RGB Explained:

The PIOC and Commensurates

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The Price Index of Operating Costs (PIOC) report contains the NYC Rent Guidelines Board (RGB) commensurate adjustments, which are predictions based on scientific methodology by the RGB's internal staff to determine the rent adjustment necessary to ensure property owners net operating income stays constant. This report often garners a lot of media attention due to these commensurate adjustments.

The RGB issues five commensurates based on rent revenues from vacancy leases, net revenue, Consumer Price Index (CPI)-adjusted Net Operating Income (NOI) and projected costs. Of these five, only two commensurates factors in inflation. Currently, year-over-year inflation for the New York Region is 6.2 percent. As this is historically high, the three non-inflation adjusted commensurates serve little functional value in discussions about rent adjustments.

Last year, the inflation-adjusted commensurates suggested a rent adjustment of a 4.5 percent increase on a one-year lease and a 9 percent increase on a two-year lease. Despite this data, the RGB only authorized a rent adjustment of a 3.25 percent increase on a one-year lease, which was slightly above the suggested commensurates when inflation was not considered, and a 5 percent increase for a two-year lease, which was a full percentage below the non-inflation adjusted commensurates.

When rent adjustments are set below commensurates, the RGB is defunding buildings. **This is a fact based on the RGB's own data, not an opinion**. In 2021, the RGB also defunded buildings by issuing a rent increase below all commensurate calculations. The same thing happened in 2020, 2019, 2018, and 2017. For the past six years, the RGB has consciously decided to adjust rents below all of the commensurates calculated by their own staff.

It is also important to note that the commensurate adjustment is set to keep NOI constant compared to last year. NOI declined by 7.8 percent in 2020 and 9.1 percent in 2021, which has plunged thousands of rent-stabilized buildings into distress when factoring for responsible debt service payments. If the RGB issues a rent adjustment in line with the commensurates, it will not be enough to help most buildings with more than 80% rent-stabilized units, it will just slow their decline.

The RGB must view the CPI-Adjusted NOI Commensurate as the floor for discussions this cycle.

PIOC Facts:

Due to high inflation, the CPI-Adjusted Commensurate is the only one that honestly calculates the rent adjustment needed

For the past six years the RGB has issued adjustments below all of the commensurates, signaling a systemic defunding of rent-stabilized buildings

For the past six years, the RGB's projections for operating costs have been lower than the actual costs calculated the following year, with an average statistical error of 1.15%

Commensurate adjustments are calculated to keep net operating income (NOI) constant to the previous year and does not factor in the massive declines in NOI from the two previous years

What is a Commensurate?

The commensurate adjustments "combine various data concerning operating costs, revenues and inflation into a single measure to determine how much rents could have to change for NOI for rent-stabilized apartments to remain constant."

The RGB calculates commensurates using five different formulas. Two of the commensurates factor in increased rent revenues from vacancy leases. The 2019 rent laws implemented a de facto vacancy control, virtually eliminating any rent increases on vacancy. It is likely that these measures will be the same, or only 0.25% lower than their accompanying commensurates.

Of the three remaining commensurates, the first evaluates "net revenue," which does not factor in inflation. The second looks at "CPI-adjusted NOI," which is the net revenue calculation adjusted for inflation and the most accurate calculation of the commensurates. The final commensurate is called the "traditional" commensurate and is calculated using the PIOC Projections, which uses a formula of price changes over previous years in order to project the price changes moving forward for seven key costs.

Using the PIOC Projections is flawed, as the 2022 PIOC report noted: **"Projecting changes in the PIOC has become more challenging in recent years."** For example, last year the PIOC projected fuel prices would go down 1.7%, but real time data suggests they actually increased by almost 20% over the past year. Over the past six years the PIOC has projected costs below the actual costs reported the next year. Over that time, the PIOC has under estimated costs by 1.15%.

