Legal Duties and Responsibilities of Co-op Board Members

Could You Be Sued as a Co-op Board Member?

Berendson Academy

By Richard Berendson

BOARD AUTHORITY

Cooperative directors often underestimate their legal responsibilities toward the co-op and its members. While many view the cooperative as a social setting for friends, it operates as a corporate entity managed by the Board of Directors and staffed by employees and members.

When a cooperative files for incorporation, it becomes a legal entity governed by the rules and regulations applicable to corporations. State or provincial laws require that corporations designate individuals to act on their behalf, forming a Board of Directors. According to the Model Business Corporation Act (MBCA), the affairs of a corporation must be managed under the direction of a board. Thus, directors' responsibilities lie not in managing daily operations but in supervising and directing the management of the cooperative. The Board is recognized as the ultimate decision-making authority within the cooperative's governance structure.

The authority of a Board of Directors is derived from statutes, bylaws, and the cooperative's membership. Board authority is granted through the Articles of Incorporation, which dictate the limits within which the cooperative may function. It is crucial for boards to ensure that their cooperative's Articles of Incorporation provide a balanced scope of authority—sufficiently broadly to allow the Board to fulfill its purposes while being narrow enough to protect member interests. These Articles establish boundaries for the Board's authority, and the Board is responsible for operating within those parameters.

While the Articles of Incorporation outline Board authority, the Bylaws define the specific powers and responsibilities of the Board. Directors and officers can only exercise the authority necessary to fulfill their duties as outlined in the bylaws. Authority is typically exercised during duly convened Board meetings, where decisions are made based on attendance, voting, and quorum requirements specified in the bylaws.

There are generally three important limitations on the Board's authority that require action from the cooperative's membership:

1. The election of Board members.
2. The removal of Board members.
3. Amendments to the bylaws, policies, and other governing documents of the cooperative.

Despite some ambiguity in the judicial definitions of a co-op's Board responsibilities and authority, there has been a trend in court rulings to uphold the contractual relationships between the cooperative and its members. Courts recognize certain aspects of the Board's authority, such as the power to accept or reject membership applications and to delegate this authority. The Board's authority is considered "complete and without limit" as long as it is exercised without discrimination based on race, religion, ethnic origin, gender, sexual preference, or ability. When establishing membership qualifications, Boards should ensure that standards are reasonable and directly related to the well-being of the cooperative.

Moreover, the Board has the authority to create and enforce rules that promote effective operations. In developing these rules, the Board acts in what it believes to be in the best interests of the community, and members consent to adhere to these rules through their occupancy agreements.

When creating rules, the Board should ensure that:

1. The objective serves overall community welfare rather than the personal interests of a few members.
2. The rule's objective and implementation methods are clear and interconnected.
3. The rule is applied uniformly to all members, avoiding discrimination against any individual or group.

BOARD RESPONSIBILITIES

The fundamental responsibility of a director is to act in the best interests of the cooperative and its members. According to the MBCA, "[a] director shall perform his duties as a director, including his duties as a member of any committee of the Board upon which he may serve, in good faith, in a manner he reasonably believes to be in the best interests of the corporation, and with such care as an ordinarily prudent person in a like position would use under similar circumstances."

This duty embodies the fiduciary responsibility of directors, who are expected to act in good faith and prioritize the welfare of the cooperative while safeguarding the interests and assets of its members.

Generally accepted legal responsibilities of directors include:

1. Directors cannot abdicate their responsibility directly.
2. They must manage business operations in alignment with the Articles of Incorporation and Bylaws.
3. Directors are tasked with appointing officers and delegating authority for executing the cooperative's functions.
4. They must be knowledgeable about corporate affairs to fulfill their roles effectively.
5. Directors must act in good faith and exercise reasonable care in managing the cooperative's affairs.
6. They have a legal obligation to represent the cooperative as trustees for its members.
7. Regular attendance at Board meetings is essential; absence does not absolve a director from responsibility for the Board's decisions.
8. Directors may be held financially liable for losses incurred by the cooperative under specific circumstances, particularly in cases of gross negligence.

By understanding their authority and responsibilities, cooperative directors can effectively uphold the well-being and growth of the cooperative while safeguarding the interests of its members.

Duties of Directors

The law recognizes several categories of duties for corporate directors.

Duty of Care

The Duty of Care establishes the level of competence expected from board members, defined as the care an ordinarily prudent person would exercise in similar circumstances. Consequently, board members are expected to make decisions on behalf of the organization with the same level of diligence they would apply in their personal and professional lives.

Under common law, directors are required to exercise a standard of care and skill commensurate with their knowledge and experience. Central to this duty is the principle of good faith, which courts consider when determining whether a director is liable for a decision or merely made an error in judgment. Courts typically assess whether the director acted in the best interests of the cooperative, recognizing that board members do not need to oversee every detail of the organization’s affairs, as responsibilities can be delegated to qualified individuals.

From judicial interpretations of the Duty of Care, board members should adhere to the following guidelines:

1. Thoroughly understand the organization.
2. Research issues meticulously and gather relevant facts.
3. Dedicate the necessary time to prepare for and attend all meetings.
4. Maintain the integrity of the office by keeping an open mind and setting aside personal egos.
5. Insist on receiving complete and timely information.
6. Allow sufficient time for thoughtful deliberation.
7. Keep meticulous records of board actions.
8. Approach their responsibilities with honesty and personal integrity.

Examples of Breach of Duty of Care

Breach of the Duty of Care can manifest in several ways, such as:

- Excessive absenteeism from board meetings.
- Neglecting to inquire about proposed actions or decisions.

A board member can only perform effectively if they are present at meetings, actively engaging with the information necessary to make informed decisions.

Legal Framework

The Duty of Care for directors is outlined in Section 8.30(a) of the Model Act. According to this legislation, a director must act in good faith and in the best interests of the cooperative, exercising the prudence expected of a reasonable person in similar circumstances. This standard allows directors to take reasonable risks, accepting that the outcomes of their decisions may not always be favorable in hindsight. What is crucial is that decisions are made honestly and thoughtfully.

While hindsight offers valuable lessons, it is important to note that directors are protected from criticisms of their past decisions through the legal doctrine known as the Business Judgment Rule. This rule affirms that directors should not be held liable for decisions that, while potentially flawed in retrospect, were made in good faith and with due diligence at the time.

DUTY OF LOYALTY

The Duty of Loyalty requires board members to prioritize the interests of the cooperative above their own personal or professional interests. This commitment to the organization means that directors must act honestly and reasonably believe that their actions serve the best interests of the co-op and its members.

Directors must remain vigilant about potential conflicts of interest. A conflict may arise when an agreement between a director and the cooperative offers preferential terms or conditions. Such conflicts can expose directors to liability. In these instances, directors are expected to prioritize the cooperative's interests and fully disclose any divided loyalties, including the nature of the relationship that may provide a financial or business benefit. While the board may choose to approve a conflict, it is advisable for the director to recuse themselves from discussions and decision-making related to that conflict.

When a director becomes aware of a business opportunity due to their position, they must defer to the cooperative as the first priority. A director may only pursue personal advantage from such opportunities after the cooperative has evaluated and decided not to act on them. Furthermore, directors have a responsibility to maintain confidentiality regarding the cooperative's affairs until such information is made public or regarded as part of the public record. This aspect can be challenging, as it involves balancing the need to keep members informed while maintaining a competitive edge for the cooperative.

Examples of Breach of Duty of Loyalty

Common breaches of the Duty of Loyalty typically involve failing to disclose or address conflicts of interest. Specific examples of problematic behavior include:

- Hiring a company owned by a board member without a bidding process or proper disclosure. For instance, if the board chooses an HVAC company owned by a board member, and that member receives compensation from the cooperative for the work.
- Renting event space from a board member's family without appropriate disclosure or discussion among the board.

These actions might be permissible if the conflict is disclosed beforehand, a board discussion takes place, and a fair bidding process is followed. However, it is crucial to acknowledge that legality does not always align with public perception and ethical standards.

Actions that are unlikely to be acceptable include:

- Engaging in any conflict without a transparent process, discussion, or vote.
- Allowing family members of board members to occupy organization-owned spaces rent-free while other members are charged fair market rates.

Legal Framework
Directors of a cooperative hold a position of trust and must not exploit this relationship for personal gain. This includes being cautious about two primary concerns: self-dealing and engaging with individuals or entities that would ordinarily transact with the cooperative.

