

## **New York City Local Law Enacted to Maintain Assisted Rental Housing**

**By: Michael J. Berey, Senior Underwriting Counsel and Senior Vice-President, and Stanley B. Blumberg, Special Counsel, First American Title Insurance Company of New York**

**On August 17, 2005 the New York City Council, overriding the Mayor's veto, enacted Local Law 79 of 2005, adding Chapter 9 ("Right of First Refusal and First Opportunity to Purchase") to Title 26 of the City's Administrative Code. The provisions of the Local Law, which has been referred to as the "Tenant Empowerment Act", went into effect on November 15, 2005. A copy of the Local Law may be located on the City Council's Web Site [1] by entering the number of the Local Law and its year of enactment.**

**The purpose of the Local Law is to maintain multi-family rental housing which is "assisted rental housing" as "affordable housing". The Local Law defines "assisted rental housing" to be a privately owned multiple dwelling in which the majority of dwelling units are subject to governmental eligibility restrictions and in which the rents are controlled, regulated or assisted by the government pursuant to a regulatory agreement or rental assistance agreement. Specifically included within the definition of "assisted rental housing" is property (i) owned by a Limited-Profit Housing Company under Article II of New York State's Private Housing Finance Law ("PHFL"), first occupied on or after January 1, 1974, (ii) owned by a Limited Dividend Housing Company under Article IV of the PHFL, first occupied on or after January 1, 1974, (iii) receiving rental assistance provided under Section 8 of the National Housing Act of 1937, or (iv) having the benefit of certain housing programs under certain Sections of the National Housing Act. [2] Property with assisted rental housing which is owned by a PHFL Article II entity is commonly known as "Mitchell-Lama" housing.**

**'Affordable' is defined in the Local Law to "mean that rental expenses for dwelling units do not exceed thirty percent of the annual gross household income of the existing tenants, and/or where rental expenses do not exceed the rent levels allowable pursuant to rent restrictions applicable to such dwelling units prior to conversion.." A "conversion", under the Local Law, is an action taken by an owner which would result in the owner terminating its participation in an assisted rental housing program.**

**The City Council acted in response to concerns that an owner of property providing affordable housing, on the expiration of the statutory period within which its property is required to be maintained as affordable housing, will "convert" the property, enabling an end to the program contract providing for rent subsidies, so that rents can be raised. To "convert", or "privatize", the owner will prepay the subsidized mortgages which financed the project or opt out of the applicable federal rent subsidy programs. Where appropriate, the owners can also sell the project or convert the property to cooperative or condominium ownership. In the case of mutual housing companies, there is an opportunity to convert to a non-supervised form of cooperative ownership and thereby enable the unit owners to keep the profits on the sale of units.**

**To privatize, the property owner-developer must comply with specific rules and regulations promulgated by DHCR or HPD, as applicable to the property. The procedures to privatize requires, among other things, notice to tenants, public hearings, and notice to the supervising governmental agency.**

**Article II of the PHFL, the "Limited-Profit Housing Companies Law, also known generally as the "Mitchell-Lama Law", was enacted in 1955 to induce private real estate developers to build and operate low and middle-income housing in the State of New York by offering them long-term, government-funded, low interest mortgage loans, together with real estate tax abatements and other financial benefits.**

**Mitchell-Lama projects may be found in various counties of New York State. In the case of projects aided by the State of New York, such as with mortgage financing provided by the Housing Finance Agency of the State of New York, they are generally supervised by the Division of Housing and Community Renewal of the State of New York ("DHCR"). Projects aided by The City of New York, such as with mortgage financing provided by the Housing Development Corporation ("HDC"), are generally supervised by the Department of Housing Preservation and Development of the City of New York ("HPD"). To a lesser extent, Mitchell Lama projects may be found in other localities which created their own redevelopment agencies utilizing DHCR procedures and regulations as their model.**

**Mitchell-Lama projects are either of a rental or cooperative nature. In the case of cooperatives, the cooperative corporation is designated a mutual housing company. The sale of cooperative apartments is regulated and any profit on the resale of a cooperative unit is paid over to the project.**

**Mitchell-Lama projects are regulated with respect to the criteria they apply to applicants for tenancies, their return on equity of investment, the rentals to be charged, repairs and replacements, the transfer of interests in the ownership of the projects and the manner of the "privatization" of a project after the number of years required by statute.**

