

PENN CENTRAL 2.0: THE TAKINGS IMPLICATIONS OF PRINTING AIR RIGHTS

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A transferable development right or “TDR” refers to the air space above a zoning lot that can be sold to neighboring landowners who seek to build structures that exceed the maximum height permitted by zoning. Until recently, if a developer in Midtown Manhattan required TDRs, he or she needed to acquire them from a landmark building. The city originally intended this scheme to benefit landmark owners, whose properties are regulated from utilizing the full envelope of their air space. However, in 2015 New York City amended its Zoning Resolution to allow developers to build higher in exchange for providing public amenities—without having to purchase TDRs from anyone.

This type of “zoning bonus” may significantly impair TDR values. Yet development bonuses often generate needed infrastructure, and whether TDRs merit the same degree of constitutional protection as land remains unclear. This Note engages in the first sustained analysis of TDRs as the principal subject of a regulatory taking by examining whether a regulation that diminishes the value of TDRs, as opposed to the underlying fee estate in land, constitutes a taking. Specifically, this Note uses Grand Central Terminal’s current claim against the City of New York as a lens through which to examine this issue. It then advances a framework by which to analyze the future generation of cases involving the diminution in value of TDRs. This Note concludes that while the position of Grand Central’s owner is not constitutionally

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protected, viable policy arguments exist for municipalities to provide incentives that support a robust TDR market.

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I. INTRODUCTION

In the landmark *Penn Central* decision, the United States Supreme Court upheld New York City’s historic zoning law restricting Grand Central Terminal’s development of its air space.¹ Now, more than thirty-seven years later, the parties may be headed back to court. In 2013 and 2014, the New York City Planning Commission developed two rezoning proposals that permit developers in Midtown East to construct buildings twice the maximum size permitted by current zoning regulations in exchange for cash payments² or public improvements.³ The proposed bonus systems enable

¹ *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104 (1978).

² See *East Midtown Rezoning Proposal*, N.Y.C. DEPT OF CITY PLANNING (Apr. 22, 2013), http://www.nyc.gov/html/dcp/html/east_midtown/index.shtml [<http://perma.cc/XJ8Z-BWRE>] [hereinafter *Midtown Proposal*] (“New commercial buildings on Qualifying Sites could exceed the base 15 FAR [floor area ratio] in exchange for contributions of \$250 per square foot to a proposed District Improvement Fund.”).

³ See Press Release, N.Y.C. Dep’t of City Planning, City Planning Begins Public Review on Zoning Changes for 5-Block Vanderbilt Corridor (Oct. 20, 2014), <http://www.nyc.gov/html/dcp/html/about/pr102014.shtml> [<http://perma.cc/5VSH-8B7L>] (“The Department of City Planning is proposing a new zoning special permit . . . requiring the property owners to make major improvements to the transit network [and] create new public spaces in the area.”).

the city to essentially print transferable development rights⁴ (“TDRs”), and allow developers to eschew purchasing TDRs from area landmarks.⁵ Grand Central’s owner argues that the zoning amendments significantly devalue and stymie the sale of its development rights, and therefore represent an unconstitutional taking of property.⁶

Although bonuses are widely implemented to create public amenities,⁷ they often operate to the detriment of neighboring landowners who hold unused development rights.⁸ This Note evaluates whether a municipal regulation that impairs the value of landowners’ unused development rights, as opposed to the underlying fee estate in land, constitutes a regulatory taking. Specifically, this Note utilizes Grand Central Terminal’s claim against the City of New York as a case study through which to examine the larger issue of the validity of municipal bonuses that provide

⁴ The terms “development rights,” “air rights,” and “TDR” will be used interchangeably throughout this Note. However, some scholars and practitioners conceptually distinguish air rights from development rights. Air rights can be thought of as property rights that extrude upward from a zoning lot *ad infinitum*, whereas development rights are tradable units capped at a specific height by the constructs of local zoning and federal aviation regulations.

⁵ See discussion *infra* Part II.C.

⁶ See discussion *infra* Part II.C.3. The Takings Clause of the Fifth Amendment to the U.S. Constitution provides in part, “nor shall private property be taken for public use, without just compensation.” U.S. CONST. amend. V.

⁷ See N.Y.C., N.Y., ZONING RESOLUTION, §§ 23-90, 81-23 (2015) (provisions on affordable housing and public plaza space bonuses); see also Jerold S. Kayden, *Zoning for Dollars: New Rules for an Old Game? Comments on the Municipal Art Society and Nollan Cases*, 39 WASH. U. J. URB. & CONTEMP. L. 3, 5 (1991) (noting that, “San Francisco . . . for example, [has] offered zoning bonuses to encourage developers to provide rooftop observatories for tourists. Anchorage . . . for climate-controlled plazas and courtyards. Miami . . . to encourage retail activity at street level[, and] Cincinnati . . . for historic preservation . . .”).

⁸ See MARY BROOKS, AM. SOC’Y OF PLANNING OFFICIALS, PLANNING ADVISORY SERV. NO. 257, BONUS PROVISIONS IN CENTRAL CITY AREAS 3 n.3 (1970) (explaining that, “[a]ny attack on bonuses will probably come from a neighboring property owner who believes the bonus will be detrimental to his property . . .”).

developers significant disincentives against purchasing TDRs from private property owners.

As an overview, Part II of this Note will explain the background law leading up to Grand Central's claim and aspects of takings law relevant to transferable development rights. It will also provide an understanding of TDRs and New York City's TDR landmark transfer program, lay out the applicable bonuses, and introduce the lawsuit. Part III will advance a framework by which to analyze future cases involving the diminution in value of TDRs with respect to relevant case law and the concept of "investment-backed expectations." Part IV will ultimately conclude that while the position of Grand Central's owner is not constitutionally protected, viable policy arguments exist for municipalities to provide incentives that support a robust TDR market.

II. SETTING THE STAGE: BACKGROUND LAW, TDRS, AND THE ZONING BONUSES

TDRs are a relatively new conception of property, yet have become an important type of currency in the real estate industry.⁹ Where development is prohibited (because of land

⁹ See Martin A. Schwartz, *It's Up in the Air: Air Rights in Modern Development*, FLA. B.J., Apr. 2015, at 42, 44 (stating that "TDRs transform potential development rights into currency for the property owner of the restricted property"). A comprehensive study conducted by the Furman Center for Real Estate and Urban Policy at NYU found that, "TDRs are increasingly discussed and used as mechanisms to help finance needed infrastructure improvements, compensate constrained land owners, and shape urban design." FURMAN CTR. FOR REAL ESTATE & URBAN POLICY, N.Y. UNIV., *BUYING SKY: THE MARKET FOR TRANSFERABLE DEVELOPMENT RIGHTS IN NEW YORK CITY 2*, 18 (2013) [hereinafter FURMAN CENTER STUDY]. The study also noted that,

TDRs are an important tool for developers building in the densest parts of the city and can be very valuable. Almost a third of the large residential and commercial buildings recently constructed in Manhattan below Central Park used development rights acquired from other lots. Citywide, between 2003 and 2011, developers paid more than a billion dollars for TDRs.

use regulations or environmental reasons),¹⁰ TDRs break the linkage between land and its development potential by permitting the transfer of that potential to another site where greater density is not objectionable.¹¹ In dense urban areas like New York City, this technique is used more than ever as a way of protecting areas of public concern¹²—such as open space and landmarks—and compensating the landowner fairly.

Part II examines how New York City's proposed bonus programs, in allowing the city to dominate the local TDR

Id. at 2. The number of TDR transfers increased by more than 400% between 2003 and 2007 before declining during the Great Recession, and have increased again since 2011. *See id.* at 5–6.

¹⁰ New Jersey's Pinelands Development Credit Program is one example of a TDR program that has successfully directed development away from 47,979.32 acres of National Reserve land and toward regional growth districts. The program offsets the severe development restrictions imposed on landowners located in protected areas by allotting them development rights to sell to landowners located in nearby receiving areas. *See generally* N.J. HIGHLANDS WATER PROTECTION & PLANNING COUNCIL, TRANSFER OF DEVELOPMENT RIGHTS TECHNICAL REPORT: ESTABLISHED TDR PROGRAMS IN NEW JERSEY (2007), <http://www.nj.gov/agriculture/sadc/tdr/casestudy/tdrexamplesnj.pdf> [<http://perma.cc/4NWT-SNDC>]; Julian Conrad Juergensmeyer et al., *Transferable Development Rights and Alternatives After Suitum*, 30 URB. LAW. 441, 448–50 (1998). Similarly, Santa Monica, California's TDR program protects against sprawl into the Malibu mountains by offering landowners substantial incentives to sell the land's development potential. *Id.* at 453–54. In Dade County, Florida, the TDR program operates to preserve a 150,000-acre portion of the Everglades by allocating development rights to area landowners owning five to forty acres of land. *Id.* at 454.

¹¹ *See* John J. Costonis, *Development Rights Transfer: An Exploratory Essay*, 83 YALE L.J. 75, 85–86 (1974) (“In freeing the bottled-up development rights for use elsewhere, the [TDR] technique . . . protects the threatened resource [such as open space or a landmark] and enables the owner of the restricted site to recoup the economic value represented by the site's frozen potential.”).

¹² *See* Norman Marcus, *Mandatory Development Rights Transfer and the Taking Clause: The Case of Manhattan's Tudor City Parks*, 24 BUFF. L. REV. 77, 109–10 (1974) (arguing that preserving open space in a dense urban area is a justifiable exercise of the state's power to promote the general welfare).

market,¹³ could render valueless Grand Central's unused air rights. Part II.A will explain the broad strokes of zoning and takings law most relevant to the issue. Part II.B will provide a brief overview of TDRs and New York City's TDR program. Finally, Part II.C will lay out the framework for the bonus programs at issue, present Grand Central's claim, and explore potential conflicts between the bonuses and the city's landmark TDR transfer mechanism.

A. Background Law

Zoning, “distilled to its essence, . . . proclaims the supremacy of collective action over individual will.”¹⁴ Through zoning laws, a community “limits the right of a private person to use his or her property in the manner in which he or she chooses.”¹⁵ In the context of commercial real estate development, zoning “pits the individualism of American capitalism against deeply rooted notions of communal public good.”¹⁶ Zoning laws have long since grown beyond their original purpose of promoting health, safety, or the welfare of citizens.¹⁷ They have become even more invasive from the “intermediate step” wherein the government regulates conflicting uses as nuisance.¹⁸ Rather, today's zoning laws “often dictate the manner in which a community will grow aesthetically.”¹⁹ *Penn Central Transportation Co. v. City of New York*,²⁰ the seminal case for modern regulatory takings law,²¹ marks the

¹³ See discussion *infra* Part I.C.

¹⁴ Georgette C. Poindexter, *Light, Air, or Manhattanization?: Communal Aesthetics in Zoning Central City Real Estate Development*, 78 B.U. L. REV. 445, 446 (1998).

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.* at 446–47.

¹⁹ *Id.* at 447.

²⁰ *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104 (1978).

²¹ It is important to distinguish eminent domain takings from regulatory takings. Eminent domain is the power of government to force the transfer of property from property owners to itself, and requires that

constitutional leap in the evolution of zoning whereby the government may single out one property for different treatment in the name of manipulating visual space.²²

In *Penn Central*, the U.S. Supreme Court held that the NYC Landmarks Law that prevented development of the air space above Grand Central Terminal, an iconic Beaux-Arts landmark, was not a taking.²³ The Court arrived at this conclusion after analyzing the claim according to a three-factor framework it developed to assess when a regulation goes so far as to require compensation.²⁴ The factors to be balanced included: (1) the “economic impact of the regulation on the claimant”; (2) “the extent to which the regulation has interfered with distinct investment-backed expectations”; and (3) the “character of the governmental action.”²⁵

Although the opinion only mentions the terminal’s TDRs in a single paragraph,²⁶ the concept of TDRs plays a notable role in the decision. Justice Brennan, writing for the majority, noted that the terminal’s leftover air rights were “valuable” because they were transferable,²⁷ implying that

compensation be paid to the owner. In contrast, when the government *regulates* property, owners retain title, but the government circumscribes the property’s use by methods such as zoning. JESSE DUKEMINIER ET AL., PROPERTY 1061 (Vicki Been et al. eds., 7th ed. 2010). While property may be regulated to a certain extent, if a regulation works too great a burden on property owners, it will be recognized as a taking requiring just compensation. *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922).

²² Kenneth Pearlman et al., *Beyond the Eye of the Beholder Once Again: A New Review of Aesthetic Regulation*, 38 URB. LAW. 1119, 1147 (2006) (“This decision permitted aesthetic goals to be a basis for regulatory action and acknowledged that landmarks preservation laws were an appropriate means for such goals: ‘States and cities may enact land-use restrictions or controls to enhance the quality of life by preserving the character and desirable aesthetic features of a city’”) (quoting *Penn Central*, 438 U.S. at 129).

²³ *Penn Cent.*, 438 U.S. 104.

²⁴ *See id.* at 124 (“[T]he Court’s decisions have identified several factors that have particular significance.”).

²⁵ *Id.*

²⁶ *Id.* at 137.

²⁷ *See id.* (“[Penn Central’s] ability to use these rights has not been abrogated; they are made transferable to at least eight parcels in the

this fact partially justified the ruling, as their value mitigated the economic impact of the judgment on Grand Central.²⁸ Moreover, Justice Brennan briefly alluded to the notion that TDRs could constitute a stand-alone property right, reasoning that, “[w]hile [TDRs] 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 regulation.”²⁹ While this holding has incited scholarly debate over TDRs’ status as property,³⁰ courts have

vicinity of the Terminal . . . [T]he New York courts here supportably found that, at least in the case of the Terminal, the rights afforded are valuable.”).

²⁸ See John J. Costonis, *The Disparity Issue: A Context for the Grand Central Terminal Decision*, 91 HARV. L. REV. 402, 407 (1977) [hereinafter Costonis, *Disparity Issue*] (explaining that, “[i]n return for retaining the Terminal site in its pristine landmark status, Penn Central was authorized to transfer to neighboring properties the authorized but unused rights accruing to the site prior to the Terminal’s designation as a landmark—the rights which would have been exhausted by the 59-story building that the city refused to countenance atop the Terminal. Prevailing bulk restrictions on neighboring sites were proportionately relaxed, theoretically enabling Penn Central to recoup its losses at the Terminal site by constructing or selling to others the right to construct larger, hence more profitable buildings on the transferee sites.”); see also *Penn Cent. Transp. Co. v. City of New York*, 366 N.E.2d 1271, 1278 (N.Y. 1977) (holding, prior to the U.S. Supreme Court’s decision, that, “the substitute rights received provide reasonable compensation for a landowner forced to relinquish development rights on a landmark site”), *aff’d*, 438 U.S. 105 (1978).

²⁹ *Penn Cent.*, 438 U.S. at 137. See also *Deltona Corp. v. United States*, 657 F.2d 1184, 1192 n.14 (Ct. Cl. 1981) (considering TDRs in evaluating the economic impact of a regulation), *cert. denied*, 455 U.S. 1017 (1982); *Gardner v. N.J. Pinelands Comm’n*, 593 A.2d 251, 261 (N.J. 1991) (upholding development restrictions against takings challenge based, in part, on availability of TDRs); *Glisson v. Alachua County*, 558 So. 2d 1030, 1037 (Fla. Dist. Ct. App. 1990) (rejecting a takings challenge based, in part, on value of TDRs).

³⁰ See, e.g., William Hadley Littlewood, Comment, *Transferable Development Rights, TRPA, and Takings: The Role of TDRs in the Constitutional Takings Analysis*, 30 MCGEORGE L. REV. 201, 204 (1998) (suggesting that if courts follow the *Penn Central* dictum on TDRs as a

generally interpreted it to signify that TDRs are property rights that should be considered in determining whether a taking has occurred.³¹ Thus, it is feasible to conclude that TDRs are property rights that may theoretically be taken.

It is understandable why the Court in *Penn Central* did not conduct an in-depth analysis of TDRs. In most regulatory takings cases, which involve an ordinance's effect on a parcel's value,³² the underlying fee estate in land—not air space—is the parcel at issue.³³ That air rights represent a relatively unknown quantity in the courtroom complicates the assessment of Grand Central's current claim. Even with

property right, that courts will effectively read out the just compensation requirement in the Constitution); Andrew J. Miller, *Transferable Developments in the Constitutional Landscape: Has Penn Central Failed to Weather the Storm?*, 39 NAT. RESOURCES J. 459, 470–71 (1999) (questioning whether the government has such far-reaching powers as to confer TDRs as a benefit to develop private property).

³¹ See, e.g., *Suitum v. Tahoe Reg'l Planning Agency*, 520 U.S. 725, 744 (1997) (implying that the value of TDRs affects the ripeness of a takings claim); *Fred F. French Investing Co. v. City of New York*, 350 N.E.2d 381, 387 (N.Y. 1976) (recognizing that, “development rights . . . are a potentially valuable and even a transferable commodity and may not be disregarded in determining whether the ordinance has destroyed the economic value of the underlying property”).

³² In less common cases, the boundaries of government action are more clear-cut. Three categorical rules on regulatory takings have emerged from Supreme Court decisions. The first is that any permanent physical occupation of a property by the government is a taking. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 426 (1982). The second is that no taking occurs when a government enacts a nuisance-control measure, regardless of the extent of loss that a property owner suffers. *Hadacheck v. Sebastian*, 239 U.S. 394, 409–10 (1915). The third stipulates that a regulation that prohibits all economically productive or beneficial use of land requires just compensation, unless the owner's use of the land violates a background principle of state nuisance or property law. *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1019 (1992).

³³ See, e.g., *Keystone Bituminous Coal Ass'n v. DeBenedictis*, 480 U.S. 470, 476–77 (1987) (rejecting claim by coal companies that challenged a state Subsidence Act requiring that fifty percent of the coal beneath certain structures be kept in place to provide surface support); *Good v. United States*, 189 F.3d 1355, 1358 (Fed. Cir. 1999) (challenging Army Corps of Engineers' denial of permit to fill wetlands for purposes of residential development).

takings claims involving land parcels, outcomes are difficult to predict. Because the takings inquiry is necessarily fact-based,³⁴ the Court and lower courts have applied the three-factor test inconsistently, have entangled the test with doctrine established in subsequent cases, and have struggled to articulate how much loss is too much.³⁵ A critical first step, then, in analyzing the constitutionality of regulations that devalue air rights is to understand what makes a TDR valuable, as well as the mechanics of TDR markets.

B. Transferable Development Rights and New York City's TDR Scheme

To determine how the rezoning will affect Grand Central's TDRs, it is useful to understand the concept of TDRs and the system presently operating in New York City. The term "development rights" refers to the maximum

³⁴ See *Penn Cent.*, 438 U.S. at 124 (observing that "whether a particular restriction will be rendered invalid . . . depends largely 'upon the particular circumstances [in that] case,'" and describing regulatory takings analyses as "essentially ad hoc, factual inquiries").

³⁵ The confusion largely stems from the Supreme Court's creation of a third categorical rule in *Lucas*, 505 U.S. at 1003. In that case, owners of beachfront property challenged a wetlands regulation that reduced the property's value to zero. The *Lucas* dissenters recognized that "the Court's [third categorical] rule conflicts with the very character of our [ad hoc] takings jurisprudence" in finding that a regulation depriving property of all economic value gives rise to a taking without considering the other *Penn Central* factors. *Id.* at 1071. For a discussion of how *per se* rules have interacted with courts' application of the *Penn Central* framework, see Costonis, *Disparity Issue*, *supra* note 28, at 409 (explaining that "[w]ithout legislative aid, and reluctant to strike out on their own, the courts have temporized with incantation that decides individual cases but leaves untouched the underlying conflicts that make these cases so troublesome"). For examples of contradictory holdings from subsequently decided cases, compare *Loveladies Harbor, Inc. v. United States*, 28 F.3d 1171, 1179 (Fed. Cir. 1994) (holding that the question is not one of balance between competing public and private claims but of basic property ownership rights), with *Palazzolo v. Rhode Island*, 533 U.S. 606, 617–18 (2001) (holding that a regulatory taking requires an analysis of all of the *Penn Central* factors).

amount of floor area permitted on a zoning lot.³⁶ When a building's actual built floor area is less than the maximum permitted floor area, the difference is referred to as "unused development rights," or "air rights."³⁷ In particular, for developers in New York City, air rights are a commodity of exceptional commercial value.³⁸

A *transfer of development rights* is a land-use planning tool that allows for the transfer of unused developments rights from one zoning lot to another for a price.³⁹ TDRs are normally transferred by merging two adjacent zoning lots.⁴⁰

³⁶ *Zoning Glossary*, N.Y.C. DEP'T OF CITY PLANNING, http://www.nyc.gov/html/dcp/html/zone/glossary.shtml#development_rights [<http://perma.cc/QD7V-TC5G>].

