

Submitted



RENT STABILIZATION ASSOCIATION • 123 William Street • New York, NY 10038

**JOINT LEGISLATIVE PUBLIC HEARING ON
2019-2020 EXECUTIVE BUDGET PROPOSAL: HOUSING**

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This testimony is submitted today on behalf of the 25,000 members of RSA who own or manage approximately one million apartments in the City of New York.

The apartment building owners and managers who belong to RSA are a diverse group. The popular perception is that the typical members own or manage a significant number of apartments, with a staff of professionals guiding them through the complex world of property management in the City. That perception is wrong. The reality is that the vast majority of our membership owns less than 50 apartments, many of whom work day jobs and then clean the halls and maintain their buildings at night and on their days off. As with any other owner, they rely upon the profits generated by their rents to pay their ever-increasing property taxes and water and sewer charges, to make improvements and to pay for all of the other costs that are associated with maintaining and operating an apartment building.

The nationalities, ethnicities and races of these owners represent the entire globe, and for many of them, they and their families have cobbled together the funds to purchase a small building and to gain a foothold on the ladder of the American dream. The bottom line is that property taxes- which typically amount to 30% of a building's operating costs- paid by these property owners increase rents paid by tenants, negatively impact the ability of owners to maintain their buildings and fund the ongoing expansion of social welfare programs in the City of New York. There is no question that any efforts to dramatically change the rent regulatory laws will impair the economic value of regulated properties and the ability of owners to maintain and operate their buildings.

The simple fact is that the rent increases authorized by the Rent Guidelines Board have never compensated owners fully for their actual increased costs. It is only by virtue of the other forms of allowable rent increases that owners can begin to close the gap between their rent roll and their actual costs. Without the increases and incentives built into the current system, the numbers speak for themselves- owners will neither be able to pay their ever-increasing share of the property tax burden nor appropriately maintain and operate their buildings. The consequences not only for owners but for their buildings, their tenants and the City itself will be disastrous. The history of the City of New York, whether in the form of a ravaged South Bronx in

the 1970's and 1980's or neglected NYCHA buildings more recently, are proof positive that history can repeat itself.

In the name of affordability, an assortment of measures that have been proposed to amend the rent laws, including proposals to eliminate high rent deregulation and to eliminate or restrict the long-existing economic incentives for owners to invest in their buildings. The reality is that while these measures would have nothing less than a punishing impact upon property owners, especially smaller owners, they would do nothing for those tenants struggling with affordability. Even if all of the measures that have been proposed would be enacted in their most extreme form, not one tenant would benefit one iota as those tenants continue their already existing struggle to pay their rent, put food on the table, and clothe their children. Instead, as the recent report by the Citizens Budget Commission demonstrates, these measures would further protect the wealthiest, not the poorest, of the regulated tenants.

Unfortunately, we are witnessing a lack of imagination and courage to create the sort of initiatives that would benefit tenants in need before they become homeless instead of after. Despite the \$3 billion currently spent by the City on the various homeless housing programs, it seems easier to scapegoat apartment building owners and make them bear the brunt of this legislative payback for their unprecedented investments in the housing stock over the past 25 years.

The specific proposals that are at issue are the following:

1. The repeal of high rent deregulation.
2. The repeal of the so-called preferential rent law.
3. Restrictions or elimination on building-wide major capital improvement rent increases
4. Restrictions on individual apartment improvement rent increases.
5. Restrictions or elimination of the statutory vacancy allowance.

High-Rent Deregulation: Notwithstanding popular belief, high-rent deregulation is not a new concept but existed for some time under the previous rent control system. It was re-established in 1993 and then took its current form in 1997. Deregulation has provided the one semblance of logic in an otherwise illogical system of rent regulation where there is no correlation between the rent protections afforded by regulation and a tenant's financial means. With the adoption of deregulation, the Legislature recognized that at some point, the rents paid by tenants were not worthy of being regulated because of the financial means of the tenants who could afford such high rents and because of the high vacancy rates at those rent levels. The legal premise of the rent regulation system is based upon a housing emergency which the State Legislature determined should be predicated upon a 5% vacancy threshold. In the City, the vacancy rate for apartments with rents above \$2,000 per month is 7.42%. Under current law, the deregulation threshold is about \$2800 per month, which means we are providing rent regulatory protections for a tenant who can afford to pay almost \$34,000 a year in rent. And this is for a category of apartments where the vacancy rate at the rent level above \$2500 is 8.74%. At a time when more

attention- and more public resources- than ever should be dedicated towards assisting those in need, someone should be asking why tenants who can afford to pay \$2800 each month should receive such protections.

Preferential Rents: Prior to 2003, on its own initiative and without any statutory authority, DHCR required that once an owner charged a regulated tenant an amount less than the legal regulated rent- a so-called "preferential rent"- the owner was prohibited from increasing that rent by any amount other than by RGB and MCI increases. In other words, the owner was punished for charging the tenant less than what the owner legally could have charged the tenant. Ultimately, the courts invalidated this policy and, in 2003, the Legislature enacted the currently existing statute. The use of preferential rents is now commonplace. Over 30% of all rent stabilized leases- approximately 250,000 apartments- involve a preferential rent. Charging a preferential rent allows owners and tenants to negotiate a rental amount which is mutually agreeable and allows owners to take note of an individual tenant's ability to pay a particular amount of rent at a particular point in time. This is, in fact, the ultimate goal envisioned for the rent stabilization system—a normal market for the owner and tenant to arrive upon a mutually agreeable rent. Tenant advocates regularly assert that preferential rents provide a mechanism whereby owners entice new tenants into signing vacancy leases only to evict them thereafter by raising the rent; the reality is that this is not the case. However, to address that concern, in 2015 the rent laws were amended so that the amount of a vacancy allowance increase was phased in after a preferential rent was charged, rather than the full 20% that would otherwise be allowed.

