

Investing In NYC Real Estate? Get Ready For Rent Laws

Law360, New York (March 03, 2015, 10:28 AM ET) --

According to the press, more and more foreigners are choosing to invest in New York City real estate because it's a safe long-term hold. While admittedly, it is safer than many locations overseas, there are substantial risks, resulting as much from the overregulation of the housing market as from the chance that a rental or condo "bubble" may burst at any time. Even foreigners coming from out of state, rather than from out of the country, are often taken aback by the confusing overlay of rent regulations affecting residential housing in the city.

New York City rent regulation started as a form of emergency rationing during and after World War II, the same way gasoline and tires were rationed, as a result of shortages of building materials, which were diverted to the war effort. But housing is a political subject, especially in New York City, and the emergency hasn't gone away in the last 70 years — at least not in the minds of those who keep renewing it.

In its current form, rent regulation keeps evolving and changing. While it is true that the rent laws sunset every few years (the Rent Stabilization Law sunsets next in June 2015), everyone in New York City knows that it will be extended. The question is not whether rent regulation will continue, but rather what tweaks and changes might result from the political compromises attendant to the process.

This time around, the political pendulum is more confused than in recent years. Sheldon Silver, the longtime speaker of the New York State Assembly who recently resigned that position, has for the past many decades been an advocate for continuing and strengthening tenant protections in the rent laws. Will the new speaker step up and take his place keeping rent regulation as one of the major bargaining tools in the New York political process? And what effect will New York City Mayor Bill de Blasio have on the process?

Due to a number of historical anomalies, the New York City rent laws may only be amended and extended by the New York State Legislature, with New York City currently having no authority to amend its own Administrative Code in these respects. Will Bill de Blasio, perhaps the most tenant-oriented champion of affordable housing in years, find some way to influence the negotiations in Albany — or even take back the rent regulations so as to be once again within the city's control?



Blaine Z. Schwadel

For those living in New York City, these questions make for an interesting, and often frustrating, political season. For investors from around the country and around the world, the process makes it seem as though there is no rhyme or reason to the New York City rent laws at all. And indeed, without knowing the politics and economics of the time, the rent laws are a mashup of often-contradictory policies and laws.

In attempting to make sense of the various laws applicable to residential housing in New York City, the New York State Court of Appeals, the highest court in the state, once remarked that the rent laws are “an impenetrable thicket, confusing not only to laymen but to lawyers.” That pronouncement was made in 1974. Since then the rent laws have been amended with ever increasing frequency — major changes to the laws and/or the regulations, which the New York State Division of Housing and Community Renewal (DHCR) applies to enforce those laws, occurred in 1983, 1993, 1997, 2000, 2003, 2009, 2011 and 2014.

The rent laws themselves are extensive and are not the subject for a short article such as this. In New York City alone, housing can be subject to the Local Emergency Housing Rent Control Act, the City Rent and Rehabilitation Law, the Rent Stabilization Law of 1969, the Emergency Tenant Protection Act of 1974, the Omnibus Housing Act of 1983, the Loft Law, the Private Housing Finance Law and a myriad of regulatory agreements between the original developer and a state or city agency that provided some form of financing or participation in a tax benefit program, to name a few. Some buildings can be subject to more than one of these laws or programs at the same time.

Suffice it to say that there are various laws that address which residential apartments are regulated, when regulated apartments may become deregulated, what rents may be charged, how to obtain rent increases and what those rent increases may be. Depending on the law or regulation to the individual apartment, the answers to many, if not all, of the relevant questions may differ. Of course, all of the laws include enforcement mechanisms that can cause an investor substantial economic pain if the often confusing and contradictory rules are not properly followed. Moreover, following the laws and regulations is not enough, as all of them are subject to review by the judiciary, which has more and more taken the position that it — rather than the “expert agency” with the experience to interpret the laws — can read the laws and know what they mean.

By way of example, I simply point to a 2009 case involving Stuyvesant Town — the largest single housing development in New York City. In that case, the Court of Appeals had the opportunity for the first time to interpret a 1993 amendment to the rent laws providing for apartment deregulation. Despite 16 years of history, clear DHCR regulations and DHCR determinations, the court held that the regulations and policies of the DHCR interpreting the law were incorrect.

Relying on its own reading of the laws, the court held that all the apartments in Stuyvesant Town and throughout New York City, which had been deregulated pursuant to that 1993 law over the prior 16 years, should not have been deregulated. Now, more than five years later, the DHCR and the courts are still sorting out the myriad of questions such “reregulation” of those apartments raised. Investing in a building that contains some or many of these deregulated/reregulated apartments presents a challenge and a risk concerning how the courts may treat them in the future.

Knowing the rent laws by itself is not enough. Knowing where to look and what to look for in evaluating residential housing is critical. Investing in a multifamily that is “50 percent fair market” (NY lingo for unregulated apartments) may look good and it may look like there’s an upside for the remaining

regulated apartments. That is, however, only if it can be confirmed that the deregulated apartments are truly deregulated, and that the regulated apartments can actually be deregulated in the future and in what manner — often timing is everything.

Moreover, an investor should want advice that there isn't some change looming on the horizon that can cause the deregulated units to be reregulated or prevent that future deregulation of the others. A caveat here is that no one can give advice on what future laws or court decisions may bring — but current trends and ongoing cases can be evaluated for the impact they may have on a current project.

The point of this article is not to scare away investors by pointing out that there are risks involved in investing in regulated housing in New York City. By their nature, investors are comfortable evaluating and taking risks. The point of this article is to highlight, for investors, the fact that New York City is a strange and different animal. Its politics and economics make for some risks that don't exist elsewhere and that require another layer of risk analysis. Clearly, no one would invest in a building without a complete structural analysis. The analysis of the rent regulatory status of the apartments in the building is just as important and could be just as devastating to the investment.

New York is indeed a vibrant, ever-changing city. That's what makes it a place where business and investors want to be. New construction and new investment in existing housing do provide a safe opportunity to make a great return. Investors know what to look for. In NYC, the trick is to get the right advice finding out what to look out for.

—By Blaine Z. Schwadel, Rosenberg & Estis PC

Blaine Schwadel is an equity member of New York real estate law firm Rosenberg & Estis.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of the firm, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.