EA 8/12/15 E

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: LOBIS Justice

PART 6

SBT COOPERATORS FOR MITCHELL-LAMA, ETAL.

-v-

N.Y.S. DIVISION OF HOUSING AND COMMUNITY RENEWAL, ETAL.

INDEX NO. 100297/15

MOTION DATE

MOTION SEQ. NO. 01

The following papers, numbered 1 to ____, were read on this motion to/for ____

Notice of Motion/Order to Show Cause — Affidavits — Exhibits ____ | No(s). 1

Answering Affidavits — Exhibits (2 respondents' 2, & 3-5) | No(s). 2-5

Replying Affidavits ____ | No(s). 6-7

Upon the foregoing papers, it is ordered that this motion is

RECEIVED
AUG 12 2015
GENERAL CLERK'S OFFICE
NYS SUPREME COURT - CIVIL

THIS MOTION IS DECIDED IN ACCORDANCE WITH THE ACCOMPANYING MEMORANDUM DECISION & ORDER

The clerk of court is directed to enter a judgment of dismissal.

UNFILED JUDGMENT

This judgment has not been entered by the County Clerk and notice of entry cannot be served based hereon. To obtain entry, counsel or authorized representative must appear in person at the Judgment Clerk's Desk (Room 141B).

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: 8/11/15

, J.S.C.

1. CHECK ONE: ..... ☑ CASE DISPOSED ☐ NON-FINAL DISPOSITION

2. CHECK AS APPROPRIATE: .....MOTION IS: ☐ GRANTED ☐ DENIED ☐ GRANTED IN PART ☐ OTHER

3. CHECK IF APPROPRIATE: ..... ☐ SETTLE ORDER ☐ SUBMIT ORDER

☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 6
----------X

SBT COOPERATORS FOR MITCHELL-LAMA
and SBT SHAREHOLDERS ASSOCIATION

Petitioners,

-against-

Index No.: 100297/15

NEW YORK STATE DIVISION OF HOUSING
AND COMMUNITY RENEWAL and
SOUTHBRIDGE TOWERS, INC.,

Respondents.

----------X

JOAN LOBIS, J.:

In this Article 78 proceeding, petitioners SBT Cooperators for Mitchell-Lama and SBT Shareholders Association (collectively Petitioners) seek an order annulling respondent New York State Division of Housing and Community Renewal's (DHCR) approval of a November 24, 2014 shareholder vote in favor of permitting Southbridge Towers (SBT) to exit the Mitchell-Lama program and become a private, market-rate cooperative.

BACKGROUND

A. Mitchell-Lama

In 1955, the New York State legislature adopted the Private Housing Finance Law (PHFL), Article II – "The Mitchell-Lama Law" – to offer private housing companies financial incentives to develop low and moderate income housing. See KSLM-Columbus Apts., Inc. v New

York State Div. of Hous. & Community Renewal, 5 N.Y.3d 303, 308 (2005). The Mitchell-Lama program encourages the development of this moderately priced housing "by offering State and municipal assistance to developers in the form of long-term, low-interest government mortgage loans and real estate tax exemptions." Columbus Park Corp. v Department of Hous. Preserv. & Dev. of City of N.Y., 80 N.Y.2d 19, 23 (1992). In exchange for receiving these benefits, developers must agree to "regulations concerning rent, profit, disposition of property and tenant selection." Id.

Because Mitchell-Lama housing developments provide housing for low to moderate income families, the demand for these apartments far exceeds the available supply. As a result, each housing company maintains waiting lists. A person can become a lawful tenant of a Mitchell-Lama apartment in only two ways: 1) by being selected from a waiting list established by the housing company and demonstrating that the income eligibility guidelines have been met, or 2) by demonstrating the right to succeed a family member who has died or relocated. See 9 NYCRR 1727-1.3 [d] and 9 NYCRR 1727-8.1 and 1727-8.2); Waldman v New York City Dept. Of Hous. Preserv. & Dev., 10 Misc. 3d 1075 [A], 2005 NY Slip Op 52241 [U] (Sup. Ct. N.Y. County 2005) *3, aff'd 36 A.D.3d 501 (1st Dep't 2007).