The legal stance on self-dealing has evolved over time. Previously, contracts between a director and the cooperative were voidable. Currently, a director can enter into a contract with the cooperative, provided that full disclosure of alternatives is made and if the contract is deemed fair and reasonable. In such cases, the director involved should abstain from participating in discussions or voting regarding the contract.

Fairness is typically assessed by comparing the terms with those that would be negotiated at arm's length by disinterested parties. Agreements that fall within a reasonable range are generally considered valid.

Since directors are also members and patrons of the cooperative, some transactions with the cooperative are inevitable. However, it is essential to ensure that directors are treated equally with other members, avoiding any special discounts or preferential treatment.

The principle of "corporate opportunity" dictates that directors should refrain from capitalizing on business opportunities that would typically have been available to the cooperative unless the cooperative has thoroughly evaluated and declined to pursue those opportunities. Directors interested in such opportunities should not engage in discussions or votes related to them.

Finally, part of the Duty of Loyalty encompasses maintaining the confidentiality of the cooperative's affairs until such information is properly disclosed to the members or made public.

Duty of Attention

The Duty of Attention encompasses the responsibility of directors to actively participate in cooperative affairs and remain informed about their operations. This includes understanding what the organization should and should not be doing. Directors can be held liable for personal negligence in fulfilling their duties, which includes providing reasonable oversight of officers and employees, reviewing documentation, and attending meetings. Ignorance stemming from "gross inattention" does not exempt directors from liability. For example, a director cannot defend their failure to participate (such as being absent from meetings or abstaining from votes) or to stay informed (like not reading board packets or not asking questions).

While directors are expected to rely on information prepared or presented by others—such as staff or external experts—they must have a reasonable belief in the reliability and competence of those sources.

Active Participation and Responsibilities

Directors are required to engage actively in the cooperative's activities, which include:

- Attending meetings regularly.
- Reviewing information and data provided by employees and experts.
- Monitoring the actions of employees and committee projects.

Directors are entitled to rely on reports, opinions, or statements, including financial data—derived from officers, employees, or committees, if they have reasonable grounds to believe in the credibility of the information source. This also extends to professionals such as attorneys, consultants, and accountants engaged by the cooperative to inform or guide decision-making. For a director to legitimately rely on such reports, they must either read the information or be present during presentations of the data.

Reasonableness of Reliance
When determining the reasonableness of reliance on a report, the standards of good faith, ordinary care, and acting in the best interests of the cooperative are applied. Close monitoring of employees and committee activities is crucial. Directors must exercise prudence in delegating tasks to individuals, ensuring that any assigned responsibilities are being performed adequately.

It is vital for the board to oversee that officers, employees, or committees fulfill their delegated tasks effectively. The board's diligence not only helps in safeguarding the cooperative's interests but also reinforces the accountability and performance of its leadership team. By actively participating and remaining informed, directors can better fulfill their Duty of Attention, thereby contributing positively to the cooperative's governance and success.

DUTY OF OBEDIENCE

The Duty of Obedience mandates that board members comply with applicable federal, state, and local laws, adhere to the organization's bylaws and policies, and uphold the mission of the cooperative. This duty also extends to honoring donor intent and ensuring that contributions are used for their intended purposes. It's important to note that some states may have additional requirements or different terminologies regarding these obligations, so consulting the specific laws of your state is advisable.

Examples of Breach of Duty of Obedience
Several real-life scenarios illustrate potential breaches of the Duty of Obedience:

- Allowing one exit to remain blocked at a homeless shelter, despite regulations requiring multiple egress points for safety.
- Accepting a donation earmarked for a specific project but subsequently reallocating those funds for a different purpose.
- Failing to follow established financial policies that mandate the separation of duties when handling money.

Importance of Obedience
The duties of care, loyalty, and obedience are fundamental responsibilities of a board of directors and are crucial for effective oversight of the organization. Upholding the Duty of Obedience not only ensures compliance with legal and ethical standards but also reinforces the integrity and trustworthiness of the cooperative, safeguarding its mission and the interests of its stakeholders.

Reducing Director Liability

Incorporating a cooperative protects directors from direct liability for the cooperative's actions, as the co-op becomes a separate legal entity responsible for its own actions. However, board members can still face liability for mismanagement when their decisions lead to illegal activities, criminal actions, or significant damages.

The Cooperative Corporations Act outlines specific examples of such liabilities, including:

- Board-approved actions leading to environmental harm.
- Noncompliance with legal requirements regarding member share capital and dividends.
- Unequal financial assistance to certain members or staff, causing financial losses to the cooperative.
- Hiring staff with the knowledge that the cooperative cannot afford their salaries.

Preventative Measures for Liability Protection

To protect themselves from liability, the Board of Directors and individual directors can implement several preventative measures:

Documentation: Thorough and accurate documentation of all major Board actions is essential. This includes detailed meeting minutes and comprehensive meeting packets. Minutes should reflect alternative options considered and document the rationale behind decisions to clarify the logic of those choices. Individual directors can safeguard themselves by recording their dissent in the minutes, thus avoiding liability for decisions they oppose.

Clear Communication: Committee assignments should be clearly defined, and reporting forms can facilitate more in-depth discussions during Board meetings. Proposals must be well-written and accompanied by sufficient supporting information to assist in informed decision-making.

Enhanced Involvement: Greater engagement between directors and management in the cooperative's planning processes can improve both understanding and collaboration, ultimately benefiting the cooperative’s strategies.

Legal Counsel: Larger cooperatives with complex operations should consider retaining a "counsel to the Board." In-house counsel may be preoccupied with routine managerial tasks, and having dedicated legal expertise can help navigate more complex legal issues.

Member Ratification: For intricate or less conventional decisions (such as policy matters), the Board can seek ratification from stockholder-members to mitigate potential liability. This additional layer of approval demonstrates diligence in the decision-making process.

Indemnification: The cooperative can offer indemnification, providing protection to directors against potential lawsuits or damages for actions taken in their capacity as Board members. This protection can be established through language in the cooperative's bylaws. Additionally, directors may obtain directors' and officers' liability insurance (commonly referred to as D&O insurance), ensuring financial backing for indemnification policies.

Consistency and Enforcement

Directors must recognize the significance of their roles in managing a multimillion-dollar cooperative. Consistent enforcement of bylaws and policies is crucial; any perceived inconsistencies can lead to legal challenges. Directors have a responsibility to treat all members equitably, reinforcing the cooperative's integrity while protecting themselves from potential liability. By proactively implementing these measures and diligently performing their governance duties, directors can significantly reduce their risk of liability while effectively overseeing the cooperative's operations.

Business Judgment Rule

The Business Judgment Rule is a legal doctrine that provides a level of protection for directors when making decisions on behalf of a corporation. Broadly speaking, the rule states that if directors act on an informed basis and in good faith while making a decision, that decision will generally be upheld, even if it leads to negative consequences. Historically, this rule granted substantial deference to directors, shielding nearly all of their decisions from legal scrutiny, as long as there is no evidence of bad faith, fraud, or self-dealing.

Evolving Standards

In recent years, courts have begun scrutinizing the decision-making processes of directors more closely. Judges are increasingly examining whether directors acted reasonably in their deliberations and decisions. This trend is particularly evident in Delaware, a state known for its favorable corporate laws where many companies are incorporated.

Three landmark decisions from Delaware have drawn significant attention regarding this evolving interpretation of the Business Judgment Rule. The outcomes of these cases influence corporate governance practices widely, given that many corporations look to Delaware's legal framework for guidance. These decisions suggest a movement toward a more rigorous examination of directors’ actions and decisions, signaling to boards the importance of serious and thorough decision-making processes.

As a result, while the Business Judgment Rule continues to provide protection for directors, it is increasingly recognized that they must document their decision-making processes and demonstrate that they acted with due diligence and good faith. This evolution in judicial scrutiny emphasizes the importance of transparency and accountability within corporate governance.

Legal Duties

In summary, a notable trend has developed where courts are more closely examining the decision-making processes of corporate directors to determine whether they acted reasonably. Traditionally, the Business Judgment Rule provided broad protection, allowing directors to make decisions with a significant degree of discretion as long as they acted in good faith and were well-informed. However, the current legal environment places greater importance on the rationale and thoroughness behind those decisions.

This shift is particularly pronounced in Delaware, a state with a favorable business environment where many companies choose to incorporate. Three pivotal court decisions in Delaware are crucial because their implications can affect corporate governance at large. As judges increasingly scrutinize directors’ decision-making processes, they are looking for evidence of adequate deliberations, information-gathering, and genuine consideration of the corporation's and its stakeholders' interests.

