To Be Argued By:
CHETAN A. PATIL

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New York Supreme Court

APPELLATE DIVISION—FIRST DEPARTMENT

STAHL YORK AVENUE CO., LLC,

Plaintiff-Petitioner-Appellant,

—against—

THE CITY OF NEW YORK; THE NEW YORK CITY LANDMARKS PRESERVATION COMMISSION; MEENAKSHI SRINIVASAN, in her capacity as Chair of the New York City Landmarks Preservation Commission,

Defendants-Respondents-Respondents.

BRIEF FOR PLAINTIFF-PETITIONER-APPELLANT

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes, Rules, and Other Authorities

INTRODUCTION

In the 1970s, Appellant Stahl York Avenue Co., LLC purchased 15 tenement-style apartment buildings that had been built in the early twentieth century. The buildings are all on the same city block. In 1990, the City of New York designated 13 of the 15 buildings as a landmark. Stahl agreed not to challenge that designation because the City agreed to permit Stahl to redevelop the remaining two buildings. Stahl intended eventually to demolish and replace them with modern apartment buildings.

For 16 years, Stahl relied on the City's promise to permit redevelopment of those two buildings and managed them with redevelopment in mind. But in 2006, when Stahl began to implement its redevelopment plan, the City abruptly reneged on the compromise and landmarked the two buildings. This change of heart was not a sincere effort to protect historically or architecturally significant buildings. It was a direct response to community pressure, taken precisely at the moment Stahl began to implement the development plan the City itself had authorized over a decade earlier.

The landmark designation rendered the two buildings commercially unviable. They are antiquated, tenement-style apartment buildings with apartment units averaging 370 leasable square feet. Some units cannot even accommodate a queen-sized bed. In their current state, the buildings are unprofitable. It would be

so costly to renovate them that doing so is not an economically viable proposition. On the other hand, if unencumbered by the landmark designation, the estimated value of the buildings is approximately $200 million. The landmark designation effectively destroyed the value of the properties.

As a result, Stahl sought relief through an administrative "hardship" proceeding under the Landmarks Law, which permits a property owner to demolish a landmarked building if it is incapable of earning a reasonable return of at least 6% of the property's assessed value. Even though the evidence proved that Stahl could not earn anything close to a 6% return, the City's Landmarks Preservation Commission ("LPC") denied the hardship application based on a jerry-rigged analysis crafted to ensure that there could be no finding of hardship regardless of what the evidence showed.

Stahl filed this suit to challenge the deprivation of its rights to redevelop its property. In its Complaint, Stahl alleged that the 2006 landmark designation of the buildings was a taking of its property without just compensation and that the denial of its hardship application was arbitrary and capricious under Article 78 of the CPLR. The City moved to dismiss the takings claim and opposed the Article 78 petition. The lower court ruled in the City's favor on both claims.

That ruling rested on a series of fundamental legal errors and should be reversed.

First, the lower court improperly granted the City's motion to dismiss the takings claim even though there were disputed factual issues. These types of takings claims are adjudicated under a fact-intensive balancing test. The Complaint plainly alleged that the 2006 landmark designation destroyed virtually all of the economic value of the buildings and interfered with Stahl's development expectations—expectations that had been substantially shaped by the City's 1990 decision to preserve Stahl's rights to develop the buildings. This was plainly enough to state a claim for a Takings Clause violation.

The lower court ignored these allegations. Instead of assuming their truth, as it was required to do on a motion to dismiss, the court resolved every factual issue in the City's favor. The court did not even devote a separate analysis to the takings issue, and believed that it could simply defer to the LPC's determination of Stahl's hardship application in rejecting the takings claim. By doing so, the lower court for all intents and purposes permitted the LPC to determine the constitutionality of its own actions, without affording Stahl even the most basic process of a judicial proceeding.

Second, the lower court erroneously dismissed the challenge to the LPC's arbitrary and capricious denial of Stahl's application. The LPC made three critical errors. First, it disregarded the plain language of the Landmarks Law by assessing hardship based on the economics of the entire 15-building complex, even though

Stahl only sought hardship relief for the two recently landmarked buildings, which sit on a single tax lot. Second, it found that the buildings could be profitable, and thus Stahl would suffer no hardship, based on post-renovation income—but failed to account for the substantial offsetting renovation costs that would make the renovations unprofitable. Finally, the LPC claimed that certain of these costs were "self-imposed"—a claim that was false and ignored that Stahl would have incurred the renovation costs under any circumstance.

The decision below should be reversed. This Court should grant Stahl's Article 78 petition and reinstate Stahl's takings claim.

QUESTIONS PRESENTED

1. May a court decide contested factual issues in adjudicating a motion to dismiss a takings claim?

The lower court answered yes.

2. May a court defer to an agency concerning the agency's own alleged constitutional violations?

The lower court answered yes.

3. Is a plaintiff asserting that an administrative agency has violated its constitutional rights entitled to present evidence in a judicial forum to adjudicate its claims?

The lower court answered no.

4. Is it arbitrary and capricious for an administrative agency to deny an application based on an internally inconsistent analysis that ignores the pertinent statutory language, disregards administrative precedent, and is incompatible with the purposes of the operating statute?

The lower court answered no.

STATEMENT OF FACTS

A. The Parties

Appellant Stahl York Avenue Co., LLC ("Stahl") is a corporation that has engaged in the real estate development business in New York City for decades, including the provision of apartment housing to New York City residents at affordable rates. Stahl owns the landmarked Buildings that are the focus of this appeal.

Respondent the LPC is an administrative agency in the New York City government. The LPC is authorized to establish and regulate landmarks in New York City pursuant to the New York City Landmarks Law, N.Y.C. Admin. Code § 25-301, *et seq.* Respondent Meenakshi Srinivasan is the current Chair and a Commissioner of the LPC. Respondent the City of New York is a municipal corporation organized under the laws of the State of New York. This brief refers to the Respondents collectively as "the City."

B. The Buildings

The Buildings at issue in this case are two architecturally insignificant six-story walk-up apartment buildings located at 429 East 64th Street and 430 East 65th Street in Manhattan. (A76, ¶ 20). The Buildings sit on a single tax lot on the eastern edge of the block bounded by East 64th Street, East 65th Street, First Avenue, and York Avenue. (A76-77, ¶ 21). The remainder of the block is occupied by 13 other buildings that Stahl also owns and that are also designated as landmarks (the "Other Buildings"). (*Id.*). Collectively, the buildings on the block are referred to as the First Avenue Estate ("FAE"). (*Id.*). Stahl acquired the FAE in 1977 (along with an unrelated building nearby) for the aggregate price of $5,725,000, with the intention of redeveloping the FAE. (A77, ¶ 22).

The Buildings contain 190 obsolete, warren-like apartments that are in many ways unfit for modern living. (A77, ¶ 23). Because they were designed in the early 1900s as tenement housing, they fall far below modern standards of quality. (*Id.*). They lack modern amenities, appliances and fixtures, and they are extremely small, averaging 370 leasable square feet per apartment. (*E.g.*, A394-96; A436). Many have inconvenient layouts, which make them incompatible with the needs of modern tenants, including bedrooms that cannot fit queen-sized beds and abnormally-shaped bathrooms that cannot accommodate ordinary fixtures. (*E.g.*, A996; A395-96).

The Buildings themselves are also outdated. They comply with all applicable legal requirements, but contain obsolete electrical, mechanical, and ventilation systems as compared to modern structures—deficiencies that have been exacerbated by age—and neither is handicap accessible. (*E.g.*, A463-65; A598-99; A77, ¶ 24). They are also the least attractive of the buildings of the FAE, as they are smaller in size, farther from subway lines and the amenities of First Avenue, and less safe because they can only be accessed through an interior courtyard invisible from the street. (A823-24; A991-93; A996-97; A910-11).

The apartments' substandard condition and design severely limit their marketability. (A77, ¶ 25). And because the apartments are small and the Buildings lack elevators, they appeal to a limited demographic, further restricting the rent Stahl can charge. (*Id.*). Many of the apartments are currently vacant, and cannot legally be rented in their current condition. (A78, ¶ 26). These vacant apartments need substantial and costly renovations to electrical systems and plumbing fixtures, repair or replacement of appliances, and abatement of lead paint in order to be legally habitable. (A511-12; A1043-44).

C. The 1990 Landmark Designation Excluded The Buildings

In 1990, the City designated the Other Buildings of the FAE as a landmark, but left the Buildings unencumbered by the designation. (A316). The FAE was constructed by the City and Suburban Home Company ("CSHC"), a now-defunct

corporation that was dedicated to solving "the housing problems of the nation's working poor." (A119; A126; A134). CSHC was known for developing "model tenement[]" projects throughout the nation, and in particular, for its "light-court" tenement style buildings, in which courtyards, apartments, and common areas were designed to maximize light and air. (A119-20). The buildings of the FAE are examples of this style.

The Other Buildings of the FAE were constructed in 1906 and, as such, are the oldest surviving example of CSHC's model tenement projects. (A172 & n.11). They were built on a single plot of land purchased by CSHC in 1896 and were designed by the renowned architect James Ware. (A172-73; A176). That plot of land did not include the entire city block, and accordingly, the Other Buildings were not designed or constructed as a full city-block development. (A173-74).

