NEW YORK COURT OF APPEALS ROUNDUP

IMPROPER SOLICITATION, POST-RELEASE SUPERVISION, STABILIZED RENT INCREASES

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This month we discuss a decision arising out of the sale of a business in which the Court of Appeals provided some guidance on what constitutes improper solicitation by the seller of its former clients. We also discuss a decision resolving six cases in which the sentencing court failed to impose post-release supervision during the initial sentencing hearing. Lastly, we discuss a decision in which the Court considered whether the New York City Rent Guidelines Board has the authority to promulgate orders allowing different rent increases for apartments based upon whether there had been a recent vacancy.

Improper Solicitation

Under New York common law there is an implied covenant by a seller "to refrain from soliciting former customers, which arises upon the sale of the 'goodwill' of an established business." *Mohawk Maintenance Co. v. Kessler*, 52 N.Y.2d 276, 283 (1981). In the absence of a more restrictive express covenant, the seller of a business is free to compete with the purchaser and even continue to do business with his former customers as long as he does not "actively solicit" their business. Last month in *Bessemer Trust Company, N.A. v. Branin*, the Court provided some guidance on the interpretation of "active" solicitation.

Plaintiff Bessemer Trust Company, N.A. is a wealth management and investment advisory firm. It purchased the assets of investment management firm Brundage, Story & Rose LLC (the seller), including seller's client accounts and related goodwill. The

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purchase agreement imposed no express restrictive covenants on seller's principals. Defendant Francis Branin had been a principal at seller, received significant compensation for the sale of his interest in the company, and worked for Bessemer Trust after the sale. Less than two years later, Mr. Branin left that job and took a position with Stein Roe Investment Counsel LLC, another wealth management firm.

Mr. Branin did not notify his Bessemer clients about his move to Stein Roe. He also followed Bessemer Trust's directives in transitioning his accounts to other investment advisors at that firm before he left. But after he joined Stein Roe, Mr. Branin was contacted by his largest client at Bessemer Trust, the Palmer Family. Mr. Branin told Palmer that he joined Stein Roe, and on advice of counsel he was not to solicit his Bessemer Trust clients. Palmer requested a meeting with Stein Roe. Mr. Branin attended strategy sessions to develop a plan for the presentation to Palmer, shared general background information about the client, and attended Stein Roe's pitch meeting, but played an essentially passive role in the meeting. Afterwards, Palmer moved its accounts to Stein Roe.

Bessemer sued Mr. Branin in federal District Court for breach of loyalty, and Mr. Branin was found liable. On appeal, the U.S. Court of Appeals for the Second Circuit took advantage of the certification procedure to ask the Court of Appeals for guidance in determining what actions constitute improper solicitation of a former client by the seller of the goodwill of a business in the absence of an express restrictive covenant.

In a unanimous opinion authored by Judge Carmen Beauchamp Ciparick, the Court noted that there was no hard-and-fast rule in determining whether solicitation was improper, and it declined to create one. Instead, the Court said, the trier of fact must consider the principles underlying the rule in *Mohawk* and the specifics of the particular industry involved to determine what conduct may impair the goodwill sold.

The Court did provide several illustrative examples of what would constitute improper solicitation, including a seller who initiates contact or takes affirmative steps to directly communicate with former customers or clients, such as sending targeted mailings or making individualized telephone calls. If a former client contacts a seller, the seller is not free to disparage the purchaser or to explain why he believes his products or services are superior to those of the purchaser.

Conversely, the Court described what a seller may do without violating the implied covenant. A seller of goodwill is permitted to compete with the purchaser and even accept the trade of former customers, absent an express covenant to the contrary. A

seller is also permitted to advertise to the public as long as the advertisement is general in nature, and not specifically aimed at the seller's former customers. If a former client contacts a seller, the seller may respond to factual inquiries if the response does not go beyond the scope of the information sought. And when contacted by a former client such as occurred here, a seller may assist his new employer in responding to inquiries, including by conveying information that is not proprietary to the purchaser of the goodwill, aid his new employer in preparing for a pitch meeting requested by a former client and be present at such a meeting, limiting his role to providing factual information in response to questions.

