

Kralik v 239 E. 79th St. Owners Corp.

2006 NY Slip Op 30550(U)

May 3, 2006

Supreme Court, New York County

Docket Number: 107822/98

Judge: Marylin G. Diamond

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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY
PRESENT: HON. MARYLIN G. DIAMOND PART 48

Justice

GEORGE KRALIK & SARAH B. KRALIK,

Plaintiffs,

-against-

239 EAST 79TH STREET OWNERS CORP.,

Defendant.

INDEX NO. 107822/98

MOTION DATE

MOTION SEQ. NO. 010

MOTION CAL. NO.

FILED
JUN 01 2006
NEW YORK
COUNTY CLERK'S OFFICE

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered: Defendant is a cooperative corporation which owns a building located on East 79th Street in Manhattan. In 1984, plaintiffs purchased an apartment in the building from the sponsor of the cooperative, Robert J. Ettinger and Lawrence E. Goldschmidt d/b/a Anby Associates. In April, 1998, plaintiffs commenced this action seeking a declaratory judgment that they are "holders of unsold shares" in the apartment and, as such, are entitled under the proprietary lease to sublet the apartment without seeking the consent of the cooperative board and without paying a sublet fee. In addition, they seek an injunction restraining the defendant from interfering with their rights as holders of unsold shares to sublease the apartment. Plaintiffs also seek damages for lost rental income because of their alleged inability to sublet the apartment due to improper interference by defendant.

By decision and order dated September 2, 2003, this court granted the defendant's motion for summary judgment and declared that plaintiffs are not holders of unsold shares and that they are therefore required to first obtain defendant's consent in order to sublet their cooperative apartment in the defendant's building and to pay all applicable sublet fees. The court's determination was based on the plaintiffs' failure to demonstrate that they or the sponsor complied with a number of statutory and regulatory prerequisites for acquiring the status of a holder of unsold shares. Although the order was affirmed by the First Department, *see Kralik v. 239 East 79th Street Owners Corp.*, 4 AD3d 144 (1st Dept 2004), it was subsequently reversed by the Court of Appeals, *see 5 NY2d 54* (2005), which held that the statute and regulations upon which this court and the First Department relied do not apply until plaintiffs offer the apartment for sale to the public. The Court of Appeals stated that whether the plaintiffs are holders of unsold shares must be determined solely by applying ordinary contract principles to the documents defining their contractual relationship with the cooperative corporation. *Id.* at 57.

On remittal, the plaintiffs have now moved for summary judgment on their complaint. They seek (1) a declaratory judgment that they are holders of unsold shares with the rights attendant to such status, (2) a permanent injunction restraining the defendant from interfering with such rights, (3) monetary damages arising from the defendant's prior interference with their right to sublease the apartment without the coop's consent and without the imposition of a fee and (4) attorney's fees. The defendant has cross-moved for summary judgment declaring that the plaintiffs are not holders of unsold shares and dismissing the plaintiffs' claims for injunctive and monetary relief.

Discussion

1. Holders of Unsold Shares Status - As prescribed by the Court of Appeals, the court's determination of whether plaintiffs are holders of unsold shares must be reached by reference to the documents which control their contractual relationship with the defendant. In its decision, the Court of Appeals, in citing the case of *Fe Bland v. Two Trees Mgt. Co.*, 66 NY2d 556, 563 (1985), suggested that the operative documents consist of the certificate of incorporation, the corporation's by-laws and the

* 2]
proprietary lease. See *Kralik v. 239 East 79th Street Owners Corp.*, 5 NY2d at 54.