**Within the City of New York and its proximate neighboring counties, Mitchell-Lama Projects constructed, developed and operated under Article II of PHFL, account for the preponderance of assisted rental housing programs.**

**On the privatization of rental property subject to Mitchell-Lama which is supervised by HPD all project reserves are payable to the City of New York. In the case of Mitchell-Lama rental property supervised by DHCR, a physical condition survey must be conducted as a condition to privatization and all mandated repairs must be made at the expense of the owner. In either case, however, upon privatization, the project or interests in its ownership may be sold and all proceeds, including profit, are retained by the Seller.**

**Article IV of PHFL deals with Limited Dividend Housing Companies and includes mutual housing companies, which are projects owned and operated by a cooperative corporation created pursuant to that Article. By statute and regulations these cooperatives are**

controlled as to carrying charges, the cost per share, and the ability to sell a unit and retain the profit. Overall, the program is intended to accomplish the same goals as in the case of Article II entities.

In addition, the Local Law encompasses project-based assistance under Section 8 of the United States Housing Act of 1937 and specified Sections of the National Housing Act. These programs include property as to which the United States Department of Housing and Urban Development ("HUD"), acting through the Federal Housing Administration ("FHA"), has insured the mortgages on the property and, as a result, the owner has entered into a Regulatory Agreement with the Secretary of HUD. The rental and operations of the property are regulated by both HUD and the local municipal and New York State regulatory and supervisory agencies.

Section 8 deals with a rental assistance funds made available to a project and its tenants based on the amount of rents that are payable by tenants. For example, the owner of the Section 8 building may have a direct contract for monthly payments from the FHA with respect to the total rent roll under which there is paid to the owner the difference between the amount of the rents payable by the tenants (reflective of the income limitations of the tenants) and the rent roll otherwise approved by FHA. Alternatively, specific vouchers may be issued to the tenants to supplement the rental amount otherwise payable by the tenant that the project owner will redeem.

In each of the assisted rental housing programs affected by the Local Law there is a common thread; the residential tenants in each of the projects benefits from a form of subsidy which reduces the rental obligation of the tenant.

Under the Local Law, when the owner of such rental assisted housing intends to effectuate a conversion, a "tenant association" or a "qualified entity" will be afforded a "first opportunity to purchase" and a "right of first refusal" to purchase the property. A "conversion", which triggers the rights of the tenant association or qualified entity under the Local Law, includes the "transfer of title, leasing, intention to sell or lease, mortgage pre-payment, withdrawal from an assisted housing program, decision not to extend or renew participation in the [rental assistance] program or any action taken by the owners that would result in the termination of participation by the owner in the assisted rental housing program".

A "tenant association" is defined in the Local law as "an association, whether incorporated or not, for which written consent to forming a tenant association has been given by tenants representing at least sixty percent of the occupied dwelling units within the same assisted rental housing". A "qualified entity" is defined as a person or entity experienced in the management of affordable housing, designated by at least 60% of the tenants in residence to act on their behalf, and approved by HPD, which obligates itself, and its successors in interest, to continue operating the property as affordable housing.

To exercise a "first opportunity to purchase", the tenant association or qualified entity will be required to purchase the property at or below its appraised value before conversion. To

**exercise a “right of first refusal”, the tenant association or qualified entity will be required to purchase the property at the higher of its appraised value or the amount offered by a bona fide purchaser.**

**The Local Law has complicated notice provisions, requirements for the obtaining of appraisals, and requirement for approvals to be issued by HPD. It must be determined that all procedural steps have been properly taken and that a tenant association or “qualified entity”, as the case may be, did not exercise the “right of first refusal” and/or “first opportunity to purchase”.**

**The Local Law also provides that on a conversion the owner or a bona fide purchaser is to allow each current tenant to remain in his or her dwelling unit for the longer of six months from the effective date of the conversion or until the tenant’s lease expires.**

**Regulations for the administration of the Local Law have not, as of the writing of this article, been issued by HPD. In addition, the Real Estate Board of New York, Inc., represented by Herrick Feinstein LLP, has commenced an action in the Supreme Court, New York County, against the City Council, The City of New York and HPD to have the Local Law declared invalid, null and void, alleging that the Law conflicts with state and federal statutes and is unconstitutional.**

**[1] <http://webdocs.nycouncil.info>**

**[2] Housing Programs governed by Sections 202,207, 221, 232, 236 or 811 of the National Housing Act, 12 U.S.C. Section 1701 et seq.**

**Published in the New York Law Journal on August 24, 2006**