable provision. This Escrow Agreement may be executed in any number of counterparts. Taken together, all constitute a single instrument.

19. Interpretation.

Wherever this Escrow Agreement refers to the Purchase and Sale Contract, that also includes any future changes to the Purchase and Sale Contract. No such change shall affect Bank unless Bank has agreed to it. This Escrow Agreement shall govern where inconsistent with the Purchase and Sale Contract. The word "include" and its variants shall be interpreted as if followed by the words "without limitation."

20. Additional Terms and Conditions.

The parties agree to these additional terms and conditions:

[NONE]

[No Further Text on This Page.]

IN WITNESS WHEREOF, the parties have executed this Escrow Agreement as of the Escrow Date.

Each Transaction Party certifies under penalty of perjury that: (a) its taxpayer I.D. number (social security or employer identification number) specified below is accurate; and (b) it has not been notified that it is subject to back-up withholding.

PARTY	**BUYER**	**SELLER**	**BANK**
Signature	X _____	X _____	X _____
Name	_____	_____	_____
Title	_____	_____	_____
Taxpayer I.D.	_____	_____	_____
Address	_____	_____	_____
	_____	_____	_____
Email Address	_____	_____	_____
Phone	_____	_____	_____
Counsel Name	_____	_____	_____
Counsel Address	_____	_____	_____
	_____	_____	_____
Counsel Email	_____	_____	_____
Counsel Phone	_____	_____	_____

Attached:

Sample Closing Confirmation and Receipt

SAMPLE CLOSING CONFIRMATION AND RECEIPT

(TO BE SIGNED ONLY AT CLOSING)

This Closing Confirmation refers to Bank Escrow Deposit Agreement dated as of _____, 20___ (the "Escrow Agreement") among Buyer, Seller, and Bank as identified below. Definitions in the Escrow Agreement apply here.

Buyer confirms: (a) the Closing has occurred (or is now occurring); and (b) Bank should release the Escrow Funds as Seller directs. Seller directs Bank to release the Escrow Funds by issuing these checks and wire transfers:

RECIPIENT	AMOUNT	BY CHECK	BY WIRE TO THIS BANK ACCOUNT
_____	$ _____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____

When Bank has released the Escrow Funds as described above, Bank shall have no further liability for the Escrow Funds or under the Escrow Agreement and shall be released and discharged of any obligations to the Transaction Parties. To the extent not fully performed, the Escrow Agreement shall survive this Closing Confirmation.

PARTY	BUYER	SELLER
Name	_____	_____
Signature	_____	_____
Date	_____, 20___	_____, 20___

RECEIPT

Bank acknowledges receipt of the above Closing Confirmation. To the extent of the Escrow Funds, Bank unconditionally and irrevocably agrees to comply with the above Closing Confirmation and disburse the Escrow Funds as requested above.

BANK: _____

By: _____

Its: _____

Dated: _____, 20___

Endnotes

1. Copyright (C) 2006 New York State Bar Association. See cover notes for certain consents to use, reprint, and republish this model document.
2. See, e.g., the following articles by Joshua Stein, former chair of the Real Property Law Section: "Short and Simple," *The American Lawyer*, October 2002, at 59; "How to Use Defined Terms to Make Transactional Documents Work Better," *The Practical Lawyer*, October 1997, at 15; "Writing Clearly and Effectively: How to Keep the Reader's Attention," *New York State Bar Association Journal*, July/August 1999, at 44; "Template for a Template: a Checklist To Prepare or Improve Any Model Document," *The Practical Lawyer*, April 2000, at 15; "Cures for the (Sometimes) Needless Complexity of Real Estate Documents," *Real Estate Review*, Fall 1995, at 63.

Extension of Reduced Real Estate Transfer Tax Rate for Real Estate Investment Trusts

The Office of Tax Policy Analysis Technical Services Division of the New York State Department of Taxation and Finance has issued an extension of the reduced real estate transfer tax rate for real estate investment trusts. The following is the text of their release: Ed

Section 1402(b)(2)(B) of the Tax Law has been amended to extend the reduced real estate transfer tax (transfer tax) rate for conveyances of real property to existing real estate investment trusts (REIT). This reduced tax rate applies to all such conveyances occurring before September 1, 2008.

