9/9/92 NYLJ 1, (col. 1)
9/9/92 N.Y.L.J. 1, (col. 1)

New York Law Journal
Volume 208, Number 49

Wednesday, September 9, 1992

Outside Counsel

LOFT LAW UPDATE

Stanley M. Kaufman [FNa]

NEW YORK State's 10-year old Loft Law, found in Article 7-C of the Multiple Dwelling Law, was scheduled to expire, in part, in June 1992, but the Legislature extended the law, amending it in various significant respects. The amendment granted owners of covered "interim multiple dwellings," many of whom have not collected any rents from their tenants for years by reason of their non-compliance with the legalization requirements of the original Loft Law, a substantial and welcomed reprieve by extending the deadlines by which such owners are required to obtain residential certificates of occupancy and authorizing the collection of interim rent in the circumstances giving rise to their creases upon the owner's completion of various stages of the legalization process.

This article will address the more significant changes brought about by the 1992 legislation, the provisions affecting an owner's obligation to legalize his or her building and an owner's right to collect rent. However, in order to understand these changes and enactment, it is necessary to summarize certain pertinent provisions of the original 1982 Loft Law and the 10-year effort by the courts and the New York City Loft Board to interpret, implement and enforce the statute.

Article 7-C of the Multiple Dwelling Law (MDL), creating §§280-287 of the MDL, initially took effect on June 21, 1982. [FN1] The 1982 Loft Law represented the final piece of what was intended to be a comprehensive solution to the problems created by the widespread illegal conversion, largely occurring in the 1970s, of loft space formerly occupied by commercial and manufacturing tenants, to residential use or to joint living-work quarters. The other components of the legislative response to the unlawful residential conversion of loft buildings consisted of revisions to Article 7-B of the Multiple Dwelling Law, which was designed to establish minimum fire and safety standards for the conversion of non-residential buildings to residential use, and comprehensive "loft" amendments to New York City's Zoning Resolution. The various socio-economic, cultural, political and legal dynamics leading to the enactment of the Loft Law are beyond the scope of this article, but they have been discussed over the years in many of the cases and the original framers of the law attempted to succinctly summarize these factors in

MDL §280 entitled "Legislative Findings." [FN2]

Covered Dwellings

The 1982 Loft Law created a class of buildings known as "interim multiple dwellings" (IMD) and established a specific statutory definition for the determination of whether a building was a "covered" IMD. [FN3] The statute imposed upon owners of these IMD buildings the obligation to "file an alteration application within nine months from the effective date of the act ..."; to "take all reasonable and necessary action to obtain an approved alteration permit within 12 months of such effective date"; to "achieve compliance with the standards of safety and fire protection set forth in Article 7-B of [the MDL] ... for the residential portions of the building within 18 months from obtaining such alteration permit or 18 months from such effective date, whichever is later; [FN4] and to "take all reasonable and necessary action to obtain a certificate of occupancy as a class A multiple dwelling for the residential portions of the building or structure within 36 months from such effective date." [FN5]

The 1982 Loft Law conferred upon tenants and other protected residential occupants the right to continued occupancy of their lofts notwithstanding the expiration of their leases or the fact that residential occupancy of their lofts was not permitted under their lease or by law. In fact, these leases were customarily commercial in form despite the fact that the owner and tenant frequently knew full well of the actual or contemplated residential use of the loft. During the period of time the building was in the process of being "legalized," these protected occupants were entitled to remain in possession at "the same rent, including escalations, specified in their lease ... or in the absence of a lease ... the same rent most recently paid and accepted by the owner." [FN6]

The statute further mandated the creation by the City of New York of a "loft board" as an administrative agency to perform various functions administering and enforcing the Loft Law. The statute directed such loft board to set guidelines "within six months from the effective date of this article" establishing rent adjustments where there was no lease in effect prior to the owner's compliance with the safety and fire protection standards of MDL Article 7-B. [FN7] Under the Loft Law's statutory scheme, upon the ultimate issuance of a residential certificate of occupancy, the Loft Board would establish initial legal rents based upon the owner's "necessary and reasonable" legalization expenses, the tenants then would be issued written leases and they would enter the Rent Stabilization system.