CSHC only purchased the rest of the block—the land on which the Buildings sit—from a different seller in 1913, seven years after it had completed the Other Buildings and 18 years after it bought the plot of land for the Other Buildings. (A173). The Buildings were designed by an undistinguished architect employed by CSHC, Philip Ohm, and were only completed in 1915. (A172; A176-77). Ohm also designed a nearby complex of light-court tenement buildings located on the Upper East Side of Manhattan, called the York Avenue Estates

("YAE"). (A173; A175). Unlike the FAE, the YAE was designed from the outset as a full-block complex. (*Id.*).

On April 24, 1990, the LPC voted to designate both the FAE and YAE as landmarks. (A142-43). Its formal designation report largely ignored the Buildings and focused instead on the historical and architectural aspects of the Other Buildings. (A129-34). It identified two reasons for including the Buildings: the "visual homogeneity" between the buildings of the FAE and the fact that the FAE comprised a full city block of light-court model tenement buildings. (A143).

At that time, the New York City Board of Estimate ("BOE") had authority to review landmark designations. The BOE recognized that designating all 15 buildings of the FAE would preclude development on a "very large site[]." (A201, ¶ 9). In order to "allow for [as-of-right] development in the future" on the site, it carved the Buildings out of the landmark designation. (*Id.*). The BOE's decision made practical sense, and tracked the historical and architectural distinctions between the Buildings and the rest of the FAE.

Neither Stahl nor the City ever contested the BOE's decision. (A80, ¶ 35). Stahl never challenged the designation of the Other Buildings because the BOE had preserved Stahl's rights to develop the Buildings (and the City had acquiesced to it), and because Stahl retained the option to transfer unused development rights from the Other Buildings to the Buildings. (*Id.*).

However, various community groups filed Article 78 petitions challenging the BOE's modification of the designation of the FAE and its modification of the designation of the YAE. (*See* A316-17). The City opposed the petitions. (*See* A318). The New York Supreme Court rejected the challenge, holding that "the compromise by the BOE was itself inherently reasonable," protecting Stahl's development rights while still protecting most of the FAE buildings, which were "significant not for their architectural merits, but the historical significance of housing created for the working poor." (A321).

The community groups did not appeal the decision as to the FAE, and the BOE's modification became final. (A80, ¶ 35). However, community groups appealed the decision as to the YAE, and this Court reinstated the LPC's designation of that property. *See 400 E. 64/65th St. Block Ass'n v. City of New York*, 183 A.D.2d 531 (1st Dep't 1992) ("*Kalikow*").

D. Stahl Began To Work On Developing The Buildings

After the BOE's decision, the City's acceptance of it, and the Supreme Court's ruling, Stahl reasonably understood that it retained its rights to develop the Buildings. (A80, ¶ 36). It operated them accordingly for 16 years. (*Id.*).

Most significantly, as early as 2000, Stahl began leaving apartments in the Buildings unleased as they became vacant. (A81, ¶ 38). In order to demolish and redevelop the Buildings, Stahl needed them to be vacant. (*Id.*). However, many of

the apartments in the Buildings were subject to rent-control and rent-stabilization restrictions, which restricted Stahl's ability to vacate those apartments when it was ready for redevelopment. (*Id.*). The apartments that came vacant also required costly renovations just to bring them up to a legally habitable level, making it economically infeasible to rent them in the interim. (*Id.*). In order to ensure that it could redevelop the Buildings at the appropriate time and to avoid spending millions renovating apartments slated to be demolished, Stahl left apartments unleased when they came vacant. (*Id.*). For the same reason, Stahl did not undertake any capital improvements in the Buildings, save for those necessary under the law. (A81, ¶ 39).

In addition, beginning in 2004, Stahl ramped up its efforts, preparing a redevelopment plan that involved demolishing the Buildings and constructing a modern condominium tower. (A81, ¶ 37). Stahl retained professionals, including attorneys and an architectural firm, to design the redevelopment plan, and it devoted personnel and internal resources to the project. (*Id.*).

E. The LPC Re-Landmarked The Buildings To Block Development

Once Stahl apprised the Community Board representing the Upper East Side of its redevelopment plans, however, the LPC geared up to block those plans. (A81, ¶ 40). The LPC announced that it had calendared a public hearing to revisit the long-decided landmark status of the Buildings. (A81-82, ¶¶ 40, 42). The

Landmarks Law prohibits the LPC from considering zoning issues like population density, access to open spaces, or the height of buildings in assessing whether to designate a property as a landmark. N.Y.C. Admin. Code § 25-304(a). Despite this prohibition, the LPC's hearing was dominated by these zoning concerns, as influential anti-development special interests sought to use a landmark designation to block all development on the basis of issues like access to air and light, the availability of street parking, and increased population density. (A82-83, ¶¶ 44-45; A211; A213; A217-19; A223).

The LPC improperly capitulated to these special interests and their zoning concerns, and voted to modify the designation of the Other Buildings to include the Buildings. (A83; ¶¶ 45-46). Its designation report largely incorporated the 1990 designation report, offering only one "new" justification for the designation of the Buildings—that their inclusion would "enhance[] our understanding of the work of [CSHC] since [the FAE] encompasses the earliest and latest surviving examples of the light-court model tenements that characterized [CSHC's] urban development projects." (A326).

Stahl challenged the landmark designation through an Article 78 petition, which was denied by the New York Supreme Court and this Court. (A84, ¶¶ 50-51). On November 18, 2010, the Court of Appeals denied Stahl's motion for leave to appeal, exhausting Stahl's judicial challenge to the designation. (A84, ¶ 52).

F. The LPC Denied Stahl's Hardship Application

The landmark designation effectively destroyed the value of the Buildings. Unencumbered by the designation, the Buildings were worth at least $100 million and possibly as much as $200 million. (A82, ¶ 41). However, the designation extinguished this value and left Stahl with a Catch-22. For years, Stahl had operated the Buildings with an eye toward redevelopment, which included keeping apartments unrented as they came vacant (A81, ¶¶ 38-39), but the landmark designation now blocked these redevelopment plans, *see* N.Y.C. Admin. Code § 305(a)(1). In their current condition, the Buildings could not be operated at a profit, and indeed, Stahl lost money on the Buildings in each year after the designation. (A84-85, ¶ 53). And because many of the units were legally uninhabitable in their current state, Stahl would have to spend millions renovating these apartments (and the Buildings themselves), without any realistic prospect of earning enough to pay for those renovations. (*Id.*).

Accordingly, Stahl sought relief through the Landmarks Law. It filed an application for a certificate of appropriateness authorizing demolition of the Buildings on the ground of insufficient return (the "hardship" application). *See* N.Y.C. Admin. Code § 25-309; (A335).

1. The Landmarks Law's hardship procedure

The Landmarks Law permits the owner of a property subject to a landmark designation to seek approval to demolish, alter, or reconstruct the property on the ground that it is not "capable of earning a reasonable return" under "reasonably efficient and prudent management." N.Y.C. Admin. Code §§ 25-302(c), 25-309(a)(1). A property owner that can establish a hardship is entitled to affirmative relief from the LPC. § 25-309(b)-(c), (g).

The Landmarks Law provides a strict, detailed procedure by which the LPC is to evaluate a claim of hardship. It defines "reasonable return" as a "net annual return" of 6% of the "valuation of an improvement parcel." § 25-302(v)(1). Because reasonable return is measured as a percentage of the property's valuation, it is calculated based on an equation: the net annual income of a property divided by the property's valuation. If the quotient of that equation is below 6%, the property owner has established a hardship.[1]

The threshold inquiry is the relevant unit of property, or "improvement parcel," the LPC is to consider in determining whether there is a hardship. The Landmarks Law defines the applicable improvement parcel, in relevant part, as

[1] As explained below, the typical reasonable return equation under the Landmarks Law is:

$$Rate\ of\ Return = \frac{Income - (Operating\ Expenses + Depreciation + Real\ Estate\ Taxes)}{Assessed\ Value}$$

"[t]he unit of real property which . . . is treated as a single entity for the purpose of levying real estate taxes." § 25-302(j).

The numerator of the reasonable return equation, or "net annual return," is the total income of the improvement parcel less its expenses in a given test year. § 25-302(v)(3)(a). "[M]ortgage interest and amortization" are excluded from expenses, but "an allowance for depreciation of two per centum of the assessed value of the improvement" must be included. *Id.* Because Stahl's application was filed in October 2010, the relevant test year for its application was 2009. *See* § 25-302(v)(3)(b).

The denominator of the equation—the value of the property—is generally the "assessed valuation" (or assessed value) of the property. § 25-302(v)(2). Assessed value is defined by the New York City Department of Finance ("DOF") as a percentage of the market value of a property; for multi-unit residential properties like the Buildings, it is only 45% of market value. This means that the statutory reasonable return of 6% of assessed value is actually just 2.7% of the market value of a property. The Landmarks Law does permit the LPC to use the sales price of the property as the value of the property (instead of the assessed value) where there has been a recent "bona fide sale" of the property. § 25-302(v)(2)(b).

Assessed value is also used to calculate depreciation and real estate taxes, which are both included in the numerator of the equation as expenses. Both depreciation and real estate taxes are defined as percentages of assessed value. § 25-302(v)(3)(a); *e.g.*, N.Y.C. Charter § 1506.

The Landmarks Law also requires that the LPC assess the property's "capacity" to earn a reasonable return "under reasonably efficient and prudent management." § 25-302(c). Thus, the LPC determines not just whether the property is currently earning a reasonable return, but whether it could generate a reasonable return after renovations or alterations to the property.

