Babad v Board of Directors of Murray House Owners Corp.
2019 NY Slip Op 31856(U)
June 26, 2019
Supreme Court, New York County
Docket Number: 650144/2018
Judge: Tanya R. Kennedy
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 63

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CHAIM BABAD, HENOCH BABAD, BERNARD STEINMETZ, PINCHOS EICHENSTEIN, MIREL BABAD, ABRAHAM WEINGARTEN, SARA SPIEGAL, YITZCHOK STEINMETZ, NAFTALI BABAD, USHER STEINMETZ and EMANUEL STEINMETZ, derivatively on behalf of MURRAY HOUSE OWNERS CORP,

Plaintiffs,

-against-

Index No. 650144/2018
Motion Sequence 001

BOARD OF DIRECTORS OF MURRAY HOUSE OWNERS CORP., and SOLSTICE RESIDENTIAL GROUP LLC.,

Defendants,

-and-

MURRAY HOUSE OWNERS CORP.,

Nominal Defendant.

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HON. TANYA R. KENNEDY, J.S.C.:

Defendants Board of Directors of Murray House Owners Corp. ("Board") and Solstice Residential Group LLC ("Solstice"), and nominal defendant Murray House Owners Corp ("Murray House or Cooperative") (collectively "defendants") move, pursuant to CPLR 3211 (a)(1) and (7), to dismiss the complaint in its entirety, based upon documentary evidence and for failure to state a cause of action. The Court heard oral argument on the motion, which is decided in accordance with the following.

FACTUAL BACKGROUND

Murray House is a cooperative apartment corporation and owner of a building located at 220 Madison Avenue, New York, New York ("Building") (verified derivative complaint, ¶2; Exhibit C, Proprietary Lease, p. 1). Defendant Board is the elected Board of Directors of Murray

House, which is authorized, pursuant to its By-Laws, to manage the business and affairs of the Cooperative (verified derivative complaint, ¶3; Exhibit B, By-Laws, Article VI, Section 1).

Defendant Solstice is the managing agent for the Cooperative (Exhibit G, Management Agreement). On November 29, 2011, Solstice entered into an agreement with the Cooperative ("Management Agreement"), requiring Solstice, among other things, to maintain the Building, manage employees, bill and collect maintenance payments from shareholders, and remain abreast of cooperative housing policies, and applicable laws and regulations (*id.*, ¶¶1-2).

Plaintiffs are eleven (11) shareholder-lessees who are "Holders of Unsold Shares" allocated to twenty-three (23) apartments in the Building (verified derivative complaint, ¶¶1-2). As "Holders of Unsold Shares," the shares allocated to plaintiffs were never owned by persons or members of their immediate family who occupied such apartments (Exhibit C, Proprietary Lease, ¶38[a]).

In May 2017, the Board revised the House Rules, which plaintiffs maintain that their consent was required before the Board engaged in such action (verified derivative complaint, ¶¶16, 36). The three May 2017 House Rules which plaintiffs challenge are as follows:

> (1) all shareholders who reside in the Building are permitted to have one dog and/or two cats in their apartment, whereas residents who are not shareholders are prohibited from harboring pets in the apartment ("Pet Policy");
>
> (2) a non-refundable $750 fee is charged to all persons who move into and out of the Building, regardless of whether the occupant is a shareholder or subtenant (the "Moving Fees");
>
> (3) all subtenants, including those of Holders of Unsold Shares, are required to submit a copy of their lease and on-line data form to the Cooperative prior to move-in (the "Move-In Requirements").
>
> (Exhibit E, May 2017 House Rules, pp. 9, 24, 26-28).

The Board revised the May 2017 House Rules in July 2017 (the "July 2017 House Rules") which remain in effect and include the same three rules which plaintiffs challenge (Exhibit F, July 2017 House Rules; Vaccaro Affidavit, ¶6).

Article II, Section 8 of the By-Laws provides that "[t]he board of directors shall have [the] power to make and change reasonable rules applicable to the apartment building owned or leased by the corporation whenever the board deems it advisable to do so" (Exhibit B, By-Laws). This same provision further provides, *inter alia*, that "[a]ll house rules shall be binding upon all tenants and occupants of the apartment building" (*id.*). Further, the Proprietary Lease provides, *inter alia*, that "[t]he Lessor has adopted House Rules which are appended hereto; and the Directors may alter, amend or repeal such House Rules and adopt new House Rules ...," as well as that "[t]he Lessee hereby covenants to comply with all such House Rules ..." (Exhibit C, Proprietary Lease, ¶13).

