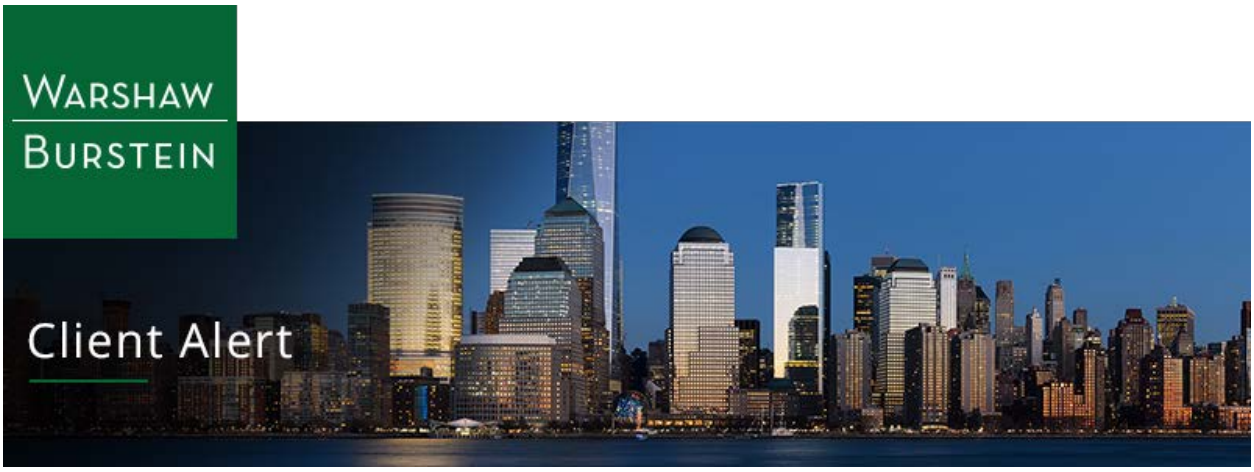

February 15, 2018

IS THIS THE END OF THE *YELLOWSTONE* BRICK ROAD?

A recent decision by the Appellate Division, Second Department may result in tenants losing their right to seek a so-called *Yellowstone* injunction to prevent the termination of their commercial leases. In 159 MP Corp. v. Redbridge Bedford, LLC, 2018 NY Slip Op 00537 (2d Dep't) (Jan. 31, 2018), the Second Department held that a lease provision, whereby the tenants expressly "waived" their right to bring a "declaratory judgment action" with respect to any lease provision or any notice served pursuant to the leases, but agreed to adjudicate lease disputes via summary proceedings, did not violate "public policy," and, as such, was valid and enforceable. This decision will encourage landlords to draft commercial leases that include a "waiver provision," in an attempt to strip tenants of a very important and powerful remedy available to them when faced with a notice to cure or a notice of termination that could lead to the termination and forfeiture of a valuable commercial lease.

Background

As noted in our prior Client Alerts, the New York Court of Appeal's 1968 decision in First National Stores Inc. v. Yellowstone Shopping Center, Inc.[1] spawned a new species of injunctions for tenants faced with termination of their commercial leases based on alleged lease "defaults." A *Yellowstone* injunction preserves the *status quo* pending adjudication of the underlying lease dispute, without regard to the likelihood of success on the merits.[2] Its very purpose is to "toll" the cure period to allow a tenant, confronted by a threat of termination of its valuable commercial lease, to obtain a stay extending the "cure period," so that a determination of the merits can be made without the tenant risking forfeiture of its leasehold.[3] The Court of Appeals has stated that a *Yellowstone* injunction serves the limited purpose of "tolling" the cure period.[4]

To obtain a *Yellowstone* injunction, a tenant first must commence a plenary action in the New York Supreme Court (because the Landlord-Tenant Courts lack jurisdiction to grant such

injunctive relief), seeking both declaratory and injunctive relief. At the same time (and before the cure period expires), tenant also must seek from the court both a Temporary Restraining Order (TRO) and a *Yellowstone* injunction.[5]

A tenant must satisfy the following well-established criteria for obtaining a *Yellowstone* injunction, specifically that tenant: (i) holds a commercial lease; (ii) has received a notice of default, a notice to cure or a threat of termination of the lease; (iii) has requested injunctive relief prior to the termination of the lease; and (iv) is prepared and has the ability to cure the alleged default by any means short of vacating the premises.[6]

Notably, because the standard for obtaining a *Yellowstone* injunction is far less onerous than the showing required for a regular preliminary injunction under Article 63 of the CPLR,[7] *Yellowstone* injunctions are granted routinely by courts to avoid lease forfeitures.[8]

What the *159 MP Corp.* Decision Means for Commercial Tenants and Landlords

In 159 MP Corp., tenants signed long-term leases for both retail space (a supermarket) and storage space. The riders to each of the leases expressly state that each tenant:

> [w]aives ~~its right to bring a declaratory judgmen~~t action with respect to any provision of this Lease or with respect to any notice sent pursuant to the provisions of this Lease. Any breach of this paragraph shall constitute a breach of substantial obligations of the tenancy, and shall be grounds for the immediate termination of this Lease. It is further agreed that in the event injunctive relief is sought by Tenant and such relief shall be denied, the Owner shall be entitled to recover the costs of opposing such an application, or action, including its attorney's fees actually incurred, it is the intention of the parties hereto that their disputes be adjudicated via summary proceedings (emphasis added).