Neither the defendant's certificate of incorporation nor its by-laws includes any provision which defines or sets forth the conditions which must be satisfied in order for a party to be considered a holder of unsold shares. The proprietary lease, however, does contain such a provision. Paragraph 38(a) provides that the term "Unsold Shares" means the shares of the lessor, *i.e.*, the cooperative corporation, which were issued to the sponsor or to individuals produced by the sponsor pursuant to the coop's offering plan. Under the offering plan, unsold shares are to be issued on the coop's closing date to the sponsor or to a financially responsible individual designated by the sponsor with respect to any apartment which has not been purchased by that date. Paragraph 38(a) goes on to provide that all shares which are unsold shares retain this status, regardless of transfer, until (1) they become the property of a purchaser for "bona fide occupancy" by himself or a member of his family or (2) the holder of such shares or a member of his family becomes a bona fide occupant of the apartment.

Here, the closing date on which the building was conveyed from the sponsor to the corporation was November 15, 1984. Since plaintiff's apartment had not yet been purchased as of that date, the sponsor became the holders of unsold shares relating to these premises. On May 16, 1985, the plaintiffs purchased the shares to the apartment in question from the sponsor. There is no evidence that either of the two plaintiffs or any member of their family has ever occupied the apartment. It would thus appear that the plaintiffs were, and remain, holders of unsold shares within the definition set forth under paragraph 38(a) of the proprietary lease.

In opposition to the plaintiffs' motion and in support of its cross-motion for summary judgment, the defendant nevertheless argues that the plaintiffs should be denied the status of holders of unsold shares. The defendant contends that the reference in paragraph 38(a) to the coop's offering plan means that a party must comply with the obligations which the offering plan imposes on holders of unsold shares and that the failure to do so precludes a party from enforcing the rights which are otherwise attendant to such status. Noting that the offering plan requires, *inter alia*, that a holder of unsold shares comply with the trust fund provisions of GBL § 352-h and that plaintiffs have never done so, the defendant contends that the plaintiffs are not entitled to be considered holders of unsold shares.

The court disagrees. It should first be noted that an offering plan is merely a disclosure statement required by the Martin Act (GBL article 23-A) in connection with the conversion of a building to cooperative ownership and the sale of real estate securities to the public. It is prepared not by the coop, but by the sponsor. Although the terms contained in the offering plan may be used to prevent the fraudulent sale of a coop's shares to the public, the terms themselves do not govern or define the contractual relationship between a shareholder/lessee and the corporation. As the Court of Appeals has stated, it is the certificate of incorporation, the by-laws and the proprietary lease which control this relationship. See *Fe Bland v. Two Trees Mgt. Co.*, 66 NY2d at 563. See also *Kralik v. 239 East 79th Street Owners Corp.*, 5 NY2d at 54; *Barbour v. Knecht*, 296 AD2d 218, 224 (1st Dept 2002). Thus, unless the terms set forth in the offering plan are incorporated by reference in any of these three controlling documents, they cannot be used to govern or define a shareholder/lessee's relationship with the coop.

In this respect, there is nothing in paragraph 38(a) which indicates that in order to be entitled to the status of a holder of unsold shares, a party must comply with the obligations set forth in the offering plan. Rather, paragraph 38(a) merely defines "unsold shares" as shares issued by the coop, pursuant to the offering plan, to the sponsor or someone produced by the sponsor. As already noted, the offering plan provides that unsold shares are to be issued on the coop's closing date to the sponsor or to a financially responsible individual designated by the sponsor with respect to any apartment which has not been purchased by that date. Although the offering plan also imposes obligations on a party to whom such shares have been issued, such as compliance with GBL § 352-h, it does not make the satisfaction of such obligations a condition precedent to the issuance of the shares. Since the reference in paragraph 38(a) to the offering plan is limited to that portion of the plan which addresses the issuance of the unsold shares, it does not otherwise incorporate the obligations on which the defendant relies. Thus, the plaintiffs' failure to satisfy the obligations which the offering plan imposes on holders of unsold shares does not preclude

them from enjoying the benefits attendant to that status.

