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Recent Developments in Roberts v. Tishman Speyer and Their Effect on Luxury Decontrol

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As part of the Firm's ongoing review of legislation and case law which may affect our institutional lending clients, we have been monitoring the case discussed below since the initial decision in 2007. Recent developments in the action have addressed whether the Court of Appeals' holding in its 2009 decision would be applied retroactively as well as prospectively. This update discusses the First Department's November 2011 decision which answers that question, at least for now. If after reviewing this update you have any further questions or comments, please feel free to contact Chris Palmer cpalmer@cullenanddykman.com or Tom Baylis tbaylis@cullenanddykman.com .**

Introduction

In January 2007 in an action entitled *Amy L. Roberts, et al v. Tishman Speyer Properties, L.P.*, a group of current and former tenants of apartments in the Peter Cooper Village/Stuyvesant Town Complex commenced a putative class action in the Supreme Court, New York County. Their claim was that their apartments, which had been subject to the protections afforded by the Rent Stabilization Law (Administrative Code of the City of NY, tit 26, ch 4), had been improperly deregulated pursuant to the luxury decontrol provisions of the Rent Stabilization Law. More specifically the case involved the interplay between the luxury decontrol provisions of the Rent Stabilization Law (Administrative Code of City of NY §§ 26-504.1 and 26-504.2) and New York City's J-51 tax abatement program (Administrative Code § 11-243 [formerly § J-51]). Stated simply, does a unit in a building which participates in the J-51 program remain subject to rent stabilization if the unit would otherwise be decontrolled pursuant to the luxury decontrol provisions of the law? At stake was not only the prospective application of rent regulations on the apartments but also the recoupment of alleged rent overcharges of more than $200 Million.

Background

The Peter Cooper Village/Stuyvesant Town Complex (the "Complex") was developed in the 1940s by Metropolitan Life Insurance Company ("Met Life") to provide affordable housing in Manhattan for middle-income families. The complex consists of 110 apartment buildings comprising 11,200 units and houses more than 20,000 people.

As the Complex was being built Met Life entered into an agreement with the City of New York pursuant to the New York Redevelopment Companies Law, which is now codified as Article V of the Private Housing Finance Law (PHFL), which provided Met Life with assistance including a real estate tax exemption for 25 years. In 1974, as that exemption was coming to an end, the New York State Legislature enacted an amendment to the Real Property Tax Law which provided that upon expiration of the 25-year tax exemption, real property taxes payable on the complex would be phased in over a 10-year period, and, in connection therewith, the apartment units in the complex would become subject to the New York City Rent Stabilization Law. In 1992, Met Life applied for and began receiving property tax benefits under New York City's J-51 tax abatement program which provided incentives for owners to rehabilitate and improve their buildings. It is the interplay between those programs which is the background for the present lawsuit.

The LItigation

In their complaint, plaintiffs alleged that more than 25% of the Complex's units, some 3,000 apartments, had been illegally deregulated under the high rent/high-income decontrol provisions of the Rent Stabilization Law because those same provisions specifically prohibit deregulation during the period in which the owner is receiving J-51 tax benefits. Plaintiffs seek, among other things, recovery of rent overcharges for the four years preceding commencement of the action, attorney's fees, and a judgment declaring that their apartments are subject to the Rent Stabilization Law and that all the apartments in the Complex will continue to be subject to rent stabilization for the duration of time in which defendants receive J-51 tax benefits.

Defendants moved to dismiss the complaint. The defendants argued that the prohibition against deregulation for apartments enrolled in the J-51 tax benefit program applies only to those apartments that are rent stabilized solely because of J-51, and that apartments that were already rent stabilized when they were enrolled in J-51 may be luxury decontrolled prior to the expiration of, and despite the fact that the owners are continuing to receive, tax benefits. In support of their argument, defendants relied on the New York State Department of Housing and Community Renewal's ("DHCR") regulations, as well as DHCR Fact Sheet 36, together which stand for the proposition that the exception to luxury decontrol for properties receiving J-51 tax benefits only applies when an apartment is subject to rent stabilization "solely by virtue of" the receipt of J-51 tax abatements (see Rent Stabilization Code [9 NYCRR] §§ 2520.11[r][5][i], [s][2][i]).

The court, by Hon. Richard B. Lowe, III, granted defendants' motion in a decision and order dated August 16, 2007. In doing so, the court adopted the DHCR's view that the term "by virtue of" means for "the sole reason" of and concluded that since the Complex became subject to "rent stabilization in 1974 pursuant to the PHFL, 18 years before applying for J-51 tax benefits, defendants did not become subject to rent stabilization [solely] by virtue of receiving J-51 tax benefits." The court, noting that the Legislature neglected to amend the statute after the DHCR promulgated its regulations, concluded that the Complex is therefore not exempt from the high rent/high-income decontrol provisions of the Rent Stabilization Law, despite receiving J-51 tax abatements.

Plaintiff appealed that dismissal and the Appellate Division, First Department reversed the lower court's dismissal in a decision dated March 5, 2009 ("Roberts I"). In this decision, the First Department reversed the dismissal of the action and reinstated the complaint. Given the significance of the decision, the First Department certified the following question to the Court of Appeals: "Was the order of this Court, which reversed the order of the Supreme Court, properly made?" In an October 22, 2009 opinion ("Roberts II"), the Court of Appeals answered the question in the affirmative and affirmed the First Department's order reinstating the complaint. That, however, was not the end of the action or the inquiry.

AfterRoberts II, MetLife, which had sold the properties prior to the date the action was commenced, moved to dismiss the action as against it on the grounds that the decision should not be applied retroactively. In an order entered August 5, 2010, the trial level court denied MetLife's motion.

MetLife appealed that order to the First Department and that court affirmed the lower court's ruling in a decision dated November 11, 2011 ("Roberts III"). The court held that the decision in Roberts II was not a "new law" which is necessary for the court to hold that the ruling would be enforced prospectively only. The court found that because Roberts II construed previously existing statutes, even if it was for the first time, it established no new legal principle. Moreover, while Roberts II was not consistent with prior DHCR rulings, such rulings were not judicial decisions and were not entitled to the same deference and precedential weight as judicial decisions. Thus, unless the Court of Appeals reverses the First Department's recent ruling, or it is overturned by legislation, the ruling of Roberts II will be applied retroactively.

Impact of Decisions

The holding of Roberts I, II and III affect not only the parties to those actions but to similarly situated landlords with buildings with decreased rent rolls, diminished ability to service debt and lowered appraised values. Roberts III adds to that the possibility of having to refund large sums of money previously collected as rent on buildings they may not even own anymore. Clearly, these concerns also affect how lenders underwrite and appraise applications for mortgage loans secured by such properties.

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