INSURANCE AND INDEMNIFICATION

Due to the increasing risk of lawsuits, which can be costly even for directors who prevail, many individuals are hesitant to accept positions on board. Cooperatives can alleviate these concerns and encourage participation through two primary mechanisms: indemnification and insurance. Additionally, certain states, such as Minnesota, allow cooperatives to limit the liability of their board members in their Articles of Incorporation.

Indemnification

Indemnification refers to the reimbursement of a director for expenses incurred as a result of serving as a director or officer of the cooperative. This can include attorney fees, costs related to legal actions, and reimbursements made to the cooperative, shareholders, or other parties. Some state statutes governing cooperatives permit reimbursement under specific circumstances. If indemnification is not explicitly mentioned in a state cooperative statute, it may still be possible to apply provisions from general business incorporation statutes. It is vital for the cooperative's bylaws to include a clear provision for indemnification under appropriate circumstances.

Determining the appropriateness of indemnification can be complex. Generally, indemnification requires that the director acted in good faith, believed their conduct was in the best interests of the cooperative, and did not engage in unlawful actions, particularly in criminal proceedings.

In many instances, definitive judgments regarding a director's culpability can be challenging to establish. Often, claims result in settlements, leaving questions of the director's good faith or intent unanswered. In such situations, indemnification may still be permitted.

The process of deciding whether to indemnify a director—and determining the amount or recipients of any payments—can involve various parties, including the remaining board members, a board committee, an independent legal advisor, shareholders, or even a court.

While indemnification is typically advantageous, it can be susceptible to misuse. Reimbursing a careless director could inadvertently encourage negligence; thus, bylaws concerning indemnification should be drafted meticulously to ensure appropriate safeguards are in place.

Insurance

Cooperatives can also obtain insurance coverage to protect against potential indemnification payments owed to directors. However, the provision of such insurance can be contentious. If the coverage is too broad, it may lead directors to act with less diligence in fulfilling their responsibilities.

Therefore, it is crucial for cooperatives to evaluate which types of behaviors they wish to insure against and to consider the various terms of available policies carefully.

Limiting Liability

The cooperative incorporation statute allows cooperatives to eliminate or limit the liability of their board members in their Articles of Incorporation.

However, there are critical exceptions where liability cannot be limited or eliminated, including cases of:

1. Breach of duty of loyalty.
2. Acts or omissions not made in good faith or involving intentional misconduct or knowing legal violations.
3. Transactions where the director derived improper personal benefits.

Cooperatives incorporated in states with similar provisions should contemplate amending their governing documents to include limits on liability where permissible. By implementing indemnification and insurance policies, cooperatives can lower the barriers to board service, ultimately encouraging a diverse range of individuals to contribute their expertise and perspectives to the organization.

Conclusion

Members of the cooperative who serve as directors play a crucial role in overseeing the management and operations of the cooperative. It is essential for directors to remain informed and make prudent decisions in their governance. When directors act in good faith, exercise care and diligence, and avoid conflicts of interest or preferential treatment, they can fulfill their legal obligations without encountering significant difficulties.

Moreover, the unique nature of cooperative businesses necessitates that director be attuned to the needs of the members. Ensuring that members are well-informed empowers them to actively exercise their rights and participate meaningfully in the cooperative's governance.

By adhering to the legal duties and responsibilities required of them, directors can proactively mitigate potential problems. Additionally, utilizing mechanisms such as indemnification, obtaining insurance, or implementing provisions in the Articles of Incorporation to limit liability (where permissible) can offer directors further protection against financial burdens.

Serving as a director is a position of responsibility, but it does not have to be overwhelming. By carefully observing the legal requirements and best practices associated with their roles, directors can contribute positively to the cooperative while effectively managing the associated risks.

Every Board's MUST-HAVE DOCUMENTS

Even the most organized, responsible, and amiable board needs to document its activities, internal rules, and processes. Some of the documentation is legally required while some is simply helpful to have. Some documents should be available to the public while others must be kept confidential. Some serve as guidelines for decision making while others are part of the record keeping. For a board that takes its fiduciary role seriously, written rules simply are part of necessary risk management.

Here are the various documents to which your board needs to pay attention.

DOCUMENTS THAT SERVE AS GUIDES FOR BOARD ACTION:

ARTICLES OF INCORPORATION

- Legal document that outlines the general purpose and structure of the organization and its intent to operate exclusively with a nonprofit purpose.
- Filed with the state when the nonprofit is incorporated; need to be refiled if any key issues change.
- Usually follow a form and contain a minimum of detail because they are cumbersome to change.
- Must not contradict state nonprofit incorporation statutes.

BYLAWS

- Significant written rules that establish the governance structure of a nonprofit
- Define the duties, authority limits, and principal operating procedures for the board and board members
- Include the highest-level board policies
- Should not contain overly detailed procedures or restrictions as changes must be approved by the membership or full board
- Should be reviewed for fine-tuning every few years

Resource: [The Nonprofit Policy Sampler]

POLICIES

- Some apply to the organization, such as whistleblower and gift acceptance policies
- The chief executive is responsible for personnel policies and office procedures but the board should ensure that they exist and are adequate.
- Some supplement the bylaws and guide board practices and oversight procedures, such as investment, internal controls, and executive compensation policies
- Some direct staff operations, such as personnel policies.
- Operating guidelines for board and staff

BOARD PROCESSES

- Explain how to implement a policy, e.g., a separate document that explains step-by-step how to remove a board member or resolve a conflict.
- Serve as standard operating procedures.

JOB DESCRIPTIONS & CHARTERS

- Expectations for individual board members, officers, committees, task forces, and the chief executive

AGENDAS

- Guide the board's official business meetings

DOCUMENTS THAT RECORD BOARD DECISIONS & ACTIVITIES

- **Meeting minutes**
- **IRS Form 990** — All nonprofits must indicate whether the board has approved certain policies and followed specific processes when making governance decisions. The laws do not require any policies but no board should be comfortable reporting that it does not have conflict-of-interest, whistleblower, or document-destruction policies.

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Document Destruction

The Sarbanes-Oxley Act addresses the destruction of business records and documents and turns intentional document destruction into a process that must be carefully monitored.

Nonprofit organizations should have a written, mandatory document retention and periodic destruction policy. Policies such as this will eliminate accidental or innocent destruction. In addition, it is important for administrative personnel to know the length of time records should be retained to be in compliance.

This information is provided as guidance in determining your organization's document retention policy.[1]

Type of Document	Minimum Requirement
Accounts payable ledgers and schedules	7 years
Audit reports	Permanently
Bank Reconciliations	2 years
Bank statements	3 years
Checks (for important payments and purchases)	Permanently
Contracts, mortgages, notes and leases (expired)	7 years
Contracts (still in effect)	Permanently
Correspondence (general)	2 years
Correspondence (legal and important matters)	Permanently
Correspondence (with customers and vendors)	2 years
Deeds, mortgages, and bills of sale	Permanently
Depreciation Schedules	Permanently
Duplicate deposit slips	2 years
Employment applications	3 years
Expense Analyses/expense distribution schedules	7 years
Year End Financial Statements	Permanently
Insurance Policies (expired)	3 years
Insurance records, current accident reports, claims, policies, etc.	Permanently
Internal audit reports	3 years
Inventories of products, materials, and supplies	7 years
Invoices (to customers, from vendors)	7 years
Minute books, bylaws and charter	Permanently
Patents and related Papers	Permanently
Payroll records and summaries	7 years
Personnel files (terminated employees)	7 years
Retirement and pension records	Permanently
Tax returns and worksheets	Permanently
Timesheets	7 years
Trademark registrations and copyrights	Permanently
Withholding tax statements	7 years

[1] Be sure to seek legal and accounting counsel prior to adoption and implementation (RCH.)

NATIONAL HOUSING COOPERATIVES CASE LAW SURVEY (5/15/15-PRESENT)

August 30, 2016 · by Coop Law · in Uncategorized · Leave a comment

***City of Iowa City v. Iowa City Bd. of Review*, 863 N.W.2d 663 (Iowa 2015)**

Petitioner City of Iowa City's board of review reclassified 18 properties held by eleven multiple housing cooperatives from commercial to residential for property tax purposes. The Iowa Code permits the classification of residential property to include all land and buildings of multiple housing cooperatives organized thereunder. In 2012, the City Board of Review sent notices to 18 properties indicating that the Board changed the classification for these properties from commercial to residential for property tax purposes. The properties were then reclassified because they had been recently organized as multiple housing cooperatives. The parties agreed that two Iowa corporations organized each of the multiple housing cooperatives for the purpose of owning residential property in a cooperative.

