REBNY
REAL ESTATE BOARD OF NEW YORK

Testimony | April 29, 2021

The Real Estate Board of New York
Regarding Rent Increase Guidelines for 2021-2022

The Real Estate Board of New York (REBNY) is the City's leading real estate trade association representing commercial, residential, and institutional property owners, builders, managers, investors, brokers, salespeople, and other organizations and individuals active in New York City real estate. REBNY strongly supports policies that expand the local economy, grow, and improve the City's housing stock, and create greater opportunities for all New Yorkers. Thank you to the Rent Guidelines Board (RGB) for the opportunity to provide our perspective regarding rent adjustments for the city's rent-regulated apartments.

We acknowledge that the 2021 Rent Guidelines Board PIOC (Price Index Operating Costs) study found that increases between 2.0% - 2.75% for one-year leases and 2.4% - 5.75% for two-year leases are required to maintain owners' current dollar Net Operating Income. In light of the significant flaws in the RGB's methodology as noted in our testimony below, and historical misalignment between RGB increases and rising expenses, we must provide a recommendation accordingly. **REBNY recommends a minimum of a 3.9% increase for one-year renewal and initial leases, commensurate with the weighted increase of expenses dedicated to property taxes.**

Only Federal Aid, Not a Rent Freeze, Can Address Tenants' Needs

The scope and scale of the COVID-19 crisis is one that can only be adequately addressed by federal resources. The National Multifamily Housing Council (NMHC)'s Rent Payment Tracker found 79.8% of apartment households made a full or partial rent payment by April 6 in its survey of 11.6 million units of professionally managed apartments across the country, as compared to 82.9% pre-pandemic. NMHC has been tracking payments throughout the pandemic. Their reporting found a direct correlation between the improvement of payment rates and tenants receiving direct federal assistance, whether that was through increased unemployment or stimulus funds. Likewise, the U.S Census Bureau Pulse Survey found that 80.2% of renters were currently caught up on rent payments, according to the most recently available data from the week of March 17-29, 2021.

These findings at the national level are comparable with what has been reported at the local level. In a report analyzing rental payments, The Furman Center found that total rent arrears increased following both the beginning of the crisis and the expiration of extended federal unemployment benefits at the end of July. Furman also noted a concern for owner ability to pay mortgages and operating expenses given these drops in revenue.

REBNY has been an tireless advocate for New York City at the federal level pushing for business interruption programs, state and local aid, reforms to expand the paycheck protection program, and an emergency rental assistance program. REBNY members were the first to pledge a 90-day moratorium on evictions, enter into voluntary rent repayment plans, and in partnership with members from the New York Association for Affordable Housing (NYSAFAH), founded Project Parachute.

[Project Parachute] is a philanthropic initiative, administered by [Enterprise Community Partners,] that seeks to help the most vulnerable New York City renters remain in their homes during and in the aftermath of the Coronavirus crisis. The tenant-facing portion of Project Parachute known as FASTEN (Funds and Services for Tenants Experiencing Need) began case management in the fall of 2020. As of this month, under FASTEN, Project Parachute has provided support to **over 1,600 individuals, with $2.6 million in rental arrears has been requested.** Importantly, the program is reaching those who were not otherwise eligible for government assistance - 87% of the served households are undocumented households and over 50% are single adults. Importantly, as most stimulus dollars and existing programs identify prior housing instability as a criterion for relief, over 80% of the households served under FASTEN would be deemed ineligible for traditional voucher assistance as they have no documented shelter history.

FASTEN has provided key lessons, including the need for trust building and leveraging partners for referrals for assistance. As part of Project Parachute, REBNY has joined with diverse stakeholders including representatives from Enterprise Community Partners, the Legal Aid Society, Homeless Services United (HSU), Court Appointed Special Advocates for Children (CASA), and NYSAFAH to develop upstream solutions to prevent evictions.

If the Board is looking for a villain in tenant hardship, it is the pandemic they should be looking to. Zero percent increases cannot solve for tenant hardship and existing rent burden or accrued rental arrears. It certainly won't solve for keeping buildings habitable, safe and in good condition over the long run.