Plaintiffs commenced this derivative action as Holders of Unsold Shares and on behalf of all shareholders similarly situated, alleging that Section 501(c) of the Business Corporation Law (BCL), as well as the Cooperative's By-Laws, Proprietary Lease and House Rules (collectively "Governing Documents") all prohibit the Pet Policy, Moving Fees and Move-In Requirements (verified derivative complaint, ¶8).

With respect to the Pet Policy, plaintiffs allege that such policy violated BCL §501(c) because "it resulted in the disparate treatment of shareholders of [the] Apt. Corp., based upon whether they resided in the Building" (*id.*, ¶13). As for the Moving Fees, plaintiffs allege that such fees are "unlawful" because the "Board does not have the requisite authority to implement such a fee" (*id.*, ¶18). Plaintiffs also allege that the Move-In Requirements constitute "impermissible requirements directed towards such Holders of Unsold Shares inasmuch as those

provisions mandate new burdens and additional requirements for them and their subtenants" (*id.*, ¶19).

Further, plaintiffs allege that Solstice was required to "enforce the Governing Documents and comply with New York Law" pursuant to the Management Agreement, and that "Solstice breached the Management Agreement" through its enforcement of the House Rules (*id.*, ¶¶43-44).

Plaintiffs assert causes of action for breach of fiduciary duty (against the Board and Solstice), a declaratory judgment (against the Board), breach of contract (against Solstice), and for reimbursement of attorneys' fees pursuant to BCL §626(e) (against the Board) (*id.*, ¶¶28-55).

ARGUMENTS

Defendants now move, pursuant to CPLR 3211 (a)(1) and (7), to dismiss the complaint in its entirety and to declare that the Board did not violate BCL§501(c), the By-Laws for Murray House, or the form Proprietary Lease for Murray House when they adopted the May 2017 House Rules and further amended those rules in July 2017.

Defendants maintain that the Governing Documents refute plaintiffs' claims of disparate treatment. Specifically, defendants maintain that the Cooperative only issued one class of shares (Exhibit D, Certificate of Incorporation) and that the challenged rules are equally applicable to all shareholders. With respect to the Pet Policy, defendants argue that such policy permits every shareholder to maintain a dog in his or her apartment and prohibits every subtenant of every shareholder from sheltering pets in the apartment.

As for the Moving Fees, defendants maintain that such fees are applicable to every shareholder, subtenant or occupant who moves in or out of the Building. Defendants note that the May 2017 House Rules explicitly state, *inter alia*, that "[t]here is a non-refundable move-in and move-out fee of $750 for each instance" (Exhibit E, May 2017 House Rules, p. 24). Additionally,

defendants note that the May 2017 House Rules further provide that "[a]ll subtenants including those of Holders of Unsold Shares are required to abide by the move-in and move-out rules that are part of these House Rules including the payment of any associated fees" (*id.*, p. 28).

Defendants also note that the May 2017 House Rules provide, *inter alia*, that "[i]f the apartment is being rented by the Holder of Unsold Shares, the Board must receive a copy of his or her lease prior to move-in . . . Holder of Unsold Shares' subtenants must fill-in the subtenant on-line data form, sign the subtenant form, submit the non-refundable move-in fee and the refundable move-in fee prior to move-in" (*id.*, pp. 27-28).

According to defendants, these same rules apply to subtenants of other shareholders who are not Holders of Unsold Shares and are described in a separate provision of the May 2017 House Rules. Defendants maintain that these sublets, unlike the sublets of Holders of Unsold Shares, are subject to board approval who must first submit an application (*id.*, pp. 26-27; Exhibit C, Proprietary Lease, ¶15). Additionally, defendants argue that its decisions are governed by the business judgment rule, which prohibits judicial inquiry into legitimate corporate actions, and that the Governing Documents refute the plaintiffs' claim that the Board exceeded the scope of its authority.

