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Short Form Order/Judgment

NEW YORK SUPREME COURT - QUEENS COUNTY

Present: HONORABLE DAVID ELLIOT
Justice

IAS Part 14

CONTINENTAL 66 ASSOCIATES, LP, et al.,
Petitioners,

- against -

CONTINENTAL GARDENS APARTMENT CORP., et al.,
Respondents.

Index No. 8297 2012

Motion Date July 10, 2012 (and re-noticed on March 24, 2013 per CPLR 7804 [f])

Motion Seq. No. 1

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Petitioners Continental 66 Associates LP (Continental 66) , Terrence Artus and Peter August re-noticed this Article 78 proceeding pursuant to this court's prior order dated October 26, 2012, and seek a judgment declaring that Mr. Artus and Mr. August are members of the Board of Directors Continental Gardens Apartment Corp. (Continental Gardens), and ordering that they be notified of and permitted to attend all meetings of said Board of Directors, be permitted to vote at said meetings and have their votes counted for the purposes of decision making, and otherwise have all the powers to act conferred upon Board members pursuant to the bylaws of Continental Gardens.

As noted in the court's October 26, 2012 order, Continental 66 is the sponsor or holder of 8,830 unsold shares and holds the proprietary lease to 27 apartments in Continental Gardens, a cooperative apartment complex. Respondents are Continental Gardens, the cooperative corporation and its Board of Directors. Petitioners alleged that, at the

cooperative's annual shareholder meeting held on October 5, 2010, Mr. Artus and Mr. August were designated by the sponsor as members of the Board of Directors, and are currently members of the Board of Directors.

At the October 6, 2011annual shareholders meeting, an issue arose as to the number of available elective seats on the Board of Directors, and whether the sponsors' designated members, Mr. Artus and Mr. August, could serve on the Board. It was agreed that the election would be postponed, as a special proceeding commenced on February 2, 2011, by two shareholders Leonid Babadjanov and Yakov Bangiyev entitled *Babadjanov v Continental 66 Associates*, Index No. (2589/2011), challenging the October 5, 2010 appointments of Mr. Artus and Mr. August to the Board of Directors, was *sub judice*. Mr. Babadjanov was also an elected member of the Board of Directors.

At the annual shareholders meeting held on December 8, 2011, five shareholders were elected to the Board of Directors. Following the election, the Board of Directors has not permitted the sponsor designees Mr. Artus and Mr. August to attend Board meetings.

The Honorable Marguerite A. Grays, in an order dated December 19, 2011, dismissed the *Babadjanov* proceeding on the grounds that Business Corporation Law §619 was not the correct mechanism for challenging the sponsor's appointments, and declined to convert said proceeding to a plenary action.

Petitioners commenced this Article 78 proceeding on April 19, 2012. No shareholder meetings and elections have been held since December 8, 2012, due to the within litigation. Petitioners contend that, as Mr. Artus and Mr. August were appointed to the Board of Directors by the sponsor at the annual shareholder's meeting held on October 5, 2010, they are entitled to remain on the Board. It is alleged that, since December 21, 2011, respondents have refused to permit Mr. Artus and Mr. August to attend, participate, vote or otherwise act as members of the Board of Directors. Petitioners' first cause of action alleges that respondents' actions are unreasonable, arbitrary and capricious; the second cause of action alleges an abuse of discretion. The third and fourth causes of action are identical, and allege that respondents have failed to perform a duty imposed upon them by law, in that they have not permitted Mr. Artus nor Mr. August to attend, participate in, vote, or otherwise act at, meetings of the Board of Directors. Petitioners, in their wherefore clause, seek a judgment declaring that Mr. Artus and Mr. August are members of the Board of Directors, and an order directing respondents to notify and permit them to attend all meetings of the Board of Directors, to vote at said meetings and have their votes counted for the purpose of decision making, and otherwise have all the powers conferred upon the Board of Directors by the bylaws.

This court, in its order of October 26, 2012, granted respondents' motion to dismiss the petition as to the individual respondents Leonid Babadjanov, Yakov Bangiyev, and Adam Meyers-Spector, and denied said motion in all other respects. The remaining respondents were directed to serve an answer within 20 days of the service of a copy of the order, together with notice of entry, and petitioners were given an opportunity to serve a reply, if they deemed it necessary, within 10 days of the receipt of the answer. The parties were directed to follow the appropriate procedures for re-noticing the within proceeding. A copy of said order, together with notice of entry, was served on respondents on November 13, 2012.