In the financial services industry, the Court noted, clients will conduct due diligence and seek factual information regarding investment strategy, resources, personnel and fee structure, and given the competitive nature and complexity of the sector, these types of questions are expected and appropriate. In this context, appropriate topics for a seller to discuss with his new employer include his former client's investment preferences, financial goals and tolerance of risk.

Now that the Court has answered the certified question and provided guidance on this aspect of New York common law, the Second Circuit will decide the appeal.

Post-Release Supervision

In *People v. Lingle*, and five other cases involving similar legal issues, the Court analyzed a defendant's statutory obligation to serve post-release supervision (PRS). Although the facts in the six cases varied, they shared two features: (1) the judges who sentenced the defendants did not pronounce PRS at the initial sentencing, and (2) the defendants were resentenced to PRS before completion of their originally imposed sentences of imprisonment. The Court held that, under these circumstances, each defendant's resentencing to PRS was proper.

In *People v. Sparber*, 10 N.Y.3d 457 (2008), the Court held that defendants subject to PRS have a statutory right to have a judge pronounce the PRS sentence in their presence in open court, and that the remedy when a judge neglects to do so is resentencing to correct the "*Sparber* error." The defendants in *Lingle* and the other cases decided with it sought upon resentencing to be relieved of their statutory obligation to serve PRS on grounds of double jeopardy and/or due process. Certain defendants also claimed that at resentencing a court has discretion to reconsider the propriety of the incarceratory component of a sentence, in addition to the PRS component. Additionally, certain

defendants contended that the Appellate Division possesses plenary power to modify a sentence after resentencing in the interest of justice.

In an opinion authored by Judge Susan Phillips Read, the Court rejected each of these arguments, affirmed the orders of the First and Second departments of the Appellate Division in *Lingle* and four of the other cases, and in *People v. Sharlow*, reversed the Second Department and ordered that the resentence imposed by the Supreme Court be reinstated.

In *People v. Williams*, 14 N.Y.3d 198 (2010), the Court held that defendants "are presumed to be aware that a determinate prison sentence without a term of PRS is illegal," and therefore "cannot claim a legitimate expectation that the originally-imposed, improper sentence is final for all purposes." Judge Read emphasized that under *Williams*, an expectation of finality arises for purposes of double jeopardy only when a defendant completes the lawful portion of an illegal sentence.

Because the defendants in the six cases before the Court had not completed their originally imposed sentences when they were resentenced to add PRS, the Court held that they could not claim a reasonable expectation of finality and therefore no double jeopardy violation had occurred. Judge Read stressed that defendants' proposed rule, under which resentencing to PRS should be precluded when a "significant" or "substantial" portion of the originally imposed sentence of imprisonment had been served, "supplies no meaningful standard by which to measure a reasonable expectation of finality."

With respect to the due process claim, the Court noted that "PRS is statutorily mandated, and defendants are charged with knowledge of the law." Indeed, the defendants did not contend that they were actually unaware that PRS would be a component of their sentences. Thus, the majority reasoned, the defendants likely knew that they were subject to PRS well before efforts to resentence them were undertaken. Accordingly, the substantive due process argument was rejected.

The majority also rejected defendants' contention that *Sparber* empowers judges to revisit the propriety of a defendant's sentence as a whole—including the incarceratory component—when resentencing to correct a *Sparber* error. Judge Read explained that *Sparber* cannot be reasonably read to suggest that at a resentencing hearing the judge should do anything other than correct a discrete error. Such a hearing is not a plenary proceeding. And because a trial court lacks discretion to reconsider the incarceratory

component of a defendant's sentence at a *Sparber* resentencing, the Appellate Division is not authorized to lessen the prison sentence on appeal in the interest of justice.

Judge Ciparick joined the majority in four of the six cases, yet dissented in *People v. Sharlow* and *People v. Rodriguez*. Chief Judge Jonathan Lippman and Judge Theodore T. Jones joined Judge Ciparick's dissent. In *Sharlow*, the Department of Correctional Services had conditionally released the defendant after he served a substantial portion of his term of imprisonment before the Supreme Court resentenced him by adding five years of PRS to the original term of imprisonment. Judge Ciparick argued that the Double Jeopardy clause bars resentencing once a defendant has been released from confinement under the Court's holding in *Williams*.