PHFL § 35 (2) provides that a limited profit housing company, like SBT, may, 20 years after the first occupancy date, voluntarily withdraw from the Mitchell-Lama program, without the consent of DHCR, and reconstitute itself as a private, market-rate cooperative entity. This process is known as privatization. After privatization, the apartments can be sold, by their owners, on the open market at market rates and prior restrictions on tenancy and income are no longer applicable.

Although DHCR's consent for privatization is not required, the agency provides regulatory oversight for the dissolution and reconstitution of a limited-profit housing company as a private cooperative. In particular, DHCR's regulations require three shareholder votes. First, the shareholders must vote to conduct a feasibility study of the housing company's dissolution. 9 NYCRR 1750.13 [c] [1]. Second, a majority of the shareholders must vote to file a notice of intent to dissolve with DHCR and to authorize the expense of preparing and filing an offering plan with the Office of the New York State Attorney General (OAG). 9 NYCRR 1750.13 [c] [2]. The third shareholder vote, and the one that forms the gravamen of this controversy, requires that two-thirds of the shareholders vote in favor of authorizing the dissolution of the Mitchell-Lama Housing Company and its reconstitution as a private company. See 9 NYCRR 1750.7.

B. Southbridge Towers

SBT is a limited-profit cooperative housing company that was incorporated in 1967 under the Mitchell-Lama Law. SBT, which is located in lower Manhattan, is comprised of nine buildings that house 1,651 residential apartments. Because the buildings have been occupied since 1970, SBT became eligible for privatization in 1990.

In 2005, a majority of SBT's shareholders voted in favor of conducting a feasibility study regarding SBT's dissolution and reconstitution as a private company. Thereafter, in 2007, a majority of SBT's shareholders voted in favor of authorizing the expenditure of funds to prepare an offering plan for submission to OAG.

Prior to that 2007 vote, SBT sought DHCR's advice regarding how the shareholder votes should be tallied and which, if any, shares should be disqualified in calculating the result. In a letter dated October 1, 2007, DHCR wrote:

> "As you know, the general rule for a shareholder vote is that one vote may be cast for each apartment by the shareholder of record, and the total number of shareholders for the purposes of the vote is the total number of apartments for which there is a shareholder of record. While there may be circumstances that call into question a shareholder's right to continue as shareholder of record, the shareholder generally retains the right to vote the shares until such time as a final adverse determination has been made and the shares have been surrendered.
>
> "DHCR is of the opinion that the general rule should befollowed in the upcoming vote with one exception discussed below. As you know, a previous attempt by DHCR to apply a similar calculation to other types of questionable tenancies (which you have also requested here) resulted in a court order directing that the subject tenants be permitted to vote.
>
> "Section 1727-g.4 (a) of the regulations provides that the shares allocated to an apartment must be surrendered upon the death of a cooperator. Accordingly, where you can demonstrate by credible documentary evidence . . . that the shareholder of record is deceased, you may decline to count any vote attributable to that apartment . . ."

Thereafter, in a letter dated October 22, 2007, DHCR responded to a letter from SBT seeking guidance regarding the treatment of specific categories of shareholders for the vote to authorize the preparation of an offering plan. In that letter, DHCR stated: 1) succession[1] applicants

[1] DHCR's successions regulations for Mitchell-Lama housing set forth the procedures by which certain family members may apply to the housing company for ownership rights. 9 NYCRR 1727-

are not permitted to vote; 2) votes by a shareholder of record who does not appear on the income affidavit should be segregated for examination and a decision about whether to count the vote; and 3) shareholders of record for two apartments may cast only one vote. Id., exhibit D. Based on these guidelines, SBT's shareholders voted, by an overwhelming majority, to authorize the expenditure necessary to prepare and file the offering plan with OAG.