Four years after entering into the leases, landlord served a ten-day notice to ~~cure, alleging various breaches of the leases. Tenants timely~~ commenced an action in the New York Supreme Court, seeking (among other relief) a declaration that the leases were in full force and effect and that no lease violations had occurred. Tenants also timely moved, by Order to Show Cause, for a *Yellowstone* injunction staying and tolling the cure period and enjoining landlord from terminating the leases or commencing a summary proceeding in Landlord-Tenant Court.[9] The Supreme Court denied tenants' motion for a *Yellowstone* injunction, holding that although the leases did not expressly prohibit tenants from seeking a *Yellowstone* injunction, such relief was nonetheless encompassed within the broader provisions of the "waiver" paragraph of the leases.

Significantly, the one issue that was not addressed by the Supreme Court (because it was not raised by the parties), but which the Second Department discussed at length in its 159 MP Corp. decision, is whether the "waiver" provision in these leases violated public policy.

The Court's Opinion

In a 3-1 decision, the Second Department affirmed the lower court's determination (in favor of the landlord), and held that the "waiver" provisions did not violate public policy in this instance, because the leases left tenants with the remedy of adjudicating disputes in summary proceedings in Landlord-Tenant Court. The Court's decision was based on the following four factors.

First, the decision cited the constitutional right of freedom to contract, and that parties may abandon or waive important rights, including certain rights under leases, such as waiving the right to a jury trial in nonpayment proceedings.

Second, the parties to these commercial leases were "sophisticated," and the leases were negotiated at "arm's-length."

Third, as the State Legislature did not enact any law or statute specifically prohibiting as void or unenforceable such waiver, the court, which is a not legislative body, should not create such blanket prohibition.

Fourth, and most importantly, this particular lease provision did not take away *all* of tenants' available legal remedies, as tenants still were free to perform under the lease, cure the alleged defaults and assert any defenses that they may have in a summary proceeding.

The Dissenting Opinion

The dissent's opinion is notable for its explanation and forceful defense of the "strategic remedy" that was implicitly created by the Court of Appeals' *Yellowstone* decision for commercial tenants to preserve their valuable leasehold interests when served with a notice to cure defaults that are in dispute.

In response to the majority's holding, the dissenting opinion argued that *Yellowstone* injunctions serve a valuable public policy role in relations between commercial landlords and tenants by providing a mechanism for a commercial tenant to protect its valuable property interest in the lease while challenging the landlord's assessment of its rights. The dissenting opinion further stated that a *Yellowstone* injunction also provides "a modicum of protection to landlords as well," since a court issuing a *Yellowstone* injunction may impose conditions to protect the landlord's interests during the pendency of the litigation, such as payment of rent or "use and occupancy" during the pendency of the action.[10]

The dissenting opinion also noted that without the remedy of a *Yellowstone* injunction, a tenant is left with no alternative but to wait until the landlord commences a summary proceeding in Landlord-Tenant Court, and then for the tenant to defend against landlord's

claims in that court. Thus, a tenant cannot preemptively protect its valuable leasehold interest by commencing a proceeding in Landlord-Tenant Court, because that court lacks the power to grant equitable relief, namely, injunctive relief to toll or stay the cure period and prevent landlord from terminating the lease or commencing a summary proceeding. Of course, a tenant may prevail in Landlord-Tenant Court, in which case, tenant would not require any equitable relief, but if the tenant loses, the tenant forfeits its lease. By contrast, "where the *Yellowstone* injunction is employed, if the tenant prevails he has no further need for a stay. If he loses, either he may cure the default during whatever part of the cure period remains, or the lease expires and he is subject to removal by summary proceedings" (internal quotation marks and brackets omitted).[11]

According to the dissenting opinion, the problem with the Court's holding and reasoning is that the waiver provision in this lease "fully divests the Supreme Court of jurisdiction to hear a declaratory judgment action brought by the plaintiffs," and that a "summary proceeding does not provide an adequate substitute for the important rights forfeited by the broad waiver at issue here." The dissenting opinion argues that because tenants have no legal standing to commence a summary proceeding to protect their rights, tenants would be left entirely dependent upon landlords commencing a summary proceeding in order to bring the issue of the validity of the notice to cure before a court. The dissenting opinion observes that a landlord may serve successive notices on a tenant, leaving tenant in a "metaphorical limbo," and without recourse to initiate judicial proceedings for a determination of tenant's rights."[12] According to the dissenting opinion, this is "precisely the type of 'uncertain or disputed' jural relation that a declaratory judgment action seeks to rectify."