Despite those claims, the facts speak for themselves:

1. 90% of preferential rents in a given year remain preferential the following year
2. The median increase for renewal leases for tenants with preferential rents is just 1.8%, bringing the median rent to \$1,440
3. For vacancy leases for a preferential rent apartment, the increase was just 7%, bringing the median rent to \$1,850
4. The median rent for all preferential rent apartments in 2017 was \$1,499.

Major Capital Improvements: Major capital improvements (MCIs) are the lifeblood of a housing stock which largely pre-dates World War II. The need for new heating systems, roofs, facades, windows and other components of apartment buildings continue as capital improvements are required in a housing stock which, on average, is 75 years old. The current system highly regulates the process by which rent increases can result from these improvements. Each building component is assigned a useful life in a schedule issued by DHCR, ensuring that these components are not replaced prematurely. To obtain rent increases for these improvements, owners must submit to DHCR lengthy, detailed applications detailing the work performed, the amounts paid, and other relevant information. Only after notice to the tenants, along with their opportunity to participate in the process, can a rent increase be approved, which is then subject to further challenges at the agency and in the courts. Even if approved by DHCR, the formula, as revised by the Legislature in 2015 to lengthen the amortization period (currently, 8 years for

buildings with less than 36 units and 9 years for buildings with 36 or more units) and, further, the rent increase is capped to minimize further the impact on the existing tenants. MCI increases are often covered by various programs in which lower income tenants participate, such as SCRIE, DRIE and Section 8. Further restrictions on MCIs, especially the proposal that such increases be a temporary surcharge rather than a permanent rent increase, would doom a program that has sustained an aging housing stock for decades.

Individual Apartment Improvements: Individual apartment improvements (IAIs) are the primary mechanism by which owners can keep their apartments marketable in an increasingly competitive environment, particularly given the age of the typical rent regulated apartment and given the typically lengthy occupancy by a rent regulated tenant. While an owner, technically, can update kitchens and bathrooms during a tenant's occupancy, the tenant's consent is needed for the owner to increase the rent. Therefore, upon vacancy, owners often replace kitchens and bathrooms and make other improvements and increase the rent in accordance with the statutory formula ($1/40^{\text{th}}$ of the cost for buildings with less than 36 units; $1/60^{\text{th}}$ of the cost for buildings with 36 or more units). The fact that owners make these individual apartment improvements, as well as major capital improvements, is the reason why the United States Census Bureau reports that the housing stock is in the best overall condition since the Bureau started to track this data decades ago. As with MCIs, eliminating or curtailing IAI rent increases would substantially limit the ability of owners to maintain their buildings and would result in inferior living conditions for tenants.

Statutory Vacancy Allowance: The statutory vacancy allowance was enacted as part of the 1997 rent laws and reflected the fact that (a) due to political pressures, renewal lease increases authorized by the Rent Guidelines Board failed to compensate regulated owners for their actual increases in operating costs and (b) the rent increase resulting from the vacancy allowance would be borne by the next tenant in occupancy, who would be in the best position to determine whether the new rental amount was affordable to them. The necessity for the statutory vacancy allowance has never been greater, as stabilized rents in the City have effectively been frozen in the past few years due to the RGB's decisions either to approve either no increases or only nominal ones at best. In response to arguments by tenant advocates that regulated owners somehow abuse this rent increase mechanism, in 2011 the Legislature limited vacancy allowances to one per calendar year and, as noted above, where a preferential rent is charged on a vacancy lease, the statutory vacancy allowance is phased in over the following four years in the event of another vacancy during that time period.

Economic Impact on the City's Economy: The rent increase mechanisms discussed above all function in their individual ways to create an artificial economic construct that does two things: limit rent increases for tenants while also trying to ensure sufficient cash flow for owners to maintain and improve their properties.

But the effects of this system go far beyond the immediately affected tenants and owners to also affect the growth and vitality of New York City neighborhoods and its residents, as well as the overall health of the City's economy.

In 2018, for example, property owners spent **\$13.3 billion** to maintain and improve rent stabilized properties resulting in a total economic impact of **\$22.4 billion**. To put this number into perspective, the economic activity resulting from expenditures by owners of rent stabilized property is equal to more than 25% of the City's \$72 billion budget for 2018, and includes **\$3.7 billion** in real estate taxes paid directly to the City to hire cops, firemen and teachers.

Overall, owners of rent stabilized properties supported more than **180,000 jobs** in 2018 with an average salary of \$62,300, which generated nearly \$12 billion in total income. A majority of these jobs support neighborhood residents who are primarily people of color.

These facts and figures should make it clear that the rent stabilized housing industry is a critical engine powering the City's economy. This industry has maintained and improved the City's oldest housing stock, bringing living conditions to the best ever; it has been part and parcel of the revitalization of neighborhoods left derelict for decades; and it has provided tax revenue that has allowed the City to pursue initiatives that have made New York the most progressive city in the country.

This source of jobs, vitality and income is now threatened by dramatic changes whose results are, at best, unknown and, at worst, catastrophic.

Rent regulations have been in place in New York City for more than 75 years and have undergone significant modification over that time. But the most extreme changes proposed now would re-fashion the industry in an untried and unpredictable manner which threatens the economic vitality of the City, its buildings and its residents.

We welcome the opportunity to work together with the New York State Legislature to craft any necessary changes to the rent laws that will continue to meet the dual goals of protecting tenants while allowing apartment building owners to continue providing quality, affordable housing.

