Real Estate

Tenants Beware: Your **Cure Period** May Not Be as Long as You Think

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BY JESSE B. SCHNEIDER AND JOSHUA B. PODOLNICK

Tenants often successfully use a landlord's failure to comply with notice requirements of a lease to seek dismissal of summary proceedings. See *Parkchester Apts. Co. v. Walker*, 1995 N.Y. Misc. LEXIS 738, at *2 (Civ. Ct. Bronx Cty. 1995) (dismissing non-payment petition because landlord failed to prove that proper predicate notice had been served, which the court held was a jurisdictional prerequisite to a non-payment petition). It is important for tenants to know, however, that, depending on the language of their lease, they may not be able to rely on the notice period provided in conditional limitation provisions as a defense in a non-payment proceeding. This is true even if the *only* notice provision contained in the entire lease is that found in the conditional limitation provision. Rather, a landlord can elect *not* to enforce a conditional limitation related to non-payment of rent and instead, commence a non-payment proceeding upon only the three-day notice required by New York's Real Property Actions and Proceedings Laws (RPAPL), leaving tenants a shorter window to respond to landlord's claims.

In a lease, a conditional limitation traditionally serves to automatically end the term of the lease upon the occurrence of a prescribed event. See 4 NY Practice Guide: Real Estate §27.04 (2018). Typically, conditional limitations include a requirement that the landlord give notice and an opportunity to cure prior to the automatic termination of the lease by operation of the conditional limitation. *See id.* In New York commercial leases, the cure period provided by a conditional limitation is often longer than the three-day written notice period required by statute prior to a landlord initiating a non-payment proceeding. Parties typically use conditional limitations to cover certain important potential breaches of the lease. See id. Such breaches can, but do not always, include failure to pay rent or late rent payments. See id.

It is important for tenants to know, however, that, depending on the language of their lease, **they may not be able to rely on the notice period** provided in conditional limitation provisions as a defense in a non-payment proceeding.

Separately, §711(2) of the New York's RPAPL separately provides in relevant part that:

> The tenant has defaulted in the payment of rent, pursuant to the agreement under which the premises are held, and a demand of the rent has been made, *or at least three days' notice in writing* requiring, in the alternative, the payment of the rent, or the possession of the premises, has been served upon him as prescribed in section 735.

See RPAPL §711(2) (emphasis added).

In other words, prior to instituting a summary non-payment proceeding, a landlord must make an oral demand or at least three days' written notice requiring payment or surrender of the premises. See id. New York allows landlords and tenants to contractually modify the amount of notice required by a landlord before instituting a non-payment proceeding. See *Oak Plaza LLC v Oak St. Check Cashing, Inc.*, LT-005388-12, 2013 N.Y. Slip Op. 50213(U), at 2 (Dist. Ct. Nassau Cty. Feb. 11, 2013) ("A landlord is required to provide a tenant with a predicate notice prior to the commencement of a non-payment summary proceeding. Pursuant to RPAPL §711(2), the notice must be made either by oral or a three (3) day written demand, *unless otherwise required pursuant to the terms of the parties' lease*." (emphasis added)); *626 E. 9 St. Hous. Dev. Fund Corp. v. Collins*, 712 N.Y.S.2d 261, 264 (N.Y. Civ. Ct. N.Y. Cty. 2000) ("Even in a rent-regulatory setting, the parties may negotiate terms of a lease that provide a tenant with greater rights than are otherwise required by law."). Critically, however, absent express and specific language to the contrary, the notice period provided in a standard conditional limitation provision will not impact the statutory notice required under RPAPL §735(2). Instead, a landlord can elect to *either* comply with the notice requirements of the lease's conditional limitation provision *or* to comply with the terms of RPAPL §735(2). Of course, if the lease specifies longer than the statutory three-day period for non-payment actions, the written lease agreement—and not the statute—will dictate landlord's notice requirement.

The landlord's choice has an important effect on the tenant. If the landlord elects to comply with RPAPL §711, the landlord-tenant relationship will be preserved while the landlord proceeds with a non-payment proceeding. Contrarily, if the landlord chooses to use a lease's conditional limitation, the tenancy will be immediately and automatically terminated upon the expiration of the notice period, and the landlord need only bring a holdover proceeding if the tenant refuses to vacate the premises.

Several decisions by New York courts reinforce a landlord's ability to elect between usage of the conditional limitation and the statutory non-payment mechanics provided in the RPAPL.

In *Frost Equities Co., LLC v. New York Brasserie Ltd.*, 61467/2004, 2004 NY Slip Op 51196(U) (N.Y. Cnty. Civ. Ct. April 22, 2004), the parties agreed in their lease that the "[t]enant shall not be deemed to be in default pursuant to this Lease by reason of its failure to pay rent unless [the landlord] shall give [t]enant notice of such failure and [t]enant fails to cure such failure to pay rent within five days thereafter." The lease further stated that "upon service of the notice to cure and expiration of the five days without a cure, the lease will terminate." Landlord did not provide five days' notice; instead, landlord sent a rent » Page 12

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Musings on **Mandated** Commercial Lease **Renewal**

BY HARLAN T. GREENMAN

The Small Business Jobs Survival Act (the Act) bill currently before the New York City Council seeks to regulate all commercial leases affecting property in the City of New York. The bill was introduced by Council Member Ydanis Rodriguez on March 22, 2018. The bill is predicated on the proposition that "New York City is more dependent than ever on small businesses for job growth and revenues" (the Act, §1) and that rising property values and other factors influencing the commercial rental market including real estate speculators have created a situation where "established small businesses are being forced out of business solely as a result of the commercial lease renewal process" (the Act, §1). The bill states that this has led to "lost jobs, tax revenues and community instability" (the Act, §1). The bill's stated intention is "to give small businesses rights in the commercial lease renewal process, and therefore, a measure of predictability of future costs through a two-step procedure of mediation and, if necessary, arbitration for negotiating commercial lease renewals and rentals" (the Act, §1).

