

New York High Court Adopts Unconscionability Standard to Overcome Statute of Frauds

By Karen E. Clarke

In *In re Estate of Hennel*, the N.Y. Court of Appeals, ruling on a matter of first impression, established a stringent “unconscionability” standard applicable when a party seeks to use the promissory estoppel doctrine to overcome the statute of frauds.¹ The lower courts had been applying this standard inconsistently and, in some cases, more expansively than the Court of Appeals considered appropriate. Accordingly, the Court took the opportunity to instruct that promissory estoppel is a rare exception to the statute of frauds that may only be invoked in cases involving true unconscionability, not mere injustice or unfairness.

Proceedings Below

In re Estate of Hennel involved a petition by two grandsons of the decedent to require the estate to pay off a mortgage loan taken by the decedent in 2001, secured on an apartment building property the decedent then owned. In 2006, the decedent and the grandsons agreed that the grandsons would take over ownership and management of the property, and the decedent orally promised that he would direct his estate to satisfy the balance of the mortgage debt upon his death. To effectuate this agreement, the decedent simultaneously executed (1) a warranty deed that conveyed the property (but not the mortgage) to the petitioners while reserving a life estate to himself, and (2) a will that specifically directed that the mortgage on the property be paid from the assets of his estate. In 2008, however, the decedent executed another will that did not contain that specific direction but did generally direct payment of “any and all just debts” as soon as practicable after his death; yet he assured the grandsons that there had been “no change” in their agreement regarding the property.

The decedent died in 2010, and the grandsons filed a petition pursuant to Surrogate’s Court Procedure Act (SCPA) 1809 to determine the validity of their claim against the estate for satisfaction of the mortgage loan. They asserted causes of action for breach of contract and promissory estoppel based upon the 2006 agreement, and sought a ruling that the estate was required to satisfy the mortgage loan as a “just debt” under the 2008 will. The respondent executor asserted that the decedent’s alleged oral promise to direct his estate to pay off the mortgage loan upon his death was not enforceable under the statute of frauds because it was not in writing,² and the decedent’s 2006 will could not satisfy the requirement of a writing because it was incomplete and was revoked in 2008.

On the parties’ cross-motions for summary judgment, the Surrogate’s Court concluded that a binding agreement was reached in 2006 and that the respondent should not be able to avoid that agreement through the statute of frauds. Given that the petitioners had performed the agreed management and maintenance duties without compensation for four years in reliance on the decedent’s promise to have his estate pay the mortgage debt, the court held that this case fell “squarely within that limited class of cases where promissory estoppel should be applied to remedy a potential injustice,” and accordingly granted summary judgment to petitioners.³

A divided Appellate Division affirmed, concluding that the elements of promissory estoppel were met and that the respondent was properly estopped from invoking the statute of frauds defense because it “would wreak an unconscionable result in this case.”⁴

Court of Appeals Majority Establishes Unconscionability Standard

The Court of Appeals (5-1) reversed, holding that petitioners could not rely on the promissory estoppel doctrine because application of the statute of frauds would not inflict an unconscionable injury upon petitioners. The majority decision, by Judge Eugene Fahey, began by announcing that the Court was now adopting the principle, which it had not previously expressly recognized, that the statute of frauds could be overcome through a showing of promissory estoppel and unconscionable injury. After discussing the policy rationales behind this doctrine, the Court established a general rule that “where the elements of promissory estoppel are established, and the injury to the party who acted in reliance on the oral promise is so great that enforcement of the statute of frauds would be unconscionable, the promisor should be estopped from reliance on the statute of frauds.”⁵

The Court specifically rejected the commonly cited standard of the Restatement (Second) of Contracts § 139 to the extent that it “permits circumvention of the statute of frauds where mere ‘injustice’ not rising to the level of unconscionability would result.”⁶ To define unconscionability, the Court looked to the general definition of an unconscionable contract—one where the inequality was “so strong and manifest as to shock the conscience and con-

KAREN E. CLARKE has been a commercial litigator in New York City, and occasionally New Jersey, for 28 years. Previously at Proskauer Rose LLP, Karen is now Of Counsel at Castaybert PLLC, handling business litigation and arbitration matters for small to mid-size businesses and individuals. <https://ac-counsel.com/of-counsel/karen-e-clarke/>.

found the judgment of any person of common sense”—and instructed that the standard to avoid the statute of frauds “must be equally demanding, lest the statute of frauds be rendered a nullity.”⁷

Applying this demanding standard, the Court held that petitioners did not demonstrate an unconscionable injury sufficient to estop respondent’s reliance on the statute of frauds. Although petitioners had performed their end of the bargain for four years, they were not forced to expend any personal funds to pay the mortgage or to manage or maintain the property, or to sacrifice other responsibilities or opportunities. Petitioners’ arguments that they were misled by the decedent in 2008 and were unfairly denied the full benefit of their oral bargain (receiving only \$150,000 in equity in the property instead of the full \$235,000 equity they were promised), also did not suffice. The Court explained that whenever an oral agreement is rendered void by the statute of frauds, one or both parties will be deprived of the benefit of their oral bargain, and some unfairness will typically result, but “what is unfair is not always unconscionable.”⁸

and must be paid by the Estate pursuant to Article First of the 2008 Will.”¹² The Surrogate’s Court rejected respondent’s argument that EPTL 3-3.6 (which provides generally that encumbrances on a decedent’s property are not chargeable against assets of decedent’s estate) effectively removed the mortgage from the will’s provision for the payment of debts. Section 3-3.6, by its explicit language, only applies when the property is “specifically disposed of by will or passes to a distributee” in intestacy, whereas the property here had been conveyed to the petitioners by deed four years prior to the decedent’s death and never became part of his estate. The Surrogate’s Court concluded,

Since the Petitioners did not assume the mortgage when accepting title to the property, and the Note that the Decedent gave to Trustco Bank is a ‘just debt’ of the Decedent, the Estate is obligated to pay the outstanding balance of the Note, which would in turn discharge the mortgage on the property.¹³

“The Court of Appeals (5-1) reversed, holding that petitioners could not rely on the promissory estoppel doctrine because application of the statute of frauds would not inflict an unconscionable injury upon petitioners.”

