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# Building Owners Face An Even Stricter NYC Climate Plan

**By Raymond Pomeroy**

On Oct. 29, the New York City Council passed an amendment to 2019's Climate Mobilization Act, or CMA, that will, if signed by Mayor Bill de Blasio, significantly expand the number of multifamily residential buildings in the city subject to the CMA's strict greenhouse gas emissions limitations.

Earlier that same week, the city's Department of Finance released draft regulations implementing a Property Assessed Clean Energy, or PACE, loan program, to complement the CMA. The amendment, and the release of regulations for the PACE program, affirm the city's intent to push forward with implementation of the CMA, despite the impacts that the COVID-19 pandemic is continuing to have on New York City's commercial real estate market, residential rental market and building owner finances.

The CMA aims to reducte greenhouse gas emissions from the city's building stock by 40% as of 2030, and by 80% as of 2050, as compared to a 2005 baseline. These reductions are implemented through mandatory GHG emissions caps for covered buildings, with the caps become increasingly stringent every five years.

The initial compliance period is from 2024 to 2029, with subsequent emissions caps established for the period from 2030 to 2034. Emissions caps for future five-year compliance periods will be established by the city's Department of Buildings, or DOB, through rulemaking.

The CMA is projected to impact about 50,000 NYC buildings, representing nearly 60% of the city's building area. It is expected that approximately 20% of the buildings that use the highest levels of energy in the city will be affected in the initial compliance period. As the emissions caps become more stringent, that number is expected to grow to 80% of covered buildings by 2030, and nearly 100% by 2035.

Subject to specific statutory exemptions, the CMA's building emissions caps apply to covered buildings. Covered buildings are defined as (1) buildings with areas exceeding 25,000 gross square feet; (2) two or more buildings on the same tax lot with areas together exceeding 50,000 gross square feet; or (3) two or more buildings held in condominium ownership that are governed by the same board of managers, and with areas that together exceed 50,000 gross square feet.

In order to achieve the dramatic reduction of GHG emissions called for by the CMA, the owners of covered buildings will be required to implement energy-efficiency retrofits to bring down overall energy usage, utilize available alternate compliance measures, or where available, apply to the DOB for a discretionary adjustment to the building's emissions cap.

The CMA permits owners of covered buildings to purchase renewable energy credits and carbon offsets as an alternate means of compliance with the emissions caps. Practically speaking, though, the use of renewable energy credits as a compliance tool is significantly constrained by the requirement that all renewable energy credits be generated in, or directly deliverable to, the NYC power grid to qualify.

The CMA further allows owners of covered buildings to apply to the DOB for discretionary adjustments to the annual emissions cap. Adjustments may be available for buildings in financial distress, where legal (e.g., landmarks designation) or physical (e.g., space constraints) prevent a building owner from installing necessary energy efficiency retrofits; or where special circumstances (e.g., 24-hour operations, or energy intensive uses) caused the building's 2018 actual energy use to be more than 40% above the building's 2014 emissions cap.

The city is also in the process of studying a GHG emissions trading scheme, to create a regulated marketplace for owners of covered building to buy and sell emissions credits. A report on the feasibility of such a trading scheme is due to be released in January 2021.

As originally enacted, the CMA provided an exemption from the definition of covered building for multifamily residential buildings containing one or more rent-regulated units. The council's recent amendment now requires that more than 35% of the building's units be rent-regulated in order for the exemption to apply.

We are not aware of any study undertaken by the council to determine the number of buildings that will no longer be exempt from emissions limitations as a result of the amendment. However, logic dictates that the number will be significant. In testimony before the council, the Council of New York Cooperatives and Condominiums estimated that the amendment would "impact hundreds of residential buildings," and stated that "at least half of the buildings that fall into the category of having less than 35% of their units rent regulated are former rental buildings that have been converted to housing cooperatives and condominiums."[1]

As one would expect, the real estate community and the environmental community have largely lined up on different sides of this issue. For the environmental community, the benefits of the amendment are essentially twofold: expanding the scope of the CMA will lead to greater citywide GHG emissions reductions; and expanding the CMA's reach to buildings with rent- regulated units will promote environmental justice, by bringing the benefits of GHG emissions reductions, and building energy-efficiency retrofits, to the rent-regulated community.

For building owners, the impacts of the amendment are more complicated. As an initial matter, the CMA has been law for a year and a half. Many building owners with covered buildings have spent that time assessing the energy performance of their buildings, planning to file adjustment applications, identifying potential energy-efficiency retrofits, planning for necessary capital expenditures, and exploring various means of alternate compliance.

Applications for the various adjustments to the CMA's emissions limitations are due to be submitted to the Department of Buildings by July 1, 2021, and the first compliance period for emissions limitations commences in 2024. A late amendment to the proposed legislation added a two-year extension for building owners subject to the new requirements to meet the emissions limitations.

Owners of these newly covered buildings now need to comply with the emissions caps starting in 2026, and must begin filing annual certifications of building energy use in May 2027. The amendment did not extend the deadline for applications for adjustments.

Further complicating matters for owners of residential buildings are limitations enacted by New York state, as part of 2019's Housing Stability and Tenant Protection Act. While the emissions limitations contained in the CMA will require building owners to invest in expensive capital improvements, the Housing Stability and Tenant Protection Act limits a landlord's ability to charge tenants for major capital improvements to no more than a 2% increase in rent.

Major capital improvement rent increases are prohibited altogether in buildings where fewer than 35% of the units are stabilized. The owners of these buildings, where fewer than 35% of the units are rent-stabilized, may now be facing the double whammy of becoming subject to the CMA's stringent GHG emissions limitations — while being unable to pass through to tenants the costs of major capital improvements necessary for the building to comply with those measures.

One potential bright spot for building owners was the Department of Finance's release of draft regulations implementing the PACE program. This program was authorized by the city as part of the CMA, and is intended to provide building owners with an option for long-term, low-interest financing for building energy retrofits and renewable energy projects.

PACE loans differ from traditional financing in a number of key respects. Loan payments are billed on the property's annual tax bill, and they run with the property. If a building is sold, the loan automatically flows to the new owner.

Loans are generally long term — typically 20-30 years, depending on the useful life of the retrofits — and have low interest rates, typically between 5% and 6%. PACE loans are also nonaccelerating and nonextinguishable — a loan default does not result in an acceleration of the loan balance, nor may a lender commence an action against the borrower for an unpaid loan.

Delinquent loan payments become a lien on the property, and are treated like other unpaid taxes — they are collectible by the city in a tax lien sale. The remaining balance on the loan continues to be an obligation on the property, and would flow to the tax sale purchaser.

While PACE loans have many benefits for building owners seeking to finance energy efficiency projects, building owners also need to be aware that many senior secured lenders prohibit borrowers from taking on new debt without consent, and many loan agreements specifically prohibit borrowers from taking out PACE loans. Building owners will need to review existing loan agreements and work with their current lenders to obtain appropriate consents prior to applying for PACE loans.

Many NYC commercial real estate industry groups and large commercial real estate owners have been guardedly hopeful that the city would delay implementation of the CMA, in light of the severe financial distress caused by the COVID-19 pandemic. It's hard to see the passage of this recent amendment to the CMA, though, as anything other than an affirmation of the city's plans to proceed without delay.

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