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Condominiums—Board Sued Sponsor, Members of the Sponsor and Architect Over Alleged Building Defects—Breach of Contract—Privity—Express Warranty—Martin Act—Negligence—Fraud—General Business Law §349—Interstate Land Sales Full Disclosure Act (ILSA)

This is an action by the Board of Managers (board) of a condominium, alleging inter alia, a breach of contract arising out of construction of a newly erected building. The defendants moved to dismiss each cause of action. The building consisted of 68 residential housing units and a non-residential garage unit, with an alleged capacity of 32 parking spaces. The defendants included the sponsor, members of the sponsor and an architectural firm.

The complaint alleged that pursuant to the offering plan (Plan), the sponsor was to "perform such work and supply such materials, or will cause the same to be performed and supplied, as is necessary in order to complete the Building with a quality of construction comparable to the currently prevailing local standards." The sponsor was obligated to bear the costs and expenses to complete the construction "substantially in accordance with the plans and specifications." Under the Plan, the sponsor was to "attempt to obtain a Permanent Certificate of Occupancy" (C of O) for the "Building within [two] years after the first closing, but in any event, before the expiration of the applicable Temporary Certificate of Occupancy" (TCO), as "the same may be renewed, replaced or extended."

The plaintiff further alleged that the sponsor "had not complied with General Business Law" (GBL) "352-e (2-b) and 352-h, to maintain a special trust account containing funds certified by the Architect as reasonably necessary to complete the work needed to obtain a [C of O]."

The plaintiff claimed that shortly after moving into their units, the owners "began experiencing 'conditions indicating that the design and construction of their individual

units and the building was defective and not constructed in a skillful manner, in that the workmanship and materials used in the construction did not meet the specific standards of the Building Code.'" The board's expert reported "various defects and violations" relating to the construction.

The complaint further alleged that after "a site visit" by the NYS Attorney General, the sponsor "acknowledged the presence of construction defects and agreed to remedy the same." However, the plaintiff alleged that "only minor patch work was ever commenced." The plaintiff also alleged that the sponsor had also "failed to pay invoices" for construction, "causing mechanic's liens to be placed against the property by multiple contractors."

The defendants argued, inter alia, that the plaintiff was "no more than a group of 'disgruntled' unit owners" and that the board lacked standing to bring the subject action. The court explained that a "condominium board has standing to make such a claim on behalf of the individual condominium unit owners by reason of..., Real Property Law §339-dd, under which the board of managers...is empowered to maintain an action on behalf of the condominium owners with respect to 'any cause of action' relating to common elements of more than one unit...." The complaint alleged numerous defects impacting common areas, as well as multiple units on different floors, thus meeting "the commonality elements required by the statute." Further, the plaintiff submitted an affidavit "showing unanimous consent of the Board members to commence the action in the form of individually signed letters...." Accordingly, the court found that the plaintiff had standing.

The defendants had also argued that individual defendants could not be held liable to the plaintiff "on a breach of contract theory, due to their lack of privity with Plaintiff." The court explained that, within the Appellate Division, Second Department, "a plaintiff may seek damages for a breach of contract against the individual principals of the sponsor, based upon certification of the...plan and the incorporation of the terms of the...plan in a specific provision of the purchase agreement...." Accordingly, the court held that the motion to dismiss for lack of privity as to the individual defendants should also be denied.

After reviewing the allegations of the complaint, the representations set forth in the Plan which were incorporated into the purchase agreements and the "itemization" of

construction defects in the plaintiff's expert report, the court found that the plaintiff had sufficiently alleged the material elements of the breach of contract claim and denied the motion to dismiss that claim as well.

The court then held that the claims against the architect should be dismissed since "[n]either the plans, nor any other agreement between Plaintiff and Defendant Architect, reflect the intent to specifically benefit Plaintiff." Thus, the contract between the sponsor and architect did not extend privity to the plaintiff as an intended third-party beneficiary. Since the plaintiff lacked standing to bring a breach of contract claim against the architect, the claim against the architect was dismissed.

