

# CLIENT ADVISORY

NOVEMBER 2001

## FIRST, A QUICK REMINDER

Ganfer and Shore, LLP will be hosting a series of breakfast panel discussions addressing topics that, we believe, will be of significant interest to cooperatives, condominiums and real estate owners. The first discussion will focus on insurance coverage issues. It will be held on November 14, 2001 from 8:00 A.M. to 9:30 A.M. in the Regency Room of the New York Grand Hyatt Hotel, located on 42<sup>nd</sup> Street adjacent to Grand Central Station between Park and Lexington Avenues. Please join us. If you would like to attend, please call Amarilys Garcia of our office at 212-922-9250, extension 262, by November 12, 2001. The next discussion will focus on security-related issues, and will be held in January 2002.

## A BAD CASE OF THE NEW CONSTRUCTION BLUES

Just four years after the design and construction of their condominium building by the sponsor/developer, Rockrose Development Corp. ("Rockrose"), the individual owners of condominium units ("Unit Owners") in the building at 99 Jane Street, through their association (the "Association"), found alleged defects in the design and construction of their condominium building sufficient for the Association to litigate. The Association, on its own behalf and on behalf of the individual owners, brought suit alleging professional malpractice and breach of contract in the design and construction of the building against Rockrose's architect, structural engineer, and mechanical, electrical, plumbing and sprinkler contractor, as well as Rockrose's general contractor. Rockrose's general contractor was an entity separate from Rockrose named Rockrose Construction (Jack) Corp. ("Rockrose-Jack"). The decision rendered by the Court limited itself solely to direct claims made by the Association against Rockrose's contractors, including Rockrose-Jack. It did not address claims that, depending upon the circumstances, may be made by an Association directly against a sponsor itself, in this case Rockrose, or its experts, including possible securities and fraud claims which may arise out of material omissions from, or misstatements of fact in, the offering plan.

The Association alleged that the Association and the Unit Owners were both the *actual* and *intended beneficiaries* of the separate contracts entered into between Rockrose and its architect, and Rockrose-Jack and each of the other contractors. In The Residential Board of Managers of the 99 Jane Street Condominium v. Rockrose Development Corp., et al., (NYLJ, October 17, 2001, p. 18, col. 3), the Court dismissed the Association's direct action against Rockrose's contractors, ruling that the Association had no relationship with either Rockrose-Jack or the various contractors which was legally sufficient to permit the Association to sue on its own behalf and on behalf of the Unit Owners.

The Court ruled that the Association and Unit Owners were not the *actual* beneficiaries under the various contracts, because they were not parties to the various contracts. The Court also ruled that the Association and the Unit Owners were not "*intended beneficiaries*" of those contracts, because

the contracts did not expressly refer to the Unit Owners or express the intention of the parties that the contracts would benefit the Unit Owners. The Association also had alleged that it should have standing as the “successors in interest” to Rockrose. However, the Court disagreed. It limited the definition of a “successor in interest” to a corporation as “ordinarily indicat[ing] statutory succession as, for instance, when a corporation changes its name but retains the same property”. Finally, the Court dismissed the Association’s negligence claims against Rockrose’s contractors, stating that the Association must either have *actual* privity of contract or one so close as to approach that of privity. Mere ownership of a unit in the building so constructed was not close enough.

While this case deals only with direct claims made by the Association against Rockrose’s contractors, it highlights an important concern of the purchaser of a unit in a newly constructed or substantially and newly renovated building. Both purchasers and their counsel should ask what recourse is available to Unit Owners in the event of the discovery of defects in the design or construction of the building or unit. Most offering plans either provide no warranties or very limited warranties that may be of little comfort to the unit owner. Accordingly, if an Association determines that the work to correct such defects is required to maintain and preserve the building and the quality of living in the building, the costs of repairs may have to be borne by the Unit Owners in the form of substantial assessments and an increase in common charges.

### **WHEN IS STOCK IN A COOPERATIVE CORPORATION CONSIDERED REAL OR PERSONAL PROPERTY?**

Since we are in fact lawyers, no reader should be surprised by our answer: IT DEPENDS. The case of The Lambs Inc. v. Diven, (NYLJ, October 10, 2001, p. 18, col. 3) does an excellent job of discussing many of the differing treatments of stock in cooperative corporations (“Stock”) by the Courts depending upon the purposes for which a litigation has been brought. For instance, in this case, a judgment creditor sought to enforce its judgment in the amount of \$276,055 by compelling the sale of the judgment debtor’s cooperative apartment. The judgment debtor was apparently a wolf in The Lambs’ den, a former director and treasurer of a not-for-profit corporation, who had wrongfully converted the not-for-profit’s monies for his own personal use.

The characterization of the Stock became paramount when the plaintiff sought to avoid the “homestead exemption” which appears in Section 5206(a) of the Civil Practice Law and Rules (“CPLR”) by characterizing the Stock as personal property and subject to sale. New York’s homestead exemption states that a *homestead*, not exceeding \$10,000 in value above liens and encumbrances, owned and occupied as a primary cooperative residence, is exempt from procedures to enforce judgments. Judge Billings, recounting many of the commercial circumstances in which Stock is considered personal property or real property, decided that the Stock should be considered real property for the purposes of New York’s homestead exemption. Accordingly, future efforts to collect judgments through the forced sale of stock in cooperative apartments should anticipate, and be prepared to address, a possible defense that the apartment is a judgment debtor’s primary residence, and that the collection action is therefore limited by New York’s homestead exemption.