...AR/RECOVERY OF EARNEST MONEY DEPOSIT

Uzan v. 845 UN Limited Partnership 10 A.D.3d 230 (N.Y.App.Div. 2004)

MAZZARELLI, Judge. This appeal presents the issue of whether plaintiffs, who defaulted on the purchase of four luxury condominium units, have forfeited their 25% down payments as a matter of law. Because the governing purchase agreements were a product of lengthy negotiation between parties of equal Bargaining power, all represented by counsel, there was no evidence of overreaching, and upon consideration of the fact that a 25% down payment is common usage in the new construction luxury condominium market in New York City, we hold that upon their default and failure to cure, plaintiffs forfeited all rights to their deposits pursuant to the rule set forth in *Maxton Builders, Inc. v. Lo Galbo.*

FACTS

In October 1998, Defendant 845 UN Limited Partnership (sponsor or 845 UN) began to sell apartments at The Trump World Tower (Trump World), a luxury condominium building to be constructed at 845 United Nations Plaza. Donald Trump is the managing general partner of the sponsor. Plaintiffs Cem Uzan and Hakan Uzan, two brothers, are Turkish billionaires who sought to purchase multiple units in the building.

In April 1999, plaintiffs and an associate executed seven purchase agreements for apartments in Trump World. Only four of those units (the penthouse units) are the subject of this lawsuit and appeal. As relevant, Cem Uzan defaulted on contracts to buy two penthouse units on the 90th floor of the building, and Hakan defaulted on contracts to purchase two other penthouse units on the 89th floor.

The building had not been constructed when plaintiffs executed their purchase agreements. In paragraph 17.4 of those contracts, the sponsor projected that the first closing in the building would occur on or about April 1, 2001, nearly two years after the signing of the agreements.

The condominium offering plan included a section titled "Special Risks to be Considered by Purchasers," which stated:

> *Purchasers will be required to make a down payment upon execution of a Purchase Agreement in an amount equal to 10% of the purchase price, and within 180 days after receipt of the executed Purchase Agreement from Sponsor or 15 days after Purchaser receives a written notice or amendment to the Plan declaring the Plan effective, whichever is earlier, an additional down payment equal to 15% of the purchase price ...*

Once construction was completed, the building's offering plan was amended to require a 15% down payment. Notably, both the original and the amended offering plans prominently disclosed the sponsor's right to retain the *entire down payment* should there be an uncured default.

NEGOTIATIONS PRECEDING EXECUTION OF THE PURCHASE AGREEMENTS

Plaintiffs were represented by experienced local counsel during the two-month-long negotiation for the purchase of the apartments. There were numerous telephone conversations between counsel, and at least four extensively marked-up copies of draft purchase agreements were exchanged. In consideration for plaintiffs' purchase of multiple units, the sponsor reduced the aggregate purchase price of the penthouse units by more than $7 million from the list price in the offering plan for a total cost of approximately $32 million. Plaintiffs also negotiated a number of revisions to the standard purchase agreement, including extensions of time for payment of the down payment. As amended, each purchase agreement obligated plaintiffs to make a 25% down payment: 10% at contract, an additional 7 1/2% down payment twelve months later, and a final

7 1/2% down payment 18 months after the execution of the contract. At no time did plaintiffs object to the total amount required as a nonrefundable down payment.

* * *

The executed purchase agreements provide, at paragraph 12(b), that:

> *[u]pon the occurrence of an Event of Default ... [i]f Sponsor elects to cancel ... [and i]f the default is not cured within ... thirty (30) days, then this Agreement shall be deemed canceled, and Sponsor shall have the right to retain, as and for liquidated damages, the Down payment and any interest earned on the Down payment.*

Plaintiffs paid the first 10% down payment installment for the penthouse units on April 26, 1999 when they signed the purchase agreements. They paid the second 7 1/2% installment in April 2000, and the third 7 1/2% installment in October 2000. The total 25% down payment of approximately $8 million was placed in an escrow account.

DEFAULT, FAILURE TO CURE, AND THIS ACTION

On September 11, 2001, terrorists attacked New York City by flying two planes into the World Trade Center, the city's two tallest buildings, murdering thousands of people. Plaintiffs, asserting concerns of future terrorist attacks, failed to appear at the October 19, 2001 closing, resulting in their default. By letter dated October 19, 2001, plaintiffs' counsel stated:

> *[W]e believe that our clients are entitled to rescind their Purchase Agreements in view of the terrorist attack which occurred on September 11 and has not abated. In particular, our clients are concerned that the top floors in a "trophy" building, described as the tallest residential building in the world, will be an attractive terrorist target. The situation is further aggravated by the fact that the building bears the name of Donald Trump, perhaps the most widely known symbol of American capitalism. Finally, the United Nations complex brings even more attention to this location.*

That day 845 UN sent plaintiffs default letters, notifying them that they had 30 days to cure. On November 19, 2001, upon expiration of the cure period, the sponsor terminated the four purchase agreements.

