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RENT REGULATION

Luxury Deregulation After J-51 Benefits End


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One of the questions left unanswered by the Court of Appeals' 2009 decision in *Roberts v. Tishman Speyer Properties*[1] was whether owners could take advantage of high income luxury deregulation once J-51 benefits expired. Tenants argued post-'Roberts' that a building's receipt of J-51 benefits permanently barred high income deregulation in that building, even after benefits were no longer being received. Owners argued to the contrary.

After several years of litigation, the rule with respect to rent stabilized apartments is clear, although the result depends on whether the apartment was stabilized before J-51 benefits were ever received. For rent controlled apartments, there is no clear rule.

Background

Under rent stabilization, there are two types of buildings that can receive J-51 benefits. First, there are those buildings—like the buildings in 'Roberts'—that were subject to rent stabilization based on their pre-1974 construction date and thereafter received J-51 benefits (hereinafter "Type A" buildings).

Second, there are those post-1973 buildings that were not stabilized at the time the owner received J-51 benefits, but became stabilized solely by virtue of receiving such benefits ("Type B" buildings). As originally conceived, apartments in Type B buildings would automatically become deregulated when J-51 benefits expired.

By 1985, thousands of apartments in Type B buildings were on the verge of losing rent stabilization status due to the expiration of J-51 benefits. In response, the Legislature added RSL §26-504(c) to the statute, which generally required owners of Type B buildings to provide stabilized tenants with a notice in their initial lease, and in each renewal thereafter, that J51 benefits were due to expire on the stated date, and that the apartment would become deregulated upon the expiration of the lease in effect on that date. Absent such notice, the apartment would remain stabilized until it became vacant.

Pursuant to the Rent Regulation Reform Act of 1993 (L. 1993, ch. 256), high income deregulation was added to both the Rent Stabilization Law and the City Rent Law ("rent control").

Type A: 'Schiffren'

In *Schiffren v. Lawlor*,[2] the Appellate Division, First Department ruled that in Type A buildings, owners may pursue high income deregulation once J-51 benefits have expired. In *Schiffren*, the tenant moved into a rent-stabilized apartment in 1989. The building, a Type A building, began receiving J-51 benefits on July 1, 1995. Those benefits expired on June 30, 2006.

In 2008, the owner sought to deregulate the subject apartment based on high income. The tenant argued that the building's receipt of J-51 benefits permanently barred high income deregulation, an argument that DHCR rejected. The Appellate Division, First Department ultimately affirmed DHCR's ruling, holding:

> The issue raised on this appeal is whether, as a matter of law, a dwelling unit that was subject to rent regulation before an owner received J-51 benefits can be subject to luxury deregulation once those benefits expire.
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> The plain language of Administrative Code §§ 11-243 and 26504(c) supports the conclusion that the Legislature intended to provide that a building that is already regulated when it receives J51 benefits will continue to be regulated under the original rentregulation scheme when the tax benefits expire. We conclude that the reversion to pre-J-51-benefit rent-regulation status includes the right of an owner to seek luxury deregulation in appropriate cases.[3]

Type B: '73 Warren'

The rule for apartments in Type B buildings was set forth by the Appellate Division, First Department in *73 Warren Street v. New York State Division of Housing and Community Renewal*.[4] In *73 Warren*, the building was a Type B building which became subject to stabilization by virtue of its receipt of J-51 benefits in 1977. Those benefits expired in 1990. In 2008, the owner sought to deregulate the apartment of Victor Schrager, a tenant

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since 1984, based on high income. DHCR denied the luxury deregulation application, holding that luxury deregulation is not available in Type B buildings.

The Appellate Division thereafter affirmed DHCR's analysis, holding:

> … an apartment that becomes rent stabilized upon the building owner's receipt of J-51 benefits remains stabilized upon the expiration of those benefits, except in two distinct instances: where the stabilized tenant vacates, or where the stabilized tenant had been consistently and properly notified in his lease that the apartment would become deregulated upon expiration of the tax benefits. The statute also provides that if the building was already deregulated when the owner began to receive tax benefits, it continues to be regulated upon the expiration of tax benefits under the statutory scheme that initially gave rise to regulation. Here, it is undisputed that because Schrager is still in possession and was not given the requisite notices, the apartment continued to be rent stabilized after the expiration of the J-51 benefits.[5]