From a substantive perspective, the bill would provide all commercial tenants in New York City with the absolute right to a renewal of their lease. The renewal term would be for a minimum of 10 years. Rent under the renewal lease would first be subject to mediation and then to binding arbitration.

The landlord may refuse to renew the lease for any of eight specified reasons. The first of those is if the tenant was a persistent late payer of the rent and certain notices were given within stipulated time frames (§22-1206(d)(1). References to §22-12xx refer to proposed new chapter 12 of Title 22 of the administrative code of the city of New York). If the tenant used the premises improperly (§22-1206(d)(2)) or illegally (§22-1206(d)(3)), the landlord would be able to refuse to renew the lease. The tenant would not be able to renew the lease if there is an uncured default for more than 30 days after notice (§22-1206(d)(4)). A bona fide intention to demolish or substantially rebuild the premises would allow the landlord not to renew the lease (§22-1206(d)(5)). If a court determines that the tenant is a "gross and persistent violator" of New York City laws, including tax and licenses (§22-1206(d)(7)), the lease would not have to be renewed. If the landlord intends to occupy a retail space to operate its own business, different from that of the tenant, then no lease renewal would be required (§22-1206(d)(8)). The last specified "exception" is for an unpermitted sublease (§22-1206(d)(6)).

While each of the various grounds for non-renewal has problematic elements, the narrow provision that is limited to an unpermitted sublease is most troublesome. Since the definition of "landlord" in the bill includes a "sublessor" (§22-1203), the bill would establish that a subtenant has a right to a renewal lease under the bill. The bill's requirement for a 10-year minimum renewal term raises the question how a renewal sublease could be effectuated if the prime lease lacks 10 remaining years of its own term. Would the sublessor be required to offer to renew the sublease if 10 years do not remain for the term of the prime lease? Since the prime lease may have more than 180 days remaining prior to its expiration, there would be no obligation on the part of the landlord of the prime lease to extend the prime tenant's (sublessor's) lease at that time. Certainly the bill should not by inferential extension create a situation where parties may only enter into subleases that upon their expiration would be coterminus with the related prime lease. In addition, if the sublessor does not desire to renew its prime lease or does not have the right to renew the prime lease at that time, does that mean that the subtenant has a right to a direct lease with the prime landlord or is the obligation to provide a renewal lease placed solely upon the sublessor? It would appear to create an undesirable burden upon sublessors to force them into a potentially perpetual cycle of subleases when their original intention in subleasing their premises was to relieve themselves of the burden of their lease for the remainder of the lease term at which time they could move on. If the subtenant were entitled to a direct lease with the » Page 13

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Real Estate Disputes Involving Delaware LLCs: **Does Forum Affect the Outcome?**

BY ADRIENNE B. KOCH

The Delaware limited liability company (LLC) is a popular form of business organization in the New York real estate industry. The reasons for this are probably as numerous and varied as the real estate projects in New York, but chief among them is a view that Delaware law offers more flexibility in certain key respects, including the extent to which members may contractually vary the obligations of managers.

For Delaware LLCs that own or manage New York real estate, disputes over the rights and obligations of members and managers are often litigated in the courts of New York—where the property is located, and where often the conduct at issue has occurred. Faced with such disputes, New York courts apply Delaware substantive law in determining those rights and obligations, but apply New York law to procedural matters. See, e.g., *Lerner v. Prince*, 119 A.D.3d 122, 127-29 (1st Dept. 2014).

Will the choice of a New York forum for such a dispute make a difference in the outcome? As a general matter, it should not. But the courts' efforts to ensure that it does not can sometimes lead to results that seem counter-intuitive. Some recent examples of this involve the procedure on motions to dismiss, the standard of appellate review, and the availability of an accounting.

Motions to Dismiss

Litigation concerning LLCs frequently includes derivative claims, where a member attempts to sue on behalf of the company—often seeking to hold managers liable for alleged breaches of their obligations to the company. To bring such a claim, the member must either demand that the LLC bring the claim itself and show that the demand was improperly refused, or show that such a demand would have been futile. See *Wandel v. Dimon*, 135 A.D.3d 515, 516 (1st Dept. 2016) (applying Delaware law).

Where a demand has been made and refused, the derivative plaintiff must meet a "heightened pleading standard" that requires particularized allegations showing that the refusal was wrongful and was not protected by the business judgment rule. See *Lerner*, 119 A.D. at 126. Those allegations are almost always met with a motion to dismiss based on an argument that the plaintiff has not met that standard.

Here, Delaware substantive law and New York procedural law appear to collide. Under the New York Civil Practice Law and Rules (CPLR), a motion to dismiss may be » Page 13

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Inside

REAL ESTATE: Angela Turturro, Sections Editor | Agnieszka Czuj, Design

MAKE A

Clear Choice

with Sightline

The New York skyline is constantly changing. We see it walking down the street, read about it in the news and are often part of the transactions. When it comes to purchasing a home in New York City, such frequent development can be worrisome; views can be obstructed, windows can be covered, or light and air can be hindered. Until now, there was no quick and cost-effective way to research how surrounding development could affect these assets.

Introducing Sightline

TitleVest's Sightline Report can give buyers greater peace of mind by providing research about potential development surrounding their prospective home. It inspects zoning regulations and recorded documents to calculate and illustrate unused development rights of neighboring properties. Going beyond the hypothetical, the report also provides a list of any active and significant construction permits to surface what owners of those properties may currently be planning. By taking into account all these aspects of development, the homebuyer has the opportunity to view potential and planned development in a report that includes a detailed 3-D model.