The RGB's Methodology is Flawed

The 2019 data is not just irrelevant because of the pandemic, but because there was a seismic law change in the passage of the Housing Stability Tenant Protection Act of 2019 (HSTPA). The HSTPA included the effective wholesale elimination of increases beyond those provided for by the Rent Guidelines Board for renewals and initial leases. There are no more vacancy allowances, severe curtailment of Major Capital Improvements (MCI) and Individual Apartment Improvements (IAI), which quite frankly only affected less than 1% of units a year, the elimination of luxury decontrol, and the elimination of changes to preferential rents within a tenancy. As a result, the burden to maintain quality housing amid escalating costs falls solely on the RGB via annual rent increases. This is especially true for 100% rent stabilized buildings who cannot rely on cross subsidization from their commercial tenants in better years or from the market rate units.

As we have previously shared with the Board, an analysis by HR&A Advisors, Inc. suggested that the HSTPA could dramatically change the economic viability of the operations and maintenance for apartment buildings across the city. Their analysis estimated that within 5 years, approximately 272,000 units could be financially distressed and unable to afford any investment beyond basic maintenance, taxes, and utilities. Already, we have seen a roughly 48% drop in the number of alteration filings in rent stabilized buildings from 2018 to 2020, and an approximately 17% decrease between 2018 and 2019. It is not surprising that these decreases in investment have been accompanied by three consecutive years of increasing numbers of distressed buildings according to the Board's 2021 Income and Expense Study. To keep buildings in good physical condition and budgets balanced, this Board must take accountability for their role in keeping these buildings financially and physically viable, especially given the new regulatory framework.

Data used by RGB staff to calculate Net Operating Income (NOI) is incomplete and inaccurate. An outdated 28-year-old analysis by RGB and the Department of Finance (DOF) is used as a basis for adjusting expenses downward 8%. Similarly, costs of building façade maintenance, increased elevator inspections, lead paint abatement, and any other government mandates imposed since the Price Index was last updated 36 years ago are not considered by the Board.

Further inflating reported NOI is the universe of buildings that the RGB studies. The RGB excludes data on smaller 1–10-unit buildings that leaves nearly 16,000 fully stabilized buildings unaccounted for, while simultaneously including predominantly market rate buildings with abated property taxes through programs such as Affordable New York or larger buildings that may only have a handful of stabilized units.

The RGB Increases Do Not Keep Pace with Expense Growth

With 71% of the rent stabilized housing stock built prior to 1947, maintenance and operational costs are a fact of business, with a regular cycle of necessary major system overhauls like gas, electricity, water, boiler, elevator, and roof replacements. It is unsurprising to see increases year over year in operating expenses. According to the RGB's Income and Expense report, operating costs increased 3.3%. Additionally, the 2019 data shows that property taxes continue to comprise the largest share of owner expenses, averaging 31.2% of all costs among rent stabilized buildings. From 2018 to 2019, the average monthly expense per dwelling unit paid toward taxes increased 6.05% and have more than doubled since 2007.

However, as we know, the RGB's methodology utilizes expense data from 2019, meaning that these figures do not capture increases in operating expenses due to COVID-19 protocols. Initial evidence indicates that expenses continued to rise during the pandemic, with reports of price gouging on cleaning supplies and personal protective equipment impacting tenants and property owners, their employees and property managers alike. During this time of crisis, property owners have gone above and beyond in meeting their responsibility of providing quality and safe housing for their residents. They continue to and must find ways to cover the increased costs for utilities and maintenance, along with continuing to pay property taxes based on pre-pandemic assessments and collection rates. Additionally, at a time in which many of us are at home, building owners have worked to ensure buildings are safe, clean, and responsive to the COVID-19 pandemic, often at significant expense.

While property owners tackle the challenges of decreased occupancy rates, decreased rent collections and increased costs due to COVID-19, while providing and maintaining quality housing, they must also abide by additional regulatory requirements that do not qualify as an eligible expense under the curtailement of the MCI and IAI programs. As an example, to achieve our shared climate goals, more buildings need to contribute to energy reductions and efficiencies. As of last year, Local Law 97 now applies to buildings containing rent stabilized units that are less than 35% stabilized. These buildings must conform to a law that invokes additional expenses that are not subsidized and cannot be captured through rent increases. Failure to comply will result in fines. This regulatory burden is not captured in the analysis by the Board.

The RGB Should Use a Formula-Based Approach

The changes incurred by the HSTPA created a new regulatory normal, the consequence of which is that the RGB is effectively solely responsible for determining whether rent increases will cover rising expenses, and in turn whether there is sufficient NOI left for ongoing maintenance and improvements. The future of the City's rent stabilized housing stock is in the RGB's hands.

