NEW YORK COURT OF APPEALS ROUNDUP:

BUYER'S AGENT'S DUTIES, LIMITED LIABILITY COMPANY DERIVATIVE ACTIONS, AND DAMAGES FOR AIDS EXPOSURE

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This month we discuss three recent decisions of the Court of Appeals. One resolved an issue of interest to the real estate industry, namely the duties owed to a client by a buyer's agent, as opposed to a seller's agent. Another held that members of a limited liability company have standing to bring a derivative suit on behalf of the entity. The third held that there should be no bar in an "AIDS phobia" case to a plaintiff seeking compensation for emotional distress experienced beyond the six-month period after which, statistically, it would be very unlikely that a person testing HIV-negative had been infected by the virus.

We also note the Court's historic visit to the Bronx on April 17. Nearly 400 people gathered in the borough's recently opened Hall of Justice to observe the Court hold argument in five cases.

Buyer's Agent Duties

The Court had never addressed the nature and extent of the duties that a buyer's real estate agent owes his principal, and thus when resolution of a case before the Second Circuit turned on that issue, the Second Circuit certified a question to the Court of Appeals. The Court's unanimous decision in *Rivkin v. Century 21 Teran Realty LLC*, responding to the certified question, concluded that, like a seller's agent, a buyer's agent owes his client a duty of undivided loyalty and full disclosure. However, multiple agents from the same brokerage firm may represent different bidders who are competing against one another.

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The dispute arose out of the plaintiff's unsuccessful attempt to purchase property. Luborsky was an associate broker with the licensed real estate brokerage firm of Century 21 Teran Realty ("Teran"). He was acting as an agent to the plaintiff, Rivkin. Teran had no system in place for tracking whether its various agents were representing multiple bidders on the same property. Unbeknownst to Luborsky or to Dresser, a broker and co-owner of Tehran, they were both representing bidders on the same house. Rivkin submitted a bid of $75,000 and was prepared to raise his offer to the asking price of $100,000, but the sellers did not counteroffer before accepting the $100,000 bid by Dresser's clients.

Rivkin sued Teran, its co-owners, and Luborsky. He asserted numerous causes of action that were all dismissed by the District Court, but only his claim for breach of fiduciary duty was the subject of the certification by the Second Circuit.

Rivkin's argument relied in part upon Real Property Law § 443 and a form that Luborsky provided to Rivkin as required by law, "Disclosure Regarding Real Estate Agency Relationship." The form stated that a buyer's agent owes the buyer the fiduciary duties of, among other things, reasonable care and undivided loyalty. It also stated that "buyer's agent acts solely on behalf of the buyer," language that has since been deleted from the statute. Judge Susan Phillips Read's opinion for the Court explained that § 443 is a disclosure statute, designed to make consumers aware of the party on whose behalf an agent is acting in a transaction. Further, the disclosure from and statute's reference to fiduciary duty applies to an "agent," defined in the statute as a "person," unlike the term "real estate broker," defined in the statute as a person *or* a firm. Thus, § 443 cannot be read to prohibit a brokerage firm from representing multiple bidders on a piece of property.

The Court turned its analysis to defendants' common law duties. Due to the conflict of interest, a buyer's agent cannot act on behalf of more than one client bidding for the same property, absent disclosure and consent. That prohibition does not extend to a brokerage firm, however. The same risks from divided loyalty are not present when different agents from one firm represent competing bidders.

Moreover, a different rule would be incompatible with the "nature and fundamental requirements of the real estate marketplace in New York." Many brokerage firms in the state are very large, with hundreds of agents associated with them; buyers are well aware that others represented by the same brokerage firm may be bidding on property shown to them; and a buyer's agent cannot be expected to decline to a client's request to see a property listed with his firm. Simply put, the scramble for real estate in New York could not co-exist with a rule that restricted brokerage firms' agents in the manner that Rivkin advocated.

Derivative Suit

The single issue in *Tzolis v. Wolff* was whether a derivative suit could be brought by members of a limited liability company ("LLC") on behalf of the LLC.

The action was brought by several members owning 25% of the membership interests in Pennington Property Company LLC ("Pennington") against its controlling members, challenging two of the company's real estate transactions as unauthorized and void. Thereafter, on defendants' motion the Supreme Court dismissed the causes of action in the complaint concerning the transactions on the ground that the plaintiffs lacked standing to assert derivative claims on behalf of Pennington. The Appellate Division, First Department, unanimously reversed and reinstated the two derivative claims. The Court granted leave to appeal on a certified question and affirmed (4-3) in an opinion by Judge Robert S. Smith for the majority. Judge Susan Phillips Read provided the opinion on behalf of the dissenting Judges.

The majority began by stating that its opinion was based upon the "long-recognized importance of the derivative suit in corporate law," and the absence of evidence that when the Legislature passed the Limited Liability Company Law in 1994 it intended to abolish derivative suits by LLC members.