Iowa City filed a notice of appeal with the district court, objecting to the Board's reclassification. The City argued that the Board's reclassification of the properties as residential was improper because two "natural persons," not two corporations, must organize multiple housing cooperatives under the Code. They also argued that the Code requires a one-apartment-unit-per-member ownership ratio for a multiple housing cooperative to be properly organized. The district court allowed the multiple housing cooperatives, Myrtle Grove Housing, Inc., to intervene in the action.

The Board argued that two corporations can organize a multiple housing cooperative because the Iowa Code defines a "corporation" as a person. The City countered that at least two of the organizers were required to be natural persons for the cooperative to be properly organized. Additionally, the City argued the organizers did not properly organize the cooperatives because each cooperative has more apartment units than members and the Iowa Code requires a one-to-one ratio. The intervenors argued that the Code specifically permits two corporations to come together to form a cooperative, not just natural persons, and that it does not limit membership to only one member per apartment unit.

The district court granted summary judgment in favor of the Board and the intervenors. The district court held that the Iowa Code defines persons to include corporations—therefore, the general assembly intended corporations to be able to act as organizers of a multiple housing cooperative. The district court further

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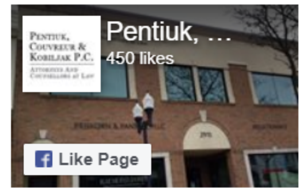

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concluded nothing in the relevant Code section was relevant to the determination of whether the cooperative was properly organized. The City appealed the board's decision to the district court. The district court affirmed the board's decision. Iowa City then appealed to the Iowa Supreme Court.

The first issue presented to the Supreme Court is whether the Board correctly classified the cooperatives as residential properties when two Iowa corporations organized them. The second issue is whether the Iowa Code requires a one-apartment-unit-per-member ownership ratio for a multiple housing cooperative to be properly organized.

The Court ruled that the proper test for determining if a property could be classified as residential pursuant to the Code is whether the multiple housing cooperative was properly organized, not the actual use of the property. Thus, its task was to determine whether the issues the City raised on appeal lead to the conclusion that the multiple housing cooperatives were not properly organized. The City claimed the Code section requires the organizers of a multiple housing cooperative to have at least two natural persons. The Board and the intervenors argued that two corporations can organize a multiple housing cooperative without natural persons.

_ The Court maintained that "We believe the legislative intent with the enactment of chapter 499A was to allow two corporations to organize a multiple housing cooperative. We also believe the intent of the general assembly at the time it enacted section 499A.1 was to put the same restrictions on corporate organizers as it did on persons who organized multiple housing cooperatives—the corporate organizers must have the authority to organize a multiple housing cooperative and a majority of the corporate organizers must be Iowa corporations." Thus, it found the City's arguments unconvincing as to the general assembly's intent.

It then reasoned that "The City makes no claim that the organizers of these multiple housing cooperatives were not duly organized Iowa corporations with the legal capacity to enter into a contract to organize a multiple housing cooperative." Consequently, it ruled that the district court was correct in finding as a matter of law that the Board was correct in holding two corporations can organize a multiple housing cooperative. The Supreme Court thus held that the Board and the district court were correct in finding that the organizers properly organized the 11 multiple housing cooperatives under Iowa law.

Finally, with regard to the City's argument that the organizers did not properly organize the cooperatives because the Iowa Code requires a one-to-one ratio, the Court said that such a position would require that it revive the "actual use" test—which it had specifically rejected in a previous case decision: "The organizational process necessarily takes place before the cooperative issues membership certificates and before the cooperative identifies all of its members…Looking beyond what is required to properly organize the cooperative to how the membership certificates are held meanders into the actual use of the property—how many apartments each member holds relates to the use of the property. This inquiry is not permitted under our decision in *Krupp.*"

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Accordingly, the Supreme Court held that the district court was correct in finding "as a matter of law the Board did not err in holding the Code does not require a one-apartment-unit-per-member ownership ratio for a multiple housing cooperative to be properly organized." Therefore, it affirmed the judgment of the district court, which upheld the decision of the Board in classifying the property held by the cooperatives as residential for purposes of property taxes.

Batista v. Cooperativa de Vivienda Jardines de San Ignacio, No. CIV. 10-1953 CVR, 2015 WL 5511748 (D.P.R. Sept. 17, 2015)

Plaintiff Priscilla Batista brought this suit alleging violations to the Fair Housing Act, among other state law tort and anti-trust claims. Cooperativa de Vivienda Jardines de San Ignacio is a housing cooperative that owns and administers a cooperative project where members like Plaintiff reside. Plaintiff also sued eight individual Defendants who comprised the Cooperativa's Board of Directors. Plaintiff's complaint was originally comprised of several causes of action, all of which were dismissed by the District Court on summary judgment. Before the Court was Defendants' Motion to Dismiss the Retaliation Claim that Plaintiff made.

Plaintiff argued that summary disposition is unwarranted, as her Complaint contained specific instances of retaliation, and because issues of fact remain as to the date the retaliatory conduct began. Plaintiff argued that the issue of the dates served to establish that the reasons given by Defendants for their actions were a mere pretext to retaliate against Plaintiff and evict her from her home.

Defendants argued that Plaintiff fails to state the actual retaliatory acts and their effects, and that she fails to sufficiently identify the protected activity which forms the basis for her retaliation claim. However, the Court did not agree. It recognized that "The FHA protects against discrimination "in the terms, conditions, or privileges of sale or rental of a dwelling ... because of race, color, religion, sex, familial status, or national origin," 42 U.S.C. § 3604(b), and renders it unlawful "to coerce, intimidate, threaten, or interfere with any person in the exercise or enjoyment of, or on account of his having exercised or enjoyed, or on account of his having aided or encouraged any other person in the exercise or enjoyment of, any right granted or protected by [§ 3604]."

In her Complaint, Plaintiff avers that, after she emerged victorious from her Department of Housing and Urban Development ("HUD") claim, "the retaliation by the San Ignacio Cooperative and its Board of Directors against Mrs. Batista was swift and immediately (sic). Defendants engaged in a definite pattern of discriminatory actions against Mrs. Batista in a concerted effort to evict her from the housing cooperative. This pattern of retaliatory and discriminatory conduct manifested itself in two-fold fashion: First, by initiating collection proceedings against Mrs. Batista for amounts she allegedly owed since 1998, when in fact Mrs.

Batista did not owe said amounts or had paid the same; and second, by demanding that Mrs. Batista move to a two bedroom apartment, denying her request for reasonable accommodations and ignoring her need to remain in her present three bedroom apartment due to her multiple health conditions."

In support of her allegations, Plaintiff proffered the following facts:

- Immediately after the administrative process with HUD culminated, on or about February 2009, Cooperativa requested that Plaintiff move to a two bedroom unit, or if she elected to remain in the three bedroom unit she occupied since 1983, to forego her Section 8 benefits and pay market rent thereafter.
- Plaintiff was summoned to a hearing wherein Cooperativa attempted to illegally collect $129.50 allegedly owed by her since 1998, charges which she disputes.
- Cooperativa held two hearings on March 25 and July 29, 2009, where Plaintiff was declared a non-member of the cooperative and was granted thirty days to abandon her apartment and ordered to pay the $132.50 she owed.
- Plaintiff was denied her rights and privileges during member's meetings, including her right to vote.
- On January 3, 2011, Cooperativa sent another notice to Plaintiff insisting she vacate her apartment and move to a smaller unit, and informing her that Cooperativa would not recognize her benefits under Section 8 and would charge her a monthly "market rent" of $359.00.
- On February 11, 2011, Cooperativa again summoned Plaintiff to a hearing in order to collect the alleged market rent unilaterally imposed on January 2011.

The Court ruled that Plaintiff should have the opportunity to carry her case forward to a jury trial: "These facts, if taken as true, make a colorable claim for retaliation under the motion to dismiss standard. That is all the Court needs to consider under this more relaxed standard to deny this motion… Whether the facts actually evidence retaliatory conduct is a factual issue that is only proper for the jury to resolve at the trial." In light of the above, the Court denied Defendants' Motion to Dismiss.

