

Seven deadly pitfalls when buying NYC multifamily

By ERIC RUBENSTEIN
AND MATTHEW ZANGWILL,
RUSKIN MOSCOU FALTISCHEK PC

Multi-family continues to be a hot sector in New York City real estate seemingly capable of only being slowed by rent reform that would, among other things, end vacancy decontrol and tamp down allowable rent increases. Even so, the competition for available properties intensifies when purchasers have deadlines for 1031 tax deferred exchanges. Overzealous buyers need to be aware of seven potential pitfalls before locking up multi-family properties in NYC — issues that may prove costly if not fully investigated and resolved.



ERIC
RUBENSTEIN

• **Apartment Rent Registrations.** Annual registration of rent stabilized apartments is required by law, and it is critical for a potential buyer to review a building's registration history to confirm that the rents charged are legal. Failure of a current owner to register may preclude a successor owner from collecting otherwise permissible rent increases, and subject them to other penalties, including treble damages for overcharging. Verification of proper filings for Major Capital Improvements and Individual Apartment Improvements is also required by law.

• **Violations.** The absence of any notes or notices of violations (such as ECB liens, sidewalk violations, boiler and elevator violations etc.) would be the exception rather than the rule for multi-family properties in NYC. Purchasers should be aware however that certain violations could carry serious consequences, including impeding an owner's ability to obtain a building permit or a new or amended Certificate of Occupancy. Since rent-impairing violations go to the heart of the valuation of the property, purchasers should insist that sellers satisfy all liens and pay any violations that have been reduced to ascertainable amounts. Sellers

should not object, but may resist any obligation to clear violations of record since that can be a herculean, if not impossible, task — even if the conditions underlying a violation are remedied.

• **Air BnB and Similar Services.** The rise of the Shared Economy over the last decade raises new concerns for purchasers of multi-family properties. Due diligence should determine whether any apartments are being used for temporary or short-term use, since landlords can be liable for illegal conditions caused by tenants. At minimum, a search for the property on the Air BnB and similar websites should be performed. In all cases, a litigation search or a review of databases such as the DOB Buildings Information System may reveal complaints against tenants in the building for dangerous living conditions or other indications of temporary hotel-type use such as excessive noise, traffic, etc.

• **RPIE Statements.** NYC requires the owners of certain income-producing properties to electronically file a Real Property Income and Expense Statement (RPIE) by June 1 of each year. Failure to timely file may result in a penalty up to \$100,000 that, if unpaid, will become a lien against the property which title insurance typically will not cover. The NYC Department of Finance website identifies properties for which RPIEs were not filed. The sales contract should include a representation that seller has complied with all RPIE requirements, as well as a surviving covenant that seller will file any RPIE before closing and be liable to pay any fines, penalties and interest resulting from RPIE non-compliance, since NYC has two years to assess the penalty.

• **Tax Certiorari and Abatements.** Tax certiorari proceedings in NYC require multi-family residential property owners to timely file an administrative application for correction of assessed value with the Tax Commission, as well as income and expense statement in certain cases. Purchasers should require at closing the J-51 and ICAP (Industrial and Commercial Abatement Program)

files for the building, including supporting documentation as to certified reasonable costs including original contracts, cancelled checks and all contract affidavits that would be necessary to submit to an HPD (NYC Housing, Preservation and Development) auditor.

• **Apportionments.** Rent apportionments typically lead to disputes about arrearages, application of rent received post-closing, additional rent items, etc. Purchasers should negotiate a detailed apportionments agreement at closing with a survival clause identifying significant arrears for identified tenants. This should prove more valuable than relying on the general boilerplate provision in form contracts.

• **Seller Representations.** Multi-family properties are generally sold in their “as is” condition, subject to casualty and wear and tear. While most sellers require purchasers to do their due diligence prior to executing the contract — and sellers will scrupulously avoid making representations as to facts which purchasers can confirm independently — purchasers need to be focused on factual issues that are unable to be determined reasonably during the due diligence process. Some examples of those items include environmental issues such as underground tanks; whether the property was ever subject to a “red herring” or condominium offering plan; and options or right of first refusals which have not been recorded. For those matters, purchasers should seek seller representations which survive closing for 6-12 months (although this is not always obtainable.)

Multi-family properties in NYC can be very profitable investments but purchasers must be mindful of issues that can prove to be expensive and negatively impact valuation and financing criteria. Thorough due diligence is vital to protect purchasers against unforeseen and costly pitfalls.



MATTHEW
ZANGWILL