New York Law Journal
SERVING THE BENCH AND BAR SINCE 1888
WWW.NYLJ.COM
An ALM Publication
VOLUME 261—NO. 108
THURSDAY, JUNE 6, 2019

Outside Counsel

Airbnb: Reconciling Conflicting Public Policies

By **Michael A. Pensabene**

And **Nicholas Kamillatos**

For the past decade, there has been a continuous struggle between policymakers, multifamily property owners, tenants, and ultimately, home-sharing Internet platforms, such as Airbnb.com, regarding the short-term usage of apartments in "Class A" apartment buildings. (For purposes of this article, we will refer to all home-sharing Internet platforms as "Airbnb".) This article will chronicle how the law has evolved during this timeframe and discuss where it may be headed.

'Class A' Apartment Buildings and the State's Multiple Dwelling Law

The State's Multiple Dwelling Law (MDL) was amended by Chapter 225, Laws of 2010, to modify MDL §4(8)(A) to provide that housing accommodations in "Class A" apartment buildings could only be occupied for "permanent residential purposes," which is defined as the same natural person or family occupying the housing accommodation for 30 consecutive days or longer. This 2010 MDL amendment, and corresponding amendments to the Administrative Code of the City of New York (NYC Code), was the Legislature's response to the Appellate Division, First Department's decision in *City of New York v. 330 Continental*, 60 A.D.3d 226 (1st Dept. 2009), wherein the Appellate Division vacated a preliminary injunction against property owners using some "Class A" housing accommodations in their apartment buildings for short-term transient use, i.e., for periods less than 30 consecutive days. The Appellate Division concluded that no violation of the City's Zoning Resolution or the "Class A" certificate of occupancy resulted from a minority of the housing accommodations being occupied by transient tenants for periods less than 30 days. In view of the vagueness of the MDL defining what amount of transient use could lawfully occur in a "Class A" apartment building, the Appellate Division vacated the preliminary junction against any transient rentals as being, at minimum, premature.

> This decade-old struggle reflects competing, and possibly irreconcilable, policy interests of the City and State governments.

By enacting Chapter 225, Laws of 2010 and amending MDL §4(8)(a), the State Legislature established clear public policy against multifamily property owners leasing any "Class A" apartments for transient use. However, the State Legislature provided explicit carve-outs intended to preserve certain well-recognized tenants' rights. Specifically, §4(8)(a)(1)(A) carved out from the definition of unlawful transient use, permanent tenants' houseguests, borders, roomers or lodgers; and Subsection (B) carved out from unlawful temporary use cases where the permanent tenant was absent for personal reasons, provided, that there is no monetary compensation paid to the permanent occupant for such occupancy. Accordingly, by enacting Chapter 225, the State's public policy was made

MICHAEL A. PENSABENE *is a member in the litigation department of Rosenberg & Estis.* NICHOLAS KAMILLATOS *is a member in the firm's administrative law department.*

clear: Apartment building owners profiteering from short-term transient rentals in "Class A" apartments, as in *330 Continental*, shall be unlawful, but this restriction was not intended to infringe on a tenants' right to lawfully host short-term guests.

Then, the rise of Airbnb in New York after the 2010 amendment to the MDL began to undermine this public policy. Rent-regulated tenants started exploiting the MDL's safe harbor protections in order to monetize their below-market regulated rents by using Airbnb to bring in transient renters for extraordinary profit. See, e.g., *Brookford, LLC v. Penraat*, 47 Misc.3d 723 (Sup. Ct., NY Co., 2014). Instead of property owners, tenants using Airbnb were now creating new de facto transient hotel rentals in violation of MDL 4(8)(a). This practice challenged two stated public policies: the prohibition of short-term rentals in "Class A" apartment buildings, and increasing the availability of affordable housing in New York City.

Housing Court Restricts Tenant Profiteering

The appellate courts addressed the issue of unlawful tenant profiteering in the pre-Airbnb case of *220 W. 93rd St., LLC v. Stravrolakes*, 33 A.D.3d 491 (1st Dept. 2006). There, the First Department held that a rent-regulated tenant renting all or part of their apartment to "short-term transient" occupants constituted a lease violation resulting from unlawful subletting, rather than a bona fide roommate situation. (A tenant's right to have a roommate is codified at §235-f of the Real Property Law, in addition to the MDL, and the cited case law establishes that rent-regulated tenants are entitled to roommates sharing the rent obligation.) Similar results followed in *42nd and 10th Associates, LLC v. Ikezi*, 50 Misc.3d 130 (Appellate Term 1st Dept. 2015) and *Goldstein 355-7 LLC v. Steele*, 53 Misc.3d 150(A) (Appellate Term 1st Dept. 2016). In each of these cases, the courts ruled that the rent-regulated tenant was engaging in unlawful profiteering rather than bona fide roommate rent sharing. The obvious question arises: What is profiteering?