Bird v. Success Vill. Apartments, Inc., No. FBTCV156050562S, 2016 WL 888145 (Conn. Super. Ct. Feb. 8, 2016)

(Conn. Super. Ct. Feb. 8, 2016)

Success Village Apartments, Inc. is the property owner and association of a residential cooperative located in Bridgeport and Stratford, Connecticut. Ownership of an apartment unit in Success Village is expressed in an Apartment Leasehold for 99, with Rights to Renew. The Success Village Bylaws provide that one of the persons signing an Apartment Leasehold is eligible to receive a membership certificate, except that a husband and wife may own a membership certificate jointly. The bylaws also provide that each member shall be entitled to a membership certificate. Danuta Dabrowska signed a Leasehold Agreement together with her husband, Pawel Ochman, and was thereby eligible to receive a membership certificate herself, or jointly with her husband. Dabrowska requested that a membership certificate be issued to her in April 2015. Dabrowska was elected to a two-year term on the Success Village board of directors on or about April 2013. It is further found that John Gula and James Capuzziello were also elected to the board of directors in 2013.

The Cooperative's bylaws designate certain committees by name, but do not designate a bylaws committee. At a meeting of the Board of Directors, a motion was made and seconded to abolish the by-laws committee. The motion carried and a letter was sent by the President of the Board of Directors to the plaintiff, Loser Lane, directing him to cease and desist from representing himself as chairman of the bylaws committee in light of the vote to disband them.

At a later meeting of the board of directors on, a motion was made and seconded to present an amendment to the bylaws to the membership for a vote. The existing Article II, section 12.E. provided for a review by the nominating committee of candidates for election to the board of directors to ascertain if they were "in good standing." That motion also carried, and a notice was sent to the membership of a meeting for the membership vote on the proposed bylaws amendment. The total vote in favor of the amendment exceeded the required two-thirds of members voting, and a notice of the amendment was sent to the membership. The new amendments were published in a revised version of the complete Success Village Bylaws.

Plaintiffs Tyreke Bird, Loser Lane, and Betty Aquino, were then nominated for the Board of Directors election, but had not obtained or submitted a nominee package, nor submitted the required forms to the nominating committee. Plaintiff Ivan Perez was not nominated for the board of directors, but he was nominated as one of the nine members of the nominating committee, and he accepted a position thereon. At the next meeting of the nominating committee, he requested to be excused from the nominating committee and he presented a nominating petition as a nominee for election to the board of directors. After consultation with the acting President of the Board, John Gula, the nominating committee determined that Perez could not withdraw from the nominating committee in order to be a candidate for election, and Mr. Perez accepted this determination.

Plaintiff Amy Espinosa was nominated for the board of directors, received a nominee's package, and returned the required forms to the nominating committee. However, the nominating committee determined that she did not meet the qualifications for candidacy in the new bylaw amendments because she was not compliant with the Success Village rules and regulations pertaining to registration of her dogs. Espinosa was informed of her lack of "compliance" by the nominating committee, and urged to achieve compliance by registering her dogs. However, she still did not register her dogs—and was therefore deemed by the nominating committee to be disqualified from a candidacy for the board of directors election.

The nominating committee then prepared a ballot for the annual board election with the names of the four candidates who had complied with the aforementioned qualifications, and Danuta Dabrowska, John Gula and Irena Waluk were elected to the three open seats on the board of directors, and Abraham Peck was elected as an alternate. The Cooperative's bylaws provide that at the annual election of directors, five alternates shall be elected to fill such vacancies as occur on the board of directors. They also provide that vacancies shall be filled from the elected alternates in the order of the vote received by the elected alternates. At the court-monitored election or the Board of Directors held in 2014, the five candidates receiving votes as alternates in the order of votes received were Eula Sutton, Richard Hyder, Lucy Bolivar, Tyreke Bird and Leeann Istvan. Thus, the plaintiff Bird would have been the fourth alternate in line to fill any vacancy on the board of Directors.

At some point in March 2015, the President of the Board of Directors, Andy Weiglein, learned that Blanche Mierzejewski might resign from the board for health reasons. A letter was sent to Mierzejewski by the new President and secretary of the Board of Directors requesting that she submit a written resignation if she intended to resign. Thereafter, board member Jim Capuzziello resigned from the Board of Directors. If an alternate had been needed to fill a vacancy for the following board meeting, the order of alternates would have been Sutton, Hyder, Bolivar, the Plaintiff Tyreke Bird, and Istvan. The Success Village Bylaws provide at Article III, section 7 that an alternate elected to fill a vacancy holds office until the next annual membership meeting. The next annual membership meeting was the election of May 26, 2015, at which time any alternate member of the Board of Directors who may have been serving out the balance of a term of a resigned member, would have expired.

As the Board of Directors conducted no business subsequent to the resignation of Capuzziello or prior to the election of the new Board of Directors on May 26, 2015, no alternate was selected to serve the unexpired portion of Capuziello's term. *If* an alternate had been selected to fill this vacancy, the plaintiff Bird would not have been the first, second or even third choice for this vacancy, as he was the fourth alternate director elected.

The plaintiffs sought a declaratory judgment that the defendants' action in denying the plaintiffs a place on the election ballot was illegal. The plaintiffs further sought a preliminary and permanent injunction restraining and enjoining the defendants from further proceeding and seating the Board of Directors that was elected on May 26, 2015. They also requested: that the Court restrain and enjoin the defendant Paniccia from further involvement in the election process; that it appoint a commission to oversee a new election process, and to replace the present Board, "which is acting illegally;" a court appointed forensic audit of the finances of the Cooperative; and that it remove the defendant Paniccia, as an employee and/or manager of Success Village Apartments, Inc. (The Court decided that it would rule on these requests at a later date.)

Count One of Plaintiffs' complaint called into question the procedural conduct of the April 7, 2015 special meeting of the membership that was held to allow the membership to vote on the proposed amendment to the bylaws' section regarding new qualifications for candidates to the Board of Directors. The plaintiffs argued that the conduct of that meeting violated the bylaws and Robert's Rules of Order. They thus asked the Court for injunctive relief to prevent the candidates for the Board of Directors, who were elected on May 26, 2015, from being seated in their positions. The plaintiffs also sought a declaratory judgment declaring that the actions of the defendants preventing the plaintiffs from having their names included on the ballot was illegal. The Court ruled that "The merits of the claim for a declaratory judgment will be determined at the trial. However, the plaintiffs have now withdrawn their claim for a new election. By doing that, they have in effect, assented to the seating of those candidates who were elected on May 26, 2015." Therefore, it denied Plaintiffs' request for relief regarding a temporary injunction.

Count Two of the complaint was Plaintiff Bird's claims that he was a candidate for the Board of Directors for the 2014 to 2015 term, and as a result of that election, he was elected to the position of next alternate to be appointed. By April 15, 2015, Bird claims that several members of the Board of Directors had resigned their positions, and Bird, as the next alternate, should be appointed to the Board of Directors. (As noted, in the court's findings of fact, Bird was elected as a fourth alternate to the Board of Directors for the 2014–2015 term, which was the court-monitored election.) There was one resignation during that term in April 2015.

Consequently, the Court reasoned that "Bird was not first, second or third in line to be appointed to that vacancy. In addition, if an alternate was to be appointed to fill the balance of the unexpired term of a resigning Board member, the term would have expired with the election of the new Board of Directors who were elected to serve from May 26, 2015 until the next annual general membership meeting in 2016." In any event, Bird was not elected as an alternate during the subject election for the 2015–2016 term for the Board of Directors. Additionally, the plaintiffs withdrew their claim that the court order a new election for the 2015–2016 term of office. Therefore, according to the Court, "there is no prohibition by the court or claim by the plaintiffs that those candidates elected on May 26, 2015 should not be seated as the current Board of Directors. Accordingly, the court cannot offer any practical relief." It ruled that temporary injunctive relief pursuant to the claims in Count Two were also denied.

Lapidus v. 1050 Tenants Corp., 138 A.D.3d 783, 30 N.Y.S.3d 175 (N.Y. App. Div.

2016)

Defendant was a corporation that owns a housing cooperative building in Manhattan, and Plaintiffs were the tenants and owners of shares allocated to apartment 4B of the building under a proprietary lease. As a result of litigation dating back to 1992, Defendant's shareholders voted to terminate Plaintiffs' proprietary lease in 2005. Following litigation to eject the plaintiffs from the apartment, the sheriff officially ejected the plaintiffs in 2007.

In 2008, Defendant entered into a contract to sell the apartment for the sum of $4.2 million. Later, the defendant sent an accounting of the sale to the plaintiffs' attorney with a check for $2,401,471.29, representing the plaintiffs' "net amount payable to them, after deducting amounts due from them to the cooperative and other parties as shown on the accounting." Plaintiffs then filed this action, alleging that the defendants converted a total of $901,270.61 from the plaintiffs by improperly withholding certain funds from the proceeds of the sale.