³⁷ *Id.*

New York's Zoning Resolution provides a districting scheme that allocates varying degrees of development rights to all real property in the city (with the exception of streets and parks). There are three basic zoning districts in New York City: residential, commercial, and manufacturing. The Zoning Resolution subdivides these districts into 21 zoning districts, and controls development within each district through a variety of use and bulk regulations.

Norman Marcus, *Air Rights in New York City: TDR, Zoning Lot Merger and the Well-Considered Plan*, 50 BROOK. L. REV. 867, 868, 868 n. 6 (1984).

³⁸ See Robin Finn, *The Great Air Race*, N.Y. TIMES, Feb. 22, 2013, http://www.nytimes.com/2013/02/24/realestate/the-great-race-for-manhattan-air-rights.html?pagewanted=all&_r=0 [<http://perma.cc/79A8-YJFB>] ("[I]f you're a developer of a residential property you should build as high as you can, because you get the higher sales price for the higher floors. The race to accumulate . . . air rights is tied to the mandate for these high-priced condos to offer views worthy of the purchase price.").

³⁹ *Zoning Glossary*, N.Y.C. DEP'T OF CITY PLANNING, *supra* note 36. Air rights are only transferable to other lots as set forth in New York City's Zoning Resolution. See, e.g., N.Y.C., N.Y., ZONING RESOLUTION, § 81-63 (2015) (provision on Transfer of Development Rights from Landmark Sites in the Grand Central Subdistrict of the Special Midtown District).

⁴⁰ A "zoning lot" is a tract of land, either unsubdivided or consisting of two or more lots of record contiguous for a minimum of ten linear feet, located within a single block, under single fee ownership. N.Y.C., N.Y., ZONING RESOLUTION, § 12-10 (2015). A "zoning lot merger" is the "joining of two or more adjacent zoning lots into one new zoning lot. Unused

However, because of the stringency of the adjacency requirement, the market for TDRs using this method is small and fairly limited.⁴¹

Landmark sites prove an exception to this rule. The city has sought to compensate landmark owners for restricting the development of their property by enhancing the transferability of landmarks' TDRs as compared with those of other buildings.⁴² Thus, landmarks may transfer unused air rights in an amount equivalent to the amount of development potential the landowner is prohibited from using to non-adjacent properties either across the street, catty corner, or, if the landmark is located in New York City's Grand Central Subdistrict, to any building within the Grand Central Subdistrict.⁴³ As an additional concession to

development rights may be shifted from one lot to another, as-of-right, only through a zoning lot merger." *Zoning Glossary*, N.Y.C. DEP'T OF CITY PLANNING, *supra* note 36.

⁴¹ See FURMAN CENTER STUDY, *supra* note 9, at 3 ("[B]ecause the lots in a zoning lot merger must form a contiguous group, the market for available development rights is very constrained and idiosyncratic: developers can only buy unused rights located on the same block as their building site; owners of unused rights can only sell if there is a development opportunity and interested purchaser on the block; and owners of lots needed to connect developers to properties with unused development rights can have considerable negotiating leverage.").

⁴² See Costonis, *Disparity Issue*, *supra* note 28, at 410 (explaining that the city implemented its TDR scheme because it anticipated charges of overregulation in its landmarks program); *Vanderbilt Corridor*, N.Y.C. DEP'T OF CITY PLANNING (May 27, 2015), http://www.nyc.gov/html/dcp/html/vanderbilt_corridor/index.shtml [<http://perma.cc/4E8A-8TYW>] [hereinafter *Vanderbilt Proposal Overview*] ("The [Grand Central] Subdistrict was put in place in 1992 to allow the transfer of development rights from Grand Central and other City-designated landmarks to development sites in the vicinity of the Terminal . . .").

⁴³ See N.Y.C., N.Y., ZONING RESOLUTION, § 74-79 (2015) (provision on Transfer of Development Rights from Landmark Sites), ("[T]he term 'adjacent lot' shall . . . mean, in the case of lots located in C5-3, C5-5, C6-6, C6-7 or C6-9 Districts, a lot contiguous or one that is across a street and opposite to another lot or lots that except for the intervention of streets or street intersections, form a series extending to the lot occupied by the landmark building or other structure."). The transfer rules and building densities vary among the city's different TDR transfer districts. This Note

landmark owners in the Grand Central Subdistrict, TDR recipients are prohibited from taking advantage of the city's public plaza bonus, which allows building owners to increase their permitted floor area by providing public space.⁴⁴ Therefore, in most instances,⁴⁵ to acquire additional air rights, developers in the Grand Central Subdistrict must purchase those rights from landmarks at a price set by the landmark owner.⁴⁶ Nonetheless, landmark owners stand to lose bargaining power, as the bonuses at issue may render their TDRs less valuable.

will only reference the rules pertaining to the Grand Central Subdistrict TDR transfer district.

⁴⁴ The city's public space bonus allows landowners to increase their maximum permitted floor area by six square feet for every square foot of public plaza space that they provide. However, as-of-right floor area bonuses are not permitted "on zoning lots, any portion of which is located in the Grand Central Subdistrict." See N.Y.C., N.Y., ZONING RESOLUTION, § 81-23(d) (2015) (provision on Floor Area Bonus for Public Plazas).

⁴⁵ An exception exists for developers whose sites are located directly adjacent to subway entrances along Vanderbilt Avenue. They may increase their floor area ratio ("FAR") up to twenty percent of the permitted floor area via a transit improvement bonus, without acquiring any air rights from landmarks. *Vanderbilt Proposal Overview*, *supra* note 42. FAR is the ratio of a building's total floor area to the size of the lot on which it is built. The FAR concept, codified in the 1961 Zoning Resolution, was designed to control the amount of physical volume on a particular zoning lot and the amount of usable floor area in each building on the lot. Each zoning district has a FAR which, when multiplied by the area of the lot, produces the maximum amount of floor area allowable on that lot. For example, a FAR of 15.0 permits the construction of floor space up to a maximum of fifteen times the square footage of the lot. *Zoning Glossary*, N.Y.C. DEP'T OF CITY PLANNING, *supra* note 36.

⁴⁶ Under the zoning scheme that existed before the designation of the Vanderbilt Corridor, a landmark located in the Grand Central Subdistrict could transfer unused air rights to a receiving lot in the Grand Central Subdistrict (including lots located in the current Vanderbilt Corridor) in an amount that did not exceed 21.6 FAR. N.Y.C., N.Y., ZONING RESOLUTION, § 81-635(a) (2015) (provision on Transfer of Development Rights by Special Permit).

C. The Zoning Bonuses and Grand Central's Claim

Incentive zoning is a type of zoning “originally conceived for the laudable purpose of raising urban amenity levels by encouraging light, air, and circulation in downtown areas.”⁴⁷ Although programs differ widely among local governments, they are all premised on a trade between the city and a developer.⁴⁸ Incentive zoning allows developers to build structures that are larger than what current zoning regulations permit in exchange for providing public amenities such as landscaped plazas, affordable housing,⁴⁹ pedestrian network improvements, or a cash payment if a benefit cannot be feasibly provided.⁵⁰ The city derives the extra floor area that it allocates to the developer by creating the floor area out of nothing and granting it to the developer as a so-called “zoning bonus.”⁵¹

There are presently few decisions on the validity of incentive bonus zoning provisions.⁵² The dearth of case law,

⁴⁷ See John J. Costonis, *The Chicago Plan: Incentive Zoning and the Preservation of Urban Landmarks*, 85 HARV. L. REV. 574, 633 n. 229 (1972) [hereinafter Costonis, *Chicago Plan*] (contending that despite these aims, an unhappy history of zoning bonuses in some cities gives cause for hesitation).

⁴⁸ *Id.* at 576.

⁴⁹ See N.Y.C., N.Y., ZONING RESOLUTION, §§ 23-90, 62-352 (2015) (provisions on inclusionary housing as relating to floor area compensation).

⁵⁰ For other types of public amenities provided in exchanges, see Aaron J. Yowell, Note, *That's Where We Print the Money: Increased Density for Public Amenities*, 15 N.Y.U. ENVTL. L.J. 493, 497 (2007).

⁵¹ Costonis, *Chicago Plan*, *supra* note 47, at 576.

⁵² See ARDEN H. RATHKOPF & DAREN A. RATHKOPF, 3 RATHKOPF'S THE LAW OF ZONING AND PLANNING § 52:7 (4th ed. 2013). Indeed, a Westlaw search conducted at the time of this writing yielded only two cases relating to New York City incentive zoning provisions. See *Mun. Art Soc'y of N.Y. v. City of New York*, 522 N.Y.S.2d 800, 804 (N.Y. Sup. Ct. 1987) (invalidating the sale of city-owned land to a private developer on the basis that the incentive zoning component of the deal constituted improper zoning for sale); *Asian Ams. for Equal. v. Koch*, 527 N.E.2d. 265, 273 (N.Y. 1988) (holding that bonuses awarded to developers to permit high density housing in their neighborhood provided sufficient incentive to encourage construction of low-cost housing). A Lexis search yielded similar results,

however, is understandable. Both private developers and municipal governments have embraced zoning bonus programs.⁵³ In most cases, “the developer receives an advantage and has no interest in attacking the legality of that advantage.”⁵⁴ The response to these programs in New York City—the nation’s foremost practitioner of incentive zoning—has been illustrative.⁵⁵ Almost every major commercial development erected in Manhattan’s central business district since the adoption of the New York Zoning Resolution has included bonus space.⁵⁶

Despite the prevalent application of incentive zoning, the approach has been challenged repeatedly in New York.⁵⁷ Critics have argued that “small-scale public amenities provide little compensation for the increased traffic, loss of light and other problems resulting from large-scale development.”⁵⁸ Conversely, some developers have contended that the bonus they received is not comparable to the improvement they provided.⁵⁹

Although criticism has been rife,⁶⁰ it has generally not addressed one important issue—namely, that bonus systems

but with numerous claims involving bonuses as related to housing discrimination claims, which are not relevant for the purposes of this analysis.

⁵³ Costonis, *Chicago Plan*, *supra* note 47, at 576. See Kayden, *supra* note 7, at 3–4 (noting that “incentive zoning has enjoyed broad support from developers and their attorneys”).

⁵⁴ BROOKS, *supra* note 8, at 3 n.3.

⁵⁵ For a detailed description of infrastructure development in Manhattan, see Costonis, *Chicago Plan*, *supra* note 47, at 576–78.

⁵⁶ *Id.* at 576.

⁵⁷ Thomas J. Lueck, *The Bulk-for-Benefits Deal in Zoning*, N.Y. TIMES (July 23, 1989), <http://www.nytimes.com/1989/07/23/realestate/the-bulk-for-benefits-deal-in-zoning.html> [<http://perma.cc/Z43V-B8NK>].

⁵⁸ *Id.*

⁵⁹ BROOKS, *supra* note 8, at 3 n.3.

⁶⁰ See, e.g., Kayden, *supra* note 7, at 6 (“As individuals have begun to understand better the connection between land use regulations and the quality of local physical environments, criticism of incentive zoning has increased. Where zoning administration was once left to planning-oriented professionals, zoning today excites neighborhood activists, political leaders, and newspaper reporters. Government approval of new

often operate to the detriment of landowners who hold unused air rights.⁶¹ Air rights transfer programs have fared poorly as a result of bonus systems.⁶² “Onerous administrative controls . . . have dampened the enthusiasm of the private sector for the program,”⁶³ an effect that the city has amplified by securing for itself an advantageous position in the air rights market. Two municipal bonus programs have recently pulled this issue into focus.⁶⁴

The East Midtown Rezoning Proposal and the Vanderbilt Corridor rezoning, described below, constitute two separate rezoning efforts by the City of New York to establish a bonus system in the Grand Central Subdistrict that competes with landowners who hold unused air rights.⁶⁵ The City Planning Commission approved the East Midtown Rezoning Proposal in September of 2013.⁶⁶ However, that application was ultimately withdrawn, as City Council members could not

development routinely triggers complaints that streets and sidewalks are already too congested, that neighborhoods have lost their human scale, and that indispensable open space is disappearing. Because incentive zoning definitionally tampers with baseline zoning rules by allowing developers to construct buildings larger than otherwise permitted, the technique has become a lightning rod for general discontent with local land use policies.”).

⁶¹ See, e.g., STATE OF R.I. DIV. OF PLANNING, SESSION 2: USE OF TDR AS PART OF A LOCAL AND REGIONAL DEVELOPMENT STRATEGY 11, 17, http://www.planning.ri.gov/documents/LU/S2_UseofTDRpresentations.pdf [<http://perma.cc/6BP9-UAJ9>] (noting that TDR schemes conflict with other means of achieving density, and that incentive zoning menus that provide amenities diminish the value of TDRs); Yowell, *supra* note 50, at 495–96 (arguing that density bonus programs “allow the municipality to shift the costs of public amenities to a small group of private property owners” and confer a “windfall” on developers that the municipality alone recaptures).

⁶² Costonis, *Chicago Plan*, *supra* note 47, at 577–78.

⁶³ *Id.* at 578.

⁶⁴ See generally *Midtown Proposal*, *supra* note 2; see also *Vanderbilt Proposal Overview*, *supra* note 42.

⁶⁵ See *infra* Part II.C.1–2 for a discussion of the two proposals.

⁶⁶ *East Midtown Rezoning: Public Review*, N.Y.C. DEP’T OF CITY PLANNING, http://www.nyc.gov/html/dcp/html/east_midtown/east_midtown6.shtml [<http://perma.cc/5UHK-KE8F>].

agree on several key parts of the plan.⁶⁷ The Vanderbilt Corridor represents the de Blasio administration’s revival of that proposal.⁶⁸ Either plan, if adopted, would affect the value and mobility of air rights owned by Grand Central—rights that the New York Court of Appeals in *Penn Central Transportation Co. v. City of New York* held constituted “significant, perhaps ‘fair,’ compensation for the loss of rights above the terminal itself.”⁶⁹

Although one proposal is no longer operative and the other has been adopted, examining both plans’ potential interaction with New York City’s TDR scheme will help answer the larger question of whether property rights are unconstitutionally deprived when a municipality establishes a TDR system that competes with and devalues building owners’ unused air rights.

1. The East Midtown Rezoning Proposal

The East Midtown Rezoning proposal, initiated by the Bloomberg administration, established a new East Midtown Subdistrict that would allow for taller skyscrapers to be built in a 73-block area surrounding Grand Central Terminal,⁷⁰ with the goal of revitalizing modern commercial development

⁶⁷ City Council members “expressed concern over the trading of air rights and the level of funding required for infrastructure improvements.” Gus Delaporte, *Midtown East Rezoning Denied by City Council*, COM. OBSERVER (Nov. 13, 2013, 8:15 AM), <http://commercialobserver.com/2013/11/city-council-midtown-east-rezoning/> [<http://perma.cc/PZU5-4WAF>].

⁶⁸ See Press Release, N.Y.C. Dep’t of City Planning, City Planning Begins Pub. Review on Zoning Changes for 5-Block Vanderbilt Corridor (Oct. 20, 2014), <http://www.nyc.gov/html/dcp/html/about/pr102014.shtml> [<http://perma.cc/LSB9-U24M>] (announcing “the first phase of the de Blasio Administration’s two-part strategy to strengthen East Midtown as a world-class 21st Century commercial district, attract more quality jobs to New York City, and deliver vital infrastructure and public realm improvements together with new development”).

⁶⁹ *Penn Cent. Transp. Co. v. City of New York*, 366 N.E.2d 1271, 1276–78 (N.Y. 1977), *aff’d*, 438 U.S. 105 (1978).

⁷⁰ *Midtown Proposal*, *supra* note 2.

in East Midtown.⁷¹ The plan permitted any building owner in the Grand Central area to increase their building's floor area ratio as-of-right by contributing cash to the City's new District Improvement Fund ("DIF"), which was formed to finance municipal transit projects.⁷² The DIF essentially created, out of whole cloth, millions of square feet of air rights to sell to developers in exchange for contributions to the fund.

Prior to the DIF, developers in the Grand Central Subdistrict looking to build higher could purchase unused air rights from area landmarks.⁷³ The East Midtown proposal, however, created a new process by which developers could increase their buildings' floor area to exceed the maximum permitted floor area by twenty percent⁷⁴ and bypass certain land use review hurdles that are normally required.⁷⁵ In

⁷¹ See *id.* While East Midtown "was, for years, a premier site for Class A office space . . . in the last two decades, only five new buildings have been developed in [the area]." Catherine Yang, *Community Members, Unions Support One Vanderbilt and 5-Block Rezoning Outside Grand Central*, EPOCH TIMES (Nov. 18, 2014, 1:27 AM), <http://www.theepochtimes.com/n3/1087658-community-members-unions-support-one-vanderbilt-and-5-block-rezoning-outside-grand-central/> [<http://perma.cc/445Q-GFHJ>].

⁷² *Midtown Proposal*, *supra* note 2.

⁷³ See Charles V. Bagli, *Owner of Grand Central Vies with Developer Over Skyscraper on an Adjacent Block*, N.Y. TIMES (Sept. 23, 2014), <http://www.nytimes.com/2014/09/24/nyregion/owner-of-grand-central-vies-with-developer-over-skyscraper-on-an-adjacent-block.html> [<http://perma.cc/2XXR-SALQ>] [hereinafter Bagli, *Owner of Grand Central*] ("[A] developer could buy unused development rights, or air rights, from the owners of Grand Central; St. Patrick's Cathedral . . . or St. Bartholomew's Church . . .").

⁷⁴ Charles V. Bagli, *Revised Plan for Taller Midtown Fails to Assuage Critics*, N.Y. TIMES (July 18, 2013), http://www.nytimes.com/2013/07/19/nyregion/revised-plan-for-taller-midtown-fails-to-assuage-critics.html?_r=0 [<http://perma.cc/6F3H-XP4X>].

⁷⁵ See Noah Kazis, *Midtown Rezoning Would Let Developers Buy Height With Ped Improvements*, STREETS BLOG NYC (July 12, 2012), <http://www.streetsblog.org/2012/07/12/midtown-rezoning-would-let-buildings-buy-height-with-ped-improvements/> [<http://perma.cc/A5WQ-L3GS>] (noting that "the city plans to allow developers in the area . . . to proceed with fewer procedural hurdles and to build bigger").

exchange, developers would have been required to contribute \$250 per square foot to the DIF,⁷⁶ in effect buying air rights directly from the city.⁷⁷

The proposal allowed developers to purchase air rights from landmarks only after contributing to the DIF for a minimum of 3 FAR.⁷⁸ In addition to imposing a minimum purchase condition, the city established a rate that significantly undercut the market value for air rights.⁷⁹ These changes, taken together, would have allowed developers to eschew purchasing air rights from Grand Central Terminal and added the incentive to avoid the “complex”⁸⁰ landmark transfer procedures, which involve a lengthy and costly public approval process.⁸¹

⁷⁶ *Midtown Proposal*, *supra* note 2.

⁷⁷ *Id.* Under this earned as-of-right framework new developments directly around the terminal could achieve a maximum FAR of 24, which is larger than the existing permitted maximum 21.6 FAR. To provide perspective, the MetLife tower near Grand Central has a FAR of 18. Matt Chaban, *How About Another Empire State Building or Two? City Outlines Mega Midtown East Rezoning*, N.Y. OBSERVER (July 12, 2012, 6:00 AM), <http://observer.com/2012/07/how-about-another-empire-state-building-or-two-city-outlines-mega-midtown-east-rezoning/> [<http://perma.cc/KP4N-CCPZ>].