The offering plan, which was submitted to OAG, explained the procedures for the final privatization vote. It stated that the "Plan of Reconstitution requires the affirmative vote of at least two-thirds (66 2/3%) of the shareholders; however shareholders shall be entitled to one vote per Apartment, regardless of the number of shareholders listed on the Occupancy Agreement or Stock Certificate." Id., exhibit E. That offering plan also incorporated the following information regarding which categories of shareholders would be entitled to cast a ballot in the final vote for reconstitution and which categories would be excluded:

> "Only individual Shareholders of record who are in good standing will have the right to vote for or against the Plan of Reconstitution, as confirmed by communications with DHCR. In accordance with the communications with DHCR, no vote will be counted from the following apartments: (a) each apartment for which there is credible documentary evidence that the shareholder of record is deceased; (b) each "Capital Grant" apartment,[2] (c) only one vote

8.2 provides that the applicant must have resided in the apartment, as his or her primary residence, with the tenant of record for the two years prior to the tenant's death or departure. Succession applications are first determined by the housing company, subject to review by DHCR (9 NYCRR 1727-8.4).

[2] Capital Grant apartments are part of a program administered by the New York State Housing Finance Agency (HFA). Under the program, HFA owns the apartments and sub-leases them to low-income tenants; the tenants themselves are not shareholders.

> will be cast by a shareholder of record in transition from one apartment to another; (d) any apartment for which there are unresolved succession claims; (e) any employee apartments and (f) apartments that have been vacated by shareholders and which are being assigned new shareholders or have been assigned to shareholders who are awaiting DHCR approval."

On March 20, 2014, SBT submitted the offering plan to the OAG. After comment and revisions, the OAG accepted the offering plan for filing. SBT then distributed a copy of the offering plan to each shareholder. SBT held the required Public Information Meeting on July 29, 2014. See 9 NYCRR §§ 1750.3 and 1750.5. In addition, prior to that required meeting, on June 4, 2014, SBT held a separate meeting for the shareholders with respect to questions they might have about the offering plan.

Disqualified Apartments

Prior to the third vote, SBT provided DHCR with a list of 44 apartments that failed to meet the "good standing" requirement and were deemed ineligible to vote. According to DHCR: a) five apartments were disqualified because the shareholders of record had died prior to the vote; b) 20 apartments were disqualified because an application for succession rights was pending and unresolved at the time of the vote; c) four apartments were part of the "Capital Grant" program; d) five apartments were excluded because the shareholders of record were moving from one apartment to another, and were listed, temporarily, as shareholders of both apartments. These shareholders

were permitted to vote once but not twice; e) eight apartments were listed as vacant but unassigned[3]; and f) two apartments were employee apartments.

The Third Vote

On September 28 through September 30, 2014, SBT held the election in which the shareholders voted to determine whether the housing company would dissolve and reconstitute as a free-market cooperative. The vote was administered by Honest Ballot Association (HBA), a private, independent organization with experience in conducting, supervising and certifying elections. On October 1, 2014, HBA certified that more than two-thirds of SBT's shareholders had voted in favor of privatization. Specifically, HBA certified that out of 1,458 valid votes received, 1,082 supported privatization, 373 opposed it, and 3 abstained. The affirmative votes were ten more than the 1,072 votes needed to constitute two-thirds of the eligible apartments. On October 2, 2014, SBT notified DHCR that the dissolution resolution had been accepted and passed by SBT's shareholders.

Thereafter, Petitioners contacted DHCR requesting detailed information regarding the process undertaken to ensure that the vote followed proper procedures and an audit of the dissolution vote. Accordingly, DHCR contacted HBA and requested specific information about how the vote was conducted. In response to DHCR's request, HBA noted that it strictly followed

[3] For the vacant but unassigned apartments, applicants had been chosen but closings had not taken place and shares had not been issued for those apartments.

the procedures set forth in the offering plan and that these same procedures were used in the May 2013 and May 2014 elections of directors. HBA also noted that the procedures it followed in all of the votes had been subject to DHCR's review and approval.

By letter dated November 24, 2014, DHCR notified Petitioners that an audit of the dissolution vote was not required because "the certification and narratives provided by HBA provide satisfactory evidence that the resolution was approved by a vote of two thirds of the shareholders who were entitled to vote." The letter provided Petitioners with a detailed description of the safeguards that had been implemented to ensure a fair vote. Specifically, DHCR noted that: 1) the involvement of SBT's management office and Board had been minimized; 2) the printing and distribution of election packets had been conducted by HBA; 3) substitute proxy ballots could only be obtained through HBA; and 4) only HBA had access to the lock-boxes where proxies were deposited and each proxy was individually bar-coded to prevent unauthorized duplication. The letter also detailed the procedures HBA used to verify the proxies and certify the vote count. In that letter, DHCR took the position that the 44 apartments disqualified from voting had been properly excluded. In particular, with respect to the succession cases, the letter stated that "[a]s to 16 of the 20, DHCR has firsthand knowledge, as the agency has been involved in processing them . . . [and] DHCR has documents from Southbirdge's management . . . establishing the existence of the [other four] cases."

