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'Penn Central': Was It Really A 'Euclid' for Landmarks?

IMAGINE a scenario in which a real estate developer purchases several obsolete apartment buildings for the sole purpose of demolishing the buildings and developing the property to the fullest potential allowable under the New York City Zoning Resolution. As would be expected, the tenants of the apartment buildings who are either rent-controlled or rent-stabilized band together in an effort to prevent demolition.


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The tenants are joined by a host of interest groups which oppose real estate developers buying old buildings for the purpose of utilizing the zoning lot to its fullest potential. After much lobbying and letter writing, these groups prevail upon the New York City Landmarks Preservation Commission to landmark the apartment buildings pursuant to the vague standards of the New York City Landmarks Law which defines a "landmark" as:

> Any improvement, any part of which is thirty years old or older, which has a special character or special historical or aesthetic interest or value as part of the development, heritage or cultural characteristics of the city, state of nation[1] . . .

Because of the landmarking, the developer's ability to demolish the buildings and develop the property has been effectively prevented.

This article will analyze and assess the developer's prospects for a challenge to the landmarking as a regulatory taking in light of the *Penn Central* decision and the recent Supreme Court's land use cases.

In *Pennsylvania Coal v. Mahon*,[2] Justice Oliver Wendell Holmes stated, "When a regulation goes too far it will be recognized as a taking"[3] and require compensation under the just compensation clause of the Fifth

Amendment of the U.S. Constitution. Justice Holmes, however, failed to establish guidelines for determining what type of regulation would constitute "too far" in a given case.

In 1978, the Supreme Court decided *Penn Central Transportation Company v. New York City*,[4] in which it established guidelines by which a court should judge a regulatory ordinance to determine if the regulation has gone "too far" and become a taking under the Fifth Amendment. In *Penn Central*, the court stated:

> "In engaging in these essentially ad hoc, factual inquiries, the Court's decisions have identified several factors that have particular significance. The economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations are, of course, relevant considerations. So too, is the character of the governmental action."[5]

In *Penn Central*, the Court applied the above test and concluded the New York City Landmarks law as applied to prevent the construction of a 55 story office tower above Grand Central terminal did not constitute a regulatory taking, nor require compensation under the Fifth Amendment.

Several preservation advocates hailed the decision as a victory for historic preservation. Norman Marcus, former counsel to the New York City Planning Commission, hailed the decision as a *Euclid* (referring to *Village of Euclid, Ohio v. Ambler Realty Co.*, the 1926 Supreme Court opinion upholding a comprehensive zoning scheme against a Fourteenth Amendment due process claim) for landmarks and favorable notice for the New York City's transfer of development rights scheme.[6]

In light of the change in the members of the Supreme Court since 1978 and the two recent land use decisions decided in the 1986 term, *Penn Central* seems not to be the *Euclid* predicted.

'Penn Central'

In *Penn Central*, the Court was faced with the most favorable of circumstances to uphold the New York City Landmarks Law. The landmarked property was the famous Grand Central terminal which was not only the most ingenious engineering solution to the problems presented by urban railroad stations, but also a magnificent example of the French Beaux-Arts architectural style.[7]

Penn Central Transportation Company accepted for the purpose of the litigation that Grand Central Terminal was capable of earning a reasonable return without constructing a high rise office tower above the terminal.[8] that the transferable development rights available to them as a result of the landmark designation were valuable compensation for the loss of the right to construct above the terminal[9] (section 74-79 of the New York City Zoning Resolution allows the owner of a landmark to transfer development rights across the street, in addition to an adjacent lot(s). The law is theoretically intended to allow an owner to realize the full zoning value of the lot without destroying the landmark.)

In other words, the Court determined, and Penn Central Transportation did not really dispute, the "economic impact on the claimant" was minimal and the claimant could earn a reasonable return. The Court pointed out two factors which indicated that Penn Central was not denied *all* the use of the air rights above the terminal.

Several commentators and the New York Court of Appeals have pointed out the many defects of the New York City Zoning Resolution's transferrable development rights scheme . . .

First, the Court pointed out that the company had not sought permission from the Landmarks Commission to build a smaller structure above Grand Central.[10] Second, the Court pointed to the transferability of the development rights to at least eight parcels which Penn Central owned or had an interest in the vicinity of the terminal.[11] The Court in discussing the relevance of the transfer of development rights stated:

> "While these rights may well not have constituted 'just compensation' if a 'taking' had occurred, the rights nevertheless undoubtedly mitigate whatever financial burdens the law has imposed on appellants and, for that reason, are to be taken into account in considering the impact of the regulation."[12]

In sum, the Court determined the economic impact of the landmarks designation was minimal upon Penn Central and the availability of the transfer development rights along with the commercial nature of the terminal mitigated whatever financial burdens the landmark law imposed upon the appellants.

factor in the above mentioned test and determined the landmarks law did not interfere with what must be regarded as Penn Central's primary expectation concerning the use of the parcel.