On December 10, 2012, respondents served their answer, and interposed eight affirmative defenses and objections in point of law which sought, in part, the dismissal of the within proceeding. Respondents also served supporting affidavits, affirmations and exhibits on that date. On December 19, 2012, petitioners re-noticed the petition, setting a return date of March 24, 2013. Petitioners also served a motion to strike respondents' objections in point of law and to vacate respondents' re-noticing of their application for dismissal. Thereafter, several conferences were held in this part. The parties entered into a stipulation dated February 13, 2013, whereby petitioners agreed to withdraw their motion to strike respondents' objections in point of law and to vacate the re-noticing of hearing. The parties agreed that petitioners' papers submitted in support of the withdrawn motion would serve as the reply to the respondents' answer, and to submit said papers to the court as the reply. It was also agreed that the respondents could submit a response to the petitioners' reply. Said stipulation was filed with the court on March 21, 2013. The re-noticed petition, answer, and reply papers have now been fully submitted in this Part.

Respondents, in their verified answer, interposed the affirmative defenses of failure to state a cause of action; documentary evidence; estoppel, laches and/or unclean hands; statute of limitations; lack of standing and/or capacity; business judgment rule; estoppel, including collateral estoppel, judicial estoppel and equitable estoppel; and law of the case based upon the court's order of October 26, 2012. The answer also interposed objections in point of law which assert that the cooperative's governing documents do not give the sponsor the right to appoint members of the Board of Directors, and that petitioners are unable to demonstrate that the sponsor's practice of designating seats derives from any valid authority.

Petitioners assert that the sponsor designees have been members of the Board of Directors for more than 25 years. Petitioners claim that the shareholders, in 1986 and 1989, voted to change the number of Board members and approved the sponsors' designation of Board members. In support of this claim, petitioners have submitted the affidavits of Robert Schwartz and James Cullen, who had previously been appointed to the Board by the sponsor.

These affidavits were previously submitted to the court in opposition to the respondents' motion to dismiss.

Mr. Schwartz states in his affidavit that, in 1986, he was the Treasurer of the cooperative and that, on April 8, 1986, a shareholder election was conducted, at which time the shareholders voted unanimously to increase the size of the Board of Directors from three to five people, with three appointed by the sponsor, and two elected by the shareholders. He states that, because the number of shares voted was more than 2/3 of the cooperative's shareholders, this effectuated an amendment to the bylaws, effective 1987. Mr. Cullen states that he was Assistant Vice President of the cooperative in 1989; that, on April 12, 1989, a shareholder election was conducted and the shareholders unanimously voted to maintain the size of the Board of Directors at five people and to reduce the number of sponsor appointees to two, and increase the number of elected members to three. He states that, because the shares voted were more than 2/3 of the cooperative's shareholders, this effectuated an amendment to the bylaws, effective 1990.

Respondents assert that, notwithstanding past practices of sponsor appointees, the Board of Directors has sought to correct this practice since December 2011. It is further asserted that there is no evidence that the shareholders intentionally relinquished for all time the right to insist that election of the directors to the Board be consistent with the governing documents and law. Respondents, therefore, assert that the number of Directors constituting the Board and the manner in which those members are chosen should be determined consistent with the governing documents, and that the petition should be dismissed. Respondents further assert that, at the least, they are entitled to a trial of issues of fact raised by their answer and supporting documents.

Respondents, in support of their answer, submit an affidavit from Adam Meyers-Spector, an elected director and President of the Board of Directors. Mr. Meyers-Spector states in his affidavit that, beginning in 2011, the shareholders and elected Board members began to raise objections to the sponsor's appointment of members of the Board. On December 8, 2011, at a newly noticed annual meeting, which specified that an election would be held for five seats, the shareholders elected the five shareholders that currently serve on the Board of Directors. Mr. Meyers-Spector states that following the election, Mr. August and Mr. Autus were not permitted to attend Board meetings as they were not elected by the shareholders to serve on the Board.