As for the cause of action for breach of fiduciary duty against the Board, defendants maintain that this claim should also be dismissed because there is a written agreement between the parties which governs the matter in dispute. With respect to the breach of contract claim against Solstice, defendants maintain that dismissal is warranted because the Management Agreement did not require Solstice to "enforce the Governing Documents and comply with New York law" as plaintiffs allege (verified derivative complaint, ¶43). With respect to the cause of action for breach of fiduciary duty against Solstice, defendants maintain that this claim is duplicative of the breach

of contract claim and should be dismissed. Lastly, defendants argue that plaintiffs are not entitled to reimbursement of attorneys' fees pursuant to BCL §626(e) because this action is without merit and should be dismissed.

Plaintiffs argue in opposition, *inter alia*, that the House Rules are incorporated into the Proprietary Lease and that any House Rules that alter the Proprietary Lease constitutes a *de facto* amendment of the Proprietary Lease and is impermissible. Plaintiffs also maintain that as Holders of Unsold Shares, they possess an absolute right to sublet their apartments without any restriction as set forth under the Governing Documents.

Plaintiffs acknowledge that the Board is authorized to adopt House Rules without shareholders' consent. However, plaintiffs argue that the Board cannot amend the Proprietary Lease or By-Laws, as such documents can only be amended by a supermajority vote of the shareholders, and with the consent of all Holders of Unsold Shares to the extent that the proposed amendment affects any rights of the Holders of Unsold Shares. Specifically, plaintiffs argue that the House Rules are invalid because they restrict the rights of Holders of Unsold Shares to freely sublease their apartments by requiring them to only sublet to persons who are non-pet owners and to pay fees and submit financial and personal information to management.

Plaintiffs rely upon the language set forth in paragraphs 6 and 38(c) of the Proprietary Lease. Paragraph 6 of the Proprietary Lease states, *inter alia*, that:

> "the proprietary leases then in effect and thereafter to be executed may be changed by the approval of lessees owning at least 2/3 of the Lessor's shares then issued [...] in no event shall any change in the form of proprietary lease and any of the provisions thereof be made which shall adversely affect certain rights granted to (i) purchasers of Unsold Shares (pursuant to paragraph 38 hereof) or (ii) the Secured Party ... [per paragraph 17(b)], unless all such purchases of Unsold Shares and the Secured Party affected thereby have unanimously agreed to each such change"
> (Exhibit C, Proprietary Lease).

As such, plaintiffs maintain the Board eliminated the right of Holders of Unsold Shares to freely sublease while not eliminating the rights of other shareholders, which constitutes unequal treatment of shares of the same class of stock in violation of BCL §501(c), without any legitimate corporate purpose.

With respect to the causes of action against Solstice for breach of contract and breach of fiduciary duty, plaintiffs maintain that they sufficiently pled such claims because the Management Contract between the Board and Solstice required Solstice to act in the Cooperative's best interests and in accordance with New York law, which Solstice violated by implementing illegal House Rules. Lastly, plaintiffs maintain that the defendants' actions, which restricted their right to sublease, caused them to incur legal fees and expenses, entitling plaintiffs to reimbursement of such fees and expenses pursuant to BCL §626(e).

In reply, defendants reiterate the arguments in support of dismissal and argue, *inter alia*, that neither paragraph 6 nor paragraph 38(c) of the Proprietary Lease involve amendments to the House Rules. Rather, both paragraphs address the required procedure and approval for amending the form Proprietary Lease. With respect to paragraph 38(c) of the Proprietary Lease, defendants note that such provision provides that any alterations to the form Proprietary Lease will not adversely affect the rights and privileges of rights which the Holders of Unsold Shares enjoy unless they consent. As such, defendants maintain that paragraph 38(c) did not expand any right to sublet and only affirmed the subletting rights previously extended to Holders of Unsold Shares.

DISCUSSION

On a motion to dismiss pursuant to CPLR 3211(a)(1), the movant is required to establish that the documentary evidence conclusively refutes the party's claim (*see AG Capital Funding*

Partners, L.P. v State St. Bank & Trust Co., 5 NY3d 582, 590-591 [2005]). The movant must demonstrate that "the documentary evidence utterly refutes plaintiff's factual allegations, conclusively establishing a defense as a matter of law" (*Goshen v Mutual Life Ins. Co. of N.Y.*, 98 NY2d 314, 326 [2002]).