Pursuant to its regulations, DHCR issued a certification to the Secretary of State stating that SBT had complied with the requirements of the PHFL and, accordingly, DHCR had no objection to SBT's filing the certificate of dissolution. See 9 NYCRR § 1750.14.

Thereafter, Petitioners commenced this Article 78 proceeding seeking to overturn, as arbitrary and capricious, DHCR's determination that SBT had provided satisfactory evidence that more than two-thirds of the shareholders who were entitled to vote had approved the resolution to exit the Mitchell-Lama program and reconstitute as a private market cooperative. In support of the petition, Petitioners argue that DHCR contravened its own regulations by disqualifying certain classes of voters. Petitioners take the position that all shareholders of record should have been included in the vote and that the decision to disqualify most of the 44 units was arbitrary and without statutory and regulatory authority. In addition, Petitioners contend that DHCR's approval of the voting procedures and result was unfounded because it made no independent effort to review and verify actual voting records or ballots, proxies, voting machine records and tally sheets.

In opposition to the petition, DHCR and Southbridge Towers, Inc. argue that the 44 apartments were properly excluded from voting because those apartments had no eligible tenants of record "in good standing." It is DHCR's position that: 1) the estates of deceased tenants cannot vote; 2) occupants of "capital shares" apartments are not shareholders; 3) building employees occupying the employee apartments are not shareholders; 4) for the succession cases there was no person, in good standing, qualified to vote because the shareholder of record had died or permanently moved out; 5) for vacant but unassigned apartments there was no shareholder of record because the closings has not occurred and shares had not been issued to the new owners; and 6) for shareholders temporarily owning two apartments, DHCR regulations and Southbridge Towers Certificate of Incorporation permit only one vote per shareholder regardless of the number of shares held by the shareholder. Moreover, DHCR contends that it was not required to independently verify

the vote count. Rather, it claims that its role was limited to determining whether the evidence established that the resolution for SBT's dissolution and reconstitution was carried by the required two-thirds majority, and, based on the information and evidence it received from HBA, its determination regarding the vote was reasonable.

DISCUSSION

The standard of review in this Article 78 proceeding "is whether DHCR acted in an arbitrary and capricious manner, in violation of lawful procedures, or in excess of its jurisdiction." 73 Warren St., LLC v State of N.Y. Div. of Hous. & Community Renewal, 96 A.D.3d 524, 526 (1st Dep't 2012)(citing Pell v Board of Educ. of Union Free School Dist. No. 1 of Towns of Scarsdale & Mamaroneck, Westchester County, 34 N.Y.2d 222 (1974)). A court's function is to determine whether a rational basis exists for the action of the administrative agency. See Arif v New York City Taxi & Limousine Comm., 3 A.D.3d 345, 346 (1st Dep't 2004). Where there is a rational basis to support the decision, a court may not substitute its judgment for that of the agency, Howard v Wyman, 28 NY2d 434, 438 (1971), and it must sustain the determination even if the court concludes that it would have reached a different conclusion. Peckham v Calogero, 12 N.Y.3d 424, 431 (2009). Moreover, the Court of Appeals has "repeatedly held that the interpretation given to a regulation by the agency which promulgated it and is responsible for its administration is entitled to deference if that interpretation is not irrational or unreasonable." Gaines v New York State Div. of Hous. & Community Renewal, 90 N.Y.2d 545, 548-549 (1997); see New York State Assn. of Life Underwriters v New York State Banking Dept., 83 N.Y.2d 353, 359-360 (1994).