Conveyances to a REIT are subject to the New York State transfer tax but may be taxed at a reduced rate. This reduced tax rate for the transfer tax may also apply to conveyances to a partnership or corporation in which a REIT will own a controlling interest immediately following the conveyance. To qualify for the reduced tax rate, however, certain conditions must be met. (Tax Law § 1402(b).)

The statutory provisions providing a reduced tax rate of $1.00 for each $500 of consideration or fractional part thereof apply to conveyances of real property to a REIT (other than those conveyances made in connection with the initial formation of the REIT) expired on September 1, 2005. However, under the amendments, these provisions are deemed to have been in full force and effect on and after September 1, 2005, and now apply to such conveyances occurring before September 1, 2008.

Refund for Real Estate Transfer Tax Paid on Conveyances to an Existing REIT

If you paid real estate transfer tax at the rate of $2.00 for each $500 of consideration or fractional part thereof with respect to a qualified conveyance to an existing REIT or to a partnership or corporation in which a REIT owned a controlling interest occurring on or after September 1, 2005, you may claim a refund within two years from the date of payment. Use Form TP-592.2, *Claim for Real Estate Transfer Tax Refund,* to claim a refund. The refund is the difference between the tax paid and the tax computed at the reduced rate.

For more information on the preferential tax treatment given to conveyances to a REIT, refer to:

- TSB-M-94(4)-R, *1994 Amendments to the Real Property Transfer Gains Tax and the Real Estate Transfer Tax*
- TSB-M-94(4.1)-R, *1996 Amendments to the Real Estate Transfer Tax Related to Real Estate Investment Trusts*
- TSB-M-96(5)R, *1996 Amendments to the Real Estate Transfer Tax Related to Real Estate Investment Trusts*
- TSB-M-96(5.1)R, *Extension of Reduced Real Estate Transfer Tax Rate for Real Estate Investment Trusts*
- TSB-M-02(1)R, *Extension of Reduced Real Estate Transfer Tax Rate for Real Estate Investment Trusts*
- Form TP-584-REIT, *Combined Real Estate Transfer Tax Return and Credit Line Mortgage Certificate for Real Estate Investment Trust Transfer*

To obtain any of these documents, download copies from our Web site at *www.nystax.gov*. They are also available by fax at 1 800 748-FORM (3676), or you can call 1 800 462-8100 to receive a copy by mail.

TP-584-REIT (4/06)

New York State Department of Taxation and Finance

Combined Real Estate Transfer Tax Return and Credit Line Mortgage Certificate for Real Estate Investment Trust Transfers

Recording Office Time Stamp

Before completing this form, see *General Information* on back.

Schedule A — Information relating to conveyance

Grantor ☐Individual ☐Corporation ☐Partnership ☐Other	Name *(if individual; last, first, middle initial)*	Social security number
	Mailing address	Federal employer identification number
Grantee ☐Individual ☐Corporation ☐Partnership ☐Other	Name *(if individual; last, first, middle initial)*	Social security number
	Mailing address	Federal employer identification number

Tax map designation			Address	City/village	Town	County
Section	Block	Lot				

Type of property conveyed *(check applicable box)*

1 ☐ Vacant land
2 ☐ Commercial/industrial
3 ☐ Apartment building
4 ☐ Office building
5 ☐ Other _____

Date of conveyance _____ (month) _____ (day) _____ (year)

Condition of conveyance *(check all that apply)*

a. ☐ Conveyance of fee interest
b. ☐ Acquisition of a controlling interest (state percentage acquired _____%)
c. ☐ Transfer of a controlling interest (state percentage transferred _____ %
d. ☐ Conveyance which consists of a mere change of identity or form of ownership or organization *(attach Form TP-584.1, Schedule F)*
e. ☐ Other *(describe)* _____

Schedule B — Real estate transfer tax return (Article 31 of the Tax Law)

Part I – Computation of tax due

1	Enter amount of consideration for the conveyance *(if you are claiming a total exemption from tax, enter consideration and proceed to Part II)*	**1**	
2	Continuing lien deduction *(see instructions if property is taken subject to mortgage or lien)*	**2**	
3	Taxable consideration *(subtract line 2 from line 1)*	**3**	
4	Tax due: $1 for each $500, or fractional part thereof, of consideration on line 3	**4**	

Part II – Explanation of exemption claimed in Part I, line 1 (check either box that applies)

a. Conveyance is a mere change of identity or form of ownership or organization where there is no change in beneficial ownership ..... a. ☐
b. Other *(attach explanation)* ..... b. ☐

Schedule C - Credit line mortgage certificate (Article 11 of the Tax Law)

Complete the following only if the interest being transferred is a fee simple interest.

