The Housing Stability and Tenant Protection Act of 2019: What Owners and Potential Owners Should Do to Protect Themselves

A Lexis Practice Advisor® Practice Note by YuhTyng Patka, Duval & Stachenfeld LLP

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On June 14, 2019, the landscape of the New York City residential rental market swiftly changed with the passage of the Housing Stability and Tenant Protection Act of 2019 (the Act) into law. The Act drastically reformed the laws of rent regulation by placing new limits on tools available to an owner to legally increase rents, along with other changes impacting security deposits, eviction procedures, and Martin Act requirements. The Act provides rent-regulated tenants with protections not seen before in recent memory, including the elimination of an owner's ability to deregulate rent-stabilized units. This article discusses the impact the Act will have on the commercial real estate market in New York City and what owners should do in light of the passage of the Act.

For a general discussion of leasing in New York, see Commercial Real Estate Leasing (NY) and Residential Lease Agreements (NY).

Prior to passage of the Act, buildings containing rent-stabilized units were valuable to investors looking for value-add opportunity. Owners utilized tools such as major capital improvement (MCI) and individual apartment improvement (IAI) rent increases to increase legal rents. MCI and IAI rent increases resulted from an owner's improvements to the property, such as upgrading elevators or heating, ventilation, and air conditioning (HVAC) systems or updating an individual kitchen or bath. Once the unit reached the high-rent deregulation threshold ($2,774 in 2018), the unit was deregulated and the owner could begin charging market rent, thereby immediately increasing the owner's net operating income which in turn increased the value of the building. Now, after passage of the Act, investors who purchased buildings in reliance upon this value-add strategy are left with an asset that is worth far less than they had predicted due to the Act effectively preventing owners from converting rent-stabilized units into market rate units.

With the Act's elimination of high-rent and high-income deregulation, the incentive for owners to rehabilitate and update their buildings and individual units has been effectively removed. Rent increases attributed to a tenant vacancy or longevity have also been eliminated by the Act, further affecting the owner's bottom line. As a result, owners have expressed distress at the added constraints on an already highly regulated real estate industry. Many are concerned about owners' willingness and financial ability to continue maintaining their buildings and individual units after the Act's passage. Some owners have already begun publicly declaring that they will no longer update their properties and will only do the bare minimum moving forward. This is likely to become a concern for tenant advocacy groups. The Act's effect, if these owners' threats are to be credibly believed, will contribute to a lack of quality housing at an affordable price, rather than protect tenants as the Act was originally intended to do.

According to sources in the New York City commercial real estate brokerage industry, it is estimated that affected properties dropped 25% in value immediately after passage of the Act. Accordingly, some investors believe the Act's passage creates a ripe investment opportunity, which will keep brokers, lenders, and attorneys busy in the coming months if owners start selling their portfolios of rent-stabilized buildings now that the Act has upended their business strategy. Management companies will also be kept busy with producing rent records when a potential purchaser performs their due diligence to confirm that the seller has not been overcharging a rent-stabilized tenant.

Under the Act, potential purchasers of rent-stabilized properties need to be more diligent than ever when reviewing rental history as part of the purchaser's due diligence. The Act replaced the four-year look-back period with a six-year period, which means an owner may be liable for up to six years of overcharge refunds, rather than four years under the old law. Additionally, if the owner is found liable for a willful overcharge, treble damages are now owed to the tenant for six years, rather than two years under the old law. The Act now also permits a tenant to recover attorney's fees, costs, and interest if the owner is found liable for an overcharge.

Owners who are not currently considering selling should nevertheless take a second look now at their portfolio's rental history and supporting records to assess the owner's potential exposure for successful overcharge complaints. Doing so not only provides the owner peace of mind, but will also make the portfolio more valuable after a showing that it is a well-managed building with little to zero exposure. Owners can be assured that their tenants, or their tenants' attorneys, are already contemplating review of the owner's records for their own peace of mind.

An owner that wishes to review its records should only do so with an attorney. Not only should the attorney have the ability to advise the owner on salient legal issues newly created by the Act, but reviewing the owner's records with an attorney enhances the protection of the analysis in the event litigation is brought against the owner in the future.

The Act will not likely be the end of tenants' rights reform; but rather, just the beginning. Owners of commercial real estate in New York should keep this in mind when evaluating the value of real estate transactions in New York City going forward since the Act is a drastic departure from current law and will undoubtably impact commercial real estate transactions in New York City for the foreseeable future.

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YuhTyng ("Tyng") Patka joined Duval & Stachenfeld LLP in 2019 as chair of the NYC Real Estate Tax and Incentives Practice Group. Ms. Patka represents NYC real estate owners and developers on all aspects relating to real estate taxes. She represents owners in challenging their property taxes (certiorari), developers in NYC tax incentive programs (421-a, ICAP, FRESH), and not-for-profits in obtaining real estate tax exemptions.

Ms. Patka's practice also includes representing developers in the acquisition/disposition of Inclusionary Air Rights and handles Voluntary and Mandatory Inclusionary Housing applications. Additionally, Ms. Patka works closely with Duval & Stachenfeld's industry leading Opportunity Zone Practice Group and NYC Climate Mobilization Task Force.

Ms. Patka's representative matters include:

- Representing a developer in the acquisition of 23,000 square feet of inclusionary air rights for a mixed use project
- Performing due diligence on behalf of a private equity lender on a project participating in the Voluntary Inclusionary Housing program
- Representing a not-for-profit charter school in obtaining a not-for-profit real estate tax exemption
- Providing an opinion letter in the sale of a $150M project on the project's eligibility under the Affordable New York (421-a) program

Prior to joining D&S, Ms. Patka was an associate at Tuchman Korngold Weiss Liebman & Lindemann, LLP as well as a large Long Island law firm where she was responsible for overseeing that firm's residential tax certiorari practice.

Ms. Patka is fluent in Mandarin Chinese.