Petitioners, in their reply, assert that this court, in its order of October 26, 2012, made certain findings of fact and conclusions of law and that it is law of the case that the shareholders abandoned the bylaws pertaining to the size of the Board of Directors and the manner of election or selection of officers for a significant amount of time; that the

shareholders cannot resuscitate said bylaws; and that respondents are not entitled to dismissal of the petition on the grounds that the sponsor did not have the authority to designate directors. Petitioners, therefore, assert that, as Mr. Artus and Mr. August were designated by the sponsor as members of the Board of Directors in 2010, no valid basis exists for respondents to have excluded them from the Board meetings, as neither the shareholders nor the directors voted to do the same.

The parties herein have agreed that the petition is to be determined on the papers submitted. This court, in its order of October 26, 2012, determined that Mr. Artus and Mr. August are not entitled to a declaration to the effect that they are members of the Board of Directors, as the petition did not state a hybrid claim for declaratory judgment. Therefore, this issue will not be revisited here. The issue to be determined here is whether the sponsor may designate members of the Board and, if so, whether the respondents' refusal to allow Mr. Artus and Mr. August to attend Board meetings, to vote as Board members and have their votes counted, and to otherwise exercise their rights as members of the Board, is arbitrary and capricious.

Public policy requires that a sponsor not only relinquish control of the Board of Directors, where as here, the offering plan requires such a result (*see* 13 NYCRR 18.3 [v] [5] [I]), but also militates against a sponsor appointing or designating members of the Board, absent a bylaw permitting such appointments. Here, it is undisputed that the offering plan contains assurances that the sponsor will relinquish voting control over the board of directors, as required by 13 NYCRR 18.3 (v) (5) (I), and that the sponsor in fact relinquished control in April 1989 (*see generally Board of Directors of Exec. House Owners, Inc. v E.H. Assoc.*, 248 AD2d 530, 532 [1998]; *see also Matter of 300 Ocean Owners Corp. v Bouskila*, 67 AD3d 919, 920 [2009]; *Park Briar Assoc. v Park Briar Owners, Inc.*, 182 AD2d 685, 686 [1992]; *Rego Park Gardens Assoc. v Rego Park Gardens Owners, Inc.*, 174 AD2d 337, 338 [1991], *app den* 78 NY2d 859 [1991]).

Petitioners' claim that the bylaws were amended by the shareholders on April 8, 1986 and again on April 12, 1989, in order to permit the sponsor to appoint members of the Board of Directors, is rejected. Despite the statements made by Mr. Schwartz and Mr. Cullen in their affidavits, no documentary evidence exists that establishes that the bylaws were in fact amended. It is undisputed that no minutes exist with respect to said shareholder meetings. Petitioners have not submitted any documentary evidence that establishes that the shareholders were given proper notice of the purported proposed amendments, and have not submitted any evidence which establishes that the purported amendments were voted on by shareholders owning 2/3 of the amount of the outstanding shares, who represented in person or by proxy, at these election meetings, as required by ARTICLE XII of the cooperative's bylaws. To the extent that the sponsor has maintained a *de facto* presence on the Board of

Directors for the past 19 years by appointing or designating Board members, this activity did not, in and of itself constitute an amendment to the bylaws.

The court, therefore, finds that, as the sponsor was not authorized to appoint or designate members of the Board of Directors, respondents' refusal to permit petitioners Terrence Artus and Peter August to attend Board meetings, to vote at said meetings, or otherwise exercise any rights as members of the Board, was not unreasonable, arbitrary nor capricious, nor constitutes a failure to perform a duty imposed upon them by law.[1]

In view of the foregoing, it is hereby

ORDERED and ADJUDGED that the relief requested is denied and the petition is dismissed.

Dated: July 2, 2013

J.S.C.

1. It is noted that this finding is not inconsistent with the court's October 26, 2012 ruling regarding the abrogation of a certain by-law. Rather, the court only determined that the shareholders had abandoned the by-laws pertaining to the size of the Board of Directors and the manner of election (or selection) of officers, *but only upon until the point of the December 2011 election*. The court did not make any determination that the approximate 19-year practice of operating under an enlarged, partially appointed, Board created any new rights or amended the by-laws.