⁷⁸ *Midtown Proposal*, *supra* note 2. Again, “FAR” or “floor area ratio” is the ratio of a building’s total floor area to the size of the lot on which it is built. *See supra* note 45 for a more detailed explanation.

⁷⁹ For a discussion of the current market value for air rights in NYC, see *infra* Part II.C.3 and note 100, *infra*.

⁸⁰ Costonis, *Chicago Plan*, *supra* note 47, at 585 (remarking that the “[p]rocedures for obtaining approval of a proposed transfer [of air rights from a landmark] are complex.”).

⁸¹ “A multi-million dollar developer does not want his project involved in administrative delays . . .” David Benson, *Bonus or Incentive Zoning—Legal Implications*, 21 SYRACUSE L. REV. 895, 904 (1970). “First, the [NYC] Landmark Commission must examine the plans for the development which will utilize the [TDRs] in order to determine whether the new development’s materials, design, scale, and location are compatible with the landmark.” Costonis, *Chicago Plan*, *supra* note 47, at 585. “Under Section 74-791 of the current Zoning Resolution, the owners of both the landmark seeking to transfer development rights and the potential receiving lot must submit an application for a special permit in order to make the transfer.” Vicki Been & John Infranca, *Transferable*

2. The Vanderbilt Corridor Rezoning

The Vanderbilt Corridor rezoning, which the New York City Council unanimously approved in 2015,⁸² represents a revived, albeit scaled-down version of the failed East Midtown proposal,⁸³ and is intended as a test case for a larger, seventy-block rezoning down the road.⁸⁴ In contrast to

Development Rights Programs: "Post Zoning"?, 78 BROOK. L. REV. 435, 444 (2013). This special permit application is subject to the City's seven-month Uniform Land Use Review Procedure (*see Uniform Land Use Review Procedure*, N.Y.C. DEP'T OF CITY PLANNING, <http://www.nyc.gov/html/dcp/pdf/luproc/lur.pdf> [<http://perma.cc/K4AM-5V9Z>]), and must include a site plan of the granting landmark lot and the receiving lot, including plans for all developments on the receiving lot, a program for the continuing maintenance of the landmark, and a report from the Landmarks Preservation Commission. *See* N.Y.C., N.Y., ZONING RESOLUTION, § 74-791 (2015) (provision on requirements for application). The CPC may only authorize development rights transfers from landmark sites upon a finding that

the transfer will not unduly increase the bulk of any development or enlargement, density of population or intensity of use in any block to the detriment of the occupants of buildings on the block or nearby blocks, and that any disadvantages to the surrounding area will be more than offset by the advantages of the landmark's preservation to the local community and the City as a whole.

Been & Infranca, *supra*, at 445. If the CPC "recommends approval, the application then goes to the Board of Estimate, which has final authority to grant or deny the application." Costonis, *Chicago Plan*, *supra* note 47, at 585–86.

⁸² Danielle Schlanger, *1 Vanderbilt Gets the Go-ahead From City Council*, COM. OBSERVER (May 27, 2015, 3:38 PM), <http://commercialobserver.com/2015/05/1-vanderbilt-gets-the-go-ahead-from-city-council/> [<http://perma.cc/F2TU-PF2W>].

⁸³ Charles V. Bagli, *65-Story Tower Planned Near Grand Central Terminal*, N.Y. TIMES (May 29, 2014), <http://www.nytimes.com/2014/05/30/nyregion/65-story-tower-planned-near-grand-central-terminal.html> [<http://perma.cc/Z7YV-9NVX>].

⁸⁴ *See* Press Release, N.Y.C. Dep't of City Planning, City Planning Begins Pub. Review on 5-Block Vanderbilt Corridor (Oct. 20, 2014), <http://www.nyc.gov/html/dcp/html/about/pr102014.shtml> [<http://perma.cc/LSB9-U24M>] (describing phase two of the plan as encompassing a "larger

its predecessor, the Vanderbilt Corridor spans only five blocks, from 42nd to 47th Streets along Vanderbilt Avenue.⁸⁵

Under the revised plan, the city will issue developers a permit termed the “Grand Central Public Realm Improvement Bonus” (“GCPRIB”) for density increases up to an “unprecedented”⁸⁶ new maximum 30.0 FAR (from the previous 21.6 FAR) in exchange for providing public amenities.⁸⁷ The idea behind the new rezoning is similar to that of the previous one except that, rather than pay cash for air rights, developers must instead provide amenities eligible for a bonus.⁸⁸ For example, SL Green, one of the largest developers in New York City, is set to build One Vanderbilt—a sixty-three-story, 1.6 million square foot tower, equal to twice the size of what is currently permitted on the block,⁸⁹ in exchange for spending \$220 million on transit and infrastructure improvements to Grand Central Terminal.⁹⁰

area roughly between East 37th Street to the south, East 59th Street to the north, Fifth Avenue to the west and Second Avenue to the east”).

⁸⁵ See *Vanderbilt Proposal Overview*, *supra* note 42. (“The east side of [Vanderbilt Avenue] is primarily made up of . . . Grand Central Terminal and the Met Life . . . building. The west side . . . is made up of five blocks (the Vanderbilt Corridor) that contain commercial buildings of [varying] scales.”).

⁸⁶ See Complaint at 19, *Midtown TDR Ventures LLC v. City of New York*, No. 1:15-cv-07647, 2015 WL 5693547, at ¶ 70 (S.D.N.Y. filed Sept. 28, 2015) (“A bonus of this magnitude [is] unprecedented. In Manhattan, the City had never [before] granted a bonus of more than 3.0 FAR in exchange for in-kind public improvements.”).

⁸⁷ N.Y.C., N.Y., ZONING RESOLUTION §§ 81-64, 81-641, 81-211 (2015).

⁸⁸ See Press Release, N.Y.C. Dep’t of City Planning, City Planning Begins Pub. Review on 5-Block Vanderbilt Corridor (Oct. 20, 2014), <http://www.nyc.gov/html/dcp/html/about/pr102014.shtml> [<http://perma.cc/LSB9-U24M>] (stating that the purpose of the Vanderbilt Corridor rezoning is to “deliver vital infrastructure and public realm improvements together with new development”).

⁸⁹ See Jessica Dailey, *City Council Green Lights 1,500-Foot One Vanderbilt*, CURBED N.Y. (May 27, 2015), http://ny.curbed.com/archives/2015/05/27/city_council_green_lights_1500foot_one_vanderbilt.php [<http://perma.cc/AD2Q-VR2R>]; Bagli, *Owner of Grand Central*, *supra* note 73.

⁹⁰ Holly Dutton, *Doors Open for Vanderbilt Corridor*, REAL ESTATE WEEKLY (May 6, 2015), <http://rew-online.com/2015/05/06/doors-open-for->

Under prior zoning, in order to build its 1400-foot office tower, “SL Green would have been required *both* to make transit improvements *and* to acquire Grand Central’s TDRs.”⁹¹ The Vanderbilt Corridor zoning will now allow developers to build much taller and larger buildings than currently permitted in exchange for making infrastructure improvements “without having to buy air rights from anyone, although they could still choose that option if they wanted.”⁹² An owner of a receiving lot located in the Corridor would be able to increase its FAR to the same maximum extent whether it purchased air rights from a landmark or through the GCPRIB.⁹³ Although this concept eliminates the minimum purchase condition and avoids the problem of setting a hard value for air rights, it still allows the City to print air rights and developers to circumvent purchasing them from area landmarks.⁹⁴

vanderbilt-corridor/ [http://perma.cc/689K-5JXG]. The City Council approved SL Green’s special permit application to build One Vanderbilt simultaneous to its approval of the rezoning, which may indicate that the rezoning was implemented to benefit a single property owner. Complaint, *supra* note 86, at 20.

⁹¹ Complaint, *supra* note 86, at 13 (emphasis in original) (noting that, “to effect a transfer of landmark TDRs pursuant to [Section 81-635 of the NYC Zoning Resolution], the developer of the receiving site not only must acquire the TDRs but also undertake significant improvements to the local pedestrian or transit infrastructure”).

⁹² Steve Cuzzo, *Proposed One Vanderbilt Tower Starts Long Slog for City Approval*, N.Y. POST (Oct. 21, 2014, 2:41 AM), <http://nypost.com/2014/10/21/proposed-one-vanderbilt-tower-starts-long-slog-for-city-approval/> [http://perma.cc/JN2V-RUTT]. The Director of the City Planning Commission corroborates that “th[e] new proposed rezoning basically lets the developer choose one or the other” Yang, *supra* note 71. See also *Vanderbilt Proposal Overview*, *supra* note 42 (in which the Department of City Planning suggests that developers building in the Vanderbilt Corridor could be “approved for either the *Grand Central Public Realm Improvement Bonus* or the *Grand Central Landmark Transfer* special permit, or some combination thereof”).

⁹³ N.Y.C., N.Y., ZONING RESOLUTION § 81-211 (establishing Maximum Floor Area Allowances for Specified Features and Maximum Floor Area Ratio by Table, Row N(d) and Row O).

⁹⁴ See BROOKS, *supra* note 8, at 13–14 (corroborating that a bonus, to be “genuinely attractive to a developer,” provides more than the usual rate

3. Grand Central's Claim

Argent Ventures (“Argent”) is a real estate company that currently owns the land under Grand Central Terminal and eighty-two miles of Metro-North railway tracks.⁹⁵ In 2006, Argent paid \$80 million for the property, which it has leased long-term to the Metropolitan Transportation Authority (“MTA”).⁹⁶ The potential profit in the deal, however, was in the 1.3 million square feet of unused air rights that came with Grand Central,⁹⁷ which would equate to approximately 1.5 million leasable feet if sold.⁹⁸ Argent’s primary purpose for acquiring the property was to profit from selling the air rights, which it originally purchased for \$61 per square foot.⁹⁹ Today, Argent claims that the rights are worth as much as \$880 per square foot.¹⁰⁰ In September 2015, after the Vanderbilt Corridor proposal was adopted, Argent filed a lawsuit against the city seeking a declaration that the zoning is invalid or, alternatively, just compensation in the amount of \$1.1 billion for a taking of its TDRs.¹⁰¹ The company

of return and more than covers the estimated cost of the required amenity, and stating that the developer will always be interested in using the bonus if the benefits outweigh the costs).

⁹⁵ Yang, *supra* note 71; Bagli, *Owner of Grand Central*, *supra* note 73.

⁹⁶ Bagli, *Owner of Grand Central*, *supra* note 73. The MTA’s lease terminates in the year 2274, and the agency alone profits from related transit and retail sales. Lois Weiss, *Air Rights Make Deals Fly*, N.Y. POST (July 6, 2007, 9:00 AM), <http://nypost.com/2007/07/06/air-rights-make-deals-fly/> [<http://perma.cc/PTR4-D9UM>].

⁹⁷ Bagli, *Owner of Grand Central*, *supra* note 73.

⁹⁸ Weiss, *supra* note 96.

⁹⁹ See Bagli, *Owner of Grand Central*, *supra* note 73 (“In 2006, Mr. Penson made a bet: He paid \$80 million for Grand Central and 82 miles of track The potential profit in the deal was in the 1.3 million square feet of development rights that came with Grand Central.”).

¹⁰⁰ Complaint, *supra* note 86, at 14. Some local land assemblage experts corroborate this figure. See FURMAN CENTER STUDY, *supra* note 9, at 9 (stating that in NYC in 2013, “prices paid in individual transactions varied widely, from less than \$50 to more than \$500 per square foot”). See also Weiss, *supra* note 96 (valuing air rights between \$250 and \$800 per square foot).

¹⁰¹ Complaint, *supra* note 86, at 4.

argues that by disincentivizing developers from purchasing air rights through landmark transfers, the city “would substantially diminish the value of development rights—[Grand Central’s] property rights—by allowing developers to essentially purchase the equivalent development rights from the City either in the form of . . . bonuses . . . or ‘in kind’ infrastructure improvements.”¹⁰²

Argent further asserts that the TDRs cannot be “taken from their owners without just compensation,”¹⁰³ and that either of the rezoning plans “would force [Argent] to bear the cost of incentivizing development,” which is equivalent to “one citizen . . . bear[ing] the cost of a public improvement that in all fairness should be borne by the public at large . . . [a] quintessential wrong prohibited by the Takings Clause.”¹⁰⁴ Concomitantly, Argent argues that TDRs are a “time-tested method for the city to preserve important resources while respecting Constitutionally-protected property rights,” and that the proposed amendments “depart from this approach to zoning, and interpose the city between [the] Terminal and potential [air] rights purchasers.”¹⁰⁵

Although the Vanderbilt Corridor rezoning, on its face, places landmarks on equal footing with the city in the air rights market by removing the minimum purchase condition,¹⁰⁶ it (and the East Midtown proposal) would allow developers to build higher structures without purchasing any

¹⁰² Dana Rubinstein, *Air Rights Owner Testifies Against Midtown Rezoning, Hints at ‘Legal Challenge,’* CAPITAL N.Y. (Oct. 24, 2013, 12:55 PM), <http://www.capitalnewyork.com/article/politics/2013/10/8534998/air-rights-owner-testifies-against-midtown-rezoning-hints-legal-cha> [<http://perma.cc/VHC4-T3RY>].

¹⁰³ Tobias Salinger, *Grand Central Owners Threatens Lawsuit Over One Vanderbilt*, COM. OBSERVER (July 16, 2014, 7:23 PM), <http://commercialobserver.com/2014/07/grand-central-landlord-threatens-lawsuit-over-one-vanderbilt/> [<http://perma.cc/Z5ZF-PB2Y>].

¹⁰⁴ Rubinstein, *supra* note 102.

¹⁰⁵ See Salinger, *supra* note 103 (quoting Paul Selver, an attorney at Argent’s land use firm, Kramer Levin Naftalis & Frankel).

¹⁰⁶ The plan would also increase the maximum permitted FAR on a site in the Vanderbilt Corridor from 21.6 FAR to 30 FAR through landmark transfer. *Vanderbilt Proposal Overview*, *supra* note 42.

of Grand Central's 1.3 million square feet of air rights. Under each plan, the City has entered the TDR market as a participant and secured for itself an advantageous position in that market.¹⁰⁷

The question of whether Argent has a viable claim against the city is complicated by the murkiness of regulatory takings doctrine.¹⁰⁸ For example, if TDRs are property rights, by how much must their value diminish to be considered appropriated? Do landowners stand any chance of succeeding in claims where a municipal bonus program provides a massive public benefit? Part III will analyze the terminal's claim in light of relevant case law, and explore the direction in which courts are heading with respect to TDRs as the principal subject of a regulatory taking.

¹⁰⁷ See Benson, *supra* note 81, at 904–05 (explaining that “most large developers would prefer to go along with the incentive system since [not doing so] would result in delay,” and that “the bonus itself is a very real and valuable asset which will pay dividends for the life of the building. As long as the planners design the bonuses to be sufficiently financially rewarding, builders will continue to favor the system.”).

¹⁰⁸ See J. David Breemer & R. S. Radford, *The (Less?) Murky Doctrine of Investment-Backed Expectations After Palazzolo, and the Lower Courts' Disturbing Insistence on Wallowing in the Pre-Palazzolo Muck*, 34 SW. U. L. REV. 351, 352 (2005) [hereinafter Breemer & Radford, *Less Murky Doctrine*] (stating that “[t]he Supreme Court's regulatory takings jurisprudence is one of the most heatedly divisive topics in contemporary constitutional law”); Andrea L. Peterson, *The Takings Clause: In Search of Underlying Principles—Part I: A Critique of Current Takings Clause Doctrine*, 77 CAL. L. REV. 1299, 1301–04, 1362 (1989) (arguing that “the Supreme Court's current takings clause doctrine is in chaos,” and that “it is difficult to imagine a body of case law in greater doctrinal and conceptual disarray,” because “the Court has used so many different definitions of ‘property’ and so many different tests for determining when a ‘taking’ of property has occurred”); J. Peter Byrne, *Ten Arguments for the Abolition of the Regulatory Takings Doctrine*, 22 ECOLOGY L.Q. 89, 102 (1995) (“The regulatory takings doctrine has generated a plethora of inconsistent and open-ended formulations that have failed to make sense of the underlying constitutional impulse.”).

III. ANALYSIS OF THE CASE STUDY IN VIEW OF CONTEMPORARY CASE LAW

Against the enormous backdrop of takings law exists a limited number of cases that specifically examine the property-like qualities of transferable development rights and regulations that impair TDR markets. Part III.A will analyze how these cases, which focus principally on the diminution in value of TDRs, have been litigated. Part III.B will examine how Grand Central's claim relates to the most relevant prong of *Penn Central's* test for when a regulation goes too far—the extent to which a regulation has interfered with an owner's “investment-backed expectations.”¹⁰⁹ Finally, Part III.C will suggest a framework by which to analyze the next generation of TDR cases, and apply that framework to Grand Central's claim.

A. TDRs as the Property Right Frustrated in a Regulatory Takings Claim

In the great majority of land use disputes, TDRs are relevant solely as concessions for restricting the development of an underlying land parcel.¹¹⁰ In Grand Central's current claim, however, TDRs are *the* property rights allegedly frustrated.¹¹¹ The case presents a matter of first impression in that the justification upon which Grand Central's land use restriction was premised in *Penn Central*—TDRs as dispensation for the restriction¹¹²—could be undermined by a rezoning that would affect the value of those TDRs. To what

¹⁰⁹ *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

¹¹⁰ *See, e.g.,* *Suitum v. Tahoe Reg'l Planning Agency*, 520 U.S. 725, 730–31 (1997) (regulators barring plaintiff from developing land she owned, but compensating her with TDRs that could be sold or used to develop other property in the Lake Tahoe basin); *Good v. United States*, 189 F.3d 1355, 1359–60 (Fed. Cir. 1999) (holding that the Army Corps of Engineers' denial of wetlands development is not a *per se* taking, as the property retains value either for development or for the sale of TDRs).

¹¹¹ *See* discussion *supra* Part II.C.3.

¹¹² *See* discussion *supra* Part II.A.

degree, then, may a municipality provide an owner with air rights and subsequently curtail their use? While no systematic body of jurisprudence provides the answer, two piecemeal cases—*Fred F. French Investing Co. v. City of New York*¹¹³ and *Sierra Nevada SW Enterprises v. Douglas County*¹¹⁴—taken together, suggest the correct framework by which to analyze this question.

1. Fred F. French Investing Co. v. City of New York

Fred F. French Investing Co. v. City of New York presents an “extreme example” of a regulatory deprivation involving TDRs,¹¹⁵ although its principles directly relate to Grand Central’s claim. In *French*, the developer of a residential complex in Midtown Manhattan sold the complex, but retained ownership over the property’s two 15,000 square-foot private parks.¹¹⁶ The developer subsequently announced plans to erect, on each park site, a building of the maximum size permitted by the zoning regulations.¹¹⁷ The proposals elicited an immediate public outcry from neighboring residents, which prompted the City Planning Commission to create a “Special Park District” and rezone the two parks to be located within that district.¹¹⁸

The zoning amendment stipulated that only “passive recreational uses” were permitted within the Special Park District, and limited any improvements to “structures incidental to passive recreational use.”¹¹⁹ The amendment also compelled compliance with onerous administrative

¹¹³ *Fred F. French Investing Co. v. City of New York*, 350 N.E.2d 381, 387 (N.Y. 1976).

¹¹⁴ *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App’x 663, 665–67 (9th Cir. 2013).

¹¹⁵ *Fred French*, 350 N.E.2d at 387.

¹¹⁶ *Id.* at 383.

¹¹⁷ *Id.*

¹¹⁸ *Id.* at 383–84.