The Court indicated the landmark designation not only permitted but contemplated that the appellants could continue to use the property precisely as it had been used since it was built.[13] In other words, the Court determined the landmarks law did not interfere with the appellants distinct investment-backed expectations because the landmark designation did not interfere with the primary use Penn Central contemplated with respect to the terminal.

Real Estate Developers

One can imagine many situations where the economic impact of the landmark designation is more severe upon the owner than in Penn Central. A classic example would be the real estate developer who purchases obsolete apartment buildings for the purpose of developing the zoning lot to its fullest potential.

The economic impact of the landmarking would be devastating because the developer would be stuck with obsolete apartment buildings filled with rent-controlled and below market rent-stabilized tenants. And in most situations, the developer would not be able to make use of the transfer of development rights afforded by the New York City Zoning Resolution because of the severe restrictions placed on the transfer of development rights.

Several commentators and the New York Court of Appeals have pointed out the many defects of the New York City Zoning Resolution's transferrable development rights scheme which include, but are not limited to, limiting transfers to adjacent lots and the maze of discretionary approvals necessary to transfer the development rights.[14]

The second factor in the *Penn Central* approach would also weigh heavily in favor of a real estate developer as opposed to the Penn Central with respect to Grand Central Terminal. When a real estate developer purchases obsolete apartment buildings, no reasonable person could attribute any other investment-backed expectation other than developing the property. In other words, the landmarks designation would severely interfere with a real estate developer's distinct investment-backed expectations.

In sum, *Penn Central* upheld the applicability of the New York City Landmarks Law as applied to one of the most famous buildings in the world which was capable of earning a reasonable return in its present state and which the owner could utilize the development rights made available un-

der the Zoning Resolution.

One cannot envision a more favorable set of circumstances for a court to uphold the landmarks law. Everyone is familiar with the statement "hard cases make bad law." In *Penn Central* the more appropriate phrase would be "easy cases make bad law."

Rehnquist's Dissent

Before turning to the recent Supreme Court's land use decisions, it is important to analyze the makeup of the Court's 6-3 decision in *Penn Central*.

Justice William H. Rehnquist authored a strong dissent joined by Justices John Paul Stevens and former Chief Justice Warren E. Burger. Justice Rehnquist maintained the New York City Landmarks Law was not analogous to a comprehensive zoning scheme and was precisely the type of ordinance which would trigger the Fifth Amendment's just compensation clause. He quoted from a previous Supreme Court case:

> "The Fifth Amendment's guarantee that private property shall not be taken for a public use without just compensation was designed to bar government from forcing some people alone to bear public burdens which, in all fairness and justice should be borne by the Public as a whole."[15]

Justice Rehnquist reminded the Court of Justice Holmes' oft-quoted warning from *Pennsylvania Coal v. Mahon*. "We are in danger of forgetting that a strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change."[16]

Since 1978, two of the six Justices in the majority opinion in *Penn Central* have been replaced by more conservative Justices. Justice Potter Stewart was replaced by Justice Sandra Day O'Conner who has voted with Justice Rehnquist in virtually every land use decision since she was appointed.

Justice Lewis Powell was replaced by Justice Anthony M. Kennedy who appears more conservative than Justice Powell and more influenced by Chief Justice Rehnquist. The arrival of Justice Antonin Scalia who has recently taken an interest in land use matters also tends to strengthen the force of Justice Rehnquist's dissent.

In the October 1986 term, the Supreme Court decided two land use cases which while not overturning *Penn Central* indicate the Court's lack of tolerance for land use regulators who ignore the mandate of the Fifth Amendment.

In *Nollan v. California Coastal Commission*[17] a majority of five Justices found a taking in a complicated permit exaction situation. The California Coastal Commission granted to plaintiffs a permit to build a home on the condition that they deed to the public an access easement across a small portion of the beach element of their parcel. Justice Scalia joined by Chief Justice Rehnquist and Justices Byron White, Powell and O'Conner found the conditional building permit to constitute a regulatory taking. The Court quietly established a new and more strict standard by which land use regulations must be judged. The Court stated:

> Contrary to Justice Brennan's claim . . . our opinions do not establish that these standards are the same as those applied to due process or equal protection claims. To the contrary, our verbal formulations in the taking field have generally been quite different. We have required that the regulation "substantially advance" the legitimate state interest "sought to be achieved," not that "the state could rationally have decided" the measure adopted might achieve the state's objective.[18]

As Fred P. Bosselman, a leading land use attorney, correctly notes, *Nollan* is an example of the Supreme Court's recent cases that reflect a "wide and growing gap between the treatment of economic regulation under the taking clause" by Justices Scalia and Rehnquist on one hand and Justices William Brennan and Thurgood Marshall on the other.[19]

The Supreme Court's basic message seems to be that government regulators and some lower courts have failed to pay sufficient attention to the constitutional protection assured to property owners by the Fifth Amendment.

