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Litigation Department

Incoming Commercial Tenant has Legal Remedy Against Commercial Holdover Tenant

By: Lewis A. Lindenberg

The Appellate Division has reaffirmed its position that an incoming tenant having executed a lease for new space and being prevented from taking possession by the holdover commercial tenant has a valid claim for tortious interference with contract against the holdover tenant.

In BBW&G's Update in March 2007, I wrote about the Court's decision in the case entitled *Kronish Lieb Weiner & Helman, LLP v. Tahari, Ltd.*: Upping the Ante – Reducing Landlord's Risk That a Tenant Will Not Timely Vacate. In that article, I discussed circumstances under which a commercial landlord was unable to perform its obligations pursuant to a commercial lease and deliver possession in a timely manner to the new commercial tenant. In *Kronish*, and a more recent case, entitled *Havana Central N.Y. Two, LLC v. Lunneys' Pub, Inc,* the landlord was prevented from delivering possession because the existing holdover tenant refused to deliver timely possession to its landlord by vacating upon the expiration of the term of its lease. As a result, the incoming tenants were not able to enter into possession as contracted for. In both cases, the landlord commenced summary proceedings and recovered

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Deeming Leases Renewed: A Solution to Unreturned Renewal Leases

By: Jordi Fernandez

As most landlords are aware, a landlord is required to offer a tenant of a rent-stabilized apartment a renewal lease before the expiration of the existing lease. The renewal lease must be offered between 90 to 150 days before the expiration of an existing lease. It must be offered by personal delivery or regular mail (we recommend keeping a certificate of mailing if mailed). It must also be on a form approved by the Department of Housing and Community Renewal ("DHCR"). The DHCR form gives landlords the opportunity to include the lawful rent guidelines increases to which the landlord is entitled. The requirement for notice for the renewal of lease and renewal procedures is found in §2523.5 of the Rent Stabilization Code.

The landlord is required to give the tenant 60 days from the service of the renewal offer to execute and return the renewal lease. There are times that a tenant does not return the signed renewal to the landlord. BBWG has seen instances where the tenant has simply and innocently forgotten to return the renewal lease, as well as cases of outright refusals. The outright refusal of a tenant to return the renewal usually indicates a serious problem, such as the tenant disputing the new rent for the renewal term. The landlord has two options available when confronted with this issue.

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Incoming Commercial Tenant . . .
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legal possession after the passage of time. In both cases, the issue was not about potential liability between the landlord and his new tenant, but rather potential liability of the holdover tenant to the incoming tenant.

The circumstances in *Havana Central* are not unlike those that many landlords encounter with holdover tenants. The commercial lease is coming to an end and the holdover tenant seeks to remain in the premises, because it wants to obtain a renewal lease, and/or the holdover tenant is seeking to avoid closing its business and losing its clientele.

In *Havana Central*, the incoming tenant sued the holdover tenant based upon three separate theories for recovery of damages. The Appellate Division permitted a claim based upon alleged damages resulting from tortious interference with contract. The Appellate Division did enable the incoming tenant to pursue its claim for damages attributable to the holdover delays and its inability to timely commence its business.

Based upon two provisions in the lease between the landlord and the incoming tenant, the Appellate Division issued a split decision in *Havana Central* — three in favor and two against permitting a case for damages for tortious interference with contract.

The lease provisions protected the landlord from potential liability from the incoming tenant, and provided the incoming tenant with the right to terminate the lease. The dissenting opinion of the Appellate Division suggested that the new tenant should not have a vested right as against the former tenant for its holding over and should not be able to sue the holdover tenant.

The majority opinion reaffirmed that once the former tenant held over, he became a trespasser, and the failure to deliver possession by the landlord to the incoming tenant at the beginning of its lease term was a breach of the incoming tenant's lease.

In *Havana Central,* the holdover tenant argued that two provisions of the new lease demonstrated a conditional rather than an absolute promise by the landlord to deliver the premises on the commencement date and it therefore contended its holding over did not render performance impossible, and was not a breach of the lease.

