CONDEMNATION AND TAX CERTIORARI

Will City's Requirement to Build Affordable Housing Effect a Taking?

By Michael Rikon

New York City Mayor Bill de Blasio has pledged to create or preserve 200,000 affordable units of housing in the next decade. Among the several proposals being considered, one idea is to amend a controversial real estate tax abatement available under section 421-a of the Rent Act of 2011. The abatement gives developers a property tax break, in decreasing amounts, over a 25-year period. In certain neighborhoods in the city, developers must set aside a percentage of units that are affordable. But in other parts of the city, there is no such requirement. The statutory authority for abatement expires this spring.

While there is no question that the tax abatement has added affordable units to the city, The New York Times on Feb. 2, 2015, reported the record-making sale of a penthouse which sold for $100.5 million. Because of a 421-a tax abatement, the real property tax bill was cut, initially, by 95 percent, or an estimated $360,000. According to the article, about 150,000 apartments got the 421-a tax exemption in fiscal year 2013, but only 12,748 were earmarked for low- and moderate-income tenants. (Charles V. Bagli, "In Program to Spur Affordable Housing, $100 Million Penthouse Gets 95% Tax Cut")

Since this is a voluntary program, it seems clear that any change in the required number of units or expansion of the geographic applicability will not represent a taking under the Fifth Amendment of the U.S. Constitution.

What we are concerned with is the proposal now being considered to amend zoning provisions to encourage affordable set-asides in new residential construction.

As it stands, in New York City there are presently inclusionary housing programs which require a percentage of units within a building to be affordable. All affordable residential units created through the inclusionary housing program must remain permanently affordable. They can be rental or ownership.

In the Special Hudson Yards District, the Special West Chelsea District and in designated areas mapped on First Avenue between East 35th and East 41st Streets in Manhattan, and along the Greenpoint-Williamsburg waterfront in Brooklyn, a percentage of units may be set aside for moderate- or middle-income households if a greater percentage of affordable units is provided. All bonus floor area must be accommodated within the height and setback provisions of the underlying zoning district.

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The power of the state over private property extends from the regulation of its use under the police power to the actual taking of all or part of the fee of the real estate under the eminent domain power. When the state "takes," that is appropriates, private property for public use, just compensation must be paid. In contrast, when there is only regulation of the uses of private property, no compensation need be paid. But, a purported "regulation" may impose so onerous a burden on the property regulated that it has, in effect, deprived the owner of the reasonable income productive or other private use of one's property and thus has destroyed its economic value. In all but exceptional cases, nevertheless, such a regulation does not constitute a "taking," and is therefore not compensable, but amounts to a deprivation or frustration of property rights without due process of law and is therefore invalid. *Fred F. French Investing Co. v. City of New York*.[1]

Said another way, 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.

Regulations and Exactions

There are quite a few examples of regulatory takings. In *Manocherian v. Lenox Hill Hospital*[2] the Court of Appeals struck down legislation that required the owners of rental property to offer renewal leases to a hospital for apartments occupied by some of the hospital's employees. The court held that the legislation suffered a fatal defect by not substantially advancing a closely and legitimately connected state interest. The Manocherian court relied on its prior decision in *Seawall Associates v. City of New York*.[3]

Seawall held that a local law that prohibited the demolition or alteration of single-room occupancy properties was a regulatory taking. Significantly, the court noted that there is no "set formula" for determining in all cases when an adjustment of rights has reached the point when "justice and fairness" require that compensation be paid. It also stated that the local law does not pass the other threshold test for constitutional validity of regulatory takings: that the burdens imposed substantially advance legitimate state interests.

In considering whether a regulation of land constitutes a taking of property requiring just compensation, an analysis is usually made in accordance with *Penn Central Transportation Co. v. New York City*.[4] The Penn Central factors include the economic impact on the property owner, the extent to which the regulation has interfered with distinct investment-backed expectations, and the character of the governmental action.

