To be Argued by:
JEFFREY TURKEL
(Time Requested: 15 Minutes)

APL-2021-00169
Appellate Division–First Department Case No. 2020-03001
New York County Clerk's Index Nos. 111723/11 and 595472/17

Court of Appeals
of the
State of New York

KATHRYN CASEY, LAURIE CAGNASSOLA, GERALD COHEN, BETTY FURR, FRANCESCA GAGLIANO, CAROLYN KLEIN, JOSEPH MORGAN, RICHARD ROSE, JESSICA SAKS and KIRK SWANSON, on behalf of themselves and all others similarly situated,

Plaintiffs-Respondents,

– and –

PAMELA RENNA and VITTINA DEGREZIA aka VITTINA LUPPINO,

Intervenor-Plaintiffs,

– against –

WHITEHOUSE ESTATES, INC., KOEPPEL & KOEPPEL, INC., DUELL 5 MANAGEMENT LLC d/b/a DUELL MANAGEMENT SYSTEMS, WILLIAM W. KOEPPEL and EASTGATE WHITEHOUSE ESTATES, LLC,

Defendants-Appellants.

(For Continuation of Caption See Inside Cover)

BRIEF FOR DEFENDANTS-APPELLANTS AND THIRD-PARTY PLAINTIFFS-APPELLANTS

JEFFREY TURKEL
HOWARD W. KINGSLEY
ETHAN R. COHEN
ROSENBERG & ESTIS, P.C.
Attorneys for Defendants-Appellants and Third-Party Plaintiffs-Appellants
733 Third Avenue
New York, New York 10017
Tel.: (212) 867-6000
Fax: (212) 551-8484
jturkel@rosenbergestis.com
hkingsley@rosenbergestis.com
ecohen@rosenbergestis.com

WHITEHOUSE ESTATES, INC., EASTGATE WHITEHOUSE LLC and WILLIAM W. KOEPPEL,

Third-Party Plaintiffs-Appellants,

– against –

ROBERTA L. KOEPPEL, ALEXANDER KOEPPEL as Executors and Trustees of the Trust created under Article Fourth of the Last Will of Robert A. Koeppel, KOEPPEL MANAGEMENT COMPANY LLC and ROBERTA L. KOEPPEL individually,

Third-Party Defendants-Respondents.

CORPORATE DISCLOSURE STATEMENT

Pursuant to Rules 500.1(f) and 500.13(a) of the New York Court of Appeals Rules of Practice, the Defendants-Appellants and Third-Party Plaintiff-Appellants Whitehouse Estates, Inc., Koeppel & Koeppel, Inc., Duell 5 Management LLC d/b/a Duell Management Systems, and Eastgate Whitehouse LLC certify that:

1. Whitehouse Estates, Inc. has no parents or affiliates, but has a wholly owned subsidiary, Eastgate Whitehouse LLC.
2. Koeppel & Koeppel, Inc. has no parents, subsidiaries, or affiliates.
3. Duell 5 Management LLC d/b/a Duell Management System has no parents, subsidiaries, or affiliates, but has a prior-existing subsidiary, Duell Management Systems LTD.
4. Eastgate Whitehouse LLC has no subsidiaries or affiliates, but has a parent, Whitehouse Estates, Inc. Eastgate Whitehouse was also incorrectly sued herein as Eastgate Whitehouse Estates LLC.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Other Authorities

STATEMENT OF QUESTIONS PRESENTED

1. Where tenants bring an action for rent overcharge, but do not allege fraud in their complaint, amended complaint, or motion for summary judgment, is it proper for Supreme Court to *sua sponte* rule that the landlord has engaged in fraud, such that the default rent formula should be used to determine the base date rents of the apartments at issue?

Answer of the First Department:

The First Department answered this question in the affirmative.

2. Do the heightened pleading requirements of CPLR 3016(b) apply in a rent overcharge action, such that each element of fraud must be pleaded in detail?

Answer of the First Department:

The First Department answered this question in the negative.

3. Where this Court has fashioned a common-law exception to the four-year lookback period where a "fraudulent scheme to destabilize" an apartment has "tainted the reliability of the rent on the base date," can a finding of such scheme be premised on conduct occurring long *after* the base date, given that such conduct could not possibly affect the reliability of a base date rent charged years before?

Answer of the First Department:

The First Department answered this question in the affirmative.

4. Can the four-year lookback period be breached where there is no fraudulent scheme to destabilize an apartment, but there is instead an alleged "fraudulent rent overcharge scheme" that has no effect on stabilization status?

Answer of the First Department:

The First Department answered this question in the affirmative.

5. Where apartments were luxury deregulated based on DHCR's erroneous policy, can a landlord's 2012 registration of those units as rent stabilized, recalculation of stabilized rents, and issuance of stabilized leases, even if done erroneously, constitute a fraudulent scheme to destabilize, especially where it was not until this Court's 2020 decision in *Matter of Regina Metro. Co., LLC v New York State Div. of Hous. & Community Renewal*, 35 NY3d 332 (2020) ("*Regina*") that the method of recalculating the rents of such apartments was clarified?

Answer of the First Department:

The First Department answered this question in the affirmative.

6. Can a Court employ the default rent formula for 72 individual apartments because the landlord allegedly "failed to provide leases showing what the actual rent on the base date was," where the record in fact establishes that the landlord provided base date leases for 55 of those apartments?

Answer of the First Department:

The First Department answered this question in the affirmative.

PRELIMINARY STATEMENT

Defendants-appellants Whitehouse Estates, Inc. ("Estates"), Koeppel & Koeppel, Inc. ("K&K"), Duell 5 Management LLC d/b/a Duell Management Systems ("Duell"), William K. Koeppel ("Koeppel"), and Eastgate Whitehouse LLC ("Eastgate") (Estates and Eastgate collectively, "Owner") appeal from an August 5, 2021 order of the Appellate Division, First Department (R. 1370-85).

Plaintiffs-Respondents Kathryn Casey *et al.* (collectively, "Tenants") are rent-stabilized tenants of the subject building and class members herein.

Starting in 1996, the New York State Division of Housing and Community Renewal ("DHCR") advised landlords throughout New York that luxury deregulation was available in buildings receiving J-51 benefits. Owner herein followed that advice and deregulated 72 apartments in the subject building. In *Roberts v Tishman Speyer Props., L.P.*, 13 NY3d 270 (2009) ("*Roberts*"), however, this Court ruled that DHCR's advice was wrong.

Following a decade of confusion as to how to calculate the rents of erroneously deregulated apartments, this Court issued its watershed decision in *Regina*, setting forth three fundamental principles for calculating such rents.

This Court first restated the standard rule, premised on the language of the Rent Stabilization Law itself, that "the base date rent [is] the rent actually charged on the base date (four years prior to the initiation of the claim) and overcharges [are]

to be calculated by adding the rent increases legally available to the owner under the RSL during the four-year recovery period."

This Court also restated the sole exception to the standard rule, which applies where a landlord's "'fraudulent scheme to destabilize the apartment tainted the reliability of the rent on the base date.'" In such an instance, the base date rent is determined pursuant to DHCR's default rent formula.

Lastly, this Court ruled that a claim of fraud in a rent overcharge case is no different from any common law fraud claim, such that the tenant must affirmatively establish "'evidence [of] a representation of material fact, falsity, scienter, reliance and injury.'"

In its order, the First Department found two independent grounds for discarding the standard rule and using the default rent formula to calculate the October 14, 2007 base date rents herein. The Court first ruled that Owner had engaged in fraud -- although not a fraudulent scheme to destabilize -- by the manner in which Owner calculated rents and registered the subject apartments as stabilized in 2012. The Court also applied the default rent formula because Owner, allegedly, "failed to provide leases showing what the actual rent charged on the base date was."

For the reasons set forth below, the order of the First Department should be reversed.

As to fraud, it is undisputed that Tenants did not allege a fraudulent scheme to destabilize -- or fraud of any kind -- in their complaint, amended complaint, or motion for summary judgment. Notwithstanding, Supreme Court *sua sponte* found that Owner had engaged in fraud, and the First Department affirmed that finding. This was error. CPLR 3016(b) provides that a cause of action for fraud "shall be stated in detail." Tenants did not do so; nor did they allege, as *Regina* mandates, a representation of material fact, falsity, scienter, reliance, or injury. Quite simply, the issue of fraud was never properly before Supreme Court or the First Department and cannot be a basis for applying the default rent formula.

In addition, the First Department's finding of fraud is contrary to *Regina*'s sole exception to the standard rule. The exception exists because rents actually paid four years prior to the complaint should not be used as base date rents where pre-base date fraud tainted the reliability of those rents. Here, the First Department premised its fraud finding on Owner's 2012 registration and calculation of rents for the subject apartments. Owner's 2012 actions, however, could not possibly undermine the reliability of base date rents paid five years *earlier* on the October 14, 2007 base date. As such, the standard rule applies.

Certainly, Owner's alleged fraud herein -- recalculating stabilized rents, registering erroneously deregulated apartments as stabilized, and issuing stabilized leases -- does not qualify as a fraudulent scheme to *destabilize*. Notwithstanding,

the First Department held that *any* kind of purported fraud warranted application of the default rent formula. *Regina*, however, does not identify any other fraud-based exception to the standard rule, especially one that is broad enough to swallow the limited exception that this Court endorsed.

The First Department also found that the default rent formula applied because Owner "failed to provide leases showing what the actual rent charged on the base date was." The record flatly contradicts that finding. Tenants' own summaries of the documents Owner produced in discovery establish that Owner submitted the leases in effect on the October 14, 2007 base date for at least 55 of the 72 apartments at issue. As Justice Gische correctly recommended in her dissenting opinion herein, the matter should be remanded "to Supreme Court so that any remaining discovery and other pretrial matters can be completed."

This Court intended that *Regina* would provide a simple framework for deciding countless rent overcharge cases stemming from *Roberts*. Extensive post-*Regina* gloss, in this and other First Department cases, has vitiated much of this Court's 2020 decision. Reversal is warranted so that lower courts can be assured that *Regina* means what it says.

STATEMENT OF FACTS

A. The Parties

Whitehouse was formerly the ground-lessee and landlord of the building located at 350 East 52nd Street in Manhattan (the "Building") (R. 88-94, 140). K&K, Duell, and Koeppel are the former managing agents of the Building (R. 141). In September 2014, Whitehouse assigned its interests in the Building to Eastgate (R. 88-94, 1300).

