

Affordable Housing and the 2025 New York State Budget: A Path Forward?

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After [last year's misfire](#) amidst a continuing housing affordability crisis, the New York State Legislature recently passed several important initiatives to increase housing availability and ease the tight rental market in New York as part of its \$237 billion total budget for Fiscal Year 2025 (the "Housing Agreement"). The Housing Agreement caps a year of intense debate around housing issues between tenant advocates, developers, landlords and legislators at the local and state levels to determine how best to address the needs of New Yorkers.

With the dust now at least partially settled, the major pieces of the Housing Agreement include a new 485-x tax incentive, incentives for residential conversions of office space, parameters around "good cause" eviction, increases in recoverable costs for landlords of rent-stabilized properties, direct development of housing on state-owned land and expanded legalization of basement apartments. This article provides detail on each of these key areas with an eye towards new opportunities for investors in New York real estate.

485-x and 421-a

Taking on the new name Affordable Neighborhoods for New Yorkers ("ANNY"), the New York State Legislature passed the 485-x tax incentive program as the long-awaited and much-debated successor to the 421-a program. ANNY has stricter requirements for affordability than did 421-a and eliminates the option for certain units rent restricted for tenants at over 100% of area median income ("AMI") to qualify as "affordable" under the terms of the tax exemption. ANNY offers a real estate tax exemption up to a maximum of 40 years (an increase from 35 years under 421-a) for housing projects that meet eligibility requirements based on project size:

- For projects containing between six and 99 units, no less than 20% of the new residential units must be rent restricted for tenants at a weighted average of 80% of AMI.

- For projects containing between 100 and 149 units, no less than 25% of the new residential units must be rent restricted for tenants at a weighted average of 80% of AMI.
- For projects containing over 150 units and located in Manhattan below 96th Street, the Brooklyn and Queens waterfronts, Dumbo, Brooklyn Heights, Astoria and other dense neighborhoods, no less than 25% of the new residential units must be rent restricted for tenants at a weighted average of 60% of AMI.

Differing from 421-a, ANNY requires permanent rent stabilization for any rent-restricted units in eligible projects, which some have described as “permanent affordability” for such units. Additionally, depending on the number of units, projects may also be subject to certain hourly wage requirements, which increase at 2.5% annually. Developers under ANNY must also make “all reasonable efforts” to spend at least 25% of “total applicable costs” on contracts with Minority- and/or Women-Owned Business Enterprises.

Along with establishing ANNY, the Housing Agreement extends the completion deadline to June 15, 2031 for new construction to receive certain 421-a benefits, so long as construction had commenced as of June 15, 2022. This extension should provide relief to developers and owners in response to uncertainty about whether 421-a benefits would be retained in the face of construction delays. To be eligible for ANNY, the Housing Agreement provides that construction must commence for a project by no later than June 15, 2034, and completion must be achieved no later than June 15, 2038.

Given its more stringent affordability requirements, ANNY is not likely to produce as much new housing as did its predecessor. Nevertheless, the passage of ANNY should provide a level of certainty to landowners who had been waiting to see whether a successor to 421-a would ever emerge, and land prices for eligible developments are expected to rebound somewhat following the passage of the Housing Agreement.

Residential Conversions and FAR Cap Increases

The Housing Agreement also includes incentives for the conversion of unused office spaces into residential housing, which is widely viewed as a positive development in the real estate community. Owners of office buildings may be eligible for a tax exemption of up to approximately 90% of real estate taxes for 25 to 35 years if they convert vacant office space into residential units. To benefit from an exemption, developers must keep 25% of new residential units rent restricted to tenants at a weighted average of 80% of AMI (and 5% of such units rent restricted for tenants at 40% of AMI), with permanent

rent stabilization for the new rent-restricted units. Importantly, eligible projects will be required to obtain a construction permit by June 30, 2026 in order to receive the maximum tax exemption, which will force owners and developers to move quickly in their efforts to boost housing supply and repurpose under-utilized office space. It will be interesting to see whether the tax incentive will be a meaningful driver towards increased housing given this timing requirement.