2. The LPC denied Stahl's application after a lengthy and rigged hardship process

The LPC's hardship process lasted from October 7, 2010 to May 20, 2014. (A335; A1348). Stahl retained two experts (a real estate valuation firm and a construction cost consulting firm), submitted substantial evidence supporting its positions, and responded to scores of questions from the LPC. (A88, ¶ 66).

During this process, the LPC held three public hearings. The hearings, like the ones in 2006 leading to the landmark designation, focused on the anti-development concerns of influential special interests groups instead of the statutory factors articulated in the Landmarks Law's hardship provisions. (A87, ¶ 63). Throughout the proceedings, LPC Commissioners made statements indicating that they had prejudged Stahl's application. (A87, ¶ 64). These comments revealed

that, before the facts were in, the LPC had already decided there could not be a "true hardship" and that the Commissioners believed it was their "job" to reject Stahl's arguments. (A960; A1292; A1289-90).

The Commissioners also openly relied on unreliable "evidence," citing the opinions of unidentified friends and acquaintances who had no factual knowledge of Stahl's application. One Commissioner discounted the poor condition of the vacant apartments because she believed that current tenants in *occupied* apartments had filled them "with art, ingenious built-ins, furnishings, personality and pride of place." (A1260). Another Commissioner disputed Stahl's expert evidence about the marketability of the Buildings because a friend of his in the fashion industry had indicated he would like to live there. (A913). Other Commissioners cited reactions of unidentified people as evidence of the rent Stahl could charge. (*See* A1248; A1292).

Stahl's evidence and its experts' findings established that Stahl could not earn a 6% return under any reasonable scenario. But unsurprisingly, the LPC disregarded that evidence and did the "job" it came to do, voting to deny Stahl's hardship application on May 20, 2014. (A1348).

3. The LPC's arbitrary and capricious reasoning

The LPC issued a written decision on May 29, 2014. (*Id.*). Its analysis was riddled with legal and factual errors. The LPC considered various potential

renovation scenarios, each reflecting varying levels of renovations and/or rental income. (A1356). It made numerous assumptions about issues like the rental income that could be generated under these scenarios; the Buildings' post-renovation operating expenses; the projected vacancy rate in the Buildings; the potential for additional income from non-rental sources, such as operating a laundromat or providing storage space—none of which Stahl challenges in this appeal. All told, the LPC considered 24 different scenarios and concluded that under any of those, Stahl could earn a reasonable return on the Buildings.

However, the LPC made three fundamental errors in its denial of Stahl's hardship application. At least one of these errors infected every single one of the LPC's 24 scenarios and rendered its decision arbitrary and capricious. If the LPC had not made these errors, even if it had used all of its own other assumptions, it would have had to find that the Buildings were incapable of generating a reasonable return.

First, the LPC erroneously determined that the relevant "improvement parcel" for the hardship analysis was the entire FAE, as opposed to the Buildings. (A1360). Under the plain language of the statute, it was clear that the Buildings were the improvement parcel. However, the LPC improperly disregarded the statute and relied on non-statutory considerations.

Second, the LPC projected the post-renovation assessed value of the Buildings by using the "income approach" rather than the "cost approach." (A1375). This resulted in a calculation divorced from economic reality, in which a fictional rate of return was generated based on projected post-renovation income, without taking into account how much it would cost to generate that income. It also violated the LPC's own administrative precedent. In addition, the analysis was internally inconsistent: the LPC used the cost approach to calculate assessed value for depreciation but used the income approach everywhere else. In other words, under the LPC's analysis, assessed value meant one thing in one place and something else in another place.

Third, the LPC arbitrarily penalized Stahl by excluding any renovation costs for 44 apartments that became vacant after the 2006 landmark designation. The LPC concluded that Stahl's decision to keep those apartments vacant was a "self-imposed hardship," and it excluded their renovation costs from the reasonable return equation. (A1360). This conclusion was irrational because it included the projected income these apartments would generate after costly renovations, but excluded the required costs. It was also irrational because it effectively required Stahl to renovate the Buildings in order to obtain permission to demolish them.

Recognizing the weakness of its analysis, the LPC attempted to safeguard its decision from meaningful review by including an alternative scenario "for

purposes of comparison only." (A1375). The LPC claimed that this comparison adopted Stahl's arguments regarding the improvement parcel, the cost approach, and the 44 vacant apartments, and that even under this scenario, Stahl could earn over 6%. (*Id.*; A1390-93; A1395). However, this comparison did not actually adopt Stahl's arguments—it used the cost approach inconsistently and failed to include the renovation costs of all 97 vacant apartments. Had the LPC fixed these errors, it would have found that Stahl was incapable of earning a reasonable return.

G. The Lawsuit And The Supreme Court's Order

On September 22, 2014, Stahl filed a hybrid Article 78 and plenary action against the City. Stahl's Article 78 petition argued that the LPC's denial of Stahl's hardship application should be overturned as arbitrary and capricious. Its plenary action alleged that the 2006 landmark designation of the Buildings was an unconstitutional taking of Stahl's property in violation of the United States and New York Constitutions.

The City opposed Stahl's Article 78 petition and moved to dismiss Stahl's takings claim under CPLR 3211(7).

In a decision, order and judgment entered January 28, 2016, the lower court denied Stahl's Article 78 petition and granted the City's motion to dismiss the takings claim. The lower court failed to address many of Stahl's arguments. Nevertheless, it held that the LPC's denial of Stahl's hardship application was not

arbitrary and capricious. In addition, the lower court held that Stahl failed to state a takings claim. The lower court did not devote a separate analysis to the takings issue, and instead treated it coextensively with the Article 78 petition.

On February 25, 2016, Stahl timely filed a notice of appeal.

SUMMARY OF ARGUMENT

The Complaint more than adequately alleged that the LPC's decision to landmark the Buildings and its refusal to grant hardship relief was an unconstitutional taking. The Complaint alleged in detail how the landmark designation destroyed the Buildings' value and upended Stahl's legitimate expectation that they could be redeveloped. The lower court ignored these allegations and, in violation of the most basic principles of civil procedure, improperly resolved factual issues against Stahl on a motion to dismiss. In so doing, the court erroneously deferred to the LPC on the questions central to whether the LPC violated the Constitution, even though the constitutional question was plainly for the court, not the agency, which was not even presented with the takings issue. The effect was that the court allowed the LPC to immunize its own actions from constitutional review. The takings claim should be reinstated.

The lower court should also have granted the Article 78 petition. The LPC disregarded clear and binding statutory language, employed an analysis that lacked any rational basis, contravened its own precedent, and provided patently false,

post-hoc rationalizations for these actions. Under black letter law, this type of arbitrary and capricious misconduct compels reversal of an agency decision.

The decision below should be reversed.

ARGUMENT

I. STAHL'S TAKINGS CLAIM SHOULD BE REINSTATED

On a motion to dismiss under CPLR 3211(7), courts must liberally construe the allegations of the complaint. In particular, courts are required to assume the truth of the facts alleged and afford the plaintiff the benefit of all favorable inferences. *See Leon v. Martinez*, 84 N.Y.2d 83, 87-88 (1994); *see also Sokoloff v. Harriman Estates Dev. Corp.*, 96 N.Y.2d 409, 414 (2001). This Court must reinstate the action if the facts as alleged fall within a cognizable legal theory. *See Lawrence v. Graubard Miller*, 11 N.Y.3d 588, 595 (2008); *accord Sokoloff*, 96 N.Y.2d at 414. "Whether a plaintiff can ultimately establish its allegations is not part of the calculus in determining a motion to dismiss." *EBC I, Inc. v. Goldman, Sachs & Co.*, 5 N.Y.3d 11, 19 (2005).

The longstanding principle of assuming the truth of a complaint's factual allegations is particularly important in the takings context. Takings claims typically present factual disputes that are often not susceptible to resolution on a motion to dismiss. That is precisely the case here.

Stahl alleged that a "partial" regulatory taking occurred when the Buildings were designated landmarks. In *Penn Central Transportation Co. v. City of New York*, the Supreme Court of the United States held that partial regulatory takings claims are subject to a "factual inquir[y]" that balances the economic impact of the regulation on the property, the extent to which it interferes with the owner's "distinct investment-backed expectations," and the nature of the governmental action. 438 U.S. 104, 124 (1978); *see also Dawson v. Higgins*, 197 A.D.2d 127, 136 (1st Dep't 1994). There is no "set formula" or "*per se* rule" governing this inquiry. *Penn Cent.*, 438 U.S. at 123-24; *Tahoe-Sierra Pres., Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 326 (2002) (internal quotation and alteration marks omitted). Because the inquiry "necessarily entails complex factual assessments of the purposes and economic effects of government actions," *Yee v. City of Escondido*, 503 U.S. 519, 523 (1992), courts must instead undertake a "situation-specific" analysis of whether a taking has occurred. *Ark. Game & Fish Comm'n v. United States*, 133 S. Ct. 511, 518 (2012).