Plaintiffs then brought this action. They alleged that Donald Trump had prior special knowledge that certain tall buildings, such as Trump World, were potential targets for terrorists. Plaintiffs also alleged that Trump World did not have adequate protection for the residents of the upper floors of the building. In their first cause of action, plaintiffs averred that the sponsor's failure to advise prospective purchasers of the specific risks of a terrorist attack on Trump World, and to amend the offering plan to describe these risks, constituted common-law fraud and deceptive sales practices pursuant to General Business Law §352. Plaintiffs' second claim is that the same acts constituted violations of General Business Law §§349 and 350. The third cause of action sought a declaratory judgment that the down payment was an "unconscionable, illegal and unenforceable penalty." The IAS court dismissed plaintiffs' first two claims in a March 2000 order not on appeal.

MOTIONS FOR SUMMARY JUDGMENT

After exchanging discovery and conducting various depositions, plaintiffs moved for summary judgment on their third cause of action, arguing that forfeiture of the down payments was an unenforceable penalty. In support of their motion, plaintiffs submitted an attorney's affirmation to which were annexed: the pleadings, correspondence between counsel, the IAS court's order denying dismissal of the declaratory judgment cause of action, and certain news articles and promotional materials about the Trump World Tower.

Defendant opposed the motion and cross-moved for summary judgment, asserting that defaulting vendees on real estate contracts may not recover their down payments.

* * *

THE ROLE OF THE 25% DOWN PAYMENT

In his affidavit in support of the cross motion, Donald Trump stated that he sought 25% down payments from pre-construction purchasers at the Trump World Tower because of the substantial length of time between contract signing and closing, during which period the sponsor had to keep the units off the market, and because of the obvious associated risks. Trump also affirmed that down payments in the range of 20% to 25% are standard practice in the new construction luxury condominium submarket in New York City. He cited three projects where he was the developer, The Trump Palace, 610 Park Avenue

and Trump International Hotel and Tower, all of which had similar down payment provisions. Trump also noted that,

[i]n new construction condominium projects, purchasers often speculate on the market by putting down initial down payments of 10% and 15% and watching how the market moves. If the market value increases, they will then make the second down payment. If the market prices drop, they may then walk away from their down payment.

* * *

Defendant also presented a compilation of sixteen recent condominium offering plans, all of which required down payments of either 20% or 25% of the purchase price for the unit. Fourteen of the sixteen offering plans required 25% down payments. Further, defendant provided proof that in July 2001, plaintiff Cem Uzan closed on the purchase of an apartment on the 80th floor of Trump World after making a 25% down payment, and that he had previously purchased another apartment at 515 Park Avenue, also with a 25% down payment provision.

THE ORDER APPEALED

After hearing oral argument on the motion, the IAS court granted defendant partial summary judgment, finding that plaintiffs forfeited the portion of their down payment amounting to 10 of the purchase price, pursuant to *Maxton Builders, Inc. v. Lo Galbo.* The court held that the remainder of the down payment was subject to a liquidated damages analysis to determine whether it bore a reasonable relation to the sponsor's actual or probable loss. Defendant appeals from that portion of the order which denied it full relief.

DISCUSSION

More than a century ago, the Court of Appeals, in *Lawrence v. Miller,* held that a vendee who defaults on a real estate contract without lawful excuse cannot recover his or her down payment. It reaffirmed this holding in *Maxton, supra,* again in 1986. The facts of *Lawrence are* common to real estate transactions, and parallel those presented here. In that case, plaintiff made a $2000 down payment on the purchase of certain real estate, and then defaulted. The seller refused to extend plaintiff's time to perform the contract, retained the down payment, and ultimately sold the property to another purchaser. In plaintiff's subsequent action for a refund of the down payment, the Court of Appeals affirmed a judgment dismissing the complaint, stating:

> *To allow a recovery of this money would be to sustain an action by a party on his own breach of his own contract, which the law does not allow. When we once declare in this case that the vendor has done all that the law asks of him, we also declare that the vendee has not so done on his part. And then to maintain this action would be to declare that a party may violate his agreement, and make an infraction of it by himself a cause of action. That would be ill doctrine.*

For over a century, courts have consistently upheld what was called the *Lawrence* rule and recognized a distinction between real estate deposits and general liquidated damages clauses. Liquidated damages clauses have traditionally been subject to judicial oversight to confirm that the stipulated damages bear a reasonable proportion to the probable loss caused by the breach. By contrast, real estate down payments have been subject to limited supervision. They have only been refunded upon a showing of disparity of bargaining power between the parties, duress, fraud, illegality or mutual mistake.