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As the Supreme Court made clear in a case subsequent to *Penn Central*, the focus of the inquiry is the severing of the burden of the regulation on the property owner. *Lingle v. Chevron USA.*[5] The Supreme Court has found two situations that do not require the Penn Central takings analysis: a permanent physical invasion in *Loretto v. Teleprompter Manhattan CATV*[6] and a regulatory taking that is a per se taking because it deprives an owner of all economic viable use of its property in *Lucas v. South Carolina Coastal Council.*[7] I would also suggest that the Appellate Division, Second Department, has held that wetlands constitute a per se taking since the wetlands regulations effectively prevent any economic beneficial use of the property. *Matter of City of New York (Paolella).*[8]

It is the zoning regulation that conditions development on exactions, like requiring construction of a definite percentage of affordable housing which run the risk of being an impermissible exaction. In *Nollan v. California Coastal Commission*[9] a requirement that property owners provide an easement to the public as a condition to demolish and rebuild their home was struck down as an unconstitutional exaction. The court held that the easement did not share an "essential nexus" with the goal the state Coastal Commission could have advanced by just denying the permission.

Another Supreme Court decision, *Dolan v. City of Tigard*,[10] added to the "essential nexus" issue by requiring that the conditioned-upon-development permission be "roughly proportional" to the harm that would be caused by just granting a permit.

Finally, in the area of "exactions," the Supreme Court decided *Koontz v. St. Johns River Water Management Dist.*[11] *Koontz* dealt with an application by an owner of wetlands who applied for a permit to develop a parcel of regulated land. But the Water Management District demanded more than it usually required in mitigation to his land, or alternatively, that there be mitigation on land that Coy Koontz did not actually own by payment of money. This was objected to as an unlawful "exaction." The Supreme Court held that by conditioning development approval on the "exaction" of property, "the government can pressure an owner into voluntarily giving up property for which the Fifth Amendment would otherwise require just compensation."[12]

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Other States

Inclusionary zoning has been utilized successfully in other states. In *Home Builders Ass'n v. City of Napa*[13] the California Court of Appeal upheld an ordinance that mandated a requirement that 10 percent of all newly constructed units be "affordable." A developer had two alternatives—first, developers of single-family units may, at their option, satisfy the inclusionary requirement by an alternative equivalent proposal such as a dedication of land, or construction of affordable units on another site. As a second alternative, a developer may choose to satisfy the inclusionary requirement by paying an in-lieu-fee. The fee was to be deposited in a housing trust fund to be used for affordable housing.

The ordinance was challenged as violating the taking clauses of the federal and state constitutions. The court upheld the inclusionary zoning noting that creating affordable housing for low- and moderate-income families is a legitimate state interest. It also held that the zoning ordinance would substantially advance the important governmental interest of affordable housing.

The court further rejected plaintiff's argument that its due process rights were violated because there was no mechanism to make a fair return if the owners were forced to sell, or rent, at an amount unrelated to market prices. But the court held that the developer had another option such as donating vacant land or paying an in-lieu-fee. There also was a waiver clause in the ordinance which allowed the city to reduce, modify or waive the requirements.

So as against this background, where does the mayor's inclusionary zoning programs leave us? Clearly if it is voluntary with the motivation of additional density, there will be no constitutional barrier. But making inclusionary zoning mandatory may present a problem. If a zoning change is used as an incentive to further growth and development, it probably will have no difficulty in obtaining judicial approval—especially since, as a legislative act, it will enjoy a strong presumption of constitutionality. But, if the mandatory inclusionary zoning is made part of and reduces existing rights of development, there may be successful challenges.

1. 39 NY2d 587, 593-594 (1976), rearg. den. 40 NY2d 846 (1976), cert. den. 429 US 990 (1976).
2. 84 NY2d 385 (1994).
3. 74 NY2d 92 (1989).
4. 438 US 104 (1978).
5. 544 US 528 (2005).
6. 458 US 419 (1982).
7. 505 US 1003 (1992).
8. 122 AD3d 859 (2014).
9. 483 US 825 (1987).
10. 512 US 374 (1994).
11. 133 S. Ct. 2586 (2013).
12. *Koontz*, 133 S. Ct. at 2594.
13. 90 Cal. App. 4th 188 (1st App. Dist. 2000), rev. den. 2001 Cal. LEXIS 6166, cert. den. 535 US 954 (2002).