Prior to the enactment of the Loft Law, the courts had begun to declare certain of these buildings containing illegally converted lofts to be "de facto multiple dwellings" and barred the owner of these buildings from collecting rent by virtue of the provisions of the MDL and the New York City Administrative Code requiring certificates of occupancy and the registration of multiple dwellings. [FN8] The 1982 Loft Law provided that notwithstanding the statutory provisions that barred

an owner of a multiple dwelling from bringing an action or proceeding to recover rents in the absence of a certificate of occupancy, "the owner of an [IMD] may recover rent payable from residential occupants qualified for the protection of this article ... and maintain an action or proceeding for possession of such premises for non-payment of rent, provided that he is in compliance with this article."

Loft Board Regulations

On Dec. 21, 1982, the then recently created New York City Loft Board (Loft Board) issued "Order No. 1" establishing interim rent guidelines applicable to registered IMD units occupied by tenants qualified for protection whose leases had expired or were to expire prior to the owner's compliance with the safety and fire protection standards of MDL Article 7-B. Essentially, these guidelines granted pre-compliance IMD owners, upon the expiration of these leases, a one time rent increase ranging from 7 percent to 39 percent depending upon the date of the last rent increase. [FN9]

Although the 1982 statute mandated the legalization of covered IMD buildings and MDL 284 established a specific legalization timetable, it was not until Dec. 1, 1985, after the statutory deadlines had passed, that the Loft Board promulgated regulations governing the manner in which, in practice, the code compliance process was to work. These regulations, commonly known as the Loft Board's Code Compliance Regulations, established another schedule of deadlines for the filing of an alteration application, obtaining a building permit, complying with Article 7-B and obtaining a certificate of occupancy. These new deadlines were established by the Loft Board in recognition of, among other things, the fact that the issue of whether many buildings were covered IMDs and the issue of which units in these buildings were "covered units" frequently had to await the outcome of contested coverage disputes as well as determinations by other administrative agencies of "grandfathering applications" under various provisions of the New York City Zoning Resolution.

Non-Compliance

Although administrative regulations were finally in place to govern the nuts and bolts of the legalization procedure and many IMD owners began and made varying progress along the road to legalization, the vast majority of IMD buildings were not brought into full compliance with the various legalization deadlines established by the Code Compliance Regulations. [FN10] The reasons for the widespread noncompliance were varied.

Some owners failed to legalize their loft buildings simply because they were unwilling to incur the substantial expense involved in bringing their buildings up to residential code requirements. In some instances, owners and their tenants chose to perpetuate what was otherwise a mutually acceptable - but unlawful and potentially dangerous - arrangement and ignored the Loft Law because the rent

levels were satisfactory to both parties, owners did not want or could not afford to incur the expense of legalization and tenants preferred the status quo, even if that meant residing in an unsafe dwelling, over the physical disruption in their homes that the required code compliance work would entail. Although the Loft Board made efforts to enforce compliance with the law, these efforts did not make a significant impact, partly because the Board's statutory authority to compel compliance was limited and, in any event, the risk of incurring a fine was preferable to some owners to incurring the cost of legalization.

Other owners, however, failed to achieve legalization for reasons beyond their control. Many loft building owners - claimed that they could not obtain sufficient financing from lenders. Under the statutory scheme of the Loft Law, although a portion of these expenses was to be recouped in the form of rent increases and the establishment of "initial legal rents" after code compliance was achieved, the up-front expense of code compliance had to be borne entirely by the owner, during which time the owner could only collect statutorily frozen below-market rents.