Development Rights

Though at times it may seem limitless, New York City development is controlled by complex zoning regulations. In fact, the New York City Zoning Text consists of over 4,000 pages that divide all New York City properties into different zones, sub-zones and other special districts. All of these zones and districts are governed by a set of rules that help determine each property's available development rights and how they can be used.

Zoning Districts are the underlying districts that regulate the ability to build on a property. Each zoning district is assigned a Floor Area Ratio, also known as FAR, that is used in the calculations that determine each property's available development rights. This calculation is:

- ☑ FAR x Lot Area = Available Development Rights (square feet)
- ☑ Zoning Districts also indicate bulk regulations that can affect a building's shape, such as maximum height.

Various other districts can also impact FAR, all of which are searched and surfaced within a Sightline Report.

Development Right Transfers

Development rights can also be transferred between properties via a zoning lot merger or a Transfer of Development Rights (TDR).

In a zoning lot merger, tax lots on the same block can combine into a zoning lot to convey development rights between each property. Properties that merge in this way must be contiguous for at least 10 linear feet, but can combine with properties further down the block as long as the intervening properties also join the zoning lot.

A TDR allows development rights to be transferred to lots on other blocks. This can only be done by: 1) Special District Transfers; 2) Off-Site Inclusionary Housing Transfers or 3) Landmark Site Transfers.

Once conveyed, these development rights can no longer be used by the transferring lot. A Sightline Report searches for and illustrates these recorded transfers.

Sightline in the Commercial Space

TitleVest's Sightline can also assist developers with site procurement for commercial property. In calculating and representing available development rights, developers can get a quick idea of what kind of construction is available to both their property and neighboring properties. There are a variety of use cases that can be implemented within a single report, allowing developers to envision the future of their prospective or existing property.

Your Sightline Report

Adjacent unused development rights may have a critical impact on a homebuyers' decision to purchase a property. The view, light and windows are not only monetarily valuable, but are also valuable to one's quality of life, which reinforces the need to understand how surrounding development could impact your transaction.

In the past, zoning analysis research has taken a great deal of time and money. For this reason, zoning and development rights due diligence has been widely under-utilized. The Sightline Report leverages TitleVest's technology to provide homebuyers with a timely and affordable solution. They can now order and receive an in-depth report within one business week. We follow up by offering a 1-hour phone consultation with one of Sightline's experts to review details of the report and answer any questions.

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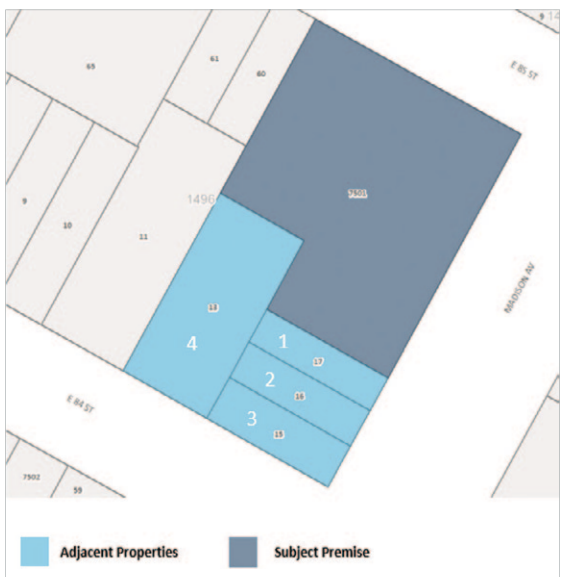
CASE STUDY

Your client is considering buying a unit on the 12th floor of 30 East 85th Street that looks south along Madison Avenue. There are three low-rise buildings immediately next door that, if expanded, would greatly affect the view from your client's prospective home. While another taller building to the southwest would not have as great an effect on the view, it would block western sunlight if built up.



Subject Property: 30 East 85th Street
Subject Property Height: 317.94 feet
Subject Property Floor Height: 10.60 feet
Searched Properties: 4

Special zones other than Zoning Districts can impact FAR.

THESE INCLUDE:

Special Districts: While basic due diligence may surface Zoning District FAR, it often does not consider the affect an overlying Special District may have. For instance, Midtown Special District grants many properties an even higher FAR, ultimately increasing their available development rights.

Limited Height Districts: This sub-district is overlaid in parts of the Upper East Side and lower Manhattan. While the base Zoning District might show one maximum height, the property's height will be limited further if it sits in a Limited Height District.

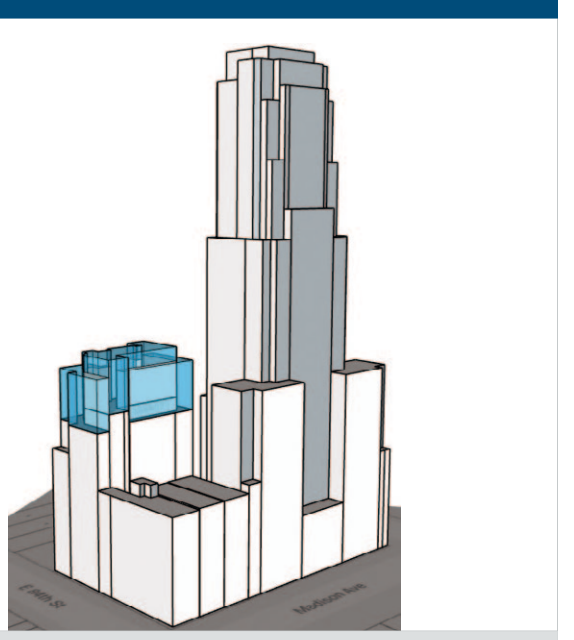
ZONING MAP

Zoning Districts: R8B and C5-1
Special Designations: Special Madison Avenue Preservation District, Metropolitan Museum Historic District & Limited Height District

