

Major Capital Improvement 'Useful Life' Requirement

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New York Law Journal

11-02-2011

Few issues in the field of rent regulation are as hotly contested as major capital improvement (MCI) rent increases. On the surface, an owner's MCI application would not seem overly controversial: the owner installs much needed equipment in a building—such as a boiler or new windows—and in exchange receives a modest (albeit permanent) rent increase. The tenants get an improved building, and the owner gets an increase in rents. In theory, everybody wins.

The reality is different. Some tenants will oppose any increase, even if they substantially benefit from the work. And some owners may perform shoddy or unnecessary work just to increase rents.

The Division of Housing and Community Renewal (DHCR) has enacted various regulations to clarify eligibility requirements and to diffuse some of these controversies. Thus, §2522.4(a)(2)(i) of the Rent Stabilization Code (RSC) provides that an MCI must meet all of the following criteria:

(a) deemed depreciable under the Internal Revenue Code, other than for ordinary repairs; and

(b) is for the operation, preservation, and maintenance of the structure; and

(c) is an improvement to the building or to the building complex which inures directly or indirectly to the benefit of all tenants, and which includes the same work performed in all similar components of the building or building complex, unless the owner can satisfactorily demonstrate to DHCR that certain of such similar components did not require improvement....

Section 2522.4(a) sets forth a "Schedule of Major Capital Improvements," i.e., a list of work that, assuming all other criteria are met, would qualify an owner for MCI rent increases. The list covers everything from aluminum siding to water tanks. Among the most common MCIs are boiler/burner work, parapet work, pointing and waterproofing, electrical re-wiring, roofing work, and new windows.

Section 2522.4(a)(2)(i)(d) states that work will only qualify as an MCI where "the item being replaced meets the requirements set forth on the following useful life schedule..." DHCR's "Useful Life Schedule for Major Capital Improvements," found in RSC §2522.4, clarifies how long an installation must last before an owner will be granted an MCI rent increase for that installation. In [Matter of Ghiggeri v. New York State Div. of Hous. & Comm. Renewal](#), NYLJ, Nov. 25, 2009, at 29, col. 1 (Sup. Ct. N.Y. Co.). DHCR described the useful life requirement as "intended to protect tenants from repeated or unnecessary rent increases."

However, DHCR recognized that for various reasons, an owner may have to replace an item before its useful life has expired. RSC §2522.4(e)(1) allows an owner to seek a useful life "waiver" from DHCR, as follows:

An owner who wishes to request a waiver of the useful life requirement...must apply to the DHCR for such waiver prior to the commencement of the work for which he or she will be seeking a major capital improvement rent increase. Notwithstanding this requirement, where the waiver requested is for an item being replaced because of an emergency, which causes the building or any part thereof to be dangerous to human life and safety or detrimental to health, an owner may apply to the DHCR for such waiver at the time he or she submits the major capital improvement rent increase application.

'925 D Realty LLC'

All of this brings us to the Appellate Division, First Department's recent decision in [925 D Realty LLC v. New York State Div. of Hous. & Comm. Renewal](#).¹ This case concerned two separate elevator projects at the subject building. DHCR's Useful Life Schedule divides elevator work into two categories: (1) "Major Upgrade," and (2) "Controller and Selector." Both have an estimated useful life of 25 years.

In *925 D Realty LLC*, the former owner of a building obtained from DHCR on Feb. 25, 1993 an MCI rent increase of \$1.97 per room per month based upon elevator work performed at a cost of \$16,300 to correct a Department of Buildings violation. The work, which was completed in or about 1991, related solely to the installation of a new controller and brake. The work was thus "controller and selector" work—not a "major upgrade"—as evidenced by its modest cost.

On Jan. 31, 2007, a successor owner of the subject building filed with DHCR an application for MCI rent increases based on a \$229,861.43 major upgrade to the elevator. This work consisted of elevator upgrading (\$196,100), associated electrical work (\$6,400), associated consulting fees (\$9,161.43), and associated restoration work (\$18,200). In short, the entire elevator, including the controller and selector, were replaced.