Other owners attempted in good faith to legalize their buildings, only to find the process mired for years in one or several of the various administrative agencies having jurisdiction over issues of zoning and building code compliance (and in inevitable Article 78 challenges to determinations of these agencies). For example, the authors of this article represent a cooperative IMD owner which has been diligently trying to obtain a certificate of occupancy since filing its Alteration Application in 1983 and, along the way, has found the following agencies to be necessary participants in the yet unfinished process: the Loft Board, the Department of Buildings, the Department of City Planning, the Board of Estimate, the Landmarks Preservation Commission, the Board of Standards and Appeals, the Department of Environmental Protection and the Department of Cultural Affairs. These agencies have their own sets of rules, regulations, policy concerns and timetables.

Finally, owners of some buildings containing IMD units which later became subject to the Loft Law only by virtue of a 1987 amendment to the law found it impossible to achieve the mandated legalization because the City of New York challenged the constitutionality and legality of the amendment and, at least for a period of time, the city's agencies did not change their own requirements to conform with the state law and thereby allow the legalization of these buildings to proceed. Under the original 1982 statute, for a building or a portion thereof to qualify as an IMD, among other things, the building had to be located in a zoning district in which residential use was permitted either "as of right, or by minor modification or administrative certification ... [or] pursuant to a special permit." [FN11] This requirement left a significant number of loft dwellers unprotected since they lived in buildings located in manufacturing zoning districts in which residential use was not allowed as of right or by virtue of the specific administrative zoning mechanisms listed in the statute.

In 1987, the Legislature enlarged the umbrella of the Loft Law by amending the statute to provide, essentially, that loft units in buildings otherwise qualifying as IMDs, that were residentially occupied from April 1, 1980 through May 1, 1987, were covered IMD units regardless of the zoning district requirements contained in the original 1982 statute. [FN12] The City of New York did not favor the enactment of the 1987 amendment because it, in effect, dispensed with zoning compliance, an integral component of the original Loft Law, as a prerequisite of IMD status. [FN13] Indeed, after the enactment of the 1987 amendment, the City of New York instituted a declaratory judgment action against the State of New York in which the city sought a determination that the 1987 amendment was invalid, among other reasons, for being violative of the home rule provisions of the State Constitution. While this litigation was pending, the city and its agencies did not conform their own laws and regulations to the Loft Law amendment and compliance with all zoning requirements continued to be a prerequisite for the issuance of a certificate of occupancy. In fact, for a period of time during the pendency of this intragovernmental dispute, the Loft Board itself put on hold the processing of applications involving these so-called "amendment buildings." These circumstances rendered it virtually impossible for some loft owners to comply with the legalization requirements of the Loft Law.

Right to Collect Rent

As stated above, the Loft Law granted an IMD owner the right to "recover rent ... and maintain an action or proceeding for possession for nonpayment of rent, provided that he is in compliance with this article." [FN14] Thus, many loft tenants of buildings whose owners had not achieved compliance began withholding rent. In July 1989, the Appellate Term in the First Department, in the case of 902 Associates Ltd. v. Total Picture Creative Services Inc., in a split decision, held that compliance with MDL §284(1), the statute containing the legalization requirements and deadlines, "must be pleaded and proven in order to successfully maintain a nonpayment proceeding against an occupant of an interim multiple dwelling." [FN15]

In May 1990, the Appellate Division, First Department, in County Dollar Corporation v. Douglas, endorsed the holding of the Appellate Term in 902 Associates and offered no solace to owners who were unable to achieve legalization for reasons beyond their control by stating that an owner's "reasonable attempt to comply with the four step legalization procedure of MDL §284(1)(i)" was insufficient. [FN16]

In March 1991, the Appellate Division adopted a more flexible approach and appeared to somewhat temper the harsh effect (for owners) of the foregoing decisions when it held, in Cromwell v. Le Sannom Building Corp., that "despite any possible contrary interpretation of our recent decision in County Dollar," MDL requires that the owner "take all reasonable and necessary action to obtain a certificate of occupancy" and whether the owner in that case (who had not yet obtained a building permit) took "all reasonable and necessary action" to obtain a certific-