TRANSFERS

Development Right Transfer(s)? Yes; 1, 2 & 3
Developed Rights transferred/available (sf):
Parcel 1: 7,420/0, Parcel 2: 8,670/0
Parcel 3: 8,670/0

RESULTS



Properties 1-3: No available development rights
Property 4: Enough development rights to build 3 additional floors, but is limited by Metropolitan Museum Historic District and LH-1A Limited Height District

Ultimately your client's immediate south-facing views along Madison Avenue are safe. Property 4, the building to the southwest, has enough development rights to build three additional floors. However, this property is in a historic district and a limited-height district, which would ultimately constrain its ability to develop. To use its development rights, the owner would have to apply for a special variance permit. Alternatively, it could transfer those development rights to an adjacent property on the block.

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Transfer Tax and the City

BY LIBIN ZHANG

On April 12, 2019, New York Governor Andrew Cuomo signed New York's 2019-2020 budget into law. One section of the new law will increase the transfer tax rates that apply to real estate transactions in New York City. The combined New York State and New York City transfer tax rates may approach 6% of the sales price for some residential transactions.

The new transfer tax rates are effective for property transfers on or after July 1, 2019. There is a limited grandfathering rule that exempts transfers made pursuant to a binding written contract entered into before or on April 1, 2019, provided that the contract's execution date is confirmed by a recording of the contract, payment of a deposit, or other independent evidence.

Introduction

New York State (NYS) and New York City (NYC) both impose transfer taxes on real estate transactions. Before the new law, there were three different transfer taxes on transactions of "residential real property," which generally includes a one-, two-, or three-family house, an individual condominium unit, or a cooperative apartment unit. Multifamily properties with four or more units are considered non-residential real properties and are subject to different tax rates discussed below.

The three transfer taxes for residential real property under prior law were:

(1) The NYS transfer tax of 0.4% of the total consideration for NYS property,

(2) The NYS additional transfer tax (sometimes called the "mansion tax") of 1.0%, if the consideration is $1 million or more for NYS property, and

(3) The NYC transfer tax of 1.0% for consideration of $500,000 or less, or 1.425% if the consideration is more than $500,000, for NYC property.

As a result, for NYC residential real properties, the tax rates under prior law for different levels of consideration were as indicated in **Chart 1**.

The consideration is generally the gross sales price of the residential real property, though sometimes reduced by any continuing mortgages on the property. The NYS and NYC transfer taxes are legally imposed on the seller, while the NYS mansion tax is legally imposed on the buyer; there is sometimes joint and several liability on the other party if the tax is not paid. The tax incidence is factored into the price as a practical matter, and some residential condominium transactions require the buyer to pay all taxes.

Example 1: Miranda has a growing family and decides to move to Brooklyn, so she purchases a brownstone for $5 million. The total NYS and NYC transfer taxes are $141,250 (2.825%), of which $91,250 (1.825%) is paid by the seller and $50,000 (1.0%) is paid by Miranda.

New York State's new law made two changes that effectively apply only to properties in New York City. First, the NYS transfer tax is increased from 0.4% to 0.65% for any transfer of NYC residential real property with $3 million or more of consideration, or any transfer of other NYC real property with $2 million or more of consideration.

Second, a new NYS supplemental transfer tax is imposed on any transfer of NYC residential real property with consideration of $2 million or more, at increasingly higher rates. The NYS supplemental transfer tax is imposed on the buyer, like the NYS mansion tax. As a result, for NYC residential real properties, the tax rates for different levels of consideration under the new law are as indicated in **Chart 2**.

Consideration	NYC Transfer Tax (paid by seller)	NYS Transfer Tax (paid by seller)	NYS Mansion Tax (paid by buyer)	Total Transfer Taxes
Up to $500,000	1.0%	0.40%	0%	1.40%
$500,000.01 to $999,999.99	1.425%	0.40%	0%	1.825%
$1,000,000	1.425%	0.40%	1.0%	2.825%

CHART 1

Consideration	NYC Transfer Tax (paid by seller)	NYS Transfer Tax (paid by seller)	NYS Mansion Tax (paid by buyer)	NYS Supplemental Tax (paid by buyer)	Total Transfer Taxes
Up to $500,000	1.0%	0.40%	0%	0%	1.40%
$500,000.01 to $999,999.99	1.425%	0.40%	0%	0%	1.825%
$1,000,000 to $1,999,999.99	1.425%	0.40%	1.0%	0%	2.825%
$2,000,000 to $2,999,999.99	1.425%	0.40%	1.0%	0.25%	3.025%
$3,000,000 to $4,999,999.99	1.425%	0.65%	1.0%	0.50%	3.575%
$5,000,000 to $9,999,999.99	1.425%	0.65%	1.0%	1.25%	4.325%
$10,000,000 to $14,999,999.99	1.425%	0.65%	1.0%	2.25%	5.325%
$15,000,000 to $19,999,999.99	1.425%	0.65%	1.0%	2.50%	5.575%
$20,000,000 to $24,999,999.99	1.425%	0.65%	1.0%	2.75%	5.825%
$25,000,000 or more	1.425%	0.65%	1.0%	2.90%	5.975%

CHART 2

Example 1A: Miranda signs a contract on April 15 to purchase a Brooklyn brownstone for $5 million and closes on July 15, 2019. Under the new law, the total NYS and NYC transfer taxes are $216,250 (4.325%), of which $103,750 (2.075%) is paid by the seller and $112,500 (2.25%) is paid by Miranda.

