



Condo conversions still make sense in N.Y's real estate market

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The wave of conversions from rental housing to condominiums continues throughout the City, notwithstanding the current credit market and a "claimed" softening in the residential real estate market. The number of conversion plans filed with the attorney general in 2007 was the highest in almost twenty years. A number of factors are providing the impetus for this conversion activity, including a weakened dollar compared to other international currencies, the high prices real estate now commands and landlord concerns about the future. What started as a trickle over three years ago is now a flood of conversion activity, with no end in sight.

There are several issues causing landlords to think twice about their long-term plans. These considerations include the often-stated goal of the mayor and the governor to preserve affordable rental housing. Additionally, if the Democrats capture the New York State Senate in 2008, there is a strong possibility the Martin Act (the cooperative and condominium conversion law) will be amended, making conversions more difficult. Furthermore, with Democrats in control of the Governorship and the legislature, luxury and vacancy decontrol would also likely end, market rate tenants would be given increased protection and possibly, a new form of rent regulations will be introduced.

On the national stage, if Democrats capture the White House and keep control of both Houses of Congress in 2008, there is a likelihood for changes to the Internal Revenue Code to raise revenue by ending the deductibility of real estate taxes and interest and eliminate the 1031 (Tax Deferred) Exchange as well as curtail basis adjustments.

This will significantly increase tax rates for higher income taxpayers and perhaps make real estate investments less attractive.

While some of the hurdles landlords and developers of residential housing may face in the future are clear, a closer analysis of the issues is necessary. Over the years, New York's Democratically-controlled State Assembly introduced and even passed numerous bills designed to provide tenants with greater rights. However, companion legislation has never gotten out of committee in the Republican-controlled State Senate, therefore no new laws made it to the Governor for his signature. Now, with Governor Spitzer's outspoken concern about preserving affordable housing and the Republican's margin of control in the Senate down to a handful, legislation of this type has a real possibility of being enacted. If this happens, landlords may be unable to convert buildings to condominiums or find tenants have a greater control over the process, as well as lifetime protection as renters. Even market rate tenants could benefit, if the legislature decides to incorporate them into Rent Stabilization or enacts regulations limiting rent increases.

A similar situation could exist nationally, where a potential Democrat President, may be looking for ways to reduce the Budget deficit without raising taxes on middle income taxpayers. This could be accomplished by raising rates for those earning more than \$100,000 a year and further eliminating some of the most popular tax deductions. Another way it could also be accomplished is by eliminating the 1031 Exchange and the Basis Adjustment on Death, each of which would have an immediate adverse impact on owners of real estate.

As stated earlier, the present boom in conversions is being fueled by the extraordinary high value of real estate as well as the weakened dollar, which has created a huge market abroad for second homes in New York City. In the last year alone, hundreds of units in new condominium buildings have been purchased by homebuyers from countries including Japan, Korea, Italy, Ireland, Israel, Russia, and China. Many of these buyers are purchasing homes for periodic occupancy when they are in New York, rather than for renting to third parties. This has helped to insulate New York's condominium market from falling victim to the same kind of excess capacity now being felt in South Florida, Phoenix, Las Vegas and even the West Coast. As those in the industry can confirm, although prices have not continued to rise as quickly as two years ago, inventory is still being absorbed as rapidly as it is being completed, without any noticeable reduction in the purchase prices. In addition, the resale market has remained strong. Given these strong market fundamentals, New York City's condominium market, including conversion projects, should continue to experience tremendous success, despite the many questions both on the local government level as well as the national stage.

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