New York Law Journal
Real Estate Trends
WWW.NYLJ.COM
An ALM Publication
VOLUME 264—NO. 88
WEDNESDAY, NOVEMBER 4, 2020

RENT STABILIZATION

Fair Market Rent Appeals


By **Warren A. Estis**
And **Jeffrey Turkel**

Years ago, bringing, or defending, a Fair Market Rent Appeal (FMRA) was a routine part of any rent regulatory practice. Because there are so few rent-controlled apartments left, FMRAs have become somewhat of a rarity. Nevertheless, the successful defense of an FMRA, under appropriate circumstances, can lead to a ruling that the apartment had been deregulated under the luxury deregulation provisions of the RSL that existed prior to the HSTPA.

Pursuant to L. 1971, ch. 371, rent-controlled apartments vacated on or after June 30, 1971 became decontrolled. *See* CRL §26-403(e)(2)(i)(9). Three years later, pursuant to the Emergency Tenant Protection Act (L. 1974, ch. 576, §4) (ETPA), decontrolled apartments in buildings with six or more units generally became subject to the RSL.

The ETPA also addressed the issue of how to calculate the first stabilized rent of a former rent-controlled apartment. The answer is codified in RSL §26-512(b)(2), which states that the "initial legal regulated rent" for such an accommodation shall be "the rent agreed to by the landlord and the tenant and reserved in a lease or provided for in a rental agreement." That sentence ends, however, with the language "provided that such initial rent may be adjusted on application of the tenant pursuant to subdivision b of section 26-513 of this chapter." That application is an FMRA.

RSL §26-513(b) provides that a tenant can file an FMRA to challenge the legality of the initial legal regulated rent, and need only allege that the rent to which the tenant and the landlord agreed "is in excess of the fair market rent." Because the fair market value of any commodity is defined as what a willing buyer and seller agree to, it is difficult to understand how the negotiated rent set forth in the lease could in any way be "unfair," or above market. As it turns out, "fair market rent" is a term of art, defined as the former rent-controlled rent as adjusted by various formulas. Thus if the negotiated rent exceeds the rent established by that formula, the rent will be adjusted downward to what the formula permits.

Setting the initial rent thus became an all or nothing game. If the tenant did not timely file an FMRA, the initial legal regulated rent became the stabilized rent, no matter how high. If the tenant timely filed, the rent could be reduced dramatically.

It turns out, "fair market rent" is a term of art, defined as the former rent-controlled rent as adjusted by various formulas. Thus if the negotiated rent exceeds the rent established by that formula, the rent will be adjusted downward to what the formula permits.

Filing Deadlines

There are two deadlines for filing an FMRA. Where the landlord served the incoming tenant with an

WARREN A. ESTIS *is a founding member of Rosenberg & Estis.* JEFFREY TURKEL *is a member of the firm.*

"RR 1" form, *i.e.*, a Notice of Initial Legal Regulated Rent, the tenant has 90 days to file. *See* RSC §2522.3(a). Where a tenant fails to do so, the FMRA will be dismissed, and the initial legal regulated rent is lawful for all purposes. *See Park v. New York State Div. of Hous. & Community Renewal*, 150 AD3d 105, 114 (1st Dept 2017), *lv. to appeal dismissed* 30 NY3d 961 (2017); *Matter of Verbalis* v. *New York State Div. of Hous. & Community Renewal*, 1 AD3d 101, 102 (1st Dept 2003).

Where the landlord did not serve an RR-1, the tenant has four years to file. RSC §2522.3(c)(2) states that an FMRA "shall be dismissed where…the appeal is filed more than four years after the vacancy which caused the housing accommodation to no longer be subject to the City Rent Law." RSC §2523.1 similarly provides that where an FMRA "is filed four years or more after the first date the housing accommodation was no longer subject to the City Rent Law, the application shall be dismissed pursuant to section 2522.3(c) of this Title."

The First Department has consistently held that if the incoming tenant did not challenge the initial rent within four years, that rent can no longer be challenged. *See Olsen v. Stellar W. 110, LLC*, 96 AD3d 440, 441 (1st Dept 2012); *Wasserman v. Gordon*, 24 AD3d 201, 202 (1st Dept 2005); *Levinson v. 390 W. End Assoc. L.L.C.*, 22 AD3d 397, 401 (1st Dept 2005).

Luxury Deregulation

Over the past several years, FMRAs have come to the fore in cases where the issue is whether an apartment coming out of rent-control prior to the HSTPA had been luxury deregulated. A typical scenario is where the first tenant after rent control pays a rent higher than the luxury deregulation threshold at the time of the vacancy, but fails to file an FMRA within the 90 day or four-year deadlines.

In such circumstances, both the Courts and DHCR have held that the apartment is deregulated. In *3505 BWAY Owner v. McNeely*, 67 Misc 3d 583 (Civ Ct, NY County 2020), the first post-rent-controlled tenant moved in to the apartment in 2009 at an agreed-upon rent of $2,000 per month, which at that time was equal to the luxury deregulation threshold under RSL §26-502(a). It was undisputed that the tenant did not timely file an FMRA.