The new transfer taxes have severe cliff effects. Parties to a transaction where the sales price is slightly above a tax threshold may find it mutually beneficial to lower the price and pay significantly less taxes. If Miranda's Brooklyn brownstone were purchased for a dollar less at $4,999,999 of consideration, the total NYS and NYC transfer taxes would be $178,750, or $37,500 in tax savings.

Other Transactions

The new transfer taxes are imposed on the consideration in any "conveyance" of NYC real property. Conveyances are not limited to real property sales and may include other types of transfers of any interest in real property, including certain leasehold transactions.

Example 2: Carrie lives in a rent-controlled single condominium apartment on the Upper East Side. After she marries Mr. Big and moves in with him, she negotiates with her landlord for a $2.5 million buyout. The landlord pays $2.5 million to acquire and terminate her leasehold interest, which is a conveyance subject to $76,875 (3.075%) of total NYS and NYC transfer taxes.

> The new transfer tax rates are effective for property transfers on or after July 1, 2019.

Taxable conveyances may include certain non-cash transactions, such as like-kind exchanges or the transfer of real property from one spouse to another spouse pursuant to a divorce or separation agreement.

Example 3: As part of Charlotte's divorce from Trey, he transfers his 50% interest in their jointly owned Park Avenue apartment to her. If the apartment is worth $12 million, it is presumed that the consideration for the transfer is $6 million, which results in $259,500 (4.325%) of NYS and NYC transfer taxes.

Other types of taxable conveyances include the creation of a lease with a purchase option or a term of more than 49 years, gifts of debt-encumbered property, and some transactions involving options to acquire real property. Certain transfers of interests in entities that own real property may also be subject to NYS and NYC transfer taxes, such as a merger or acquisition of a corporation that owns a corporate apartment or other real estate.

Other Properties

For NYC non-residential real properties, the NYS mansion tax and NYS supplemental tax do not apply, the NYC transfer tax is at a higher rate, and the NYS tax rate of 0.65% starts at $2 million of consideration under the new law, as indicated in **Chart 3**:

Consideration	NYC Tax	NYS Tax	Total Tax
Up to $500,000	1.425%	0.40%	1.825%
$500,000.01 to $1,999,999.99	2.625%	0.40%	3.025%
$2,000,000 or more	2.625%	0.65%	3.275%

CHART 3

Example 4: Samantha's public relations business has an office lease in a Greenwich Village commercial building, with 12 years left. She moves to Los Angeles and assigns her below-market lease to Anthony for his wedding planning business, in exchange for a $2.1 million installment note payable over 12 years. The lease assignment is subject to $68,775 (3.275%) of NYS and NYC transfer taxes. Alternatively, Samantha may sublease the space to Anthony, in which case the rent is subject to the 3.9% NYC commercial rent tax and its exemptions.

As noted above, the new supplemental transfer tax applies only to transactions involving a one-, two-, or three-family house, an individual condominium unit, or a cooperative apartment unit. Multifamily properties with four or more residential units are considered non-residential real properties and are not subject to the NYS mansion tax or the supplemental transfer tax. In addition, case law and other authorities sometimes treat the purchase of two or more condominium units (or coop units) as a non-residential property transaction.

Conclusion

The new law did not enact a previously proposed "pied-à-terre" tax, which would have imposed a property tax of up to 4% annually on NYC residential real properties that were not occupied as a primary residence by an owner or a parent or child of an owner. Therefore, despite the pied-à-terre tax's name and intended target of unoccupied housing, it would have applied to many residential properties held for rental or occupied by a grandchild or more distant family member, as well as generally residential real properties owned by an LLC or other entity.

The New York State legislature was promptly educated on the pied-à-terre tax's shortcomings and decided instead to dramatically increase transfer taxes on NYC residential property transactions and to modestly increase transfer taxes on NYC non-residential property transactions. The changes may adversely affect real property sales and other real estate transactions in New York City that close on or after July 1, 2019, or at least encourage some transactions to close before the end of June.

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Cure

« *Continued from page 9*

demand and then, four days later, initiated a non-payment proceeding. The tenant argued that the rent demand provided by landlord prior to instituting a non-payment proceeding was insufficient given five-day requirement in the lease.

The court held that the landlord was allowed to elect to proceed by non-payment proceeding rather than the conditional limitation in the lease. Indeed, the court noted that the landlord's "choice to pursue a nonpayment proceeding under [RPAPL] §711(2) [was] in fact the very antithesis of declaring respondent's default and terminating the lease" because a non-payment proceeding is premised on the tenant still being a tenant under an unexpired rental agreement. A major difference, noted the court, was that in the non-payment proceeding, the tenant still had the right to honor the lease and pay any judgment for rent to avert a warrant of eviction and keep the rental agreement in effect. Accordingly, the landlord was not required to provide the extended notice required by the conditional limitation and could, instead, institute a non-payment proceeding on three-days' notice.

Similarly, in *Reckson Operating Partnership, L.P. v. LJC Corp.*, 2007-142 N C., 2007 NY Slip Op 52335(U) (N.Y. App. Div. 2d Dep't. 2007), the parties agreed in the lease that "upon the occurrence … of any one or more of the following events …: (i) If Tenant shall default in the payment when due of any installment of rent … and such default shall continue for a period of ten (10) days after notice by Landlord to Tenant of such default … then … Landlord, at any time thereafter, at Landlord's option, may give to Tenant a five (5) days' notice of termination of this lease … ." The Landlord commenced a non-payment proceeding and provided three-days' notice. Like in *Frost Equities*, the court held that nothing in the lease prevented landlord from maintaining a nonpayment proceeding without serving a 10-day notice.

