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Penn Central v. City of New York: A Landmark Landmark Case

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I. Introduction

Governmental land use regulations such as zoning, historical districting, landmark designation and eminent domain are often flies in the ointment of real property owners. Although there is general agreement concerning the need for a thoughtful plan for community realty growth and development, individual land owners and developers often resent governmental limitations on their entrepreneurial schemes. The debate between the urban planners and the laissez-faire realty developers has raged since the United States Supreme Court first approved governmental zoning regulations in *Euclid v. Ambler Realty Co.*

This Note will examine the controversy over governmental regulation of realty, focusing on the operation of the New York City Landmarks Preservation Act. The Act and the various cases which have been decided thereunder will be compared to similar methods of realty regulation. A focus will be placed on the uniqueness of a recent evolving statutory standard in the Landmark Act and other general trends in the overall scheme and legal analysis of governmental land use regulation.

II. New York City Landmarks Preservation Act

The purpose of the New York City Landmarks Preservation Act (Landmark Act) is to preserve unique physical reminders of the City's past which, if destroyed, would amount to an irreplaceable loss to the "education, pleasure and welfare" of New York's several million inhabitants. It defines a landmark as "[a]ny improvement, any part of which is thirty years old or older, which has a special character or special historical or aesthetic interest of value as part of the development, heritage or cultural characteristics of the city, state or nation and which has been designated as a landmark pursuant to the provisions of [the Act]."

3. Id. § 205-1.0 (b).
4. Id. § 207-1.0 (n).
The New York City Landmarks Preservation Commission (Commission) is a body of eleven persons empowered to designate buildings as landmarks and monitor statutory compliance by real property owners whose buildings are protected under the Landmark Act. The Commission is composed of three architects, one city planner or landscape architect, one historian, one realtor and one representative from each of New York City's five boroughs. The Commission designates buildings to be registered as landmarks or historical districts through a public hearing procedure. This process requires public notice of the Commission's agenda and a public hearing open to anyone who wishes to challenge proposed designations.

Once a building has been designated as a landmark, the Commission may regulate and restrict the conditions of ownership of that structure. An owner of a designated landmark may not alter, demolish or change the use of the structure without the Commission's permission which is given through the issuance of a certificate of appropriateness. The Commission considers issuance of certificates at public hearings on landowner requests for changes in use, alterations or demolition and decides the outcome within ninety days.

Although the Commission may limit the beneficial use of a designated landmark, the property owner is still entitled to realize a six percent return on the money invested in the realty. If there is no possibility of the owner realizing a reasonable return on his real property, the Commission may direct the city to grant the landowner certain ameliorative benefits such as tax exemptions, tax remissions, plans for alteration and reconstruction or any combina-

5. NEW YORK, N.Y., ADMIN. CODE ANN. ch. 21, § 534 (1976).
6. Id.
7. Landmark Act § 207-2.0.
8. Id. § 207-12.0.
9. Id. § 207-3.0. The Landmark Act gives the Commission a carte blanche in this area. The scope of restrictions on sale, alteration and demolition exceeds the Commission's enumerated powers as set out in the Landmark Act. For example, the Commission has full discretion as to the restrictions, such as limitations on use and alteration, it may place on a landmark structure which has been offered for sale.
10. Id. § 207-6.0.
11. Id. § 207-8.0(g)(2).
12. Id. § 207.1.0(v). The landowner is entitled to realize the six percent return on the sale or rental of the property.
tion of the above.\textsuperscript{13}

The various measures set out in the Landmark Act may not be adequate in instances where the real property owner makes a reasonable request for demolition of the landmark structure. If the owner makes such a request, the Commission may stay any action for 180 days.\textsuperscript{14} During this period, it may search for a purchaser of the property subject to the landmark restrictions thereon. If the Commission is unable to find a purchaser, it may institute another stay of ninety days during which time it may attempt to obtain the purchase price of the structure from New York City.\textsuperscript{15}

The Commission uses the statutory provisions of the Landmark Act as insurance against a rapidly vanishing "old New York." Designations, restrictions and alternatives to demolition are the tools which enable the Commission to guarantee to the people of the city that private landowners cannot put myopic financial considerations above the need to preserve the rich urban architectural heritage.

Federal tax law\textsuperscript{16} and transferable air development rights\textsuperscript{17} are two important ancillary ingredients of landmark preservation. They are designed to ameliorate the sometimes harsh effect of landmark regulation on the private land owner in possession of a landmark.

Several provisions of the Internal Revenue Code provide tax incentives to people who want to purchase or remain in possession of designated historical sites. Owners may accelerate the amortization of costs to rehabilitate the landmark.\textsuperscript{18} They may calculate the tax base of the building as if it were possessed by its original owner during the period of its original use.\textsuperscript{19} Original use treatment allows the owners to claim accelerated depreciation deductions based upon a longer depreciable life of the structure which has already depreciated substantially.

