

# CLIENT ADVISORY

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## **COOPERATIVES AND TENANTS MUST CONSIDER RIGHTS OF LENDERS IN LITIGATING AND SETTLING DISPUTES**

Litigation between a cooperative board and a shareholder/proprietary lessee can typically be resolved if the board and the shareholder agree upon a settlement. However, where other interested parties' rights are implicated by the dispute, they must also be addressed.

In **Klingsberg v. River Terrace Apartments**, *New York Law Journal*, June 21, 2005, p. 18, col. 3 (Sup. Ct. Bronx Co.), the Cooperative had sued shareholders for maintenance arrears. In a separate litigation, the shareholders had sued the board in a dispute over a parking space. The parties entered into a settlement of both cases under which the shareholders paid the arrears and gave up any claim to the parking space. In return, the Cooperative waived any claim under the proprietary lease for its attorneys' fees incurred in the litigation.

What the parties apparently did not take into account in their settlement, however, was that the shareholders had financed their apartment through a bank loan. As is typical in most cooperative apartment loans, the bank obtained a recognition agreement protecting its security by having the Cooperative notify the bank of any maintenance defaults so the bank could ensure that payment was made. During the litigations, the Cooperative had billed the shareholders for several thousand dollars in legal fees. When the shareholders did not pay the fees, the bank paid them on the shareholders' behalf and demanded reimbursement. The shareholders, contending that the Cooperative had waived any right to recover legal fees, asked the court to enforce the settlement by ordering that the Cooperative repay to the bank the legal fees it had paid. The court granted the motion, holding that the Cooperative had unambiguously waived all claims for past and future legal fees and that this waiver included the fees that the bank had paid on the shareholders' behalf.

This case is a reminder that settlement agreements must be drafted carefully, taking into account not just the rights and obligations of the immediate parties, but those of lenders and other interested third parties as well. Another pointer from the case is that when settling a litigation, the parties should consider whether to file a formal stipulation of discontinuance. In this case, the parties had not filed a stipulation of discontinuance and the court concluded it still had jurisdiction over the attorneys' fee issue. If a stipulation of discontinuance had been filed, the court said, the case would have been over and the shareholders would have had to bring a new lawsuit if they wished to enforce the settlement's waiver of attorneys' fees.

## **LENDER NOT ENTITLED TO SELL COOPERATIVE SHARES TO RECOUP LEGAL FEES THAT COURT FINDS ARE NOT OWED**

Another recently reported case also involved a three-cornered dispute between a cooperative, a shareholder-tenant, and a lending bank holding a secured loan on a cooperative apartment. The shareholder in **Robinson v. Dime Savings Bank**, *New York Law Journal*, July 6, 2005, p. 19, col. 3 (Sup. Ct. Kings Co.), disputed several charges that the Cooperative had placed on her maintenance bill, claiming that they had not been adequately explained. When the Cooperative threatened nonpayment proceedings, the shareholder paid the disputed sums under

protest and then brought a suit against the Cooperative for reimbursement, which was dismissed on the ground that the shareholder had paid the disputed amounts voluntarily.

The Cooperative thereupon billed the shareholder for several thousand dollars in additional maintenance, representing the legal fees it had incurred in the shareholder's suit, and advised the shareholder's bank of the alleged default in paying such legal fees. The bank paid the fees to the Cooperative on the shareholder's behalf, and then noticed a non-judicial UCC sale of the shareholder's shares of the Cooperative in order to recoup the amount paid.

The shareholder sought and obtained a preliminary injunction against the sale. In its opinion, the court expressed concern about several aspects of the proceedings, including the fact that if an injunction were not granted, the shareholder would have no opportunity to dispute the validity or amount of the legal fees before being required to either "voluntarily" pay them or lose her apartment. The court also observed that the Cooperative should have asserted its claim for legal fees as a counterclaim in the earlier litigation, where it could have been resolved economically as part of that case, rather than waiting and commencing a second action arising from the same facts. Because the shareholder did not owe the Cooperative any money, the court concluded, the bank had no claim against the shareholder to recover the amount it had advanced on her behalf.

### **NEW BANKRUPTCY LEGISLATION BENEFITS COOPERATIVES, CONDOMINIUMS, AND LANDLORDS**

Cooperatives, condominiums, and landlords must deal from time to time with owners or tenants filing for protection under the Bankruptcy Code. A bankruptcy filing triggers an automatic stay of most legal proceedings against the debtor (including non-payment or foreclosure actions), which cannot be continued outside Bankruptcy Court without that court's permission.

Extensive amendments to the Bankruptcy Code were recently enacted in the **Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23**, which will generally apply to all bankruptcy cases filed after October 17, 2005. Among other changes, the Act provides that under certain circumstances, a bankruptcy filing will not trigger an automatic stay of a landlord's dispossession action if the landlord had already obtained a judgment of possession prior to the bankruptcy filing (the tenant still retains rights to cure under applicable non-bankruptcy law). In addition, the lifting of the automatic stay can now also be accelerated in some cases where a residential landlord claims that the tenant has endangered the premises or allowed controlled substances to be used there. Condominiums and homeowners associations will now be able to collect post-petition rent and assessments from residents who have abandoned their units. Additionally, the timetable for a debtor to either assume or reject an unexpired commercial lease has been accelerated by limiting the permissible extensions of the statutory deadlines.

This is only a brief summary of complex legislation that will dramatically affect all aspects of bankruptcy practice. Whenever a shareholder or lessee files for bankruptcy – or there is reason to believe that a filing is likely – qualified counsel should be consulted to ensure that the rights of the cooperative, condominium, or landlord are protected.