Given the foregoing cases, it is clear that a tenant must be wary of relying on the defense of improper notice in a non-payment proceeding if the landlord provides three days' notice under the RPAPL but does not comply with the notice required by a conditional limitation in the lease. If the parties to a lease desire to extend the notice period required for both termination of the lease by conditional limitation *and* the initiation of a non-payment proceeding, they must do so using express language. For example, in *Hendrickson v. Lexington Oil Co.*, 340 N.Y.S.2d 963 (2d Dep't. 1973), the lease stated that the landlord would give the tenant 30 days' notice "before the landlord shall be entitled to commence *any proceeding* to enforce its rights [under the lease,] … except, however, for default in rent for which the tenant shall be entitled to only 10 days' notice." The landlord did not provide 10 days' notice prior to instituting a non-payment proceeding. The court held that the 10 days' notice was required because of the "any proceeding" language in the lease.

In sum, parties to a lease must be clear about the notice requirements for both conditional limitations and any amendments to the statutory notice required under RPAPL prior to instituting a non-payment proceeding. Absent such clarity, a landlord will likely be able to elect whether to comply with the conditional limitation notice requirements or, if it wants to use a shorter period, whether to comply with the three-day statutory requirement in RPAPL 711(2) before instituting a non-payment proceeding.

Can a **Combined Zoning Lot** Include a Partial Tax Lot?

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BY CHRISTOPHER WRIGHT

Recently, the Manhattan Supreme Court issued a decision regarding the definition of zoning lots. The issue before the court was whether the New York City zoning regulations mandate that a zoning lot containing more than one tax lot (a "combined zoning lot") must include the entire tax lot or can it include a portion of a tax lot. See *The Committee for Environmental Sound Development v. Amsterdam Avenue Development Associates LLC,* 2019 WL 1206357 (N.Y. Sup.), 2019 N.Y. Slip Op. 30621 (U) (Trial Order) Hon. W. Franc Perry).

The matter involved three proceedings. First, an application was submitted to the New York City Department of Buildings (the DOB) seeking a permit to construct a 55-story residential building based on a combined zoning lot that included partial tax lots. Second, the DOB permit was appealed by a local civic group to the New York City Board of Standards and Appeals (the BSA) alleging that the combined zoning lot's use of partial tax lots did not comply with zoning regulations. Third, after the BSA rejected the appeal and upheld the permit based on a finding that the combined zoning lot was zoning compliant, a lawsuit was filed alleging that the combined zoning lot was faulty and that the BSA was in error. The court reversed the BSA and held that the plain language of the zoning regulations prohibited a combined zoning lot from including portions of tax lots.

These proceedings involved complex zoning arguments, however the central issue was relatively simple. The question to be decided is: Can a zoning lot that consists of more than one tax lot include a portion of another tax lot or must it include the entire tax lot?

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Tax lots are combined into a single zoning lot for the purpose of transferring development rights or other zoning requirements between the tax lots to achieve a more efficient development scenario. The combined zoning lot in question was being used to construct a 55-story building located at 200 Amsterdam Avenue that abuts the Lincoln Towers residential complex located between Amsterdam and West End Avenues, between 66th and 70th Street. Lincoln Towers houses several thousand apartments and has large open areas between the buildings that are used as green space and driveways for the residents. These open areas are considered "open space" pursuant to the New York City Zoning Resolution (the ZR). All residential developments are required to provide a certain amount of open space, depending on the size of the building.

The developer of 200 Amsterdam Avenue wanted to create a combined zoning lot to transfer both development rights and open space from Lincoln Towers to the proposed project. The transfer of development rights was significant, totaling over 200,000 sq. ft. of zoning floor area. The open space transfer was carefully calculated to satisfy the open space requirements generated by the transferred development rights.

Certain residential zoning districts do not have building height limits. These are called height factor buildings. Height factor requires a series of setbacks as the building goes higher, causing the building to taper at the higher floors. The tapering factor defines the "zoning envelope." The building must be constructed within the zoning envelope. However, as the building goes higher, more open space is required at the ground level to allow light and air to reach the streets and sidewalks.

The Zoning Diagram of the proposed building submitted to DOB demonstrated that a tapering 55-story building could be built on the development site using the applicable height factor zoning envelope. (The Diagram can be located on the DOB website.) However, due to the size of the building the tax lots comprising the development site were not large enough to provide the required open space. To solve this problem a combined zoning lot was created that included portions of the Lincoln Tower open space, including the green space and driveways. This open space was located on portions of various tax lots throughout the Lincoln Towers complex. The combined zoning lot allowed the development site to claim this open space as satisfying the open space requirement for the 55-story building. Essentially, portions of Lincoln Towers' open space were transferred to the development site, not physically like development rights, but for the purpose of satisfying open space zoning calculations.

The development site is at the corner of West 69th Street and Amsterdam Avenue. As shown on the Zoning Diagram, the combined zoning lot basically extends tentacles from the development site to encircle the Lincoln Towers green space and driveways. The combined zoning lot crosses several of the Lincoln Towers tax lot lines to reach this open space.

During these proceedings, the parties on both sides referenced numerous zoning regulations that used the terms "zoning lot" and "tax lot." The proponents of partial tax lots argued that the zoning regulations were vague and never explicitly stated that a combined zoning lot must include the entire tax lot. The parties in opposition argued that the plain language of the zoning regulations clearly inferred that full tax lots must be included in any combined zoning lot.

The proponents also referenced a 1978 DOB memorandum (the Minkin Memo) that stated that combined zoning lots could include "parts of tax lots" and argued that this had been the standard interpretation for 50 years. The developer identified 34 examples of combined zoning lots containing partial tax lots. However, the court distinguished all of these combined zoning lots as applying to special circumstances not applicable to the developer's combined zoning lot.

The court reversed the BSA and held that the **plain language of the zoning regulations** prohibited a combined zoning lot from including portions of tax lots.

