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Questions of Rent Tactics by Private Equity

Hiroko Masuike for The New York Times

Tenants of an apartment building in the Washington Heights neighborhood of Manhattan gather in their lobby to discuss allegations of harassment by the building's owner.

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Private investment firms have been amassing what may seem like unusual stakes in New York real estate: they have bought hundreds of apartment buildings with thousands of rent-regulated units across the city that produce decidedly meager returns.

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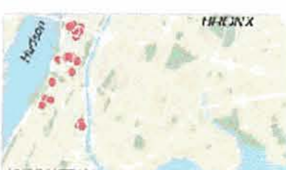

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As regulatory filings and promotional materials show, the companies expect to generate higher returns quickly by increasing rents after existing tenants vacate their units. Their success depends upon far higher vacancy rates than are typical in rent-regulated apartments in New York.

Some residents and tenant advocates say that they began seeing what they consider a pattern of harassment of low-income tenants this year and suspect that it is a result of the new owners' business models. Tenants have been sued repeatedly for unpaid rent that has already been received by the landlords; they have been sent false notices of rent bills, lease terminations and nonrenewals; and they have been accused of illegal sublets.

The companies dispute the charges of harassment and say they are protecting their rights.

Nevertheless, tenants must answer the notices in court, but many have responded by moving out, court documents indicate. When they vacate the apartments, the owners can increase the rents substantially.

"Predatory equity is undermining the best efforts of New York City and state elected officials to slow the loss of affordable housing," said Benjamin Dulchin, deputy director of the Association for Neighborhood and Housing Development, a nonprofit organization. "Both the private equity funders and the lending institutions are aware, or should be aware, that harassment of tenants is taking place as a result of their financial models."

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30

Private investment funds have boomed in recent years, buying companies they considered undervalued in industries as diverse as communications, hotels and energy, streamlining operations and then selling them at a profit. For example, private equity firms have bought nursing homes, often slashing expenses and reducing staff to increase their profit.

New York provides an unusual opportunity because it is one of the few cities with a large inventory of apartments whose rental rates are regulated and kept below market levels.

In the last four years, developers backed by private equity firms have acquired almost 75,000 rent-regulated apartments, Mr. Dulchin said, or about 6 percent of the city's 1.2 million such units. Major private equity-backed participants in this market include Vantage Properties, which has partnered with Apollo Real Estate Advisors; the Pinnacle Group, a unit of Praedium Capital; and Normandy Real Estate Partners.

These companies often make clear that raising rents is crucial to their financial goals. On its Web site, Normandy Partners states "the increased institutional appetite for New York City rent-stabilized housing transactions" and adds: "There is a near-term opportunity to increase cash flow by converting rent-stabilized apartments to market rate as tenants vacate units."

The companies say that they are not harassing tenants and that they are only trying to protect their rights by enforcing legitimate rules governing regulated apartments.

But the New York City Rent Guidelines Board says the vacancy rate on rent-regulated apartments is 5.6 percent each year. Buildings with vacancy rates far higher suggest resident harassment, tenant advocates say.

Vacancy rates have risen above 20 percent in some buildings owned by Vantage Properties; in some Normandy buildings, the rates exceed 30 percent.

If an apartment is rent regulated, yearly increases cannot exceed the amount set annually by the Guidelines Board. Most recently, it was 3 percent on a one-year renewal lease.

When an apartment becomes vacant, rents can climb as much as 20 percent. When that rent rises above $2,000, regulations no longer apply, and tenants must pay market prices.

To generate returns expected by private equity investors and to pay off the debt used for their purchases, tenant advocates say that managers of the properties are intimidating residents in the hopes of forcing them to leave so that rents can be raised.

Rent-regulated apartments account for 57 percent of the total in the Bronx, 42 percent of the apartments in Brooklyn, 59 percent in Manhattan, 43 percent in Queens and 15 percent of those on Staten Island, the Guidelines Board says. Many of the buildings bought by private equity investors are in neighborhoods that are being gentrified.

Vantage Properties, led by Neil L. Rubler, has paid more than $1 billion in the last two years to buy 9,200 rent-regulated apartments in Queens and Upper Manhattan. Investing alongside Vantage in many buildings is Apollo Real Estate Partners, an investment firm founded by William Mack in partnership with Apollo Management, a private equity firm created by Leon D. Black, a former Drexel Burnham Lambert banker and acolyte of Michael R. Milken.

Last month, Mr. Black announced a plan to sell $500 million worth of Apollo Management shares to the public. Apollo Real Estate Partners will not be part of that sale. A spokesman for Mr. Black said it was a separate company in which he had a stake but exercised no control over it.

In a group of buildings in Queens with 2,124 apartments, Vantage has filed almost a thousand cases in housing court against tenants since October 2006, according to Robert McCreanor, director of legal services at the Immigrant Tenant Advocacy Project of the Catholic Migration Office in Sunnyside.