Unfortunately, the provisions of the Code are a "Catch-22" for many landmark owners. One cannot use these provisions unless the

\begin{footnotes}
\item[13] Id. § 207-8.0.
\item[14] Id. § 207-8.0(i)(4)(a).
\item[15] Id. § 207-8.0(i)(4)(b).
\item[16] See generally, I.R.C. §§ 167, 191.
\item[18] I.R.C. § 191.
\item[19] Id. § 167(c)(2). Tax treatment of the structure would be based on the value of the improvement as if it were undepreciated. This would allow for a full schedule of building depreciation as if the new owner was occupying a new building for the first time.
\end{footnotes}
site has been certified as a historical landmark. A certified site must be listed in the National Register, the Department of the Interior register or registered pursuant to state or local statutes including municipal ordinances which are recognized by the federal government for tax purposes. This limits the tax advantages to only those landmark owners who enjoy an official New York City or federal landmark designation. The tax code also limits the applicability of these tax incentives to landmarks which are income productive or used in a trade or business rather than those used as residential dwellings.

Certain sections of the federal tax code disallow landmark tax advantages where there has been demolition and reconstruction on a landmark site. If the purchaser of a landmark site demolishes the historic edifice and replaces it with a new structure, he must add the cost of demolition to the tax base of the land underneath the structure. This increases the taxable value of the property and consequently the new owner's or lessee's tax burden. Furthermore, the new owner or lessee cannot use an accelerated depreciation rate, thus preventing him from writing off an advantageously large amount of depreciation during the beginning of the new building's useful life when he should be trying to minimize his liabilities in light of construction and finance costs.

Transferable air development rights allow a person who has built or purchased a building which does not extend to the upward reaches of space; according to height limitations as mandated by local ordinances, to transfer the unused footage to another site where it can be tacked onto another structure or parcel. Zoning height limitations are determined by a formula which takes into account the height, bulk and density of a structure. This floor area

20. Id. § 191(d)(1).
22. I.R.C. § 167(a). This would exclude landmarks used as dwellings exclusive of their ability to produce income for their landlord, the landmark owner.
23. I.R.C. § 280B(a)(1); § 280B(a)(2); § 167(i).
25. Id. § 167(i).
ratio (FAR)\textsuperscript{27} is used to calculate the height development potential of geographic areas within the urban area.

"Traditionally, the New York City zoning laws have permitted the transfer of air rights between contiguous building sites held in common ownership."\textsuperscript{28} Transferable air development rights in active commercial areas such as midtown Manhattan no longer need be contiguous, although the traditional rule still applies to less active commercial and residential areas.\textsuperscript{29} The doctrine of transferability allows the landmark owner who has foregone potential air development rights to apply those rights to other parcels of realty under his ownership. This ameliorates the harshness of Landmark Act provisions which prevent the demolition of landmark structures and their replacement with skyscrapers.

Transferability aids only those persons who have other buildings which can make use of the development potential.\textsuperscript{30} Furthermore, unless the transfer and tacking of the excess is made during a period of a "healthy private development market,"\textsuperscript{31} it will be difficult for the owner to find a lessee or a purchaser for his property even though it bears a greater air development right.

\textbf{III. Landmark Preservation as Land Use Regulation}

Few landmark regulation cases discuss all of the essential aspects of land use regulation. Fortunately, regulations analogous to landmark preservation aptly illustrate the general concepts of governmental land use regulation.

Zoning is "the legislative division of a community into areas in each of which only certain designated uses of land are permitted so that the community may develop in an orderly manner in accordance with a comprehensive plan."\textsuperscript{32} Eminent domain, a stricter form of land use regulation, is "the power of the nation or a sovereign state to take, or to authorize the taking of, private property for a

\textsuperscript{27} Id. at 373. For example, if the FAR in a downtown business district permits buildings of sixty stories and a person constructs a building which is only thirty stories tall, he has theoretically amassed a transferable air development right of thirty stories.

\textsuperscript{28} Id.

\textsuperscript{29} Id. at 378. In low-density areas, the sites must be contiguous or opposite the landmark site. \textit{New York, N.Y., Zoning Resolution} §§ 74-79, 791-93 (1968).


\textsuperscript{31} Marcus, \textit{supra} note 26, at 378.

\textsuperscript{32} 82 Am. Jur. 2d \textit{Zoning} § 2, at 387 (1976).
public use without the owner's consent, conditioned upon the payment of just compensation."\textsuperscript{33} The essence of landmark regulation is akin to zoning. Preservation of landmarks by statute rests upon a legislative scheme of designated use without the compensatory thrust of eminent domain.