¹¹⁹ *Id.* at 384.

requirements,¹²⁰ and required parks to be open daily to the public between 6:00 a.m. and 10:00 p.m.¹²¹ Although the amendment permitted granting lots within the district to transfer air rights to other areas, it deprived the sites of any possibility of producing a reasonable return, since only park uses were permitted on the land.¹²²

Chief Judge Breitel of the New York Court of Appeals (who authored the New York Court of Appeals' opinion in *Penn Central*) held that the zoning amendment was not a taking, but rather constituted an unreasonable exercise of the State's police power, as it deprived the owner of reasonable income and all property rights "except the bare title and a dubious future reversion of full use."¹²³ The court

¹²⁰ *Id.* A receiving lot's ability to increase its floor area to the maximum amount permitted through TDR transfer was contingent upon a public hearing and approval by the CPC and the Board of Estimate. The CPC Chairman also had to "certify the suitability of a plan for the continuing maintenance, at the owner's expense, of the granting lot as a park open to the public." *Id.*

¹²¹ *Id.*

¹²² *Id.* at 383. *See id.* (explaining that "[t]he zoning amendment permits the transfer of development rights from a privately owned lot zoned as a Special Park District, denominated a 'granting lot', to other areas in midtown Manhattan . . . [and that] [t]he owner of a granting lot would be permitted to transfer part of his development rights to any eligible receiving lot, thereby increasing its maximum floor area up to 10%."); *id.* ("[T]he city has, despite the severance of above-surface development rights, by rezoning private parks exclusively as parks open to the public, deprived the owners of the reasonable income productive or other private use of their property."). *See also* Penn Cent. Transp. Co. v. City of New York, 366 N.E.2d 1271, 1278 (N.Y. 1977) (agreeing that "[t]he regulations [in *French*] deprived the original site of any possibility of producing a reasonable return, since only park uses were permitted on the land," and distinguishing the regulation in *French* as a "depriv[ation] of property without due process of law," as the air rights were not "made transferable to numerous sites in the vicinity," as they were in Penn Central's case), *aff'd*, 438 U.S. 105 (1978).

¹²³ *Fred French*, 350 N.E.2d at 387. Chief Judge Breitel distinguished a physical "taking" by eminent domain from a "frustration of property rights" by regulation, noting that, "[i]n all but exceptional cases . . . a regulation does not constitute a 'taking', and is therefore not compensable,

took issue with the fact that the regulations created “floating development rights,” which are not assigned to a receiving parcel, and have uncertain or contingent market value.¹²⁴ Chief Judge Breitel contended that such rights are “utterly unusable until they [can] be attached to some accommodating real property, available by happenstance of prior ownership, . . . and subject to the contingent approvals of administrative agencies . . . which may never happen because of the exigencies of the market”¹²⁵

a. The New York Court of Appeals’ Reasoning
as Applied to Grand Central’s Claim

Compared to the plaintiff in *French*, the owner of Grand Central has an objectively weaker takings claim, as the bonuses at issue do not create a classic case of spot-zoning as does the city’s action in *French*.¹²⁶ In *French*, the city changed the law specifically to inhibit the development of a particular piece of property,¹²⁷ whereas it did not develop the recent zoning amendments to block the development of

but amounts to a deprivation or frustration of property rights without due process of law and is therefore invalid.” *Id.* at 385.

¹²⁴ *Id.* at 388. *See also id.* at 383 (“The attempted severance of the development rights with uncertain and contingent market value did not adequately preserve those rights. Hence, the . . . zoning amendment is violative of constitutional limitations.”).

¹²⁵ *Id.* at 388.

¹²⁶ “Spot zoning,” which usually arises from zoning amendments, is a zoning change limited to a small plot of land. Spot zoning creates an “island of nonconforming use within a larger zoned district” that “dramatically reduces the value . . . of either the rezoned plot or abutting property.” *DUKEMINIER ET AL.*, *supra* note 21, at 963–64

¹²⁷ *See Fred French*, 350 N.E.2d at 383–84 (inferring that the city regulated the property in question on the basis of “adverse public reaction to the owner’s proposals, especially from Tudor City residents. After public hearings, the [CPC] recommended . . . an amendment to the zoning resolution establishing Special Park District ‘P.’”). The city prohibited further development of the parks, and authorized the owners to transfer the unused development potential of the parks to a “transfer district” elsewhere in the city. *PATRICIA E. SALKIN*, 1 *NEW YORK ZONING LAW AND PRACTICE* § 7:50 (4th ed. 2014).

Grand Central's property or prohibit its commercial use,¹²⁸ although the City Planning Commission may have intended to "break [Argent's] monopoly" in the air rights market.¹²⁹ The bonuses at issue, in contrast, would apply not only to the terminal but to *all* landmark properties in the Grand Central Subdistrict.¹³⁰ Moreover, compared to the vacant park lots in *French*, the terminal would have more of an opportunity to produce a reasonable economic return from the rent it collects from the MTA.¹³¹ On the other hand, Chief Judge Breitel viewed landmark designation as singling out

¹²⁸ See *Midtown Proposal*, *supra* note 2 (asserting that "[t]he purpose of the rezoning is to ensure the area's future as a world-class business district and major job generator for New York City. The plan provides zoning incentives to promote the development of a handful of new, state-of-the-art commercial buildings over coming decades so that East Midtown's office stock remains attractive to a broad range of businesses, including major corporate tenants. Development under the rezoning is expected to expand the City's tax base, add thousands of permanent jobs in East Midtown and fund improvements to the subway and pedestrian network in the area."); *Vanderbilt Proposal Overview*, *supra* note 42 (stating that the plan was adopted "to facilitate commercial development along Madison and Vanderbilt avenues in Manhattan, improve pedestrian circulation within Grand Central Terminal and its vicinity, and allow greater opportunity for area landmarks to transfer their unused development rights").

¹²⁹ See *Complaint*, *supra* note 86, at 25 (asserting that, "Commissioner Weisbrod told [Argent] expressly that his intention for the rezoning was not to 'benefit' landmark owners but to 'break [Argent's] monopoly'").

¹³⁰ The East Midtown rezoning proposal, for instance, would have encompassed major landmarks within the newly mapped district, such as St. Patrick's Cathedral, St. Bartholomew's Church, Central Synagogue, and Lever House. *East Midtown Rezoning "A" Applications*, N.Y.C. DEPT OF CITY PLANNING, http://www.nyc.gov/html/dcp/html/east_midtown/east_midtown7.shtml [<http://perma.cc/GC77-VUV4>].

¹³¹ See discussion *infra* Part III.B.1.

owners for disadvantageous treatment,¹³² which could be akin to spot-zoning.¹³³

However, assuming *arguendo* that the bonus systems constitute spot-zoning, that fact would not be enough for Grand Central to prevail. Despite the city's intentionally directed action in *French*, the New York Court of Appeals clarified that the plaintiff's air rights were not nullified, since they were still transferable to another section of Midtown, although not to a particular parcel.¹³⁴ In fact, the potential value of the plaintiff's air rights in *French* doubled as a result of the conversion from a residential district to a commercial district.¹³⁵ Rather, the problem was that the severance of the air rights ultimately "rendered their value so uncertain and contingent, as to deprive the property owner of their practical usefulness, except under rare . . . circumstances."¹³⁶

Under this line of reasoning, Grand Central would not be able to argue that the bonuses nullify its air rights, as the rights are still transferable to other properties within the

¹³² Costonis, *Disparity Issue*, *supra* note 28, at 414 ("The landmark owner, [Chief Judge Breitel] said, 'may or may not benefit from the limitation but his neighbors most likely will.'") (citing Penn Cent. Transp. Co. v. City of New York, 366 N.E.2d 1271, 1274 (N.Y. 1977)).

¹³³ *Penn Central* made clear that landmark preservation laws do not constitute reverse spot zoning where they are formulated as part of a comprehensive land use plan. See Penn Cent., 438 U.S. at 132. However, courts in some cases have held height restrictions on development unconstitutional. These cases generally involve "reverse spot zoning" situations and include airport zoning and historic preservation. See ARDEN H. RATHKOPF et al., 3 RATHKOPF'S THE LAW OF ZONING AND PLANNING § 52:5 (4th ed. 2011) (citing Harris Trust & Sav. Bank v. Duggan, 435 N.E.2d 130 (Ill. App. Ct. 1982), *aff'd*, 449 N.E.2d 69 (Ill. 1983) (downzoning of mansion to historic landmark would make building an island of open space in area of high density)).

¹³⁴ Fred F. French Investing Co. v. City of New York, 350 N.E.2d 381, 387–88 (N.Y. 1976).

¹³⁵ See Marcus, *supra* note 12, at 83–84 (observing that at the time *French* was litigated, land values in residential districts in Midtown Manhattan ran for \$150 per square foot, as compared to \$300 per square foot in commercial districts).

¹³⁶ *Fred French*, 350 N.E.2d. at 389.

Grand Central Subdistrict,¹³⁷ although the Vanderbilt Corridor may have the only sites with TDR-receiving potential on any “reasonable time horizon.”¹³⁸ However, unlike the air rights in *French*, the terminal’s air rights would suffer a *decrease* in value as a result of the regulation.¹³⁹ Their value would not be rendered “uncertain” so much as the owner would need to sell them at a price that undercuts what developers would pay to construct a public improvement under the Vanderbilt Corridor bonus.¹⁴⁰ It is more accurate to say that the bonus systems would, through competition, reshape the local air rights market so as to deprive Grand Central of its air rights’ “practical usefulness.”¹⁴¹ Thus, its TDRs would likely not be considered as “loose-ended” as the TDRs in *French*, which “[e]ll short of achieving a fair allocation of economic burden” between the city and landowner.¹⁴²

¹³⁷ See N.Y.C., N.Y., ZONING RESOLUTION §§ 74-79, 81-212 (2015) (provisions on Transfer of Development Rights from Landmark Sites and Special Provisions for Transfer of Development Rights from Landmark Sites).

¹³⁸ Complaint, *supra* note 86, at 18. Commissioner Weisbrod has also acknowledged that he is “unaware of any East Midtown property owner with a concrete development plan in the near term other than those on the Vanderbilt Corridor.” *Id.* at 22, 2015 WL 5693547, at ¶ 82.

¹³⁹ See discussion *supra* Part II.C.

¹⁴⁰ See discussion *supra* Part II.C. However, it must be remembered that the courts have upheld rather severe drops in value as against the claim that the restriction constitutes a taking. See *Village of Euclid v. Ambler Realty Co.*, 272 U.S. 365, 384, 397 (1926) (upholding a 75% diminution in value caused by a zoning law); *Hadacheck v. Sebastian*, 239 U.S. 394, 405, 414 (1915) (upholding a 92.5% diminution in value).

¹⁴¹ See *Fred French*, 350 N.E.2d. at 389 (holding that “[e]ven though the development rights have not been nullified, their severance has rendered their value so uncertain and contingent, as to deprive the property owner of their practical usefulness, except under rare and perhaps coincidental circumstances”).

¹⁴² *Id.*

2. Sierra Nevada SW Enterprises v. Douglas County

While *French* demonstrates a court's attitude toward a regulation that goes too far in restricting the transfer of air rights, *Sierra Nevada Southwest Enterprises v. Douglas County*, an unpublished decision by the United States Court of Appeals for the Ninth Circuit, serves as an instructive example of a municipality's exercise of police power to affect a local TDR market by printing additional development rights through zoning amendments.¹⁴³ In *Sierra Nevada*, plaintiff developer, Sierra Nevada SW Enterprises ("SNSW"), claimed that Douglas County's amendment of its master zoning plan to benefit a similarly-situated developer constituted a taking, as the rezoning caused a diminution in value of SNSW's TDRs.¹⁴⁴ The master zoning plan, prior to being amended, granted TDRs to owners of agricultural land located in "Sending Areas" in exchange for placing conservation easements on their land (forever restricting the land's development).¹⁴⁵ These landowners could then sell the

¹⁴³ See discussion *infra* Part II.A.2. See generally MICHAEL A. ZIZKA ET AL., STATE & LOCAL GOVERNMENT LAND USE LIABILITY §13:6 (2014) (noting that the case stands for the proposition that "[t]he alleged decrease in one landowner's property values as a result of the governmental approval of a different landowner's development plans will not, in itself, create a cognizable claim for violation of constitutional due process").

¹⁴⁴ *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App'x 663, 665 (9th Cir. 2013).

¹⁴⁵ See Brief for Appellant at 13–14, *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App'x 663 (9th Cir. 2013) (No. 11-16451) ("This procedure, set forth in DCC 20.500.020, requires an owner of Agricultural (A-19) or Forest (FR) zoned land to apply to the County for certification of TDRs available from such lands. In order for the County to issue a TDR certificate establishing the legal existence of the TDRs, the owner must record a deed restriction or grant a perpetual open space easement in favor of the County . . . which deed restriction or easement must be approved by the County. Once the open space easement or deed restriction is recorded, the TDR certificate will issue.").

TDRs to landowners with property located in designated “Receiving Areas.”¹⁴⁶

The master zoning plan *required* landowners in receiving areas to acquire TDRs in order to develop their land.¹⁴⁷ SNSW specifically took issue with the county’s approval of a zoning amendment request that would allow Peri Enterprises (“Peri”), a neighboring landowner, to develop its land in exchange for constructing a local parkway rather than by purchasing TDRs.¹⁴⁸

SNSW, like Argent Ventures, acquired 2074 TDRs with a market value of \$6000 per TDR¹⁴⁹ (a total value of \$12,444,000) for the primary purpose of reselling them at a profit to neighboring developers.¹⁵⁰ SNSW argued that the master zoning plan amendment destroyed the local market for TDRs,¹⁵¹ and hence the value of its TDRs,¹⁵² as Peri would have otherwise been required to purchase TDRs from SNSW to support its project.

¹⁴⁶ *Id.* at 13 (explaining that “DCC 20.500 establishes the eligibility of agricultural and forest lands to transfer development rights to property in designated Receiving Area [sic] as shown in the Master Plan” according to the procedure detailed in note 145 *supra*).

¹⁴⁷ *Id.* at 6 (emphasis added) (citing Douglas County Code DCC 20.612.010 which requires developments in excess of 160 acres (and planned development projects of 40 acres in size or greater) to use TDRs in connection with any change in intensity or density of use, including any change to a residential, commercial, or industrial zoning district or combination thereof).

¹⁴⁸ *Id.* at 8–9.

¹⁴⁹ *Id.* at 7–8.

¹⁵⁰ *Id.* at 3.

¹⁵¹ *Id.* (“Now, because the County has permitted and even encouraged owners of Receiving Area lands to avoid the TDR requirements by obtaining Master Plan amendments, SNSW is the owner of approximately 1,600 TDRs for which there is no longer a market should SNSW wish to sell them to other owners of Receiving Area lands.”).

¹⁵² *See id.* at 10–11 (arguing that “the diminution in the value of [SNSW’s] TDRs was so substantial as to amount to a taking without just compensation”).

Although the Ninth Circuit assumed without deciding that TDRs constitute property rights,¹⁵³ the court held that the zoning amendment was not a regulatory taking because the plaintiff did not allege the *deprivation* of a constitutionally protected property interest.¹⁵⁴ Thus, for a rezoning to be a taking, it *must deprive* the property owner of its TDRs, not merely “diminish . . . the value of TDRs by reducing demand in the TDR market as a whole.”¹⁵⁵ The court also rejected the notion that the rezoning could be a *per se* taking,¹⁵⁶ as the plaintiff did not assert “that the price of TDRs in Douglas County had actually collapsed; [but] merely speculate[d] regarding what other landowners might think . . . and the effect of those possible thoughts on demand.”¹⁵⁷

Perhaps most illuminating in the case, however, is the court’s holding that the plaintiff could not state a claim under *Penn Central*’s three-factor inquiry.¹⁵⁸ Even if the diminished value of the plaintiff’s TDRs demonstrated the first factor—that the rezoning economically impacted the

¹⁵³ See *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App’x 663, 665 (9th Cir. 2013) (“We assume, without deciding, that the . . . [TDRs] created by section 20.500 of the Douglas County Code constitute property rights for purposes of this federal constitutional analysis.”).

¹⁵⁴ *Id.*

¹⁵⁵ See *id.* (“An indirect impact of that kind is not a ‘deprivation’ for purposes of procedural due process.”) (citing *Dumas v. Kipp*, 90 F.3d 386, 392 (9th Cir. 1996)).

¹⁵⁶ *Id.* at 666 (“The district court correctly dismissed Plaintiffs’ takings claim. A *per se* taking requires that the government action deprived them of ‘all economically beneficial or productive use’ of the affected property.” (citing *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1015 (1992))).

¹⁵⁷ *Id.* (“That ‘sheer possibility’ of a taking is inadequate to state a claim.” (citing *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009))).

¹⁵⁸ *Id.* As discussed in Part II.A *supra*, the factors that are relevant in a *Penn Central* inquiry include: (1) “the economic impact of the regulation on the claimant,” (2) “the extent to which the regulation has interfered with distinct investment-backed expectations,” and (3) “the character of the governmental action.” *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

plaintiff—the latter two factors precluded the claim.¹⁵⁹ SNSW could not show that the regulation interfered with its investment-backed expectations, as the county “acted on legal authority that existed at the time of Plaintiffs’ investments.”¹⁶⁰ Nor could it prove that the character of the governmental action was arbitrary, as “the grant of development rights to a third party on a different parcel does not have the character of a ‘classic taking in which government directly appropriates private property or ousts the owner from his domain.’”¹⁶¹

a. The Ninth Circuit’s Reasoning as Applied to Grand Central’s Claim

As a preliminary matter, it is imperative to note that as an unpublished decision, *Sierra Nevada* carries no precedential weight with respect to the resolution of this issue.¹⁶² That being said, of the few takings claims in which TDRs are the property rights at issue, *Sierra Nevada* has the most similar fact pattern to Grand Central’s case, and may possibly be considered persuasive.¹⁶³

¹⁵⁹ *Sierra Nevada*, 506 F. App’x at 666–67.

¹⁶⁰ *Id.* at 667.

¹⁶¹ *Id.* (citing *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 528, 539 (2005)).

¹⁶² The Ninth Circuit’s Federal Rules of Appellate Procedure clearly establish that unpublished dispositions are not precedent. *See* 9TH CIR. R. APP. P. 36-3(a) (“Unpublished dispositions and orders of this Court are not precedent, except when relevant under the doctrine of law of the case or rules of claim preclusion or issue preclusion.”).

¹⁶³ “A federal circuit decision is mandatory [or binding] on all federal courts within its circuit, but not federal courts in other circuits.” THE WRITING CENTER AT GEORGETOWN UNIV. LAW CTR., WHICH COURT IS BINDING? MANDATORY VS. PERSUASIVE CASES 4 (2004), http://www.law.georgetown.edu/academics/academic-programs/legal-writing-scholarship/writing-center/upload/which_court_is_binding_painter-and-mayer-final.pdf [<http://perma.cc/RVA5-FW7L>]. If a federal issue, such as a Takings Clause claim, is litigated in federal or state court, such court may look to the decisions of the following courts as persuasive authority: other federal circuit courts, other federal district courts, and all state courts. *See id.* at 5. Rule 32.1 of the Federal Rules of Appellate Procedure dictates that Courts of Appeals “may not prohibit or restrict the citation of federal

Unlike the TDRs at issue in *Penn Central* and Grand Central’s current claim, the TDRs in Douglas County were neither created nor awarded to compensate a property owner for government-imposed restrictions on development.¹⁶⁴ The Ninth Circuit does not examine this distinction, however, nor signify whether one method of acquisition yields a stronger claim.¹⁶⁵ Nonetheless, the decline in economic value of the TDRs in each case occurred because of the deregulation of other properties that would have otherwise required the use of TDRs to support development.¹⁶⁶ Perhaps uniquely to both Douglas County and the Grand Central Subdistrict, the TDR is a “separate and distinct right for which a market exists, the value of which depends on the consistent application of [municipal] ordinances regarding TDRs and the avoidance of arbitrary [actions] which can . . . eliminate the market by

judicial opinions . . . that have been: (i) designated as ‘unpublished,’ . . . and [that are] (ii) issued on or after January 1, 2007.” FED. R. APP. P. 32.1. However, Rule 32.1 is “extremely limited” and “says nothing about what effect a court must give to one of its unpublished opinions or to the unpublished opinions of another court.” Committee Note to FED. R. APP. P. 32.1, *reprinted* in 28 U.S.C. app. at 64 (2012).