The New York Supreme (trial) Court granted the part plaintiffs' motion which was for summary judgment on the cause of action to recover damages for the conversion of $250,000 allegedly withheld by the defendant as a "claimed litigation reserve," but denied the remainder of their claims. Plaintiffs now contend that the Supreme Court erred when, upon granting that branch of their motion which was for summary judgment on the cause of action to recover damages for the conversion of $250,000 allegedly withheld by the defendant as a claimed litigation reserve, it stayed entry of judgment pending resolution of the remaining causes of action and counterclaims.

The Appellate Court opined that the trial court "improvidently exercised its discretion in staying entry of a judgment pending resolution of the remaining causes of action and counterclaims…In addition, upon granting that branch of the plaintiffs' motion which was for summary judgment on the cause of action to recover damages for the conversion of $250,000, the court should have awarded interest on that sum running from June 10, 2008, and should have granted that branch of the plaintiffs' motion which was for summary judgment dismissing so much of the second counterclaim as was for a declaration that the sum of $250,000 was properly withheld by the defendant as a litigation reserve."

Plaintiffs also contended that the Supreme Court erred in denying that branch of their motion which was for summary on the cause of action to recover damages for the conversion of $491,541.99 allegedly withheld by the defendant as offsets for certain attorneys' fees. However, the evidence submitted by the plaintiffs established that *they* were contractually liable for any attorneys' fees involved in the sale of the co-op building. Thus, Plaintiffs failed to demonstrate, that Defendant improperly withheld the relevant funds for this purpose.

The plaintiffs further argued that the Supreme Court erred in denying that branch of their motion which was for summary judgment on the cause of action to recover damages for the conversion of $81,077.07, allegedly withheld by the defendant as offsets for unpaid maintenance charges plus interest. However, the defendant as offsets for unpaid maintenance charges plus interest. However, the plaintiffs' evidence failed to back up their claims for such maintenance charges.

The plaintiffs then argued that the Supreme Court erred in denying the portion of their summary judgment motion to recover damages for the conversion of $84,000—which were allegedly withheld by Defendant as offsets for a certain unpaid "flip" tax. However, the plaintiffs again failed to establish the requisite evidence with respect to this cause of action. Accordingly, the Court held that this part of the plaintiffs' motion was properly denied.

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***Robbins v. Penn Ctr. House, Inc.*, 138 A.3d 734, 736–39 (Pa. Commw. Ct. 2016)**

This case arose out of a policy enacted by Defendant Penn Center House, Inc. ("PCH")'s board of directors limiting the number of dwelling units that a member may own in its housing cooperative building, and PCH's rejection of the Robbinses' purchase of an additional unit from the Estate based on that policy. The trial court held that a limitation on the number of units that a member may own can be imposed only by amendment of PCH's bylaws—and therefore granted a declaratory judgment in Plaintiffs' favor that the Board's policy was void.

PCH's articles of incorporation do not define who may become a member or acquire an interest in a unit and do not set forth any rights or restrictions concerning sale or transfer of memberships or units, but provide that "[t]o the extent not addressed in these Articles of Incorporation, Members shall have such qualifications, rights and privileges as set forth in the by-laws." PCH's bylaws provide with respect to membership:

"*Eligibility*. Any natural person approved by the Board of Directors shall be eligible for membership, provided that he or she executes a Subscription Agreement and an Occupancy Agreement in the usual form employed by the Corporation covering a specific unit in the cooperative."

The bylaws can be amended only by a two-thirds vote of the members, not by a vote of the Board, and restrict transfer of units and provide that PCH has an option to purchase a member's membership and right of occupancy before he or she may sell it to a third party. They also provide that if PCH does not exercise that option, "*the member may sell his/her membership to any person who (i) fulfills the Corporation's membership eligibility requirements, (ii) is duly approved by the Corporation as a member,* (iii) executes a Subscription Agreement and an Occupancy Agreement with the Corporation, and (iv) pays the Administrative Transfer Fee and such other charges as may be established from time to time by the Board."

PCH's occupancy agreements in effect at the time of these events provided that if PCH did not exercise its option to purchase the unit, "the Member may sell his membership to any person, but such sale shall not entitle the purchaser to any right of occupancy unless he has been duly approved by the Corporation as an occupant."

PCH's bylaws neither restrict the number of units that an individual may own, nor do they state that a member has a right to own more than one unit or purchase an interest in additional units. The bylaws contain language addressing the situation where an individual owns more than one unit, providing that such individuals count as a member for each unit that he or she owns in membership meetings and votes. These provisions include a reference to possible ownership of three units, stating with respect to annual meetings and special meetings of the members: "For illustrative purposes, should a member have interest in three Units, such member shall count as three members for purposes of determining whether a quorum is present."

In a crucial point, the Commonwealth Court of Pennsylvania noted that nothing in the occupancy agreements addresses ownership of multiple units. With respect to the powers of its board of directors, PCH's bylaws provide:

"Powers and Duties. The Board shall have the powers and duties necessary for the administration of the affairs of the Corporation and may do all such acts and things as are not by law or these Bylaws directed to be exercised and done by the members. The power of the Board shall include but not be limited:

(a) To accept or reject all applications for membership and admission to occupancy of a Unit in the cooperative, either directly or through an authorized representative;

(b) To establish monthly carrying charges prescribed in the Occupancy Agreement, based on an annual operating budget formally adopted by such Board;

(c) To promulgate such rules and regulations pertaining to use and occupancy of the premises as may be deemed proper and which are consistent with these Bylaws and the Articles of Incorporation."

The Board's policies concerning membership applications in effect at the time of these events provided that when a unit became available, it was to be offered first to the members occupying the adjacent units. (They also required income and financial condition minimums for approval of memberships and transfers, which are based on the sale price of the unit and the amount of the monthly charges to which the unit is subject, and provided for criminal background checks.)

Plaintiff Robbinses own and occupy Penn Center House Units 1001 and 1013, which they had merged internally into a single, combined dwelling. In December 2012, the Robbinses notified PCH's general manager that they had learned that the occupant of Unit 1015, which is adjacent to their Unit 1013, had passed away and that they wished to purchase it if it became available. The Robbinses intended to merge Unit 1015 with their combined Units 1001 and 1013.

In March of 2013, the Board enacted the following policy:

"As a new policy, *any one member may not own more than two units.* Further, the name(s) on the certificate(s) for these unit(s) must be identical on both unit's [*sic*] certificates. Lastly, any name(s) on these certificate(s) may not appear on any other Unit certificate. *The only exception to this rule would be if additional unit(s) are to be purchased by an existing Member or Members and their original unit(s) are under agreement of intent to vacate and sell.* Adjoining Units are to be defined as being on the same floor, are physically connected internally, and do not breach the floor slabs of building fire walls."

In May of 2013, co-Plaintiff Estate of Shirley Braverman (the deceased occupant of Unit 1015) gave notice to PCH that Unit 1015 was available. In November 2013, the Plaintiffs entered into an Agreement of Sale to sell the Estate's interest in Unit 1015 to the Robbinses, subject to PCH's approval of the transfer and issuance of a membership certificate and occupancy agreement for Unit 1015 to the Robbinses. On December 9, 2013, the Estate submitted to PCH the Robbinses' application to purchase Unit 1015 and requested approval of the transfer of Unit 1015 to the Robbinses. (Estate Letter to PCH, R.R. at 66a.) On December 16, 2013, PCH rejected the application for transfer of Unit 1015 to the Robbinses based on the two-unit limitation enacted by the Board. (PCH Letter to Estate, R.R. at 68a.) Although Plaintiffs submitted financial information and a release for criminal background check, the Board did not make a determination whether the Robbinses satisfied the other requirements for approval.

The Robbinses commenced this action against PCH on September 16, 2013. On February 26, 2014, the Robbinses and the Estate filed an Amended Complaint asserting claims for tortious interference with contract, breach of contract and declaratory judgment, contending that a limitation on the number of units that a member may own can be imposed only by amendment of PCH's bylaws, not by Board action. PCH filed a counterclaim, asserting that Plaintiffs' action was a violation of PCH's bylaws and the occupancy agreements that the Robbinses and the Estate's decedent signed.