IV. The Purposes and Criteria for Land Use Regulation

\textit{Euclid v. Ambler Realty Co.}\textsuperscript{34} was the first case in which the United States Supreme Court upheld a challenged zoning ordinance. The Village of Euclid, just outside of Cleveland, is a suburb once noted for its unspoiled character.\textsuperscript{35} In the wake of World War I, the village passed zoning regulations to insulate its realty from the ravages of the industrial boom in Cleveland. The Ambler Realty Company claimed that the local ordinances constituted a fourteenth amendment taking of property without due process because of depressed realty values due to commercial land use restrictions.\textsuperscript{36}

The Supreme Court decided that, as a general principle, zoning statutes do not violate a private realtor's constitutional right to due process if the legislation is neither arbitrary nor unreasonable and bears a "substantial relation to public health, safety, morals, or general welfare."\textsuperscript{37}

The Court extended the doctrine of zoning in the public interest or for the general welfare to include zoning regulations for aesthetic purposes in \textit{Berman v. Parker.}\textsuperscript{38} Here, petitioner alleged that a District of Columbia land development statute\textsuperscript{39} which entitled the community to mandate specific limitations on land use to achieve the goals of an urban master plan amounted to a deprivation of property without due process or just compensation under the fifth amendment.\textsuperscript{40} The Court's opinion, by Mr. Justice Douglas, declared that

miserable and disreputable housing conditions may do more than spread disease and crime and immorality. They may also suffocate the spirit by

\begin{itemize}
\item \textsuperscript{33} 26 AM. JUR. 2d, Eminent Domain § 1, at 638 (1966).
\item \textsuperscript{34} 272 U.S. 365 (1926).
\item \textsuperscript{35} Id. at 379-80.
\item \textsuperscript{36} Id. at 384.
\item \textsuperscript{37} Id. at 395.
\item \textsuperscript{38} 348 U.S. 26 (1954).
\item \textsuperscript{39} District of Columbia Redevelopment Act of 1945, 60 Stat. 790 (codified at D.C. Code §§ 5-701 to 5-719 (1951)).
\item \textsuperscript{40} 348 U.S. at 31.
\end{itemize}
reducing the people who live there to the status of cattle. . . . They may also be an ugly sore, a blight on the community which robs it of charm, which makes it a place from which men turn. . . . [A legislature may insure] that the community should be beautiful as well as healthy.41

The New York Court of Appeals adopted the aesthetic criterion of land use regulation in People v. Stover.42 Petitioner protested the high taxes in Rye, New York by hanging dirty rags on a clothesline in her front yard in violation of a 1961 local ordinance forbidding the use of a clothesline on property abutting the streets unless the property owner petitioned the city manager for a clothesline permit because she had no other place to hang her wash.43 First, the court said, “[w]e have actually recognized the governmental interest in preserving the appearance of the community. . . .”44 Then the court held that “once it be conceded that aesthetics is a valid subject of legislative concern, the conclusion seems inescapable that reasonable legislation designed to promote that end is a valid and permissible exercise of the police power.”45

This decision led the New York Supreme Court to extend the aesthetics doctrine as a reasonable zoning criterion in Landmark Act litigation by holding “the promotion of the general welfare includes the historical and cultural purpose envisaged by the City Law.”46

These cases establish zoning as an allowable function of the legislature and aesthetics as an allowable criterion for zoning and landmark regulation if the legislation is reasonable and in furtherance of a public interest. Since the concept of aesthetics as a criterion for

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41. Id. at 32-33. See also Pearlmutter v. Green, 259 N.Y. 327, 182 N.E. 5 (1932) (dictum). In this case, the New York Court of Appeals anticipated the Berman decision by holding that the state may obstruct the view of a billboard abutting a public highway for both safety and aesthetic reasons. The court declared that “beauty may not be queen but she is not an outcast beyond the pale of protection or respect. She may at least shelter herself under the wing of safety, morality or decency.” Id. at 332, 182 N.E. at 6.
43. Id. at 465, 191 N.E.2d at 273-74, 240 N.Y.S.2d at 735-36.
44. Id. at 466-67, 191 N.E.2d at 274, 240 N.Y.S.2d 737.
45. Id. at 467, 191 N.E.2d at 275, 240 N.Y.S.2d at 738.
46. Manhattan Club v. Landmarks Preservation Comm’n, 51 Misc. 2d 556, 560, 273 N.Y.S.2d 848, 852 (1966). In this case, the plaintiff, a New York City social club, claimed that its landmark designation (of a French Second Empire structure once owned by Jennie Jerome) impaired a private contract for its sale in violation of the due process clause of the fourteenth amendment. Id. at 557-58, 273 N.Y.S.2d at 850.
land use regulation is no longer a controversial issue, the focus of zoning and landmark preservation litigation has shifted towards the creation of a standard for the reasonableness of such regulation.47