This reality is not unexpected, and was foreseen by academics, including those at the Furman Center, who wrote prior to the passage of the HSTPA, that "eliminating rent increases that reflect investment (including Major Capital Improvements and Individual Apartment Improvements), could cause the Board to account for these costs with higher across-the-board, basic rent adjustments...the need for investment in improvements is conditional on building-level factors, such as physical condition of a building, and an owners' access to capital. Thus, without some form of MCI's and IAI's, the Board may need to account for those costs when fulfilling its constitutional obligation to provide a fair return."

The rapid adverse changes COVID-19 wrought on the market and housing landscape lend additional credence to serious consideration for moving to a new standard formula that inputs various indices for generating RGB increases that can operate independent of political machinations and in real time. A two-year lag in data is unacceptable most years, and more so today.

We therefore continue to believe there are merits to a formula system and therefore suggest a formula that encompasses the following: CPI and wage growth; property taxes, unfunded regulatory requirements, subsidized regulatory requirements; labor; maintenance; insurance; administrative costs; capital investment needs; debt service; and utilities such as energy, water/sewer, and fuel. This would follow other jurisdictions with a similar system and keep focus on adjustments commensurate with operating costs and inflation.

Conclusion

This Board's responsibility is to provide increases that allow for maintenance of quality housing for millions of New Yorkers. We appreciate that raising rents on tenants seems like a losing proposition, and even a formula would not address this concern. The RGB operates within a broken system that places the role of subsidizing housing regardless of whether the tenant is in need, wholly on the private sector, and places the financial cost of rising expenses inclusive of property taxes, whether they can afford to or not, on the tenant.

What the government policies in this pandemic, and our own lessons from the involvement in Project Parachute has shown us, is that direct, targeted interventions make the biggest differences to tenants in need and struggling to pay rent. Direct assistance to owners for public goods also have a track record for improving outcomes – in this case building quality without relying on rent increases to cover the difference in capital expenses. Programs like J51 should and must be reformed to do this role, to make it financially feasible to bring buildings into 21st century and to also meet sustainability goals. In 2017, building quality was at highest level in decades. That is not sustainable with de minimus increases.

Rental income and capital investment are the lifeblood of rental housing. To change this paradigm in a manner that ensures affordability for tenants without sacrificing building quality will require another seismic shift in political discourse– a regulatory landscape that recognizes property tax revenue will power social programs, that direct assistance to tenants in need while they are already housed provides stability and is effective eviction protection, and to keep rents affordable without sacrificing building quality abatement programs are necessary.

Maintaining the housing ecosystem in a way that balances all stakeholders should be the goal of an administrative body. For multiple years, this Board under this administration has weighted tenant needs over rising expenses—with the biggest driver of those expenses being increases to City property taxes. This deficit was previously balanced by other statutorily available revenue streams beyond RGB annual increases. Now that the State has eliminated those revenue streams with the passage of the HSTPA, the role of the RGB is more critical to maintaining the economic viability of the City's rent-stabilized apartment stock, which is already in decline, the extent of which is not captured by the RGB due to methodological challenges.

The 2021 Rent Guidelines Board PIOC (Price Index Operating Costs) study found that increases between 2.0% - 2.75% for one-year leases and 2.4% - 5.75% for two-year leases are required to maintain owners' current dollar Net Operating Income. **REBNY recommends a minimum of a 3.9% increase for one-year renewal and initial leases, commensurate with the weighted increase of expenses dedicated to property taxes.**

It is appreciated and appropriate that the guidelines last year applied to both renewal and initial leases, recognizing the expenses that occur at turnover due to several regulatory provisions related to health and safety, including lead abatement and painting that are not permitted as an IAI expense. The majority of apartments do not utilize preferential rent and absent a guideline applying to initial leases will not have a chance till 2023 to even recoup a portion of those required costs, which may now include heightened cleaning procedures related to COVID-19. We encourage this precedent to continue.

The City has been experiencing an affordability crisis that impacts hundreds of thousands of New Yorkers both in and out of rent stabilized housing for decades. We will also not know the full impact of COVID-19 for some time. What we do know is that direct assistance will do more for rent burden and rental arrears than blanket policies that address neither. We also know that property taxes help significantly fund the programs that can be most impactful. We encourage the board to adopt guidelines that support high-quality rental stock and allow for property owners to meet their financial obligations to maintain a functioning housing ecosystem. Again, government policies can intervene for good; and at minimum, should not cause additional harm.

Thank you to the members of the Rent Guidelines Board for considering our testimony.

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