The majority opinion reaffirmed that once the former tenant held over, he became a trespasser, and the failure to deliver possession by the landlord to the incoming tenant at the beginning of its lease term was a breach of the incoming tenant's lease. A potential cause of action did lie for interfering with contract against a holdover tenant by an incoming tenant who is prevented from taking possession because of the holdover tenant's wrongful acts.

Based upon *Kronish* and *Havana Central*, landlords increasingly will not be placed in that uncertain position often created by a holdover tenant, who refuses to vacate timely upon the expiration of the term of its lease. In addition to the remedies available to landlords against holdover tenants, the Courts have stated that remedies exist for incoming tenants against holdover tenants.

Lewis A. Lindenberg is a senior partner in the firm's Litigation Department, specializing in commercial litigation of real estate matters.

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In most scenarios, and/or before any legal action is taken, we suggest writing the tenant a letter (include a copy of the renewal lease riders) and remind the tenant that he/she must sign the renewal if the tenant wants to continue the tenancy.

If after sending the "reminder" letter there is still no signed renewal lease returned, the landlord can sue the tenant in Housing Court in a holdover proceeding for possession of the apartment based on the tenant's failure to renew the lease. This type of case is brought pursuant to RSC § 2524.3(f). In some instances a landlord may be able to evict a tenant for failing to renew the lease. For instance, a tenant who will not or cannot execute the renewal lease upon the same terms of the original lease is likely to be evicted. Generally, we do not recommend this option since it is almost certain that a Court will give the tenant the opportunity to execute the renewal lease after the parties have appeared in Court. Although RSC § 2524.3(f) does not authorize the Court to fashion a cure (*i.e.*, signing the lease after the tenancy was terminated), the appellate courts have upheld the lower court decisions in these cases. To offset its expenses the landlord can ask the Court to award attorneys' fees because it was the tenant who caused the landlord the expense. Despite the availability of reimbursement for fees, in most cases it is more practical to utilize the second option.

The second option permits the landlord to simply deem the offered lease renewed under RSC § 2523.5(c)(2). Under this option when the tenant's time to return the lease has passed the landlord can charge the tenant for the lawful increases set forth in the renewal lease and enforce the right to collect the rent guideline increases. After the landlord deems the lease renewed, the tenant often pays the rent under the prior lease, but not the higher rent under the deemed renewal lease. Sometimes the tenant simply stops paying rent. In either instance, the landlord can bring a non-payment case either for the shortfall representing the unpaid guidelines increases or the full rent under the deemed renewal lease.

In order for a landlord to make the best case, it is imperative that the landlord be able to prove that it made a timely renewal offer to the tenant. We cannot emphasize enough the importance of mailing the renewal lease to the tenant by regular mail with a certificate of mailing. We also recommend the follow up letter in which the landlord informs the tenant that the lease has been deemed renewed. If the landlord timely makes the renewal offer and is able to prove it, then the tenant is required to pay the rent, including the lawful rent increases to the landlord.

The landlord should not, as a result of the tenant's failure to return the renewal lease, be bullied into accepting less rent than it is entitled to. The law which governs renewal leases does not exist to give tenants the opportunity to negotiate lower rents upon the expiration of their current leases. While the landlord is required to timely offer renewal leases to all tenants in rent stabilized apartments and the tenant is given ample opportunity to execute and return these offers, the landlord is never compelled to accept a lower rent than it is entitled to.

This article was written by Jordi Fernandez, an associate in the Litigation Department. If you have any questions relating to this article, please contact Mr. Fernandez.

Transactional

The Importance of the Loan Commitment

By: Cody Campbell

When purchasing residential property, selecting the right property and negotiating the contract, as well as securing financing, can be such a daunting process for prospective purchasers that the significance of signing an innocuous looking short commitment letter can easily be overlooked. Some purchasers may feel as if the negotiation process begins and ends with the contract of sale and the actual rate on their proposed loan, while other purchasers may simply feel pressured to lock in a rate as quickly as possible in order to secure a loan on what they believe are the most advantageous terms. However, signing a commitment prematurely, or in haste, without consulting your attorney, can be potentially problematic and costly in two ways.

