



ABCs of TICs

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I recently sold a tenant-occupied building in a popular part of San Francisco. It was built before 1979 and was under rent control. The tenants in the building were combative and had many demands regarding buyer and broker access during the sales process. This process is never easy in San Francisco, but in this case, the tenants' actions were far beyond what is usual. They called the Department of Public Health with complaints that resulted in multiple Notices of Violation. They posted signs indicating they were protected while demanding that they had verbal authorization to enjoy rights to areas not noted on the lease.

Perhaps they followed the San Francisco Tenants Union's advice, which is posted on its website:

“The best thing to do is not worry about which just cause will eventually be used and fight the conversion. If the landlord can't sell it, then no one will be evicted by a new owner. Start fighting the day a 'for sale' sign goes up. Potential buyers often have not thought through the fact that they will be evicting someone or evicting a family or someone who is senior or disabled. Nor have they usually thought through what it might cost in money and time to evict someone. They're thinking and hoping that you will move out the moment they buy the building. Educate prospective buyers! Let them know they will be evicting people and what that will mean to those people, as well as what it will mean to the landlord's pocketbook and time schedule. If you show that you will put up a fight, you can probably convince almost two-thirds of prospective buyers that they don't want to buy your building, because it looks like a lot of hassle. And maybe you can slow down the process so much that the sale becomes unprofitable. Many tenants have fought their condo conversion evictions this way.”

The battle between owners and the city government over losing rent-controlled units has waged on for many years in San Francisco. The essence of the battle on the side of the owners is they want to cash out of their rent-controlled apartment investment buildings. Many of the buildings with fewer than 10 units are bought by investors who hope to vacate the units and sell them individually through a Tenants in Common (TIC) sale or a condominium conversion. On the other side of

the battle are many of the Supervisors, tenant rights activists, and groups like the SFTU who see the TIC or condo sale of rent-controlled units as an erosion of their progressive voting base. The common position is that if owners exit the rental business through a TIC sale, those units that house voters in “distributed owner-subsidized housing,” aka rent-controlled housing, will house owners who are less supportive of the progressive agenda. Once a tenant is replaced by a TIC owner who is directly responsible for payment of utilities and property taxes, the new households are more often prone to be more conservative in their voting preferences. Our Supervisors have not, as a group, been on the conservative side historically.

Some of the highlights of recent skirmishes include:

2013 Condo Conversion Moratorium

In 2013, the San Francisco Board of Supervisors suspended the city's condominium conversion lottery scheme until 2024. Currently, the only properties allowed to convert are 2-unit buildings and larger buildings that were already TICs in 2013. Condos are a superior form of ownership of units versus TIC ownership when it comes to individual loans. This redirected the efforts of would-be converters only to TIC ownership.

2014 San Francisco Ordinance No. 54-14 (aka 24-Month Payout Differential)

This legislation, proposed by David Campos, required property owners to pay the difference between a tenant's current rent and two years' rent for a similar apartment when evicting them using the Ellis Act.

This was signed into law in 2014, but later overturned in a court decision by the First District Court of Appeal in 2017.

2015 Buyout Registration No. 37.9E

In 2015, the Supervisors adopted a mandatory disclosure and registration of owners who execute buyout agreements. The legislative findings stated in support of this ordinance reads as follows: “Anecdotal evidence indicates that many buyout negotiations are not conducted at arm's length, and landlords sometimes employ high-pressure tactics and intimidation to induce tenants to sign the agreements.” The registration process is meant to regulate and count all buyouts to move them from “anecdotal evidence” to a clear count with the names of the owners, but not the tenants, published.

2017 Owner Move-In Ordinance

With this new law, owner move-in evictions have become more regulated. The period when the unit cannot be rented at a market price has moved from three to five years.

Tenant activists and private non-profits now can directly sue owners who do not follow the new rules, and the damages can be up to triple the rent differential, plus legal fees that a tenant incurs after an alleged wrongful owner move-in. These damages, most landlord attorneys feel, will be excluded from most insurance coverage.

As each side attempts to advance or defend its respective position, the battles become more focused. Despite multiple attacks, the Ellis Act continues to be one of the few options for owners to escape rent control because it is a state law and supersedes local authority to some extent. (Municipalities like ours still get to enact onerous regulations to impede use of the Ellis Act.)



Incremental TIC Conversion

One process that has been quietly progressing without much battle is the incremental conversion of buildings to TIC ownership. The most common TIC conversion strategy in San Francisco is to vacate the entire building through the Ellis Act or buyouts, renovate the building completely, then sell the units individually as TICs. In an “Incremental TIC Conversion,” an owner can simply sell units as they naturally vacate, when a tenant moves out voluntarily, which requires no notification to the city or regulation of the unit by the city’s governing agencies.

Andy Sirkin, an attorney who authors many San Francisco TIC agreements, noted, “If a new TIC owner is willing to be a co-owner with a landlord who still has under-market tenants as their responsibility, then this can be mutually beneficial without the stigma of Ellis or buyouts.”

In a conversation I had with another well-known TIC attorney, Lyssa Paul, she explained, “As property owners are reviewing their buildings and considering options going forward, one consideration is selling interests as tenancy in common through natural attrition of tenants. In fact, some tenants may even be interested in purchasing the occupancy rights to their units. This avoids the issues associated with potentially evicting / buying out tenants. It does require forethought depending upon the building size and financial situation, but is worthy of evaluation. The fact that tenants remain in place does not necessarily eliminate the possibility of tenancy in common interests. The location, type of property and amenities will influence whether prospective buyers will be deterred by units being tenant occupied.”

I spoke with a client last week who had a 6-unit building in the Sunset District with a very good location near the retail shops, good public transit and Golden Gate Park. He said he has been selling units as they vacate. He is now holding the last one of the six units. In that unit resides a tenant who pays 40% of market rent, but even that tenant cannot live there forever. He commented on the state of rent control in San Francisco. “I was born and raised in a communist country. I left that country and came to San Francisco. Some of the rent control aspects I see remind me of communism. We had a saying in the old country that seems to apply to tenants’ manipulation of the laws. My last remaining tenant really ‘knows how to dance the dance’ of rent control.”

Another owner I spoke to did an incremental conversion a few years ago with a larger building in the upper part of the Tenderloin. He owned his 30-unit property with no debt and one next door of similar size. He was able to move many of his tenants into one of the buildings with no buyout or Ellis Act, and then could sell the units in the vacant building. This movement without Ellis Act, buyout, or owner move-in eviction was a smooth transition that eventually emptied the building.

Who is to say where the Incremental TIC Conversion strategy will end up in this ideological battle, but one thing is for certain: If enough owners utilize this strategy, it could have a serious impact in the market, causing the Board of Supervisors to focus on the issue and try to regulate it. So far, it has escaped their watchful eyes.

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