Defendant PCH argued that its Board has the power under PCH's governing documents to impose a restriction on the number of units that a member may own by policy *without* a vote of the members to amend the bylaws. The Court did not agree, ruling that under Maryland law—this case was governed by the law of the state under which PCH was incorporated, Maryland—regarding articles of incorporation (specifically, the qualifications, rights, and privileges of its members), Defendant's restrictions on ownership and on transfer of units had to be set forth in its corporate bylaws. Therefore, the board of directors lacked the authority to enact the above policy limiting ownership to two units.

The Court opined that the cooperative's bylaws granting its Board a general power to "do all such acts and things as are not by law or these Bylaws directed to be exercised and done by the members" did not give its the authority to limit the number of units that its members could own: "Such a grant of power authorizes the Board to manage PCH's business and act on matters that neither law nor its articles of incorporation require be addressed in the bylaws. Limiting member ownership rights is not the management of PCH's business as a housing cooperative; it is a regulation of the rights and privileges of PCH's members, which, under PCH's articles of incorporation, must be set forth in its bylaws."

PCH then argued that "the nature of housing cooperatives gives its Board the power to limit the number of units a member may own." The Court pointed out that "PCH is correct that its members do not hold fee simple title to their units and are in a landlord-tenant relationship with respect to occupancy of the units." However, it qualified this statement by opining that the threshold issue "is not whether PCH may limit ownership to two units, but how it may impose that limitation. None of the cases cited by PCH suggest that restrictions on the number of units that members own may be imposed by board of directors' action rather than by bylaw." In that regard, the Court held that "a housing cooperative's board of directors lacks authority to impose substantive restrictions on transfer and ownership rights that are not set forth in the bylaws or the proprietary lease."

Finally, Defendant argued that the Board's policy limiting ownership to two units is protected by the business judgment rule. The Court disagreed, holding that that the business judgment rule—which protects decisions of a corporation's board of directors from judicial review where it is not shown that the board's actions were in bad faith, arbitrary, or fraudulent—had no applicability to the instant issue of authority of a co-op's board to limit the number of units that could be owned by any individual owner, where board lacked the authority as described above to so limit. It therefore ruled in Plaintiffs' favor: "Because the Board lacked authority to limit unit ownership by policy, the business judgment rule has no applicability here."

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New Liability Ruling: How Does It Affect Boards?

DESCRIPTION	How does a new liability ruling affect boards?
TOPICS	**Liability, Board of Directors, Board Operations**
AUTHOR	Richard Siegler and Dale J. Degenshein
ISSUE	**September 2012**
ARTICLE TYPE	**Case Notes**
PAGE #	52-56
ABSTRACT	Is an individual board member exempt from liability if acting in his or her capacity as a board member?

New Liability Ruling: How Does It Affect Boards?

Is an individual board member exempt from liability if acting in his or her capacity as a board member? That was one of the many questions in *Fletcher v. The Dakota Inc.*

Alphonse "Buddy" Fletcher Jr. was a resident of The Dakota, a co-op apartment house at 1 West 72nd Street in Manhattan. Fletcher, an African-American, alleged that the co-op and two of its directors discriminated against him because of his race when the board refused to approve his purchase of an apartment adjacent to the one he already owned, for the purpose of combining the two. Fletcher claimed that the co-op and two individual board members retaliated against him because he sought to protect the rights of minority and Jewish shareholders and applicants. He also claimed he was defamed by the defendants.

Before it addressed this particular case, the appellate court discussed potential individual director liability. In a prior case, *Pelton v. 77 Park Avenue Condominium*, the same court that was deciding this motion discussed individual director liability. Here, the defendants argued that claims should have been dismissed against two board members because the complaint failed to show that they took action separate and distinct from the actions they took as board members – in other words, that Fletcher failed to allege that they had engaged in any independent tort-related conduct.

The court first reviewed the state human rights law (a discrimination statute), which prohibits discrimination by an owner, "lessee, sub-lessee, assignee, or managing agent of, or other person having the right to sell, rent, or lease a housing accommodation … or any agent or employee thereof." The city human rights law similarly provided for individual liability. The court noted that there were no exceptions in either statute for directors of co-ops or directors of any other corporation.

The court then discussed the "Business Judgment Rule," as enunciated by New York's highest court – the Court of Appeals – in *Levandusky v. One Fifth Avenue Corporation*. The *Levandusky* court found that the rule was the proper standard of judicial review so that the court would not review actions taken by corporate directors if taken in good faith, in the exercise of honest judgment, and in the lawful furtherance of corporate purposes. In *Levandusky* and a later case, the court cautioned that the rule should not serve as a rubber stamp for board actions. Accordingly, the *Fletcher* court explained, arbitrary, malicious, or discriminatory acts were not protected.

The court found that there was nothing in these Court of Appeals cases to suggest that there was a safe harbor for directors. There was also no principle of corporate law that a director would be liable only if he or she committed a tort independent of the tort committed by the corporation itself. Indeed, the court explained that it had long been the law that a corporate officer who participated in a tort could be individually liable.

In addition to reviewing case law, the court cited a leading treatise in corporate law. Directors could be personally liable to third persons if they participated in, directed, controlled, approved, or ratified the decision that led to a plaintiff's injuries.

The court then discussed its 2006 decision in *Pelton* and determined that it had misapplied the dictates of a 1978 Court of Appeals case. The court noted that it had improperly conflated the concepts for breach of contract (where an individual director would not be liable) and commission of a tort (where an individual director may be liable).

With respect to discrimination claims, the Court of Appeals recently determined that the city's discrimination statutes should be construed broadly in favor of plaintiffs who claim discrimination. Accordingly, the court did not dismiss discrimination claims against the individual board member.

The court next discussed Fletcher's claim of retaliation by the co-op and a board member. The New York State discrimination statute stated that it was unlawful to retaliate against someone because he or she opposed any practice of discrimination. The court explained that to make out a claim for retaliation under state law, the complaint had to allege that (i) Fletcher opposed conduct protected by the statute, i.e., discrimination; (ii) the defendants knew about Fletcher's conduct; (iii) Fletcher was subject to an adverse action; and (iv) there was a causal connection between Fletcher's actions and the adverse action.

The city discrimination laws were similar – one could not retaliate against someone because the person opposed discriminatory practices. With respect to the city law, however, the retaliation need not have resulted in an ultimate action or in a materially adverse change but must be reasonably likely to deter a person from acting.

The court interpreted the city law, as it was required to, "broadly in favor of discrimination plaintiffs" to the extent such a construction was "reasonably possible." The court relied on an earlier case, which explained that when reviewing a retaliation claim, the court had to have a "keen sense" of the realities and that the "chilling effect" of conduct was dependent upon the surrounding circumstances. To make out a claim for retaliation under the city laws, Fletcher had to allege that (i) Fletcher opposed discriminatory practices; (ii) the defendants took an action that disadvantaged Fletcher; and (iii) a causal connection existed between Fletcher's actions and the adverse action.

In the complaint, Fletcher alleged that he began to oppose conduct that he believed was discriminatory after he was elected president of the co-op board in May 2007. In September of that year, Fletcher complained to one of the individual defendants that another board member had referred to certain applicants as the "Jewish mafia." Those applicants were initially rejected, although Fletcher and one other voted to approve them. Fletcher claimed that the board member asked him not to raise the issue again, but that Fletcher urged the board to meet the applicants and, upon doing so, it approved the application. Based upon Fletcher's allegations of discussions about the Jewish applicants' ethnicity and religion, the first element of the retaliation claim had been established.

Fletcher alleged that the defendants denied him the benefit of a specific building policy concerning his application to purchase another apartment, denied him an impartial and unbiased review of his financial disclosures, and recommended rejection of his application. Thus, Fletcher alleged sufficient claims to establish that he was subjected to an adverse action.

Because an individual director had knowledge of Fletcher's actions, his knowledge was imputed to the co-op. The court addressed whether the time lag between Fletcher's challenge to the board's initial rejection of the Jewish applicants and the board's alleged retaliation was an issue. It held that the approximate three-year gap did not defeat the claim; Fletcher's application to purchase another apartment was the first opportunity the board had to retaliate.

As to another director who was individually named, he did not become a board member until after September 2007, and the retaliation claims were dismissed against him on the theory that he did not know about Fletcher's actions in September 2007. If it was determined that he did know, Fletcher had the right to ask the court to reinstate the claim. As to the co-op, the court refused to dismiss Fletcher's claims as they related to the Jewish applicants.

The complaint also alleged that Fletcher "made it clear" to the board that its jokes about another shareholder's bathroom repairs were inappropriate. However, even though the shareholder was African-American, there was no claim that Fletcher had made reference to her race. Accordingly, claims of retaliation based on statements made about this shareholder were dismissed without prejudice so that if discovery showed that the defendants knew Fletcher was opposing discrimination when discussing her, Fletcher could ask that the claim be reinstated.