Additionally, the Housing Agreement raises the floor area ratio (“FAR”) cap for new residential developments in New York City from a density limit equal to 12 times the size of the lot to a limit between 15 and 18 times the size of the lot. Projects eligible to take advantage of the higher FAR cap, however, must comply with any applicable mandatory inclusionary housing provisions, which often include their own affordability requirements.

“Good Cause” Eviction

Perhaps the most-discussed portion of the Housing Agreement is its “good cause” eviction component, which restricts landlords’ ability to remove tenants from residential units and prescribes what constitutes “reasonable” rent increases. A landlord may only remove a residential tenant upon a showing of “good cause” and procurement of a court order. “Good cause” includes defaults such as (1) a tenant not paying rent (unless the rent is “unreasonable”), (2) a tenant being a nuisance or maliciously or grossly negligently damaging the premises and (3) a tenant using the premises for an illegal purpose and similar acts. The “good cause” eviction provisions of the Housing Agreement apply only to New York City, though other municipalities may opt into the program.

With respect to what constitutes a “reasonable” rent increase, tenants may challenge a rent increase with the presumption that it is unreasonable if it is greater than (i) 10% or (ii) 5% plus the annual percentage change in the local Consumer Price Index, whichever is lower, and a court will evaluate the rent increase in light of other relevant factors.

Important to an analysis of “good cause” eviction is a review of exemptions from its requirements, which could be significant for investors depending on the composition of their portfolios. Buildings constructed in 2009 or later are exempt for 30 years following issuance of a TCO, and apartment units with monthly rents greater than 245% of the local fair market rent for the applicable unit type are exempt as well. Landlords may evict tenants if they plan to demolish a unit or withdraw a unit from the market.

Several West Coast states and other East Coast cities have implemented similar forms of “good cause” eviction in recent years. It will be interesting to observe whether New York’s embrace of this concept in the Housing Agreement triggers “good cause” eviction becoming a foundational underwriting consideration for residential landlords going forward.

Cost Recovery for Rent Stabilized Apartment Landlords

The Housing Agreement also provides some relief to landlords of rent stabilized units in their ability to recover renovation costs. Following the enactment of the 2019 Housing Stability & Tenant Protection Act, landlords owning rent stabilized units were limited to rent increases covering a maximum of \$15,000 in renovations capitalized over a 15-year period. This cap on recoverable expenditures has been raised to \$30,000 over 15 years and can reach as high as \$50,000 if a unit had been continuously occupied for 25 years or registered as vacant in 2022, 2023 and 2024.

Housing Development on State Land

As part of the Housing Agreement, the New York State Legislature earmarked \$500 million for a fund to develop housing on land owned by the State of New York, certain localities, non-profits and land trusts across New York State. This housing will likely take the form of limited-equity cooperatives—housing developments where income-restricted buyers purchase shares in the cooperative at below-market prices in exchange for limits on resale prices—and the State estimates this will create up to 15,000 units of housing. It remains to be seen what, if any, opportunities this funding will create for developers and investors, but we expect the State to attempt to leverage private sector resources and expertise as part of this initiative.

ADUs and Basement Apartments

In a long-awaited initiative, the Housing Agreement includes a pilot program for legalizing the tens of thousands of basement apartments that already exist in New York City as a way to increase the number of legal housing units available to renters. The pilot program allows for the legalization of existing basement units in 15 of the City’s 59 community divisions—four in the Bronx, four in Brooklyn, six in Manhattan and one in Queens—though additional details have not yet been provided. Further, the Housing Agreement gives New York City and other localities the authority to create incentives

for the development of “accessory dwelling units,” which are free-standing, single, independent housing units on the lots of single-family homes.

Early reactions from developers to the Housing Agreement are more favorable than those from landlords or tenant advocates, which should be viewed positively from the perspective of investors looking to increase housing supply in the New York real estate market. ANNY could provide an important boost to projects that have stalled over the years while awaiting a replacement for 421-a, and exemptions from “good cause” eviction along with higher cost recoveries for landlords should provide some more flexibility to building owners. We remain hopeful that the 2025 State budget will spur development opportunities, provide a baseline for further accretive policy changes and relieve housing affordability pressures on New Yorkers.

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