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CO-OP, CONDO & REAL ESTATE ADVISOR

Grandfathering Needs a Legislative Green Light

By Bruce A. Cholst and Karol S. Robinson

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This article highlights an issue that bedevils cooperative and condominium boards in the governance of their communities, and suggests an expedient legislative solution. The problem: Even when boards conclude that changes to a longstanding practice or policy are warranted to accommodate shifting needs, priorities, or demographics within the community, they are often stymied out of concern for residents who have been granted prior approvals and have adjusted their lifestyles based on those allowances. Examples include permission to harbor pets, sublet their apartments, maintain washers and dryers within their apartments, or permissions relating to smoking habits, each made in accordance with existing board policies.

For equitable or political reasons, boards frequently opt to grandfather in the existing rule or policy so that current residents who received certain allowances are permitted to retain their privileges until they naturally expire (e.g., their pet passes, their sublet term comes to an end, or their appliance cannot be repaired), while the new policy applies immediately to residents not granted prior approval or who prospectively enter the community.

The problem is, this expedient practice is strictly prohibited by New York's Business Corporation Law (BCL), Section 501(c), which mandates that "each share (of corporate stock) shall be equal to every other share of the same class." Inasmuch as there is typically only one class of stock in a residential co-op apartment corporation, this provision has been consistently construed to mean that no tenant-shareholder may receive preferential treatment relative to other tenant-shareholders in the administration of corporate policy. A two-tiered policy that permits accommodation through grandfathering to some shareholders, but not to others, is clearly preferential in nature and would be vulnerable to legal challenge.

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This article suggests a solution to the dilemma by legislative amendment to the statute, which would permit the expedience of grandfathering to facilitate desirable governance changes within residential communities, while still preserving the fundamental mandate of parity among corporate stockholders of the same class. We believe that the time has come for the state Legislature to consider an amendment to BCL Section 501 (c) that would carve out an exception to the provision's applicability in situations where co-op boards amend their governance policies prospectively but elect to grandfather in accommodations made to existing shareholders under the policies then in existence. (An analogous provision should be incorporated into the Condominium Act).

Such an exception would not be unprecedented. The Legislature has already enacted a similar carve-out for "flip taxes" payable to residential co-op corporations. (*See* BCL Section 501 (c) (3)).

Absent legislative intervention of this nature, co-op and condo boards will be impeded in their efforts to operate their communities at optimum efficiency.

We strongly urge you to appeal to your state senators and assemblymen for adaption of this reform if you agree that it would facilitate governance of residential communities.

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