¹⁶⁴ Brief for Appellant, *supra* note 145, at 17–18.

¹⁶⁵ The Ninth Circuit simply states that the plaintiffs could not state a takings claim under *Penn Central*. *Sierra Nevada*, 506 F. App’x 663, 666–67. The District Court was similarly reticent, explaining only that the law establishing the TDR system

does not on its face require owners of property in the Receiving Area to purchase TDR, as Plaintiffs claim, but only notes that development rights may be transferred from property in [agricultural and forest] districts to property in the Receiving Area . . . and that the owner of property in the Receiving Area may not transfer more TDR to a parcel therein than the density provided by the base zoning district

Sierra Nevada SW Enter. v. Douglas County, No. 3:10–CV–354–RCJ–RAM, 2011 WL 1304472, at *1 (D. Nev. Mar. 30, 2011).

¹⁶⁶ Brief for Appellant, *supra* note 145, at 47.

decisions to circumvent the mandatory nature of the use of TDRs.”¹⁶⁷

Although evidence of a TDR market exists in each jurisdiction, market harm is less obvious in Grand Central’s case, as TDR owners in the Grand Central Subdistrict have had comparatively less control over the TDR market and avenues of development. In Douglas County, the market’s mechanics are explicitly codified in a county ordinance.¹⁶⁸ While New York’s TDR program “artificially” restricts zoning densities within transfer districts to create a market for air rights,¹⁶⁹ the NYC Zoning Resolution does not *mandate* that developers purchase TDRs from landmarks.¹⁷⁰ Moreover, in the Grand Central Subdistrict, developers whose sites are located directly adjacent to subway entrances can already acquire extra floor area without ever having to purchase air rights from landmarks.¹⁷¹

Harm to the Grand Central Subdistrict’s TDR market is also less evident in that transfers have occurred extremely infrequently in past decades.¹⁷² In fact, since the Grand

¹⁶⁷ *Id.* at 18. “The integrity of [these] market[s] and the value of TDRs are preserved only so long as landowners in Receiving Area[s] *must* acquire them to . . . develop those [properties].” *Id.* at 13.

¹⁶⁸ See DOUGLAS COUNTY, NEV., CONSOLIDATED DEV. CODE § 20.612.010 (provision on Specific Plan Applicability), <http://dcnvda.org/Userpages/CountyCodes.aspx?TID=58&CID=279&SID=1905> [<http://perma.cc/6J5B-T2L4>] (requiring developments in excess of 160 acres (and planned development projects of 40 acres in size or greater) to use TDRs in connection with any change in intensity or density of use, including any change to a residential, commercial, or industrial zoning district or combination thereof).

¹⁶⁹ See Costonis, *Disparity Issue*, *supra* note 28, at 417 (describing how municipal zoning resolutions create TDR markets).

¹⁷⁰ See *supra* Part II.A for a discussion of TDRs as applicable to landmarks.

¹⁷¹ See discussion *supra* note 45 (describing eligibility requirements to receive a transit improvement bonus in the Grand Central Subdistrict and sidestep acquiring TDRs from landmarks).

¹⁷² When planning the East Midtown rezoning proposal, “the Department of City Planning noted the ‘limited success’ of the Grand Central Subdistrict, which was created in 1992 to allow for easier transfer of landmark development rights in the area. Only one major transfer has

Central Subdistrict was established in 1992, only one TDR transfer has taken place.¹⁷³ Moreover, the Vanderbilt Corridor rezoning would modify the existing landmark transfer process to increase the maximum permitted floor area of receiving lots, which would theoretically allow for a greater opportunity for landmarks to sell air rights.¹⁷⁴ Developers would not have to choose between providing an amenity or buying from landmarks, but could use a combination of the two.¹⁷⁵ Although the differences between the two TDR schemes is negligible in practice, as developers could elect to never buy air rights from landmarks since

occurred through that program since its creation” Been & Infranca, *supra* note 81, at 454. Argent, however, argues that the 2008 financial crisis postponed development and prevented any opportunity for it to sell its TDRs until 2011 when SL Green acquired for development a full-block site in the Vanderbilt Corridor. *See* Complaint, *supra* note 86, at 2–3.

¹⁷³ Jake Mooney, *Midtown Rezoning Has Air Rights Players Watching and Waiting*, THE REAL DEAL: N.Y. REAL ESTATE NEWS (Oct. 1, 2012), http://therealdeal.com/issues_articles/up-in-the-air/ [<http://perma.cc/686N-VQ8S>]. The transfer was to 383 Madison Avenue, a forty-seven-story building completed in 2001. *Id.* Between 1968 (when the NYC Zoning Resolution was adopted) and 1991, only two special permit applications were submitted to transfer a portion of Grand Central’s air rights. In 1979, the Philip Morris building received 74,655 square feet of air rights. The second application for the transfer of 787,335 square feet to 383 Madison in 1989 was originally rejected due to, *inter alia*, potentially significant adverse environmental impacts. N.Y.C. DEP’T OF CITY PLANNING, GRAND CENTRAL SUBDISTRICT 11 (1991), http://www.nyc.gov/html/dcp/pdf/history_project/grand_central_subdistrict.pdf [<http://perma.cc/BX2X-KMZS>]. In contrast, Douglas County hosts an active TDR exchange and tracking system for property owners, realtors and land banks. *See TDR Marketplace*, TAHOE REG’L PLANNING AGENCY, <http://www.trpa.org/permitting/transfer-development-rights/tdr-marketplace/> [<http://perma.cc/56JS-R65Y>].

¹⁷⁴ *See* Press Release, N.Y.C. Dep’t of City Planning, City Planning Begins Public Review on 5-Block Vanderbilt Corridor (Oct. 20, 2014), <http://www.nyc.gov/html/dcp/html/about/pr102014.shtml> [<http://perma.cc/FT95-F3Y7>] (explaining that the Vanderbilt Corridor proposal’s modification of the Grand Central Subdistrict Landmark Transfer Special Permit would increase the maximum permitted floor area for receiving lots located in the Vanderbilt Corridor from 21.6 FAR to 30 FAR, allowing a greater opportunity for landmarks to transfer their unused air rights).

¹⁷⁵ *Id.*

bonuses promise a greater return on investment,¹⁷⁶ these facts take much wind out of Grand Central's sails.

Considering that it may be more difficult for the terminal to show market harm than the plaintiff in *Sierra Nevada*, a court following the Ninth Circuit's reasoning would likely not find a total taking of Grand Central's air rights.¹⁷⁷ Like SNSW, Grand Central would be required to prove that the Vanderbilt Corridor rezoning deprived the company of its TDRs as opposed to reducing demand in its TDR market.¹⁷⁸ The terminal could, however, argue that by providing developers increased floor area at a much lower cost than purchasing air rights at market value, the proposal *in effect* deprives it of the practical use of its TDRs.

Yet even if Grand Central could prove that developers would always choose to provide a public amenity over buying from landmarks, the TDRs would still retain some value if the company were to sell them at a price that undercuts the developers' cost of providing an amenity.¹⁷⁹ Whether this kind of diminution constitutes a "collapsed"¹⁸⁰ market is unclear, as the Ninth Circuit does not define the term, although the TDR market could presumably collapse if a

¹⁷⁶ For a discussion of the enormous benefits that developers derive from bonuses, see *infra* Part IV.

¹⁷⁷ Recall that a *per se* taking requires a total denial of "all economically beneficial or productive use." *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1015 (1992).

¹⁷⁸ See *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App'x 663, 665 (9th Cir. 2013) (holding that the complaint failed to establish a procedural due process claim, because "plaintiffs did not allege that defendants *deprived* them of their TDRs," but rather that the approval of the master plan amendment "*diminished the value* of those TDRs by reducing demand in the TDR market as a whole, and "[a]n indirect impact of that kind is not a 'deprivation' of due process").

¹⁷⁹ In order to make a profit, Argent would have to sell its air rights for more than the basis cost of \$61 per square foot, while accounting for inflation. See discussion *supra* Part II.C.3.

¹⁸⁰ See *Sierra Nevada*, 506 F. App'x at 666 (holding that a deprivation is not alleged because the price of TDRs was not asserted to have "collapsed").

bonus were to completely obviate the need to purchase air rights from landmarks.¹⁸¹

Moreover, even if the bonuses diminished the value of the terminal's TDRs to some extent, the third *Penn Central* factor—the character of the governmental action¹⁸²—may preclude the claim,¹⁸³ although that factor may be accorded less weight than the other two.¹⁸⁴ In *Sierra Nevada*, SNSW could not show that the county's action was arbitrary, even though it contracted with a single party¹⁸⁵ as opposed to

¹⁸¹ See David Alan Richards, *Downtown Growth Control Through Development Rights Transfer*, 21 REAL PROP. PROB. & TR. J. 435, 438–39 (1986) (explaining that “no one will transfer development rights unless it literally pays to do so”).

¹⁸² *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

¹⁸³ See *Sierra Nevada*, 506 F. App'x at 666–67 (wherein a *Penn Central* claim was precluded even though “the county's conduct diminished the value of Plaintiffs' TDRs to some extent” because “the grant of development rights to a third party on a different parcel does not have the character of a classic taking in which government directly appropriates private property or ousts the owner from his domain”) (internal quotation marks omitted).

¹⁸⁴ See *Lingle v. Chevron U.S.A. Inc.*, 544 U.S., 528, 538–39 (2005) (holding that “[p]rimary” among the factors considered in takings analyses are “[t]he economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations” and that the “character of the governmental action’ . . . may be relevant.”) (emphasis added).

¹⁸⁵ See PATRICIA E. SALKIN, 1 AMERICAN LAW OF ZONING § 9:21 (5th ed. 2015) (“[C]ontract zoning is present where a local government ‘contracts away its zoning power or obligates itself by an advance contract to provide a particular zoning for the benefit of a private landowner.’” When a “municipality has bargained away a portion of its zoning power, such zoning is unlawful except in the unusual situation where a statute authorizes agreements between governmental units.”); see also Philip L. Fraietta, Note, *Contract and Conditional Zoning Without Romance: A Public Choice Analysis*, 81 FORDHAM L. REV. 1923, 1947 (2013) (noting that “[j]urisdictions are split on whether to permit contract zoning,” but that the Court of Appeals of New York expressed its approval of the method in *Church v. Town of Islip*, 168 N.E.2d 680, 683 (N.Y. 1960) (holding that a town's rezoning of a residential district to a business district to benefit a business owner in exchange for certain restrictions of the owner's use of the lot was not unconstitutional although “there is really no New York law

establishing a system giving all area landowners the choice to contribute amenities eligible for a bonus.¹⁸⁶ New York City, in contrast, gains significant public improvements through the bonuses that it would not have otherwise attained under the pre-existing TDR scheme.¹⁸⁷

Because the Vanderbilt Corridor bonus is arguably rationally related to the city's goal of obtaining free infrastructure,¹⁸⁸ and the potential economic impact on Argent's investment may be less severe than in other instances in which regulations have been upheld,¹⁸⁹ the crux of the case for Grand Central lies in the second *Penn Central*

on the subject [and] [a]ll legislation 'by contract' is invalid in the sense that a Legislature cannot bargain away or sell its powers").

¹⁸⁶ Indeed, Douglas County argued that "[t]he benefits associated with entering into a development agreement were equally available to Plaintiffs, but they simply failed to take advantage of that process." See Motion to Dismiss at 17–18, *Sierra Nevada SW Enter. v. Douglas County*, 2011 WL 1304472 (D. Nev. Mar. 30, 2011) (No. 3:10–CV–354–RCJ–RAM). The Ninth Circuit held the county's actions to be "reasonable," *Sierra Nevada*, 506 F. App'x at 666, although its conduct lacked a rational relationship to its interest in obtaining free infrastructure, as Peri was already obligated to construct the parkway adjacent to its property. Brief for Appellant, *supra* note 145, at 22. Thus, the county gained nothing by changing the master plan or eliminating the TDR requirement. See *id.* (noting that the County admits that it normally requires developers to provide infrastructure at the time of development).

¹⁸⁷ See N.Y.C., N.Y., ZONING RESOLUTION § 81–61 (2015) ("In order to preserve and protect the character of the Grand Central Subdistrict, as well as to expand and enhance the Subdistrict's extensive pedestrian and mass transit circulation network, and to facilitate the development of exceptional and sustainable buildings within the Vanderbilt Corridor, special regulations are set forth in Section 81-60 . . . inclusive, governing urban design and streetscape relationships, [TDRs] from landmarks, and the improvement of the surface and subsurface pedestrian circulation and mass transit circulation network.").

¹⁸⁸ The city's goal with respect to the Vanderbilt Corridor is "to facilitate commercial development along Madison and Vanderbilt avenues in Manhattan [and] improve pedestrian circulation within Grand Central Terminal . . ." *Vanderbilt Proposal Overview*, *supra* note 42.

¹⁸⁹ For relatively severe deprivations that been upheld, see *Village of Euclid v. Ambler Realty Co.*, 272 U.S. 365, 384, 397 (1926) (upholding a 75% diminution in value caused by a zoning law); *Hadacheck v. Sebastian* 239 U.S. 394, 405, 414 (1915) (upholding an 92.5% diminution in value).

factor—“the extent to which the regulation has interfered with . . . investment-backed expectations.”¹⁹⁰ The Ninth Circuit, however, did not weigh this factor in its analysis in *Sierra Nevada*, as it deduced that “the grant of [air] rights to a third party on a different parcel does not have the character of a ‘classic taking in which government directly appropriates private property or ousts the owner from his domain.’”¹⁹¹ Thus, according to that court, a plaintiff’s investment-backed expectations are immaterial because viable takings claims are limited to those that mimic physical ouster.¹⁹²

The Ninth Circuit, in inferring that air rights are second-class citizens to land rights, perhaps mistakenly failed to consider that TDRs possess significant commercial value¹⁹³ and have become an important land use tool since *Penn Central*.¹⁹⁴ Of course, the value of air rights is tightly connected to a locality’s density and economy, which may

¹⁹⁰ *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

¹⁹¹ *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App’x 663, 667 (9th Cir. 2013). The court referenced dictum in *Lingle v. Chevron U.S.A. Inc.*, a U.S. Supreme Court decision in which Justice O’Connor observed that “*Loretto, Lucas, and Penn Central* . . . [all] aim[] to identify regulatory actions that are functionally equivalent to” a direct appropriation of or ouster from private property. 544 U.S. 528, 539 (2005).

¹⁹² *Sierra Nevada*, 506 F. App’x at 667. However, this line of reasoning is directly at odds with other dicta in *Lingle* which emphasizes that, “[p]rimary” among the factors considered in takings analyses are “[t]he economic impact of the regulation on the claimant and, *particularly*, the extent to which the regulation has interfered with distinct investment-backed expectations.” *Lingle*, 544 U.S. at 538–39 (emphasis added) (quoting *Penn Central*, 438 U.S. at 124).

¹⁹³ See Finn, *supra* note 38 (explaining that “[t]he payoff for [entering air rights transactions] is 360-degree views, more spacious apartments, abundant light and higher resale value,” and that “[t]he reason behind the big increase in air-rights trades is that, bottom line, they can make the difference between a marginal and a profitable project”).

¹⁹⁴ *Id.* (“Air rights are . . . not fluffy chunks of available or orphaned air. . . . They have become the reigning currency of the redevelopment realm, major components in the radical vertical transformation of the city’s skyline.”).

affect how a court perceives the stakes associated with an investment. To be sure, the underlying events of *Sierra Nevada* occurred in a rural market, not one in which developers vie with one another to construct Class A office buildings or command premium views.¹⁹⁵ However, the Ninth Circuit refrains from exploring the distinctions between urban and rural air rights markets and the attending investment expectations associated with each.

Because the Ninth Circuit's analysis is wanting on the issue of investment-backed expectations, which is critical to Grand Central's case, Part III.B looks to takings cases beyond the piecemeal cases provided within this section to explore the rules that have emerged on this factor.

B. Applying Investment-Backed Expectations to the Case Study

The doctrine of “investment-backed expectations” refers to the idea that “a purchaser who pays a substantial price for a parcel of property can be assumed to have expectations that the parcel can be used for some lawful purpose,”¹⁹⁶ and that regulations that interfere with investments already made frustrate property rights.¹⁹⁷ *Penn Central* first held

¹⁹⁵ See Brief for Appellant, *supra* note 145, at 43 (noting that the Douglas County Master Plan describes Douglas County as containing “large areas of the county designated as resource lands ([with] Agriculture and Forest and Range designations)” and that the Master Plan further specifies that “[r]eceiving areas have rural underlying zoning . . . [and] are currently not zoned for urban-sized lots or . . . platted for urban densities.”). *Id.* at 16.

¹⁹⁶ See J. David Breemer & R.S. Radford, *Great Expectations: Will Palazzolo v. Rhode Island Clarify the Murky Doctrine of Investment-Backed Expectations in Regulatory Takings Law?*, 9 N.Y.U. ENVTL. L.J. 449, 451 (2001) [hereinafter Breemer & Radford, *Great Expectations*].

¹⁹⁷ See Frank. I. Michelman, *Property, Utility, and Fairness: Comments on the Ethical Foundations of “Just Compensation” Law*, 80 HARV. L. REV. 1165, 1172 (1967) (postulating that when the government exercises its “regulatory powers to override the market-expressed preferences of owners about the use of resources . . . [such action] (through retrospective impact on investments already made and expectations already formed) gives rise to claims for compensation”).

that the reasonableness of a property owner’s “distinct” investment-backed expectations is a “significant” factor in determining whether a government measure constitutes a taking.¹⁹⁸ Although the role of expectations in the takings calculus has required clarification virtually since its inception,¹⁹⁹ the Court has more recently recognized the importance of this inquiry.²⁰⁰ The question that has long

¹⁹⁸ Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 124 (1978).

¹⁹⁹ See ROBERT MELTZ ET AL., THE TAKINGS ISSUE: CONSTITUTIONAL LIMITS ON LAND USE CONTROL AND ENVIRONMENTAL REGULATION 133–34 (1999) (characterizing the investment-backed expectations standard as “amorphous” and stating that “[i]ts parameters remain uncertain even today”); Peterson, *supra* note 108, at 1324 (arguing that “[i]t is not at all clear . . . what role ‘interference with . . . expectations’ plays in the Court’s takings analysis”).

²⁰⁰ See Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg’l Planning Agency, 535 U.S. 302, 336 (2002) (stating that “interference with investment-backed expectations is one of a number of factors that a court must examine”); Palazzolo v. Rhode Island, 533 U.S. 606, 633–34 (2001) (“We have identified several factors that have particular significance in these essentially ad hoc, factual inquiries. Two such factors are the economic impact of the regulation on the claimant and, *particularly*, the extent to which the regulation has interfered with distinct investment-backed expectations.”) (emphasis added) (citation omitted) (internal quotation marks and alterations omitted); Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1019 n.8 (1998) (clarifying that the extent to which a regulation has interfered with distinct investment-backed expectations is “keenly relevant” to the takings analysis). The *Lucas* Court also suggested, in dicta, that expectations might provide a solution to the problem of determining the relevant property interest against which loss of economic use was to be measured (in Grand Central’s case, the value of TDRs alone versus the value of the terminal and TDRs combined as one parcel).

The answer . . . may lie in how the owner’s expectations have been shaped by the State’s law of property—*i.e.*, whether and to what degree the State’s law has accorded legal recognition and protection to the *particular interest in land* with respect to which the takings claimant alleges a diminution in . . . value.