In *Nollan*, the majority closely scrutinized the justifications put forward in support of the conditional building permit by the California Coastal Commission and seemed eager to analyze and reject any and all such justifications. The Court stated:

> "We do not share Justice Brennan's confidence . . . We view the Fifth Amendment's property clause to be more than a pleading requirement, and compliance with it to be more than an exercise in cleverness and imagination. As indicated earlier, our cases describe the condition for abridgement of the property rights through the police power as a 'substantial advancing of a legitimate state interest.' "[20]

The conservative majority indicated the Fifth Amendment is alive and well and any regulations which impinge upon a property owner's right will be subjected to a rigorous analysis to determine if the regulation passes constitutional muster.

'First English'

In *First English Evangelical Lutheran Church of Glendale v. County of Los Angeles*,[21] the Supreme Court settled the question of whether or not temporary takings require just compensation under the Fifth and Fourteenth Amendments. The Court held that temporary takings require the government to pay the landowner from the time the offending regulation is in effect until the time the courts find the regulation to constitute a taking. This time period is what the court meant by the term "temporary taking."

First English also implicates the heightened scrutiny applied in *Nollan*. It shows the Justices' concerns that governmental regulations have left property owners' rights overexposed to regulation by governmental regulations. Requiring the government to pay for overreaching regulation will force regulators to scrutinize property restrictions more carefully.

As the Court stated in *First English*:

> "We realize that our present holding will undoubtedly lessen to some extent the freedom and flexibility of land-use planners and governing bodies of municipal corporations when enacting land-use regulations. But such consequences necessarily flow from any decision upholding a claim of constitutional rights; many of the provisions of the constitution are designed to limit flexibility and freedom of governmental authorities and the just compensation clause of the Fifth Amendment is one of them."[22]

Real estate developers and land use attorneys should not take too seriously the claim that 'Penn Central' is the 'Euclid' of historic preservation.

The importance of *First English* cannot be overstressed. Once again, the Court held governmental agencies could be held monetarily liable for even good-faith overregulation. The Court held a temporary taking (the time between the enactment or restrictions of the regulatory ordinance takes effect and the time in which a court strikes down the regulatory ordinance) requires just compensation under the Fifth Amendment.

This further indicates the Court's current trend of protecting property owners' Fifth Amendment rights. The Court by requiring government to pay for overreaching land use ordinances is in effect telling legislators and land use commissions to analyze the constitutionality of the ordinance. If a court later determines the ordinance is unconstitutional, the government must compensate the landowner.

Ramifications

Nollan indicates the Court is going to scrutinize more strictly land use restrictions which impinge upon a property owner's Fifth Amendment rights.

A developer could use *Nollan* in a variety of ways in combatting the landmarking of a particular building including a situation where the Landmarks Commission designates a building for landmark status which is of questionable architectural, historical or cultural significance, or where the Landmarks Commission designates all of a developer's buildings when the buildings are all very similar, or a situation in which the owner cannot earn a reasonable return on the landmarked buildings.

First English indicates a landowner whose property is improperly landmarked can recover monetarily for the time between the landmarking and the time when a court finally declares the landmarking unconstitutional. *First English* requires the Landmarks Commission to landmark only deserving properties such as Grand Central Terminal. If the landmarking is found unconstitutional, the city will have to pay the owner for the "temporary taking."

Conclusion

Real estate developers and land use attorneys should not take too seriously the claim that *Penn Central* is the *Euclid* of historic preservation. *Penn Central* was a close decision which upheld the landmarks law as applied to Grand Central Terminal. One would have a difficult time finding a more favorable case to uphold a challenge to the New York City Landmarks Law. The change in the Supreme Court since 1978, Chief Justice Rehnquist's growing influence and the Court's recent land use decisions seem to indicate Penn Central was not the *Euclid* for landmarks but a sui generis situation.

(1) New York City Administrative Code Section 25-302(N)
(2) 260 U.S. 393(1922)
(3) ID. at 415
(4) 438 U.S.104 (1978)
(5) Id at 124.
(6) See Norman Marcus: The Grand Slam Grand Central Terminal Decision: A Euclid for landmarks, favorable notice for TDR and a resolution of the regulatory/taking impasse. 7 Ecology Law Quarterly 731 1979.
(7) 438 U.S. at 115.
(8) Id at 129
(9) Id
(10) 438 U.S. at 137
(11) Id
(12) Id
(13) 438 U.S. at 136
(14) See Costonis, "The Chicago Plan: Incentive Zoning and the Preservation of Urban Landmark" 85 Harvard L. Rev 574 (1972) See also *Penn Central Transportation Company v. City of New York* 42 N.Y.2d 324, 366 N.E. 2d 1271 (1977)
(15) 438 U.S. at 148. Quoting from *Armstrong v. United States* 364 U.S. at 49
(16) 438 U.S. at 152
(17) 107 S. Ct. 3141 (1987)
(18) Id at 3147
(19) Unpublished speech to Attorneys General of certain western states August 12, 1987
(20) 107 S. Ct. at 3151
(21) 96 L. Ed 250
(22) Id at 268

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