November Surprises

There has been much talk about elections recently, but in New York, the elections that commercial real estate market participants are thinking about are the state and local elections in November that could tangibly change the face of the city's multifamily housing stock.

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New York's rent-regulation laws do not come up for renewal until next spring but that is not stopping the topic from being front and center right now.

Tenant advocates have been enthusiastically endorsing candidates that want to make rent-regulation laws even more pro-tenant than they are currently. The City Comptroller's office has produced a report that estimated that over 1 million low-rent apartments have been "lost" over the last 12 years and even the editorial board of a major local newspaper wrote a piece in September that called on New Yorkers to vote for candidates who would support anti-property-owner policies and laid out several aspects of rent regulation that should be changed in the name of keeping housing affordable. Additionally, the New York City Council passed eight resolutions earlier this year that would end policies that have helped owners maintain the quality of the city's housing stock.

In recent decades, legislative headwinds have been a concern for players in the regulated multifamily sector in New York. Narrow majorities for Republicans in the State Senate, whether they were actual majorities or majorities created by the Jeff Klein-led IDC (Independent Democratic Conference) which voted with the Republicans, led to owners losing ground but not nearly as extensively as would have been lost otherwise. This year, Klein lost his primary, and control of the Senate looks like it may change hands.

The issues in jeopardy include ending high-rent vacancy decontrol, ending the 20 percent vacancy bonus, ending preferential rent bonuses, making the individual apartment improvements (IAI) and major capital improvements (MCI) bonuses temporary and overturning the Urstadt Law which transited control of regulation to the state from the city. Keeping these policies in place is critical for preserving the quality of our housing stock. The rationale for implementing these changes appears to be misguided.

The comptroller's report grossly overestimates the "loss" of low-rent units which included units where rents rose even just a few cents over the $900-per-month threshold and the overwhelming majority of those units are still rent stabilized. In fact, the Rent Guidelines Board tracks regulated units and, according to them, from 1994 to 2017 the net negative change in the number of rent-stabilized units has been a loss of just 12,000 units.

The entire premise that rent regulation is an affordable housing program is inaccurate and a favorite sound bite for politicians. Rent regulation is an inertia program that rewards tenants who remain in their apartments and has no means of testing associated with it. Rent regulation, in its present form, leads to a severe misallocation of our housing stock.

Being able to use aspects of the present law to increase rents that are well below market levels is important as rents in regulated apartments do not come close to keeping pace with expenses. Real estate taxes, which are supposed to be pegged to market value, go up every year even if property values fall as they did by an average of 38 percent from 2007 to 2010. And the basket of expenses that the Rent Guidelines Board uses to determine regulated-rent increases has not been updated to take into consideration the hundreds of new codes.

In the 1970s, rent increases fell short of expense increases, which led to significant deferred maintenance, tax foreclosures and abandonment. Some owners opted to burn their buildings down for insurance proceeds. I'll always remember Howard Cosell saying, "Ladies and gentlemen, the Bronx is burning," during his broadcast of the 1977 World Series as a shot from the Goodyear blimp panned the surrounding neighborhoods that were ablaze. Subsequent to these disastrous times, the MCI and IAI bonuses incentivized unprecedented private-sector investment into the housing stock. According to the Real Estate Board of New York, the percentage of renter-occupied dilapidated units has dropped from 4.16 percent of the stock in 1981 to just 0.2 percent in 2017. Making the MCI and IAI bonuses temporary will curtail the capital investment that housing has so greatly benefited from.

Eliminating the 20 percent vacancy bonus would mean that supporters of this move believe that residents who earn approximately $110,000 to $135,000 per year should be protected under the law. And if the Urstadt Law is overturned, the same City Council that endorses many of these anti-owner positions, would have the ability to implement these harmful changes.

The headwinds this time around are real. After the November elections we will have a clearer picture of what is likely.