The Appellate Division, interpreting the relevant RSL high income deregulation provision (§ 26-504.3), when on to hold that high income deregulation can never be obtained in a Type B building:

> This provision authorizes luxury decontrol for eligible stabilized apartments, with one important general exception; those apartments that are regulated 'by virtue of receiving tax benefits' cannot be decontrolled based on income or the amount of the legal rent….[6]

In the recent DHCR decision of *Matter of Medevoy*,[7] issued on Oct. 9, 2013, the tenants of an apartment in a Type A building insisted that *73 Warren* "conclusively held that luxury deregulation was not available against tenants who resided in the building while J-51 benefits were being received, even after those J-51 benefits expired." DHCR rejected the tenants' claim, explaining the difference between the rules in *Schiffren* and *73 Warren*:

> In *Schiffren v. Lawlor*, the Appellate Division held that high income rent deregulation is not per se prohibited once J-51 tax benefits expire on a housing accommodation that was subject to the RSL prior to J-51 tax benefits having been obtained. Thus, the reversion to pre-J-51-benefit rent stabilization status upon expiration of J-51 tax benefits includes the right of owner to seek high income rent deregulation.
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> …*73 Warren Street LLC* is inapposite because that case involved a housing accommodation that was not rent stabilized prior to receiving J-51 tax benefits—which is not the same status of the building that is the subject of this appeal (internal citations omitted).

Rent Control

Neither *Schiffren* nor *73 Warren* applies to rent-controlled tenancies. DHCR's policy as to rent-controlled apartments was set forth in DHCR's Oct. 26, 2011 decision in *Matter of Berk*.[8] In *Berk*, the owner filed for luxury deregulation in 2008, after J-51 benefits had expired. Although the rent-controlled tenant claimed that her income did not exceed the $175,000 threshold during the relevant years, the Department of Taxation and Finance found otherwise. On Nov. 30, 2010, DHCR's Rent Administrator issued an order of deregulation. The tenant then filed a petition for administrative review (PAR).

After several years of litigation, the rule with respect to rent stabilized apartments is clear.

DHCR issued an order granting the tenant's PAR, ruling that for purposes of rent control, there are no Type A or Type B buildings. Instead, the one-size-fits-all rule is that upon the expiration of J-51 benefits for rent controlled apartments, high income deregulation is not available:

> …Section 26-403(e)(2)(j) of the New York City Rent and Rehabilitation Law… defines those apartments eligible for high income luxury deregulation. Section 26-403(e)(2)(j) also provides that the high income rent deregulation provision does not apply to those housing accommodations which became or become subject to rent regulation by virtue of receiving J-51 tax benefits.
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> The high income rent deregulation exemption from rent control…is not available for apartments in buildings that have been receiving or have received J-51 benefits. Furthermore, there is nothing in the rent control law which provides for the resumption of the availability of high income rent deregulation after J-51 tax benefits have expired. Accordingly, high income rent deregulation is not available to rent controlled apartments for which J-51 tax benefits had been received such as the subject apartment, even after those J-51 benefits have expired.

In *Ram I v. New York State Division of Housing and Community Renewal*,[9] New York County Supreme Court Justice Geoffrey D.S. Wright annulled DHCR's determination in *Matter of Berk*. The court held that there was nothing in the Roberts decision to warrant the conclusion that the receipt of J-51 benefits "at any time in the past will forever condemn an apartment to the restraint of rent regulation, even after the expiration of the tax benefit of the J-51 program."

Accordingly, although the rules for rent stabilized apartments are clear, it remains to be seen how other courts will view DHCR's ruling that high income deregulation is forever prohibited for rent controlled apartments where the building in question has received J-51 benefits.

1. 13 N.Y.2d 270, 890 N.Y.S.2d 388 (2009).
2. 101 A.D.3d 546, 955 N.Y.S.2d 44 (1st Dept. 2012).
3. 101 A.D.3d at 457.
4. 96 A.D.3d 524, 948 N.Y.S.2d 2 (1st Dept. 2012).
5. 96 A.D.3d at 527.
6. Id. at 528.
7. DHCR Adm. Rev. Dckt. No. AV-410042-RT.
8. DHCR Adm. Rev. Dckt. No. YL-420051-RT.
9. Supreme Court New York County Index No. 114412/11.