In Pennsylvania Coal Co. v. Mahon,48 the petitioner claimed that a Pennsylvania statute49 preventing him from exercising his contractual right to mine coal on another person's land constituted a due process violation under the fourteenth amendment.50 The United States Supreme Court held that this statute was violative of "[t]he general rule . . . that while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking."51

One of the New York Court of Appeals' earliest formulations of the reasonableness standard52 declared that

[i]t is not necessary, in order to render a statute obnoxious to the restraints of the Constitution, that it must in terms or in effect authorize an actual taking of the property or of the thing itself, so long as it affects its free use and enjoyment, or the power of disposition at the will of the owner.53

The doctrine of unreasonable regulation as confiscation is a generally accepted standard for testing the constitutionality of zoning and landmark preservation regulations. The doctrine has produced widely differing results.54 Although the rationale of each of the pre-

47. E.g., Board of Educ. v. City of Glen Cove, 29 N.Y.2d 681, 274 N.E.2d 749, 325 N.Y.S.2d 415 (1971). The New York Court of Appeals held that a local ordinance requiring one acre lot minimums for residential developments adjacent to a school was unreasonable "having no rational relation to the location or nature of the land itself." Id. at 683, 274 N.E.2d at 749, 325 N.Y.S.2d at 416.
50. 260 U.S. at 394-95.
51. Id. at 415.
52. Forster v. Scott, 136 N.Y. 577, 32 N.E.976 (1893). Here, petitioner successfully challenged a New York City ordinance which said that if municipal plans, plats, maps or diagrams indicated that private improvements were built in the path of streets and public squares which were registered prior to the improvement, then the landowner was on notice and the municipality need not provide compensation for the loss of the improvement. Id. at 582, 32 N.E. at 977.
53. Id. at 584, 32 N.E. at 977. See also Vernon Park Realty v. City of Mt. Vernon, 307 N.Y. 493, 121 N.E.2d 517 (1954). Petitioner's realty in downtown Mt. Vernon, New York was zoned only for a parking garage although he wanted to construct a shopping center on the property. The court held that the zoning was unreasonable because the realty was situated among commercial lots and only petitioner's lot had been arbitrarily singled out and substantially robbed of its value by the limitation on its free use. Id. at 499, 121 N.E. at 520.
54. Although the courts have been wrestling with this issue for the last twenty years, they generally fail to specify the terms of the test and the degree of the restriction which is acceptable or too burdensome.
viously discussed opinions seems clear enough, the case by case weighing of the reasonableness of these restrictions remains hazy and uneven.

Courts have been willing to deprive a private land owner of a substantial or the full beneficial use of his property in spite of due process considerations. This line of cases upheld various zoning statutes as reasonable in light of certain public interests. In Goldblatt v. Town of Hempstead, the United States Supreme Court held that a zoning regulation which banned quarry excavation in Hempstead, New York and forced petitioner to go out of business was a proper exercise of the police power. A New York Court of Appeals decision held the de facto ban on a housing development due to statutory lot size minimums to be a valid exercise of the police power. In this decision, the court held that "restrictions upon the unencumbered use of property, quite apart from its professed purposes, will have an adverse effect upon its market value. That hardship is inevitably the product of police regulation and the pecuniary rights . . . of common weal."

This position has been reaffirmed by the New York Court of Appeals in subsequent proceedings. The court reiterated its past position that the exercise of the police power to regulate land use, even to the point of a complete denial of beneficial use, can be justified as protection of the public interest if it is "within the limits of necessity." The court added the proviso that, even if such a regulation should be found to be confiscatory, it would not be a compensable taking unless the government intended to deprive the private

55. "Beneficial use" is "[the right to use and enjoy property according to one's own liking or so as to derive profit or benefit from it. . .]" BLACK'S LAW DICTIONARY 199 (4th ed. rev. 1968).
57. Id. at 596. "If this ordinance is otherwise a valid exercise of the town's police powers, the fact that it deprives the property of its most beneficial use does not render it unconstitutional." Id. at 592.
58. Salamar Builders v. Tuttle, 29 N.Y.2d 221, 275 N.E.2d 585, 325 N.Y.S.2d 933 (1971). The lot size minimums were required to prevent septic tank pollution.
59. Id. at 225, 275 N.E.2d at 588, 325 N.Y.S.2d at 937.
60. Charles v. Diamond, 41 N.Y.2d 318, 360 N.E.2d 1295, 392 N.Y.S.2d 594 (1977). Petitioner claimed that his property was appropriated without just compensation because he is barred from constructing a residential development in Camillus, New York until he can connect into the village sewer system although that cannot be accomplished until the village sewer system meets state environmental standards. Id. at 320, 360 N.E.2d at 1297, 392 N.Y.S.2d at 597.
61. Id. at 324, 360 N.E.2d at 1300, 392 N.Y.S.2d at 599.
real property owner of the actual use of his property so that the parcel of land would become public property in the future.  