This analysis is "seldom appropriate for resolution on the pleadings." *White Oak Realty, LLC v. U.S. Army Corp of Eng'rs*, No. 13-4761, 2014 WL 4387317, at *9 (E.D. La. Sept. 4, 2014) (internal quotation marks omitted). Motions to dismiss partial regulatory takings claims are thus routinely denied because of the "fact-intensive" nature of the inquiry. *2910 Georgia Ave. LLC v. District of Columbia*,

983 F. Supp. 2d 127, 137 (D.D.C. 2013); *accord, e.g.*, *Neumont v. Monroe Cnty. Fla.*, 104 F. Supp. 2d 1368, 1371 (S.D. Fla. 2000) (takings inquiry could not "be resolved on a motion to dismiss"); *M&N Materials, Inc. v. Town of Gurley, Ala.*, No. CV-14-S-184-NE, 2014 WL 2590473, at *3, 6 (N.D. Ala. June 10, 2014) (same); *New Horizon Inv. Corp. v. Mayor & Mun. Council of Belleville*, No. Civ. A. 04-3973 (KSH), 2005 WL 2237776, at *7 (D.N.J. Sept. 14, 2005) (same); *Colo. Springs Prod. Credit Ass'n v. Farm Credit Admin.*, 695 F. Supp. 15, 21 (D.D.C. 1988) (same); *Carpenter v. United States*, 69 Fed. Cl. 718, 731-32 (Fed. Cl. 2006) (same); *Sacramento Mun. Utility Dist. v. United States*, 61 Fed. Cl. 438, 441-42 (Fed. Cl. 2004) (same).

The lower court disregarded these principles when it granted the City's motion to dismiss. It overlooked the Complaint's allegations and the material issues of fact they created and erroneously resolved every factual dispute in the City's favor. Stahl alleged that (1) the Buildings are the property that was taken, (2) the designation destroyed the Buildings' value, and (3) Stahl's legitimate, investment-backed expectations for the Buildings were upended by the designation. These allegations plainly state a claim for a partial regulatory taking. However, the lower court erroneously failed to accept these allegations as true. As a result, this Court should reverse and reinstate Stahl's takings claim.

A. Stahl Adequately Alleged That The Relevant Parcel For The Takings Claim Was The Buildings

The threshold inquiry for a regulatory takings claim involves identifying the property that was allegedly taken. *See Keystone Bituminous Coal Ass'n v. DeBenedictis*, 480 U.S. 470, 497 (1987). To identify the relevant parcel, courts look to "the economic expectations of the claimant with regard to the property." *Forest Props., Inc. v. United States*, 177 F.3d 1360, 1365 (Fed Cir. 1999). Because the claimant's expectations will "largely depend upon the facts of the particular case," *Sharp v. United States*, 191 U.S. 341, 354 (1903), courts use "a flexible approach" that "account[s] for factual nuances." *Loveladies Harbor, Inc. v. United States*, 28 F.3d 1171, 1181 (Fed Cir. 1994); *see also 2910 Georgia Ave.*, 983 F. Supp. 2d at 137 ("[T]he relevant 'property' for purposes of this case is a fact intensive inquiry.").

Here, Stahl alleged that the relevant parcel was the two Buildings—the only property that Stahl sought to redevelop. That is because under the 1990 compromise the BOE carved the Buildings out of the FAE landmark to "allow for [as-of-right] development" of the Buildings, but not the rest of the FAE. (A80, ¶ 34). Stahl agreed not to challenge the landmark designation of the Other Buildings precisely because the City had preserved Stahl's rights to develop the Buildings. (A80, ¶ 35). In reliance upon this compromise, Stahl treated the Buildings as separate, and spent over a decade preparing them for redevelopment.

For example, Stahl kept the Building's apartments unrented as they became vacant, so that new rent-regulated tenants would not impede Stahl's redevelopment plan. (*See* A81, ¶¶ 38-39); *see also Palm Beach Isles Assocs. v. United States*, 208 F.3d 1374, 1381 (Fed Cir. 2000) (contiguous properties were distinct parcels where owner had not intended to develop both parcels as single unit).

The lower court erroneously held that the relevant parcel for Stahl's takings claim was the entire FAE and not the Buildings. The court acknowledged the 1990 BOE compromise permitting the Buildings' redevelopment, but brushed it aside as a "politically motivated anomaly." (A43-44). Apparently, the court was suggesting that because the City always had the right to repudiate the 1990 compromise and re-designate the Buildings as a landmark, Stahl should have simply ignored the City's promise to allow redevelopment of the Buildings and taken no steps to redevelop them. (A43-45).

That conclusion was unsupportable. When the City told Stahl that it could redevelop the Buildings, Stahl took the City at its word. The City's decision to allow redevelopment went unchallenged for 16 years. The reasonable "economic expectation[]" during this time was that redevelopment of the Buildings—unlike the remainder of the FAE—was permissible. *Forest Props.*, 177 F.3d at 1365.

The City ultimately broke its promise and precluded redevelopment, but that did not retroactively negate the reasonable expectation that Stahl previously held.[2]

The Federal Circuit's decision permitting a takings claim to go forward in *Loveladies Harbor* is analogous. There, the plaintiff acquired a 250-acre parcel and developed 199 acres of that parcel over several years. 28 F.3d at 1174. The remaining 51 acres of the parcel later became subject to wetlands regulations, such that the plaintiff could no longer develop them without approval from both the New Jersey Department of Environmental Protection ("NJDEP") and the Army Corps of Engineers ("Corps"). *Id.* During the application process, the plaintiff reached a deal with NJDEP, in which NJDEP granted permission to develop 12.5 acres of the 51-acre parcel, with the remaining 38.5 acres being effectively conveyed to the state. *Id.*; *id.* at 1181.

After the conveyance, NJDEP reneged on the deal and advised the Corps to deny the plaintiff a federal permit, which would block development of the 12.5 acres. *Id*. at 1174. The plaintiff brought a takings claim, and the government argued that the relevant parcel was either the full 250-acre parcel or, alternatively, a smaller parcel comprising the 51 undeveloped acres (and 6.4 developed acres that

[2] Contrary to the lower court's suggestion, Stahl does not "insinuate[] that the City should be estopped from reconsidering the BOE's determination." (A45). Stahl's point is that, before the City's sudden repudiation of the 1990 compromise, Stahl reasonably understood that the Buildings could be redeveloped.

the plaintiff had not yet sold). *Id.* at 1180. The Federal Circuit rejected both of these arguments. It held that the parcel for the plaintiff's takings claim was the 12.5 acres that the plaintiff had understood it could develop under its compromise with NJDEP, because of the unfairness that would otherwise result from requiring the plaintiff "to convey to the public the rights in the 38.5 acres in exchange for the right to develop 12.5 acres, and then to include the value of the grant as a charge against the givers." *Id.* at 1180-81. Here, similarly, the purpose of the 1990 compromise was to preserve Stahl's rights to redevelop the Buildings, in exchange for Stahl's agreement not to challenge the 1990 landmark designation of the Other Buildings. As in *Loveladies Harbor*, the City may not simply renege on that compromise and then claim that the entire FAE is the relevant parcel.

At a minimum, the lower court was not free to ignore the Complaint's allegations and declare Stahl's expectation "unrealistic" as a matter of law. (A46). Factual disputes like these cannot be resolved on a motion to dismiss. *See 2910 Georgia Ave.*, 983 F. Supp. 2d at 137; *cf. Knight Sec., L.P. v. Fiduciary Trust Co.*, 5 A.D.3d 172, 173 (1st Dep't 2004) ("[T]he reasonableness of . . . reliance [generally] implicates factual issues whose resolution would be inappropriate" on "a motion to dismiss" (internal quotation marks omitted)). Had the lower court applied the proper standard, it would have recognized that this fact-intensive inquiry can only be decided by a jury after development of a full factual record.

The lower court also appeared to defer to the LPC's supposed determination of which parcel was relevant to the takings claim. (A42). This was legally erroneous for three reasons.

First, the LPC made no such determination. Nor could it have done so, as it was merely deciding whether to grant the hardship application—not whether denying the application would violate the Takings Clause.

Second, because the takings claim was not before the LPC, Stahl had no opportunity to present evidence demonstrating its "economic expectation[]" of what the relevant parcel would be. *Forest Props.*, 177 F.3d at 1365. In a hardship proceeding, the LPC only identifies the "improvement parcel" under the Landmarks Law. What constitutes an "improvement parcel" depends solely on how the City levies taxes on the property, and not how the claimant expects to use the property. § 25-302(j) (defining the parcel for the hardship application as "[t]he unit of real property which . . . is treated as a single entity for the purpose of levying real estate taxes"). But it is the claimant's expected use that determines the relevant parcel for purposes of the takings analysis.[3] The lower court dismissed Stahl's constitutional claim without affording Stahl the opportunity to develop and

[3] The City conceded below that the Landmarks Law's definition of an improvement parcel "has no relevance . . . for purposes of a takings claim." (A300).

present evidence showing that, based on Stahl's expectations, the Buildings were the relevant parcel.

Finally, even if the LPC had addressed Stahl's takings claim, it would not be entitled to deference. It is for the courts, and not the LPC, to assess whether the LPC's conduct violates the Takings Clauses of the United States and New York Constitutions. *See, e.g.*, *Cumberland Farms, Inc. v. Town of Groton*, 262 Conn. 45, 69 (2002) ("[T]he plaintiff is entitled to a de novo review of the factual issues underlying its inverse condemnation claim, unfettered by the [zoning] board's previous resolution of any factual issues."); *Hensler v. City of Glendale*, 8 Cal. 4th 1, 15 (1994) (en banc) ("A property owner is, of course, entitled to a judicial determination of whether the agency action constitutes a taking."); *Bencin v. Bd. of Bldg. & Zoning Appeals*, No. 92991, 2009 WL 3387695, at *2 (Ohio Ct. App. Oct. 22, 2009) (holding that an "administrative agency . . . cannot determine whether an ordinance is unconstitutional as applied to a particular parcel" and that such "constitutional claim[s] must be tried originally in the court of common pleas, with the court permitting the parties to offer additional evidence"); *cf. N.Y. State Ass'n for Retarded Children, Inc. v. Carey*, 612 F.2d 644, 648-49 (2d Cir. 1979) (refusing to defer to fact-finding of state-agency-defendant in action alleging that it violated the Fourteenth Amendment); *Johnson v. Charles City Cmty. Sch. Bd. of Educ.*, 368 N.W.2d 74, 84 (Iowa 1985) ("The authorities which in general require

courts to yield to non-arbitrary administrative determinations uniformly provide an exception for constitutional questions."). Otherwise, a city or state agency could immunize itself from constitutional review—which is precisely what the court below erroneously allowed the LPC to do.