In sum, the dissenting opinion found that this particular lease provision violates public policy, "because enforcement of the contractual waiver at issue in this action would deprive plaintiffs of any affirmative and meaningful means of accessing the court[.]"

Conclusion

Based on the 159 MP Corp. decision, it is expected that commercial landlords will be tempted to draft lease "waiver" provisions similar to the provision upheld in that case. Of course, tenants do not have to agree to such onerous terms, and they either can try to negotiate a better deal or simply walk away.

However, the 159 MP Corp. decision still may be challenged. As this is a case of first impression and because there is a possible conflict with precedent in the First Department,[13] the tenants may seek leave to reargue before the Second Department and/or seek leave to appeal to the Court of Appeals (there is no automatic right of appeal, as there was only one dissenting vote), or if the Second Department were to deny these motions, tenants may file a motion with the Court of Appeals for leave to appeal.

So, it may still be a while before it is truly the end of the *Yellowstone* brick road.

If you have any questions concerning *Yellowstone* injunctions or any other real estate-related litigation matters, please contact the following attorneys at our firm:

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[1] 21 N.Y.2d 630, 290 N.Y.S.2d 721 (1968).

[2] See Post v. 120 East End Ave. Corp., 62 N.Y.2d 19, 475 N.Y.S.2d 821 (1984); John Stuart, Div. of Robert Allen Fabrics v. D & D Assocs., 160 A.D.2d 547, 554 N.Y.S.2d 197 (1st Dep't 1990).

[3] See, e.g., Empire State Bldg. Assocs. v. Trump Empire State Partners, 245 A.D.2d 225, 667 N.Y.S.2d 31 (1st Dep't 1997); Mann Theatres Corp. v. Mid-Island Shopping Plaza Co., 94 A.D.2d 466, 464 N.Y.S.2d 793 (2d Dep't 1983), aff'd, 62 N.Y.2d 930, 479 N.Y.S.2d 213 (1984); Garland v. Titan West Assoc., 147 A.D.2d 304, 543 N.Y.S.2d 56 (1st Dep't 1989).

[4] See Graubard Mollen Horowitz Pomeranz & Shapiro v. 600 Third Ave. Assocs, 93 N.Y.2d 508, 693 N.Y.S.2d 91 (1999).

[5] As noted in a prior Client Alert, it also may be advisable to seek a regular preliminary injunction under Article 63 of the CPLR in the event that the court declines to grant a *Yellowstone* injunction for any reason.

[6] See, e.g., 225 E. 36th St. Garage Corp. v. 221 E. 36th Owners Corp., 211 A.D.2d 420, 421, 621 N.Y.S.2d 302, 303-304 (1st Dep't 1990); Graubard Mollen, *supra*.

[7] 225 E. 36th St. Garage, *supra*.

[8] See Post, 62 N.Y.2d at 25, 475 N.Y.S.2d at 823.

[9] The dissenting opinion notes that applications for a stay are made in conjunction with an action for a declaratory judgment. While it would be possible theoretically for a tenant to commence an action only for a *Yellowstone* injunction and a permanent injunction, tenant also requires a declaration that tenant has not defaulted under the lease, that landlord is not entitled to terminate the lease, and that the lease is valid and enforceable. Indeed, the Second Department held that because the "waiver" provision precludes the tenant from bringing a declaratory judgment action, it also precludes the tenant from seeking a *Yellowstone* injunction.

[10] Quoting Graubard Mollen, *supra*.

[11] Quoting Post, *supra.*

[12] Tenant also would be left without the remedy of seeking a stay of the cure period in the event that the time to cure the alleged lease default would take longer than the cure period provided in the lease or notice. For instance, in 159 MP Corp. the alleged defaults included tenants' failure to obtain permits and to permit an inspection of the premises by the Fire Department, which would be very difficult, if not impossible, to accomplish in the 15 days given in the cure notice.

[13] As noted in the dissenting opinion, previously lower courts in New York split on this issue and no appellate court until now had decided this particular issue. Thus, the Second Department's decision is now the law in New York State. However, as noted in a recent article that appeared in *Law360.com* (Schwartz, NY Decision Opens Door For Yellowstone Injunctions Waivers, Feb. 9, 2018), it appears that the Second Department's decision may be in conflict with precedents in the Appellate Division, First Department, which covers the Counties of New York and Bronx County. As discussed in the *Law360* article, in Village Center for Care v. Sligo Realty Service Corp., 95 A.D.3d 219, 222, 943 N.Y.S.2d 11 (1st Dep't 2012), the First Department stated that the New York "Court of Appeals has acknowledged that courts routinely grant *Yellowstone* relief to reflect this State's policy against forfeitures," citing that Court's decision in Post, *supra*.