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Open Questions About The NY Rent Act Of 2015

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On June 26, 2015, Governor Andrew Cuomo signed into the law the Rent Act of 2015. Among other things, the act amends the laws regulating more than 1 million rent stabilized and rent controlled apartments in New York City.

The act was a result of various last minute political compromises. On the face of things, the act leaves the fundamental structure of New York City apartment rent regulation in place but with some new limitations on the "luxury deregulation" of apartments. The act extended the state enabling legislation that authorizes New York City rent regulations for another four years; increased the monthly rental amount necessary to deregulate apartments on vacancy; lengthened the amortization period for rent increases based on owners' installation of major capital improvements; and limited vacancy allowance rent increases where the outgoing tenant paid a "preferential rent." The act also amended the New York real estate tax benefit program under RPTL 421-a and completely unrelated provisions of the state's Education Law.[1]

The act's amendments to the apartment rent regulatory laws and related 421-a tax benefit program can be summarized as follows:

Extension Dates and Retroactivity

New York's rent laws were extended for four years through June 15, 2019, and made retroactive to June 15, 2015. Section 1-a of the act, extends the Emergency Tenant Protection Act through June 15, 2019. Section 2 of the act extended the state enabling statute governing rent controlled tenants in New York

City to that same date.

Luxury Deregulation

The act increased the rent at which apartments are deregulated after a vacancy from $2,500 to $2,700 per month (the “deregulation threshold”). Furthermore, the deregulation threshold will now automatically adjust annually, starting on Jan. 1, 2016 by the same percentage as the one year renewal adjustment adopted by the Rent Guidelines Board (RGB). The deregulation threshold was also increased to $2,700 per month for "rent controlled" (as opposed to rent stabilized) apartments. That deregulation threshold will also adjust annually by the same percentage, even though rent controlled apartments are not affected by the RGB orders.

The act also modified (in inconsistent ways) the timing of the triggering mechanism for luxury deregulation. Prior to this amendment the statutory language addressing when the legal rent had to reach the deregulation threshold for various time periods said that the legal rent had to reach the deregulation threshold either “at the time the tenant vacated” or, for a different period, a vacancy had to occur “with a legal regulated rent” [at the deregulated threshold]. The language in the act applicable to vacancies which occur on or after June 15, 2015, chooses neither of those options. Instead, the act states that deregulation will apply when the high rent apartment “becomes vacant ... where such legal rent was $2,700 or more.” To make things even less clear, the same section of the act also provides that deregulation will occur for any apartment “with a legal regulated rent that was $2,700 at any time after 6/15/15 ... which becomes vacant after 6/15/15.”[2] These subtle language changes could have a substantive effect on how the courts interpret and apply the luxury deregulation rules.

Vacancies

The act also limits the vacancy allowance for apartments with “preferential rents.” A preferential rent occurs when an owner agrees to temporarily accept a rent less than the maximum legal regulated rent for an apartment, usually due to market conditions. The statutory vacancy allowance provides for a 20 percent increases in the legal regulated rent for a two year vacancy lease and an increase equal to 20 percent less than the difference between the one-year and the two-year renewal guidelines for a one year vacancy lease. However, if a tenant paying a preferential rent vacates, the act provides that the vacancy allowance by which the legal regulated rent is increased cannot exceed:

… 5 percent of the previous legal regulated rent if the last vacancy lease commenced less than two years ago; 10 percent of the previous legal regulated rent if the last vacancy lease commenced less than three years ago; 15 percent of the previous legal regulated rent if the last vacancy lease commenced less than four years ago; 20 percent of the previous legal regulated rent if the last vacancy lease commenced four or more years ago.

Note that this new limitation on the vacancy allowance does not apply where the outgoing tenant was not paying a preferential rent, but was paying the full legal regulated rent.[3] The act is the first statutory amendment to the vacancy allowance formula since its enactment in 1997.

Major Capital Improvement Increases

The act limits the amount by which owners can increase apartment rents to recover the cost of installing building-wide major capital improvements (MCI), by extending the amortization or recoupment period. Prior to the act, the recoupment period was 84 months. The act extends that recoupment period to 108 months (nine years) for buildings containing more than 35 units. For buildings with fewer than 35 units, the recoupment period increased from 84 months to 96 months (eight years). However, the act did not change the rule that the MCI rent increase remains permanently part of each apartment's legal regulated rent, even after the cost is fully recovered.

RPTL 421-a

The act also includes amendments to RPTL 421-a. These amendments provide that projects which "commence" prior to Dec. 31, 2015, are grandfathered under the pre-act 421-a eligibility rules.