9/9/92 NYLJ 1, (col. 1)
9/9/92 N.Y.L.J. 1, (col. 1)

ate of occupancy presented a question of fact. [FN17]

Despite the holding in Cromwell to the effect that the failure to obtain a certificate of occupancy did not, ipso facto, disqualify an owner from collecting rent and the suggestion that the sufficiency of the owner's legalization efforts would be reviewed on a case by case basis, the difficulties faced by owners, who had failed to legalize for reasons beyond their control, was perhaps most glaringly illustrated by an early 1992 Civil Court decision in Baer v. Jarzonbek. [FN18] That case involved a building in a manufacturing zoning district that had been made subject to the Loft Law by virtue of the 1987 amendment discussed above. The owner had taken no steps to legalize the building but argued that any such attempts would have been futile since the City of New York had not amended the Zoning Resolution to permit residential use in the subject district. The owner further argued that no legalization standards and timetables had been adopted or promulgated with respect to buildings covered by the 1987 amendment. The court flatly rejected these arguments, relying on County Dollar and 902 Associates (and seemingly ignoring Cromwell) and stated, in pertinent part:

At least during the pendency of its challenge ... to the constitutionality of the 1987 amendments to the Loft Law, it appears that the City of New York took the position that it would not take steps to compel loft building landlords to proceed to legalize their buildings. These actions by the City of New York in not cooperating with landlords to implement the legalization process pursuant to the 1987 Loft Law amendments placed those landlords in a most unfortunate position, but it did not mean that Petitioners had to, or legally could, sit back and do nothing. Petitioners could have moved to intervene in the aforesaid declaratory judgment action challenging the constitutionality of the 1987 Loft Law amendments, and sought appropriate relief from the court. Petitioners could have attempted to file the necessary papers with the New York City Department of Buildings and Loft Board in order to begin the compliance process, and, if their application was rejected, Petitioners could have brought an Article 78 proceeding to have the New York State Supreme Court review the City of New York's actions, and/or mandate that the City of New York permit Petitioners to take the required legalization steps ...

The refusal by the court in Baer v. Jarzombek to grant relief to the owner and the suggestion by the court that the owner could have achieved compliance with the Loft Law by taking on the City of New York and its agencies via an Article 78 writ of mandamus or certiorari were compelling proof, at least from the point of view of owners not yet in compliance, that the 1982 statute was in dire need of fixing.

1992 Amendments

By virtue of Chapter 227 of the Laws of 1992, effective June 21, 1992, the Legislature extended the Loft Law to June 30, 1996 and amended the law in several significant respects. The amendment created a new subdivision (ii) of MDL 284(1)

9/9/92 NYLJ 1, (col. 1)
9/9/92 N.Y.L.J. 1, (col. 1)

which provides:

An owner of an interim multiple dwelling who has not complied with the requirements of paragraph (i) of this subdivision by the effective date of the chapter of the laws of 1992 which added this paragraph shall hereafter be deemed in compliance with this subdivision provided that such owner files an alteration application by Oct. 1, 1992, takes all reasonable and necessary action to obtain an approved alteration permit by Oct. 1, 1993, achieves compliance with the standards of safety and fire protection set forth in Article 7-B of this chapter for the residential portions of the building by April 1, 1995, or within 18 months from obtaining an approved alteration permit, whichever is later, and takes all reasonable and necessary action to obtain a certificate of occupancy as a class A multiple dwelling for the residential portions of the building or structure by June 30, 1995 or within six months from achieving compliance with the aforementioned standards for the residential portions of the building, whichever is later.