In *Maxton,* plaintiff had contracted to sell defendants a house, and accepted a check for a 10% down payment. When defendants canceled the contract and placed a stop payment on the check, plaintiff sued for the down payment, citing the *Lawrence* rule. Defendants argued that plaintiff's recovery should be limited to its actual damages. In ruling for the vendor, the Court of Appeals identified two legal principles as flowing from *Lawrence.* First, that the vendor was entitled to retain the down payment in a real estate contract, without reference to his actual damages. Second, the "parent" rule, upon which the first rule was based, that one who breaches a contract may not recover the value of his part performance.

The Court noted that the parent rule had been substantially undermined in the 100 years since *Lawrence.* Many courts had rejected the parent rule because of criticism that it produced a forfeiture "and the amount of the forfeiture increases as performance proceeds, so that the penalty grows larger as the breach grows smaller."

The Court also noted that since *Lawrence,* the rule of allowing recovery of down payments of not more than 10% in real estate contracts continues to be followed by a "majority of jurisdictions," including in New York. Thereafter, the court noted the long and widespread reliance on the *Lawrence* rule in real estate

transactions, and it concluded that, based upon notions of efficiency and avoiding unnecessary litigation, the rule should remain in effect.

After acknowledging that "[R]eal estate contracts are probably the best examples of arms length transactions," the Court broadly concluded:

> *Except in cases where there is a real risk of overreaching, there should be no need for the courts to relieve the parties of the consequences of their contract. If the parties are dissatisfied with the rule of [Lawrence], the time to say so is at the bargaining table.*

The *Maxton/Lawrence* rule has since been followed by this Court as well as the other departments to deny a refund of a down payment when a default has occurred.

* * *

Applying the reasoning of these cases to the facts of the instant matter, it is clear that plaintiffs are not entitled to a return of any portion of their down payment. Here the 25% down payment was a specifically negotiated element of the contracts. There is no question that this was an arm's length transaction. The parties were sophisticated business people, represented by counsel, who spent two months at the bargaining table before executing the amended purchase agreements.

Further, the record evidences that it is customary in the pre-construction luxury condominium industry for parties to price the risk of default at 25% of the purchase price. The purchase agreements included a detailed nonrefundable down payment clause to which plaintiffs' counsel had negotiated a specific amendment. That amendment allowed for the payment of 25% of the purchase price in three installments: 10% at contract, an additional 7 1/2% twelve months later, and a final 7 1/2% eighteen months later. Clearly, plaintiffs were fully aware of and accepted the requirement of a non-refundable 25% down payment for these luxury pre-construction condominiums. In fact, Cem Uzan has purchased two other condominiums, one in the same building, with similar down payment provisions.

Plaintiffs negotiated the payment of the 25% down payments in installments to spread their risk over time. In the event of a severe economic downturn, plaintiffs were free to cancel the deal, capping their losses at the amount paid as of the date of their default. For the sponsor, the 25% deposit served to cover its risk for keeping the apartments off the market should the purchaser default.

Finally, there was no evidence of a disparity of bargaining power, or of duress, fraud, illegality or mutual mistake by the parties in drafting the down payment clause of the purchase agreements. The detailed provision concerning the non-refundable deposit was integral to the transaction. If plaintiffs were dissatisfied with the 25% non-refundable down payment provision in the purchase agreements, the time to have voiced objection was at the bargaining table. Because they chose to accept it, they are committed to its terms. Thus, upon plaintiffs' default and failure to cure, defendant was entitled to retain the full 25% down payments.

Accordingly, the order of the Supreme Court, New York County (Alice Schlesinger, J.), entered July 21, 2003, which, to the extent appealed from, denied defendant 845 UN Limited Partnership's motion for summary judgment, should be reversed, on the law, with costs, defendant's motion granted and the complaint dismissed. The Clerk is directed to enter judgment in favor of defendant-appellant dismissing the complaint as against it.

RESCISSION DUE TO FEAR/RECOVERY OF EARNEST MONEY DEPOSIT

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