Section 63-c of the act sets forth the substantive amendments to 421-a for projects which commence on or after Jan. 1, 2016, and before Dec. 31, 2019. These amendments substantially increase the "affordability requirement" for participation in the program. For such new projects there are three affordability options. The first option provides for a 35 year benefit period which includes a 25 year 100 percent exemption, conditioned on developers setting aside 25 percent of the newly constructed apartments as "affordable" and leasing them to tenants whose household income ranges from 40 percent to 130 percent of adjusted median income (AMI). This option is eligible for government financing and tax credits. The second option also includes a 35 year benefit period with a 25 year 100 percent exemption, but is conditioned on 30 percent of the apartments being set aside as affordable for tenants whose household income ranges from 70 percent to 130 percent of AMI. This affordability option is also eligible for government financing. The third affordability option also includes a 35 year benefit period, with a 25 year 100 percent exemption, based on setting aside 30 percent of the apartments as affordable for tenants whose household income is up to 130 percent of AMI and the projects in this category, however, are not eligible for government financing, or as to properties south of 96th street in Manhattan.

Furthermore, the act provides that market rate condominiums are no longer eligible for 421-a tax benefits, with a limited exception for small, market value capped, structures in the outer boroughs.

Finally, the extension of 421-a tax benefits beyond Dec. 31, 2015 is conditioned on there being a negotiated "prevailing wage" agreement between the construction trade unions and property developers before the end of 2015. This is apparently an unprecedented mechanism to trigger the effect of a state statute and there is no assurance such an agreement will be reached. In that case the RPTL statute will "sunset" Dec. 31, 2015.

The Intent and Effect of the Act

The undeniable intent of the act is to reduce the number of apartments which are luxury deregulated each year. This results in more apartments remaining subject to the rent regulations, albeit at higher rents. The act implements this intent in several ways:

1. The high rent deregulation threshold is increased from $2,500 to $2,700 per month and the threshold is indexed to the annual RGB orders for one year renewal leases. Therefore, an apartment with a legal rent currently below the threshold will never reach the threshold so long as the tenant remains in occupancy and chooses one-year renewal leases.

2. Arguably, according to tenant advocates the act may for the first time require that the legal regulated rent has to be $2,700 per month or greater prior to the vacancy which triggers luxury deregulation.

3. The vacancy allowance for apartments with preferential rents and MCI rent increases are reduced, so that it takes longer for an apartment's legal regulated rent to reach the deregulation threshold.

What the Act Did Not Change

1. Despite the political pressures brought by various advocacy groups, the act does not eliminate luxury deregulation.

2. The act does not alter the fact that luxury deregulation is based on legal rents rather than rents charged and collected. Therefore, in cases where there are preferential rents, if the legal rent exceeds the deregulation threshold, deregulation will occur even though a rent in excess of $2,700 per month was not actually collected. Furthermore, preferential rents can still be limited to a single lease term and not be carried forward into renewal leases.

3. MCI rent increases remain a permanent rent increase; they do not end when the MCI costs are fully amortized.

Discussion

Immediately after enactment of the act, advocates for interested parties, i.e., regulated apartment tenants and regulated building owners, began a public debate concerning the appropriate meaning and intent of the act and what it does to the rent regulations. Tenant advocates described the modifications in the act as a "big deal for tenants;" while attorneys for regulated property owners responded that "the statute as a whole doesn't change anything."[4] The advocates for both positions can find support in the language of the act.

For instance, Section 10 of the act undeniably amends the high rent deregulation provision of the RSL so as to provide that deregulation occurs when the $2,700 per month deregulation threshold rent is reached and the apartment "becomes vacant." Tenant advocates claim that this language implies that in order to deregulate an apartment, the $2,700 per month threshold must first be reached and a subsequent vacancy must occur.

Owner advocates on the other hand, point to Section 12 of the act which amends the preferential rent rules for apartments. Both sides recognize that the legislature limited the vacancy allowance for those opponents to keep them in the system ledger. Yet, the explicit language of Section 12 of the act provides that the deregulation threshold need only be met during the vacancy period, that is "subsequent to vacancy," rather than prior to the vacancy occurring. This means no change in the deregulation rules which have been in effect since 1993.

Ultimately, the courts will have to resolve the inconsistencies and contradictions in the statute concerning the mechanisms by which apartments are deregulated. Presumably, the courts will reach a rational result based on the actual language of the act. However, the need for judicial interpretation could have been avoided by a clearer statute being enacted by the Legislature in the first place. Residential tenants plan their housing needs based on these laws and massive amounts of private investment capital in residential multi-family housing, turns on the exact meaning of these rent regulations.

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[1] Rent Act of 2015, ch. 20, 2015 N.Y. ALS 20.

[2] Rent Act of 2015, ch. 20, §10, 2015 N.Y. ALS 20 (amending N.Y.C. Admin. Code § 26-504.2).

[3] For a one year vacancy lease the vacancy allowance is 20 percent less the difference between RGB two year and one year lease renewal allowance. See N.Y.C. Admin. Code § 26-511(c)(5-a).

[4] Josh Barbanel, New York Rent Act Draws Conflicting Interpretations: Lawyers disagree on whether law extending regulation also expands tenant protections, WALL ST. J., July 16, 2015.