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RENT STABILIZATION

Rent Concession Cases: The Score So Far


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Suppose a landlord renting up a new 421-a building gives an incoming tenant a two-month rent concession during the fourth and fifth months of an initial two-year lease. The monthly rent recited in the lease is $3,000 per month. Over the course of the 24 months, the tenant will pay a total of $66,000.

The question then arises as to what is the initial legal regulated rent for the apartment. RSC §2521.1(g) states in its entirety:

> The initial legal regulated rent for a housing accommodation constructed pursuant to section 421-a of the Real Property Tax Law shall be the initial adjusted monthly rent charged and paid but not higher than the rent approved by HPD pursuant to such section for the housing accommodation or the lawful rent charged and paid on April 1, 1984, whichever is later.

For the landlord in our hypothetical, the calculation of the initial stabilized rent is simple: it is the $3,000 rent the tenant was actually charged and paid. For some tenant advocates, however, the issue is more complex. They claim that the $66,000 the tenant will pay over the two-year lease term, when divided evenly by 24 months, yields an initial stabilized rent of $2,750. They further assert that, to the extent that the landlord has taken subsequent increases over the claimed $3,000 initial rent, tenant has been overcharged and defrauded.

The stakes, at least for landlords, are substantial. In the hypothetical, a $2,750 initial rent is an 8.33% reduction over the $3,000 rent set forth the lease. If the landlord granted that rent concession throughout the building, an 8.33% reduction in the building's cash flow would be disastrous.

Starting in 2020, tenants of various 421-a buildings throughout the city wherein rent concessions have been granted have commenced putative class action litigation asserting that the initial legal regulated rent for each of their apartments is not the lease rent, but is the "net effective rent," *i.e.*, the total rent actually paid over the lease term, divided by the number of months in that term.

To date, the tenants' efforts have met with mixed success. The five decisions rendered to date are analyzed below. In the interest of full disclosure, co-author Jeffrey Turkel represents *amici curie* RSA, CHIP and REBNY in the *Chernett*, *Flynn*, and *Marantz* decisions discussed below.

'Chernett'

The first case decided was *Chernett* v. *Spruce 1209, LLC*, 2021 WL 1253807 (Sup. Ct. New York County). There, the tenants of 1209 DeKalb Avenue in Brooklyn, a 421-a building, commenced a class action claiming that the landlord had engaged in fraudulent scheme to evade the Rent Stabilization Law by registering as the initial stabilized rent the lease rent, rather than the "net effective rent." They also argued that the rent concession was merely a disguised preferential rent, and that the "net effective rent" figure should govern all future increases with respect to any tenant who received the concession.

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The landlord moved to dismiss, raising two primary arguments. The landlord first cited *Matter of Century Operating Corp. v. Popolizio*, 60 NY2d 483 (1983), where the complaining tenant alleged that the

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two-month rent concession in his initial lease should be carried forward in each renewal. The Court of Appeals rejected that argument, focusing on the actual language of the rent concession rider itself:

> The explicit terms of the rider, including that the tenant 'shall not be required to pay rent for the two months period commencing on the date on which possession of the apartment is given or the apartment is available for occupancy', limit the rent concession to the commencement of the original vacancy lease. The terms 'possession…is given' and 'available occupancy' have no rational relation to a renewal lease, where the tenant is already in possession and occupancy of the apartment. The rider must be read 'in the light of the circumstances existing at its making' (*Becker v. Frasse & Co.*, 255 NY10, 14), and examination of the language of the rider as a whole confirms that the two-month rent concession is tied to the other rider provisions concerning the possibility that building construction would not be complete by the beginning of the specified term.
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> The concession under consideration, fixed as it was to the giving of possession and assumption of occupancy in the uncertainty of building completion, cannot be construed to carry forward to renewal leases.

60 NY2d at 488-89.

The landlord also focused on DHCR's Fact Sheet #40 (rev. January 2014), wherein DHCR wrote:

> Concessions
>
> There are two types of rent concessions. One is a concession for specific months, as for example, where the lease provides that the tenant will not have to pay rent for one or more specified months during the lease term. This type of concession is not considered a preferential rent.
>
> The other type is a prorated concession, where the dollar value of the rent-free month(s) is prorated over the entire term of the lease and not tied to a specific month or months. A prorated concession is really the same as a preferential rent and will be treated in the same manner.

In *Chernett*, Supreme Court (Bluth, J.) denied the landlord's motion to dismiss and rejected the landlord's reliance on both DHCR Fact Sheet #40 and *Popolizio*:

> The Court…questions the utility of [DHCR Fact Sheet #40] to the instant circumstances--there is no reason offered for why these two types of concessions should be treated differently when, in practice, they are functionally the same exact thing.
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> * * *
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> In *Popolizio*, the Court of Appeals rejected a tenant's claim that a two-month rent concession should apply to the calculation of his rent for subsequent leases for his rent-stabilized apartment where the concession was given for construction. That case does not compel dismissal of the instant action; this is not a situation where plaintiffs allege there was a one-time concession for construction. Rather, plaintiffs point to the suspected use of construction concessions long after construction was completed.

'Flynn'

Justice Debra A. James reached the opposite conclusion in *Flynn v. Red Apple 670 Pacific St., LLC*, 2021 WL 3080022 (Sup. Ct. New York County), where the court dismissed the tenant's complaint. The court found that the concession rider explicitly stated that it was one-time only, and that "plaintiff does not dispute that he has contractually agreed to the terms therein." The court also deferred to DHCR's Fact Sheet #40:

> Plaintiff's argument that this Court should not defer to DHCR's determination in Fact Sheet #40, regarding the distinction between 'rent concession' and 'preferential rent', is unavailing. It has long been established that a court should defer to the determination of an administrative agency, such as DHCR, where interpretation of a statute or its application involved the agency's specialized knowledge and understanding of its operational practices and/or data evaluation unless the agency's determination is 'irrational or unreasonable.'

Other Decisions

In *Marantz v. MD CBD 180 Franklin LLC*, Sup. Ct. Kings Co. Index No. 521055/20, decided Oct. 6, 2021, Justice Ingrid Joseph dismissed the tenants' complaint. In addition to relying on DHCR's Fact Sheet #40, the court looked to the language of DHCR's regulation:

> In accordance with basic principles of statutory construction, the language of RSC §2521.1(g) must be given its plain meaning, without resort to forced or unnatural interpretations. Given their plain meaning, the words 'initial adjusted monthly rent charged and paid' clearly mean the first monthly rent of rent charged under the lease and paid by the tenant, not the average or 'net effective' monthly rental amount charged and paid over the course of a lease term.

In two additional cases, however, *Abdelrazek v. 12-15 B'way Astoria*, Sup. Ct. Queens Co. Index No. 701984/21 (Butler, J) and *Bascom v. 1875 Atlantic Ave. Dev. LLC*, Sup. Ct. Kings Co. Index No. 502056/2021 (Velasquez, J.), the courts succinctly denied the landlord's motion to dismiss, holding that the tenants had stated a cause of action.

First Department Proceedings

The *Chernett* and *Flynn* cases will be argued in the Appellate Division, First Department on Nov. 23, 2021. It remains to be seen how the court will view the competing arguments therein.