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RENT STABILIZATION

First Department Splits on Four-Year Rule


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The Appellate Division, First Department recently issued two decisions, *Regina Metropolitan v. DHCR*, 164 AD3d 420 (First Dept. 2018) and *Raden v. W 7879*, 164 AD3d 440 (First Dept. 2018), which alter the method for determining the base date rent where there has been no fraudulent scheme to destabilize an apartment. Both cases stem from *Roberts v. Tishman Speyer,* 13 NY3d 270 (2009), where the Court of Appeals generally held that luxury deregulation is not available where a building is receiving J-51 benefits.

'Regina Metropolitan'

In *Regina Metropolitan*, the building received J-51 benefits from 1999 until 2013. The apartment in question was "luxury deregulated" in 2003 in accordance with the *Division of Housing and Community Renewal's* (DHCR) interpretation of the statute. Over time, the "deregulated" rent went above $5,000. Under *Roberts*, however, the apartment was in fact not deregulated.

The tenant filed an overcharge complaint with DHCR on Nov. 2, 2009, just after the Court of Appeals ruled in *Roberts*. This made the base date Nov. 2, 2005. The rent on that date was $5,195. The issue is *Regina Metropolitan* was how to determine the proper rent on the base date.

The owner asserted in the proceedings before DHCR that the base date rent should be $5,195. The owner argued that because the owner had not engaged in a fraudulent scheme to deregulate the apartment, whatever rent was charged on the base date should be the legal rent, even if it was an erroneous "fair market rent" at that time. Absent fraud, the four year look-back period could not be breached.

The tenant argued that the rent should be either (1) calculated pursuant to DHCR's default rent formula; or (2) frozen at the last stabilized rent of $2,096.47, because no registrations were filed once the owner illegally deregulated the unit. The tenant also sought treble damages and attorney fees.

DHCR adopted a middle ground. Finding that there was no fraudulent scheme to deregulate, DHCR started its calculations with the last stabilized rent of $2,096.47, which had been charged in 2003, well beyond the four-year look-back period. DHCR did so because it deemed that figure to be the last "reliable" stabilized rent. DHCR then added all subsequent lawful stabilized increases.

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This yielded a base date (Nov. 2, 2005) rent of $3,325.24. DHCR then calculated what the stabilized rent should be thereafter (again, including all lawful increases), and compared it to the rent actually paid. The total overcharge, including interest, was $283,192.59. Because there was no bad faith, DHCR did not award treble damages. Supreme Court (Schlesinger, J.) thereafter affirmed DHCR's order.

The Appellate Division majority (David Friedman, Marcy Kahn, and Peter Moulton) modified. In *Grimm v. DHCR*, 15 NY3d 358 (2010), the Court of Appeals held that the four-year look-back period could be breached where, *inter alia*, there has been a fraudulent scheme to deregulate an apartment. The majority in *Regina Metropolitan* reasoned that, conversely, where there was no fraudulent scheme, the base rent should be whatever was actually charged on the base date:

The Court of Appeals has made what we have called a 'limited exception' to the four-year limitations in cases where landlords act fraudulently. To expand this exception to landlords who have not engaged in fraud would create a much broader exception than would appear to negate the temporal limits contained in the Rent Stabilization Law (internal citations omitted).

The majority acknowledged that just last year, in *Taylor v. 72A Realty*, 151 AD3d 95 (First Dept. 2017), the First Department allowed a look-back of more than four years in the absence of fraud. The majority held that *Taylor* was contrary to *Grimm*, and was wrongly decided. Instead, the majority cited various First Department cases where the court, in the absence of fraud, had declined to look back more than four years before the filing of a rent overcharge complaint to set the base date rent. *See Stulz v. 305 Riverside Corp.*, 150 AD3d 558 (First Dept. 2017); *Matter of Park v DHCR*, 150 AD3d 105 (First Dept. 2017); *Todres v. W 7879, LLC*, 137 AD3d 597 (First Dept. 2016).

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The majority concluded: "Where, as here, there are insufficient indicia of a fraudulent scheme to evade rent regulation, there can be no consideration of the rental history beyond four years for the purpose of calculating a rent overcharge."

The majority, however, did not decide *how* to calculate the base rent, and sent the case back to DHCR. The court stated that "DHCR is not limited to calculating the base date rent according to the market rate that obtained pursuant to the parties' lease," and that "the agency has the discretion to implement other methods of base date rent calculations that do not run afoul of the limitations period." In other words, DHCR was authorized to calculate the base rent in any reasonable manner, as long as it did not look at rental events prior to the Nov. 2, 2005 base date.

The dissent, authorized by Justice Judith Gische, and joined by Justice Barbara Kapnick, held that DHCR's methodology was "fair," in that it put the parties in the same position they would have been in had DHCR properly advised landlords in the first place. The dissent also opined that *Taylor v. 72A Realty* had been correctly decided.

'Raden'

In the second case, *Raden v. W 7879 LLC*, the tenant raised an overcharge claim before Supreme Court in 2010. In 1997,

a tenant had moved into the unit at a "deregulated" rent of $2,444. Because the building was receiving J-51 benefits at that time, the apartment was, in fact, not deregulated. The complaining tenants moved into the apartment in 2005.

After the tenants commenced the action in 2010, the owner's attorney took the rent charged on the May 1, 2010 base date and deemed that to be the base rent. He then had the owner refund the overcharge and register the unit for several of the missing years.

After denying tenant's motion for summary judgment, the court (Kenney, J.) referred the matter to a referee to hear and report on the legal rent and the amount of overcharges. After a hearing, the referee determined that there was no fraud and no basis for treble damages. Because there was no fraud, the referee determined that the four-year look-back period could not be breached, as the majority later ruled in *Regina Metropolitan*. The referee held that the rent charged on May 1, 2006 base date would be the "market" rent that the tenant was being charged on that day. (Notably, in *Regina Metropolitan*, the majority held that the four-year look-back period could not be breached, but left it to DHCR to come up with an appropriate method for calculating the base rent.) The referee found a total overcharge of $448.50.

The Supreme Court affirmed the referee's methodology. On appeal, Justices John Sweeney, Richard Andrias, Kahn, and Moulton agreed with the referee's finding that "setting the free market rent in May 2006 was a reliable method of establishing the stabilized rent," and that "further look-back was inappropriate." The majority further held that for the reasons set forth in *Regina Metropolitan*, it preferred to follow its ruling in *Stulz v. 305 Riverside* rather than its ruling in *Taylor v. 72A Realty*.

In a brief dissent, Justice Rosalyn Richter cited to and agreed with the dissent in *Regina Metropolitan*.

Conclusion

Raden is important because the majority held that where there is no fraud, accepting the base date rent (even if it was an illegally high "market" rent for a "deregulated" apartment) is a lawful method for calculating the base rent and any subsequent overcharges. In *Regina Metropolitan*, the majority merely hinted that such an approach was permissible, but left it up to DHCR. Based on *Raden*, DHCR now knows that the *Raden* methodology will be favorably viewed by the First Department.

In *Raden*, the tenant has moved the First Department for leave to appeal to the Court of Appeals. In *Regina Metropolitan*, DHCR has also moved the First Department for leave to appeal, while the tenant has sought leave directly from the Court of Appeals. All of these motions are pending.