Case Background – *CHIP, RSA, et al. v. City of New York, et al. (2d Cir.)*

For fifty years, New York City has declared its rental housing market to be in a perpetual state of "emergency" in order to justify a legal regime that forces a small set of property owners to subsidize housing for a randomly selected population of individual tenants. Those property owners have been deprived of all meaningful rights with respect to their property, including the right to exclude others from the property; to occupy, possess or use the property; and to freely dispose of the property. In addition, the New York Rent Guidelines Board has precluded stabilized property owners from raising rents at a rate consistent with the Board's own estimate of rent increases that are necessary to cover the increased costs of ownership and maintenance.

Not surprisingly, as a result of these onerous burdens the value of rent stabilized properties are now far below their market-based peers. And despite the RSL's imposition of what amounts to a privately funded and randomly assigned housing subsidy, the law has failed to achieve any of the goals for which it was ostensibly created: it does not increase vacancy rates, it does not increase the supply of affordable housing, it does not target those in greater financial need, and it does not promote diversity in the City.

Far from recognizing the futility of the RSL, or the burdens that the law unfairly imposes on certain New York property owners, the New York legislature recently doubled down on the irrational RSL, enacting the HSTPA on June 14, 2019—touted by some to be the "strongest tenant protections in history." Under the HSTPA, all opportunities for rental properties to be relieved of RSL regulation (high rents and high-income tenants, for example) were stricken. Owners of properties are now precluded from using more than a single unit for their themselves or their family, and even then, may do so only if they can demonstrate a compelling need for the unit. The HSTPA prevents owners from substantially recovering investments in individual apartment improvements (IAIs) or major capital improvements (MCIs), forcing owners to choose between bearing repair costs themselves without an ability to recover those costs through increased rent or allowing buildings to deteriorate over time. The HSTPA further restricts the ability of owners to convert properties to condominiums or cooperatives. Under the new law, they must have 51% of all tenants agree to purchase contracts for their units—a requirement that effectively precludes the ability to convert altogether.

On July 16, 2019, CHIP and RSA, joined by a number of individual property owners, commenced the Action in federal court in the Eastern District of the New York by filing a 120-page complaint asserting, on three grounds, the facial unconstitutionality of the RSL.

First, the complaint states that the RSL violates substantive due process because it is not reasonably related (let alone narrowly tailored) to achieving the purported goals of the law. The law does not result in an increase in apartment vacancies in New York (and actually achieves the opposite effect), it does not increase the supply of affordable housing (again, it achieves the opposite effect), and it does not target its benefits to lower income families (there are a large number of documented instances of high-income individuals living in regulated apartments).[1] After fifty years in existence, and despite New York City's rote declaration of a housing emergency every three years over that period, the RSL has not, and will not, remedy or alleviate the problem.

[1] The increased vacancy rates, especially in Manhattan, and huge increase in delinquent rent payments due to COVID-19 further undermine the legitimacy of the RSL. These facts will be developed on remand if we prevail at the appellate level.

Second, the complaint alleges that the RSL constitutes a physical taking of the property of owners of regulated buildings. By requiring owners to permit rent stabilized tenants and their successors and sublessees to occupy private property for indefinite periods of time, the RSL deprives owners of the fundamental right to exclude individuals from their properties. And by restricting the ability of owners to occupy their own units, or re-purposing those units to other rent-bearing uses, the RSL denies owners the right to occupy, possess, use, or dispose of their own property.

Third, the complaint alleges that the RSL also constitutes a regulatory taking. At its heart, the RSL forces a small segment of the population (a small subset of building owners) to bear the public burdens (subsidizing housing costs) that in fairness and justice should be borne by the public as a whole. That is the essence of a regulatory taking, as defined by the Supreme Court in *Armstrong v. United States*, 364 U.S. 40, 49 (1960). In fact, New York's highest court has confirmed that rent-stabilized leases are considered a local public assistance benefit, which is funded solely by the owners of rent subsidized real estate. *See Santiago-Monteverde v. Periera*, 22 N.E. 3d 1012, 1015 (N.Y. 2014). By imposing this public burden on private building owners, the RSL has impaired owners' ability to generate reasonable and expected returns on their investments.

Defendants and Intervenors moved to dismiss the complaint on November 1, 2019 and, after full briefing, Judge Eric Komitee heard oral argument on the motions on June 23, 2020. As anticipated, the district court dismissed the Action in its entirety. Its September 30, 2020, opinion held, in relevant part, that (1) although the restrictions that the RSL places on landlords' use of their properties are significant, they are insufficient under current Supreme Court and Second Circuit precedent to sustain a physical takings claim, (2) two of the three factors in the Supreme Court's *Penn Central* analysis applicable to regulatory takings claims—*i.e.*, the economic impact of the regulation on the claimant and the extent to which that regulation interferes with reasonable investment-backed expectations—were not susceptible to review on a facial (as opposed to an as-applied, owner-by-owner) basis, and (3) the RSL is at least related to some legitimate government interest and, therefore "the Court is bound to defer to legislative judgments, even if economists would disagree."

We filed a notice of appeal to the Second Circuit on October 2, 2020. The Appeal raises three questions for the Second Circuit to consider, each of which the court will review *de novo*:

- Whether the district court erred in dismissing Plaintiffs' physical taking claim, despite the fact that the RSL forces owners of regulated properties to offer leases to renters in perpetuity at sub-market rates (and to renters' family members and care givers who are eligible successors to the renters' statutory rights) and effectively prevents owners of regulated properties from recovering possession of those properties, converting rent stabilized buildings into commercial property, or even occupying a rent stabilized unit as the owner's personal residence, among other restrictions on owners' ability to use and enjoy their property, or forces them to sell the property completely;

- Whether the district court erred in dismissing Plaintiffs' regulatory taking claim, despite the facts that, as the New York Court of Appeals has acknowledged, the RSL is "a local public assistance benefit" that is paid for not by the government or

the City's residents as a whole, but by the relatively small set of owners of rent stabilized properties, and that the RSL greatly diminishes the value of the privately-owned properties subject to its regulations by denying owners the ability to increase rents to keep up with increased operating costs; and

- Whether the district court erred in dismissing Plaintiffs' due process claim, despite the fact that New York City declares a housing "emergency" every three years so that they can continue to control rents without explaining how the RSL operates to abate any such emergency, in particular because both statistical research as well as lessons from history show the RSL actually exacerbates affordable housing shortages by reducing the vacancy rate and housing supply, driving up rental prices in the nonregulated market, and discouraging development—all while failing to target benefits to renters in need of them.