The court then discussed that, because The Dakota is a corporation, it does not owe a fiduciary duty to its shareholders. Claims based on fiduciary duty were dismissed against The Dakota with prejudice so that they cannot be re-pleaded. As to the individuals, however, the fiduciary duty claims were dismissed without prejudice, so that if discovery showed additional information, Fletcher could request that they be reinstated.

The court then turned its attention to the defamation claims. To the extent any defamation claims were based on papers submitted in the lawsuit, they were dismissed because the statements were protected communications made in the context of a lawsuit.

As to other statements, the assertion was that the defendants "knowingly and maliciously spread false statements and rumors to third parties, including the media, concerning Fletcher's financial condition." The court acknowledged that the complaint set forth specific allegedly defamatory statements verbatim. While the co-op claimed that the statements were the subject of a "qualified privilege," presumably because they were made only to shareholders at The Dakota (the decision does not specify), the privilege can be defeated by a claim that the statements were made with malice, which Fletcher alleged. As to the individuals, the defamation claim was not dismissed for one who Fletcher alleged had made defamatory statements.

The court next turned to the claim that the co-op tortiously interfered with Fletcher's contract to purchase the apartment. The court stated that a cause of action could be present and did not dismiss the co-op's claim. It did, however, dismiss the claim against one individual board member as there was no evidence that he had committed an independent tortious act outside his role as a board member. **Comment**

: *While this decision is being reported by some as a departure from prior decisions, and it does specifically "overrule" the* Pelton v. 77 Park Avenue Condominium *decision in which it was found that board members were not liable for* *discrimination, it is our belief that in many respects the appellate court is merely reiterating long-standing corporate law, i.e., that in the context of a tort or a claim of discrimination (and not contract claims), if a board member acts in furtherance of that tort, he or she may be liable. This is consistent with such well-known cases as the* Broome v. Biondi (Beekman Hill Apartments) *matter, where board members were held personally liable for refusing to allow a mixed-race couple to sublet based upon actions taken by board members, who, according to testimony, took the husband's African-American race into consideration when rejecting the couple.*

Indeed, the court is clear that board members will not be responsible for the co-op's breach of contract. What is of concern is whether board members may be held liable for torts committed by their co-op, such as negligence. While certain provisions of the decision would lead one to believe that this may be the case, the court specifically dismissed the claim of tortious interference with contract against a board member, stating that "the complaint does not allege that [the board member] committed independent tortious conduct outside of his role as a board member." We believe these aspects of the case will be reviewed and interpreted by the courts in future decisions.

As to the defamation claims, while there is a qualified privilege that permits board members and shareholders to discuss information about their building without being subject to a claim for defamation, that privilege will not apply in the event there is a claim of "malice," i.e., that the statement was made with knowledge that it was false or with reckless disregard of whether it was true. In this case, it appears that certain statements were alleged to have been made to the press, and were not subject to the privilege in any event. Other statements made to board members and shareholders were alleged to have been made with malice and therefore were not dismissed.

We note that the motion to dismiss the claims was made at the early stage of the case so that discovery may shed a different light on certain allegations and defenses.

Attorneys

For Plaintiff

Vladeck, Waldman, Elias and Engelhard and Kasowitz, Benson, Torres & Friedman

For Defendants

Quinn Emanuel Urquhart & Sullivan and Balber Pickard Maldonado & Van Der Tuin

The New York Times | https://www.nytimes.com/2018/04/27/realestate/could-you-be-sued-as-a-co-op-board-member.html

Could You Be Sued as a Co-op Board Member?

By Kathleen Hughes

April 27, 2018

Let's say you volunteer to serve on the board of your New York co-op apartment, and conflicts arise. Legal threats follow.

Just how much personal risk have you taken on?

While most boards carry liability insurance for the directors and officers, would it protect you in the event of legal action? Or could you be forced to pay legal fees and suffer damages?

No one seems to be keeping track of the total number of lawsuits filed against the boards and individual directors of the roughly 6,000 cooperative apartment buildings in New York City. But lawyers say it is extremely common for angry co-op members to file lawsuits and name individual directors — often as a bullying tactic.

At the same time, court awards against individual directors are so rare that many co-op lawyers cannot name a single recent example.

"Board members get sued on a regular basis as an act of extortion by a plaintiff wanting to get the board to act in a particular way," said Stuart M. Saft, the chairman of the Council of New York Cooperatives and Condominiums and a partner at Holland & Knight.

It is a tactic that usually backfires. Most boards are covered by liability insurance, and those policies usually kick in, covering the legal costs of the board and the individual directors.

The plaintiffs, however, are left paying their own mounting legal costs, winning mostly the enmity of their neighbors. "The plaintiffs think, 'We'll sue the individuals, they will panic, and we will have them in our grasp!'" said Mr. Saft. "But that's not what happens."

Most co-op boards, of course, are made up of volunteer shareholders elected at a building's annual meeting. The group then rules on everything from approving new buyers to reviewing and approving renovations and building projects.

But because so many decisions involve the volatile combination of people's homes, money and control, conflicts can quickly become heated. Many suits seek to overturn a board decision, and many of those decisions are about pets: the weight and size of the dogs allowed in the building.

"Mostly, no one is suing for money," said Kevin Davis, president of Kevin Davis Insurance Services. "They are fighting over every little detail, and particularly rules on pets. The more money and the more time people have, the more lawsuits you are going to get."

Mr. Davis added, "In New York City, you have a lot of money, so it's more intense. Lawsuits are usually filed by the people who live there who don't want to follow the rules."

Lawyers say New York courts have tended to protect individual directors of co-ops and condominiums as long as they were acting legally, in good faith and using honest business judgment.

The courts also tend to protect corporate boards acting in the best interest of the corporation, under what is known as the business judgment rule. “As long as you are acting in the best interest of the corporation, you won’t be held liable,” said Terrence A. Oved, chairman of the real estate and transactional department at Oved & Oved LLP.

The big exception, of course, is willful legal wrongdoing such as discrimination and self-dealing. Not surprisingly, directors’ and officers’ liability insurance is not likely to cover damages in those types of claims.

“The risks of legal liability are not high unless you engage in some sort of nefarious conduct,” said Steven D. Sladkus, a partner with Schwartz, Sladkus, Reich, Greenberg, Atlas, LLP.

One inherently tricky part of being on a co-op’s board of directors is that while you have a legal obligation to act in the best interest of the corporation, individual directors are also shareholders — and may have a personal stake in the outcome of a board vote on something like whether to spend money on a roof garden or a gym.

The best way for a board and for individual directors to avoid legal threats, lawyers advise, is to study all corporate documents carefully — the bylaws, the proprietary lease, the offering plan, the house rules and the certificate of occupancy — and follow them uniformly.

“Directors need to know they are handling a multimillion dollar corporation, and if you don’t enforce the documents uniformly, you can be sued. You have to treat everyone the same,” Mr. Davis said.

And the best defense against getting hit with your own personal legal fees is to make sure the board has adequate liability insurance. Not all policies are the same. Most co-op bylaws include legal indemnification for directors — but directors should check.

Insurance brokers say smaller buildings often wind up underinsured either by oversight or because they were trying to save money on insurance. Some try to save money by tacking a so-called endorsement for the coverage on their general liability policy as opposed to having a more expensive stand-alone policy.

“I do run across buildings that don’t have coverage,” said Edward J. Mackoul, president of Mackoul Risk Solutions, in Island Park, N.Y. “There are co-ops that don’t want to pay even $150 to add coverage because there are just five units and they all know each other.”

Court-ordered monetary awards against individual co-op board directors are so rare that most lawyers can name just one case, frequently referred to simply as Biondi. After a biracial couple was turned down for a sublet in the upscale Beekman Place neighborhood on the East Side of Manhattan, the couple claimed they were victims of racial discrimination.

In 1997, a federal jury in Manhattan awarded them $640,000 in damages, including $410,000 in punitive damages against Beekman Hill House and its board members. The jury awarded $150,000 against the co-op, $125,000 against Nicholas Biondi, the board president, $60,000 against Richard Appleby, another board member, and $25,000 each against three other directors.

“In more than 30 years of doing this, that is the only case I know where there was any personal liability against individual board members,” said Mr. Saft, the real estate attorney.

A version of this article appears in print on , Section RE, Page 14 of the New York edition with the headline: Board Members Beware