Stahl more than adequately alleged facts demonstrating its economic expectation that the Buildings were a distinct parcel, separate from the remainder of the FAE. This disputed issue of fact cannot be resolved on a motion to dismiss.

B. Stahl Adequately Alleged The Economic Impact Of The Landmark Designation

The lower court also disregarded the Complaint's allegations regarding the severe economic impact of the City's landmark designation and denial of hardship relief.

The key issue in any regulatory takings claim is the severity of the economic impact imposed by the challenged regulation on the property. As with the other aspects of the *Penn Central* test, there are no *per se* rules. "[T]he line from a noncompensable 'mere diminution' [in value] to a compensable 'partial taking'" is not a bright one. *Fla. Rock Indus., Inc. v. United States*, 18 F.3d 1560, 1570 (Fed. Cir. 1994). There is no "automatic numerical barrier preventing compensation, as a matter of law, in cases involving a smaller percentage diminution in value." *Cienega Gardens v. United States*, 331 F.3d 1319, 1340 (Fed. Cir. 2003) (internal quotation marks omitted); *see also Hendler v. United States*, 175 F.3d 1374, 1385

(Fed. Cir. 1999) ("The question of the economic impact of a particular regulatory action is of course fact-specific to the case."). Accordingly, the economic impact analysis, like the *Penn Central* test as a whole, is a fact-intensive inquiry that should not be resolved on a motion to dismiss. *See, e.g.*, *M&N Materials*, 2014 WL 2590473, at *3, 6 (denying motion to dismiss where plaintiff alleged that, as a result of denial of license to open quarry, it sold property "at an amount far less" than property's value before denial); *Neumont*, 104 F. Supp. 2d at 1371 (takings inquiry could not "be resolved on a motion to dismiss").

The Complaint detailed the landmark designation's crippling effect on the Buildings' value. The Complaint alleged that Stahl (1) lost money by operating the Buildings in each year since the designation (A89, ¶ 74); (2) cannot renovate the Buildings without incurring additional losses because, so long as they are subject to the landmark designation, the Buildings cannot generate enough income to offset the renovation costs (A89-90, ¶¶ 75-76); and (3) has identified no alternative use for the Buildings, other than the current (unprofitable) one (A84-85, ¶ 53). Given the substantial value of the Buildings if unencumbered by a landmark designation (A82, ¶ 41), it is clear that the designation destroyed virtually all of the Buildings' economic value. (A89, ¶ 73; A101, ¶ 121). At a minimum, the Complaint alleged ample facts from which the landmark designation's impact may be inferred. (*Id*.).

It is not entirely clear why the lower court found these allegations insufficient. The court appears to have determined that (1) despite the restrictions imposed by the Landmarks Law, Stahl may still "use . . . the property to obtain rental income" (A33); and (2) deference was owed to the LPC's purported finding that the Buildings can yield a "reasonable" economic return (A37-38; A60; A61). Assuming that was the basis for the lower court's ruling, then as demonstrated below, it erred as a matter of law and should be reversed.

1. Although the Building's antiquated apartments may be rented, they can only generate meager rental income, which comes nowhere close to making the Buildings economically viable. (A89-90, ¶¶ 74-76). The Complaint explained in detail why the Buildings lose money with or without this rental income. (*Id*.). The lower court simply ignored these allegations, which must be assumed true for purposes of the motion to dismiss.

2. The lower court was not permitted to defer to the LPC's skewed economic impact "analysis." As set forth above, the LPC's alleged constitutional violations must be reviewed *de novo*. As many courts have held, judicial review is needed most of all for determining the critical issue of the regulation's economic impact on the property. *See, e.g.*, *Cumberland Farms*, 262 Conn. at 63 (refusing to "accord preclusive effect to the board's findings" because doing so "would be to vest the board with the responsibility of deciding the facts underlying the

plaintiff's constitutional claim and, in effect, would give the board the authority to settle the issue raised by that claim"); *Hensler*, 8 Cal. 4th at 15-16; *see also Brown v. Painesville Twp. Bd. of Zoning Appeals*, No. 2004-L-047, 2005 WL 2709586, at *5 (Ohio Ct. App. Oct. 21, 2005) ("[T]he trial court cannot substitute its duty of responsibility for reaching a decision by deference to the [agency].").

The LPC administrative proceedings offered none of the protections afforded by a judicial proceeding; they lacked evidentiary rules, there was no testimony offered under oath, Stahl could not cross-examine adversarial witnesses, and Stahl's application was not adjudicated by a disinterested factfinder. Consequently, much of the "evidence" the LPC relied on fell far below the indicia of reliability required in a court of law. The LPC relied, for example, on anecdotal opinions of unidentified persons with no knowledge of the facts (*see* A913 (citing opinion of random person in fashion industry as "evidence" that apartments were marketable); A1248, A1292 (citing unverified reactions of anonymous individuals as evidence of what rent Stahl could charge)); prejudicial non-sequiturs (*see* A1260 (asserting that apartments could be made marketable because occupied apartments have "personality")); and other patently unreliable evidence (*see* A1265 (claiming vacancy rate proffered by Stahl could not be verified because one Commissioner supposedly "was unable to locate the [Buildings'] rental office")).

Deference under these circumstances would defeat the constitutional rights of property owners without any legitimate process. In *Healing v. California Coastal Commission*, for example, the plaintiff brought a hybrid action challenging the administrative denial of his application for a development permit and asserting a takings claim. 22 Cal. App. 4th 1158, 1165-66 (Cal. Ct. App. 1994). The defendant-commission argued that the trial court was required to determine the takings claim on the basis of the administrative record, without a trial on the merits. *Id.* at 1169. The court disagreed and held that the plaintiff was entitled to present evidence anew at trial. *Id.* at 1170. The court noted that the administrative record was "created under circumstances where . . . witnesses are not sworn, testimony is not presented by means of direct or cross-examination but rather by narrative statements, and the Commission does not have the authority to issue subpoenas or compel anyone to attend its hearing." *Id.* Simply put, an administrative hearing under these circumstances was not "a satisfactory substitute for an evidentiary trial on the takings issue." *Id.* at 1177; *see also Hensler*, 8 Cal. 4th at 16 (where "the administrative hearing is not one in which the landowner has a full and fair opportunity to present evidence relevant to the taking issue, one in which witnesses may be sworn, and testimony presented by means of direct and cross-examination, the administrative record is not an adequate basis on which to determine if the challenged action constitutes a taking"); *Cioffoletti v. Planning &*

Zoning Comm'n of Town of Ridgefield, 209 Conn. 544, 551 (1989) ("[T]he trial court should decide the taking issue de novo in the light of all the evidence properly presented to it, including, *but not limited to*, the administrative record."); *cf. N.Y. State Ass'n*, 612 F.2d at 649 ("Clearly, deference to a state agency's fact-finding is inappropriate once that agency is the defendant in a discrimination suit.").[4]

By rotely adopting the LPC's analysis, the lower court also precluded Stahl from proffering critical takings-related evidence that was not before the LPC. (A32). Whether a taking occurred depends on how the landmark designation "dimin[ished] [the] value" of the Buildings. *Cienega Gardens*, 331 F.3d at 1340 (internal quotation marks omitted). Measuring this diminution in value requires a determination of (1) the value of the Buildings prior to the landmark designation, (2) the value of the Buildings afterwards, and (3) the value of any alternative economic use of the property.[5] None of those facts were before the LPC, which is

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[4] Deference to the LPC would effectively preclude judicial determination of takings claims brought against any regulation that (like the Landmarks Law) provides for a hardship exception. A takings claim is unripe until the hardship process is exhausted. *See, e.g.*, *Church of St. Paul & St. Andrew v. Barwick*, 67 N.Y.2d 510, 522 (1986). Thus, if deference were owed to the denial of the hardship application, then no takings claim would ever succeed.

[5] Contrary to the lower court's opinion (A59), Stahl did "identify th[e] 'additional facts'" it intended to present in support of the takings claim. These facts appear both in the Complaint itself (A89, ¶ 73; A101, ¶ 121) and in Stahl's opposition to the City's motion to dismiss (A334).

another reason for reversal. *See, e.g.*, *Spears v. Berle*, 48 N.Y.2d 254, 261, 264 (1979) (remanding for additional fact-finding relevant to regulation's economic impact); *Brotherton v. Dep't of Envtl. Conservation of State of N.Y.*, 189 A.D.2d 814, 815-16 (2d Dep't 1993) (denying Article 78 petition challenging denial of development permit on wetlands parcel, but remanding for evidentiary hearing on takings claim);[6] *see also Cioffoletti*, 209 Conn. at 551 (plaintiff was entitled to introduce additional evidence beyond administrative record because "an administrative agency is incompetent to decide" takings claim); *Bencin*, 2009 WL 3387695, at *2 (noting that appellate courts have reversed trial courts that "denied the parties the opportunity to present evidence in a de novo hearing as to constitutional challenges to zoning codes as applied to the subject property").