Id. at 1018 n.7 (emphasis added). See also Breemer & Radford, *Less Murky Doctrine*, *supra* note 108, at 380 (specifying that “[i]t is . . . clear that expectations do play an important role when the claim is that a regulation

dogged the inquiry is how to determine when a landowner's development expectations are sufficiently "reasonable" such that their frustration actually counts against the government as a factor in the *Penn Central* calculus.²⁰¹

The extant cases on TDRs as the subject of regulatory takings are few, and provide minimal insight as to whether Grand Central's expectations to profit from its investment in air rights are reasonable. Part III.B analyzes the company's expectations through the lens of a public benefit theory proffered by the New York Court of Appeals in *Penn Central* in combination with black letter doctrine gleaned from more recent jurisprudence on the factor.²⁰²

1. The "Social Increment Theory" with Respect to Investment-Backed Expectations

The *Penn Central* Court held that the reasonableness of the terminal owner's expectations as to how it could use its property was inextricably linked to the type of business the owner operated.²⁰³ Yet the entity that owns Grand Central Terminal today is not only distinct from the entity that owned it at the time *Penn Central* was litigated, but operates an altogether unrelated core business.²⁰⁴ Therefore, in assessing the reasonableness of the investment-backed expectations held by Grand Central's current owner, it is instructive to compare that entity's expectations with those of the Penn Central Transportation Company ("Penn Central Company")—the owner at the time of *Penn Central*.

In *Penn Central*, Justice Brennan reasoned that the Penn Central Company's expectations were not frustrated because it could still "use the property precisely as it ha[d] been used

causes a taking by depriving a property of something less than all of its beneficial use or value—the classic *Penn Central* claim").

²⁰¹ See *Philip Morris, Inc. v. Reilly*, 312 F.3d 24, 36 (1st Cir. 2002) (noting that, "[d]espite the importance of reasonable investment-backed expectations under the *Penn Central* framework, the courts have struggled to adequately define this term").

²⁰² For this discussion see *infra* Parts III.B.1 and III.B.2.

²⁰³ See *infra* notes 205–06 and accompanying text.

²⁰⁴ *Id.*

for the past 65 years: as a railroad terminal containing office space and concessions.”²⁰⁵ Therefore, “the law [did] not interfere with what must be regarded as the company’s *primary expectation* concerning the use of the parcel.”²⁰⁶ However, the Penn Central Company was, foremost, a transportation company in the business of operating trains,²⁰⁷ while Argent is a diversified real estate investment company that purchased the terminal for the primary purpose of acquiring its air rights.²⁰⁸ Moreover, the Penn Central Company collected rent from a variety of commercial interests that leased space in the terminal,²⁰⁹ while the MTA, which leases the terminal from Argent,²¹⁰ is the sole recipient of any revenue that Grand Central generates. Although some portion of those revenues is funneled to Argent in the form of rent,²¹¹ “the value of that rent stream is de minimis in comparison to the potential value of the TDRs,” which represent 85% of the property value Argent

²⁰⁵ Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 136 (1978).

²⁰⁶ *Id.* (emphasis added).

²⁰⁷ For a brief description of the company’s business and history, see *Penn Central Transportation Co., Baker Library Lehman Brothers Collection—Contemporary Business Archives*, HARVARD BUS. SCH., http://www.library.hbs.edu/hc/lehman/company.html?company=penn_central_transportation_company [<http://perma.cc/Z7NL-LE8C>].

²⁰⁸ See discussion *supra* Part II.C.3.

²⁰⁹ Complaint, *supra* note 86, at 10.

²¹⁰ The MTA’s lease terminates in the year 2274. See Weiss, *supra* note 96.

²¹¹ See Press Release, Metro. Transp. Auth., MTA to Lease Two Brand New Spaces in Grand Central Terminal (May 20, 2012), <http://www.mta.info/press-release/mta-headquarters/mta-lease-two-brand-new-spaces-grand-central-terminal> [<http://perma.cc/4FVP-UP63>] (“The re-emergence of the Terminal as an increasingly popular retail destination and transportation hub has been mirrored by an increase in leasing revenue to the MTA. In 1994, before the renovation, the MTA earned \$7 million in rent for retail space at Grand Central. By 2002, rental income reached \$15 million from . . . 100 retail tenants. By 2011 the MTA nearly double [sic] the rent again, to \$27 million.”). Of that revenue, the MTA pays annual rent to Argent of \$2.24 million. Weiss, *supra* note 96.

purchased.²¹² Considering this, the *Penn Central* Court's aforementioned dicta on expectations may not be entirely instructive for Argent. The New York Court of Appeals' opinion, on the other hand, provides some insight by which to evaluate an air rights holder's investment-backed expectations.²¹³

Chief Judge Breitel, writing for the New York Court of Appeals, theorized 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."²¹⁴ Chief Judge Breitel relied in part on this "social increment theory of valuation," finding that governmental and public aid in making the terminal a "major transportation nexus" had "contributed substantially to the site's value."²¹⁵ Among the public contributions to the terminal's value that he cited were government-granted subsidies to railroads, rights of way created by eminent domain, real estate tax exemptions, and most importantly, the routing of subway lines to converge below the terminal.²¹⁶ Considering these

²¹² Complaint, *supra* note 86, at 14.

²¹³ However, note that this opinion predates judicial discussion of "investment-backed expectations," the concept which as applied to regulatory takings was first referenced in a judicial decision in the U.S. Supreme Court's *Penn Central* opinion. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124–28 (1978). The Court cited the analysis of Frank Michelman, who suggested that just compensation should be paid when the government interferes with a property owner's "distinctly perceived, sharply crystallized, investment-backed expectation." Michelman, *supra* note 197, at 1233.

²¹⁴ *Penn Cent. Transp. Co. v. City of New York*, 366 N.E.2d 1271, 1278 (N.Y. 1977), *aff'd*, 438 U.S. 105 (1978). Chief Judge Breitel echoed this philosophy in *Fred F. French Investing Co. v. City of New York*, noting that "no property is an economic island, free from contributing to the welfare of the whole of which it is but a dependent part." 350 N.E.2d 381, 389 (N.Y. 1976).

²¹⁵ *Costonis, Disparity Issue, supra* note 28, at 410. *See also Penn Cent.*, 366 N.E.2d at 1275 (observing that "society . . . especially through its government . . . has created much of the value of the terminal property").

²¹⁶ *See Costonis, Disparity Issue, supra* note 28, at 416 (citing *Penn Cent.*, 366 N.E.2d at 1275–76).

government-secured benefits, Chief Judge Breitel stated that one issue to consider in evaluating a regulatory takings claim is the extent to which the government must assure a reasonable return on “that ingredient of property value created not so much by the efforts of the property owner, but instead by the accumulated indirect social and direct governmental investment in the physical property, its functions, and its surroundings.”²¹⁷ To prevail, “plaintiffs [in regulatory takings cases] must establish that there was no possibility of earning a reasonable return on the privately contributed ingredient of the property’s value.”²¹⁸ The New York Court of Appeals, however, did not clarify what constitutes a privately created ingredient.

Put simply, Chief Judge Breitel stated that the crux of the matter is that whether a regulation interferes with a property owner’s investment-backed expectations depends on whether that owner created value. To what extent the social increment theory was essential to the final outcome in *Penn Central* is unclear.²¹⁹ Nonetheless, Chief Judge Breitel’s cogent argument²²⁰ is one that either party—air rights owner

²¹⁷ *Penn Cent.*, 366 N.E.2d at 1272–73.

²¹⁸ *Id.* at 1276.

²¹⁹ See Costonis, *Disparity Issue*, *supra* note 28, at 417 (“[W]hether and to what extent the social increment theory was essential to the outcome in *Grand Central Terminal* is unclear.”). The U.S. Supreme Court did not comment on the theory in its opinion, possibly to avoid making sweeping new changes in law. See PATRICIA A. SALKIN, 1 NEW YORK ZONING LAW AND PRACTICE § 7:50 (4th ed. 2015) (stating that the U.S. Supreme Court affirmed, but avoided some of the issues resolved by the Court of Appeals); Frank Schnidman, *A Trip Back in Time, Including Judge Charles D. Breitel’s Rationale for His Fred French and Penn Central Decisions*, 30 TOURO L. REV. 421, 428–29 (2014) (suggesting that the U.S. Supreme Court may have been “scaredy cats” for avoiding taking a position on this assertion).

²²⁰ See Costonis, *Disparity Issue*, *supra* note 28, at 403–11 (calling the court’s efforts “bold” for recognizing that TDRs do not provide a fully compensatory offset that affords the landowner an equitable return on his property, and commencing the job of chipping away at that issue’s “impenetrable densities” by excluding from the base upon which that return is calculated the “social increment” of value accruing to the regulated property by virtue of government’s activities).

or municipality—may employ to strengthen its case. However, an owner of unused air rights may have a difficult time succeeding in this argument considering that the value of TDRs depends on an external market²²¹ comprised of a variety of factors that are difficult to capture.²²² As for municipalities, the theory will likely apply with more force to a small number of properties—like the terminal—“whose commercial utility is largely a consequence of massive public investments at or near the site and whose owners are the beneficiaries of dramatic infusions of public largess.”²²³

²²¹ See Note, *The Unconstitutionality of Transferable Development Rights*, 84 YALE L.J. 1101, 1110–11 (1975) [hereinafter *Unconstitutionality of TDRs*] (stating that, “[t]he market for development rights, if it exists, determines their value.”).

²²² Such factors may include “the number of possible TDR buyers and sellers on a block, the type of project the purchaser is developing, and where on a block a development site is located” as well as “the quality of views from the buildings using the TDRs” FURMAN CENTER STUDY, *supra* note 9, at 14–15. The value of air rights is generally thought of as a residual value of the underlying land (or “fee simple”) after deductions for costs and losses associated with erecting structures in or upon the air rights. Extra costs associated with developing air rights may include construction costs (such as extra foundation and suspension systems necessary to support higher buildings), financing and carrying charges (particularly interest) caused by the longer construction period resulting from the fact that the air rights holder may be required to construct his project around existing construction, and additional legal transaction costs. See *Appraisal of Air Rights*, in DEP’T OF HOUS. & URBAN DEV., VALUATION ANALYSIS FOR PROJECT MORTGAGE INSURANCE HANDBOOK, <http://www.hud.gov/offices/adm/hudclips/handbooks/hsggh/4465.1/44651c4HSGH.pdf> [<http://perma.cc/23BP-XD46>].

²²³ Costonis, *Disparity Issue*, *supra* note 28, at 416. Hence, according to Costonis,

one should read very literally indeed . . . Breitel’s admonition that Grand Central Terminal is no *ordinary* landmark. . . . [T]he segregation and quantification of an individual property’s public and private increments of value are truly formidable tasks, especially when the respective governmental and private contributions have been made continuously over a long period.

Id. at 416–17 (internal quotation marks omitted).

2. Investment-Backed Expectations as Applied to Modern Partial Takings Cases

In addition to Chief Judge Breitel’s social increment theory, holders of unused air rights may bolster their arguments by considering how the doctrine of investment-backed expectations has evolved over time to present new challenges and opportunities.

Under current regulatory takings law analysis, most cases will be decided under rules that must consider a property owner’s investment-backed expectations.²²⁴ However, the doctrine of investment-backed expectations has evolved to adopt varying forms since its inception in *Penn Central*,²²⁵ shifting from an inquiry having the potential to “strengthen the position of the property owner against government regulation”²²⁶ to one that resembles a procedural bar.²²⁷ In *Penn Central*, the U.S. Supreme Court originally applied a theory of expectations that asks “whether or not [a] measure . . . can easily be seen to have practically deprived the claimant of some *distinctly perceived, sharply crystallized, investment-backed expectation*.”²²⁸ Justice Brennan described “distinct” investment-backed expectations as one of several factors significant to a partial takings

²²⁴ Thomas Ruppert, *Reasonable Investment-Backed Expectations: Should Notice of Rising Seas Lead to Falling Expectations For Coastal Property Purchasers?*, 26 J. LAND USE & ENVTL. L. 239, 246 (2011).

²²⁵ For a general discussion of the doctrine’s evolution, see Breemer & Radford, *Less Murky Doctrine*, *supra* note 108.

²²⁶ Breemer & Radford, *Great Expectations*, *supra* note 196, at 460.

²²⁷ *See id.* at 480 (noting that the “expectations analysis [has been elevated] from its initial place as one element in *Penn Central*’s multi-factor balancing test, and converted . . . into something resembling a procedural bar”).

²²⁸ *See id.* at 453 (noting that Professor Michelman originated the notion of investment-backed expectations as a factor in takings analysis, and describing Justice Brennan’s incorporation of the concept in *Penn Central*). “Michelman proposed a regulatory takings test that focused on the nature of the property interest impacted by government regulation, rather than merely the extent to which the regulation may have diminished the property’s value.” *Id.*

inquiry,²²⁹ and considered several issues relevant to that factor, such as whether a broad or narrow range of expectations had been frustrated, and whether the opportunity to put property to profitable use had been foreclosed.²³⁰

The U.S. Supreme Court subtly altered the expectations analysis one year later in *Kaiser Aetna v. United States* by replacing “distinct” with “reasonable” without explaining the distinction between the two terms.²³¹ This change had the effect of shifting the inquiry’s focus from the impact of a regulation²³² and whether an investment was made in furtherance of a planned land use to an objective standard that evaluates the appropriateness of the plaintiff’s expectations, particularly in the context of the regulatory landscape extant at the time of acquisition.²³³ Lower courts have often since seized on this discrepancy to find property owners’ expectations unreasonable when they should have anticipated that the government might curtail the expected continued use of their land.²³⁴ During the period between *Penn Central* and *Lucas*, for instance, courts routinely rejected takings claims based on investment-backed expectations if a landowner merely operated in a highly

²²⁹ See *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

²³⁰ See Breemer & Radford, *Great Expectations*, *supra* note 196, at 459 (describing Justice Brennan in *Penn Central* as having concluded that a taking does not occur when: “(1) only a narrow range of expectations had been completely frustrated, while other plans for construction above the terminal might yet come to fruition; (2) to the extent the firm’s expectations of building in a particular spatial area had been foreclosed, comparable expectations might be realized through the use of TDRs; [and] (3) the owners’ fundamental expectation of being allowed to continue to put their property to profitable use had not been foreclosed . . .”).

²³¹ See *Kaiser Aetna v. United States*, 444 U.S. 164, 175 (1979); Robert Meltz, *Takings Law Today: A Primer for the Perplexed*, 34 *ECOLOGICAL L.Q.* 307, 329 n.150 (2007).

²³² Meltz, *supra* note 231, at 329 n.150.

²³³ *Id.*

²³⁴ See Breemer & Radford, *Great Expectations*, *supra* note 196, at 461–62.

regulated field such as real estate development,²³⁵ regardless of whether the regulation at issue was enacted at the time of investment. Where a general regulatory scheme existed that might authorize subsequent restrictions in the future, an owner was presumed to have notice that the rules concerning land use could change at any time.²³⁶

While the Court subsequently scaled back this expansive notice-based view, acknowledging that an owner's expectations are "keenly relevant" to partial takings decisions²³⁷ and that cases should be analyzed using an ad hoc balancing approach,²³⁸ lower courts have continued to use the expectations test as a shield for the government.²³⁹

²³⁵ See, e.g., *Good v. United States*, 39 Fed. Cl. 81, 84 (Fed. Cl. 1997) (finding no takings liability in part because "[l]and development . . . was a highly regulated business . . .").

²³⁶ See *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1008–09 (1984) (holding that even if no restraint exists at the time of investment, if the industry is highly regulated, then an owner does not have a reasonable expectation that his or her property would be protected); *Connolly v. Pension Benefit Guaranty Corp.*, 475 U.S. 211, 227 (1986) (holding that property owners operating in a highly regulated field (including private businesses as well as highly regulated industries) with a long history of government regulation could not have a reasonable expectation that government regulation would not be altered to their detriment); *Good v. United States*, 189 F.3d 1355, 1361–62 (Fed. Cir. 1999), *aff'g* 39 Fed. Cl. 81 (Fed. Cl. 1997) (upholding a revocation of a landowner's permit to develop property on the grounds that the owner received constructive notice of a regulation not by the existence of any regulations that pre-dated development plans, but by an increasingly strict regulatory environment and resulting regulations).

²³⁷ *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1019 n.8 (1992).

²³⁸ See *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 303 (2002) (stating that "regulatory takings jurisprudence is characterized by 'essentially ad hoc, factual inquiries,' designed to allow 'careful examination and weighing of all the relevant circumstances (citing *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978) and *Palazzolo v. Rhode Island*, 533 U.S. 606, 636 (2001))").

²³⁹ See JULIAN CONRAD JUERGENSMEYER & THOMAS E. ROBERTS, *LAND USE PLANNING AND DEVELOPMENT REGULATION LAW* § 10:7 (3d ed. 2013) ("While some initially saw in this concept [of investment-backed expectations] 'new support for landowner takings claims, the factor has become, instead, a shield for government.'") (internal alterations omitted);

A “full application” of the three *Penn Central* factors can “occasionally” be found in post-*Lucas* takings decisions.²⁴⁰ For example, Justice O’Connor’s concurrence in a more recent case makes clear that regulatory climate alone is not dispositive of whether investment-backed expectations are frustrated,²⁴¹ and prescribes that courts must generally “attend to . . . what fairness requires in a given case.”²⁴² According to one practitioner, this principle may leave room for the identification of additional expectations considerations, which might include what the government told the owner about the property before it was acquired, and whether it allowed the owner to take concrete steps toward the desired use before prohibiting it.²⁴³

Still, a significant number of regulatory takings cases continue to rely *solely* on investment-backed expectations, especially as imputed via constructive notice rules, as dispositive of Fifth Amendment takings claims.²⁴⁴ Moreover,

Mehaffy v. U.S., 499 Fed. App’x 18, 22 (Fed. Cir. 2012) (holding that landowner’s reasonable investment-backed expectations had to be assessed “in light of the regulatory climate that existed when he purchased the property”).

²⁴⁰ Breemer & Radford, *Great Expectations*, *supra* note 196, at 496. See, e.g., *Tahoe-Sierra*, 545 U.S. at 336 (stating that, “under [partial regulatory takings] cases, interference with investment-backed expectations is one of a number of factors that a court must examine”).

²⁴¹ *Palazzolo*, 533 U.S. at 634–36 (O’Connor, J., concurring) (stating that “the state of regulatory affairs at the time of acquisition is not the only factor that may determine the extent of investment-backed expectations,” and clarifying that the decision “does not remove the regulatory backdrop against which an owner takes title to property from the purview of the *Penn Central* inquiry. It simply restores balance to that inquiry. Courts properly consider the effect of existing regulations under the rubric of investment-backed expectations in determining whether a compensable taking has occurred.”).

²⁴² *Id.* at 635.

²⁴³ See Breemer & Radford, *Less Murky Doctrine*, *supra* note 108, at 393.

²⁴⁴ See Breemer & Radford, *Great Expectations*, *supra* note 196, at 496–97 (“Indeed, some lower courts have voiced what amounts to a third ‘categorical’ rule: that the takings inquiry ends, and the government is absolved of liability, once the court finds against a claimant on the issue of imputed expectations.”). See, e.g., *Good v. United States*, 189 F.3d 1355,

“courts have generally refrained from allowing the purchase price of land to qualify as an investment-backed expectation,”²⁴⁵ and have held that “disappointed expectations” based on the price paid does not create a taking.²⁴⁶

That an industry’s regulatory climate should not be dispositive in determining the reasonableness of an investor’s expectations cuts somewhat in Grand Central’s favor, as the city would likely argue that incentive zoning bonuses are an historic part of the city’s regulatory fabric.²⁴⁷ Grand Central’s owner may also invoke the aforementioned additional expectations considerations, given that the Court partially justified the terminal’s regulation as a landmark upon the receipt of TDRs that would lead to profit,²⁴⁸ and given that the city’s landmark TDR transfer mechanism aided the company in taking concrete steps toward selling the TDRs at market value.²⁴⁹ Moreover, the Court has noted that while expectations are important they are “not

1363 (Fed. Cir. 1999) (denying the plaintiff a development permit after it had already been granted based on the plaintiff’s awareness of general increasing concern for environmental matters during the 1970s); *Deltona Corp. v. United States*, 657 F.2d 1184, 1193 (Ct. Cl. 1981) (denying a development permit based on the plaintiff’s awareness that the standards and conditions governing the issuance of permits could change, although at the time the plaintiff “had every reason to believe that those permits would be forthcoming when it sought them”).

²⁴⁵ *JUERGENSMEYER & ROBERTS*, *supra* note 239, at § 10:7 n.20 (citing *New Port Largo, Inc. v. Monroe County*, 95 F.3d 1084 (11th Cir. 1996), for the proposition that the “purchase price does not create a property right immunizing the landowner from future land use changes”).