The Court held that, to avoid severely undermining the statute of frauds, unconscionability will be found only when application of the statute of frauds would render “a result so inequitable and egregious ‘as to shock the conscience and confound the judgment of any person of common sense.’”⁹ Finding no such unconscionable result here, the Court reversed the Appellate Division’s order and directed that respondent’s motion for summary judgment dismissing the petitioners’ claim be granted.¹⁰

Dissent Focuses on Distinct “Just Debts” Issue

In his dissenting opinion, Judge Rowan Wilson fully agreed with the majority’s conclusions regarding the unconscionability standard and petitioners’ failure to meet it. He dissented only as to the result, stating that instead of reversal, the matter should be remitted to the Appellate Division for resolution of the Surrogate’s Court’s alternative holding that decedent’s estate was obligated to satisfy the mortgage as a “just debt” of the decedent, which the Appellate Division had not addressed.¹¹

The Surrogate’s Court had ruled that “despite the omission from the Decedent’s 2008 Will of the language contained in Article Fifth of his 2006 Will, the Court finds that the mortgage debt is a ‘just debt’ of the Decedent

The Appellate Division did not decide the “just debt” issue, apparently deeming it unnecessary in light of its conclusion that the Surrogate’s Court had the authority to direct the estate to pay the mortgage debt as a “valid claim against the estate” based on promissory estoppel.¹⁴

In the Court of Appeals, as dissenting Judge Wilson explained, “The parties did not brief or argue the ‘just debts’ issue..., so the Surrogate Court’s determination remains law of the case, meaning we cannot reverse and order judgment for respondent. The correct result here should be to remit the matter to the Appellate Division to determine the ‘just debts’ issue.”¹⁵ Thus, the dissenting judge believed that the question whether the decedent’s mortgage debt owed to the bank was a “just debt” payable by the decedent’s estate was distinct from, and not necessarily dependent upon, the question whether the petitioners had a legally enforceable contract with the decedent. The dissent acknowledged the possibility that the Surrogate’s Court, with its broad equitable authority under SCPA 201, could deem the bank loan a “just debt” that was required to be paid under the will’s terms regardless of the legal unenforceability of the decedent’s agreement with the petitioners.¹⁶

The majority, in contrast, viewed the Surrogate's Court's "just debt" ruling as dependent upon its finding that the decedent was bound by the oral agreement. Thus, the majority believed that to remit for further consideration of the "just debt" issue would be "inconsistent" with the Court's holding that the decedent was not bound by the oral bargain. The majority also noted that neither party had raised any argument on the "just debt" issue in the Court of Appeals.¹⁷

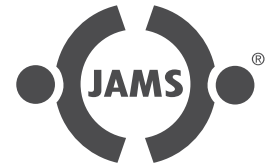
Conclusion

In *In re Estate of Hennel*, the New York Court of Appeals provided a helpful clarification of the demanding unconscionability standard that must be met to avoid the statute of frauds on promissory estoppel grounds. Although the issue arose in an estate case, this instructive ruling will presumably govern all commercial cases. In estate cases, as the dissenting judge noted, there is an additional lingering question regarding the extent to which a Surrogate's "just debt" determination may be analytically distinct from a determination of the legal enforceability of an oral promise.

Endnotes

1. *In re Estate of Hennel*, 29 N.Y.3d 487, 58 N.Y.S.3d 271 (2017).
2. The pertinent statute of frauds provisions are N.Y. Estates, Powers & Trusts Law (EPTL) 132.1(a)(2), covering promises to make testamentary provisions of any kind, and N.Y. General Obligations Law § 5-701(a)(1), applicable when the performance is not to be completed before the end of a lifetime.
3. *In re Estate of Hennel*, 40 Misc. 3d 547, 557-60, 967 N.Y.S.2d 625 (Sur. Ct. Schenectady Co. 2013).
4. *In re Estate of Hennel*, 133 A.D.3d 1120, 1123, 20 N.Y.S.3d 460 (3d Dep't 2015).
5. 29 N.Y.3d at 494.
6. *Id.* at 494 n.3.
7. *Id.* at 495.
8. *Id.* at 497.
9. *Id.* (citation omitted).
10. *Id.* at 498.
11. *Id.* at 498.
12. 40 Misc. 3d at 560.
13. *Id.*
14. 133 A.D.3d at 1123.
15. 29 N.Y.3d at 499-500.
16. *Id.* at 499.
17. *Id.* at 498.

JAMS is proud
to support the
New York State Bar
Association (NYSBA)
Commercial and
Federal Litigation
Section and Dispute
Resolution Section



JAMS New York
Resolution Center
620 Eighth Avenue
34th Floor
New York, NY 10018
212.751.2700
Resolving Disputes
Worldwide
www.jamsadr.com

paid advertisement