Here, contrary to Petitioners' argument, DHCR did not act irrationally or in violation of lawful procedure in interpreting its regulations to exclude from voting 44 apartments that had no eligible tenant of record. DHCR's determination to exclude those apartments from the privatization vote was consistent with the law, its regulations, the offering plan, SBT's certificate of incorporation and by-laws, and SBT and DHCR's treatment of those apartments during previous votes. Nor did it fail to properly verify the election results.

a. Deceased Shareholders and the Estates of Deceased Shareholders

DHCR's regulations for the Mitchell-Lama program provide that the shares allocated to an apartment must be surrendered upon the death of a cooperator. 9 NYCRR 1727-8.3 [a] ("the lease and the shares of stock for such decedent's apartment shall be surrendered by the decedent's estate or survivors for redemption"). An estate cannot claim voting rights to a decedent's apartment simply by refusing or delaying the return of the shares to the housing company. In addition, a decedent's estate is not a tenant in occupancy that automatically has succession rights or the right to vote in the dissolution decision. See Rubinstein v 160 W. End Owners Corp., 74 N.Y.2d 443, 446 (1989); De Kovessey v Coronet Props. Co., 69 N.Y.2d 448, 457-458 (1987)(estates "did not legally . . . accede to [the] status of their decedents"); see also Chatham Towers v Estate of Tom, 159 Misc. 2d 890, 892 (Sup. Ct. N.Y. County 1993)(regulatory agreement with New York places restrictions on transferability of shares through testamentary disposition, because customary rights of cooperative ownership are restricted in government subsidized housing developments). Moreover, in a December 16, 2014, letter, DHCR explained that its "rules do not contemplate possession of Mitchell-Lama apartments by estates at any time." Accordingly, the

decision not to include the five apartments where the tenant of record had died prior to the vote, and only an estate remained, had a rational basis and was supported by law.

b. Capital Grant Tenants are not Shareholders

Four of the non-voting apartments were owned by the New York State Housing Finance Agency (State HFA) and were subleased to low-income tenants under the State's Capital Grants program. PHFL § 44-a. The State HFA is barred by statute from voting the shares of these apartments. Id. § 44 [20] ("Shares owned by the agency may not be voted"). Moreover, tenants who sublease their apartments from State HFA under the Capital Grants program are barred by statute from owning shares in the cooperative. Id. § 44-a [1]. Accordingly, because neither the State HFA nor the residents in the Capital Grant apartments are shareholders, DHCR's decision to disqualify these apartments was rationally based.

c. Building Employees are not Shareholders

Two of the non-voting apartments are occupied by the building superintendent and the assistant superintendent. These employees are not shareholders. They are allowed to live in these apartments simply because they are employees of the cooperative. As non-shareholders, the employees do not have the right to vote on privatization, in board elections, or in any other cooperative matter. Accordingly, DHCR's disqualification of these apartments was rational.

d. Temporary Transfers

On the date of the vote, five tenants were listed as shareholder of record for two apartments in SBT because the tenants were in the process of moving from one apartment to another within the cooperative. Each of these tenants was permitted to vote only once because each tenant could occupy only one apartment as his/her primary residence. See, e.g. 9 NYCRR 1727-5.3[a] [12]. Moreover, pursuant to SBT's certificate of incorporation and by-laws, each shareholder is allotted one vote regardless of the number of shares held by such shareholder. Thus, DHCR's regulations and SBT's certificate of incorporation and by-laws provide a rational basis for disqualifying five apartments as temporary transfers.

e. Vacant but Assigned

Eight apartments were vacant at the time of the vote. Although SBT had chosen applicants from the waiting list to purchase and occupy these apartments, the closings had not occurred. Accordingly, because there were no tenants in possession of these apartments as their primary residence, there were no shareholders entitled to cast a ballot for these eight units. Moreover, DHCR has consistently taken the position that shareholders who have permanently vacated are ineligible to vote after they leave the apartment because those apartments are no longer their primary residences. 9 NYCRR § 1727-5.3 [a] [12](failure to maintain apartment as primary residence is a ground to terminate tenancy).