Tenants are various rent-stabilized tenants of the Building (R. 139-40). Pursuant to Supreme Court's August 6, 2012 class certification order (R. 182-97), Tenants are comprised of:

> "All current, former, and future tenants of 350 E. 52nd Street whose apartments have been, are currently being, or will be, deregulated by, or subjected to attempts to be deregulated by, Defendants, their predecessors in interest, or their successors in interest, pursuant to Luxury Decontrol, while defendants are or have been in receipt of J-51 tax abatement benefits"

(R. 187).

B. Pursuant to DHCR's Guidance, Owner Deregulates Apartments while the Building Received J-51 Tax Benefits

The Building has 137 apartments, most of which were registered as stabilized in 1984 (R. 102-05, 339-42). From 1991 through June 30, 2014, the Building received J-51 tax benefits (the "J-51 Period") (R. 106-31).

During the J-51 Period, but before this Court's decision in *Roberts*, Owner deregulated approximately 72 apartments in the Building (the "subject apartments") when those apartments became vacant with a legal rent above the threshold for luxury deregulation (R. 367-446).[1] Owner did so in good faith reliance on DHCR's pre-*Roberts* interpretation of the governing statutes (R. 169, 1192-93).

C. Owner Notifies Tenants of *Roberts*, Calculates Stabilized Rents, and Begins to Register the Subject Apartments as Stabilized Immediately after the Retroactive Application of *Roberts* became Clear

This Court decided *Roberts* in 2009, holding that notwithstanding DHCR's guidance, landlords could not luxury deregulate apartments while a building received J-51 tax benefits (*see* 13 NY3d at 286-87). This Court expressly left open the question of whether its ruling should be applied retroactively (*id.* at 287). On August 18, 2011, the First Department ruled in *Gersten v 56 7th Avenue LLC*, 88 AD3d 189 (1st Dept 2011), *appeal withdrawn* 18 NY3d 954 (2012) ("*Gersten*"), that *Roberts* should be given retroactive application. On March 6, 2012, the *Gersten* appeal to the Court of Appeals was discontinued (*see* 18 NY3d 954 [2012]).

On September 28, 2011, right after the First Department decided *Gersten*, Owner wrote to Tenants advising them that (1) pursuant to *Roberts*, "units that were

[1] In June 2011, when filing its 2011 registrations, Owner inadvertently did not register Unit 2J as stabilized, despite having registered Unit 2J as stabilized in 2010 and every year prior thereto (R. 439). In March 2012, Owner retroactively registered unit 2J as stabilized for the year 2011 (R. 439). Every other subject unit that was deregulated (and/or not registered as stabilized) during the J-51 Period was deregulated prior to *Roberts* (R. 367-446).

switched to market rates will now be corrected back to stabilized rents;" and (2) Owner had hired a consultant (Stephen Trynosky) to calculate the legal rents for the subject apartments (R. 132-33). Owner's letter further stated:

> "This massive effort will take some time, but we anticipate that in a few weeks we will have recalculated the stabilized rate for each unit. Once finished, we will amend the registration statements with the City of New York and provide you with a new lease.
>
> If you have been overcharged, we will reimburse any overpayments and issue a new rent stabilized lease with a J-51 rider. If you signed a lease below the newly configured amount, we will honor the lower rent amounts now being paid. You will then be given a new stabilized lease, but with your lower 'preferential' rent number intact
>
> Although some tenants may soon be paying lower stabilized rates, other tenants will actually have higher rent numbers in the stabilization program, due to legal increases we may take. Again, even if the newly recalculated stabilization rate is higher, you will not be charged more than your current lease dictates for the balance of your present term…"

(R. 133 [emphasis in original]).

Mr. Trynosky, an expert with more than 20 years' experience calculating stabilized rents, made a good faith effort to calculate the rents of the subject apartments by "using the rent amount from the last time each apartment was registered as the starting rent" and "us[ing] the relevant allowances and guidelines as set forth by DHCR and the Rent Guidelines Board" (R. 1193, 1196-98). As of 2011, however, the correct methodology for recalculating stabilized rents for

apartments that were erroneously deregulated prior to *Roberts* was not settled, and would not be resolved until this Court's 2020 decision in *Regina*.

Owner began to prepare retroactive rent registrations for the subject apartments, using Mr. Trynosky's recalculations (R. 1197-98).

D. Tenants Commence this Action

On October 14, 2011, after Owner notified Tenants that their apartments were in fact stabilized, Tenants commenced this putative class action (R. 134-54). Accordingly, the base date for purposes of determining the legal rents of the subject apartments is October 14, 2007 (*see* RSC §§ 2520.6[f][1] and 2526.1[a][3][i]).

Tenants' first cause of action sought a declaration that "the apartments of Plaintiffs…and other members of the Class are subject to rent stabilization or rent control, and that Defendants are required to offer renewal leases on forms approved by the DHCR and required by the RSL at legal regulated rents" (R. 150, 152-53).

Tenant's second cause of action sought damages for rent overcharge (R. 151-53). Tenant's third cause of action sought attorneys' fees (R. 152-53).

Critically, as further detailed *infra* (*see* Point I, p. 29), Tenants did not allege in their complaint or amended complaint[2] that Owner had engaged in a fraudulent scheme to destabilize the apartments, or fraud of any kind (R. 134-54, 1296-1312).

[2] Tenants amended their complaint to add Eastgate as a defendant, with no other substantive changes (R. 284-301, 1296-1312).

E. Owner Registers the Subject Apartments as Rent Stabilized

By letter dated October 20, 2011, Mr. Trynosky provided Tenants with copies of the retroactive "DHCR rent filings for the past several years for your apartments," advising Tenants that (1) "[t]his, as you are aware is required by a recent court decision…;" and (2) "[a]ll new leases will be considered Rent Stabilized leases and appropriate Rent Stabilization rules administered by DHCR will henceforth be in effect…" (R. 155-56, 1198).

By November 1, 2011, Owner completed the 2006 registrations of the subject apartments and a majority of the 2007 registrations (R. 419-26, 1198). Owner registered as stabilized all apartments that had been deregulated during the J-51 Period, with legal rents based on Mr. Trynosky's calculations (R. 419-26, 1198).

F. Owner Answers the Complaint

Owner answered the Complaint on December 16, 2011 (R. 157-71). Owner's answer asserted, *inter alia*, that Owner "did, reasonably and in good faith, rely on…the pronouncements and conduct of DHCR and the New York City Department of Housing Preservation and Development in determining whether apartments could be deregulated" (R. 169), as well as other affirmative defenses (R. 166-70).

G. Counsel for Owner and Counsel for Tenants Send a Joint Letter to Tenants Advising them to Disregard Owner's Prior Letters and Calculations

On January 12, 2012, shortly after Tenants commenced this action, counsel for Owner and Tenants sent a joint letter to Tenants advising them that the letters

from Owner and Trynosky pertaining to the rent registrations and calculations "are hereby withdrawn" and "should be ignored" (R. 45, 173). The joint letter added that "[t]he attorneys for both sides agree that the calculation of past, current and future legal regulated rents at the building are the subject of pending litigation" (R. 173).

H. Owner Completes the Retroactive Registrations

By March 8, 2012, Owner filed with DHCR retroactive rent registrations for the subject apartments for the years 2006-2011, registering as stabilized all of the apartments that had been deregulated during the J-51 Period, with legal regulated rents based on Mr. Trynosky's calculations (R. 419-42, 864-1135, 1198).[3] Owner also offered Tenants stabilized leases with the recalculated rents (R. 486-863, 1198).

I. Supreme Court Grants Class Certification

On August 6, 2012, Supreme Court granted Tenants' motion for an order certifying the class action (R. 182-97).

[3] For the 2008 and 2009 registrations, Owner listed the calculated rent as the "Legal Regulated Rent" in response to question 8 of the registration form (*e.g.*, R. 870-71, 874-75, 878-79). For question 9a, which asked for the rent on April 1st of the year in question if different from the "Legal Regulated Rent," Owner listed the rent the Tenant *actually paid* on that date, denoting that rent as a "preferential rent" if it was less than the calculated "Legal Regulated Rent" (*e.g.*, R. 870-71, 874-75, 878-79). For the 2010 and 2011 registrations, Owner listed the calculated rent as the "Legal Regulated Rent" in response to question 8a of the registration form (*e.g.*, R. 872-73, 876-77, 880-81). However, Question 9a was eliminated from the 2010 and 2011 registration forms; for those years, Owner listed the rent actually paid on April 1st of the year in question as a "preferential" rent in response to question 8b on such form if the rent actually paid was less than the calculated "Legal Regulated Rent" (*e.g.*, R. 872-73, 876-77, 880-81).

J. The Parties Begin Discovery and Document Production

On or about January 3, 2013, Tenants served their first document demand on Owner (R. 198-207). Tenants, using the "reconstruction method" for recalculating the legal rents (discussed *infra,* p. 13-14), sought "records sufficient to determine what rents have been charged and collected from the first date when [any] apartment was deemed, considered, or treated deregulated through and including the present" (R. 204). In many instances, Tenants were demanding documents going back to the 1990s (R. 204, 367-446).

Supreme Court agreed with Tenants' methodology and issued a Preliminary Conference Order on July 3, 2013 directing Owner to produce records "of all apartments removed from rent regulation while a J-51 tax benefit was in effect," including (1) the "[l]ast rent regulated Tenant's lease;" (2) "other entitlements to raise rent under RSC establishing legal regulated rent;" and (3) all "leases executed for apartment [sic] that were de-regulated" (R. 208-10).

Tenants' discovery demands, and the Court's Preliminary Conference Order, employed the so-called "reconstruction method" to calculate the base date rents of the apartments at issue (*see, e.g., 72A Realty Assoc. v Lucas,* 101 AD3d 401, 402 [1st Dept 2012]). Under that method, rents are reconstructed "by identifying the last legal regulated rent before improper deregulation -- even though the apartment was deregulated more than four years prior to the imposition of the claim -- and applying

all permissible rent increases between the date of that regulated rent and the base date" (*Regina*, 35 NY3d at 358). Thus, if Owner improperly deregulated a unit at issue in 1994, the reconstruction method would take the last registered stabilized rent and add allowable stabilization increases to "bridge the gap" between that rent and what the rent would have been on the October 14, 2007 base date. Under this example, Owner would have to provide leases and other records preceding the base date by 13 years.

In *Regina*, this Court held that the reconstruction method was illegal.[4]

Owner began to produce documents to Tenants upon issuance of the Preliminary Conference Order and continued to produce documents following a May 21, 2014 status conference (R. 211-13).

