

Can a Co-op Director be Held Personally Liable for Discrimination?

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The Appellate Division, First Department decision in the case of Alphonse Fletcher, Jr. et al. v. The Dakota, Inc., et al. continues to be the subject of much discussion in the legal community. This case represents a wakeup call for every director of a cooperative corporation or condominium association alerting them once again that they cannot hide behind the "Business Judgment" rule when issues of discrimination are involved. The Appellate Court reversed a prior decision of the same court finding that a director's participation in a corporation's tortious behavior is sufficient to give rise to individual liability for the director.

The Iconic Dakota House

Arguably, the Dakota is the highest profile cooperative apartment building in the world. It is located at the corner of 72nd Street and Central Park West on the Upper West Side of Manhattan and was completed in 1884. The building is often credited as the one structure that prompted construction of numerous luxury apartment buildings throughout Manhattan. Following the murder of John Lennon at the entrance of the building on December 8, 1980, the co-op Board of Directors has reversed the history of celebrity occupants by refusing Billy Joel, Carly Simon, politicians and other high profile individuals. Through it's almost 130 years it has been home to numerous celebrities including Lauren Bacall, Leonard Bernstein, Rosemarie Clooney, José Ferrer, Roberta Flack, Judy Garland, Boris Karloff, Joe Namath, Gilda Radner, Jerry Seinfeld and of course Yoko Ono who reportedly still owns several apartments in the building. According to internet research, apartments in the Dakota range in price from \$4,000,000.00 to \$30,000,000.00. At the time this article was written, there were two apartments for sale in The Dakota, a three bedroom for \$6,800,000.00 and a four bedroom at \$14,500,000.00.

Fletcher v. The Dakota, Inc., et al 99 A.D.3d 43, 948 N.Y.S.2d 263 (July 3, 2012)

In this case brought by Alphonse Fletcher, Jr., an African American, it was alleged that after Mr. Fletcher had been the president of the Cooperative Board and objected to discriminatory behavior during his presidency involving Jewish applicants for ownership in the coop, the subsequent Board of Directors retaliated by rejecting his application to purchase an apartment which adjoined the one he already occupied. He wanted to combine them into one large apartment. He alleged as well that one of the Board members actively communicated to other apartment owners that Mr. Fletcher was being rejected because of financial concerns when in fact, Mr. Fletcher believed that he had sufficient financial resources for the approval of his purchase. He sought to impose personal liability against two of those directors, defendants Barnes and Nitze, for what he alleged was direct and overt discriminatory behavior.

The Court Reverses Itself

In 2006 the same Appellate Court made a determination in *Pelton v. 77 Park Ave. Condominium*, 38 A.D.3d 1, 825 N.Y.S.2d 28 [2006]. In that decision, the Court had stated:

“In bringing an action against the individual members of a cooperative or condominium board based on allegations of discrimination or similar wrongdoing, plaintiffs were required to plead with specificity independent tortious acts by each individual defendant in order to overcome the public policy that supports the business judgment rule...”

Accordingly, in the Fletcher case the defendants stated that their only conduct was the disapproval of Fletcher’s application for ownership of the second apartment which was based upon the “business judgment rule”. The defendants asserted that Fletcher could not show they had committed tortious acts individually which were outside the context of their vote as members of the Board of Directors.

The Court in the Fletcher case immediately addressed this issue and stated that its prior decision in the Pelton case was inappropriate and therefore,

“[We] therefore decline to follow and expressly overrule, the pleading rule articulated in Pelton.”

The Business Judgment Rule

In arriving at its decision to not require specific pleadings about tortious behavior of the defendants, the Court affirmed that the directors of a cooperative corporation can be held personally liable for discriminatory decisions made in the context of their actions as a Board member.