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Mr. McCreanor said he searched public records for similar actions by the previous landlord. He found no more than 350 in any year. "What's offensive about these business practices is they seek to generate above-average profits by displacing poor people and people who are vulnerable," Mr. McCreanor said.

A spokeswoman for Apollo Real Estate declined to comment on the accusations. But Mr. Rubler called them baseless. "Any exploration of the way we conduct business would reveal that we are steadfastly determined to uphold the rights of our residents and have absolutely no interest in harassing them," he said. "They are our valued customers, and we treat them as such."

Mr. Rubler said most of his tenants have positive experiences. Claudia Williams, of Corona, Queens, was asked by Mr. Rubler to talk with a reporter. She said that Vantage was allowing her to live in her mother's apartment even though she had not been the primary leaseholder.

Phyllis Miller, a resident of Savoy Park in upper Manhattan, said she believed that tenants who were unhappy with Vantage simply disliked change.

But Jose Ricardo Aguaiza, 45, who works as a doorman in Manhattan, said he has lived in the same apartment in Woodside for 14 years and never had a problem until Vantage took over in 2006. Since July 2007, Mr. Aguaiza has been sued by Vantage three times, twice for nonpayment of rent that he was able to demonstrate the company had received.

"They refused to give me a renewal contract," Mr. Aguaiza said. "And in court, the lawyer from Vantage offered to give me three months' free rent for moving out." Mr. Aguaiza said he turned down the offer.

On April 10, Mr. Aguaiza and five other rent-stabilized tenants living in Queens sued Vantage. The plaintiffs say the company has engaged in deceptive practices that violate New York's consumer protection laws. Five more tenants are joining the suit.

Janice Williams, who works as a freelance producer in television, has lived in a Vantage building in Sunnyside since July 2005 and is a plaintiff. When she moved in, the building was owned by Nathan Katz Realty.

In October 2006, Vantage bought the building. Ms. Williams said the property managers rejected her request for a lease renewal in April 2007. They said she was not entitled to the rent-regulated unit because her primary residence was in Greenwich, Conn. But the Sunnyside apartment has been her primary residence since September 2005, Ms. Williams said, and is on her driver's license and her voting card. She appealed to the New York State division of housing and community renewal and won.

"Our apartment building is 72 units, and a little over 20 apartments in the span of a year and a half have turned over since Vantage bought it," said Ms. Williams, who has organized tenants.

The turnover Ms. Williams cited is in keeping with a description of Vantage's strategy in a 2007 document filed with the Securities and Exchange Commission after its purchase of 455 rent-regulated apartments in Washington Heights. The filing described the company's business model as a "recapturing" strategy. Under the plan, Vantage expected in its first year to turn over 20 percent to 30 percent of the units, five times the typical vacancy rate. Vantage aimed to recapture 10 percent of the units each year afterward.

Only 5 of the 455 units were empty at the time of the filing. All but one unit was regulated, with average monthly rent of $752, or 65 percent below market.

Once the apartments become vacant, the document said, Vantage will renovate the units and raise rents "to market levels." That will generate enough cash to service the $70 million in debt that comes due in 2014.

Vantage's debt service is an estimated $1,098 monthly on each unit, almost 50 percent more than the average rent. Mr. Rubler said that the description of the recapture program was "not our words," but those of the debt security's underwriter, Credit Suisse Securities. "I think they overstated significantly the focus on turnover in the business plan," he said.

When asked about legal actions taken against tenants, Mr. Rubler said all were mounted solely to protect his company's rights. "Only in instances where we need to act to protect our own rights do we ever find ourselves in any litigation with a tenant and it is never with the intention to harass them," he said.

The company is also meeting with its tenants to improve communications, he said.

Normandy Partners, with almost 2,000 rent-regulated apartments in 42 buildings in the Bronx, East Village and Sunnyside Queens, is another significant landlord backed by private equity. It is a partner with Vantage in 1,650 units in Queens, the Bronx and Brooklyn.

Mr. Dulchin said the Normandy Partners' buildings have also had high turnover — more than 30 percent — since they were purchased by the investors.

A spokesman for Normandy declined to comment.

Pinnacle Group is a third big developer that has joined forces with a private equity firm, Praedium Capital of Chicago. In December 2006, Pinnacle settled a suit brought by the New York attorney general's office accusing it of rent-gouging. Pinnacle paid $100,000 without admitting to or denying the accusations. The company did not return a phone call seeking comment.

Responding in part to indications that harassment is systemic, Mayor Michael R. Bloomberg signed legislation in March making it illegal for a landlord to file repeated and baseless court proceedings to force a tenant to vacate an apartment.

Under previous rules, tenants could take their landlord to housing court only over the apartment's condition or for a failure to provide essential services.

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