Interestingly, during the BSA proceedings the General Counsel Office for DOB requested that the BSA uphold the subject combined zoning lot (DOB had issued the 200 Amsterdam permits and construction had commenced) based on the current interpretation of the Minkin Memo. However, at the same time DOB testified that the Minkin Memo was in error and that, in fact, the ZR required combined zoning lots to include full tax lots. DOB went further and stated that a revised DOB memo would be issued shortly correcting this error and clarifying that combined zoning lots must include full tax lots. In its decision to annul the combined zoning lot, the court gave great weight to DOB's testimony and the pending retraction of the Minkn Memo's language regarding partial tax lots. It was the court's opinion that DOB has the legal authority to retract permits issued in error and that these permits were, in fact, issued based on a flawed zoning lot.

I have never come across a combined zoning lot using partial tax lots. In addition, although the court did not address this issue, for the residential developments that I have analyzed, the required open space is in proximity to the building for the purpose of providing an amenity to the residents. Here, the open space had no physical relationship to the 55-story building. Open space designed for use by Lincoln Towers residents was being used to give the proposed building open space credits. The proposed building itself was not creating any new open space.

Despite this ruling, the importance of the Minkin Memo to zoning should be not be diminished. This decision could be interpreted as holding that the Minkin Memo imposed a flawed zoning doctrine for 50 years. That is not the case. It was the Minkin Memo's interpretation of the ZR that provided the road map to creating combined zoning lots. The Minkin Memo, written in 1978, offered an interpretation of a 1977 amendment to the ZR that permitted the creation of combined zoning lots for development purposes. The Minkin Memo specifically referenced five documents (with templates attached) to be recorded that would effectuate the combined zoning lot and allow DOB to issue building permits. Every combined zoning lot created since 1978 has followed the Minkin Memo's direction. The Minkin Memo did state "parts of tax lots," but these four words have had little to no impact on the combined zoning lot industry that the Minkin Memo spawned and the resulting zoning flexibility it afforded to developments.

Renewal

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prime landlord upon the expiration of the term of its sublease, would that direct lease be for only the remaining portion of the 10-year period following the expiration of the prior sublease or would the prime landlord be required to offer the subtenant a full 10-year term at that time? However, since there is no expiring lease between the prime landlord and the subtenant, would the bill apply to this situation at all as any lease from the prime landlord would not be a renewal?

If the landlord has no valid reason to refuse to renew the lease, the statutory regime would then apply. The landlord would need to provide a notice to the tenant at least 180 days before the expiration of the lease of the intention to renew the lease. The 180-day notice triggers a 90-day period during which the parties are intended to negotiate to reach an agreement concerning a renewal lease "with any agreed to terms and conditions, not inconsistent with the provisions of this chapter" (§22-1206(e)(1)). It is unclear which provisions of a negotiated agreement between the landlord and the tenant may be inconsistent with the bill. While the bill specifically states that "a lease of shorter or longer duration may be selected" (§22-1206(a)) by the tenant, subject to the landlord's agreement, would it be inconsistent with the bill if the parties were to include a unilateral termination right in the lease on the part of the landlord for a prospective future demolition of the building during the term of the lease and prior to 10 years from the beginning of the renewal term?

In fact, would the landlord be able to refuse to renew the lease, pursuant to the bill's grounds for non-renewal, if the landlord were to cite as its reason for non-renewal a bona fide intention to demolish or substantially rebuild the premises within the 10-year period following the scheduled expiration date of the lease then in force? What would then be the result if the landlord's plans were to change during the 10-year period due to changed circumstances, such as an economic downturn or unavailability of financing?

The mandatory renewal scheme that the bill would establish would also not allow a landlord to eliminate an undesirable use from its property. For example, as societal attitudes have shifted, uses that were at one time in vogue, such as a tobacco shop, may later become out of favor and a landlord may not want its property to play host to such a business. Also, uses that were relatively non-controversial may later become the focus of protests, which an owner may also prefer to avoid as there could be resultant negative effects on other tenants in the building, some of whom may even choose to locate elsewhere, leaving the landlord with an underperforming property.

It should be noted that even during the initial 90-day period following the giving of the 180-day notice of intention to renew given by the landlord, either party may demand mediation at any time. Pending a determination of the renewal period rent, the tenant must continue to pay rent at the rate set forth in the expiring lease. If the landlord and the tenant do not reach an agreement or do not accept the mediator's non-binding determination of the renewal lease rent, then the tenant may require binding arbitration to determine the rent (§22-1206(e)). If the tenant is unwilling to pay the rent determined by the arbitrator, the tenant may choose not to proceed with the renewal. But subject nevertheless to a right to remain in the premises beyond the lease expiration date at the last rent charged under the lease plus 10%. The tenant still retains a right of first refusal on any subsequent deal the landlord reaches with a new tenant (§22-1206(g)).

The bill lists numerous criteria to be considered by the arbitrator in determining rent. However, the bill does not take into account the realities of New York City. For example, one factor is "the cost of leasing similar premises within a one-mile radius of the property" (§22-1206(e)(3)(d) and (e)) and "the past five year rental market history within a one mile radius of the property" Id. In Manhattan, for example, the market based differences in rental cost within a one-mile radius can be as vast as the distances between galaxies in the cosmos.

It should also be noted that a stated factor arbitrators should use in determine rent under the bill is "the rental guidelines as set forth by the administering agency" (§22-1206(e)(3)(d) and (e)). It is possible that any such guidelines will be construed as an attempt at rent control, somewhat akin to the rent stabilization guidelines that regulate rents for certain residential properties in New York City.