The business judgment rule as set forth in the *Matter of Levandusky v. One Fifth Ave. Apt. Corp.*, 75 N.Y.2d 530, 554 N.Y.S.2d 807, 553 N.E.2d 1317 [1990] is the decision of the New York State Court of Appeals (our highest court), affirming that “the “business judgment” rule is the correct standard of judicial review for the actions of the directors of a cooperative corporation. That rule prohibits judicial inquiry into the actions of corporate directors ‘taken in good faith and in the exercise of honest judgment in the lawful and legitimate furtherance of corporate purposes.’” The Court in the Fletcher case reiterated statements made by the Court of Appeals in the Levandusky case that “the broad powers of a cooperative board hold potential for abuse through arbitrary and malicious decision making, favoritism, discrimination and the like.” The Levandusky Court affirmed that “those types of abuses are incompatible with good faith and the exercise of honest judgment.”

Discriminatory Behavior is Not Protected by the Business Judgment Rule

The Court in the Fletcher decision then goes on to state emphatically:

“[A]rbitrary or malicious decision making or decision making tainted by discriminatory considerations is not protected by the business judgment rule.”

The Court therefore indicated that there is no “safe harbor” from inquiry into the behavior or actions of a director that is protected by the business judgment rule. The Court reviewed extensive precedents on this subject and affirmed once again that:

“[T]he officers, directors and agents of a corporation are jointly and severally liable for torts committed on behalf of a corporation and the fact that they also acted on behalf of the corporation does not relieve them from personal liability.”

Allegations of Retaliation

Fletcher asserted in his complaint that when he was elected president of the coop in May of 2007 he complained to the defendant Nitze about another board member’s inappropriate comments about new applicants for ownership who were referred to as “Jewish mafia”. When Fletcher supported the application of the Jewish couple for an apartment in the building, Nitze allegedly tried to persuade Fletcher from advocating for the couple. Ultimately, Fletcher prevailed and the board granted the couple an interview after which it approved their application.

The Court noted that these allegations were sufficient to form a basis for retaliation in 2010 when Fletcher sought to purchase an adjoining apartment to create one larger apartment. His complaint, based on the State’s and City’s Human Rights Laws asserted that the Dakota’s Board of Directors retaliated against him and then engaged in conduct intended to embarrass and defame him. After rejecting Fletcher’s application to purchase the apartment the Board of Directors took it upon itself to send a letter to certain Dakota shareholders. It was alleged in Fletcher’s pleadings to have stated: “[b]ased on the financial information submitted by Fletcher, the Board concluded that approving such a purchase would not be in the best interest of The Dakota’...[The letter] also contained the false and misleading statement that Fletcher had declined the Board’s request to provide additional financial information.”

In finding that Fletcher’s action against the Board should continue, the Court affirmed that the complaints made under the Human Rights Law require that the Court construe the laws broadly in favor of “discrimination plaintiffs, to the extent that such a construction is reasonably possible.”

Aren’t Board Members Insured?

Almost all cooperative corporations maintain errors and omissions insurance coverages which insure the volunteer board members against personal liability. In the area of discrimination however, an individual board member can be held accountable to pay compensatory and punitive damages. Such payments are required to be paid personally by the board member and are not reimbursable from the cooperative corporation's funds or under any insurance policy. Discrimination constitutes an illegal act and almost every errors and omissions insurance policy excludes coverage for illegal acts.

Our Association's Efforts

The Hudson Gateway Association of Realtors, Inc. has advocated for many years in favor of proposed legislation that would require a Board of Directors of a cooperative corporation to communicate to prospective owners the reasons for their rejection. This legislation has been actively opposed by the very powerful lobby for cooperative corporation owners who assert that board members would be living in fear of lawsuits and that cooperative boards would be defending decisions previously made in the best interest of the cooperative corporation based upon the business judgment rule. Unfortunately, the business judgment rule is too easily used to hide discriminatory behavior. In the absence of a board member's willingness to accuse other board members of improper conduct, it is virtually impossible to identify when and how discriminatory conduct occurs. Those board members who have chosen to confront discriminatory behavior by other board members often find themselves ostracized and rejected. Our Association will continue to support transparency.

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