²⁴⁶ *Id.* at § 10:7 n.21 (citing *William C. Haas & Co. v. City and County of San Francisco*, 604 F.2d 1117, 1121 (9th Cir. 1979)).

²⁴⁷ The city would likely argue that it has regularly implemented bonuses since the inception of the Zoning Resolution. *See supra* notes 55–56 and accompanying text in Part II.C; *see also generally History of NYC Transit Bonuses 1982–2014*, N.Y.C DEP’T OF CITY PLANNING, http://www.nyc.gov/html/dcp/pdf/vanderbilt_corridor/history_of_transit_bonuses.pdf [<http://perma.cc/3ZTS-WBW6>].

²⁴⁸ *See supra* notes 26–29 and accompanying text.

²⁴⁹ *See supra* Part II.B.

talismanic.”²⁵⁰ In other words, unreasonable expectations alone are not sufficient to deny a taking, and reasonable expectations, without more, are not sufficient to find a taking. Courts must weigh and balance the three *Penn Central* factors in any partial takings analysis.²⁵¹

In practice, however, a trial court may still measure the reasonableness of Argent’s expectations to profit from the sale of its air rights against the backdrop of the existing zoning regime—a regime that Chief Justice Rehnquist once suggested constituted “part of a landowner’s reasonable investment-backed expectations”²⁵²—and may hold that no taking occurred based on Argent’s awareness of the regulatory risk.²⁵³ In that scenario, Argent would have to do more than simply show that it was denied the ability to exploit a property interest that it had believed was available for development.²⁵⁴ The company would need to argue that the three *Penn Central* factors tip the scales in its favor by emphasizing the economic loss Argent suffered from its inability to sell the air rights (i.e., the first factor)—in connection with the company’s primary expectation to profit from the sale (i.e., the second factor)—as a result of sudden and unforeseeable government action (i.e., the third factor).²⁵⁵

²⁵⁰ *Palazzolo v. Rhode Island*, 533 U.S. 606, 634 (2001).

²⁵¹ *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 342 (2002).

²⁵² JUERGENSEMEYER & ROBERTS, *supra* note 239, at § 10:7 n.18 (citing *Tahoe-Sierra*, 535 U.S. at 352 (Rehnquist, C.J., dissenting)).

²⁵³ *See supra* notes 237–239 and accompanying text (explaining that while the U.S. Supreme Court has scaled back its expansive notice-based view of expectations, some lower courts have not followed suit).

²⁵⁴ *See Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 130 (1978) (“The submission that appellants may establish a ‘taking’ simply by showing that they have been denied the ability to exploit a property interest that they heretofore had believed was available for development is quite simply untenable.”).

²⁵⁵ According to Professor Mandelker’s analysis of Supreme Court regulatory takings precedent, a landowner’s investment-backed expectations are only reasonable when the government acts “suddenly, unexpectedly, and substantially to interfere with property rights.”

C. A Framework for Air Rights Takings Analysis Going Forward and an Outcome for Grand Central

In the decades since *Penn Central*, TDRs have become an important land use tool²⁵⁶ and a valuable commodity in urban areas where they are traded at a premium.²⁵⁷ Where municipal zoning amendments impair TDR markets established by existing zoning code, cities may increasingly find themselves embroiled in takings litigation.²⁵⁸ Given that air rights' value is tied to a plethora of circumstantial factors,²⁵⁹ and that challenges of bonus systems represent unmapped legal territory,²⁶⁰ this next generation of TDR cases will require a unique framework for analysis apart from the "classic" takings analyses²⁶¹ reserved for land parcels. The correct framework should consider how zoning amendments compare to the amendments in the two extant cases on the diminution in value of TDRs,²⁶² and weigh the reasonableness of the landowner's investment-backed

JUERGENSMEYER & ROBERTS, *supra* note 239, at § 10:7 n.41. For an overview of the three *Penn Central* factors, see discussion *supra* Part II.A.

²⁵⁶ See Finn, *supra* note 38 ("Air rights are, in actuality, not fluffy chunks of available or orphaned air. They are unused or excess development rights gauged, like building density or lot size, by the square foot and transferable . . . from one buildable lot to another. They have become the reigning currency of the redevelopment realm, major components in the radical vertical transformation of the city's skyline.").

²⁵⁷ See discussion on air rights' value *supra* Part II.B.

²⁵⁸ As air rights continue to increase in value as a form of currency, more developers may purchase them as an alternative real estate investment.

²⁵⁹ A few of these factors include district-specific rules, the availability of developments requiring more air rights, and the market value of specific neighborhoods. See discussion *supra* note 222.

²⁶⁰ See discussion *supra* Part II.C.

²⁶¹ See Yowell, *supra* note 50, at 529 (citing *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 528, 539 (2005)) (describing the classic taking as one "in which the government directly appropriates private property or ousts the owner from his domain.").

²⁶² See *supra* Part III.A for a thorough discussion of these two cases, *Fred F. French Investing Co. v. City of New York*, 350 N.E.2d 381 (N.Y. 1976) and *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App'x 663 (9th Cir. 2013).

expectations with the other *Penn Central* factors,²⁶³ a step the Ninth Circuit failed to take in *Sierra Nevada*.²⁶⁴

Considering Grand Central's claim exclusively in view of the holdings in *Fred French* and *Sierra Nevada*, the terminal is not likely to prevail in challenging the constitutionality of the Vanderbilt Corridor rezoning, as that proposal is not as intentionally directed against the terminal as was the city's action toward the developer in *French*.²⁶⁵ Neither would the GCPRIB²⁶⁶ render the value of Grand Central's air rights "so uncertain and contingent, as to deprive the property owner of their practical usefulness, except under rare . . . circumstances,"²⁶⁷ unless the terminal can show that developers would consistently elect the bonus even if the terminal were to price its air rights so as to subsume any benefit that developers derive from the bonus.²⁶⁸

Grand Central's claim would also fail under *Sierra Nevada*, as the proposal would not completely deprive the company of its TDRs but merely reduce demand in the TDR market.²⁶⁹ Moreover, the fact that only one TDR transfer has occurred since 2001 weighs against a finding of market collapse.²⁷⁰ The proposal could also theoretically benefit the

²⁶³ For a discussion of the significance of investment-backed expectations, see *supra* Part III.B.

²⁶⁴ See discussion *supra* in Part III.A.2.

²⁶⁵ See *supra* notes 126–27 and accompanying text.

²⁶⁶ Again, "GCPRIB" stands for Grand Central Public Realm Improvement Bonus.

²⁶⁷ *Fred French*, 350 N.E.2d. at 389.

²⁶⁸ See *infra* Part IV for a discussion of the attractiveness of bonuses to developers.

²⁶⁹ *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App'x 663, 665 (9th Cir. 2013) (holding that the complaint failed to establish a procedural due process claim, as plaintiffs did not "allege that defendants *deprived* them of their TDRs," but that the approval of the master plan amendment "*diminished the value* of those TDRs by reducing demand in the TDR market as a whole," and an "indirect impact of that kind" is not a "deprivation" of due process).

²⁷⁰ See Mooney, *supra* note 173. Argent, however, argues that the 2008 financial crisis postponed development and any opportunity for it to sell its TDRs until 2011 when SL Green acquired all of the buildings on a

terminal by increasing the number of transfer opportunities.²⁷¹ However, no New York court or federal court in the Second Circuit is bound to follow *Sierra Nevada*²⁷² (although it is one of the only cases with a comparable fact pattern), and the opinion's omission of an analysis of investment-backed expectations may be misguided.²⁷³ The key for Grand Central's owner, then, may be to argue that the zoning amendment interfered with its primary expectation concerning the use of the parcel²⁷⁴ (namely, profiting from the resale of the terminal's air rights)²⁷⁵—a factor that must be weighed in accordance with the other *Penn Central* factors. Grand Central must also distinguish itself from the plaintiff in *Penn Central* in order to safeguard its expectations from being negated by Chief Judge Breitel's social increment theory of valuation.²⁷⁶

full-block site in the Vanderbilt Corridor for development. See Complaint, *supra* note 86, at 2–3.

²⁷¹ See Press Release, N.Y.C. Dep't of City Planning, City Planning Begins Public Review on 5-Block Vanderbilt Corridor (Oct. 20, 2014), <http://www.nyc.gov/html/dcp/html/about/pr102014.shtml> [<http://perma.cc/7PJF-TWAG>] (explaining that the Vanderbilt Corridor proposal's modification of the Grand Central Subdistrict Landmark Transfer Special Permit would increase the maximum permitted floor area for receiving lots located in the Vanderbilt Corridor from 21.6 FAR to 30 FAR allowing a greater opportunity for landmarks to transfer their unused air rights).

²⁷² Indeed, as an unpublished opinion, even the Ninth Circuit is not bound by *Sierra Nevada*. See *supra* notes 162–63.

²⁷³ For a discussion of U.S. Supreme Court precedent that calls for the weighing of investment-backed expectations in partial takings analyses, see *supra* Part III.B.2.

²⁷⁴ The Court in *Penn Central* upheld the regulation because the regulation “[did] not interfere with what must be regarded as *Penn Central's primary expectation* concerning the use of the parcel.” *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 136 (1978) (emphasis added).

²⁷⁵ For a discussion of Argent's primary expectation concerning investment in the terminal, see *supra* Part II.C.3.

²⁷⁶ Again, Chief Judge Breitel's social increment theory posits that a public regulation need not guarantee a reasonable return on “that ingredient of property value created . . . by the accumulated indirect social and direct governmental investment in the physical property, its functions and surroundings,” although it must do so on value created by the “efforts

IV. MUNICIPALITIES SHOULD SUPPORT TDR MARKETS DESPITE THE CONSTITUTIONAL UNCERTAINTY SURROUNDING TDR DEVALUATION

Zoning bonus programs have allowed valuable public amenities to be built that the city would not have otherwise been able to afford.²⁷⁷ However, the fairness of a government's action is called into question when landowners who have invested in a property for the primary purpose of selling that property's air rights—and who relied on the existing regulatory scheme in making the investment—suffer a staggering loss when the government changes the rules of the game. When a municipality undermines the integrity of a TDR market, owners left with a substantial number of unused air rights are economically jeopardized.²⁷⁸ But as the foregoing analysis shows, these holders of unused air rights are likely not constitutionally protected from this position.

Part IV.A of this Note qualifies the framework for the analysis of TDR takings claims established in Part III by illuminating additional arguments that may cut against the constitutional protection of TDRs. However, Part IV.B argues that, despite these arguments, compelling policy reasons exist for cities to create incentives that support a

of the property owner,”—i.e., the “privately contributed ingredient of the property's value.” *Penn Cent. Transp. Co. v. City of New York*, 366 N.E.2d 1271, 1272–73 (N.Y. 1977). *See supra* notes 214–19 and accompanying text.

²⁷⁷ *See* BROOKS, *supra* note 8, at 2 (contending that, “[w]ithout the bonus . . . desired amenities would not be economically feasible”); Kayden, *supra* note 7, at 8 (noting that the technique of incentive zoning “enjoys a superior track record for creating amenities which otherwise might not exist”).

²⁷⁸ This problem arises when holders of unused air rights, such as Argent Ventures, who purchase the air rights for the primary purpose of selling them at a profit to neighboring developers under an existing zoning scheme designed to facilitate the transfer of development rights, are unable to offload those rights if a municipality subsequently creates an end-run regulation that allows developers to build higher without using any air rights at all. *See generally supra* Part II.C.

robust TDR market. It also sets forth potential solutions that would allow municipal bonus and TDR systems to coexist. Finally, Part V concludes.

A. Arguments that Cut Against the Constitutional Protection of TDRs

While TDRs have become an important investment option and land use currency, it is questionable whether they will ever be perceived the same as property rights in land. The root of the difficulty in equating the two may lie in TDRs' dual nature as both real property and personal property. TDRs are conceptually slippery. On the one hand, they exist only in relation to real property. However, like personal property, they are tradable, belong to an individualized market, and have an economic value that fluctuates with that market. The significance of the real versus personal property distinction lies in the idea that, while government is bounded in its authority to restrict the use of a land parcel,²⁷⁹ the scope of non-compensable government action is greater with regard to personal property.²⁸⁰

Andrus v. Allard is a pertinent U.S. Supreme Court decision that explores the distinction between real and personal property in a takings challenge.²⁸¹ In *Andrus*, two traders of Native American artifacts were prosecuted for selling artifacts composed of bald eagle feathers.²⁸² The traders were charged with violating the Bald and Golden Eagle Protection Act, which makes it unlawful to “take, possess, sell, purchase or . . . transport” eagles or parts

²⁷⁹ See *Penn. Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922) (holding that, “while property may be regulated to a certain extent, if a regulation works too great a burden on property owners, it will be recognized as a taking requiring just compensation”).

²⁸⁰ See Glenn P. Sugameli, *Lucas v. South Carolina Coastal Council: The Categorical and Other “Exceptions” to Liability for Fifth Amendment Takings of Private Property Far Outweigh the “Rule,”* 21 ENVTL. L. 939, 986 (1999).

²⁸¹ *Andrus v. Allard*, 444 U.S. 51 (1979). *Andrus* was decided the year following *Penn Central*.

²⁸² *Id.* at 54.

thereof, with the proviso that the prohibition does not apply to “possession or transportation” of parts taken prior to the Act’s effective date.²⁸³ The traders brought suit alleging that the Act did not forbid the sale of their artifacts insofar as the constituent bird parts were obtained prior to the effective date, and that if the Act applied to such property, it amounted to a taking.²⁸⁴

The Court unanimously held that the proviso did not apply to sales activity,²⁸⁵ and that “the simple prohibition of the sale of lawfully acquired property . . . does not effect a taking.”²⁸⁶ “[G]overnment regulation,” wrote Justice Brennan, “by definition involves the adjustment of rights for the public good.”²⁸⁷ This adjustment “curtails some potential for the use or economic exploitation of private property.”²⁸⁸ Justice Brennan reasoned that “[g]overnment hardly could go on if to some extent values incident to property could not be diminished without paying for every such change in the general law.”²⁸⁹ The holding in *Andrus* did not unconstitutionally deprive the plaintiffs of their property because there was no physical invasion or restraint upon their possession of the feathers,²⁹⁰ but, rather, a restraint on “one means of disposing of the [property].”²⁹¹ Indeed, the opinion concedes that it is “undeniable that the regulations . . . prevent the most profitable use of appellees’ property.”²⁹² “But,” said the Court, “[t]he denial of one traditional property right does not always amount to a taking,” and, “the destruction of one ‘strand’ of [an owner’s]

²⁸³ Bald and Golden Eagle Protection Act, 16 U.S.C. § 668 (2012).

²⁸⁴ *Andrus*, 444 U.S. at 54–55.

²⁸⁵ *Id.* at 64.

²⁸⁶ *Id.* at 67–68.

²⁸⁷ *Id.* at 65.

²⁸⁸ *Id.*

²⁸⁹ *Id.* (citing *Penn. Coal Co. v. Mahon*, 260 U.S. 393, 413 (1922)).

²⁹⁰ *Id.* at 65–66.

²⁹¹ *Id.* at 65.

²⁹² *Id.* at 66.

bundle [of rights] is not a taking, because the aggregate must be viewed in its entirety.”²⁹³

The plaintiffs in *Andrus* were in the business of selling Native American artifacts containing eagle feathers and, like Grand Central’s current owner, had purchased the property only to sell it at a profit.²⁹⁴ According to the Court, however, the “loss of future profits—unaccompanied by any physical property restriction—provides a slender reed upon which to rest a takings claim.”²⁹⁵ The Court elaborated that, because of the uncertainty of predicting profits, “the interest in anticipated gains has traditionally been viewed as less compelling than other property-related interests.”²⁹⁶ Thus, if TDRs are a discrete part of an investment’s value, as were the eagle feathers, the loss of future profits from the inhibited use of TDRs is not a compelling argument. Put another way, if TDRs are more like eagle feathers than land, they will not merit the type of constitutional protection reserved for land, especially if devalued TDRs constitute one “strand” in an owner’s bundle of rights.

Moreover, even if TDRs were conceptually severed from land,²⁹⁷ and their stand-alone value reduced to zero, the

²⁹³ *Id.* at 65–66.

²⁹⁴ BERNARD SCHWARTZ, THE UNPUBLISHED OPINIONS OF THE REHNQUIST COURT 103 (1996).

²⁹⁵ *Andrus*, 444 U.S. at 66.

²⁹⁶ *Id.*

²⁹⁷ Conceptual severance

views any conceptually distinct aspect of a person’s property as a separate strand within the bundle of rights—as property itself. Following this reasoning, the taking of a strand constitutes a compensable taking of property under the Fifth Amendment of the Constitution. Of course, this assertion is true only if one first accepts the view that any conceptually severable aspect of property is itself property in the constitutional sense.

Courtney C. Tedrowe, Note, *Conceptual Severance and Takings in the Federal Circuit*, 85 CORNELL L. REV. 586, 592–93 (2000). *Penn Central* rejected the notion of conceptual severance. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 130–31 (1978) (“‘Taking’ jurisprudence does not divide a single parcel into discrete segments and attempt to determine

Supreme Court has repeatedly limited *per se* takings cases to land.²⁹⁸ Indeed, Justice Scalia in *Lucas v. South Carolina*, the seminal case on *per se* takings, cited *Andrus* in support of a fundamental distinction between land and personal property: “[I]n the case of personal property, by reason of the State’s traditionally high degree of control over commercial dealings, [the owner] ought to be aware of the possibility that new regulation might even render his property economically worthless (at least if the property’s only economically productive use is sale . . .).”²⁹⁹ That same limitation, Scalia asserted, is not implied with land.³⁰⁰

There are “innumerable instances where regulations destroy all value and use of personal property.”³⁰¹ Many of these instances involve legislatively created prohibitions on the sale of previously legal and valuable goods,³⁰² while others involve government-authorized competition that

whether rights in a particular segment have been entirely abrogated. In deciding whether a particular governmental action has effected a taking, this Court focuses rather both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole . . .”).

²⁹⁸ See Sugameli, *supra* note 280, at 986 (stating that “Justice Scalia repeatedly limited *Lucas* ‘per se’ liability to cases involving land”).

²⁹⁹ *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1027–28 (1992). For a recap of the facts of *Lucas*, see *supra* note 35.

³⁰⁰ *Lucas*, 505 U.S. at 1028 (“In the case of land, however, we think the notion pressed by the Council that title is somehow held subject to the ‘implied limitation’ that the State may subsequently eliminate all economically valuable use is inconsistent with the historical compact recorded in the Takings Clause that has become part of our constitutional culture.”).

³⁰¹ See Sugameli, *supra* note 280, at 986 (suggesting that Justice Scalia’s support of a fundamental distinction between land and personal property was necessitated by the desire to establish a rule for land “that would be compatible with the innumerable instances where regulations destroy all value and use of personal property”).

³⁰² *Id.* See, e.g., *Burns Harbor Fish Co. v. Ralston*, 800 F. Supp. 722, 727 (1992) (rejecting a takings claim that challenged a state ban on the use of gill nets in the waters of Lake Michigan, and rejecting as “patently unreasonable” plaintiff’s “investment-backed expectations” that it could indefinitely fish using gill nets based on plaintiff’s prior purchase of a net and fishing license).

destroys a market, such as in Grand Central’s case.³⁰³ Consequently, when an individual or corporation “purchases personal property (as opposed to real property) to engage in a commercial venture,” the buyer assumes a risk that “government regulation will diminish the value of that property.”³⁰⁴ Investing in TDRs can be considered a gamble, similar to investing in stock.³⁰⁵ Once severed from the

³⁰³ An example of the latter includes the recent proliferation of app-based transportation services in New York City such as Uber and Lyft. New York City created and has long sustained an insulated transportation market for taxis by artificially restricting the number of cabs via a costly medallion system. Until recently, barriers to entry and stringent regulations have protected taxi drivers from competition. Today, however, the city permits app-based transportation services to compete in this market without subjecting them to the same regulations. Similarly, the city has created a TDR system to benefit landmark owners, yet proposes to institute bonus programs that will compete in and devalue the TDR market. For the rules to which medallion taxis are subject, see N.Y.C. TAXI & LIMOUSINE COMM’N, TAXI AND LIMOUSINE COMMISSION RULES AND LOCAL LAWS, ch 58, http://www.nyc.gov/html/tlc/downloads/pdf/rule_book_current_chapter_58.pdf [<http://perma.cc/4LB9-SXQC>].