Finally, even if some deference were owed to the LPC (and none is), the LPC's denial of Stahl's hardship application was arbitrary and capricious. *See infra* Part II. For all of these reasons, the lower court's deference to the LPC was erroneous.

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[6] The lower court distinguished *Brotherton* purportedly "because the issue of whether the petitioner suffered an unconstitutional taking was not addressed" by the trial court in that case. (A61). That misses the point. *Brotherton* confirms that courts do not simply defer to an agency's decisionmaking when adjudicating a takings claim, and instead should conduct their own "evidentiary hearing," as the trial court was ordered to do on remand. 189 A.D.2d at 815-16.

C. Stahl Adequately Alleged That The Designation Interfered With Stahl's Investment-Backed Expectations

The *Penn Central* test also instructs courts to consider whether the challenged regulation interfered with a property owner's "distinct investment-backed expectations." *Penn Cent.*, 438 U.S. at 124. The existence of investment-backed expectations "is an objective, but fact-specific inquiry into what, under all the circumstances, [a property owner] should have anticipated." *Cienega Gardens*, 331 F.3d at 1346. Stahl's Complaint adequately alleged such interference.

Stahl alleged that when it acquired the FAE, it intended to redevelop the properties. (A91, ¶ 79). And, as set forth above, *see supra* p. 9, the City agreed to carve the Buildings out of the 1990 landmark designation "to allow for [as-of-right] development in the future." (A201, ¶ 9; A80, ¶ 36); *accord Laguna Gatuna, Inc. v. United States*, 50 Fed. Cl. 336, 347 (Fed. Cl. 2001) (EPA's statements to owner regarding its right to redevelop property supported investment-backed expectations); *Woodland Manor, III Assocs., L.P. v. Reisma*, No. C.A. PC89-2447, 2003 WL 1224248, at *14 (R.I. Super. Ct. Feb. 24, 2003) (approval of a permit established owner's investment-backed expectations).[7] Stahl has taken costly steps

[7] Contrary to the lower court's opinion, Stahl does not seek to "establish a 'taking' simply by showing that [it] ha[s] been denied the ability to exploit a property interest that [it] heretofore had believed was available." (A46). The court ignored the critical fact that the City itself endorsed Stahl's belief that the Buildings could be developed.

to pursue the redevelopment in direct reliance on the BOE's decision. (A81, ¶¶ 37-39; A91, ¶¶ 81-82).

The lower court disregarded these allegations. It held that Stahl lacked the requisite "investment-backed expectations" because (1) when Stahl purchased the Buildings, it supposedly should have known they "would always be low-scale, rent regulated rentals"; and (2) the 1992 *Kalikow* decision overturned the BOE's de-designation of portions of the YAE. (A46-47). The court was wrong on both counts.

1. The lower court was wrong to assume that rent regulations restrict development in perpetuity. In fact, rent restrictions lapse over time, *see, e.g.*, 9 N.Y.C.R.R. § 2200.2(f)(12) (apartments that come vacant after April 1, 1953 not subject to rent control); 9 N.Y.C.R.R.§ 2211.3 (apartments may be deregulated where tenants' income exceeds threshold), and do not even prohibit redevelopment, *see* N.Y.C. Admin. Code § 26-408(b)(4)-(6) (governing eviction of rent-controlled tenants where owner intends to redevelop property); 9 N.Y.C.R.R. § 2524.5(2) (owner who intends to demolish building not required to offer rent-stabilized tenants renewal leases). The restrictions in place when Stahl purchased the Buildings were not a permanent bar to redevelopment. That is why Stahl left apartments unrented as they became vacant—to ensure that the prior rent restrictions would not preclude future redevelopment. In other words, Stahl

certainly could have intended to redevelop the Buildings when it purchased them in 1977, and its subsequent conduct proves that is precisely what Stahl intended to do. The lower court was not free to ignore the Complaint's allegation that this was Stahl's intention. (A91, ¶ 79).

2. *Kalikow* does not contradict Stahl's position. The BOE approved compromises for both the YAE and the FAE; it removed four buildings from the YAE's landmark designation and the two Buildings from the FAE's designation. The YAE compromise was appealed and overturned in *Kalikow*. 183 A.D.2d at 533-34. But the FAE compromise was never appealed, and thus became final. Stahl was therefore entitled to rely on it. The theoretical possibility that the City might someday attempt to revisit the BOE's decision did not make Stahl's reliance unreasonable. Otherwise, nothing the government ever did could affect a landowner's reasonable expectations, because the government can always change its mind. The LPC may have had the authority to amend its designation as a matter of administrative law, but after the New York Supreme Court's affirmance, the LPC did nothing to suggest it had any intent to do so for 16 years.

Moreover, unlike the designation at issue in *Kalikow*, the carve out of the Buildings from the designation of the FAE had a clear rationale consistent with the Landmarks Law—the Buildings were designed by a different architect, constructed at a different and later time, and were built on a plot of land acquired at a different

time and from a different seller than the Other Buildings. (*See* A78-79, ¶¶ 30-31). To the extent that reconsideration of the BOE's YAE designation made sense in *Kalikow*, there was no corresponding rationale for revisiting the BOE's treatment of the FAE.

* * * * * *

Stahl's Complaint clearly alleged a partial taking under *Penn Central*, and Stahl is entitled to develop a full factual record in support of that claim. Accordingly, the Complaint should be reinstated.

II. THE LPC'S CONCLUSION THAT THE BUILDINGS CAN EARN A REASONABLE RETURN WAS ARBITRARY AND CAPRICIOUS

The lower court also erred by upholding the LPC's arbitrary and capricious denial of Stahl's hardship application. The administrative record does not support the LPC's conclusion that the Buildings, once renovated, could generate a "reasonable return." The LPC ignored unambiguous statutory language defining the relevant "improvement parcel" as the Buildings, and not the entire FAE; flouted its own precedent; applied an irrational methodology to assess the Buildings' value; and reached the pre-ordained conclusion that the Buildings could be profitable by ignoring nearly half of Stahl's renovation costs. Any rational assessment of the record compels but one conclusion—that the Buildings cannot yield a "reasonable return."

A. Standard Of Review

This Court reviews a lower court's decision on an Article 78 petition *de novo*. *Hunts Point Terminal Produce Co-op. Ass'n v. N.Y.C. Econ. Dev. Corp.*, 36 A.D.3d 234, 244 (1st Dep't 2006). The Court is "empowered to examine the record de novo," and its "authority 'is as broad as that of the trial court.'" *Id.* (quoting *N. Westchester Prof'l Park Assocs. v. Town of Bedford*, 60 N.Y.2d 492, 499 (1983)).

Landmark designation decisions by the LPC are administrative, not "quasi-judicial." *See Lutheran Church in Am. v. City of New York*, 35 N.Y.2d 121, 128 n.2 (1974). They are therefore reviewable under CPLR 7803(3), *see Halpert v. Shah*, 107 A.D.3d 800, 801 (2d Dep't 2013), which requires a court to strike down an agency decision that "was affected by an error of law or was arbitrary and capricious or an abuse of discretion." CPLR 7803(3); *accord N.Y. State Ass'n of Counties v. Axelrod*, 78 N.Y.2d 158, 166 (1991).

A decision is arbitrary and capricious if it (1) is without a "sound basis in reason or regard to the facts," *Murphy v. N.Y. State Div. of Hous. & Cmty. Renewal*, 21 N.Y.3d 649, 652 (2013) (internal quotation marks omitted); (2) is based on an error of law, *see McCambridge v. McGuire*, 62 N.Y.2d 563, 568 (1984) (agency decision was arbitrary and capricious where it "applied an erroneous legal standard"); or (3) deviates from the agency's precedent without

adequate grounds, *see, e.g.*, *In re Charles A. Field Delivery Serv., Inc.*, 66 N.Y.2d 516, 518 (1985); *Klein v. Levin*, 305 A.D.2d 316, 319 (1st Dep't 2003).

A court reviewing an agency's decision is limited to consideration of the reasons given by the agency. *See, e.g.*, *Scherbyn v. Wayne-Finger Lakes Bd. of Coop. Educ. Servs.*, 77 N.Y.2d 753, 758 (1991). Thus, the court is "powerless to affirm the administrative action by substituting what it considers to be a more adequate or proper basis." *Montauk Improvement, Inc. v. Proccacino*, 41 N.Y.2d 913, 913 (1977) (internal quotation marks omitted).

B. Under The Landmarks Law, The Relevant Improvement Parcel Was The Buildings, Not The Whole FAE

The LPC's determination that the relevant "improvement parcel" for the hardship analysis was the entire FAE rather than just the Buildings themselves contravened the Landmarks Law.

The Landmarks Law defines the "improvement parcel" as the unit of property that "is treated as a single entity for the purpose of levying real estate taxes." § 25-302(j). The City does not and cannot dispute that the Buildings comprise a single tax lot (Lot 22) while the Other Buildings occupy three different tax lots. (A92, ¶ 87; A239, ¶ 81; A1358). Nor does the City dispute that for tax purposes, the DOF calculates an assessed value for Lot 22 on a standalone basis, not with the remainder of the FAE. (*See* A1169; A861-98 (real property income and expense filings for block 1459-22, or Lot 22)). Thus, under the plain language

of the Landmarks Law, Lot 22 was the relevant "improvement parcel" for Stahl's hardship application

The LPC nevertheless found that Stahl's rate of return should be calculated based on the entire FAE. In reaching this conclusion, the LPC ignored the Landmarks Law and improperly cited factors nowhere to be found in the statute. It reasoned that the FAE properties should be grouped together because they all are "stylistically" and "physically" similar and shared certain expenses. (A1359). In addition, the LPC cited its "belie[f]" that Stahl "has managed all of the buildings [of the FAE] in light of its desire to demolish the Subject Buildings." (*Id.*). But these factors have nothing to do with how the Buildings are taxed—the sole consideration permitted by § 25-302(j)—and it is black-letter law that an agency cannot disregard a statute. *N.Y.C. Campaign Fin. Bd. v. Ortiz*, 38 A.D.3d 75, 84 (1st Dep't 2006); *see also Trump-Equitable Fifth Ave. Co. v. Gliedman*, 57 N.Y.2d 588, 595 (1982).