The court then denied the defendants' motion to dismiss the breach of an express warranty claim. The Plan had required the sponsor to "correct, repair, or replace any and all defects relating to the construction of the Building." The defendants had argued that the Plan provided that "[n]othing contained in this section will be construed so as to render sponsor liable for money damages (whether based on breach of warranty, or otherwise), it being intended that sponsor's sole obligation under the plan will be to repair or replace any defective item of construction." The plaintiff had alleged that the defendants had "discontinued the repairs that were not only required under the express warranty, but were agreed to after a meeting with the Office of the Attorney General...." Since the defendants had "allegedly abandoned their prescribed duties under the express warranty provided, the motion to dismiss this cause of action" was denied.

The defendants had also moved to dismiss a claim based upon a "breach of the common law housing merchant implied warranty. The defendants argued that the common law implied warranty was inapplicable to the present case, since "the codification of the Housing Merchant Implied Warranty contained in [GBL] Article 36-B is a substitute for plaintiff's common law remedy for breach of warranty." The court explained that "[u]nder New York [GBL] §777-b, the exclusion or modification of the housing merchant implied warranty is permitted only if the buyer is offered a limited warranty in accordance with the provisions of that statute." Since the court did not have the complete Plan, it had "an incomplete accounting of all warranties prescribed therein," and could not determine whether a cause of action for breach of the housing merchant implied warranty had been stated. Thus, the court denied the motion to dismiss such claim.

The court then denied the defendants' motion to dismiss the claim against the sponsor and its principals which alleged a breach of contract regarding the sponsors' failure to timely obtain a C of O. The defendants argued that the Plan did not require the acquisition of a C of O as long as a TCO is in place and that this cause of action was duplicative of the plaintiff's prior breach of contract claim. Since the court did not have the full Plan, it could not determine the duties imposed under the terms of the contract.

Moreover, this claim was "solely predicated upon the failure of the Defendants to obtain a [C of O], which is more than adequately set forth with the requisite detail required under CPLR 3013." Additionally, these facts had not been set forth elsewhere in the complaint. Therefore, the cause of action was not duplicative of other causes of action and the court denied the defendants' motion to dismiss this breach of contract cause of action.

With respect to the claim that the defendants had failed to comply with GBL §§352-e(2)(b) and 352(h), the complaint alleged that the defendants "were obligated to certify that sufficient funds were available in an Escrow Account to complete the project and obtain a [C of O]." The complaint alleged that the sponsor knew or should have known that there were "deficient and untruthful certifications when it improperly directed the escrow agent to release funds needed to obtain a [C of O]." The defendants argued that this cause of action should be dismissed, since "the Attorney General is vested with exclusive authority to litigate claims under the Martin Act."

The Court of Appeals previously held that "a private litigant may not pursue a common-law cause of action where the claim is predicated solely on a violation of the Martin Act or its implementing regulations and would not exist but for the statute. But, an injured [party] may bring a common-law claim (for fraud or otherwise) that is not entirely dependent on the Martin Act for its viability. Mere overlap between the common law and the Martin Act is not enough to extinguish common-law remedies." The court found that the Martin Act claims must be dismissed since "[b]y the terms of the statute, the determination as to the sufficiency of the escrow fund and releases therefrom, is vested exclusively in the Attorney General."

The court then dismissed the negligence claim on the grounds that the plaintiff failed to allege that the defendants had a legal duty to it "outside the contract" and the negligence claim was "nothing more than an allegation of a breach of contract against the sponsor

and its principals." The court also dismissed the plaintiff's cause of action for fraud that was based on alleged misrepresentations as to whether the work would be adequately performed, since the court found such claims to be duplicative of the breach of contract claim.

Additionally, the plaintiff had alleged that the defendants had made "'false, deceptive and misleading statements' in the purchasing agreements and [the Plan] regarding the construction of the building in violation of General Business Law §349(a)." In order to prevail on such claim, a plaintiff must allege that the improper act was "consumer oriented," the improper act was "misleading in a material respect," and "the plaintiff was injured as a result of the deceptive practice, act, or advertisement." In order to demonstrate that an act is "consumer-oriented," a plaintiff must demonstrate that "the acts or practices have a broader impact on consumers at large."

In order to meet such criteria and establish that the defendants' alleged misrepresentations had the "requisite broad impact upon the public at large, plaintiff has cited to three other pending suits against the Sponsor Defendants alleging similar defects in construction." However, although the plaintiff could pursue a viable common law fraud cause of action, the plaintiff lacked standing to pursue its claim under [GBL] §349 "as 'pursuant to the Martin Act, the Attorney General has exclusive jurisdiction to prosecute sponsors who make false statements in condominium offering plans filed thereunder'...."