³⁰⁴ Sugameli, *supra* note 280, at 987 (citing *Burns Harbor Fish Co.*, 800 F. Supp. at 726).

³⁰⁵ There are, of course, obvious differences between investing in air rights and investing in stocks. First, the risks associated with each type of investment differ. While real estate ownership incurs certain costs and taxes, “the values of physical assets are less likely to become worthless than stocks.” Additionally, “property owner[s] have more control over the value and use of [their] investment than the standard stockholder does. . . . Stocks are [also] more liquid assets than real estate.” *What are the Differences Between Investing in Real Estate and Stocks?*, INVESTOPEDIA, <http://www.investopedia.com/ask/answers/100214/what-are-differences-between-investing-real-estate-and-stocks.asp> [<http://perma.cc/X63F-C2JD>]. Investment expectations also differ. For example, investors who purchase air rights to sell them at a profit do so if the extant zoning regime promotes TDR trade. In contrast, stock investment is more speculative, as prices can be affected by factors such as investor knowledge, mergers, product performance, or investor game strategy. Yet air rights, like stocks, are not physical assets (in the same sense that real property is), and a gold standard does not underlie their value. “The trade of air [is] based on a speculative concept of its worth. As in any market, investors have an interest in increasing the value of [air rights], which can lead to speculation and the inflated value of these tradable claims to paper wealth.” Theo Games Petrohilos, *Air Futures*, URBAN OMNIBUS (Oct. 17,

underlying land, they become tradable goods whose value is subject to the market's ebb and flow.³⁰⁶ Although there has not been an express ruling on TDRs' status as real or personal property, courts may explore the real versus personal property distinction in analyzing whether TDR devaluation is indeed unconstitutional.

B. Policy Arguments in Favor of a Robust TDR Market

While it may be difficult to make a successful constitutional argument with respect to regulations that devalue TDRs, compelling policy arguments exist for cities to create incentives that support a robust TDR market. The problem with bonus and TDR programs competing with each other as a means for building in excess of the limits set by the zoning law³⁰⁷ is that, given the option, developers will always choose the bonus—even if the cost of providing the amenity is greater than the purchase price of the air rights. This is because the developer who elects the bonus system obtains not only the increased floor area, but also an amenity, such as direct subway access, that may attract tenants and their customers.³⁰⁸ Part of the developer's expenditure for increased area may thus be recouped in higher rent or occupancy.³⁰⁹

2012), <http://urbanomnibus.net/2012/10/air-futures/> [<http://perma.cc/23R5-AF9A>]. Essentially, the gamble is in air rights' speculative nature.

³⁰⁶ This, in turn, raises a question of baseline value. If Argent Ventures purchased the terminal's unused TDRs for \$61 per square foot, from what price should the diminution be measured: the original purchase price or the fair market value at the time of the zoning amendment's adoption?

³⁰⁷ See *Unconstitutionality of TDRs*, *supra* note 221, at 1112 n.57 ("A bonus system enables developers to increase the floor area ratio permitted on their lots by providing certain amenities. . . . Therefore, it competes with TDR as a means for building in excess of the limits set by the zoning law.").

³⁰⁸ *Id.*

³⁰⁹ *Id.*

Consequentially, when a bonus encroaches on a TDR market, TDR sales tend to decline.³¹⁰ Holders of unused air rights may therefore be incentivized to immediately offload their unused air rights. Their willingness to hold out for a suitable buyer is thus affected by the stability of the TDR regime. In a stagnant regime with no likelihood of revival, sellers who prefer to reduce their risk and increase liquidity will likely sell their TDRs to the first willing buyer. The result of this accelerated market dynamic is that development will not occur at an optimal time, but prematurely.³¹¹ The lack of timing controls on development could then adversely affect the urban landscape.³¹² If a

³¹⁰ See MARGARET WALLS & VIRGINIA MCCONNELL, RESOURCES FOR THE FUTURE, TRANSFER OF DEVELOPMENT RIGHTS IN U.S. COMMUNITIES: EVALUATING PROGRAM DESIGN, IMPLEMENTATION, AND OUTCOMES 18 (2007), http://www.rff.org/files/sharepoint/WorkImages/Download/Walls_McConnell_Sep_07_TDR_Report.pdf [<http://perma.cc/8R44-T7GM>] (asserting that “[t]he underlying zoning in both the sending and the receiving areas [of a city] . . . will influence how well a TDR program works”) “[S]ome communities with TDR programs allow additional density if the developer connects to public water and sewer, includes affordable housing units, submits a ‘planned unit development’ proposal, or devotes a certain percentage of the land to open space. Such possibilities tend to dampen the demand for TDRs.” *Id.* at 26.

³¹¹ “The orderly pacing and placing of development has been a consistent aspiration and source of frustration for American land use regulatory systems.” Donald M. Carmichael, *Transferable Development Rights as a Basis for Land Use Control*, 2 FLA. ST. U. L. REV. 35, 41 (1974). Planning usually

seeks to further broad policies for long-range patterns of development. Emphasis is consistently on the placing and pacing of development over time Between the constitutional scheme and the planning scheme, . . . the tensions [are] inevitable . . . [and have] been manifested in the form of sprawling, leapfrogging, premature, ill-coordinated development, despite efforts at regulation.

Id. at 39.

³¹² For example, when multiple commercial building projects occur simultaneously, the demand on utilities and mass transit increases. See JAMES A. KUSHNER, 1 SUBDIVISION LAW AND GROWTH MANAGEMENT § 2:18 (2d ed. 2011) (explaining that time controls on land use assure the adequacy of infrastructure to accommodate development). “Timed

municipality regards the ability to direct time controls that stimulate optimal development as socially useful, it should promote an active TDR exchange.³¹³ This can be achieved by fostering a regulatory environment that facilitates the capacity of intermediaries like Argent Ventures to purchase and bank TDRs.

1. Solutions that Support a TDR Market: Complementary Bonus and TDR Systems

One method by which a municipality may support an active TDR market while obtaining free infrastructure through a bonus is to design the bonus and TDR systems to complement each other. The problem inherent in the conflict between bonus and TDR systems is that they operate independently from each other.³¹⁴ The Vanderbilt Corridor bonus and Argent's TDRs, for example, represent binary, mutually exclusive options for developers looking to increase their project's floor area. Yet the market is not truly competitive, as the city sets the market price and is not subject to the complex TDR transfer procedures that are landmarks.³¹⁵ Despite this disparity, however, it is possible for a city to design bonus programs that reduce the degree to which the bonus conflicts with the TDR system.

Tacoma, Washington serves as an example of a municipality that has experienced some measure of success

sequential zoning in mapping districts for development according to the timed availability of services and facilities to accommodate development, is conceptually simple, and is likely to result in the appearance of a well-planned community designed to grow in certain directions at certain times." *Id.* See LOREN LUTZENHISER & NICOLE WOOLSEY BIGGART, MARKET STRUCTURE AND ENERGY EFFICIENCY: THE CASE OF NEW COMMERCIAL BUILDINGS vi, http://www.uc-ciee.org/downloads/market_struc.pdf [<http://perma.cc/9JLD-62P6>] (describing commercial office building markets as dynamic and reflecting local building markets and economies).

³¹³ An active market has the advantage of spurring collateral investment in the city. See generally Finn, *supra* note 38.

³¹⁴ *Unconstitutionality of TDRs*, *supra* note 221, at 1112 n.57.

³¹⁵ For a detailed description of landmarks' costly and lengthy TDR transfer procedure, see *supra* notes 80–81.

in designing complementary TDR and bonus systems.³¹⁶ City planning officials in Tacoma recognized that developers have little incentive to include TDRs in acquiring additional floor area as opposed to constructing amenities that directly benefit their project.³¹⁷ The city's planning strategy attempts to eliminate this deterrent in two critical ways.

First, when Tacoma implements a bonus program in a specific neighborhood, it does not increase the maximum permitted building height in the affected area.³¹⁸ For example, the Vanderbilt Corridor bonus increases the maximum building height permitted in the Grand Central Subdistrict from 21.6 to 30 FAR.³¹⁹ If developers wish to achieve this new maximum density, they will require many more air rights than they would have otherwise needed to reach the previous maximum. Air rights holders lose in this scenario³²⁰ because they possess a finite amount of TDRs to

³¹⁶ The city was nominated for a planning award for integrating these two systems. At the time of this writing, no other municipality in the United States had attempted to do so, likely because few urban areas even utilize TDRs. See TACOMA TRANSFER OF DEVELOPMENT RIGHTS PROGRAM MARKET STUDY, 2013 APA Washington Award Submittal, i (May 30, 2013) (noting that Tacoma's TDR program integration into the incentive zoning system is a "unique" and "new innovation").

³¹⁷ *Id.* at 5 ("An innovative solution for Tacoma's TDR program was required to include TDR into the city's incentive zoning menu. Incentive zoning menus are typically designed to provide infrastructure and amenities that serve the project and its surrounding neighborhood, but TDR programs conserve land that may not be near the project, so the question arose as to why would a developer include TDRs rather than other amenities that directly benefit the project?").

³¹⁸ *Id.* at i.

³¹⁹ See *supra* note 87 and accompanying text.

³²⁰ See Curtis J. Berger, *The Accommodation Power in Land Use Controversies: A Reply to Professor Costonis*, 76 COLUM. L. REV. 799, 806 (1976) ("At the superstructure level [in which the basic FAR is exceeded] . . . transfer rights [purchased from holders of unused air rights] would begin to hold value only if they were the sole means for breaching the basic FAR. . . . [I]n most urban centers . . . the codes stand replete with zoning bonuses: builders may go beyond the basic FAR—sometimes well beyond it—by agreeing to provide prescribed amenities ranging from plazas and wider set-backs to shopping arcades and theatres. Thus the transfer rights would be worthwhile to the builder, that is, he would be

sell, while the city may print an unlimited amount of square footage. It is in the developer's interest to minimize transaction costs by purchasing TDRs from one seller—the city—as opposed to purchasing TDRs from both the city and a landmark. By creating bonuses that do not increase the maximum permitted building density, Tacoma obviates developers' need to transact with a source that can produce an unlimited amount of air rights.

Second, Tacoma expends more effort to compensate landowners than does New York City's TDR program by allowing inter-jurisdictional transfer from in-city to county areas,³²¹ thereby enhancing the overall transferability of TDRs.³²² If New York City permitted holders of unused air rights to sell those rights to buyers in neighboring transfer districts or boroughs, this would avoid the lock-in effect that ties up sellers' capital and prevents financial resources from moving to their most productive use.³²³ While integrative

willing to pay something for them, only if they let him build *more efficiently* than do the existing bonuses. Yet the efficiency route for transfer rights collides with the zoning code's urban design goals.”).

³²¹ TACOMA TRANSFER OF DEVELOPMENT RIGHTS PROGRAM MARKET STUDY, *supra* note 316, at 6 (“[T]he dual local/regional nature of the program permits it to dynamically interact with the regional program or operate exclusively within the city. This is a useful example that is relevant to other local municipalities struggling with the question of why they should accept development rights from outside jurisdictions. Tacoma’s TDR program is unbiased to where the sending-area development rights originate.”).

³²² *Id.* at 2 (“The program is one of only a few that is designed for functionality both as a city-based program and an interjurisdictional program.”). See Costonis, *Chicago Plan*, *supra* note 47, at 598 (contending that a plan that permits transfers throughout development rights transfer districts “prevent[s] urban design abuse through proper planning controls and facilitate[s] the marketability of development rights by freeing them of onerous restrictions”); Berger, *supra* note 320, at 806 (“To make the transfer right more valuable to the builder than the bonus right would be, the city must relax design restrictions on the transfer right.”).

³²³ Property scholar, John Costonis, has suggested locating transfer districts—whenever possible—in transition areas, i.e., neighborhoods moving to higher densities as a result of market forces or local planning. For a description of this strategy and criticisms of it, see Berger, *supra* note 320, at 809.

planning is certainly not constitutionally required, cities may find that such an approach simultaneously fulfills the two goals of preserving historic buildings³²⁴ and creating needed infrastructure.

2. Solutions that Support a TDR Market: TDR Banks

A second method by which a municipality may support a TDR market in conjunction with a zoning bonus is by establishing a municipal TDR bank. Should a landmark owner decide to sell her unused air rights in the market—perhaps if she requires immediate access to capital—the city could step in and institute a condemnation action for the landmark’s air rights.³²⁵ The owner would receive instant cash from the city in exchange for her air rights—just compensation for a true taking—to be placed in this bank, from which other enterprises may purchase air rights to use on their own land.³²⁶ The city would then sell

³²⁴ See *Unconstitutionality of TDRs*, *supra* note 221, at 1101 (explaining that TDR systems “have been widely acclaimed by many planners, government officials and lawyers as a panacea which will enable municipalities to finance the preservation of landmarks and open spaces”); Costonis, *Chicago Plan*, *supra* note 47, at 584–85 (contending that a healthy TDR system is important to finance the preservation of landmarks and open spaces and that “New York City’s effort to redistribute [preservation] costs through development rights transfers constitutes a giant step in this direction”).

³²⁵ For an in-depth discussion on the functioning of development rights banks and a comparison of the TDR schemes of Chicago (which uses such banks) and New York City, see generally Costonis, *Chicago Plan*, *supra* note 47.

³²⁶ In this procedure,

[c]ondemned development rights are credited to the municipal bank in an amount strictly calculated to reimburse the city for its condemnation costs. Besides, since developers will be expected to bid for the development rights on the open market, the value of these rights will be returned to the city in the form of cash payments from these developers.

Id. at 605.

these pooled rights to developers to recoup condemnation costs³²⁷ and finance infrastructure.

A market that “adequately reflects the value of the condemned rights” must exist in order for the city to recoup its condemnation costs.³²⁸ The bank must act, “as do[es] [a] stock exchange specialist . . . , to maintain [the] market any time the balance goes awry.”³²⁹ Whether a bank could sustain a TDR market in a recession is questionable, however, as sellers would greatly outnumber buyers.³³⁰ Additional risks posed by a city-administered bank include potential claims related to antitrust liability, lack of just compensation for “taking” property, and spot zoning.³³¹ A local government may also stand to reduce the local tax base by serving as an intermediary in TDR transactions, as “the TDRs hang in limbo, are not assignable to any private party, and are not taxable.”³³² Yet New York City has operated TDR banks in a limited number of transfer districts to some success,³³³ with the South Street Seaport TDR bank even finding the purchase and sale of TDRs to be profitable.³³⁴

³²⁷ See *id.* at 590–91.

³²⁸ *Unconstitutionality of TDRs*, *supra* note 221, at 1113.

³²⁹ Berger, *supra* note 320, at 805. Factors that would shape the TDR market include: “the number of [structures that retain unused development rights]; the size and location of the transferee districts; the present zoning; and the underlying demand for new construction.” *Id.*

³³⁰ *Id.* at 806.

³³¹ For a more detailed explanation of these issues, see Norman Marcus, *Transferable Development Rights: A Current Appraisal*, PROB. & PROP., Mar.-Apr. 1987, at 40, 41–42.

³³² Sarah J. Stevenson, *Banking on TDRs: The Government’s Role as Banker of Transferable Development Rights*, 73 N.Y.U. L. REV. 1329, 1372 (1998).

³³³ The South Street Seaport TDR Bank, for example, has instituted a number of transfers: 175 Water Street utilized 142,868 square feet to increase its coverage from 40 to 80 percent of its zoning lot, and another 143,132 square feet for additional improvements, while One Seaport Plaza purchased 275,000 square feet. However, this particular middleman bank was not New York City but a consortium of banks that held the original mortgages on the landmarked properties. Though the city operated the bank, private commercial entities funded it. “Municipal resources are typically not available to purchase and store development rights [on a

Despite the aforementioned potential shortcomings, government-operated TDR banks could resolve valuation and marketability problems by “setting minimum purchase prices, guaranteeing loans that use TDRs as collateral, and purchasing the TDRs outright.”³³⁵ “A TDR bank may also act as a clearinghouse and an information source, helping to match buyers with sellers and assisting with transactions.”³³⁶ But perhaps most importantly, TDR banks could alleviate unfair burdens placed on a single property owner³³⁷ by giving property owners the choice of whether to remain in a volatile TDR market.

V. CONCLUSION

Although bonuses are widely implemented to create public amenities,³³⁸ they often operate to the detriment of neighboring landowners who hold unused air rights.³³⁹ However, a zoning amendment that devalues landowners’ unused air rights will generally not implicate a regulatory taking unless it is intentionally directed to injure a particular landowner³⁴⁰ or completely deprives an owner of

large scale.]” Richards, *supra* note 181, at 464–65, 475 n.142 (citing Marcus, *supra* note 37, at 903).

³³⁴ Stevenson, *supra* note 332, at 1372.

³³⁵ *Id.* at 1331–32.

³³⁶ *Id.* at 1332.

³³⁷ See *Fred F. French Investing Co. v. City of New York*, 350 N.E.2d 381, 388 (N.Y. 1976) (suggesting that a scheme such as a TDR bank would prevent scenarios in which property is regulated unconstitutionally as, “[i]nsofar as the owner of the granting parcel is concerned, his development rights are taken by the State, straightforwardly, and he is paid just compensation for them in eminent domain”).

³³⁸ See N.Y.C., N.Y., ZONING RESOLUTION, §§ 23-90 and 81-23 (2015) (provisions on the housing and public plaza space bonuses).

³³⁹ See *supra* Part IV & note 8 (explaining the tension and conflict inherent between TDR and bonus systems).

³⁴⁰ See *Fred French*, 350 N.E.2d at 386, 388 (holding that “[a] zoning ordinance is unreasonable, under traditional police power and due process analysis, if it encroaches on the exercise of private property rights without substantial relation to a legitimate governmental purpose” and that

its TDRs rather than merely reduce demand in the neighborhood TDR market.³⁴¹ The key for any holder of unused air rights, then, may be to argue that the zoning amendment interfered with its primary expectation concerning the use of the parcel³⁴² (i.e., selling the amassed air rights for profit)—a factor that must be weighed in any taking analysis in accordance with the other *Penn Central* factors.³⁴³ The correct framework for analyzing the next generation of TDR cases should consider how zoning amendments compare to those in the two extant cases on the diminution in value of TDRs,³⁴⁴ and give weight to the reasonableness of the landowner's investment-backed expectations.³⁴⁵

As case law continues to develop in this emerging niche, parties on both sides should consider the constitutional and policy arguments that both undermine and support protecting TDR markets. Cities may find that implementing integrative planning solutions or establishing TDR banks fulfills the goal of preserving historic buildings and creating needed infrastructure, while equitably compensating investors and stimulating reinvestment in commercial areas.

limitations on development create “floating development rights” that have uncertain or contingent market value and are “utterly unusable”).

³⁴¹ See *Sierra Nevada SW Enter. v. Douglas County*, 506 F. App'x 663, 665 (9th Cir. 2013) (holding that no taking occurs when plaintiffs do not allege that they were deprived of their TDRs, and that no taking occurs when a zoning amendment diminishes the value of unused TDRs by reducing demand in the TDR market as a whole).

³⁴² *Penn Central* upheld the law because it “[did] not interfere with what must be regarded as Penn Central's *primary expectation* concerning the use of the parcel.” *Penn Centr. Transp. Co. v. City of New York*, 438 U.S. 104, 136 (1978) (emphasis added).

³⁴³ The three *Penn Central* factors must be weighed and balanced in any partial takings analysis. See *Tahoe-Sierra Pres. Council v. Tahoe Reg'l Planning Agency*, 535 U.S. 302 (2002).

³⁴⁴ See *supra* Part III.A for a discussion of *Fred French* and *Sierra Nevada*.

³⁴⁵ For a discussion of the significance of investment-backed expectations, see *supra* Part III.B.