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Cooperative/Condominium Boards and Breach of Fiduciary Duty

By Alan M. Goldberg



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As cooperative shareholders and condominium unit owners join boards of directors and boards of managers, they will undertake fiduciary duties toward those entities. (Although this article applies to both coops and condos, for convenience sake, it refers only to coops.) This article is to help new (and longtime) board members avoid breaching their fiduciary duties.

The members of a coop's board of directors have a legal obligation to act in the best interest of the corporation and its shareholders. They can, however, breach that duty by:

- Taking unauthorized actions.
- Ignoring critical issues.

In order to render informative decisions, directors must be knowledgeable about their coops, including:

- The corporation's financial condition.
- The property's physical condition.
- The existence of building violations.
- Residents' complaints.
- Existing or potential litigation.
- New laws, rules and regulations that must be complied with.

Directors must review the governing corporate instruments and corporate records to obtain vital information. No director can be prevented from inspecting the books and records.

The board must:

- Act within the authority granted to it under the corporate documents.
- Maintain the coop in good financial condition.
- Effectuate necessary repairs/capital improvements.

- Enforce the coop's rules.
- Cure building violations.
- Ensure the safety of the building and residents.
- Retain necessary contractors and professionals.

The board cannot ignore:

- The coop's deteriorating financial health.
- The property's structural problems.
- Violations of the coop's rules
- Unpleasant building conditions.
- Proposed apartment renovations.

Ignoring such matters can lead to problems or allow existing problems to fester.

While the business judgment rule protects authorized board decisions that are devoid of discrimination, fraud and self-dealing, it does not protect breaches of fiduciary duty. How the board deals with an impending financial or structural crisis may be a business decision (e.g., replace or patch a leaking roof), but the need to address that crisis is a fiduciary duty of the board.

Board members cannot ignore a proposed apartment alteration, as the intended work may damage the building and harm residents.

In a lawsuit I handled, the board rejected a shareholder's proposal to build a second bathroom over a resident's living room. This "wet-over-dry" type of alteration has been rejected by numerous coops, since a leak from the bathroom can cause extensive damage to artwork, furniture and flooring in the downstairs living room. The court upheld the board's rejection under a reasonableness standard, especially as new pipes would have had to connect to old, deteriorated pipes, and leaks were likely to occur. Had the board ignored the proposal and water damage resulted from the renovation, the board may have been sued for breach of fiduciary duty.



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Another lawsuit I handled involved a shareholder's installation of a Jacuzzi in his apartment and other renovations without the board's knowledge. After learning of the Jacuzzi, the board retained an architect who inspected the Jacuzzi and the building, and who determined that the Jacuzzi's shoddy installation could cause leaks, the shaking of the Jacuzzi could damage the building's flimsy wooden structure, and its loud noise could inconvenience residents. The court ordered the removal of the Jacuzzi. Had the board ignored this renovation, it could have been sued for breach of fiduciary duty by an injured resident.

The board has a duty to investigate an odor emanating from an apartment, since the odor may be an indication of a serious problem, such as hoarding, infestation of roaches and rodents, and deterioration of the apartment.

An involved, proactive board that doesn't shy away from the building's problems, but seeks to confront and solve them, can help avoid claims of breach of fiduciary duty. ▲

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