When evaluating a defendant's motion to dismiss pursuant to CPLR 3211(a)(7), the court "must give the pleadings a liberal construction, accept the allegations as true and accord the plaintiffs every possible favorable inference" (*Chanko v American Broadcasting Cos. Inc.*, 27 NY3d 46, 52 [2016], citing *Goshen v Mutual Life Ins. Co. of N.Y.*, 98 NY2d 314, 326 [2002]).

"The relationship between the lessee and a cooperative corporation is governed by the certificate of incorporation, the corporation's bylaws, and the proprietary lease, which must be read together" (*Anchev v 335 W. 38th St. Coop Corp.*, 29 Misc3d 1223(A), *3 [Sup Ct, New York County 2010]).

Generally, "when parties set down their agreement in a clear, complete document, their writing should as a rule be enforced according to its terms . . . [and extrinsic evidence] is generally inadmissible to add to or vary the writing" (*W.W.W. Assoc. v Giancontieri*, 77 NY2d 157, 162 [1990]; *see also Beal Sav. Bank v Sommer*, 8 NY3d 318, 324-325 [2007]).

The language of the Governing Documents are unambiguous and a court may not vary their terms (*Greenfield v Philles Records*, 98 NY2d 562, 569 [2002]). Rather, a court must enforce the parties' explicit understanding as set forth in the above referenced documents.

This Court's reading of the Governing Documents unequivocally demonstrate that the Board was authorized to amend the House Rules. Contrary to plaintiffs' contention, paragraphs 6 and 38(c) of the Proprietary Lease did not require that the Board obtain consent from the Holders of Unsold Shares to amend the House Rules. Rather, these provisions addressed amendments to

the Proprietary Lease and not to the House Rules. Further, neither provision expressly indicates that the Board is required to obtain consent from the Holders of Unsold Shares to amend the House Rules.

Defendants correctly argue that the challenged House Rules did not violate BCL §501(c), which provides that "each share shall be equal to every other share of the same class." The challenged House Rules are applicable to all subtenants, whether they are subtenants of a Holder of Unsold Shares or of an ordinary shareholder. Further, the challenged House Rules did not eliminate any rights of the Holders of Unsold Shares.

The Court of Appeals has ruled that "the business judgment rule prohibits judicial inquiry into actions of corporate directors taken in good faith and in the exercise of honest judgment in the lawful and legitimate furtherance of corporate purposes" (*Matter of Levandusky v One Fifth Ave. Apt. Corp.*, 75 NY2d 530, 538 [1990] [internal quotation marks and citation omitted]). "So long as the board acts for the purposes of the cooperative, within the scope of its authority and in good faith, courts will not substitute their judgment for the board's *(id.* at 538). Since the Governing Documents authorized the Board to amend the House Rules, which all shareholders, including plaintiffs herein, consented to comply with, and the challenged amendments did not violate BCL §501(c), the cause of action for breach of fiduciary duty is dismissed pursuant to CPLR 3211(a)(1) and denied as moot pursuant to CPLR 3211(a)(7).

Contrary to plaintiffs' contention, *330 W. End Apt. Corp. v Kelly*, 124 Misc2d 870 (Sup Ct, New York County 1984) is not applicable to this matter. The motion court in *330 W. End* determined that the residential cooperative board was without authority to unilaterally impose a flip tax as a condition of the sale of a tenant-shareholder's apartment shares and assignment of the proprietary lease. Specifically, the motion court in *330 W. End* found that the proprietary lease

was silent with respect to the board's authority to implement a flip tax. Also, without merit is plaintiffs' reliance upon *Fe Bland v Two Trees Mgt. Co.*, 66 NY2d 556 (1985), in which the Court of Appeals invalidated the board's imposition of a flip tax because the by-laws and proprietary lease did not authorize such action. As previously discussed herein, the Board did not amend the Proprietary Lease, but rather amended the House Rules in accordance with its expressed authority under the Governing Documents. Further, this matter does not concern the imposition of a flip tax.