As a result of this provision, owners of IMD's who have not complied, for whatever reason, with the legalization deadlines contained in the 1982 statute and the subsequent Loft Board Code Compliance Regulations have received a new life. The statute now provides that these owners "shall hereafter be deemed in compliance" if the first step in the code compliance process, the filing of an alteration application with the Department of Buildings, is achieved by Oct. 1, 1992 and the new schedule of further deadlines - for obtaining an alteration permit, complying with Article 7-B and obtaining a residential certificate of occupancy - is met. The "deemed in compliance" language of the amendment also makes it clear that owners who meet the new deadlines are entitled to collect rent.

In recognition of the hurdles many IMD owners have encountered in their efforts to achieve legalization, the amendment also adds a new subparagraph (iii) to MDL 284(1) which authorizes the Loft Board, upon application by the owner, to grant an extension of any of the new deadlines where "the owner demonstrates that he/she has made good faith efforts to satisfy the requirements" and the owner is "unable to satisfy any requirements specified in paragraph (ii) of this subdivision for reasons beyond his/her control." while the original 1982 statute empowered the Loft Board to "twice extend the time of compliance with the requirement to obtain a residential certificate of occupancy for periods not to exceed 12 months each," such extension could be granted only where the owner had proved his or her compliance with the fire and safety standards of Article 7-B. Under the 1992 amendment, the Loft Board's power to grant relief to an owner who has acted in good faith but has been unable to meet any of the deadlines for reasons beyond his or her control is no longer limited in such a manner.

The 1992 amendment also addresses the issue of the amount of rent owners may collect during the code compliance process. Amending MDL 286(2), the statute now provides that the base rent "for residential units in [IMD's) that are not yet in compliance with" §284(1) shall be increased by 6 percent upon the owners' filing

of an alteration application, an additional 8 percent upon obtaining an alteration permit and an additional 6 percent upon achieving Article 7-B compliance. If any of these steps have already been achieved, the amendment authorizes immediate prospective adjustments in corresponding percentages. Thus, an owner who has achieved Article 7-B compliance is entitled to a prospective increase equal to 20 percent [6 percent + 8 percent + 6 percent] of the base rent. The amendment further provides that these rent adjustments are inapplicable to loft units that were rented at market value after June 21, 1982.

As stated, under the 1982 law and the Loft Board's Order No. 1, owners were entitled to collect a one time only lease expiration rent increase prior to obtaining a certificate of occupancy and the establishment of the Loft Board of an initial legal rent. The amended MDL 286(2) now authorizes several prospective rent adjustments during the legalization process.

The 1992 amendment contains some additional "finetuning" of the Loft Law and of Article 7-B. However, the most significant changes in the law are clearly the legalization deadline extensions and rent adjustment provisions.

Open Issues

While the 10-year old Loft Law surely was in need of a facelift, many unresolved issues were not addressed by the Legislature and the competing interests of loft owners and tenants will undoubtedly keep the Loft Board busy and the courts involved in this area. The Legislature, subject to intense lobbying by both owner and tenant groups, also appeared, quite intentionally, to defer several issues of interpretation to others. The obvious issue of whether owners, who now and in the future may be deemed in compliance, may collect the substantial rents that their tenants may have withheld as a result of the owners' non-compliance prior to the 1992 amendment, is an issue that the drafters of the 1992 amendment plainly avoided. With respect to prospective rents, while the amendment appears to suggest that owners should be "deemed in compliance" immediately since the Oct. 1, 1992 deadline for filing an alteration permit has not yet passed, a tenant may argue that the "deemed in compliance" status is only triggered by the actual filing of the alteration application by the Oct. 1, 1992 deadline.

The 1992 amendment also creates a potential anomaly that will undoubtedly have to be addressed by the Loft Board or the courts. The new schedule of rent increases provided for in MDL 286(2) applies to units "that are not yet in compliance with the requirements of [MDL 284(1)]." MDL 284(1) is the section that requires the owner to pursue various steps to ultimately obtain a residential certificate of occupancy. However, in some instances, owners have already obtained a certificate of occupancy but the tenants' initial legal rents have not yet been established by the Loft Board - the final statutory stage for an IMD building before the residential tenants enter the rent stabilization system - either because the owner has not yet filed the legalization rent adjustment application or such application is

pending before the Loft Board. A literal reading of the amended statute would seem to suggest that these owners are not entitled to collect any interim rent increases. However, if an owner who has complied with the law and obtained a residential certificate of occupancy (but whose building has not yet been removed from the Loft Law process by the Loft Board's establishment of initial rents) may not collect the 20 percent interim rent increase available to those owners who have not yet obtained a certificate of occupancy but have achieved Article 7-B compliance, then the amended statute contains a glaring defect that will result in an obvious injustice in these limited situations.

