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Six Years After Roberts Rent-Setting Uncertainty Continues to Loom

In 2009, *Roberts v. Tishman Speyer Props, L.P.*, 13 NY 3d (2009), sent shockwaves through the real estate community by effectively re-regulating tens of thousands of apartments. Six years later there has still been no guidance from either the Legislature or the Division of Housing and Community Renewal (DHCR) on how to recalculate legal rents in apartments that were deregulated under the pre-Roberts misinterpretation of the law. There have been attempts on the part of the courts to bring clarity to this issue, and a housing court judge did in fact devise a simple and consistent method—only to be subsequently reversed by an Appellate Division, First Department decision that gave rise to more questions than answers.

A recent court decision, however, may shed some light on the way legal rents are to be calculated in apartments that were impacted by *Roberts*. Although the decision leaves something to be desired in its explanation and reasoning, its ultimate holding is nonetheless useful as a guide. The case, *Ten Sheridan Assoc., LLC v. Cohen*, Index No. 151253/2014 (Sup. Ct., NY, 8/10/15), was commenced by an owner seeking declaratory judgment from the court approving its calculation of an apartment's legal rent that had been reregulated post-*Roberts*. The case arose out of a dispute with a tenant that refused to sign a renewal lease offered by the owner.

The tenant had taken occupancy of the apartment in December 2011 pursuant to a one-year rent stabilized lease. The legal rent was listed at $4,237 per month and a preferential rent was listed as $2,350. Upon renewal, the owner offered a lease with both the legal and preferential rents increasing according to the renewal guide- line adopted by the Rent Guidelines Board (RGB). The tenant opted for a one-year lease renewal term. Upon the second renewal, the owner increased the preferential rent by an amount greater than the RGB guideline. The tenant refused to sign the lease and disputed the owner's calculation of the rent, in essence claiming that the legal rent should be significantly lower—lower, even, than the preferential rent being charged. The owner commenced the instant action seeking verification of its rent-setting method.

In calculating the apartment's legal rent, the owner took the last regulated rent that qualified the apartment for deregulation in 2005 and added all vacancy and renewal increases that would have been applicable had the apartment been treated as stabilized during that period. The owner treated the rent charged to tenants during that time period as a preferential rent and recorded the higher legal rent on apartment registrations. To prove the validity of the recalculated legal rent, the owner pro- vided records dating back to 2005, including copies of contracts, invoices, and can- celled checks as evidence of individual apartment improvements (IAIs) performed at the time. The court also reviewed the entirety of the apartment's registration history. The court found that a long-term tenant had vacated the apartment in January 2005, and with IAIs and vacancy increases, the legal rent became $1,924. The next tenant entered into a lease commencing in March 2005 with a properly preserved preferential rent of $1,850. That tenant vacated in December 2005 and, pursuant to the one-year statutory vacancy increase, the legal rent surpassed the $2,000 deregulation threshold.

The owner believed the apartment to be deregulated and treated subsequent tenancies as such. Until 2010, when the owner entered into a vacancy lease for the first time post-*Roberts*. The owner treated that tenancy, and subsequent tenancies, as rent stabilized. That tenant vacated after one year, and the current tenant began occupancy in December 2011.

In determining the legal rent for the apartment, the court looked to the rent charged on the base date four years prior to the filing of the action—in this case, February 2010. The court then calculated the legal rent by taking the base date rent and adding all lawful subsequent increases.

In doing so, the court ignored the owner's reconstruction of the legal rent from the time of deregulation. The court's methodology resulted in a legal rent that was lower than what the owner calculated. Fortunately for the owner, the newly calculated legal rent was still greater than the preferential rent offered to the tenant, meaning that no overcharges could apply. The court did not opine, however, on whether the owner's lease renewal offer containing the now-incorrect legal rent—yet a valid preferential rent—was a proper offer under the law.

Although it was not discussed in the decision, an important detail to note in the court's calculation of the legal rent is that the waiver rule was not applied. Under the waiver rule, a lease that does not preserve the higher legal rent and only sets forth a lower collectible rent causes the owner to waive that higher legal rent. Accordingly, the legal rent for the next lease (vacancy or renewal) is calculated from the collectible rent stated in the prior lease. The court in this instance did not apply the waiver rule even though the leases in question did not preserve the higher legal rent.

That the waiver rule was not applied is a welcome development, as most DHCR decisions on this issue apply the waiver rule when a reconstructed legal rent is greater than what was actually charged to the tenant, but was not properly preserved in the lease. These instances most commonly arise when an owner deregulates an apartment under the pre-*Roberts* DHCR guidance in neighborhoods where the market dictates rental amounts below the deregulation threshold.

Although the court's decision did not explain why the waiver rule was not applied, it could be interpreted as an exercise of judicial discretion to prevent penalizing an owner for following the DHCR's misguidance on the issue.

Also interesting to note is the absence of any citation to *72A Realty v. Lucas*, 2012 NY Slip Op 08241, an Appellate Division, First Department, decision that left owners perplexed about how to recalculate rents for apartments that were impacted by *Roberts*. In *72A Realty*, the Appellate Division held that "the record does not clearly establish the validity of the rent increase that brought the rent-stabilized amount above $2,000, the free market lease amount should not be adopted, and the matter must be remanded for further review of any available record of rental history necessary to set the proper base date rate." However, there was no further explanation from the court as to how to proceed after determining the validity (or invalidity) of the base date rent. Although the *Ten Sheridan* court did not cite to *72A Realty*, it seems to have followed the Appellate Division's decision and taken the next step in determining the legal rent. If *Ten Sheridan* serves as any guidance, it would appear that once the deregulation is found to be valid (but for the pre-*Roberts* misinterpretation of the law), the standard four-year rule applies to setting the new legal rent (i.e., the rent charged on the base date plus all lawful increases subsequent thereto).

However, the question remains as to how the court would have set the legal rent if the validity of the rent increases leading to deregulation had not been established. It may be six more years before we have an answer.

The owner in this case was represented by David Cabrera. Mr. Cabrera is a partner at the law firm of Borah Goldstein Altschuler Nahins & Goidel, PC, in the Administrative Division. Mr. Cabrera has experience in all types of proceedings before state and city administrative agencies, as well as real estate litigation and transactions. Mr. Cabrera can be reached at 212-431-1300, ext. 333 or dcabrera@borahgoldstein.com. ♦