

The Role of a Co-op Board

Some background: co-ops are generally established by a sponsor which files an offering plan with the Attorney General's office and then sells co-op shares to the public. A co-op board of directors is elected by the co-op's shareholders, according to its bylaws. In the early phase of a co-op, the sponsor usually owns most of the shares and thus controls the board of directors. In most cases, the Attorney General requires sponsors to give up their control of the board after they sell over fifty percent of the shares, or after five years have passed since the closing, whichever comes first.

A board of directors in a cooperative has two basic, legal obligations:

- It must exercise prudent business judgment in making decisions, just like any other corporate board.
- It must follow the co-op's internal rules (as set forth in the by-laws, the proprietary lease, the certificate of incorporation and the house rules).

By-laws, Leases, House Rules

Copies of the original by-laws and proprietary lease (plus house rules, if any) can be found in the offering plan that was distributed when the building was first converted. It is possible that the offering plan is not current and might not contain an updated version of the co-op's documents, especially if it has been several years since the co-op was formed.

If you do not have a copy of these documents, the board of directors, your managing agent, or another shareholder may provide you with them. The by-laws and proprietary lease will set forth crucial terms, including:

- The timing, conduct and notice of annual shareholder meetings and elections to the board.
- How many seats the sponsor can have on the board of directors and when the sponsor must give up control.
- The ability of shareholders to call special meetings.
- The procedure for amending the by-laws.
- The quorum for voting and whether cumulative voting is allowed.
- Sublet provisions.

Legal Restrictions: Business Corporation Law

The Business Corporation Law (BCL) is the main New York State law which governs how most co-ops must operate, with court decisions providing the case law which interprets the statute.

You can find this law online at <http://public.leginfo.state.ny.us>.

Some important provisions of the BCL and the sections in which they are found include:

- Annual meeting of shareholders to elect directors is held (Section 602(b)).
- "Proxy" voting by absent shareholders (Section 609).
- Appointing an election inspector on request (Section 610).
- Ability of shareholders to examine or review minutes of shareholder meetings, record of shareholders, and annual balance sheet and profit and loss statement (Section 624).
- Removal of a director for cause (that is, a good reason), or without cause, if stated in the certificate of incorporation or by-laws (Section 706).
- Right of shareholders to receive an annual report disclosing contracts (Section 713). Each shareholder is entitled to receive an annual report disclosing any contract or transaction entered into or voted on by the board wherein a director was an interested party. If there are no such contracts or transactions, the board must still send shareholders a document executed by all of the directors affirming there were no such contracts or actions taken by the board. Prospective purchasers are encouraged to examine this annual report prior to entering into an agreement of sale.
- Ability of shareholders to sue directors and officers for misconduct (Section 720).

If the Board is Not Complying with Bylaws

There are a couple things to keep in mind when approaching the board about noncompliance with the bylaws, proprietary lease or law. First, remember that board members are usually your neighbors who may or may not be fully trained in what is required by the rules and law. A shareholder should tactfully point out a lack of compliance to the board, expressing the expectation that the matter will be corrected. Sometimes that is all that is needed to solve a problem. Second, know that the board must act as a body; individual members cannot speak or act on behalf of the whole.

Put It in Writing

If the board does not respond to an oral request, write a letter. Make it concise, factual and not hostile. Keep copies of any letter or other paperwork you send and notes of telephone conversations (date, time, who called whom, and the gist of the conversation) in case the matter is not quickly resolved.

Strength in Numbers

An attempt to influence the board is always more persuasive if it is presented by a significant number of shareholders. If your problem is one that will affect others, it is worth organizing the other shareholders. If you do, and the attempt to change the situation is not successful, the organized group can always seek to elect new directors at the next annual meeting.

Hiring a Lawyer

In serious situations in which a board remains unresponsive, shareholders may consider retaining a private attorney. Here are some things to keep in mind:

- Look for someone with experience in handling co-op shareholders' problems. Ask others for recommendations, or you may contact a local bar association for referrals.
- Some lawyers will charge a minimal or no fee for an initial consultation.
- Most lawyers will attempt to resolve any matter through negotiation before considering litigation, since litigation is costly and usually lengthy. It can also be very unpleasant to litigate against one's neighbors.

Important note: Keep in mind that if the board is not addressing serious problems, such as a bank threatening to foreclose on an underlying mortgage or a sponsor's failing to pay maintenance on unsold shares, it is important to act swiftly. Often such problems can be resolved, if shareholders organize and act right away.

The Role of the Attorney General

The Attorney General's office regulates the offer and sale of real estate securities (which includes shares in co-ops) by the sponsor. If the sponsor of the co-op is still controlling the board of directors or is not keeping the commitments which it made in the offering plan, the Attorney General's Real Estate Finance Bureau may have jurisdiction. If you have a question or concern we may be able to help you with, please send a letter to:

Real Estate Finance Bureau
Office of the NYS Attorney General
28 Liberty Street
New York, NY 10005
www.ag.ny.gov/bureau/real-estate-finance-bureau

We have also included other resources that may be helpful on the back of this brochure.