By letter dated February 12, 2015 to Owner's counsel, Tenants' counsel acknowledged that Owner had "provided records as to 60 apartments," but asserted that "none of those records are sufficient to determine what rents have been charged and collected from the first date the apartment was deemed deregulated through the present" (R. 214-17). The alleged deficiency related to records necessary to calculate the legal rents pursuant to the illegal "reconstruction method," as opposed to those necessary to determine the rents actually charged on the base date.

[4] "The reconstruction method…violated the pre-HSTPA law by requiring review of rental history outside the four-year limitations and lookback period in the absence of fraud" (*Regina*, 35 NY3d at 358).

Owner's counsel responded on March 17, 2015 (R. 250-52), stating that:

> "I have requested all of the documents that our client has in their possession. I have been diligently reviewing these documents and as you can appreciate this is no small task. We hope to have an updated document production to you as soon as possible…"

(R. 252).

By letter dated March 23, 2015, Tenants' counsel implied that Tenants would seek relief from the Court if additional documents were not produced (R. 253-55).

Through February 2016, Owner continued to produce thousands of documents (R. 455-58, 1216-17, 1257-58).

K. Tenants Move for Discovery Penalties and Summary Judgment, Arguing that Owner Failed to Produce Records Sufficient to "Reconstruct" the Legal Rent

In December 2015, before the completion of document discovery and before any depositions were conducted, Tenants moved (1) to amend their complaint to add Eastgate as a defendant; and (2) for an order "pursuant to CPLR 3126 and 3212(a)":

> "granting Plaintiffs summary judgment on their first cause of action to the extent of granting a declaratory judgment with respect to the rent stabilized status of Plaintiffs' tenancies, and on their second cause of action to the extent of finding Defendants in default of their discovery obligations, finding that Plaintiffs' legal rents are to be calculated pursuant to the Default Formula, finding that Plaintiffs' rents should be frozen due to Defendants' failure to properly register their apartments, and calculating the amount of refund due to each Plaintiff and Plaintiff class member"

(R. 39-42).

Tenants' motion did not assert, let alone establish, that Owner engaged in fraud or a fraudulent scheme to destabilize, such that the Court should use the default rent formula (R. 41-87, 1313-49). Tenants instead argued that:

> "the Court should grant a declaratory judgment with regard to the regulatory status of Plaintiffs' apartments, and the Court should determine that Defendants are in default of their discovery obligations, and that Plaintiffs are entitled to summary judgment on their overcharge claims to the extent that their damages be calculated based upon the DHCR's Default Formula"

(R. 58, 1323).

Tenants' default claim was rooted in their unlawful demand under the reconstruction method that Owner produce hundreds, if not thousands, of documents that preceded the October 14, 2007 base date to reconstruct the base date rents. Tenants' motion repeatedly and incorrectly argued that "the correct methodology is to determine the last proper legal rent and 'bridge the gap' between that time and the base date by deeming allowable rent increases" (R. 1339). Tenants further argued that:

> "in order to establish the legal regulated rents for Plaintiffs' apartments, it is necessary to review the entire rental histories of those apartments. However, the records produced by Defendants are entirely inadequate to perform the necessary review and make the required calculations…
>
> Plaintiffs' attorneys have thoroughly analyzed the documents provided by Defendants. Defendants have not provided sufficient documents to calculate the legal

> regulated rent for a single apartment. It is therefore impossible to calculate the legal regulated rent amount for any apartment occupied by Plaintiffs or any member of the Plaintiff class, using the methodology required by the Appellate Division in *Lucas*…"

(R. 78-79, 1340-42).

Tenants concluded by arguing that "[t]he consequence of a landlord's failure to provide adequate records to establish the legal rent amount is that the legal rent is determined based upon the Default Formula" (R. 80, 1342).

Significantly, on December 8, 2015, as part of their motion for summary judgment, Tenants submitted an apartment-by-apartment summary of the leases that Owner *had* produced to Tenants to date (R. 256-78). Tenants' summary established that Owner had produced the lease in existence on the October 14, 2007 base date for at least 41 of the subject apartments (R. 257-67).[5]

L. After Moving for Discovery Penalties and Summary Judgment, Tenants Twice Stipulate that Owner could Produce Additional Documents, and Owner does so

While Tenants' motion was pending, the parties stipulated on December 22, 2015 that Owner "shall serve additional documents responsive to Plaintiffs' demand for documents" on or before January 15, 2016 (R. 455-56). Thereafter, by stipulation dated February 11, 2016, Tenants stipulated that "Defendants have

[5] The 41 apartments are: 1D, 2H, 2J, 2K, 3C, 3G, 3K, 4A, 5B, 5C, 5G, 6F, 6G, 6H, 7C, 7D, 7G, 8E, 8J, 8K, 9A, 9C, 9G, 9H, 10A, 10D, 10G, 10H, 11B, 12H, 12K, 14C, 14G, 14H, 14J, 15B, 15E, 15G, PHB, PHC, and PHD (R. 257-67).

discovered even further related documents and by February 22, 2016, Defendants shall serve additional documents responsive to Plaintiffs' demand…" (R. 457-58). Pursuant to these stipulations, Owner produced approximately 17,000 additional pages (R. 1216-17, 1257-58).

M. Owner Opposes Tenant's Motion for Discovery Penalties and Summary Judgment

In opposition to Tenants' motion, Owner argued:

- Owner had deregulated the subject apartments by relying in good faith on DHCR's guidance (R. 1192-93, 1217-18);
- Owner had, in good faith, complied with *Roberts* and its progeny by notifying Tenants of *Roberts* promptly after *Gersten* was decided, hiring a consultant to calculate the legal rents of the subject apartments, and registering the previously deregulated apartments as stabilized by March 2012 (R. 1192-93, 1196-98, 1214-19);
- The legal rents of the subject apartments should be determined using the "Four Year Rule," as Tenants did not allege that Owner engaged in fraud (R. 1216-18);
- Owner had produced documents sufficient to determine the base date rents of the subject apartments, and had in fact produced more than 17,000 additional pages *after* Tenants filed their motion (R. 1213-14, 1216-18);
- There were issues of fact as to Tenants' rent overcharge claims (R. 1213).

N. Tenants Reply

On reply, Tenants continued to rely upon the reconstruction method for their claim that Owner failed to supply documents sufficient to calculate the base date rents, such that the default rent formula applied (R. 1251-69). Tenants acknowledged that "[i]n January and February 2016, Defendants provided additional discovery documents" (R. 1257), but conclusorily argued (in an *unsworn* Memorandum of Law) that:

> "Plaintiffs' attorneys have reviewed and analyzed those records, which consisted of over 10,000 pages of documents. It has been concluded that Defendants have not provided any sufficient records to determine the legal regulated rent for any apartment occupied by Plaintiffs"

(R. 1257-58).

Counsel's self-serving assessment that Owner had not produced sufficient records to calculate the legal rents of the subject apartments (which assessment Supreme Court would ultimately adopt) was based upon Tenants' erroneous position that the reconstruction method applied (R. 1258). Tenants argued:

> "In order to determine the legal regulated rent for Plaintiffs' apartments, Defendants must provide the leasing records from the period of time when the apartment was timely registered as rent stabilized…Defendants must provide the market leases from the time the apartment was deregulated to date. In no case have Defendants provided a complete set of those documents as to any apartment"

(R. 1258).

Tenants also submitted on reply an updated summary of discovery documents that Owner had produced, submitting a list of "what documents are missing" (R. 1226, 1228-41). This summary conceded that Owner produced the lease in effect on the base date for an additional 14 subject apartments (in addition to the 41 subject apartments in Tenants' initial summary), as Tenants' summary did not list the October 2007 base date lease for these units as "missing" (R. 1228-41).[6]

Accordingly, Tenants have conceded that Owner produced base date leases for at least 55 of the subject apartments.

Tenants did not argue on reply that Owner committed fraud or engaged in a fraudulent scheme to destabilize the subject apartments (R. 1251-69).[7]

O. Supreme Court Grants Tenants' Motion, and Directs that Rents be Calculated Pursuant to the Default Rent Formula

By order dated March 23, 2017 (R. 9-38), Supreme Court (1) declared the subject apartments to be stabilized (which Owner did not dispute) (R. 18-20); (2) found that Owner engaged in fraud based on Owner's March 2012 retroactive re-registration of the subject apartments as stabilized and recalculation of legal rents

[6] The 14 apartments are: 3A, 3E, 3J, 4C, 4D, 5D, 8C, 11D, 12C, 12D, 12E, 12J, 14D, and 14E (R. 1228-39).

[7] On June 28, 2016, after the motions were fully briefed, the parties stipulated, and the Court so ordered, *inter alia*, that (1) Tenant's motion to amend the complaint "is granted on consent," and (2) "Plaintiffs' attorney is to file a corrected memo of law…" (R. 1350). Tenants filed a superseding memorandum of law in support of their motion (R. 1313-49), which superseded Tenants' prior memorandum of law in support (R. 48-87). On July 15, 2016, Owner filed its answer to Tenants' amended complaint (R. 1351-62).

(R. 26-27); (3) after purporting to have reviewed the thousands of documents Owner produced in discovery, agreed with Tenants' counsel's assessment that under the since-rejected reconstruction method, Owner had not produced sufficient records to determine the legal regulated rent of a *single* apartment (R. 22); and (4) held that as a result of Owner's fraud and inability to "reconstruct" the rents from the last stabilized lease, the default formula should be used to calculate the October 14, 2007 base rents (R. 27), finding:

> "[I]t was on March 8, 2012, that defendants filed back-dated rent registration statements for all 78 apartments with the DHCR for 2007-2011. By back-dating the apartment registrations for five years…defendants were seeking to (1) obviate an official determination that the building's apartments were and are rent stabilized; and (2) impose their own rent calculations, as the presumptively legal rent for the duration of the statutory four-year look-back period…
>
> The court finds this en masse filing a fraudulent attempt to (1) avoid the consequences of defendants' previous illicit deregulation of the 78 subject apartments herein; and (2) to use the RSL to prevent plaintiffs from challenging the rents that defendants had unilaterally calculated for those apartments. In other words, it satisfies the 'fraud' showing specified in *Grimm*…Following *Grimm*, the court finds that, because the rent history in this action is unreliable, the default formula should be used to determine the base rent date and to calculate the rent for each of the 78 subject apartments herein. The court directs a Special Referee to hear and report on such calculations"

(R. 27).

Supreme Court also held that the reconstruction method applied and that Owner had not produced sufficient records to reconstruct the rents of any of the subject apartments:

> "Plaintiffs acknowledge that [Defendants] did indeed provide a large volume of discovery material in January and February 2016; however they assert this material is nonetheless insufficient evidence from which to calculate the legal base rent of the building's 78 improperly deregulated apartments. After reviewing all the relevant discovery material, the court agrees with plaintiffs' assessment"

(R. 22 [emphasis supplied]).

