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# CLIENT ADVISORY

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## INDEMNIFICATION CLAUSE OF ALTERATION AGREEMENT INVALIDATED FOR OMITTING REQUIRED EXCLUSIONS

Virtually all cooperatives require that any alterations in a tenant-shareholder's apartment must be approved by the Board of Directors and that, before commencing work, the tenant-shareholder must enter into an Alteration Agreement with the Cooperative. Among other things, the Alteration Agreement will require that the tenant-shareholder indemnify and hold harmless the Cooperative for any claims arising from of the alterations. However, an overly broad indemnification clause may prove to be unenforceable, as has occurred in cases such as Hadzihasanovic v. 155 East 72nd Street Corp., 2010 WL 378041, 2010 N.Y. Slip Op. 809 (App. Div. 2d Dep't Feb. 2, 2010).

This case arose when a subcontractor's employee working in a cooperative apartment was injured during the construction. He filed suit for personal injuries against the Cooperative, its managing agent, and the tenant-shareholders of the apartment. The Cooperative and the managing agent then demanded that the tenant-shareholders indemnify them for any liability they might incur in the litigation. They relied on a provision of the Alteration Agreement in which the tenant-shareholders "agree[d] to indemnify and hold harmless [the Cooperative], its stockholders, Managing Agent, consultants and employees, from any personal injury, liability or damage to any personal property . . . which may arise from the work being performed."

The court held that this indemnification provision was unenforceable. In doing so, the court relied on New York General Obligations Law § 5-321, which provides that "[e]very covenant, agreement or understanding in or in connection with or collateral to any lease of real property exempting the lessor from liability for injuries to person or property caused by or resulting from the negligence of the lessor, his agents, servants or employees, in the operation or maintenance of the demised premises or the real property containing the demised premises shall be deemed to be void as against public policy and wholly unenforceable."

The courts have held that an Alteration Agreement for a cooperative apartment is deemed to be "made in connection with or collateral to" the proprietary lease. Accordingly, in the court's words, "[a] broad indemnification provision in a lease, such as the alteration agreement here, which is not limited to the lessee's acts or omissions, fails to make exceptions for the lessor's own negligence, and does not limit the lessor's recovery under the lessee's indemnification obligation to insurance proceeds, is unenforceable...."

Significantly, this and several prior cases have invalidated indemnification clauses that failed to contain the required limitations, such as the exception for injuries caused by the Cooperative's or the Cooperative's own negligence, even where there was no allegation or showing that the Cooperative was actually negligent in that case. Accordingly, it is important that all Cooperatives and Managing Agents review and update their forms of Alteration Agreement to avoid this pitfall.

**ELECTION OF COOPERATIVE BOARD MEMBERS VOIDED  
BASED ON ERRORS THAT VIOLATED STATUTE AND BY-LAWS**

A Cooperative's annual election of directors has been set aside by a court based on a series of errors in noticing and conducting the shareholder meeting. **White v. Kings Village Corp., 2010 WL 532384, 2010 N.Y. Slip Op. 50210(U) (Sup. Ct. Kings Co. Feb. 11, 2010)**. The decision addresses several issues that frequently arise in connection with elections.

The court first addressed whether a holder of unsold shares retained the contractual right to designate one of the seven board members. The court noted that this holder had purchased its shares in 2001, but that by 2010 it owned less than three percent of all shares. Therefore, "it would be totally inequitable for [this holder] to maintain that level of control of the board of directors nine years after purchasing [its] units." Moreover, the court found that the entity claiming a board seat was not the investor to whom the Cooperative had granted this right, but a subsequent purchaser to whom, the court held, the right did not transfer when it acquired its shares. The court contrasted this holder's situation with that of another holder, which had stepped into the shoes of the Sponsor and continued to have the right to designate a board member.

The court went on to offer several bases for holding the election of directors invalid. One of these was that the annual shareholder meeting was not called on the date provided for in the By-Laws. Also, the meeting notice, upon which shareholders may have relied in completing their proxies, incorrectly stated the number of directors to be elected.

Additionally, the record left it unclear whether a quorum was present at the meeting. The court's decision discussed confusion surrounding the question of what constituted a quorum of this Cooperative's shareholders. Initially, the By-Laws provided that 25% of all shares would constitute a quorum, but this provision was invalid because New York law permits a corporation to establish a quorum that must not be less than one third of the shares. Thus, the court would deem the required quorum to be 33 1/3%.

The court then invalidated a board resolution that sought to increase the quorum requirement to 51%. Although the board probably had intended simply to restore the usual rule of "one more than half of all shares" for a quorum, the court noted that 51% of the shares is actually greater than 50% of the shares plus 1 share. In the context of this large Cooperative, the difference could represent several apartments. Thus, a 51% quorum represented a "supermajority" quorum requirement, which must be contained in the Certificate of Incorporation, not only the By-Laws. Moreover, even if this quorum requirement could have been enacted by amending only the By-Laws, the resolution had apparently not been adopted by the two-thirds board majority required to amend the By-Laws. The court also rejected an argument that the Board's later approval of the minutes of the Board meeting served to validate the invalid action that had been taken at that meeting. The court observed, however, that at a still later meeting, the Board had validly voted to amend the By-Laws to change the quorum to 40%. The court held that this amendment to the quorum requirement was valid, but directed that notice of the change must be provided to all shareholders.

Based on the various errors, no valid election of directors had taken place in 2009. Therefore, the directors elected in 2008 would remain in office until the 2010 annual meeting. However, the court limited their authority to conducting the Cooperative's routine business, and enjoined them from undertaking any long-term commitments until the new Board members take office.