In fact, it is open to debate whether the entire bill is beyond New York City's power in the absence of enabling legislation by New York State. This issue has been raised by the New York City Bar in a Report on Legislation by the Committee on Real Property Law.

LLCs

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denied where "affidavits submitted in opposition" indicate "that facts essential to justify opposition may exist but cannot then be stated." CPLR 3211(d). Under those circumstances, the court may "order a continuance to permit … disclosure to be had." Id. Under Delaware law, however, a derivative plaintiff in a demand-refused case is "not entitled to discovery" in order to meet the applicable pleading requirements. See *Scattered Corp. v. Chicago Stock Exch., Inc.*, 701 A.2d 70, 77 (Del. 1997), overruled in part on other grounds, *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

What happens in a New York court when a pre-answer motion to dismiss a demand-refused derivative claim governed by Delaware law is met with a request for discovery under CPLR 3211(d)? In *Lerner*, supra, the court held that Delaware law applied; on that basis, it affirmed the lower court's denial of the plaintiff's request for discovery. 119 A.D.3d at 127-29.

Because CPLR 3211 is on its face a rule of procedure, this might seem unusual at first blush. The court reasoned, however, that "[a]lthough New York courts have applied the law of the forum when deciding matters, such as discovery, affecting the conduct of the litigation … Delaware law on discovery is an integral part of the legal framework governing derivative proceedings … ." 119 A.D.3d at 128 (citations omitted). To allow discovery under CPLR 3211(d) with respect to a derivative claim governed by Delaware law would therefore "almost certainly lead future plaintiffs to forum shop in an effort to circumvent the Delaware prohibition against discovery." Id. at 129. The court therefore held that Delaware law on discovery was substantive and CPLR 3211(d) should not displace it.

Standard of Review

Another area that has generated recent case law on the distinction between substance and procedure in derivative claims relates to the standard of review on an appeal from a dismissal for failure to make a demand. Under New York law, such a dismissal is reviewed for abuse of discretion. See *Marx v. Akers*, 88 N.Y.2d 189, 192 (1996); accord *Deckter v. Andreotti*, 170 A.D.3d 486, 487 (1st Dept. 2019); *PDK Labs, Inc. v. Krape*, 277 A.D.2d 212 (2d Dept. 2000). Under Delaware law, however, "appellate review of a lower court's decision to dismiss on the ground that demand was not excused 'is de novo and plenary.'" *Deckter*, 170 A.D.3d at 486 (quoting *Brehm*, 746 A.2d at 253).

Which standard applies if Delaware law governs substance but New York law governs procedure? In *Deckter*, the court chose Delaware law and reviewed the lower court's determination de novo.

As a practical matter, this may not have made much difference at the Appellate Division level. "The Appellate Division, as a branch of the Supreme Court, is vested with the same discretionary power and may exercise that power, even when there has been no abuse of discretion as a matter of law by the nisi prius court." *Small v. Lorillard Tobacco Co., Inc.*, 94 N.Y.2d 43, 52-53 (1999) (citation omitted). If a matter reaches the Court of Appeals, however, the difference in the standard of review could impact the outcome. See id. Treating it as substantive rather than procedural ensures that the choice of forum has as little effect on the outcome as possible. The overall result here is thus to the same effect as *Lerner*.

Accounting

A third area where procedural differences between Delaware law and New York law have recently been explored in the context of claims involving an LLC is the availability of an accounting. Under Delaware law, accounting is only an "equitable remedy" for a breach of duty; it is not a cause of action in itself. *Garza v. Citigroup, Inc.*, 192 F. Supp. 3d 508, 511-12 (D. Del. 2016). In contrast, under New York law a request for an accounting may proceed as an independent cause of action. See generally 1 N.Y. Jur. 2d Accounts and Accounting §37.

What happens when a New York court is called upon to adjudicate a claim for an accounting against a manager of a Delaware LLC? In *Estate of Calderwood v. ACR Group Int'l LLC*, 157 A.D.3d 190, 198-99 (1st Dept. 2017), lv. dism'd, 31 N.Y.3d 1111 (2018), the court held that the availability of an accounting is a "matter[] of procedure" governed by New York law even where Delaware law governs on substance. Accordingly, a plaintiff suing in a New York court under Delaware law can seek an accounting as a freestanding claim, even though such a claim could not proceed in a Delaware court.

In *Calderwood*, the application of New York law on a "procedural" matter technically meant that the plaintiff could assert a cause of action that did not exist under Delaware law. That sounds like a substantive difference. Importantly, however, it did not actually change the outcome: The court went on to dismiss the accounting claim based on the absence of a fiduciary relationship. 157 A.D.3d at 198-99. This is consistent with New York law: A claim for an accounting requires "a confidential or fiduciary relationship and a breach of the duty imposed by that relationship" (or, at the very least, "some other special circumstances"). *Adam v. Cutner & Rathkopf*, 238 A.D.2d 234, 242 (1st Dept. 1997) (citations and internal quotations omitted).

Under these principles, the theoretical ability to bring a free-standing accounting claim will generally add nothing if the plaintiff does not also have a claim for breach of fiduciary duty. Since such a claim is exactly what the plaintiff would need in order to be able to seek an accounting as part of its remedy in a Delaware court, the procedural difference once again does not change the result.

Conclusion

There is a unifying principle in these cases: The courts attempted to ensure that the application of New York procedural rules would not change the outcome. This is significant, because a member of a Delaware LLC that owns or manages New York real estate will often have a choice as to whether to bring claims in New York or in Delaware.

The choice of forum is a weighty decision that should be very carefully considered. In some cases, it may make a real difference. But choosing a New York forum for a Delaware dispute will not automatically subject the dispute to New York procedural rules that differ from Delaware law. As these cases make clear, the analysis is more nuanced and looks to obviate those differences.