I (we) certify that: *(check the appropriate box)*

1 ☐ The real property being sold or transferred is not subject to an outstanding credit line mortgage.

2 ☐ The real property being sold or transferred is subject to an outstanding credit line mortgage. However, an exemption from the tax is claimed for the following reason:
- ☐ The transfer of real property is to a person or entity where 50% or more of the beneficial interest in such real property after the transfer is held by the transferor.
- ☐ The maximum principal amount secured by the credit line mortgage is $3,000,000 or more and the real property being sold or transferred is **not** principally improved nor will it be improved by a one- to six-family owner-occupied residence or dwelling.
  Please note: for purposes of determining whether the maximum principal amount secured is $3,000,000 or more as described above, the amounts secured by two or more credit line mortgages may be aggregated under certain circumstances. See TSB-M-96(6)R for more information regarding these aggregation requirements.
- ☐ Other (attach detailed explanation).

3 ☐ The real property being transferred is presently subject to an outstanding credit line mortgage. However, no tax is due for the following reason:
- ☐ A certificate of discharge of the credit line mortgage is being offered at the time of recording the deed.
- ☐ A check has been drawn payable for transmission to the credit line mortgagee or his agent for the balance due, and a satisfaction of such mortgage will be recorded as soon as it is available.

4 ☐ The real property being transferred is subject to an outstanding credit line mortgage recorded in _____ (insert liber and page or reel or other identification of the mortgage). The maximum principal amount secured in the mortgage is _____ . No exemption from tax is claimed and the tax of _____ is being paid herewith. *(Make check payable to county clerk where deed will be recorded or, if the recording is to take place in New York City, make check payable to the **NYC Department of Finance.**)*

For recording officer's use	Amount received ►	Date received	Transaction number

General Information

A conveyance of real property to a real estate investment trust (REIT), as defined in section 856 of the Internal Revenue Code, may be subject to the transfer tax at the reduced rate of $1 for each $500 or fractional part of consideration. The conveyance may be to the REIT itself or to an entity, such as a partnership or a corporation, in which a REIT owns a controlling interest immediately following the transfer (REIT transfer).

To qualify for the reduced transfer tax rate, REIT transfers that are *in connection with the initial formation* of the REIT must occur on or after June 9, 1994. In addition, the REIT transfer must also meet certain o*wnership retention requirements* and the *use of proceeds requirement* described below. **See TSB-M-94(4)R for the requirements for determining whether a REIT transfer qualifies as being a transfer that occurs in connection with the initial formation of the REIT.**

In addition, REIT transfers ***other than*** *those in connection with the initial formation* of the REIT qualify for the reduced transfer tax rate if they occur on or after July 13, 1996, but before September 1, 2008. Furthermore, in order to qualify for the reduced transfer tax rate, a REIT transfer must meet the *ownership retention requirements* described below.

Ownership retention requirements

As part of the consideration for the conveyance of real property or interest therein, the grantor(s) must receive ownership interests in the REIT or in an entity controlled or to be controlled by the REIT which have at least a certain minimum value as described herein. The value of those ownership interests received in the REIT or in an entity controlled or to be controlled by the REIT must be equal to at least 40% (50% if the conveyance is ***other than*** *in connection with the initial formation* of a REIT) of the equity value of the real property or interest therein conveyed by the grantor(s) to the grantee. In addition, the ownership interests in the REIT or in an entity controlled or to be controlled by the REIT received by the grantor(s) as part of the consideration for the conveyance must be retained by the grantor(s) (or an owner of the grantor) for a period of at least two years from the date of the REIT transfer, except in the case of the subsequent conveyance of these interests as a result of the death of an individual grantor. **See TSB-M-94(4)R for the method used to calculate the equity value of the property and the value of the ownership interests received.**