In opposing the plaintiffs' motion for summary judgment, the defendant also argues that there is a ~~factual issue as to whether the plaintiffs purchased the apartment for investment only or for "bona fide occupancy."~~ In support of this argument, the defendant asserts that there are number of factors which suggest that the plaintiffs did not intend to purchase the apartment as holders of unsold shares, such as the absence in the contract of sale of any reference to the purchase of unsold shares, the absence of any reference in any of the amendments of the offering pan to the plaintiffs as holders of unsold shares and plaintiffs' payment of sublet fees during the period between 1988 and 1992. The problem with this argument is that there is no evidence that the plaintiffs or any member of their family have ever occupied the apartment at any time during their twenty-one years of ownership. The fact that they have never occupied the apartment is dispositive of the issue of whether the plaintiffs purchased the apartment for bona fide occupancy. They clearly did not.

The court therefore concludes that the plaintiffs are entitled to a judgment declaring that they are holders of unsold shares with the rights attendant to such status. In view of the defendant's continued refusal to extend such rights to the plaintiffs, such as the right to sublease their apartment without the coop's approval and without the imposition of a fee, the plaintiffs are also entitled to the injunctive relief which they seek.

2. Damages and Attorney's Fees - Neither side has adequately addressed the extent of the damages to which the plaintiffs are entitled by reason of the defendant's refusal to afford them the status of holders of unsold shares. Clearly, the plaintiffs are entitled to recover the fees, if any, which they paid to the coop during the six years (*see* CPLR 213) prior to their commencement of this action.

The plaintiffs, however, also seek to recover as damages the rent which they lost as the result of not having subleased their apartment on account of the defendant's insistence that its prior consent first be obtained. It appears that the only time the defendant denied plaintiffs the right to sublease their apartment to a particular tenant was in 1998. Clearly, the plaintiffs are entitled to some measure of damages flowing from this denial since the coop did not have the authority to deny the sublease. In this respect, the coop's invocation of the business judgment rule as a defense to the plaintiffs' claim for damages is without merit since the rule is inapplicable to unauthorized actions taken by a corporate board. *See Matter of Levandusky v. One Fifth Ave. Apt. Corp.* 75 NY2d 530, 538 (1990).

It also appears that, subsequent to the denial of their sublease in 1998, the plaintiffs did not even attempt to sublease the apartment. Although the defendant may have been in breach of the proprietary lease by requiring that its consent to a sublease first be obtained, the plaintiffs were nevertheless under an obligation to mitigate damages by seeking to subsequently obtain the coop's consent for the occupation of the apartment by other proposed sublessees, unless doing so would have been futile. *See Savitsky v. Sukenik*, 240 AD2d 557, 558 (2nd Dept 1997). In this respect, there is nothing in the record before the court which indicates whether it would have been futile for the plaintiffs to obtain the coop's approval for other proposed sublessees. Thus, the extent of the damages which plaintiffs are entitled to recover herein can only be determined at a later date.

As to attorney's fees, the parties have not briefed the issue of whether plaintiffs are entitled to such relief under the proprietary lease given the fact that this is primarily a declaratory judgment action not involving the plaintiffs default on any of its lease obligations. The resolution of this issue must therefore be deferred to a later date.

Accordingly, the plaintiffs' motion for summary judgment is granted to the extent that they seek an order (1) declaring that they are holders of unsold shares with the rights attendant to such status, (2) enjoining the defendant from interfering with their right to sublease the apartment at issue as holders of unsold shares and (3) finding that they are entitled to some monetary damages, to be determined at a later date, arising from the defendant's refusal to afford them the status of holder of unsold shares. The plaintiffs' application for attorney's fees is denied without prejudice.

The parties shall appear before the court in Room 412, 60 Centre Street, New York, New York on June 6, 2006 at 10:30 a.m. for a status conference, which will include a discussion regarding the proper calculation of the monetary damages which the plaintiffs have incurred.

ENTER ORDER

Dated: 5/3/06

MGD

MARYLIN G. DIAMOND, J.S.C.

Check one: FINAL DISPOSITION

NON-FINAL DISPOSITION

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