On these facts, Civil Court declared that the apartment had been luxury deregulated in 2009:

> Here, the Petitioner not only decontrolled the Premises after the last rent-controlled tenant vacated, but simultaneously deregulated the Premises pursuant to the luxury deregulation provisions in effect at the time, now repealed, RSL §26-504.2(a). Therefore, Respondent cannot challenge the rent regulated status of the Premises other than by challenging the legality of the first rent which qualified the Premises for deregulation. The only means by which to challenge the first rent is to prove that the rent exceeded the higher of either comparable rents or RGB increases plus IAI's, which is the exact process of a FMRA. Although Respondent claims she is challenging the rent regulatory status of the Premises in her fifth affirmative defense, in substance, she is requesting a FMRA.

Citing RSC §2522.3, Civil Court concluded that "the statute of limitations for filing an FMRA must be enforced here and bars Respondent from challenging the rent regulatory status of the Premises." On that basis, the Court dismissed the tenant's fifth affirmative defense, which alleged that the apartment was subject to rent stabilization. *See also 400 E. 58 Owner LLC v. Herrnson*, 64 Misc 3d 1202(A) (Civ Ct, NY County 2019) (Ortiz, J.).

DHCR has consistently ruled to the same effect. In *Matter of Del Guercio*, DHCR Adm. Rev. Dckt. No. GQ-410077-RT, issued May 8, 2019, DHCR held:

> A review of DHCR records reveals that the subject apartment was rent-controlled and therefore subject to the New York City Rent and Eviction Regulations (RER) until 2004. RER Section 2200.2(f)(13) exempts an apartment from rent control after the last rent-controlled tenant vacates.
>
> Section 2520.11(r)(4) of the Rent Stabilization Code (RSC) and

Section 26-504.2 of the Rent Stabilization Law exempt from stabilization housing accommodations which became vacant on or after June 19, 1997, with a legal regulated rental $2,000.00 or more per month.

Here, the first tenants in occupancy following the vacancy of the rent-controlled tenant paid a rent of $2,000.00 per month in March 2004 thereby exempting the apartment from rent stabilization. As such, the Commissioner agrees that the subject apartment was already deregulated when the petitioner took occupancy in 2013 at a rent of $2,300.00 per month.

The tenant's challenge to the initial rent following rent control represents a Fair Market Rent Appeal (FMRA) which was untimely. RSC Section 2522.3(a) states that no FMRA may be filed after four years from the date the housing accommodation was no longer subject to the City Rent Law, which was the date the last rent-controlled tenant vacated the apartment. In this case, the last rent-controlled tenant vacated the apartment in 2004. Therefore, the petitioner's FMRA filed over 12 years later was untimely. The owner's alleged failure to serve a decontrol notice on the tenant or otherwise advise the first tenant of the change in the rent regulated status of the apartment does not extend the four year deadline to file an FMRA. Furthermore, the owner's failure to register the apartment since 1984 does not extend the time to file an FMRA.

In *Matter of Katz*, DHCR Adm. Rev. Dckt. No. DU-410066-RT, issued on Jan. 26, 2016, the last rent-controlled tenant vacated in June of 2000, and a new tenant took occupancy pursuant to a lease setting forth a rent of $2,800 per month. DHCR ruled that because the rent was above the statutory decontrol threshold, and because no timely FMRA had been filed, the apartment was luxury deregulated:

> The Rent Administrator properly determined that the subject apartment was not under the jurisdiction of the agency. Pursuant to RSC §2520.11(r)(4), a housing accommodation which became vacant on or after June 19, 1997 but before June 24, 2011, with a legal regulated rent of $2,000 or more per month, is not subject to Rent Stabilization. The undisputed facts of this case indicate that the prior tenant's rent exceeded $2,000.00 per month in July 2000 thereby exempting the apartment from rent stabilization. As such, the Commissioner agrees that the subject apartment was already deregulated when the petitioner took occupancy on December 21, 2013 at a rent of $3,500 per month. The Rent Administrator also correctly determined that the petitioner's FMRA was untimely. RSC §2522.3(a) states that no FMRA may be filed after four years from the date the housing accommodation was no longer subject to the City Rent Law, which was the date the last rent-controlled tenant vacated the apartment. In this case, the last rent-controlled tenant vacated the apartment in June 2000. Therefore, the petitioner's FMRA filed over 14 years later was untimely.

Accordingly, in any case where the first tenant following decontrol alleges rent-stabilized status, practitioners should check to see whether (1) the first stabilized rent exceeded the luxury deregulation threshold at the time of the vacatur; and (2) the tenant timely filed an FMRA to challenge that rent. If the first rent exceeded the deregulation threshold and no timely FMRA was filed, the unit is not rent-stabilized. If the tenant filed a timely FMRA, the apartment will be stabilized if and only if the initial legal rent is adjusted below the luxury deregulation threshold.