The LPC did state that Stahl "filed consolidated filings" with the New York City Tax Commission "for all of the lots" of the FAE between 2007-2012 (A1360), but in reality, Stahl was *precluded* from filing consolidated returns by the Tax Commission. Moreover, tax *filings* do not determine the relevant improvement parcel. The statute focuses on how "real estate taxes" are "*lev[ied]*." § 25-302(j) (emphasis added). It is undisputed that the DOF assesses value—and thus "levies"

real estate taxes—on Lot 22 alone. *See* Black's Law Dictionary 1047 (10th ed. 2014) (defining levy as "[t]o impose or assess").

The Landmarks Law therefore required the LPC to calculate the rate of return solely based on the Buildings. The lower court reached the opposite conclusion because it thought that (1) the LPC is entitled to rely on factors extraneous to the Landmarks Law in defining the improvement parcel, (2) the courts must rely on the LPC's "interpretation of its own regulations," and (3) the "disparate designations by the BOE in 1990 was [sic] a politically motivated anomaly." (A43-44). As demonstrated below, these conclusions are inconsistent with the Landmarks Law.

1. The lower court's opinion states, without citation to any New York authority, that factors other than the DOF's tax levying may be "used to determine the relevant parcel." (A44). That is simply untrue. As explained above, the Landmarks Law has a precise standard for defining an improvement parcel. Under this standard, the *only* relevant factor is whether a unit of property "is treated as a single entity for the purpose of levying real estate taxes." § 25-302(j).

The lower court similarly erred in concluding that Landmarks Law § 25-302(c) "affords the [LPC] discretion" in defining the improvement parcel. (A42). Section 25-302(c) does not even purport to address how an improvement parcel is defined. It deals with the separate issue of how "reasonable return" is calculated.

In any event, the LPC never claimed to rely on § 25-302(c), so this provision supplies no basis for affirming the LPC. *See Montauk Improvement*, 41 N.Y.2d at 913 (court is "powerless to affirm the administrative action by substituting what it considers to be a more adequate or proper basis" (internal quotation marks omitted)).

2. Though a court may defer to an agency's interpretation of its "own regulations" (A44), the improvement parcel is defined by statute, *see* § 25-302(j), not an LPC regulation. An agency is owed no deference on questions "of pure statutory interpretation." *KSLM-Columbus Apts., Inc. v. N.Y. State Div. of Hous. & Cmty. Renewal*, 5 N.Y.3d 303, 312 (2005) (internal quotation marks omitted). Where, as here, "the words of the statute are clear and the question simply involves the proper application of the provision 'there is little basis to rely on any special competence or expertise of the administrative agency' . . . especially when the interpretation . . . directly contravenes the plain words of the statute." *Trump-Equitable*, 57 N.Y.2d at 597 (quoting *Kurcsics v. Merchants Mut. Ins. Co.*, 49 N.Y.2d 451, 459 (1980)).

3. Finally, the BOE's 1990 decision to carve the Buildings out of the FAE designation has no bearing on the definition of the improvement parcel. (A43-44). Whatever the BOE decided and regardless of its motivations, the definition of an "improvement parcel" remains the same, and depends solely on

how taxes are levied on the parcel. It was arbitrary and capricious for the LPC to rely on extraneous factors, and it was error for the lower court to affirm the LPC on that basis.

C. The LPC Erroneously Used The Income Approach To Calculate Assessed Value

The LPC also employed an irrational methodology for calculating whether the Buildings could generate a reasonable return. To calculate reasonable return, the LPC must determine the Buildings' post-renovation assessed value. (A93, ¶ 90). Assessed value is the denominator in the reasonable return equation, and both real estate taxes and depreciation—which appear in the numerator—are defined as percentages of assessed value. *See supra* pp. 14-16 & n.1.

Stahl used the "cost approach," which is the only valid way to calculate post-renovation assessed value. That is because the cost approach takes account of the cost of renovations in calculating whether a return is reasonable. But the LPC rejected Stahl's analysis and instead employed the so-called "income approach," which looks solely to the income that will be generated by the renovated property without considering renovations costs. By using the income approach, the LPC was able to generate theoretical rates of return in excess of the 6% statutory minimum. But that approach makes no sense where, as here, the property must undergo costly renovations.

1. The income approach ignores renovation costs

An owner must be able to recoup its renovation costs within a reasonable time if the renovations are to make any sense. For example, a property might earn $1 million per year after renovations, but that does the owner little good if the cost of renovations is $100 million. In this scenario, the income approach considers only the $1 million annual earnings, and ignores that the owner is losing millions because the renovations were so expensive. By failing to consider how much renovations cost, the income approach radically overstates a property's expected return.

This case is no exception. None of the LPC's renovation scenarios would be reasonable—under the statutory standard or any other—if renovation costs were taken into account. For example, in one scenario, an annual return of $245,949 is considered "reasonable." (A1387). Yet achieving that return would require renovation costs totaling more than $8 million. (A1389). It would take over three decades for the Buildings to even recoup these renovation costs (close to six decades once the time value of money is factored in). (*See also, e.g.*, A1387 (another scenario requiring 38 years to break even); A675, A682, A1169 (another scenario requiring 68 years to break even)). No property owner would consider that rate of return "reasonable."

The "returns" predicted by the statutory hardship equation are significantly overstated in any event. The hardship equation calculates the rate of return based on *assessed* value, which is only 45% of the building's *market* value. Consequently, a 6% return in the equation is really just a 2.7% return. What this means is that the owner of a landmarked building is not entitled to hardship relief even if the real world rate of return is as low as 2.7%. The LPC thus compounded the difficulties imposed by the hardship equation by using a methodology that is even further divorced from economic reality.

The lower court appears to have blessed the income approach by reasoning that, because "the cost approach generates a higher assessed value than the income approach," the income approach would result in a value that lowers "real estate taxes." (A51). But the question is not what taxpayers might favor when the City calculates real estate taxes. The question is which methodology makes sense when calculating a post-renovation rate of return for purposes of a hardship application. For this calculation, the income approach makes no sense at all.

2. The LPC's stated rationale for using the income approach was false

The LPC attempted to justify its use of the income approach by citing a statement by a DOF Assistant Commissioner that the DOF always uses that approach to assess the value of residential rental dwellings (A1374 (citing A1169-70; A1202)), but this is not true. The DOF routinely uses the cost approach.

The DOF frequently adjusts the assessed value of properties to account for the costs of physical improvements. (*See* A1175-77 (citing adjustment of over 5,000 buildings based on physical improvements); A1152-53). That is the cost approach. Indeed, the DOF took this approach with respect to these very Buildings. For the 2008/2009 and 2009/2010 tax years, the DOF sent Stahl Notices of Property Value that explicitly stated that the Buildings' assessed value would be increased based on the "cost[s]" of physical alterations. (A1180-81, A1185; *see also* A1175-76).

The DOF also factors the costs of physical alterations into tax reductions and abatements, and requires taxpayers seeking such relief to submit a full accounting of the alteration's costs. (A1157-58). Similarly, the City's J-51 program makes property owners who engage in alterations to their properties eligible for tax abatements equal to a percentage of the costs of those alterations. N.Y.C. Admin. Code § 11-243(c)(1).

The LPC's justification for using the income approach was therefore false. The DOF takes account of renovation costs when assessing the value of property—exactly what the LPC falsely claimed the DOF does not do. Without a legitimate explanation for its methodology, the LPC's decision cannot stand. *See, e.g.*, *Pell v. Bd. of Educ.*, 34 N.Y.2d 222, 231 (1974) (administrative action is arbitrary and

capricious where it "is without foundation in fact" (internal quotation marks omitted)).

3. The use of the income approach violated the LPC's administrative precedent

Another reason the LPC's decision was arbitrary and capricious is that it contradicted its *own* precedent by using the income approach, and failed to justify its change in position. *See Field Delivery*, 66 N.Y.2d at 520 (absent "valid reasons," an agency's "failure to conform to agency precedent will . . . require reversal on the law as arbitrary, even though there is in the record substantial evidence to support the determination made"); (A107-08, ¶ 143).

In the "KISKA" case, the LPC evaluated the potential return of three properties under various renovation scenarios. (*E.g.*, A1324-25). It used the cost approach to determine assessed value in each of these scenarios. (A1329-32; A1335-36; A1339-40; A1343-46). As the LPC explicitly recognized in that case, "the Commission assumes that the renovation costs will increase the assessed value of the building." (A1322).[8]

[8] The lower court found that KIKSA used the income approach for certain scenarios it analyzed (A50), but that is simply untrue. As the City conceded below, every time the LPC calculated assessed value in KISKA, it did so using the cost approach. (A107, ¶ 142; A244, ¶ 120 (admitting the LPC "used the cost approach in estimating post-renovation real estate taxes in KISKA"); A1322 (stating that "costs of renovation should be added to the assessed valuation of the buildings . . . to calculate the depreciation allowance")).