It is hard to believe that Supreme Court reviewed "all the relevant discovery material" (R. 22). Neither party submitted those documents on summary judgment, and the documents produced by Owner in discovery (including the 17,000 pages produced in January and February 2016) were not part of the record.

Supreme Court did not assess whether the records produced by Owner were sufficient to determine the actual rent charged on the base date (the correct standard pursuant to *Regina*).

THE FIRST DEPARTMENT'S ORDER

On August 5, 2021, the First Department affirmed Supreme Court's Order in a 3-1 decision (R. 1370-85), with Justice Gische dissenting (R. 1378-85).

The First Department began its analysis by addressing an argument that Owner had never raised:

> "Defendant's primary argument on appeal is that the motion court erred in determining that the default formula applied, and instead the court should have used defendant's calculations of what the base date rent was in October 2007, because those calculations were made in good faith"

(R. 1373).

In fact, Owner argued that because Tenants had not claimed or established that Owner engaged in fraud, *Regina* mandated that the base date rents shall be the actual rents charged on the October 14, 2007 base date (C-14, 42-43, 48, 54-56).[8] As Justice Gische correctly recognized in dissent, Owner(s) "deny withholding any discovery and maintain there is enough information…to establish the base date rents" (R. 1381).

The First Department next affirmed Supreme Court's *sua sponte* finding of fraud, which Supreme Court premised on Owner's retroactive registration of the subject apartments in 2012:

[8] Citations to "C" are to the Compendium of the Appellate Division briefs submitted herewith.

> "Here…after commencement of the action, defendants, without court approval, unilaterally registered rents from the base date forward that were not the rents actually paid, and instead registered rents far higher, without explanation…[T]hese intentional misstatements of fact, which were intended to artificially increase the legal regulated rent, constitute fraud under *Grimm*.
>
> * * *
>
> We find that the motion court correctly determined that plaintiffs' legal regulated rent should be calculated according to the default formula set forth in RSC (9 NYCRR) § 2522.6(b). Although defendants may have been following the law in deregulating apartments during the period before *Roberts* was decided (see Regina, 35 NY3d at 356), their 2012 retroactive registration of the improperly deregulated apartments was an attempt to avoid the court's adjudication of the issues and to impose their own rent calculations rather than face a determination of the legal regulated rent within the lookback period"

(R. 1373-74).

The First Department tacitly conceded that *Regina* had invalidated the reconstruction method (R. 1373), but nevertheless affirmed Supreme Court's finding that Owner failed to produce sufficient records to determine the base date rent for *any* of the subject apartments -- even though the discovery Owner had produced was not in the record:

> "RSC 2522.6(b)(2) also calls for application of the default formula where '(i) the rent charged on the base date cannot be determined; or (ii) a full rental history from the base date is not provided.' Both of these scenarios apply here, and differ from situations in which the base date rent is known (*Regina*, 35 NY3d at 359 ["the alternative methods

> proposed by the tenants…reflected in the regulations…are available only [‘w]here the rent charged on the base date cannot be established’”]).
>
> * * *
>
> Here, the base date rent cannot be established because defendants failed to provide leases showing what the actual rent charged on the base date was, or whether the actual rent was known.
>
> * * *
>
> We find that the motion court correctly determined that plaintiffs’ legal regulated rent should be calculated according to the default formula…Although defendants maintain that they provided evidence showing the legal regulated rent on the base date on which the motion court should have relied, the DHCR rent history for the apartments within the four-year lookback period shows that the rents beginning in 2007, four years before the complaint was filed, were registered in 2012, based on defendant’s unilateral calculations and not the actual rent charged
>
> * * *
>
> [D]efendants’ actions were more than simply imperfect registrations, and as a whole the evidence was sufficient to satisfy plaintiffs’ burden on summary judgment. Defendants failed to produce leases for the class reflecting the actual rent charged on the base date, October 14, 2007”

(R. 1373-76 [emphasis supplied]).

The First Department concluded:

> “Based on defendants’ conduct, and in light of the absence of evidence in the record as to the actual rent charged on the base date by which to calculate legal regulated rents under RSC 2526.1(a)(3)(i), plaintiffs’ overcharges, if any, must be determined according to the default formula set forth in RSC 2522.6(b)…

> In view of the foregoing, defendants' fourteenth, fifteenth, and seventeenth defenses affirmative defenses, asserting their good faith and compliance with the Division of Housing and Community Renewal's interpretation of the law during the relevant period, were correctly dismissed…"

(R. 1376-77 [emphasis supplied]).

The Hon. Justice Gische filed a lengthy dissent finding no fraud:

> "I disagree that plaintiffs met their burden on summary judgment. They failed to present any evidence of defendants' fraud.
>
> * * *
>
> Plaintiffs' fraud claim rests almost entirely on uncontroverted evidence that the defendants began treating numerous apartments as deregulated sometime between 1993 and 2011 while receiving tax benefits. This is precisely what *Regina* instructs is not evidence of willfulness to establish common-law fraud. *Regina* clearly provides that in the absence of fraud, neither the DHCR formula nor the reconstruction method may be applied. To do so "violate[s] the pre-HSTPA law by requiring review of rental history outside the four-year limitations and lookback period" and "no award or calculation of an award of the amount of an overcharge may be based on an overcharge having occurred more than four years before (former RSL § 26–516[a][2]; *see* former CPLR 213–a)" (*Regina* at 358)"

(R. 1381-82).

Justice Gische continued:

> "*Regina* dictates that in case of a good-faith deregulation in a J-51 context, a market rent charged on the base date may be used to calculate the legal regulated rent…It is completely unclear in this record that the *Regina* mandated

> rent calculation is not possible for all of the apartments in the class, so that application of a building-wide default formula is necessary.
>
> Since plaintiffs have not proved that defendants committed fraud, whether in 2009, or with respect to the latter reregistration, Supreme Court erred in applying DHCR's default formula or ordering reconstruction of each apartment's rent history. The rent history reconstruction method was expressly rejected in *Regina*. The correct way to determine the tenant's legal regulated rent and any overcharge is by using "the rent actually charged on the base date (four years prior to initiation of the claim)," as former CPLR 213-a provided, here October 14, 2007, and then "adding the rent increases legally available to the owner under the RSL during the four-year recovery period" (*Regina* at 355-356; *AEJ*, 194 AD3d at 472)"

(R. 1384-85).

The dissent concluded:

> "Given Supreme Court's sweeping determination that the entire rent history of the deregulated apartments had to be reconstructed going back to when they were deregulated, possibly in the mid-1990's[,] I believe that Supreme Court's order directing calculation of rent overcharges is incorrect and should be reversed. It is unclear whether the records made available by either party provide enough information to determine the base date rent in accordance with *Regina* for any of the subject apartments. Given those circumstances, I would remand this matter to Supreme Court so that any remaining discovery and other pretrial matters can be completed"

(R. 1385).

ORDER GRANTING LEAVE
TO APPEAL TO THE COURT OF APPEALS

By Order entered October 7, 2021, the First Department granted Owner's motion for leave to appeal to the Court of Appeals (R. 1368-69).

POINT I

TENANTS DID NOT PLEAD FRAUD IN THEIR COMPLAINT OR ASSERT FRAUD IN THEIR MOTION FOR SUMMARY JUDGMENT, AND IMPROPERLY ALLEGED FRAUD FOR THE FIRST TIME ON APPEAL

A. Tenants did not Argue before Supreme Court that Owner Engaged in Fraud

Tenants did not plead fraud of any kind in their complaint or amended complaint, much less a fraudulent scheme to destabilize (R. 134-54, 1296-1312). Their complaints mention "fraud" twice. First, Tenants recited that DHCR's default rent formula can be used "where the legal rent on the base date cannot be determined, either because records of the legal rent do not exist, were not provided, were inherently unreliable, or were created by fraud or the owner's violations of the law" (R. 144-45, 1303). That is a characterization of applicable law, not an allegation of fraud.

Second, Tenants stated:

> "Upon information and belief, the base date rents for the 72 improperly deregulated apartments cannot be determined because of the lack of reliable records of the legal rent, fraud, and/or intentional violations of the law on the part of Defendants and their predecessors…"

(R. 146, 1305).

CPLR 3016(b) governs the heightened pleading requirements relating to fraud, providing: "[w]here a cause of action or defense is based upon

misrepresentation, fraud, mistake, willful default, breach of trust or undue influence, the circumstances constituting the wrong shall be stated in detail."

Tenants' sole conclusory reference to fraud -- stated upon "information and belief," no less -- does not satisfy the heightened pleading standard of CPLR 3016(b) (*see Brennan v 3250 Rawlins Ave. Partners, LLC*, 171 AD3d 603, 604 [1st Dept 2019]). Moreover, Tenants never asserted a fraudulent scheme to destabilize.

Nor did Tenants allege fraud in their motion for summary judgment, which Tenants made *before* the parties completed discovery (R. 48-87, 1313-49). In Point IV.D of their June 28, 2016 Memorandum of Law in support (R. 1342-45), and in their reply (R. 1264-65), Tenants clarified that their default rent formula claim was based on Owner's purported failure to submit rent records sufficient to reconstruct the legal rent, *not* on fraud:

> "As clearly laid out in the RSC, the Default Formula is to be applied not only where a landlord committed fraud or engaged in a scheme to evade rent regulations, but also in any case where the rental history records sufficient to establish the base date are unreliable or unavailable.
>
> * * *
>
> Accordingly, because Defendants have failed to produce adequate and credible rental records sufficient to determine the legal base rent for Plaintiffs' apartments, the rents must be calculated pursuant to the Default Formula"

(R. 1344-1345).

Although Tenants did not plead fraud, or argue fraud on summary judgment, Supreme Court *sua sponte* found that "plaintiffs have demonstrated the necessary quantum of 'fraud'" to justify using the default rent formula (R. 26). This was error.

As Appellate Term held in *150 E. Third St LLC v Ryan,* 71 Misc3d 1, 4 (App Term, 1st Dept 2021):

> "The trial court erred in considering the rental history for the apartment beyond the four-year lookback period. Tenants' pre-HSTPA answer did not allege that there was any fraudulent scheme to deregulate the apartment (*see* CPLR 3018[b]), and Tenants never moved to amend their answer to assert fraud during the one and one-half years the proceeding was pending prior to the enactment of the HSTPA. Moreover, no mention of fraud was made in the parties' detailed stipulation, which was prepared by the attorneys for the parties. Under the circumstances the trial court should not have considered Tenants' belated contention of fraud, which was raised for the first time in Tenants' posttrial motion."