Use of proceeds requirement

At least 75% of the net cash proceeds (after deducting underwriting discounts) received by the REIT from its initial offering must be used for the following purposes:

(a) to make payments on loans secured by any interest in the real property owned directly or indirectly by the REIT;

(b) to pay for capital improvements to the real property owned directly or indirectly by the REIT;

(c) to pay costs, fees and expenses (including brokerage fees, commissions and professional fees) incurred in connection with the creation of a leasehold or sublease pertaining to the real property owned directly or indirectly by the REIT;

(d) to make payments to or on behalf of a tenant as an inducement to enter into a lease or sublease, including but not limited to the following:
  (i) a cash bonus paid to a tenant for signing a lease;
  (ii) a payment for the unexpired term of a tenant's previous lease;
  (iii) payment of a tenant's moving costs;
  (iv) payment for a tenant's improvements that do not constitute capital improvements (such as temporary partitions or non-permanent electrical wiring for computer equipment); and
  (v) payment of a tenant's attorneys' fees;

(e) to acquire any interest in real property (including an ownership interest in any entity owning real property) **except** an acquisition that would qualify for the reduced rate of tax provided for a REIT transfer (without regard to this requirement); or

(f) for reserves established for any of the purposes described in items (a), (b), (c) or (d) above.

For purposes of this requirement, the term *real property* includes real property owned directly or indirectly by the REIT, whether located inside or outside New York State. Also, the calculation of the net cash proceeds from the initial offering of the REIT is made without regard to any proceeds resulting from the exercise of any underwriter's over-allotment option in connection with the initial offering of the REIT shares.

Payment of estimated personal income tax by individuals, estates, and trusts

Nonresidents – Nonresident individuals, estates, and trusts taxed under Article 22 of the Tax Law must comply with the provisions of Tax Law section 663, estimating the personal income tax on the gain, if any, from the sale or transfer of certain real property located in New York State. Such nonresident individuals, estates, and trusts are required to either complete Form IT-2663, *Nonresident Real Property Estimated Income Tax Payment Form*, or Form TP-584, Schedule D, *Certification of exemption from the payment of estimated personal income tax*, and file it with Form TP-584-REIT.

Residents – The requirement for payment of estimated personal income tax under Tax Law section 663 does not apply to individuals, estates, and trusts who are **residents** of New York State at the time of the sale or transfer. Resident individuals, estates, and trusts must complete Form TP-584, Schedule D, *Certification of exemption from the payment of estimated personal income tax*, and file it with Form TP-584-REIT.

See *Payment of estimated personal income tax*, on page 1 of Form TP-584-I, *Instructions for Form TP-584*, for more information.

Specific instructions

Schedule A

Condition of conveyance

Indicate the condition of conveyance by checking all the condition(s) that apply. If you check item d, attach Form TP-584.1, *Real Estate Transfer Tax Return Supplemental Schedules,* to Form TP-584-REIT, with Schedule F completed.

Schedule B

Line 1 – Enter the consideration for the conveyance as set forth in section 1402(b)(3) of the Tax Law. **See TSB-M-94(4)R for more information on the calculation of consideration and net cash flow from operations.**

Line 2 – See Form TP-584-I, *Line Instructions for Completing Form TP-584,* page 2, for more information on the continuing lien deduction.

Line 3 – Enter the taxable consideration by subtracting line 2 from line 1.

Line 4 – Compute and enter the amount of tax due based on the consideration entered on line 3. The rate is $1 for each $500, or fractional part thereof, of taxable consideration on line 3.

Schedule C

Check the appropriate box on Schedule C, if this schedule is required.

Signature and affirmation (both the grantor(s) and grantee(s) must sign).

The undersigned certify that the above return, including any certification, schedule or attachment, is to the best of his/her knowledge, true and complete.

Grantor signature	Title	Grantee signature	Title
Grantor signature	Title	Grantee signature	Title

BERGMAN ON MORTGAGE FORECLOSURES:

Forgetting Assignment Proves Fatal

By Bruce J. Bergman

While mortgage servicers have no doubt come to recognize the importance of getting the proper mortgage assignments—and advising foreclosure counsel of their existence—problems raised by a lack of an assignment are probably viewed as fixable. That is indeed true much of the time, although curing the problem of the missing assignment can often consume considerable time and generate higher legal fees.