On Oct. 25, 2007, DHCR's Rent Administrator (RA) issued an order denying the owner's MCI application. The RA held that because the useful life of the controller and selector work performed at the subject building in 1991 had not yet expired, the owner could not obtain MCI rent increases for the major upgrade.

The owner thereafter filed a Petition for Administrative Review (PAR), arguing that the MCI granted in 1993 for the controller and selector work did not constitute a basis for denying the owner's subsequent MCI application for major upgrade work at approximately 14 times the cost. On Jan. 14, 2009, DHCR denied the owner's PAR, ruling that the RA had properly denied the owner's MCI application for the major upgrade because the owner had not sought a waiver of the useful life requirement.

The owner thereafter commenced an Article 78 proceeding before New York County Supreme Court Justice Eileen Rakower. [Justice Rakower denied](#) the owner's Article 78 petition, holding in relevant part:

Equally unavailing is Petitioner's argument that a waiver was not required because the nature of the current elevator upgrading was much greater in scope than the prior upgrading. While this might have been a compelling argument for granting Petitioner a waiver had it timely applied for one, the Rent Stabilization Code provides that, unless a waiver is obtained, the useful life span of a 'major upgrade' to an elevator is twenty-five years. Accordingly, the 1993 MCI rent increase precludes an additional MCI rent increase for the current upgrading.

The owner then appealed to the Appellate Division, First Department. The owner asserted that DHCR's useful life/waiver policy was intended to prevent tenants from paying twice for the same work within its useful life. Because DHCR itself conceded that a major upgrade was different than controller and selector work, there was no such danger. The only overlap between the two projects was that the 2007 major upgrade encompassed controller and brake work, which was the subject of the 1991 project that resulted in the 1993 MCI.

DHCR argued that a useful life waiver was required because although the scope of the work for the two projects was different, the work "was performed on the same component of the building, the elevator."

In response, the owner observed that notwithstanding the de minimis overlap, the two projects were completely different in scope. The owner also pointed out that DHCR's policy created a dilemma for owners and for tenants alike. Assume that a building elevator only requires a new controller and selector. A sensible owner would perform the controller and selector work only, obtaining (as here) a small MCI rent increase and sparing the tenants a much larger MCI rent increase for an unnecessary major upgrade. But if the owner took that sensible course, then, according to DHCR's logic, it would be completely barred from obtaining any form of elevator MCI for the next 25 years.

Thus, if the elevator as a whole needed to be replaced during that 25-year useful life period, the owner would be barred from collecting an MCI rent increase for a major upgrade. The tenants would then get a new elevator without having to pay for it. DHCR's policy, perversely, encourages owners to always perform major upgrade work, whether or not such work is needed.

The Appellate Division, First Department agreed with the owner, stating succinctly:

Under the circumstances of this case, it was arbitrary and capricious for respondent to fail to recognize that the 2007 MCI was completely different from the 1991 MCI. Accordingly, we reverse and remand for further proceedings consistent herewith. To the extent that there may be any overlap, no rent increase should be granted that duplicates the MCI rent increase in 1993.

Justice Luis A. Gonzales disagreed, writing in dissent:

It is also argued that the 25-year useful-life requirement for the prior MCI should not apply because the present application contemplates work different from that which was approved in 1993. Both claims were rejected by the agency, whose expertise in interpreting its statutes and regulations is entitled to deference unless shown to be irrational or unreasonable. Mindful of our limited standard of review, I would affirm the judgment appealed.

The First Department majority offered a pragmatic solution to the problem: grant the major upgrade MCI, but take into account the earlier controller and selector work, which had not yet exhausted its useful life. Conversely, the majority rejected DHCR's rigid "all or nothing" approach, which would have unduly penalized the owner, and would have granted a windfall to the tenants.

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Endnotes:

1. 85 A.D.3d 649, 925 N.Y.S.2d 822 (1st Dept. 2011). In the interest of full disclosure, Jeffrey Turkel of Rosenberg & Estis, P.C., co-author of this article, represented the owner in that case.

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