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First, the purchase of residential property is a multifaceted process that requires the input, coordination and cooperation of multiple third parties over whom you as the purchaser exercise little control. These parties include the seller, seller's counsel, outgoing lenders, the new lender, new lender's counsel and the management company, to name a few. Because there are so many independently operating parties who must come together and be ready to close the deal at the same time, a delay on the part of anyone can delay the closing and may even force an adjournment.

Pinpointing a specific closing date well in advance can be a complicated and inexact science. The sometimes tumultuous nature of scheduling closings can be a problem and even costly for purchasers where they are faced with an expiring commitment that will no longer be good at the time of closing. In the event that the deal cannot close before the expiration of the commitment, the purchaser may have to pay additional fees in order to secure a rate lock extension to make sure that financing is still available at a later date when the closing can actually occur.

In more dire circumstances, the purchaser may have to sign a new commitment, in which case the purchaser would be exposing itself to the changing market forces and may in fact end up with a worse rate than it had initially bargained for. In order to avoid both scenarios, purchasers should not treat the financing component of their purchase as wholly separate from the contractual part and should consult with their attorney before signing. The attorney will be able to give a more comprehensive picture of the pace of the transaction and let them know of possible roadblocks to closing, thus avoiding the pitfall of prematurely signing a commitment and facing the possibility of having it expire before the transaction is ready to close.

Second, consulting your attorney before signing the commitment can work to the purchaser's advantage because the attorney can use its relationships to negotiate better terms in the commitment than the purchaser may be able to garner for itself, ultimately resulting in a better loan. Often, the attorney is able to secure better terms because the attorney has had multiple interactions with the lender and has had the opportunity to negotiate beneficial terms on past deals. The purchaser who may have had limited experience in this regard and may not be aware that it can or should negotiate certain rights such as a smaller prepayment penalty window, or the right to transfer the property to family members without having to get the prior consent of the lender.

In sum, sometimes purchasers do not maximize the value of an attorney when purchasing residential property because they perceive the financing component and the contractual component as two mutually exclusive processes. In fact the purchaser's attorney can create value for the purchaser in both the negotiation of the contract terms as well as the negotiation of the financing terms.

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Administrative Department

Article 78 Proceedings

By: Phillip L. Billet

A building owner that deals with DHCR on a regular basis will often find itself in need of assistance from the New York State Supreme Court, either to appeal a DHCR order or to compel DHCR to act on a matter that is pending before it. An "Article 78" proceeding (i.e., a proceeding brought pursuant to Article 78 of the New York State Civil Practice Law and Rules) is the mechanism by which an owner can seek the Court's assistance in a DHCR matter.

Generally, there are two types of Article 78 proceedings relevant to DHCR: (1) a proceeding by which a party can seek review of a "final" DHCR order; and (2) a "mandamus" proceeding, by which a party can ask the Court to compel DHCR to decide a matter before it. This article will examine both types of proceedings.

Pursuant to CPLR Article 78, a party aggrieved by a final DHCR order may seek judicial review of that order in Supreme Court. There are, however, several rules of which an owner contemplating such a challenge must be aware.

The first rule is that an Article 78 proceeding may only be used to appeal a "final" DHCR order. DHCR orders may be divided into three categories – "initial" orders, "remand" orders and "final" orders.

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An initial order, which is usually issued by one of DHCR's "Rent Administrators," is an order that adjudicates a tenant's complaint or an owner's application. Examples of initial orders are an orders: deciding a tenant's complaint of a decrease in services; deciding an owner's application to restore rents that were previously reduced by DHCR; adjudicating an owner's "MCI" Application; adjudicating an owner's application to modify services at its building; adjudicating an owner's "MBR" Application; calculating the legal rent of an apartment and adjudicating a tenant's complaint of rent overcharge.