Due to these factors, an objective view of the commensurates suggests that the CPI-adjusted NOI is the only honest and accurate commensurate measure that will be put forth by the RGB. It should be the starting point for discussions.

Why The PIOC Is Different Than The I&E

The PIOC calculates the change in price for various things, including fuel, labor, insurance, administrative costs, and more. But the PIOC does not calculate the change in how much a rent-stabilized building uses these services or expenses. Therefore, the Income & Expense (I&E) report is a better guide to the amount of revenue a building is producing and the amount an owner is spending on operating expenses. For example, fuel prices could go up 10%, but if it was a warm winter, the expense for fuel could stay the same.

The only advantage the PIOC has over the I&E is that the data is more timely because it is calculated by looking at the change in prices over the past year up to the moment the report is released, while the I&E looks at data compiled from two years earlier (the 2023 report uses 2021 data). But the I&E has the advantage of being extremely detailed by pulling actual income and expense data from thousands of buildings in order to determine the overall health of the rent-regulated housing stock.

PIOC Predictions

In order to calculate the commensurate adjustments, the PIOC projects the cost changes of seven core items they track by using a formula of price changes over previous years in order to project the price changes moving forward.

While this method is statistically sound, the approach is problematic.

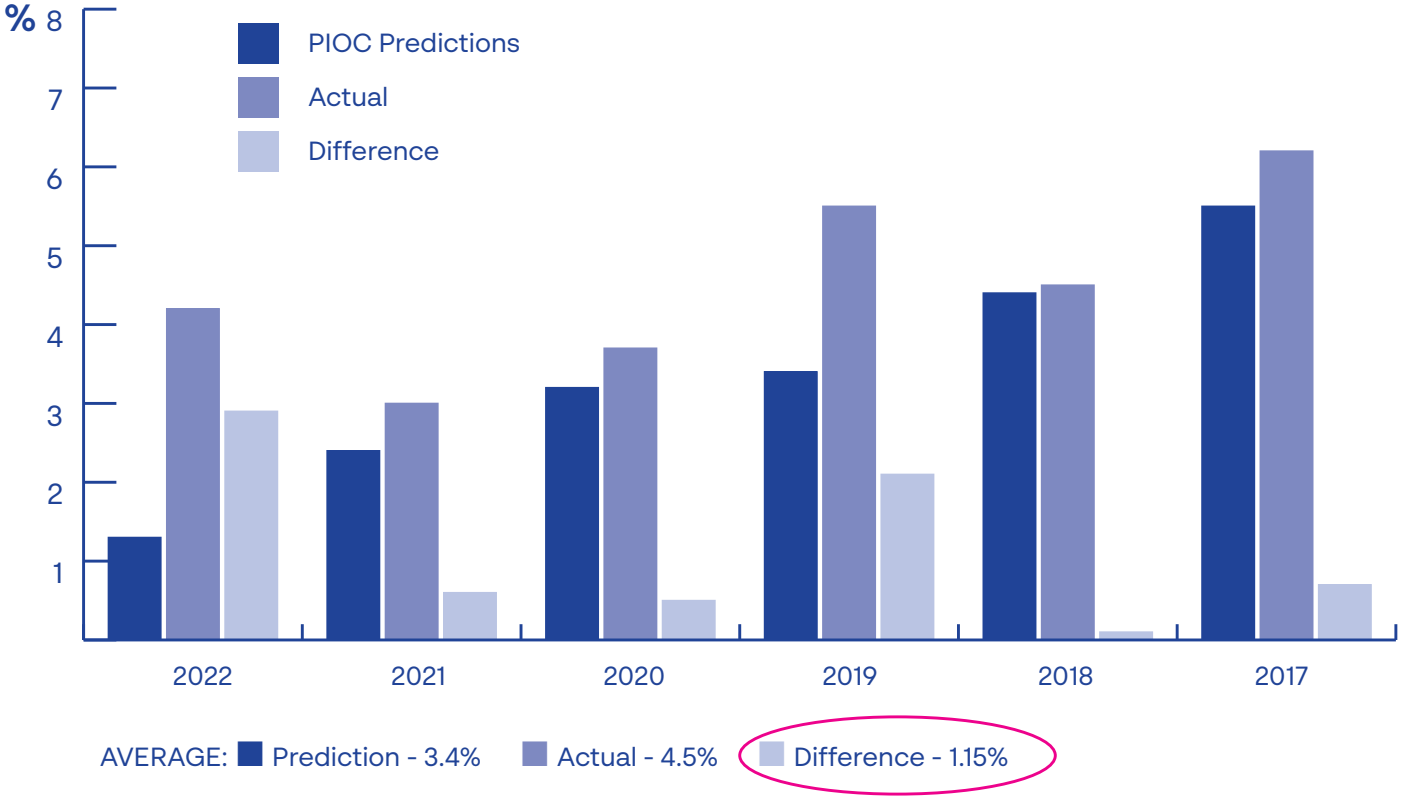
The current methodology determines that taxes make up approximately one-third of costs, and fuel, labor, maintenance, administrative, utilities (sewer & water), and insurance make up the rest of the costs.