B. Pursuant to *Regina*, Each Element of Common Law Fraud Must be Established in order to Find Fraud in Rent Overcharge Cases

Supreme Court's *sua sponte* finding of fraud resulted from its mistaken belief that fraud in a rent overcharge case fundamentally differs from a claim of common law fraud. Supreme Court wrote that "in cases of rent overcharge, the 'fraud' to which the parties refer is essentially a term of art that has arisen in Court of Appeals case law on the subject" (R. 23). Following Supreme Court's analysis of that case law -- *Thornton v Baron*, 5 NY3d 175 (2005); *Matter of Grimm v New York State Div. of Hous. & Community Renewal*, 15 NY3d 358 (2010); and *Conason v Megan*

Holding, LLC, 25 NY3d 1 (2015) -- Supreme Court concluded that "fraud, in the context of rent-overcharge claims, refers to the test in *Grimm* for determining whether a party has made a showing sufficient to warrant examination of an apartment rental history further back than the four-year look-back period specified in the RSL" (R. 23-25). *Regina* establishes that Supreme Court was wrong.

In *Regina*, after analyzing the "fraudulent scheme to destabilize" exception to the four-year look-back period, this Court noted:

> "Fraud consists of 'evidence [of] a representation of material fact, falsity, scienter, reliance and injury" (*Vermeer Owners v Guterman*, 78 NY2d 1114, 1116, 570 NYS2d 128, 585 NE2d 377 [1991]; *see e.g. Ambac Assur. Corp. v Countrywide Home Loans, Inc.*, 31 NY3d 569, 81 NYS3d 816, 106 NE3d 1176 [2018]; *Pasternack v Laboratory Corp. of Am. Holdings*, 27 NY3d 817, 827, 37 NYS3d 750, 59 NE3d 485 [2016])."

(35 NY3d at 356, n 7).

Regina thus establishes that an allegation of fraud in a rent overcharge case is the same as any common law fraud claim, and "must be pleaded with the requisite particularity under CPLR 3016(b)" (*Eurycleia Partners, LP v Seward & Kissel, LLP*, 12 NY3d 553, 559 [2009]). As such, CPLR 3016(b) applies and requires that the alleged fraud be "stated in detail." Tenants' bare-bones allegation in the complaint and amended complaint does not satisfy the statute.

Moreover, *Regina* establishes that a finding of fraud in a rent overcharge case must be based upon "evidence [of] a representation of material fact, falsity, scienter,

reliance and injury" (35 NY3d at 356, n 7). Here, Tenants did not put forward, let alone establish, evidence of the elements of fraud in their motion for summary judgment.

Following *Regina*, Courts have applied CPLR 3016(b) to rent overcharge claims. In *Gridley v Turnbury Vil., LLC*, 196 AD3d 95 (2d Dept 2021), *lv denied* 2021 NY Slip Op 75990, ___ NY3d ___ (2021), the Second Department held that in a rent overcharge case, "[t]he elements of fraud must be pleaded, and each element must be set forth in detail (*see* CPLR 3016[b]; *699 Venture Corp. v Zuniga*, 69 Misc3d 863, 869 [Civ Ct, Bronx County 2020]). That requirement was not met in this case" (196 AD3d at 101). Nor was that requirement met here (*compare Henry 85 LLC v Roodman*, 2021 WL 4776230, *4 [Sup Ct, Kings County 2021]).

Ordinarily, a fraud claim that does not comply with CPLR 3016(b) is subject to dismissal (*see Eurycleia Partners, LP v Seward & Kissel, LLP*, 12 NY3d at 557). Here, because Tenants did not allege fraud on their motion for summary judgment, Owner was not required to rebut the elements of fraud, and Supreme Court's finding of fraud was in error.

C. The First Department Erred in Considering Tenants' Fraudulent Scheme to Destabilize Argument

In their February 3, 2021 brief to the First Department, Tenants argued for the first time in this litigation -- which they had commenced a decade earlier -- that Owner "engaged in a fraudulent scheme" (C-105). Although Owner argued that

Tenants had improperly raised this claim for the first time on appeal (C-137-40), the First Department affirmed Supreme Court's *sua sponte* finding (R. 1373-76).

It is well-settled that "arguments not presented to the motion court on an application for summary judgment are not properly raised for the first time on appeal" (*Tortorello v Carlin*, 260 AD2d 201, 205 [1st Dept 1999]; *see P.T. Cent. Asia v Chinese American Bank*, 229 AD2d 224, 229 [1st Dept 1997]). A party may not argue on appeal a theory never advanced before the court of original instance (*see Admiral Ins. Co. v Marriot Intl., Inc.*, 79 AD3d 572 [1st Dept 2010], *lv denied* 17 NY3d 708 [2011]); *Sean M. v City of New York*, 20 AD3d 146, 150 [1st Dept 2005]). This is especially true where, as here, the newly raised claim could have been obviated or cured by factual showings or legal countersteps in the trial court (*see U.S. Bank N.A. v Brown*, 186 AD3d 1038, 1040 [4th Dept 2020]; *Robles v Brooklyn-Queens Nursing Home, Inc.*, 131 AD3d 1032, 1033 [2d Dept 2015]). Fraud, of course, is an inherently factual issue.

Accordingly, the First Department erred in (1) considering Tenants' fraud argument raised for the first time on appeal; and (2) affirming Supreme Court's *sua sponte* finding of fraud.

POINT II

AS A MATTER OF LAW, THERE WAS NO FRAUDULENT SCHEME TO DESTABILIZE HEREIN

A. *Regina*'s Standard Four-Year Rule in Rent Overcharge Cases

In *Regina,* this Court set forth the standard rule for determining the legal regulated rent in pre-HSTPA overcharge claims. Citing RSL § 26-516(a)(i) and DHCR's Rent Stabilization Code ("RSC"), this Court wrote:

> "With exceptions not relevant here, the regulations provided that '[t]he legal regulated rent for purposes of determining an overcharge shall be deemed to be the rent charged on the base date, plus in each case any subsequent lawful increases and adjustments' (RSC § 2526.1[a][3][i] [emphasis added]; *see also id.* § 2520.6[e]). Under the pre-HSTPA law, the base date rent was therefore the rent actually charged on the base date -- i.e. four years prior to the overcharge complaint -- even if no registration statement had been filed reflecting that rent"

(*Regina*, 35 NY3d at 354).

B. *Regina's* Sole Fraud-Based Exception to the Standard Rule: A Fraudulent Scheme to Destabilize

The *Regina* Court next restated the sole fraud-based exception to the standard rule. Summarizing its prior holdings in *Thornton, Grimm, Conason,* and *Matter of Boyd v New York State Div. of Hous. & Community Renewal*, 23 NY3d 999 (2014), this Court held:

> "The rule that emerges from our precedent is that, under the prior law, review of rental history outside the four-year lookback period was permitted only in the limited

> category of cases where the tenant produced evidence of a fraudulent scheme to deregulate and, even then, solely to ascertain whether fraud occurred -- not to furnish evidence for calculation of the base rent or permit recovery for years of overcharge barred by the statute of limitations (*Grimm*, 15 NY3d at 367). In fraud cases, this Court sanctioned use of the default formula to set the base date rent. Otherwise, for overcharge calculation purposes, the base date rent was the rent actually charged on the base date (four years prior to the initiation of the claim) and overcharges were to be calculated by adding the rent increases legally available to the owner under the RSL during the four-year recovery period. Tenants were therefore entitled to damages reflecting only the increases collected during that period that exceeded legal limits"

(*Regina*, 35 NY3d at 355-356).

Regina thus holds that where there is no fraudulent scheme to destabilize, the rent actually charged on the base date four years prior to the overcharge claim shall be the base date rent and the basis for all overcharge calculations. Where a fraudulent scheme to destabilize is present, the base date rent is calculated pursuant to DHCR's default rent formula, codified at RSC §§ 2522.6(b) and 2526.1(g).

C. There was no Pre-Base Date Fraudulent Scheme to Destabilize herein

The base date in this appeal is October 14, 2007 (R. 135), which pre-dates *Roberts* by two years. In *Regina,* this Court held that as a matter of law, a landlord's pre-*Roberts* luxury deregulation of rent regulated apartments in a J-51 building did not constitute a fraudulent scheme to destabilize:

> "Deregulation of…apartments during receipt of J-51 benefits was not based on a fraudulent misstatement of fact but on a misinterpretation of law -- significantly, one that DHCR itself adopted and included in its regulations"

(35 NY3d at 356; *see Montera v KMR Amsterdam LLC*, 193 AD3d 102, 105 [1st Dept 2021] ["in pre-*Roberts* cases where landlords relied on DHCR guidance there could be no fraudulent scheme to deregulate"]; *see also Gridley v Turnbury Vil., LLC*, 196 AD3d at 101).

Moreover, there is no evidence, and no court has found, that Owner's pre-*Roberts* deregulations were based on anything other than Owner's reliance on "DHCR's own contemporaneous interpretation of the relevant laws and regulations" (*Matter of Park v New York State Div. Hous. & Community Renewal*, 150 AD3d 105, 115 [1st Dept 2017], *lv dismissed* 30 NY3d 961 [2017]; *see Stultz v 305 Riverside Corp.*, 150 AD3d 558 [1st Dept 2017], *lv denied* 30 NY3d 909 [2018]).

D. An Alleged Fraudulent Scheme to Destabilize cannot Occur after the Base Date

1. The First Department's Ruling herein

The First Department held that although Owner did not commit fraud before the base date, Owner allegedly did so *five years later*:

> "Although defendants may have been following the law in deregulating apartments during the period before *Roberts* was decided, their 2012 retroactive registration of the improperly deregulated apartments was an attempt to avoid the court's adjudication of the issues and to impose

> their own rent calculations rather than face a determination of the legal regulated rent within the lookback period"

(R. 1374).

For the reasons set forth below, the First Department was wrong.