Because the LPC used the cost approach each time it calculated assessed value, it was required to do so here absent a "rational explanation" for the deviation. *Huff v. Dep't of Corr.*, 52 A.D.3d 1003, 1004 (3d Dep't 2008); *Klein*, 305 A.D.2d at 319 (agency action was arbitrary and capricious where it failed to provide "an adequate explanation" for deviating from precedent). The LPC offered no such justification. The only apparent explanation for the agency's change in position here is that the LPC will use whatever approach leads to its desired outcome. That kind of pretext is arbitrary and capricious. *See, e.g.*, *Field Delivery*, 66 N.Y.2d at 519.

4. The LPC's approach was internally inconsistent

Though the LPC used the income approach for the vast majority of its analysis, it nevertheless used the cost approach to determine assessed value for depreciation. (A1371); § 25-302(v)(3)(a). The result was a reasonable return equation in which assessed value meant one thing for depreciation and something completely different for everything else. Assessed value cannot logically mean two different things in the same calculation; that, by definition, is irrational. *See, e.g.*, *KSLM-Columbus*, 5 N.Y.3d at 315 (vacating agency determination based on reasoning that was "inherently contradictory"). Moreover, the logic behind the LPC's inclusion of renovation costs in depreciation was that Stahl necessarily would have to incur expenses in renovating apartments. (A1371). That same logic

is precisely what compels the cost approach for the other components of the reasonable return equation.

D. The LPC Arbitrarily Excluded Renovation Costs For 44 Vacant Apartments

The LPC further erred by excluding from even the depreciation calculation the renovation costs for 44 vacant apartments that Stahl would legally have to renovate. The LPC erroneously concluded that these costs were a "self-imposed hardship."

Because Stahl had long understood that it retained its rights to redevelop the Buildings after the 1990 landmark designation, it began leaving the apartments unrented as they came vacant to prepare for that redevelopment. *See supra* pp. 10-11. By the 2009 test year, 97 apartments were vacant. (A97, ¶ 103). Every single one required substantial renovations in order to be legally rented. (A78, ¶ 26; A511-12; A1043-44).

Forty-four of these apartments became vacant after the 2006 designation. (A97, ¶ 103). The LPC said that Stahl's decision to leave these apartments vacant was a "voluntary assumption of risk," and thus "any costs associated with renovating the 44 apartments . . . are a self-imposed hardship." (A1360). On this basis, the LPC excluded these costs from the depreciation calculation. (*Id.*).

This made no sense. First, even though it excluded renovation costs from these calculations, the LPC included the income that the renovations would yield.

To include the income but exclude the costs concededly necessary to generate that income is an irrational way to calculate the rate of return. Second, the LPC effectively punished Stahl for exercising its legal right to challenge the 2006 designation and preparing for redevelopment of the Buildings should that challenge succeed. Under the LPC's logic, in order for Stahl to succeed on its hardship application, it had to incur the massive costs to renovate the vacant apartments even though it would be demolishing these apartments if its legal challenge to the landmark designation succeeded. A property owner obviously should not be required to spend money renovating a property to obtain permission to demolish that same property.[9]

The renovation costs were a necessary expense for generating additional rental income for all of the Building's vacant apartments. The exclusion of half of the renovation costs was arbitrary and capricious.

E. The LPC's "Alternative" Calculation Was Flawed

The LPC also presented an "alternative" calculation which purported to fix the problems set forth above. This analysis purported to use the correct improvement parcel, apply the cost approach, and include renovation costs for all

[9] The lower court's opinion contains a lengthy critique of Stahl's methodology for calculating losses that would arise from future vacancies. (A52-56). The opinion suggests that this somehow relates to the LPC's "self-imposed hardship" finding, but it does not. Regardless of how vacancy losses are calculated, the LPC was not free to ignore renovation costs when calculating post-renovation return.

vacant apartments. (A1375-76). The LPC claimed that even in these scenarios, Stahl could earn a reasonable return. (A1376).

But the "alternative" calculation failed to eradicate the problems that plagued the remainder of the LPC's analysis. For example, the alternative calculation used real estate taxes calculated using the income approach, not the cost approach. (*Compare, e.g.*, A1382 *and* A1387, *with* A1389). The LPC made this same error for *every* renovation scenario. (*Compare* A1382-85, *and* A1387, *with* A1389; *compare* A1390-93, *and* A1395, *with* A1397). And the alternative analysis continued to exclude the renovation costs for the 44 vacant apartments from the depreciation calculation. (*See* A1386 (calculating depreciation based on renovations to 53 apartments); A1394 (same)).

The result was a reasonable return equation in which (1) in the denominator, assessed value was calculated under the cost approach using renovation costs for 97 apartments; (2) in the numerator, depreciation was determined by the cost approach, but only for 53 apartments; and (3) elsewhere in the numerator, real estate taxes were calculated using the income approach. Assessed value cannot logically mean three separate things in the same calculation. Had the LPC's alternative scenario in fact done what the LPC said it would do—namely, used the cost approach consistently—the LPC would have had to conclude that under any renovation scenario, Stahl would earn below 6% of the Buildings' assessed value.

(A1398-99, ¶¶ 2-3; A1402, ¶ 19; A1403, ¶ 22; A1404-05; A1406-07 (demonstrating that under every scenario, Stahl's return would be below 6%)).

CONCLUSION

For the foregoing reasons, this Court should reverse the Supreme Court's order denying Stahl's Article 78 petition and granting the City's motion to dismiss.

Dated: November 23, 2016

Respectfully submitted,

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SUPREME COURT OF THE STATE OF NEW YORK
APPELLATE DIVISION, FIRST DEPARTMENT

STAHL YORK AVENUE CO., LLC,

Plaintiff-Petitioner,

vs.

THE CITY OF NEW YORK; THE NEW YORK CITY LANDMARKS PRESERVATION COMMISSION; MEENAKSHI SRINIVASAN, in her capacity as Chair of the New York City Landmarks Preservation Commission,

Defendants-Respondents.

Index No. 100999-2014

PRE-ARGUMENT STATEMENT OF PLAINTIFF-PETITIONER STAHL YORK AVENUE CO., LLC

1. Title of the action: The title of the action is as captioned above.

2. Full names of original parties: The Plaintiff-Petitioner-Appellant is Stahl York Avenue Co., LLC ("Stahl"). The Defendants-Respondents-Appellees are the City of New York, The New York City Landmarks Preservation Commission ("LPC"), and Meenakshi Srinivasan, in her capacity as Chair of the LPC (collectively, the "City"). There has been no change to the parties since the commencement of the action.

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5. Appeal From: Decision, Order and Judgment of the Supreme Court, New York County dated January 8, 2016 and entered January 28, 2016.

6. Nature and object of the action: The lawsuit concerns the landmark designation of two buildings owned by Stahl and the LPC's subsequent denial of an application for a certificate of appropriateness to demolish the two buildings on the ground of insufficient return. Stahl's Verified Petition and Complaint alleged that the designation of the buildings was an unconstitutional taking under the United States and New York State Constitutions, and challenged the denial of the application under Article 78 of the New York Civil Practice Law and Rules as arbitrary and capricious and affected by an error of law.

7. Result reached below: In its Decision, Order and Judgment entered on January 28, 2016, the Supreme Court of the State of New York, County of New York (Stallman, J.) dismissed Stahl's Article 78 petition and granted the City's cross-motion to dismiss Stahl's Takings Claim.

8. Grounds for seeking reversal, annulment, or modification: The Supreme Court erred in dismissing Stahl's Article 78 petition and granting the City's cross-motion to dismiss.

Among other things, the Court committed legal error with respect to the denial of the Article 78 petition by (1) concluding that the relevant improvement parcel for assessing Stahl's application for a certificate of appropriateness constituted all of the buildings owned by Stahl on the city block, when the Landmarks Law required considering only the two buildings at issue in the certificate; (2) permitting the LPC to use a method for assessing the value of the buildings that was contrary to the LPC's administrative precedent, logically inconsistent, and incompatible with the purpose of the statutory provisions of the Landmarks Law at issue; (3) endorsing the LPC's exclusion of the cost of renovations for apartments that Stahl was legally required to renovate ; and (4) excluding certain renovation expenses, contrary to the statutory provisions of the Landmarks Law. In addition, the Court committed legal error with respect to Stahl's Takings Claim by, *inter alia*, (1) holding that all of the buildings owned by Stahl on the city block constituted the relevant parcel; (2) failing to adequately consider the severe deprivation of the buildings' economic value; (3) improperly deferring to the LPC's denial of Stahl's application in adjudicating Stahl's distinct constitutional claim; (4) and ignoring the effect of the City's actions in shaping Stahl's investment-backed expectations.

On September 22, 2014, Stahl filed a related complaint in the United States District Court for the Southern District of New York against Defendants the City of New York and the LPC, alleging that the LPC's denial of Stahl's application for a certificate of appropriateness violated Stahl's substantive due process rights under the Fourteenth Amendment of the United States Constitution. The District Court granted Defendants' motion to dismiss the Complaint. That decision is now pending on appeal before the United States Court of Appeals for the Second Circuit. *See Stahl York Avenue Co., LLC v. City of New York, et al.*, No. 15-2000.

There is no additional appeal in this action.

Dated: New York, New York
February 25, 2016

Respectfully submitted,

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