The court believed that "[t]o permit plaintiff to proceed with its private claims under [GBL] §349, given the allegations contained in the [subject] cause of action, which are exclusively premised upon the representations contained in the purchase agreement and offering plan, and track the breach of contract claims, would be to authorize 'a backdoor private cause of action to enforce the Martin Act' in violation of the statutory scheme...." Thus, the court dismissed the GBL §349(a) claim.

The plaintiff had also alleged a violation of the Interstate Land Sales Full Disclosure Act ("ILSA"), i.e., 15 U.S.C. §1703(a)(2)(A),(B) and (C). Section 1703(a)(2) of ILSA provides that it is unlawful for any developer or agent, directly or indirectly, to make "made false, deceptive and misleading statements in the purchase agreements and the joint certification in the offering plan with respect to constructing the building in accordance

with the offering plan and local standards, as well as with respect to the correction of any defects in the construction of the building."

These allegations were directed solely at the sponsor defendants. The defendants argued that this claim should be dismissed because it is duplicative of a breach of contract claim and the plaintiff had not sufficiently pled a violation of ILSA against the "individual Defendants, which requires the Defendants to have a personal involvement in the sale of any condominium unit, or allege fraud with the required level of particularity."

The court noted that New York state courts "do not appear to have ever addressed the pleading requirements of a 15 U.S.C. §1703 cause of action or the issue of whether it must be dismissed where the allegations are duplicative of the claims in a breach of contract cause of action." However, a recent federal District Court had recently held that a condominium board lacked standing to assert a cause of action under ILSA statute "as an association does not have standing to litigate such cause of action where 'the relief requested requires the participation of individual members in the lawsuit'...."

The federal case held that "'associational standing [could not] be maintained...because proving the claims in the complaint would require the participation of each individual purchaser' with respect to, among other issues, the prices each individual paid for the units and the costs expended by the purchasers...." The federal court had noted that "individual unit purchasers were 'free to institute their own federal action or to interpose their claims in [another] pending state litigation'...." The subject court concluded that the plaintiff lacked standing to bring the ILSA claim and dismissed such claim without prejudice to the claims of the individual unit owners.

The plaintiff had further alleged that the defendants breached their contractual obligations by permitting more than 32 cars within the parking garage, "causing 'the walkways to the mechanical room, electrical room and exit to the basement to be blocked with little or no access.'" The plaintiff sought injunctive relief compelling the defendants "to eliminate the 'unlawful and dangerous overcrowding of the parking garage.'" The defendants countered that the plaintiff had not suffered irreparable harm and whatever the lack of access may involve, it did not constitute "a 'substantial prejudice' to plaintiff" and did not warrant injunctive relief. The court found that the plaintiff had sufficiently alleged a cause of action for a permanent injunction.

The court then denied the defendants' motion to dismiss the plaintiff's claim for attorney fees. The plaintiff argued that under the condominium by-laws, "the Board may collect costs and expenses incurred in order to abate and/or enjoin any nuisance and/or violation of the by-laws from the unit owner that necessitated such costs and expenses." Since there had been no actual determination regarding nuisance or a violation of the by-laws, the court held that it would be premature to dismiss such claim and denied the motion to dismiss the attorney fees claim.

Finally, the plaintiff had sought damages against the sponsor and the principals for failure to pay common charges, which was allocated to "unsold residential units prior to the closing of said units. The allegations contained the "requisite detail" to provide notice of that claim and the court denied the motion to dismiss relating thereto.

Disclosure: While my firm was not counsel on the matter, it has represented certain of the defendants in other matters.

Comment: Adam Leitman Bailey, counsel to the plaintiff, stated that this decision is notable because it, inter alia, upheld the board's standing pursuant to RPL §339-dd, to sue the sponsor and to sue principals of the sponsor for breach of contract and breach of warranty, based upon the certification in the offering plan and the incorporation of such certification into each purchase agreement. Bailey also noted that this decision permitted a claim for money damages against the sponsor, notwithstanding certain offering plan language that limited relief to remediate the defects. The plaintiff had argued that the sponsor had abandoned its obligation to correct the alleged defective work.

Board Managers of the Crest Condominium v. City View Gardens Phase II, **4873/2011, NYLJ 1202555399490, at *1 (Sup., KI, Decided May 11, 2012), Demarest, J.**