In *Goldstein v. Lipetz*, 158 N.Y.S.3d 562 (1st Dept. 2017), the First Department, by a 3-2 majority, gave a clear explanation of unlawful tenant profiteering, also known as commercializing a rent-regulated apartment. In *Goldstein*, the First Department, first noted that rent-regulated tenants could lawfully charge a maximum 10% rent premium to roommates or lawful subtenants for use of a furnished apartment. For that reason, rent-regulated tenants charging a 10% surcharge or less would not constitute unlawful profiteering. More significantly, the First Department concluded that the 10% premium would be calculated by a per diem analysis, by comparing the daily stabilized apartment rent against the short-term rental charges imposed by the rent-regulated tenant on their Airbnb users. By using the per diem methodology, the court concluded that the rent-regulated tenant had "realized a 72% profit during the days she had subleased the apartment," i.e., about seven times the 10% premium permitted by the RSL, with the result that the tenant was subject to eviction for unlawful profiteering.

The profiteering and commercialization cases are holdover proceedings commenced in the Housing Court by multi-family property owners, based on the tenant's violation of the lease and the Rent Stabilization Law and Code. Generally, breach of lease cases allow rent stabilized apartment tenants to cure the violation of the lease and applicable law and avoid eviction. See, e.g., Real Property Actions and Proceedings Law 753(4). The majority in *Goldstein* held that a profiteering rent-regulated tenant has no right to cure as a matter of law. As with the definition of "profiteering," the question of cure is also a fact based totality of the circumstances test. The majority cited the lengthy 18-month term of the profiteering as the basis to deny a cure and evict the tenant. The court contrasted the holding in *Cambridge Development LLC v. Staysna*, 66 A.D.3d 614 (1st Dept. 2009) where the unlawful conduct had a much shorter duration and thus the rent-regulated tenant was not denied the right to cure.

2016 Legislative Response To Prolific Airbnb Use

In recognition of the fact that Airbnb was undermining the clear public policy against transient use of "Class A" apartments, the State Legislature enacted Chapter 396, Laws of 2016 which added §121 to the MDL and §27-287.1 to the NYC Code. This new law imposed escalating fines up to $5,000 for the third and subsequent violations, for "advertising" "Class A" housing accommodations for purposes other than permanent residence (i.e., transient use).

In response, Airbnb immediately commenced an action in the Southern District of New York, seeking to enjoin the enforcement of MDL §121

and declaring it invalid. *Airbnb.com v. Schneiderman, et al*., 16 CV 8239 (SDNY). Interestingly, however, that action was settled and dismissed by stipulation pursuant to which the City of New York agreed to permanently refrain from enforcing MDL §121 as against Airbnb. The City intended to enforce the law as against Airbnb users through the Mayor's Office of Special Enforcement (OSE). In theory, this should have permitted OSE to verify a host's statutory compliance by simply monitoring their advertisements on the Internet. However, in practice, this was not the case.

As Airbnb operates akin to "cyber-brokerage," it connects a "host" to a "guest," like a landlord to a tenant, for a percentage of guest's cost for the stay. Thus, Airbnb must ensure that the transaction closes through Airbnb, and not "offline," in order to collect its fee. To do this, Airbnb will only show very limited information in the advertising posted on its website, although Airbnb maintains proprietary detailed records of each transaction. For example, an advertisement will only show an Airbnb user's profile name, rather than their legal name, and a general description of the accommodations, such as their size and the neighborhood where they are located, instead of the actual address. Needless to say, with respect to multiple dwellings in New York City, this makes it very difficult for OSE to connect advertising to specific apartments, and to the specific individuals renting them.

New York City's Failed Effort To Crackdown

The City, having grown frustrated with its inability to regulate home-sharing through Airbnb, and in an effort to collect taxes payable from these transactions but which are otherwise unrealized, enacted Local Law 2018/146, codified at NYC Code §26-2101, et seq. (the "Local Law"). The Local Law requires Airbnb and other "booking services" (see N.Y.C. Admin. Code §26-2101) to submit monthly transaction reports to an administering agency, stating (1) the full address of each dwelling rented, (2) the full legal name, address and phone number of each host, together with the profile information that host uses on Airbnb, (3) the identifying name, number and uniform resource locator (URL) for each advertisement, (4) a statement as to whether the transaction involved a full or partial short-term rental of a dwelling, (5) the number of days booked for each transaction, (6) the total amount of the fees collected for each transaction, and (7) if the "booking service" collects the rent on behalf of a host, the amount of the rent the booking service collected, and the amount paid to the host, together with the account information. N.Y.C. Admin. Code §26-2102(a)

> Rent-regulated tenants started exploiting the MDL's safe harbor protections in order to monetize their below-market regulated rents by using Airbnb to bring in transient renters for extraordinary profit.