With respect to *Rodriguez*, the dissenting judges disagreed that *Sparber* does not authorize a resentencing court to revisit the incarceratory component of a sentence, and therefore agreed with the defendant that the Appellate Division may consider whether the sentence imposed by the lower court at resentencing was unduly "harsh or excessive" in its "interest of justice discretion." The dissent contended that the "Appellate Division's authority to modify a judgment of resentence is not limited to a resentencing where it has been established that an 'error or defect' has occurred."

Stabilized Rent Increases

In the *Matter of Mercedes Casado v. Marvin Markus*, the Court held that the New York City Rent Guidelines Board (RGB) had the authority to promulgate orders allowing larger rent increases for low-rent apartments where there has been no recent vacancy than for apartments where there has been a fairly recent vacancy. At issue were two RGB orders concerning the rent increases permitted in renewal leases. These orders distinguished between apartments for which there had not been a vacancy lease executed for six or more years and those for which there had been. For the former category, the percentage increase was subject to a dollar floor, allowing a greater increase in percentage terms as compared to the latter category.

Two rent-stabilized tenants and a tenants' rights organization initiated Article 78 proceedings challenging the orders. The Supreme Court for New York County held that the orders exceeded RGB's authority, and the Appellate Division, First Department, affirmed. In a 5-2 decision authored by Judge Robert S. Smith, the Court reversed.

The Court found that the purpose of RGB's orders was to "remedy what it saw as an inequity" with respect to apartments that had not had a recent vacancy. The permissible

rent increase for a rent-stabilized apartment depends on historic rents, with modest annual increases authorized by RGB, and larger increases when the apartment becomes vacant. The annual rent increases do not typically keep pace with increases in maintenance costs for services provided to the tenant. This discrepancy between rents and maintenance costs is more acute when the apartment has not been vacated—and therefore not had a vacancy rent increase—for a number of years. In order to cover the maintenance costs in excess of rent payments, "tenants paying higher rents must subsidize those paying lower rents." To address this inequity, RGB authorized minimum dollar increases upon lease renewals for rent-stabilized apartments where the rent was less than $1,000 and the tenancy greater than six years.

The Court held that RGB did not exceed its authority under NYC Administrative Code §26.510 (b), which is part of the Rent Stabilization Law (RSL) and authorizes RGB to "establish annually guidelines for rent adjustments," and to file annually "a statement of the maximum rates of rent adjustments, if any, for one or more classes of accommodations." The Court found that on its face the RSL does not prohibit RGB from distinguishing between types of apartments within classes, including distinctions based on length of tenancy, in order to set increases. Moreover, the Court found, RGB has traditionally made distinctions within classes of accommodations in setting increases, for example, distinguishing apartments for which the landlord provides heat from those for which the landlord does not.

Finally, the Court found unpersuasive petitioners' argument that the Legislature had addressed the same problems that RGB was attempting to remedy by the Rent Regulation Reform Act of 1997, which amended the RSL to provide a vacancy increase up to 20 percent, and even greater increases where there had not been a previous vacancy within eight years. The Court found that there was no conflict between the legislation and RGB orders because, even if both forms of relief provided to landlords were "cumulative" they "are not logically inconsistent." Moreover, the legislation was not so detailed and comprehensive to imply the Legislature had preempted the field.

The dissent, authored by Judge Ciparick and joined in by Judge Jones, found that RGB's orders contravene the will of the Legislature, and exceeded the authority of the agency. In the dissent's view, RGB was attempting to rectify an inequality that was deliberately created by the Legislature. The inequality between long-term and short-term tenant rent increases is due to the Rent Regulation Reform Act of 1997, which provided that apartments with greater turnover and more recent tenants would be charged higher rents than those apartments with longer tenancies.

The Legislature's purpose in adopting this scheme was to bring apartments closer to market rent as they became vacated, but, critically, the Legislature did not couple the vacancy increases permitted for new tenants with any change to the calculation of rent increases for current tenants. It was therefore by legislative design that new tenants paying higher rents provided by vacancy increases subsidize long-term tenants paying lower rents. The dissent argued that RGB usurped the Legislature's powers by creating separate increases based on what it perceived to be an inherent structural inequity in the rent laws.