2. The First Department's Order Violates *Regina's* Standard Rule

Regina teaches that in rent overcharge cases, the base date is all. Under the standard rule, absent a fraudulent scheme to destabilize, the base date rent shall be the rent actually charged to the tenant on the date "four years prior to the overcharge claim," as thereafter adjusted by increases "legally available to the owner under the RSL" (35 NY3d at 354, 356). This Court created the fraud-based exception to the standard rule because pre-base date fraud could render unreliable the rent the tenant paid on the all-important base date. This Court so ruled in *Grimm*, 15 NY3d at 167, and reaffirmed that holding in *Regina*:

> "We elaborated on this fraud exception to the lookback rule in *Matter of Grimm v New York State Div. of Hous. & Community Renewal*, holding that where a tenant has made a 'colorable claim of fraud' by identifying 'substantial indicia,' i.e., 'evidence,' of 'a landlord's fraudulent deregulation scheme to remove an apartment from the protections of rent stabilization,' that apartment's 'rental history may be examined for the limited purpose of determining whether a fraudulent scheme to destabilize the apartment tainted the reliability of the rent on the base date.' Consistent with *Thornton*, we directed that, if reviewing the rental history revealed such a fraudulent scheme, the default formula should be used to calculate any resulting overcharge"

(35 NY3d at 355 [emphasis supplied]).

After *Grimm*, DHCR promulgated RSC § 2526.1(a)(2)(iv), which states that the four-year lookback period can be breached to determine "whether a fraudulent scheme to destabilize the apartment…rendered unreliable the rent on the base date."

The First Department's finding of post-base date fraud violates *Regina's* standard rule. Because there was no pre-base date fraudulent scheme to destabilize -- and the First Department did not find to the contrary -- the rents Tenants actually paid on the October 14, 2007 base date are *untainted and reliable*. Nothing Owner did or did not do in 2012 could possibly alter that. It is thus highly ironic that the First Department cited *Grimm* to support its finding of post-base date fraud and the use of DHCR's default rent formula:

> "As properly found by the motion court, [Owner's] conduct fulfilled the Court of Appeals test in *Grimm* that:
>
> > 'What is required is evidence of landlord's fraudulent deregulation scheme to remove an apartment from the protections of rent stabilization [in which case] the rental history may be examined for the limited purpose of determining whether a fraudulent scheme to destabilize the apartment <u>tainted the reliability of the rent on the base date</u>'"

(R. 1375 [emphasis supplied]).

Because Owner's post-base date actions could not taint the reliability of the rents actually charged and paid on the 2007 base date, the standard rule applies.

Rents must thus be computed using the actual base date rents plus allowable increases, if any, under the RSL.

The First Department's obvious displeasure with Owner's 2012 retroactive registrations and rent calculations (discussed *infra*, pp. 43-54) did not justify the Court's deviation from *Regina*. The standard rule provides that where the base date rent is untainted by fraud, a tenant's legal rent "shall be deemed to be the rent charged on the base date, plus in each case any subsequent lawful increases and adjustments" (RSC § 2526.1[a][3][i]). As to post-base date misconduct, if any, the standard rule relies on existing RSL penalties that increase overcharge awards and deprive landlords of post-base date rent adjustments that are otherwise lawful.

Specifically, if a landlord's post-base date conduct results in overcharges, RSL § 26-516(a) mandates that DHCR or the Court shall assess "a penalty equal to three times the amount of such overcharge" unless the landlord proves that the overcharge was not willful (*see Matter of Century Tower Assoc. v New York State Div. of Hous. & Community Renewal*, 83 NY2d 819, 823 [1994]). That is the penalty that the Legislature deemed appropriate, rather than deviating from the standard rule. Here, Tenants waived treble damages so that this matter could proceed as a class action (R. 151, 186-91, 1310). That was their choice.

Similarly, Owner's purportedly improper or untimely registrations are governed by RSL § 26-517(e), which states that a landlord's "failure to file a proper

and timely initial or annual rent registration" shall result in a rent freeze "until such time as such registration is filed." As Justice Gische wrote in her dissent in *Montera*:

> "I fully recognize that an owner's failure to register the premises with DHCR is a violation of the rent stabilization laws and code, but there is an independent statutory remedy for such transgressions…
>
> RSL § 26-517(e) specifies the remedy. It provides that '[t]he failure to file a proper and timely…registration statement' precludes an owner from collecting rent increases until the registration is filed.' Defendant's failure to register in itself does not permit a court's review of the rent history of this apartment prior to November 29, 2013…Since there is already a statutory remedy for non-registration, there is no reason to devise an alternative method of relief"

(193 AD3d at 116-17).

Regina confirms that Justice Gische was right:

> "The method for calculating the amount of recoverable damages--i.e., the overcharge--is governed by the RSL.
>
> * * *
>
> We therefore decline to create a new exception to the lookback rule and instead clarify that, under pre-HSTPA law, the four-year lookback rule and standard method of calculating legal regulated rent govern in *Roberts* overcharge cases, absent fraud."

(35 NY3d at 351-52, 361).

Accordingly, the First Department erred in finding that Owner's alleged post-base date fraud warranted application of the default formula.

POINT III

EVEN IF POST-BASE DATE ACTIONS CAN CONSTITUTE A FRAUDULENT SCHEME TO DESTABILIZE, THERE WAS NO SUCH SCHEME HERE

The First Department ruled that Owner had engaged in a fraud by (1) retroactively registering the apartments as stabilized in 2012 without court approval; and (2) registering erroneously calculated rents (R. 1373-76). As Owner establishes below, the First Department was in error.

A. Owner's March 2012 Registrations and Rent Calculations were a Prompt and Good-Faith Effort to Comply with *Roberts* and *Gersten*

When the Court of Appeals decided *Roberts* on October 22, 2009, it noted that the Court's decision left open the issue of whether its ruling should be given retroactive effect (13 NY3d at 287). In *Gersten*, decided August 18, 2011, the First Department answered that question in the affirmative (88 AD3d at 198). On March 6, 2012, the *Gersten* appeal to the Court of Appeals was withdrawn and discontinued (*see* 18 NY3d 954 [2012]). Here, Owner retroactively registered all of the subject apartments as stabilized by March of 2012 (R. 419-42, 864-1135), promptly after *Gersten* was decided.

It is difficult to understand how Owner's (1) registration of the apartments in question as stabilized; (2) calculation of stabilized rents in good faith; and (3) issuance of stabilized leases -- even if all done erroneously -- can constitute a

fraudulent scheme to *destabilize* these units. Owner's actions are the logical antithesis of a destabilization scheme.

As Justice Gische wrote in her dissent herein, "Defendant's filing of the amended registrations evinces an effort to comply with law once *Gersten* made it clear that *Roberts* had retroactive effect" (R. 1383).

Ironically, the First Department has consistently held that it would have been fraud had Owner *not* registered the apartments in the building as stabilized after *Gersten* was decided (*see Nolte v Bridgestone Assoc. LLC*, 167 AD3d 498, 498-499 [1st Dept 2018] ["The record shows that defendant failed to promptly register the apartments and 30 other apartments in the building as rent-stabilized in March 2012, when the applicability of *Roberts* was clear"]; *see also Montera v KMR Amsterdam LLC*, 193 AD3d at 105-06; *Kreisler v B-U Realty Corp.*, 164 AD3d 1117 [1st Dept 2018], *lv dismissed* 32 NY3d 1090 [2018]).

B. Owner did not Seek to Avoid a Judicial Determination as to how Rents were to be Calculated and Registered

Particularly puzzling is the First Department's ruling that Owner engaged in fraud because (1) Owner registered the apartments and calculated rents in 2012 "without court approval" (R. 1373); and (2) Owner's "2012 retroactive registration of the improperly deregulated apartments was an attempt to avoid the Court's adjudication of the issues and to impose their own rent calculations rather than face the determination of the legal regulated rent within the lookback period" (R. 1374).

First, the RSL does not require a landlord in a *Roberts*-type case, or in any other type of case, to obtain court approval before registering apartments as stabilized or re-calculating stabilized rents.

More to the point, Owner did not attempt to avoid judicial adjudication of the lawful stabilized rents. Tenants commenced this action on October 14, 2011 (R. 135), and Owner began registering the subject apartments on or about November 1, 2011 (R. 419-26). On January 12, 2012, almost a decade before the First Department's Order, counsel for Owner and Tenants sent a joint letter to Tenants stating that (1) Owner's prior correspondence to Tenants regarding rent calculations and registrations "are hereby withdrawn" and "should be ignored;" and (2) "[t]he attorneys for both sides agreed that the calculation of past, current and future legal regulated rents at the building are the subject of pending litigation" (R. 45, 173).

As such, Owner acknowledged ten years ago that rents would be determined by the Court, not by Owner's calculations or registrations. Owner did not seek to evade adjudication or "impose" rent calculations on Tenants who were represented by knowledgeable counsel in a rent overcharge action that Tenants had already commenced. The First Department erred in finding otherwise.

C. Owner's Good-Faith Attempts to Calculate and Register Stabilized Rents did not Constitute a Fraudulent Scheme to Destabilize

Neither *Roberts* nor *Gersten* provided any clue as to how to calculate rents for apartments that landlords had erroneously deregulated pursuant to DHCR's guidance prior to *Roberts*. "After *Roberts* there was understandable confusion how the decision should be implemented, including whether *Roberts* should be given retroactive effect and, if so, how that should be accomplished" (*Regina*, 35 NY3d at 357). That confusion continued until 2020, when *Regina* restated both the standard rule and the sole fraud-based exception thereto, clarifying that: (1) "the four-year lookback rule and standard method of calculating legal regulated rent govern in *Roberts* overcharge cases, absent fraud" (*id.* at 361); and (2) "review of rental history outside the four-year lookback period was permitted only in the limited category of cases where the tenant produced evidence of a fraudulent scheme to deregulate…Otherwise, for overcharge calculation purposes, the base date rent was the rent actually charged on the base date" (*id.* at 355-356).

Owner registered the apartments and calculated the rents in 2011 and 2012, during the "understandable confusion" following *Roberts* and *Gersten*. Owner promptly hired an experienced consultant, who made a good-faith effort to calculate the legal rents "using DHCR's guidelines for all the apartments that were again

subject to rent stabilization following the *Roberts v Tishman* decision and its progeny" (R. 1193, 1196).

Notwithstanding the lack of judicial or administrative guidance as to how to register apartments and calculate rents, the First Department held that Owner's "retroactive rent registrations…reflected rents significantly higher than those actually charged, and some purported to classify the actual rent as a 'preferential rent' to justify registration of the higher amount" (R. 1376). In fact, Owner's retroactive rent registrations calculated the legal rents in good faith, listed the calculated rents as the "Legal Regulated Rents," and also advised DHCR of the actual rent paid by the tenant, denoting same as a "preferential rent" if it was less than the calculated "Legal Regulated Rent" (R. 864-1135; *see* footnote 3, *supra*). Owner's error was thus incorrectly anticipating what methodology this Court would ultimately adopt to calculate legal rents after *Roberts* and *Gersten*. Certainly, Owner's methodology did not violate any established policy or rule. Guessing wrong is not fraud, and to the extent that Owner's 2012 calculations resulted in willful overcharges, the remedy -- but for Tenants' waiver -- is found in RSL § 26-516(a)(1), not in the *ad hoc* creation of a new exception to the standard rule.