But historically, tax payments have been incredibly difficult to project, especially in the past few years due to the pandemic. A massive influx of federal funding during the pandemic prompted the government to keep property taxes lower, but as federal assistance ran out, the assessments on rent-stabilized buildings rose dramatically, which increased the property tax burden.

A similar thing occurred for fuel prices, as the impacts of geo-political events made projecting the supply and cost of natural gas and oil more difficult. Last year's projections also failed to fully understand the impact of inflation on the labor market, and projected labor costs to only rise 3.9%. Additionally, sewer and water increases were historically high last year, though utility projections predicted the increase would only be 2.4%.

In fact, the RGB's PIOC Predictions have been consistently lower by an average of 1.15% for the past six years. Lower predicted operating costs lead to lower commensurate adjustment calculations. In addition to the RGB putting forth final adjustments below the commensurates, they have also been calculating lower commensurates using faulty data analysis as proven over the past six years.

PIOC Predictions Should Be Adjusted higher by 1.15%



Conclusion

Commensurate adjustments are an important tool used to calculate necessary rent changes to ensure rent-regulated buildings are properly financed. Historically, these adjustments have been largely ignored by the RGB in final votes. The RGB often dismisses the data due to a misguided belief that deregulated apartments in rent-regulated buildings would be able to offset rent adjustments that did not keep up with operating costs.

But approximately 80% of rent-stabilized buildings outside of the Core of Manhattan have few or no deregulated apartments. Additionally, the changes to the 2019 rent laws have eliminated any ability to increase rents on vacant apartments on turnover. This makes the financial viability of these units completely dependent on the actions of the Rent Guidelines Board.

Over the past several years, the RGB has continued to defund these buildings, which provide the majority of affordable housing to hard-working New Yorkers.

Any rent adjustment below the CPI-adjusted NOI commensurate is a conscious decision to defund the majority of rent-regulated buildings in New York City.

Any rent adjustment below the CPI-adjusted NOI commensurate is a conscious decision to defund the majority of rent-regulated buildings in New York City. Since the RGB has consciously chosen to do this for the past six years they have put many buildings with more than 80% rent-stabilized units on shaky financial standing.

The RGB should factor this into their final decision and advance a final adjustment that is higher than the CPI-adjusted NOI commensurate. This is the only way to bring financial stability to buildings that have been systematically defunded for years and are now in severe trouble due to the massive increase in interest rates over the past year.

New York City is in a housing crisis.

Hundreds of owners and property managers of rent-stabilized apartments can't keep up with skyrocketing costs. According to NYC's own numbers, the 2022 rent-adjustments don't come close to covering the increase in fixed-costs, and it has been that way for years.

New York City's Rent Guidelines Board needs to listen to their report and housing experts, and implement a more reasonable rent adjustment in 2023. Our city depends on it.

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