If a party wishes to appeal an initial order, it must do so by filing a "Petition for Administrative Review" (or "PAR") with DHCR, within 35 days of the issuance date of the initial order. A PAR will generally be decided by DHCR's Deputy Commissioner. Since an initial order does not represent DHCR's final determination on the matter at issue (as the order can be challenged by the filing of a PAR), it cannot be appealed by an Article 78 proceeding.

A remand order is a DHCR order which rules that a proceeding must be further reviewed by DHCR. Since a remand order likewise does not represent DHCR's final determination in a matter, it also may not be appealed by an Article 78 proceeding.

A final order is one which "finally" determines the rights of the parties. "Finality" requires that there remain no further DHCR act or determination necessary to conclude the rights of the parties. An example of a "final" order is an order which adjudicates a PAR. Thus, an Article 78 proceeding is often used to challenge a DHCR order which adjudicates a PAR.

The second rule is that an Article 78 proceeding must be commenced within 60 days of the issuance date of the order being challenged. If a party fails to commence its Article 78 proceeding within 60 days, DHCR will ask the court to dismiss the proceeding, and the court will generally do so, unless the party can demonstrate that it was never served with the final order or it was not served with the final order until well after the order was issued.

The third rule is that a court will uphold a DHCR order if it finds that the order was "rationally based." Even if the court concludes that it might have decided the case differently than DHCR, it will still uphold DHCR's decision if it finds that DHCR acted in a rational manner.

An DHCR order will be deemed "irrational," warranting reversal, if: (a) it is "arbitrary and capricious;" (b) it contains an error of law; (c) it was made in violation of lawful procedure; (d) DHCR abused its discretion in issuing the order; or (e) a hearing was conducted and evidence taken, and the order was not supported by "substantial evidence."

One example of a DHCR action being deemed "arbitrary and capricious" is where DHCR failed to follow its prior procedures and did not provide an explanation for its failure. Even though DHCR is not strictly bound by its prior precedent, there is a general rule which states that an agency which wishes to depart from its prior procedure may not do so without an explanation.

The final rule which an owner must be aware of is that a Court is not required to consider any argument that was not made during the proceedings before DHCR. Even if an owner has an excellent argument as to why a DHCR order should be reversed, the Court will not be required to consider this argument if the owner failed to make it during the proceeding before DHCR.

This means that, as a practical matter, when an owner files a PAR against an initial DHCR order, it should set forth every possible argument so as to preserve its rights in the event it finds it necessary to file an Article 78 proceeding at a later date.

in contrast to the above, a mandamus proceeding is a proceeding in which a party asks the Court to compel an administrative agency to perform a particular duty. The duty must be one which: (a) the agency is required by law to perform; and (b) does not involve the exercise of discretion.

The courts have determined that a party to a DHCR complaint or application may commence a mandamus proceeding asking the court to compel DHCR to decide the complaint or application. This is because (a) DHCR is required to decide a matter before it; and (b) DHCR's responsibility to decide a matter before does not involve the exercise of discretion. While DHCR has the discretion to decide how to decide a matter, it has does not have discretion to decide whether or not it may decide the matter.

In the case of a PAR proceeding, the Rent Stabilization Code specifically provides that if DHCR does not decide the PAR within 90 days, the Owner can consider the PAR to be denied and then commence an Article 78 proceeding challenging the "denial" of the PAR. As a practical matter, however, a Court will not decide whether the PAR was properly "denied" but, rather, will direct DHCR to render a decision on the PAR within a certain specific time.

When an owner commences a mandamus proceeding in order to compel DHCR to issue an order, DHCR will usually contact the owner and offer to settle the proceeding by agreeing to issue the order within a specific time period. Generally, an owner can expect to receive a DHCR order within five to six months after it commences a mandamus proceeding.

It should be noted, however, that the commencement of a mandamus proceeding and an agreement by DHCR to adjudicate the case within a certain time period, does not necessarily mean that DHCR will decide the case in a favorable manner.

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