Ironically, the "understandable confusion" following *Roberts* equally affected both Tenants and Supreme Court herein. Tenants asserted that their rent should be calculated pursuant to the reconstruction method (R. 78-80, 1339-42, 1257-58).

Supreme Court agreed (R. 22). In *Regina*, however, this Court held that the reconstruction method "violated the legislative mandate that 'no award or calculation of an award may be based on an overcharge having occurred more than four years before'" (35 NY3d at 358). Tenants and Supreme Court, obviously, did not commit fraud by using the unlawful reconstruction method; they were merely caught up in the confusion following *Roberts* and guessed wrong. The same is true of Owner, who made a transparent and good faith effort to promptly comply with *Roberts* and *Gersten*.

Regina provides another basis for finding that Owner's retroactive registrations and recalculations do not constitute fraud, and certainly not on summary judgment. In *Regina*, this Court clarified what constitutes "fraud" for purposes of determining whether there has been a fraudulent scheme to destabilize. A tenant must plead with particularity and establish "evidence [of] a representation, material fact, falsity, scienter, reliance and injury" (35 NY3d at 356, n 7). The First Department found that Owner "unilaterally registered rents from the base date forward that were not the rents actually paid, and instead registered rents far higher, without explanation" (R. 1373). The Court concluded that "these intentional misstatements, which were intended to artificially increase the legal regulated rent, constitute fraud under *Grimm*" (R. 1373). In so holding, the Court disregarded that

in 2012, the parties had jointly advised the Tenants that the calculation of their legal rents was the subject of the pending litigation (R. 173).

"Scienter" is defined as "a misrepresentation or a material omission of fact which was false and known to be false by defendant" (*Lama Holding Co. v Smith Barney Inc.*, 88 NY2d 413, 421 [1996]). "It is fundamental that a knowing misrepresentation is a necessary element of a cause of action for fraud" (*Marine Midland Bank v Russo Produce Co.*, 50 NY2d 31, 43 [1980]). The First Department thus necessarily found that Owner's registrations and recalculations were not only false, but that Owner *knew* they were false when transmitted to Tenants during the "understandable confusion" after *Roberts* and *Gersten*.

Under the circumstances, Owner's 2012 registration and good faith calculation of the legal rents could not have been a willful misrepresentation to Tenants, especially because Tenants' counsel and Owners' counsel specifically advised Tenants to disregard the registered amounts and agreed that the Tenants' legal rents would be determined by the Court in the pending litigation (R. 173).

Even if Owners' actions could constitute fraud, scienter is ordinarily a question of fact which cannot be resolved on summary judgment (*see Shisgal v Brown*, 21 AD3d 845, 847 [1st Dept 2005]). Tenants offered no proof before Supreme Court to eliminate any question of fact as to scienter. Accordingly, even if

it is possible that a fraudulent scheme to destabilize could have occurred herein, that determination could not be summarily made on this record.

D. Because Tenants did not Rely on Owner's Registrations and Rent Recalculations, there can be no Fraudulent Scheme to Destabilize

As this Court held in *Regina*, reliance is an essential element of any fraud claim (35 NY3d at 356, n 7). Absent reliance, there can be no fraud as a matter of law (*see ACA Fin. Guar. Corp. v Goldman, Sachs & Co.*, 25 NY3d 1043, 1044 [2015]). In *Vermeer Owners, Inc. v Guterman*, 78 NY2d 1114, 1116 (1991), this Court wrote:

> "Plaintiffs argue that defendants City Partners and Guterman misrepresented the lease transaction in the offering plan. Although it is clear that the offering plan contained statements that were demonstrably false, plaintiffs have not met their burden. They were required to prove by clear and convincing evidence a representation of material fact, falsity, scienter, reliance and injury. Nothing in this record establishes that plaintiffs in fact relied on any misrepresentation by defendants to their detriment. Thus, they have failed to establish common-law fraud and the complaint was properly dismissed."

In *Kostic v New York State Div. of Hous. & Community Renewal*, 188 AD3d 569 (1st Dept 2020), the tenant alleged a fraudulent deregulation scheme because the landlord had filed an exit registration in error. Citing *Regina*, the First Department found no fraud:

> "Under the circumstances, the fact that the owner filed an erroneous exit registration on the ground of high-rent vacancy, does not compel a finding of fraud. The error

> was plain on its face, since Kostic never vacated the apartment. Therefore, she could not have reasonably relied on the exit registration. Reasonable reliance is an element of fraud for purposes of evading the four-year lookback restriction for pre-HSTPA overcharge claims (*see Matter of Regina Metro Co., LLC*, 35 NY3d at 356 n 7)"

(188 AD3d at 570).

The evidence of record establishes that Tenants did not rely on Owner's 2012 registrations and rent calculations (nor did Tenants argue otherwise). By January 12, 2012, counsel for both parties issued a joint letter agreeing that: (1) Owner's letters, wherein Owner's consultant "purport[ed] to calculate the legal regulated rent for the apartments," were "hereby withdrawn" and "should be ignored" (R. 45, 173). The joint letter further advised Tenants that "both sides agreed that calculation of past, current and future legal regulated rents at the building are the subject of pending litigation" (R. 173). Thus, because Tenants cannot claim (nor did claim) to have relied on the rents and registrations that both parties disavowed ten years ago, there can be no fraud or fraudulent scheme to destabilize.

E. There is no "Fraudulent Rent Overcharge Scheme" Exception to the Standard Rule

Because there was no fraudulent scheme to destabilize, Tenants hedged their bets before the First Department by relying on *435 Cent. Park W. Tenant Assoc. v Park Front Apts. LLC*, 183 AD3d 509 (1st Dept 2020) (C-111-12), a post-*Regina* case that the First Department cited favorably herein (R. 1376). There, the First

Department held that even where there is no fraudulent scheme to destabilize, DHCR's default rent formula will be used where a landlord "engaged in a fraudulent rent overcharge scheme" (*id. at* 510-11; *see Montera v KMR Amsterdam LLC*, 193 AD3d at 107 ["the fraud exception to the four-year lookback period applie[s] to both a fraudulent scheme to deregulate and a fraudulent overcharge scheme"]).

As Owner establishes below, *Regina* does not authorize a second fraud-based exception to the standard rule. Nor, in any event, was there any fraudulent scheme to overcharge Tenants herein.

In *Thornton v Baron*, the landlord and various illusory prime tenants collusively entered into leases stating that the prime tenants would not use their apartments as their primary residences (5 NY3d at 178). The prime tenants then "sublet" the apartments at unregulated rents (*id*.). The Court of Appeals described this conduct as "a scheme to remove a number of…apartments from the protections of rent regulation by taking advantage of the statutory exemption for non-primary residences" (*id*. at 177-78).

Grimm involved "a scheme between a landlord and an illusory tenant to agree that an apartment would not be used as a primary residence, resulting in the elimination of the rent-stabilized status of the apartment" (15 NY3d at 365). In response, this Court in *Grimm* defined the sole fraud-based exception to the standard rule:

> "Generally, an increase in the rent alone will not be sufficient to establish a 'colorable claim of fraud,' and a mere allegation fraud alone, without more, will not be sufficient to require DHCR to inquire further. What is required is evidence of a landlord's fraudulent deregulation scheme to remove an apartment from the protections of rent stabilization. As in *Thornton*, the rental history may be examined for the limited purpose of determining whether a fraudulent scheme to destabilize the apartment tainted the reliability of the rent on the base date"

(*id.* at 367 [emphasis supplied]).

In *Conason*, the landlord "'created an entirely fictitious tenant'" in "connection with a stratagem devised by Megan to remove tenants' apartment from the protections of rent stabilization" (25 NY3d at 16 [emphasis supplied]). The *Conason* Court held that given the fraudulent scheme to destabilize, "the lawful rent on the base date must be determined by using the default formula devised by" DHCR (*id*. at 6).

Upon reviewing its prior authority, the Court in *Regina* stated the sole fraud-based exception to the standard rule: "review of rental history outside the four-year lookback period was permitted only in the limited category of cases where the tenant produced evidence of a fraudulent scheme to deregulate" (35 NY3d at 355).

In contrast to this "limited category," it would be impossible to create a broader fraud-based exception to the four-year lookback period than a "fraudulent rent overcharge scheme." First, the exception is so broad and undefined that it can

be alleged in any case where there has been an overcharge. At best, this exception creates a gaping hole in the four-year rule; at worst, it swallows the rule.

Second, the fraudulent scheme to destabilize exception would *necessarily be subsumed* within the purported fraudulent rent overcharge scheme exception; where there is a fraudulent scheme to destabilize, there is necessarily a fraudulent scheme to overcharge. Thus, if a fraudulent rent overcharge scheme exception exists (as the First Department held herein), *Regina*'s fraudulent destabilization scheme exception would become meaningless.

Accordingly, because there was no fraudulent scheme to destabilize herein, *Regina's* standard rule applies. A so-called "fraudulent rent overcharge scheme" is at most a willful overcharge, for which treble damages must be assessed pursuant to RSL § 26-516(a). As this Court cautioned in *Regina*, it is not "necessary to recognize an additional common-law exception that would create or increase the amount of overcharge damages in order to give proper effect to *Roberts*" (35 NY3d at 360).

POINT IV

OWNER'S DOCUMENT PRODUCTION WAS JUDGED UNDER AN ILLEGAL STANDARD, AND THE FIRST DEPARTMENT'S HOLDING THAT OWNER DID NOT PRODUCE BASE DATE LEASES IS BELIED BY THE RECORD

The First Department ruled that the default rent formula should also be used because Owner had failed to produce base date leases for *any* unit, such that the actual rents charged on the base date were unknown:

> "RSC 2522.6(b)(2)…calls for application of the default formula where '(i) the rent charged on the base date cannot be determined; or (ii) a full rental history from the base date is not provided.' Both of these scenarios apply here, and differ from situations in which the base date rent is known (*Regina*, 35 NY3d at 359 ["the alternative methods proposed by the tenants…reflected in the regulations…are available only ['w]here the rent charged on the base date cannot be established'"]).
>
> * * *
>
> Here, the base date rent cannot be established because defendants failed to provide leases showing what the actual rent charged on the base date was, or whether the actual rent was known
>
> * * *
>
> Defendants failed to produce leases for the class reflecting the actual rent charged on the base date, October 14, 2007…
>
> * * *
>
> Based on defendants' conduct, and in light of the absence of evidence in the record as to the actual rent charged on the base date by which to calculate legal regulated rents

> under RSC 2526.1(a)(3)(i), plaintiffs' overcharges, if any, must be determined according to the default formula set forth in RSC 2522.6(b)…"

(R. 1373-74, 1376 [emphasis supplied]).

