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Using Consumer Protection Suits Against Real Estate Sellers

The New York Court of Appeals, in an opinion issued in November of 2001, has again expanded the potential liability for parties selling real estate. In *Polonetsky v. Better Homes Depot, Inc.*,¹ the Court held that New York City's Consumer Protection Law, which is designed to protect consumers from deceptive practices involving "goods and services," applies to a business offering services in connection with the sale of real estate. In reaching this conclusion, the Court of Appeals also signaled its approval of Appellate Division decisions that have applied the New York State consumer protection statute to real estate transactions. The *Polonetsky* decision continues the trend, in both case law and legislation, towards more possible exposure to liability for sellers of real estate in New York.

The *Polonetsky* case arose out of the sale of a number of homes in New York City by Better Homes Depot, Inc. (Better Homes). Better Homes is in the business of buying, repairing, and then reselling houses in New York City. Better Homes markets its services to prospective home buyers through newspapers and flyers. A number of consumers filed complaints with the City's Department of Consumer Affairs (DCA), alleging that Better Homes engaged in deceptive sales practices in marketing and selling houses. In *Polonetsky*, the DCA brought suit against Better Homes alleging violations of the New York City Consumer Protection Law.

The DCA asserted that Better Homes offered potential purchasers substandard properties at inflated prices while representing that their houses were priced "below market value" because they were acquired as the result of foreclosures. The DCA also claimed that Better Homes made promises to buyers regarding repairing houses but that the repairs were poorly done, were not completed, or were made without the necessary permits.

If a buyer expressed reluctance to go through with a sale because of the poor condition of a house, Better Homes allegedly threatened to retain the buyer's down payment. In addition, the DCA contended that Better Homes falsely represented to prospective buyers that their interests were being protected throughout the sales process and discouraged buyers from obtaining their own legal representation while encouraging buyers to



work with attorneys with whom Better Homes had ties. Indeed, Better Homes allegedly represented to prospective buyers that the attorneys and other contractors it recommended were approved by the Federal Housing Administration (FHA), when, in reality, the FHA does not "approve" attorneys or contractors. DCA concluded that this was all part of an attempt to falsely lead buyers to believe that the FHA was involved in the transactions and would protect the buyers or guarantee that they were satisfied.²

Homes and Consumer Goods

In its effort to enforce the City's laws against deceptive practices, the DCA argued that this pattern of conduct violated the City's Consumer Protection Law §20-700, which prohibits, inter alia, "any deceptive or unconscionable trade practice in the sale, lease, rental or loan ... of any consumer goods or services."³ Better Homes moved to dismiss the complaint, maintaining that §20-700 did not apply because homes were not "consumer goods or services" within the meaning of the provision. The Appellate Division, First Department, dismissed the complaint as to Better Homes, holding that the City's Consumer Protection Law did not apply to transactions involving the sale of real property.⁴

While the Court of Appeals had no trouble concluding that the alleged conduct, if proven, would constitute deceptive or unconscionable trade practices, the scope of the City's Consumer Protection Law was less clear. Better Homes argued, and the Court of Appeals agreed, that "the simple sale of a house does not involve consumer goods or services within the meaning of" the City's Consumer Protection Law.⁵ The Court of Appeals stated, however, that Better Homes provided more to its customers than merely facilitating the sale of homes — Better Homes "allegedly orchestrated a system of providing services under which prospective buyers were defrauded or misled every step along the way," including promoting overpriced homes, promising repairs, and falsely representing FHA involvement in the transactions.⁶

Noting that if Better Homes had offered those services without selling homes, its actions would have undoubtedly been subject to the City's Consumer Protection Law, the Court of Appeals refused "to insulate fraudulent conduct from the reach of the Code whenever the conduct occurs in connection with the sale or attempted sale of a house."⁷ The Court of Appeals therefore ultimately concluded that the City's Consumer Protection Law could be applied to Better Homes.

The 'Polonetsky' decision continues the trend, in both case law and legislation, towards more possible exposure to liability for sellers of real estate in New York.

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In reaching this conclusion, however, the Court of Appeals has also taken the position that New York's state consumer protection law, New York General Business Law §349(a), applies to real-estate transactions. Section 349(1) makes it unlawful to perform "deceptive acts or practices in the conduct of any business, trade or commerce or in the furnishing of any service in this state."⁸ The Court of Appeals has previously stated, in another context, that the state's consumer-protection provisions apply "to virtually all economic activity."⁹ But before *Polonetsky*, the Court of Appeals apparently never commented on the specific applicability of §349 to real-estate transactions.