There exists another line of New York precedents which disputes the government’s right to regulate and restrict the private real property owner’s beneficial use of his land. These opinions share the rationale that severe limitation or restriction on the beneficial use of real property is unreasonable because it is a non-compensable public taking of private property. The New York Court of Appeals shifted the focus on reasonableness to the reasonable limitation on the use and ownership of private realty rather than the reasonableness of the public interest upon which the land use regulation is legislated.

In Fred F. French Investing Co. v. City of New York, the New York Court of Appeals held that “[t]he State may not, under the guise of regulation by zoning, deprive the owner of the reasonable income productive or other private use of his property and thus destroy all but a bare residue of its economic value.” The zoning statute which was challenged in the French case prohibited the mortgagee of Tudor City which is a New York City residential complex, from financing and constructing an office building on property which was zoned for the tenants’ recreational purposes. The court held that the zoning statute amounted to a “frustration of property rights, under the guise of an exercise of the police power . . . [which] forces the owner to assume the cost of providing a benefit to the public without recoupment.” The Second Department of the Appellate Division of the New York Supreme Court in Grimpel Associates v. Cohalan, has held that while title and use remain

62. Id. at 329, 360 N.E.2d at 1303, 392 N.Y.S.2d at 603.
63. E.g., Golden v. Planning Bd. of Ramapo, 30 N.Y.2d 359, 285 N.E.2d 291, 334 N.Y.S.2d 138 (1972). A violation of the private property owner’s rights occurs when the property cannot be put to its desired use at a reasonable profit. Id. at 382, 285 N.E.2d at 304, 334 N.Y.S.2d at 155-56; Keystone Assoc. v. Moerdler, 19 N.Y.2d 78, 224 N.E.2d 700, 278 N.Y.S.2d 185 (1966). This case involved the debate over the fate of the old Metropolitan Opera House. The private owners won the right to demolish the structure in order to construct a forty story office building.
64. See note 63 supra.
66. Id. at 591, 350 N.E.2d at 383, 385 N.Y.S.2d at 7.
67. Id. at 596, 350 N.E.2d at 387, 385 N.Y.S.2d at 11.
with the owner, the free use of the real property is so severely restricted that it amounts to a confiscation.

V. Reasonableness of Regulation Under Judicial Scrutiny

Keystone Associates v. Moerdler marks an instance in which landmark preservation was subordinated to the private realty owner's right to ensure that he realizes a reasonable return on his investment. The concept of land use regulation as an unreasonable deprivation of the private property owner's right to realize a reasonable return on his investment is of paramount importance in litigation under the Landmark Act because that statute states that the private property owner is entitled to realize a reasonable return on his investment.

Thus far, land use regulation challenges have followed one of three basic tests in analyzing the reasonableness of restrictions on the property owner. The reasonable return test guarantees a reasonable return on the realty investment of the private property owner whose property is restricted by a land use regulation. Under this formula, governmental regulation which deprives the property owner of a reasonable return amounts to an unconstitutional restriction on the owner's beneficial use.

The beneficial use test forbids intrusive governmental regulation if it deprives the private property owner of a substantial portion of the beneficial use of his realty. The public interest test allows governmental regulation of land use even to the point of denying all beneficial use if the regulation promotes a clear and necessary public interest.

The courts discovered that yet another formula was necessary for regulation of real property owned by charitable and religious institutions. The reasonable return formula and its variations are work-

69. 19 N.Y.2d 78, 224 N.E.2d 700, 278 N.Y.S.2d 185 (1966); see also 51 App. Div. 2d at 801, 380 N.Y.S.2d at 282.
able within the framework of regulation of real property which is income productive or used in a trade or business. However, the formula is not successfully applicable to realty owned by not-for-profit charitable and religious groups. The New York Court of Appeals held that landmark regulation and zoning may be a bare taking of property without compensation if the regulation seriously impedes the use of the structure for the not-for-profit institution. In Lutheran Church of America v. City of New York, the New York Court of Appeals decided that a regulation which hampers the not-for-profit institution’s use of real property can amount to an economic hardship which is analogous to a taking. The court stressed that charitable institutions are given tax exemptions on the basis of their status. Since they already possess these tax breaks, they would not be able to take advantage of the tax abatements, remissions and exemptions which lie at the heart of the Landmark Act’s ameliorative powers and help to make landmark ownership tenable for commercial institutions and individuals. The court concluded that the Landmark Act violated the church’s property rights in this instance, but would not necessarily work such a result in all cases.