As Owner establishes below, the First Department's ruling was legally and factually in error.

A. As a Matter of Law, Owner could not be Compelled to Submit Rent Records Prior to the October 14, 2007 Base Date

Any analysis of whether Owner produced records sufficient to establish the rents actually charged on the base date for the subject apartments, and thereby avoid application of the default formula, necessarily begins with the scope of rent records that Owner could be required to submit as a matter of law.

Regina -- decided after the discovery process herein commenced and after Supreme Court ruled in 2017 -- sets forth the applicable rule:

> "The rule that emerges from our precedent is that…review of rental history outside the four-year lookback period was permitted only in the limited category of cases where the tenant produced evidence of a fraudulent scheme to deregulate and, even then, solely to ascertain whether fraud occurred -- not to furnish evidence for calculation of the base rent or permit recovery for years of overcharge barred by the statute of limitations (*Grimm*, 15 NY3d at 367). In fraud cases, this Court sanctioned use of the default formula to set the base date rent. Otherwise, for overcharge calculation purposes, the base date rent was the rent actually charged on the base date"

(35 NY3d at 355-56 [emphasis supplied]).

As Owner established in Point I, Tenants did not allege in their complaint, amended complaint, or motion for summary judgment that Owner engaged in a fraudulent scheme to destabilize the subject apartments. As such, the standard rule applies, and Owner could not be compelled to submit rent records prior to the base date.

B. Supreme Court Judged Owner's Document Production under an Illegal Standard

It is undisputed that Tenants' discovery demands, and Supreme Court's discovery orders were all premised on the reconstruction method rejected in *Regina* (R. 204, 210). Therefore, the entire process, from discovery through Supreme Court's assessment that Owner's production was insufficient to determine the base date rents for any subject apartment, was tainted by an unlawful methodology.

Supreme Court, while professing to have reviewed "all the relevant discovery material,"[9] expressly agreed with the assessment of Tenants' counsel that Owner's records were insufficient to reconstruct base date rents for any of the subject apartments (R. 22).

The First Department acknowledged that Tenants and Supreme Court were unlawfully proceeding under the reconstruction method (R. 1373). Accordingly, to

[9] It is hard to believe that Supreme Court reviewed "all the relevant discovery material" (R. 22). Neither party submitted those documents on summary judgment, and the documents produced by Owner in discovery, including the 17,000 pages produced in January and February 2016, were not part of the record.

the extent that Supreme Court and the First Department applied the default rent formula because Owner failed to supply pre-base date rent records to reconstruct the base date rents, those Courts were in error.

C. The Record Establishes that Owner Provided Base Date Leases for at least 55 of the Subject Apartments

Despite acknowledging that Supreme Court had employed an illegal methodology to assess Owner's document production, the First Department held that Owner had failed to produce any leases reflecting the actual rent charged on the base date (R. 1373-74, 1376), such that the default formula should be used to calculate the legal rents for all the apartments (R. 1376). The First Department's finding is demonstrably incorrect.

In support of their summary judgment motion, Tenants submitted on December 8, 2015 an apartment-by-apartment "Summary of Documents provided by Defendant" (R. 256-78). That summary concedes that Owner produced base date leases, establishing the actual rent charged on the base date, for 41 of the subject apartments: 1D, 2H, 2J, 2K, 3C, 3G, 3K, 4A, 5B, 5C, 5G, 6F, 6G, 6H, 7C, 7D, 7G, 8E, 8J, 8K, 9A, 9C, 9G, 9H, 10A, 10D, 10G, 10H, 11B, 12H, 12K, 14C, 14G, 14H, 14J, 15B, 15E, 15G, PHB, PHC, and PHD (R. 257-67).

It is further undisputed that after Tenants moved for summary judgment, Owner produced thousands of additional pages of documents (R. 1216-17, 1257-58). On or about May 4, 2016, in further support of their summary judgment motion,

Tenants submitted to Supreme Court another schedule showing the documents that Owner had allegedly still *not* yet produced (under the reconstruction method) (R. 1228-41). A careful reading of the schedule establishes that Tenants did *not* list as "missing" the base date leases for an additional 14 subject apartments (3A, 3E, 3J, 4C, 4D, 5D, 8C, 11D, 12C, 12D, 12E, 12J, 14D, and 14E), thus admitting that Owner had produced those leases (R. 1228-39).

Accordingly, Tenants conceded on summary judgment that Owner had produced base date leases for at least 55 of the subject apartments. As such, the First Department's repeated finding that Owner failed to provide "leases showing…the actual rent charged on the base date" is erroneous with respect to those units.[10] So too was the First Department's holding that the base date rents for those 55 units should be calculated pursuant to the default rent formula.

Moreover, the default rent formula cannot be applied on a blanket basis across all units in the building to determine base date rents, especially where the actual rent charged on the base date is undisputedly known for at least 55 of the subject apartments. If the default formula is applied, it must be applied on an apartment-by-apartment basis. The base date rent in a rent overcharge claim refers to the actual rent charged on the date four years prior to the action *for a particular apartment*,

[10] Moreover, the First Department's erroneous finding was made without any of the discovery material in the record. Nor was discovery complete.

and each apartment has a distinct base date rent and requires an individualized analysis of whether the actual rent charged on the base date is known. The First Department's failure to undertake such analysis, particularly in light of the 55 base date leases produced by Owner, is reversible error.

As Justice Gische correctly concluded in dissent:

> "Given Supreme Court's sweeping determination that the entire rent history of the deregulated apartments had to be reconstructed going back to when they were deregulated, possibly in the mid-1990's[,] I believe that Supreme Court's order directing calculation of rent overcharges is incorrect and should be reversed. It is unclear whether the records made available by either party provide enough information to determine the base date rent in accordance with *Regina* for any of the subject apartments. Given those circumstances, I would remand this matter to Supreme Court so that any remaining discovery and other pretrial matters can be completed"

(R. 1385).

POINT V

OWNERS' AFFIRMATIVE DEFENSES ASSERTING GOOD FAITH SHOULD BE REINSTATED

Although Tenants never alleged fraud before Supreme Court, the First Department affirmed Supreme Court's dismissal of Owner's fourteenth, fifteenth, and seventeenth affirmative defenses, asserting "good faith and compliance with [DHCR]'s interpretation of the law during the relevant period" (R. 1377).

Given the First Department's error herein, Owner respectfully submits that this Court should reinstate Owner's fourteenth, fifteenth, and seventeenth affirmative defenses.

POINT VI

OWNERS' UNOPPOSED ARGUMENT ON APPEAL THAT SUPREME COURT ERRED IN DISMISSING OWNERS' SECOND AND THIRD AFFIRMATIVE DEFENSES ASSERTING THAT THE MANAGING AGENTS ARE NOT LIABLE SHOULD HAVE BEEN GRANTED

On appeal to the First Department, Owner argued that Supreme Court erred in dismissing Owner's second and third affirmative defenses asserting that defendants K&K, Duell, and Koeppel, acting as agents for disclosed principals, cannot be held liable for rent overcharges (C-59-61).

Tenants did not oppose this argument on appeal, and in fact, Tenants affirmatively stated that: "[Tenants] have previously stated to this Court that they do not oppose that part of the appeal which deals with Defendants' affirmative defenses that two of the Defendants were acting as agents of a disclosed principal" (C-122). Justice Gische duly acknowledged this in her dissent, noting: "[Tenants] are no longer opposed to dismissal of claims against the managing agents because they are disclosed agents of disclosed principals" (R. 1379, n 1).

Nevertheless, the First Department did not reinstate Owner's second and third affirmative defenses, and instead held that: "We have considered defendants' remaining contentions and find them unavailing" (R. 1377). Owner respectfully submits that reversal is warranted.

It is well-settled that a managing agent for a disclosed principal cannot be held liable for rent overcharges unless there is clear and explicit evidence of the agent's

intention to substitute or add its personal liability for, or to, that of its principal (*see Paganuzzi v Primrose Mgmt. Co.*, 181 Misc2d 34, 36 [Sup Ct, NY County 1999], *affd* 268 AD2d 213 [1st Dept 2000]; *Crimmins v Handler & Co.*, 249 AD2d 89, 91-92 [1st Dept 1998]). In affirming the Supreme Court's decision in *Paganuzzi*, the First Department held: "The action was properly dismissed as against the managing agent, since it always acted as an agent for a disclosed principal" (*Paganuzzi v Primrose Mgmt. Co.*, 268 AD2d 213, 213-214 [1st Dept 2000]). The same result should follow here.

CONCLUSION

The order of the First Department should be reversed insofar as it (1) granted Tenants' motion for summary judgment declaring that Tenants' rents should be calculated pursuant to the Rent Stabilization Code's default rent formula due to (a) Owner's fraud, and (b) Owner's alleged failure to submit documents necessary to establish base date rents; and (2) dismissed Owner's second, third, fourteenth, fifteenth, and seventeenth affirmative defenses; in addition, this Court should remand the matter to Supreme Court so that (a) any remaining discovery and other pretrial matters can be completed; and (b) rents can be calculated on an apartment-by-apartment basis.

Dated: New York, New York
January 13, 2022

ROSENBERG & ESTIS, P.C.
Attorneys for Defendants-Appellants and Third-Party Plaintiffs-Appellants

By: _____

Jeffrey Turkel
Howard W. Kingsley
Ethan R. Cohen
733 Third Avenue
New York, New York 10017
(212) 551-1223

JEFFREY TURKEL
HOWARD W. KINGSLEY
ETHAN R. COHEN
Of Counsel

CERTIFICATE OF COMPLIANCE

Certificate of Compliance
Pursuant to Part 500.13(c)(1) of the Rules of Practice of the
Court of Appeals, State of New York

The foregoing brief was prepared on a computer. A proportionally spaced typeface was used, as follows:

Name of typeface: Times New Roman
Point size: 14
Line spacing: Double

The total number of words in the brief, inclusive of point headings and footnotes and exclusive of pages containing the table of contents, table of citations, statement of questions presented, proof of service, certificate of compliance, or any authorized addendum containing statutes, rules and regulations, etc. is 13,694 words.

Dated: New York, New York
January 13, 2022

Jeffrey Turkel