The opinion traced the origin of the derivative suit as part of the corporate law of New York as early as 1832. The Court noted the salutary effect of permitting shareholders to pursue those in control of a corporation who breach their fiduciary duty, comparing a derivative suit to an action brought against a faithless trustee of a trust, which the courts have been open to hear. The Court also pointed to the Legislature specifically providing for derivative suits in the Business Corporation Law, and later in the Partnership Law, but only after the validity of such suits had been recognized in the courts. It concluded that such suits should be available in the LLC context, as well.

Unlike the dissent, the majority found the legislative history "far too ambiguous" to infer an intent to eliminate derivative suits as to LLCs.

The dissent characterized the outcome of the appeal as "curious," and presented a broad array of reasons why, in its view, the majority was wrong. It provided, *inter alia*, an extraordinarily detailed tracing of the Legislature's actions over the course of several years in dealing with the issue of whether derivative suits could be brought by LLC members. It interpreted the Legislature's deletion of language authorizing derivative actions from a draft of the LLC legislation as evidence of a clear legislative intent that such suits should not lie. The dissent referenced the failure of the majority to cite a single case in which the Court had read into a statute a choice that the Legislature had rejected, stating that the Court had "never done such a thing."

The dissent also related the history of efforts in New York at various times to take steps to make the state a more hospitable business climate in order to be competitive with Delaware, including discouragement of derivative suits. Judge Read's opinion suggested that the majority's result was at odds with that objective.

It seems worth noting that LLCs under the law of New York have received significant benefits in terms of limited liability and tax treatment, and that expecting the

management of such entities to deal fairly with their members and be sued on behalf of the entity if they do not, places no undue burden on that method of doing business. If the Legislature wishes to change what the majority has done here, it has certainly been shown the way.

AIDS Phobia/Time Limits

The issue in *Ornstein v. New York City Health and Hosp. Corp*. was whether the plaintiff had a viable claim for damages for the emotional injury she allegedly suffered in the period more than six-months after her negligent exposure to the HIV, the virus that causes AIDS. A unanimous Court, in an opinion by Judge Victoria A. Graffeo, reversed the judgment entered after trial and the interim order of the Appellate Division, First Department, dismissing the plaintiff's claim for such damages. The Court of Appeals remitted the case for trial solely on that issue.

Plaintiff was a nurse at Bellevue Hospital, working in the emergency ward and providing care to a critically ill patient suffering from AIDS. While she was bathing the patient, her thumb was punctured by a needle that allegedly had been left in the bed by an intern. She immediately received treatment that continued for several months and commenced regular HIV-antibody testing that continued over the course of two years. The tests were all negative.

Within a year of her exposure, plaintiff sued the hospital and the intern, seeking damages for emotional injuries, including "AIDS phobia," post-traumatic stress disorder and recurrent depression. The defendants, while not challenging plaintiff's exposure to the virus, moved pursuant to CPLR 3211(a)(7) to dismiss any claim by plaintiff for such damages sustained by her more than six months after the incident. Defendants relied principally upon an opinion of the Appellate Division, Second Department in *Brown v. New York City Health and Hosp. Corp.*, 225 A.D.2d 36 (1996), which concluded that damages for AIDS phobia become unreasonable as a matter of law more than six months after exposure.

Plaintiff, admittedly to avoid *Brown* and similar rulings issued by the Second Department, took the position that her claim was not subject to the asserted reasonableness limitation of six months for AIDS phobia cases, but instead was a "plain vanilla" claim for negligent infliction of emotional distress suffered by her long after the six-month period. The trial court restricted plaintiff's proof of damages to the six-month period, however, and the jury awarded plaintiff $333,000 for past pain and suffering and $15,000 for past loss of wages.

On appeal, the First Department saw plaintiff's claim as an "end run around the six-month AIDS phobia restriction on emotional damages." It dismissed the claim for damages beyond that limited period on the basis of statistical improbability – plaintiff's failure to test positive for antibodies within the first six months of exposure made it "highly unlikely" that plaintiff had been infected with HIV. The well-reasoned dissent in the Appellate Division saw the *Brown* precedent as a departure from common-law principles of tort liability, which should

lie only with the Legislature.

The Court noted that there was no challenge to the genuiness of plaintiff's claim and, therefore, to her right to a jury trial. In reviewing (but expressing no view as to the correctness of) the *Brown* decision, the Court saw the imposition of the six-month limitation on damages in that case as a compromise largely arrived at by the court because the plaintiff there had refused to submit to meaningful testing to establish her HIV status, while nonetheless seeking damages for a fifteen-year period after she had been exposed (again through a needle).

In the end, the Court concluded that reliance upon statistics was an inappropriate basis for restricting recovery of emotional distress damages for all plaintiffs as a matter of law. In addition, limiting damages based upon statistics for HIV testing does not deal with injuries a plaintiff may suffer after exposure that are distinct from the fear of contracting AIDS. If proof of such injuries is accepted by a jury, as the Court observed, that may justify an award of damages.

Finally, the Court rejected application of "public policy" considerations to support the fixing of a time limit for emotional distress damages in cases involving possible exposure to the AIDS virus, and concluded that – as they do any other tort case – trial judges and the Appellate Division can deal with verdicts and judgments that may deviate from what is reasonable compensation.