A new formula for testing the reasonableness of landmark preservation and zoning regulations on charitable and religious institutions was announced by the First Department of the Appellate Division in Sailors’ Snug Harbor v. Platt. A home for old sailors wanted to demolish landmark designated dormitories to provide the retired sailors with modern living facilities. The court indicated that reasonableness was still the key to all land use regulation. Commercial property is entitled to yield a reasonable return for its owner, and not-for-profit property is entitled to be regulated by reasonable restrictions which neither physically nor financially frustrate the property’s charitable purpose. This test is a variation of the beneficial use test: regulation of not-for-profit institutions is unreasonable

75. Lutheran Church in America v. City of New York, 35 N.Y.2d 121, 316 N.E.2d 305, 359 N.Y.S.2d 7 (1974). Here, the church needed additional office space but it could not expand its quarters because it wanted to demolish its landmark structure without the Commission’s permission.
76. Id. at 128, 316 N.E.2d at 307, 359 N.Y.S.2d at 14.
77. Id. at 124, 316 N.E.2d at 307, 359 N.Y.S.2d at 10.
78. Id. at 130, 316 N.E.2d at 311, 359 N.Y.S.2d at 15.
80. Id. at 379, 288 N.Y.S.2d at 316.
81. Id.
if it deprives the owner of a substantial portion of the structure's charitable use.

All of the variables of the reasonable return and beneficial use tests revolve around the issue of whether land use regulation deprives the real property owner of the reasonable return which he expects to reap from his capital investment. Reasonable return and beneficial use are mere euphemisms for profit. The real property owner expects to realize a profit through his ownership of land. Zoning and landmark regulations often seem to defeat that purpose.

VI. The Penn Central Decision

The New York Court of Appeals confronted the issue of profit versus regulation in Penn Central Transportation Co. v. City of New York.\textsuperscript{82} The court examined the reasonable return doctrine and attempted to clarify the test as it applies to realty under the Landmark Act.\textsuperscript{83}

The case involved a proposed scheme by the Penn Central Transportation Company and UGP, a British property development firm, to build a thirty-story glass and steel tower atop the the Grand Central Terminal.\textsuperscript{84} The tower, designed by Marcel Breuer, violated the Landmark Act's prohibition on cosmetic and structural changes to the facade of landmark structures in the absence of a certificate of appropriateness issued by the Landmark Commission.\textsuperscript{85} Penn Central and UGP sued the City of New York claiming that the Landmark Act prevented the owners from realizing a reasonable return on their investment. The New York Court of Appeals agreed that "the landowner must be allowed a reasonable return or equivalent private use of his property."\textsuperscript{86} Penn Central and UGP demonstrated to the court that no reasonable return was possible on the basis of the appraised value of the Grand Central Terminal at that time. The court agreed that while a reasonable return was not possible based on the current appraised value, a reasonable return could be realized under a new judicially-created formula for valuation of


\textsuperscript{83} Id. at 327, 366 N.E.2d at 1272-73, 397 N.Y.S.2d at 915-16.

\textsuperscript{84} Kibbe, Landmark Preservation—A Survey, Art & the Law, Apr.-May, 1976, at 2, col. 2. Therein lies a description of Penn Central's plan for the structural modification and expansion of the terminal property.

\textsuperscript{85} See note 4 supra.

\textsuperscript{86} 42 N.Y.2d 324, 330-31, 366 N.E.2d 1271, 1275, 397 N.Y.S.2d 914, 918. The Landmark Act statutorily sets the reasonable return rate at six percent of the investment's commonly appraised value. See note 15 supra.
landmark structures. It held that only the value of the realty which is the product of the property owner's efforts should be guaranteed a reasonable return. The court stated that "a property owner is not absolutely entitled to receive a return on so much of the property's value as was created by social investment."

Grand Central Terminal was built between 1907 and 1913 by Warren & Wetmore, Reed & Stem. It is credited as one of the great "Beaux-Arts buildings [which] were built to inspire. They remain the moral statements, self-perceptions, and the grand accomplishments of an era." The building was registered as an historical landmark on August 2, 1967 by the Landmark Commission.