In response to the Local Law, Airbnb and a similar platform, Homeaway.com, wasted no time commencing actions in the Southern District Court of New York seeking to enjoin the City from enforcing this Local Law, prior to it becoming effective on Feb. 2, 2019. *Airbnb, Inc. v. City of New York*, 18 CV 7712 (SDNY). They asserted, among other arguments, that the Local Law violated the Fourth Amendment of the United States Constitution, and Article I, §12, of the New York State Constitution.

On Jan. 3, 2019, the District Court, citing to *Patel v. City of Los Angeles*, 738 F.3d 1058 (9th Cir. 2013), aff'd 135 S. Ct. 2443 (2015), granted the injunction and enjoined the City from enforcing the Local Law. The District Court (Engelmayer) found that Airbnb's business records are its private property and that the Local Law constituted an unreasonable search and seizure of those records.

Again, as in 2016, Airbnb successfully avoided government regulation to its operations in New York.

2019 Proposed Legislation

In light of the past legislative failures, Assemblymember Joseph Lentol and State Senator James Skoufis are now proposing new State legislation which will mark a significant departure from current public policy. Their respective bills (Assembly Bill A6392 and Senate Bill S4899), contemplate adding an Article 7-D to the MDL, which would affirmatively legalize home-sharing in New York, with certain restrictions, and conditioned on Airbnb and its users complying with registration and tax requirements. Under the proposed law, a "Class A" apartment may be operated for transient use, provided that the apartment is registered with the New York State Division of Housing and Community Renewal (DHCR) and notices are posted in the apartment containing emergency contact information and emergency egress instructions. This

apartment sharing practice would be limited to one unit per host. Although home sharing would not be permitted in rent controlled apartments or in multiple dwellings designated for use as single room occupancy (SRO), the law would permit home-sharing in rent stabilized apartments, provided that it would not serve as grounds for eviction under the Rent Stabilization Code (e.g., profiteering). DHCR would be charged with enforcing this new law. Airbnb would be required to provide anonymous statistical data to DHCR and collect the taxes to be paid for each transaction.

This proposed law raises serious policy issues.

First, this proposed state law would permit free-market apartments to effectively operate as hotel rooms, perpetually, without any mechanism to restrict the number of units used for this purpose in any building. This effectively brings us back full circle to the state of affairs that the City sought to address in the *330 Continental* litigation. If numerous individual tenants in one multiple dwelling rent out their apartments for transient use, the multiple dwelling may operate more like a de facto hotel than a "Class A" apartment building. This would be an affront to the quality of life of the tenants (free-market or rent-regulated) who actually live in their apartments as their home. Clearly this would run afoul of City planning and public policy to maintain safety and a quality of life for permanent rental tenants, i.e., the specific public policy rationale for Chapter 225, Laws of 2010.

Furthermore, contrary to stated public policy, this proposed law would permit rent-stabilized tenants to monetize their benefit of having a regulated rent below prevailing market rates. This will encourage more Airbnb practice in the affordable housing stock, limiting its availability for prospective permanent tenants.

Finally, although DHCR would receive registrations from hosts and anonymous statistics from Airbnb, it would still lack the information necessary to effectively enforce the law, as accepted after the passage of §121 of the MDL. The Airbnb transactions will remain sub rosa, and it is unclear whether or not DHCR has the appropriate resources and enforcement power to regulate an entire new class of regulated tenancies, currently estimated to be approximately 50,000 apartments, if not more.

Conclusion

This decade-old struggle reflects competing, and possibly irreconcilable, policy interests of the City and State governments. There are obvious safety and quality of life concerns underlying the MDL's strict prohibition against transient rental of "Class A" apartments, yet the legislature is more tolerant of tenants engaging in this practice, without regard for the private property owners who often find themselves having to enforce the law against their tenants through expensive and time consuming Housing Court litigation.

Although the State would like to permit some form of short-term occupancies, in order to realize the economic benefits from tourism and taxes it has not yet developed any effective means to realize that result. Its effort to monitor advertisements as a method to regulate the practice has been ineffective and its attempt to compel Airbnb to turn over proprietary information so it could be monitored has been held to be unconstitutional.

The most recent proposal in the State Legislature is to legalize Airbnb in New York City, with some regulations, apparently for the purpose of realizing the economic benefits. However, the proposed regulations fall far short of fully reconciling all of the public policy issues which the government sought to address when it first enacted Chapter 225, Laws of 2010.

To date there has not been a coherent policy approach, but perhaps the legislature looking now to DHCR for regulatory oversight is an indicator of where the law might be heading. DHCR currently oversees the rent controlled and rent stabilized apartments in New York City, so it is possible that a comprehensive form of Airbnb regulation, similar to rent regulation, is on the horizon. It remains to be seen whether or not the legislature can establish a coherent and enforceable apartment sharing policy which rationally balances all of the competing policy issues.