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LAND ACQUISITION MEMORANDUM #197

197-1 NEW YORK COURT OF APPEALS REVERSES SCRAP VALUATION OF RAPID TRANSIT PROPERTY AND AWARDS DEPRECIATED ORIGINAL COST VALUE WHERE CITY INTENDED TO CONTINUE IDENTICAL USE OF THE PROPERTY.

Appellants, Hudson Rapid Tubes Corporation, were the former owners of the rapid transit tunnel system connecting New York City and the New Jersey suburbs. Constructed in 1911 to service some 28,000,000 passengers yearly, the system had, in recent years, steadily declined in use and profitability until eventually forced into a bankruptcy reorganization in 1961. Under the reorganization, the tunnel property was placed in one corporation and the non-tunnel property in another. The corporations continued deficit operation until the New York Port Authority decided that the only way to continue efficient operation of this essential transportation link would be under public ownership. Consequently, the Port Authority Trans-Hudson Corporation exercised its power of condemnation over the property of the Hudson Rapid Tubes Corporation as well as over the property of the Hudson and Manhattan Corporation which owned the non-tunnel facilities.

The New York Supreme Court, Special Term, awarded the two corporations $55,000,000 as valuation of the railroad property--$30,000,000 for the tunnel property, $20,000,000 for the non-tunnel property, and $5,000,000 for "going concern" value--and awarded 6 percent interest on the New Jersey property and 4 percent on the New York property. The Special Term had ascertained value as a return of original investment in the property minus the depreciation already taken out. The fact that the city was going to continue identical operation was deemed justification for finding a "going concern" value.

The Supreme Court, Appellate Division, modified the award of the lower court to $3,500,000, using scrap valuation as the basis for determination. In reaching this conclusion on the Appellate Division reasoned that there was no market for the property outside the condemnor and therefore loss due to condemnation should be the amount that otherwise could have been obtained on the public market. Since there was no public market--the facility was admittedly a deficit operation--the tunnel property was worth nothing in terms of owner's loss. Similarly, since the other facilities were specially adapted to the unusually small size of the Hudson Tubes,

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their only market value would be as scrap. The Appellate Division also refused to recognize any worth in the facility as a going concern and reduced the interest rate on the New Jersey properties to 4 percent.

In reversing the Appellate Division's determination based on scrap valuation, the Court of Appeals, through Judge Keating, emphasized that the property could be, and would be, put in service by the city at minimal cost thereby contradicting the Appellate Division's conclusion that the property's only value was for scrap. While the court framed its discussion in broad equity terms, it was obviously quite concerned with the fact that the facility was not going to be scrapped but instead would be continued in its present use. Viewing the situation in this manner, the court deemed it most appropriate to consider what an equivalent facility would cost the city today. Judge Keating noted that the cost of constructing a facility capable of handling a similar volume of passengers would be in excess of $400,000,000 at current construction prices. Repair of the present system would only cost $88,000.

Although it used replacement value as a justification for raising the condemnation award, the court did not use replacement cost as the measure of the award but simply as an indication that scrap valuation was inadequate. The court then noted the many physical limitations of the present system and acknowledged that any replacement would be a far superior facility and, in fact, would most probably not be in the form of a rapid transit operation. Having thus demonstrated that any replacement valuation would be a gross exaggeration of the value of the present operation, the court concluded that reimbursement for depreciated initial investment would fairly represent the present value of the system while not overcompensating for its many limitations.

Having concluded that the system was worth more than scrap, the court then challenged the Special Term's finding of "going concern" value without a clear showing that there was an ascertainable value in the existence of operating schedules, records and procedures. The court was unwilling to find any inherent "going concern" value and, in an apparent contradiction, cited the present deficit operation of the system as evidence that there was no value as a "going concern."

Finally, the court restored the 6 percent interest rate on the New Jersey property since it was not an unconstitutional rate. It concluded that the Appellate Division had erred in reducing the rate because of the deficit operation of the system, pointing out that the factor of deficit operation was already considered in the principal award.

In a vigorous dissent, Judge Burke took issue with the majority's adoption of a depreciated cost valuation. Disputing the court's attention to the taker's gain rather than the owner's loss, he pointed out that "the property in the case at bar has utility only in the hands of the petitioner which has the financial capacity to engage in a deficit operation, whereas

it is conceded that no private investors can be found who would undertake such an operation." The dissent further argued that the existence of a public need for the property should not serve to inflate the value of a facility which is otherwise "inherently incapable of profitable operation."

SUMMARY

The case represents a somewhat unique approach to the very difficult problem of valuing a specialty property. Ordinarily, where there is no comparable property against which to make a relative valuation, the courts will consider the cost of replacement or duplication of the improvements condemned to find an appropriate value. However, only last year, in the Casamassima case, the New York Court of Claims reaffirmed the rule that property could not be considered a specialty when it is used for the same purpose both before and after the condemnation. On the other hand, the litigation over the condemnation of the Polo Grounds also established that replacement cost was totally inappropriate where the facility condemned, albeit a specialty, was extremely outdated and admittedly obsolete and inadequate. Faced with these limitations, the court avoided treating the property as either a specialty or a going concern. Instead, it used scrap and replacement values as the polar extremes for reaching a more moderate and equitable award.

The award of depreciated original cost, while founded on no apparent judicial precedent, afforded the court a reasonable alternative to condemning as scrap property which would be continued in identical use. On the other hand, the condemnees, having no public market and having received a return on original investment, should have no further complaint against a city which will be operating what was, for the condemnees, a losing proposition.

A point of particular interest in this case is the apparent conclusion of the court that where there is a current demand for the services provided by a facility even though there is no market demand for the facility itself, such a demand will warrant some consideration of replacement cost and going concern value. This would be distinguishable from the Polo Grounds situation where the withdrawal of the baseball franchise and the construction of a new ballpark in Flushing Meadows eliminated both the public demand for the facility's services and the market demand for the facility itself. (Port Authority Trans-Hudson Corp. v. Hudson Rapid Tubes Corp., 20 N.Y.2d 457, 231 N.E.2d 734 (1968)).

197-2 NEW YORK SUPREME COURT, APPELLATE DIVISION, HOLDS THAT BOARD OF ESTIMATES MAY NOT REFUSE REDEMPTION OF FORECLOSED PROPERTY WHERE THE CITY HAS NO USE FOR THE PROPERTY.

Petitioner was delinquent on his taxes for certain business property and the City placed a tax lein on the property which it subsequently foreclosed. The value of the property was in excess of $145,000 and the delinquent taxes, plus charges, amounted to $50,467.06. Petitioner tendered the proper amount of delinquent taxes and filed for redemption of his property.