The New York Court of Appeals noted that "society as an organized entity, especially through its government, rather than as a mere conglomerate of individuals, has created much of the value of the terminal property." In addition to the affection which the local citizenry holds for the terminal, the citizenry, in its role as the government, has showered the terminal with distinctions of great economic benefit. The local government granted Penn Central a monopoly on the right of way for the railroad tracks entering Manhattan, various tax advantages and exemptions and connections with all of the major mass transit facilities in New York City. The court said: "Absent this heavy public governmental investment in the terminal, the railroads, and the connecting transportation, it is indisputable that the terminal property would be worth but a fraction of its current economic value."

The sentimental value attributed to the terminal by the populace, the easements for the railroad right of way, the tax advantages and the mass transit connections all have a tangible value which, in turn, gives value to the terminal structure. Although the quantification of the value that these items bestow upon the terminal is difficult to measure, the New York Court of Appeals insisted that the task could and should be performed. This new formulation for the

87. Id. at 328, 366 N.E.2d at 1273, 397 N.Y.S.2d at 916.
88. Id. at 336, 366 N.E.2d at 1278, 397 N.Y.S.2d at 921.
90. Id.
91. 42 N.Y.2d at 328, 366 N.E.2d at 1273, 397 N.Y.S.2d at 916.
92. Id. at 332, 366 N.E.2d at 1275, 397 N.Y.S.2d at 918.
93. Id., 366 N.E.2d at 1275-76, 397 N.Y.S.2d at 919.
94. Id., 366 N.E.2d at 1276, 397 N.Y.S.2d at 919.
95. Id. at 333, 366 N.E.2d at 1276, 397 N.Y.S.2d at 919. For example, if a court decides
valuation of a reasonable return states that the assessed value of landmark property (for the purpose of tabulating a reasonable return) equals the commonly assessed value of the landmark realty less the value of the landmark which is attributable to social investment.

Although this new formula depresses the private property assessment value of the landmark so that the six percent return yields a lesser dollar amount based on a lower realty value, the *Penn Central* case presents a situation in which there is no reasonable return at all. The Penn Central Transportation Company claimed that, as to the terminal, they were consistently in debt; nevertheless, the New York Court of Appeals said that the terminal may take a loss and at the same time appreciate the value of adjacent Penn Central properties such as Park Avenue and several adjacent hotels so that they may realize an overall reasonable return. The attribution of value to adjacent properties by the terminal stems from the convenience of travel to and the centrality of the terminal which benefits these properties. The aggregation of these appreciated properties adjacent to the landmark is an ancillary feature of the new method of landmark realty valuation which rarely benefits anyone but the large urban realtors because few people are able to amass several buildings in such an expensive commercial district.

Finally, the court increased the amount of Penn Central’s reasonable return figure by allowing the corporation to sever the undeveloped air rights above the terminal. The air development potential, the difference between the maximum construction height permitted by zoning and the actual height of a structure, was quantified and assigned a dollar value which helped to elevate the aggregate return on the properties out of the red. Although the British development corporation could not build atop the terminal, “the challenged regulation permitted splitting of the [air] development rights among several receiving parcels, to allow optimal use of the rights.”

The finalized formula as enunciated by the *Penn Central* court can be stated as a reasonable return on the real property valued

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96. Id. at 333-34, 366 N.E.2d at 1276-77, 397 N.Y.S.2d at 920.
97. Id. at 328, 366 N.E.2d at 1273, 397 N.Y.S.2d at 916.
98. Id. at 335, 366 N.E.2d at 1277, 397 N.Y.S.2d at 921.
according to the social investment theory plus profits from appreciated properties and the value of transferable air development rights.

Still at issue is whether landmark regulation pursuant to the Landmark Act is a taking without due process in violation of the fourteenth amendment despite the new method of assessment valuation and ancillary profits.

The New York Court of Appeals stated that "landmark regulation is a limitation on exploitation of property, an attribute shared with the classifications of zoning and historic districting, [(a grouping of landmark structures)]. Yet, landmark regulation is different because the burden of limitation is borne by a single owner." The Landmark Act is a land use regulation very much like zoning. Both zoning and landmark regulation are designed to benefit the community. Zoning implements a land use plan so that all people in the zoned area, including the realty owners, enjoy the benefits of the restriction against exploitation of property, while landmark preservation restricts a single landowner so that everyone else may enjoy his forbearance. The Landmark Act is a good deal more than just historical districting. Historical districting protects existing buildings while the Landmark Act regulates alteration, demolition, and changes in use and improvements. The Landmark Act is also different from eminent domain because "there is no taking for which just compensation must be paid."

The Landmark Act defies characterization as zoning, eminent domain or historic districting although it can affect property in much the same manner as any of them. The Penn Central case can be compared and distinguished from both prior landmark preservation cases and analogous zoning cases.