Conclusion

As the term "interim multiple dwelling" suggests, the Loft Law was intended to be a temporary measure to regulate the legal conversion of formerly commercial and industrial space that had been illegally converted to residential use. The significant 1992 amendment and the extension of the law for another five years are a testament to the fact that the law has not yet nearly fulfilled its purpose. While the Loft Law, by virtue of its transitional scheme, should not be expected to become as embedded in New York city's culture as other temporary rent regulatory measures, it is clear enough that IMDs will continue to remain part of the city's landscape for some time. Practitioners in this field can take comfort from the many issues left unanswered or unadressed by the recent amendment that much of the law in this uniquely specialized area remains uncharted territory and loft disputes will continue to be an interesting and fertile ground for litigation well into the 1990s.

FNa Stanley M. Kaufman, a partner in Mandel & Resnik, P.C., specializes in real estate and commercial litgation. David F. Yahner, counsel to Mandel & Resnik and a former hearing officer at the New York City Loft Board, assisted in the preparation of this article. Certain statistics were supplied by Lee Fawkes, director of the Loft Board.

FN1 Chapter 349 of Laws of 1982.

FN2 E.g., Dworkan v. Duncan, 116 Misc2d 853, 456 NYS2d 939 (Civ.Ct. N.Y. Co. 1982).

FN3 MDL §281.

FN4 MDL Article 7-B, originally enacted in 1964, prescribes minimum fire and safety standards for loft, commercial or manufacturing buildings coverted to residential use.

FN5 MDL §284(1)(i).

FN6 MDL §286(1) and (2).

FN7 MDL §286(2).

FN8 See, e.g., Lipkis v. Pikus, 99 Misc2d 518, 416 NYS2d 694 (App. Tm. 1st Dept. 1979), aff'd, 72 AD2d 697, 421 NYS2d 825 (1st Dept. 1979).

FN9 In 126 Front Street Realty Co. v. New York City Loft Board, 126 AD2d 646, 510 NYS2d 902 (2d Dept. 1987), the Appellate Division, Second Department, rejected an Article 78 challenge to the legality of the "one time only" rent increase formula established by the Loft Board in its Order No. 1.

FN10 According to statistics maintained by the Loft Board, as of June 24, 1992, only 166 IMD buildings out of a total of 769 required to be legalized had obtained certificates of occupancy.

FN11 MDL §281(2).

FN12 Chapter 466, Laws of 1987, adding MDL §281(4).

FN13 In fact, comprehensive "loft" amendments to the New York City Zoning Resolution were enacted in 1981 in conjunction with and in anticipation of the Legislature's enactment of the Loft Law and the city was an active player in the Loft Law's enactment. In addition, MDL §280, the "Legislative findings" section, states, in pertinent part, that "the intervention of the state and local governments is necessary to effectuate legalization, consistent with the zoning resolution, of the present illegal living arrangements in such 'de facto' multiple dwellings ..."

FN14 MDL §285(1).

FN15 144 Misc2d 316, 547 NYS2d 978 (App. Tm. 1st Dept.).

FN16 161 AD2d 537, 556, NYS2d 533 (1st Dept. 1990).

FN17 171 AD2d 458, 567 NYS2d 41 (1st Dept. 1991).

FN18 NYLJ 1-30-92 p.25, c.4.

9/9/92 NYLJ 1, (col. 1)

END OF DOCUMENT