Although Petitioners argue that, pursuant to the Business Corporation Law (BCL) § 612, every shareholder of record is entitled to one vote, that argument is unavailing because SBT was incorporated under the PHFL, not the BCL, and PHFL § 17 (1) expressly provides that the powers of a private housing company pursuant to the BCL are "[s]ubject to the limitations of this article." Thus, the general principles of the BCL, are subject to the specific mandates of the PHFL and its implementing regulations. Moreover, Petitioners' reliance on DHCR's statement that, generally, one vote may be cast for each apartment by the shareholder of record does not demand a different result. In subsequent correspondence, DHCR refined that statement and detailed which categories of apartments could be excluded from voting because there was no shareholder, in good standing, entitled to vote for those apartments. Accordingly, DHCR's disqualification of the "vacant but assigned" apartments had a rational basis because there was no shareholder, in good standing, who was entitled to vote for those apartments.

f. Succession Cases

DHCR does not deny that each of the 20 apartments that was disqualified based on unresolved succession claims had nominal shareholders, but it does contend that those nominal shareholders were not entitled to vote because they had either died or permanently vacated the apartments. DHCR avers it has first-hand knowledge regarding 16 of those apartments because it was processing the succession applications and it received documentary evidence from SBT as to the nominal shareholder's status regarding the other 4. As discussed above, DHCR's position that shareholders who have permanently vacated their apartments are not "in good standing" and are

not entitled to vote has a rational basis based on DHCR's interpretation of its own regulations and the case law and regulations.

g. Election Results

Moreover, as to Petitioners' argument that DHCR acted arbitrarily in accepting the election results, the record reveals that DHCR had "satisfactory evidence" that two-thirds of the shareholders voted to authorize dissolution. 9 NYCRR § 1750.7. With respect to SBT's privatization vote, DHCR had a limited role. Pursuant to regulation, DHCR need only certify the results of the vote when presented with 'satisfactory evidence' that two-thirds of the shareholders of record have approved the privatization measure. 9 NYCRR § 1750.7.

Here, DHCR was in possession of sufficient evidence to satisfy this standard. By letter dated October 2, 2014, SBT notified DHCR that the dissolution resolution had been passed by the cooperative. Attached to the letter was the certification by HBA, which stated that: the vote was conducted fairly and honestly; shareholders who voted in person were required to provide identification; the proxies were checked to verify the authenticity of the signatures; 1,458 valid votes were received; 1,082 shareholders voted in favor of the plan; 373 shareholders opposed the plan; and the privatization plan was approved. Upon receiving SBT's letter, DHCR did not simply accept HBA's certification. Rather, DHCR contacted HBA and requested a "detailed narrative concerning the process . . . used in connection with the Southbridge dissolution vote to (1) verify the proxies, and (2) determine the vote count."

In response, HBA stated that it followed the procedures set forth in the offering plan, which were used in prior elections and which had been subject to DHCR's review and approval. HBA stated that the vote count was determined by a list provided by SBT's general manager, and that the signatures on the proxies were verified by comparing them to income affidavits or occupancy agreements the shareholders had signed and, in addition, at its office, HBA verified the proxies it received through the use of a barcode scanner. HBA also stated that SBT management had no involvement with the lockboxes which were used to collect the proxies. Moreover, HBA stated, "the importance of this election and the likelihood that our efforts would be questioned was known well in advance and every effort was made to ensure both the integrity and transparency of the election. The election was held in strict compliance with the procedures you mandated . . . ."

In a November 24, 2014, letter, DHCR apprised Petitioners of the information contained in HBA's letters and it added that, with respect to the vote count, SBT's manager provided HBA with a sign in sheet and the vote count was based on that list. DHCR also informed Petitioners that HBA provided a tally for each of the two voting machines for each day of the vote and that the numbers it reported were consistent with the result reported in HBA's October 1, 2014, resolution. Accordingly, it cannot be said that DHCR acted irrationally in certifying that two-thirds of the shareholders had approved the privatization measure.

CONCLUSION

Therefore, it is

ADJUDGED that the petition is denied and the proceeding is dismissed.

Dated: August 11, 2015

ENTER:

Joan Lobis, J.S.C.

UNFILED JUDGMENT

This judgment has not been entered by the County Clerk and notice of entry cannot be served based hereon. To obtain entry, counsel or authorized representative must appear in person at the Judgment Clerk's Desk (Room 141B).