The Lutheran Church case held that the landmark regulation which banned demolition and construction on the site of the J.P. Morgan, Jr. mansion amounted to an unconstitutional taking of private property without just compensation. The petitioner was a charitable institution which occupied a landmark structure; there-

99. Id. at 330, 366 N.E.2d at 1274, 397 N.Y.S.2d at 917.
100. Id. at 329, 366 N.E.2d at 1274, 397 N.Y.S.2d at 917.
101. Id. at 330, 366 N.E.2d at 1274, 397 N.Y.S.2d at 917.
102. Id.
104. Id. at 132, 316 N.E.2d at 312, 359 N.Y.S.2d at 16.
fore, the owner was unable to realize a profit by owning the building. A formula for reasonableness other than the statutory six percent return rate should have been used. The Penn Central decision said that the Lutheran Church holding could not be an obstacle to social investment assessments because commercial landmark regulation observes the standards of due process unless there is a total denial of a reasonable return, while not-for-profit landmark regulation follows the substantial frustration of charitable purpose formula.

Frustration of air development rights has been held to constitute a due process violation of property rights because it is viewed as a taking of property without compensation. The French case referred to transferable air development rights as "disembodied abstractions of man's ingenuity, [which] float in a limbo." This argument did not affect the outcome of Penn Central because Penn Central, unlike the petitioner in the French case, did not lose its air development rights. Penn Central owned several good parcels of adjacent property onto which it could tack the severed air development potential. The ability to utilize these air development rights assures the property owner that their value will not be dissipated. This dispels the notion that air development rights which cannot be fully utilized on one parcel of realty will necessarily be lost.

VII. Conclusion

The Penn Central decision supports the principle of land use regulation for the aesthetic interests of the general public even in instances of substantial or complete restriction on beneficial use. The decision "should be seen as an illustration of the ability, and propensity, of the courts of New York to vary the standards with which they determine the reasonableness of restricted use in the landmark context." The general landmark test of social investment-assessment and ancillary profits is an altogether new standard which solves a unique problem through an objective test.

105. The Lutheran Church court should have applied the Snug Harbor "frustration of purpose" test.
106. 42 N.Y.2d at 334, 366 N.E.2d at 1277, 397 N.Y.S.2d at 920.
108. Id. at 598, 350 N.E.2d at 388, 385 N.Y.S.2d at 11.
110. 2 Art & the Law at 4.
which allows a great deal of interplay for the intricacies of each situation. The objective test demands that all factors of profitability be categorized into one of two groups. The arithmetic process of balancing the public investment against private investment will result in a specific value for the real property. The *Penn Central* decision stands as a new method of valuation of landmark structures and recognizes the interaction between the structure and its environment. The urban environment gives certain structures an additional quantifiable value. This value may not be attributed to the value of the structure when assessing its worth to the community. The inclusion of the social investment in the property assessment would create a double payment situation in which society enhances the value of private realty while the government guarantees that the landowner realizes a profit on its own gratuitous contribution to the structure’s value.

One critic of the *Penn Central* decision has suggested that “the *Grand Central* case is *sui generis*: the opinion [is] tailored to the *Grand Central* context.” This decision is intricate, unique and generally inapplicable to other land use regulation situations. Nonetheless, it enunciates a general principle of universal value for all land use regulation challenges.

The *Penn Central* decision opens the door for a more thorough probe into the needs of society while directing a deeper examination of the needs of the individual who is frustrated by land use restrictions. The New York Court of Appeals has demonstrated a desire to create unique programs to aid unprofitable landmark property owners so that society and the individual can enjoy a community which is designed to promote health, cohesion and beauty.

This decision is an important boon to landmark preservation challenges because it finally puts an end to society’s double payment of social benefits and governmental guarantees to the landmark owner. It is equally important as an illustration of the willingness of the courts to strike a compromise between society and the individual which guarantees the interests of both in land use controversies.

Regardless of the outcome of the final adjudication before the United States Supreme Court, this case has provided the ground-

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112. *Id.*

work for a new outlook concerning social guarantees and investment opportunities for the private property owner and the public.

Richard Wolloch

Editor's Note: The United States Supreme Court held, on June 26, 1978, that Penn Central was not entitled to compensation when New York City designated Grand Central Terminal an historical landmark. Penn Central v. City of New York, 46 U.S.L.W. 4856 (U.S. June 27, 1978) (No. 77-444). The Court upheld the New York Court of Appeals' holding that Penn Central was entitled to a "reasonable return" on its investment alone and not on the portion of the terminal's value which has been enhanced by social investment. The Court stated that "[a]greement with [Penn Central's] argument would . . . invalidate not just New York City's law, but all comparable landmark legislation in the nation. We find no merit in it." 46 U.S.L.W. at 4864.