While the issue whether §349 applies to real estate was not itself presented to the Court of Appeals, *Better Homes* argued that §349 did apply to real estate based on its broad language, in contrast to the narrow scope of the City's law. The Court of Appeals commented favorably on two earlier Appellate Division cases that have interpreted General Business Law §349 to cover real-estate transactions.¹⁰

In *Board of Managers of Bayberry Greens Condominium v. Bayberry Greens Assocs.*,¹¹ the Second Department permitted a party to assert a cause of action under General Business Law §349 in connection with alleged deceptive practices in the advertisement and sale of a condominium. In reaching that conclusion, the court did not cite any prior New York authority but apparently presumed that the consumer-protection law did apply.

In *Latiuk v. Faber Constr. Co.*,¹² the plaintiffs sued a builder under §349 for deceptive practices relating to the design and construction of their new home. In affirming the lower court's denial of summary judgment on the issue, the Fourth Department court also appears to have presumed that the state consumer-protection law did apply. While the Court of Appeals' favorable citation of these two cases is dicta, it does indicate that the Court of Appeals apparently agrees that state con-

sumer-protection laws do apply to real-estate transactions.

In *Polonetsky*, the Court of Appeals has given home buyers additional weapons, under both state and local law, to use against sellers. In particular, sellers who also offer or make recommendations regarding other services, such as repair work, mortgage banking, or legal representation, may find themselves liable under the City's Consumer Protection Law in addition to state law. And, while a simple sale of a home, in and of itself, will not invoke the City's law, the Court of Appeals has made it plain that such a sale may result in liability under state consumer-protection provisions.

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The decision, by expanding the scope of New York City's consumer-protection laws to include real-estate transactions that involve other covered services and accepting Appellate Division cases applying state consumer-protection laws to real estate transactions, continues the trend in New York towards more potential liabilities arising in the context of real-estate sales. By observing that the state consumer protection laws can be used by dissatisfied home buyers, the Court of Appeals has also continued the erosion of the caveat emptor doctrine as applied to home sales.

New York courts have traditionally adhered to the doctrine of caveat emptor and placed a duty on buyers to conduct a reasonable investigation in connection with the purchase of a property. Under the doctrine, if a buyer fails to conduct such an investigation, a buyer is generally barred from raising claims based on a seller's misrepresentations. The Court of Appeals previously recognized an implied,

common-law "Housing Merchant" warranty of habitability (now superseded by statute).¹³

Other exceptions to the doctrine have also been created, placing certain duties to disclose on sellers where defects in the property could not be discovered through a diligent inspection.¹⁴ The New York Legislature, late in the 2001 session, approved Senate Bill S05339, the "Property Condition Disclosure Act," that further erodes the caveat emptor doctrine in New York by requiring certain sellers of residential real estate to give prospective buyers a Property Condition Disclosure Statement stating all known defects relating to the property and the improvements, prior to the execution of a Contract of Sale.

The Court of Appeals' ruling in *Polonetsky* should also be considered as a warning to anyone involved in the sale of real estate. After *Polonetsky*, conducting a purportedly "simple" sale of real estate in New York creates significant exposure risks for the unwary. As the potential for liability continues to grow, it becomes increasingly important that all parties to a real estate transaction have independent, competent counsel involved to represent their interests, even before a Contract of Sale is prepared.

(1) 97 NY2d 46, 735 NYS2d 479 (2001).

(2) 97 NY2d at 51.

(3) Administrative Code of City of New York §20-700.

(4) *Polonetsky v. Better Homes Depot, Inc.*, 279 AD2d 418, 720 NYS2d 59 (1st Dept. 2001), rev'd, 97 NY2d 46, 735 NYS2d 479 (2001).

(5) 97 NY2d at 53.

(6) 97 NY2d at 53-54.

(7) 97 NY2d at 54.

(8) N.Y. Gen. Bus. Law §349(a).

(9) *Karlin v. IVF America, Inc.*, 93 NY2d 282, 290, 690 NYS2d 495 (1999).

(10) 97 NY2d at 53, citing *Latiuk v. Faber Constr. Co.*, 269 AD2d 820, 703 NYS2d 645 (4th Dept. 2000); *Board of Mgrs of Bayberry Greens Condominium v. Bayberry Greens Assocs.*, 174 AD2d 595, 571 NYS2d 496 (2d Dept. 1991).

(11) 174 AD2d 595, 571 NYS2d 496 (2d Dept. 1991).

(12) 269 AD2d 820, 703 NYS2d 645 (4th Dept. 2000).

(13) *Caceci v. Di Canio Construction Corp.*, 72 NY2d 52, 530 NYS2d 771 (N.Y. 1988). See *Fumarelli v. Marsam Development, Inc.*, 92 NY2d 298, 302, 680 NYS2d 440, 442 (N.Y. 1998) (holding statute imposing waivable, implied warranty supersedes common-law implied warranty recognized in *Caceci*).

(14) See, e.g., *Stambousky v. Ackley*, 169 AD2d 254, 572 NYS2d 672 (N.Y. App. Div., 1st Dept. 1991) (seller's failure to disclose that house was purportedly haunted by poltergeists is actionable).