Similarly, the cause of action for a declaratory judgment is dismissed pursuant to CPLR 3211(a)(1) since the Governing Documents refute the plaintiffs' claims (*see Fillman v Axel*, 63 AD2d 876, [1st Dept 1978]; *see also Guthart v Nassau County*, 55 Misc3d 827, 834 [Sup Ct, Nassau County 2017] ["A court, however, may reach the merits of a properly pleaded cause of action for a declaratory judgment upon a motion to dismiss for failure to state a cause of action where no questions of facts are presented by the controversy...Under such circumstances, the motion to dismiss the cause of action may be treated as a motion for a declaration in the defendant's favor and treated accordingly"] [internal quotation marks and citations omitted]. Rather, defendants are entitled to a declaration that defendants did not violate BCL§501(c), the By-Laws for Murray House, or the form Proprietary Lease for Murray House when they adopted the May 2017 House Rules and further amended those rules in July 2017. The branch of the motion to dismiss this claim pursuant to CPLR 3211(a)(7) is denied as moot.

"[W]here a written agreement . . . ambiguously contradicts the allegations supporting a litigant's cause of action for breach of contract, the contract itself constitutes documentary evidence warranting the dismissal of the complaint pursuant to CPLR 3211(a)(1), regardless of

any extrinsic evidence or self-serving allegations offered by the proponent of the claim" (*150 Broadway N.Y. Assoc., L.P. v Bodner*, 14 AD3d 1, 5 [1st Dept 2004]).

Plaintiffs allege that Solstice was required to "enforce the Governing Documents and comply with New York Law" pursuant to the Management Agreement, and that "Solstice breached the Management Agreement" through its enforcement of the House Rules (*id.*, ¶¶43-44). However, as defendants correctly contend, the Management Agreement did not require Solstice to "enforce the Governing Documents and comply with New York law" as plaintiffs allege (*id.*, ¶43). Rather, Solstice was required under the terms of the Management Agreement, among other things, to maintain the Building, manage employees, bill and collect maintenance payments from shareholders, and remain abreast of cooperative housing policies, and applicable laws and regulations (Exhibit G, Management Agreement, ¶¶1-2).

As such, the Management Agreement conclusively refutes plaintiffs' breach of contract claim against Solstice (*see AG Capital Funding Partners, L.P. v State St. Bank & Trust Co., supra at* 590-591; *Goshen v Mutual Life Ins. Co. of N.Y.*, *supra* at 326; *150 Broadway N.Y. Assoc., L.P. v Bodner*, *supra* at 5). Therefore, the breach of contract claim against Solstice is dismissed pursuant to CPLR 3211(a)(1) and dismissal under CPLR 3211(a)(7) is denied as moot. The cause of action for breach of fiduciary duty against Solstice is also dismissed pursuant to CPLR 3211(a)(7) because it is duplicative of the claim for breach of contract (*see Ellington v Sony/ATV Music Publ. LLC*, 85 AD3d 438, 439 [1st Dept 2001]).

BCL §626(e) provides, in pertinent part, that:

> "If the action on behalf of the corporation was successful, in whole or in part . . . the court may award the plaintiff or plaintiffs, claimant or claimants, reasonable expenses, including reasonable attorney's fees. . ."

In as much as the first through fourth causes of action have been dismissed, plaintiffs are not the "successful" party entitled to reimbursement of attorneys' fees under BCL §626(e). Therefore, this remaining claim is also dismissed pursuant to CPLR 3211(a)(7).

Accordingly, it is

ADJUDGED AND DECLARED that defendants did not violate BCL§501(c), the By-Laws for Murray House, or the form Proprietary Lease for Murray House when they adopted the May 2017 House Rules and further amended those rules in July 2017; and it is further

ORDERED that defendants' motion to dismiss is granted to the extent that the first, second and third causes of action are dismissed pursuant to CPLR 3211(a)(1) and the fourth and fifth causes of action are dismissed pursuant to CPLR 3211(a)(7), and the complaint is dismissed in its entirety, with costs and disbursements as taxed by the Clerk of the Court, and the Clerk is directed to enter judgment accordingly.

This constitutes the Decision, Order and Judgment of the Court.

Dated: New York, New York
June 26, 2019

ENTER:

Hon. Tanya R. Kennedy
J.S.C.

HON. TANYA R. KENNEDY