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(Almost) Every Tenant Has His Price

How much would you pay to purchase an apartment that you already own?

By [Adam Bonislowski](#) • 09/30/16 12:31pm



Buyouts can mean a headache—or a windfall—for tenants. Camilla Perkins

Tenant buyouts! The real estate equivalent (for landlords, anyway) of an M.C. Escher sketch. How much would you pay to purchase an apartment that you already own?

The answer? Quite a lot sometimes. In a city where development parcels are in hot demand, rent-stabilized properties are natural targets. Before you can build, though, you have to somehow accommodate existing residents, and

while stabilization is primarily a tool to protect New York's middle class from a voracious housing market, the ongoing building boom has given some rent-stabilized tenants shots at a jackpot.

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For instance, Steve Wagner, co-founder and partner at real estate firm Wagner Berkow, told the Observer that in the past two to three years he has negotiated for clients "six seven-figure buyouts." And that, he noted, isn't counting a number of others that came in just under the million-dollar mark, or a case he's currently working on in which his four clients have actually turned down million-dollar offers.

You could always, of course, just try to harass your tenants away. And certainly some landlords do—refusing repairs, cutting utilities, violating construction

codes, even, on occasion, employing physical intimidation. But aside from being unethical, immoral, and just generally the mark of a terrible human being, such practices are typically frowned upon by law enforcement and might well land you in jail. For instance, Manhattan landlord Steven Croman was this spring brought up on criminal charges after years of allegedly harassing his rent-regulated residents. (Christened the “Bernie Madoff of landlords” by New York Attorney General Eric T. Schneiderman, Croman is also up on fraud charges for, among other things, allegedly inflating his buildings’ rental incomes in order to score some \$45 million in loans.)

Easier, then, to just pay your tenants to leave. Which brings us back to the original question—how much?

That depends on a variety of factors, Wagner said. Among the most important is the strength of the resident’s claim to tenancy.

Tenants, assuming they have a strong tenancy case, hold most of the leverage in buyout situations. Camilla Perkins

“That is No. 1,” he said. “Is that tenant illegally subletting? Is that tenant not using the premises as his or her primary residence? Have they altered the apartment illegally?”

Wagner noted a recent case involving a client with what amounted to a very weak claim to her rent-stabilized unit. “She hadn’t lived in the apartment for years and was subletting it to somebody,” he said. “Her tax returns didn’t show the apartment. Her voting records didn’t show the apartment. Her driver’s license didn’t show the apartment.”

Even so, she was able to score a five-figure buyout, Wagner said, calling it a “decent settlement under the circumstances.” Given the woman’s weak tenancy case, the owner likely could have gotten her out through litigation, but Wagner noted that the delays involved in such a process have their own costs to a development project.

In fact, the state's Division of Homes and Community Renewal has a formal process developers can use to remove rent-stabilized tenants from buildings they plan to demolish that involves relocating and compensating these residents. It's almost never used, though, said Robert Sedaghatpour, principal of real estate firm STRATCO Property Group, which advises investors on repositioning properties.

Taking a project through the DHCR takes an average of around five years, Sedaghatpour said, meaning that by the time a developer receives approval, the market might have completely changed. Sitting on a project that long can also significantly cut into a builder's rate of return.

"I've yet to see a landlord apply to DHCR in any of the deals I've been a part of," Wagner said. An opposing lawyer once threatened to do so, he said, but his developer clients quickly put the kibosh on that idea and instead upped their buyout offer.

"Their attorney was making a legal argument, but the [developers] knew that the [DHCR approval] wasn't guaranteed and that it was going to take so long it would kill their internal rate of return," he said. "They wanted us out now, not two years from now."

Buyout money should be set aside for any project based on removing rent-stabilized tenants, said Aviv Zumin, president of FirstService Realty. “You have to include it in your development budget just like you would construction or marketing or anything like that.”

Sedaghatpour added that developers often come to these projects unprepared for the more personal aspects of the process—to wit, how to incentivize someone to leave their home.

‘When [developers] are looking at these projects, they are looking purely at how the numbers work out on paper. The intricacies of how to handle the human aspect are often not at the forefront of their mind.’—Robert Sedaghatpour of STRATCO Property Group

Cooperation on details like taxes can help smooth the way, Wagner said. He recalled a case in which he negotiated a

nearly million-dollar buyout for clients who'd somehow swung a rent-stabilized penthouse on the Upper West Side.

“There was no construction going on, it was just that the tenants were paying this amazing low rent for this apartment with views and a terrace and everything else, and the landlord wanted it desperately,” he said. The two parties agreed on a number, but Wagner and his clients wanted the deal structured such that the buyout would be taxed at the (lower) capital gains rate, as opposed to as conventional income.

“The landlord was refusing to give my clients what they needed in order to get capital gains treatment, even though it was going to cost him nothing,” he said. “So I went back to the attorney and told him we can’t do the deal at \$975,000 or whatever it was. I said, ‘We’ll pay the tax, but you have to pay us more money.’ That changed his mind.”

Whatever you do, landlords, don’t come to the table with a low-ball offer, Sedaghatpour advised. Fundamentally, he said, tenants, assuming they have a strong tenancy case, hold most of the leverage in such situations. And things are more likely to get contentious—and by extension, costly and time consuming—if they suspect they’re not being treated fairly.

“Unless [a rent-stabilized tenant] is doing something outside the terms of their lease, they have no obligation to go anywhere or even entertain any type of buyout,” he said. “You have to be prepared to give them enough money to maintain their quality of life in their neighborhood.”

He cited the cautionary tale of a building in Midtown that recently tried to buy out its tenants for around \$250,000 each—well below the going rate of pretty much anything in the neighborhood. Rather than take the offer, the tenants hired an attorney to help them negotiate. In the end, Sedaghatpour said, the buyouts will likely prove more expensive than if the developer had simply come with a reasonable offer in the first place.

“What happens is, many shortsighted operators come up with initial negotiations that may be very favorable to them, but that don’t work for these residents. And it ends up creating two sides that are often antagonistic, and the negotiation ends up being much more expensive,” he said.

Sometimes staying is better anyway. Mirador Real Estate agent Jessica Milton noted a friend of hers who was offered a \$10,000 buyout to leave his Clinton Hill apartment but declined.