How to solve the myriad dilemmas raised by lost or non-existent assignments is not the subject here. Rather, the focus is the unfortunate and frightening message that neglecting an assignment can simply destroy a foreclosure action—and a recent case in New York tells us this is so. [*Colony Mort. Bankers v. Levell*, 194 Misc.2d 447, 753 N.Y.S.2d 820 (Sup. Ct. 2003).]

Here is the chilling (and perhaps not so uncommon?) scenario: Lender X originates a mortgage loan in August. In September the loan is assigned to Y. The loan goes into default the following year and in July a foreclosure is commenced in the name of X as plaintiff. (How it is that X still had the file and sent it to counsel without mention of the assignment is unclear—and pointedly lamentable.)

When the foreclosure judgment was sought, the defaulting borrower awakened and moved to dismiss the foreclosure action on the ground that plaintiff X had sold its interest in the mortgage (via assignment to Y) and so had no right to bring the action in the first place. Plaintiff responded by moving to amend the complaint to show Y as plaintiff.

Conveniently, CPLR 2001 allows a court to correct a mistake or defect upon terms which are just, or even disregard the mistake if a party is not prejudiced. And to be sure, it should have been obvious to the borrower that the foreclosure was really being brought on behalf of the actual mortgage holder.

With one servicer name changed to protect the embarrassed, this is precisely what happened in the new case—and plaintiff lost. Amendment to show Y as plaintiff was denied and the entire foreclosure was *dismissed*.

Yes, said the court, a misnomer can be corrected. But here, the proposed amendment was more than that. Such an amendment would allow a non-party (Y) to step into the shoes of the plaintiff. This was not a case commenced by Y under a mistaken name. It was begun by X under the impression that it was the mortgagee.

The lesson: forgetting an assignment can have consequences far beyond the ministerial. Sure, Y can now begin the foreclosure anew with itself correctly named as the plaintiff. But the cost is loss of all legal fees and expenses in the first action together with a delay of at least 18 months. Know thy assignments!

Mr. Bergman, author of the three-volume treatise, *Bergman on New York Mortgage Foreclosures* (Matthew Bender & Co., Inc., rev. 2004), is a partner with Berkman, Henoch, Peterson & Peddy, P.C., Garden City, NY; an Adjunct Associate Professor of Real Estate with New York University's Real Estate Institute, where he teaches the mortgage foreclosure course; and a special lecturer on law at Hofstra Law School. He is also a member of the USFN and the American College of Real Estate Lawyers.

CORRECTION

Please note:

The UCC-related article by Michael Berry in the Spring 2006 edition of the *N.Y. Real Property Law Journal* has a typo. The sentence in the left column on the final page should read as follows:

"The description of the real property is to be made either by reference to a deed or mortgage book and page of recording or by street address, and, in the City ***or*** New York and the Counties of Nassau and Onondaga, also by reference to the tax block and lot number of the property in which the real estate is situated."

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The Real Property Law Section encourages members to participate in its programs and to volunteer to serve on the Committees listed below. Please contact the Section Officers or Committee Chairs for further information about the Committees.

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The *Journal* welcomes the submission of articles of timely interest to members of the Section in addition to comments and suggestions for future issues. Articles should be submitted to any one of the Co-Editors whose names and addresses appear on this page.

For ease of publication, articles should be submitted by e-mail to any one of the Co-Editors, or if e-mail is not available, on a 3½" floppy disk, preferably in Microsoft Word or WordPerfect. Accepted articles fall generally in the range of 7-18 typewritten, double-spaced pages. Please use endnotes in lieu of footnotes. Please also include one laser-printed copy. The Co-Editors request that all submissions for consideration to be published in this *Journal* use gender neutral terms where appropriate or, alternatively, the masculine and feminine forms may both be used. Please contact the Co-Editors regarding further requirements for the submission of articles.

Unless stated to the contrary, all published articles represent the viewpoint of the author and should not be regarded as representing the views of the Co-Editors, Board of Editors or the Section or substantive approval of the contents therein.

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