DEVELOPER § 1983 CLAIMS, CITY BAILOUT BONDS, POTHOLE LAW

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Last month the Court of Appeals set high hurdles for developers seeking damages under 42 U.S.C. § 1983 for land-use permit denial (*Bower Assoc. v. Town of Pleasant Valley*); upheld the New York City bond bailout statute, the MAC Refining Act, against constitutional challenge (*Local Government Assistance Corp. v. Sales Tax Asset Receivable Corp.*); and addressed the "Pothole Law" and comparative negligence (*Bruni v. City of New York*).

§ 1983 PERMIT DENIAL CLAIMS

In *Bower Assoc. v. Town of Pleasant Valley* and *Home Depot, U.S.A., Inc. v. Dunn*, decided together, the Court of Appeals affirmed the dismissal of claims brought under 42 U.S.C. § 1983 for wrongful denial of land-use permits. The federal statute permits federal or state law damages actions in the land-use context for violation of property owners' rights to due process, equal protection or just compensation for the taking of property. The Court's opinion expresses its concern that the statute not be used as simply another vehicle for imposing oversight on local land-use decisions.

Both appellants had been successful in article 78 proceedings in having the denial of their permit applications overturned as arbitrary and capricious. In an opinion by Chief Judge Judith S. Kaye, the Court explained that establishing a § 1983 claim requires significantly more.

In order to prove a violation of substantive due process, a claimant must establish first, that it had a "vested property interest," and second, that the government action was "wholly without legal justification." As to the first hurdle, the Court rejected the argument that when an issuing authority acts outside of its discretion in rejecting an application it necessarily deprives the applicant of a protected property interest: "While the existence of discretion in a municipal actor does not alone defeat the existence of a property interest in a permit applicant, that discretion must be so narrowly circumscribed that approval is virtually assured."

As to the second hurdle, the Court drew a distinction between the arbitrariness that will suffice to overturn government action in an article 78 proceeding and "constitutional[]" arbitrariness. The latter involves "egregious" conduct. As an example of when municipal conduct rises to that level, the Court referred to its decision in *Town of Orangetown v. Magee*, 88

N.Y.2d 41, 53 (1996), in which the Town's actions were found to be "without legal justification and motivated entirely by political concerns."

Proving an equal protection violation also involves a two-step process of showing (1) selective treatment (2) based upon impermissible considerations such as race, religion, the exercise of constitutional rights or "malicious or bad faith intent to injury a person." Home Depot, which had raised the equal protection claim, was unable to show either that it had been treated differently that others similarly situated or improper motive. Even a decision to reject a permit application based upon political considerations would not constitute the requisite intent to injure, the Court stated. That element of the claim requires "proof that the applicant was singled out with an 'evil eye and an unequal hand'." (Quotation omitted.)

BAILOUT MAGIC

The Court in *Local Government Assistance Corp. v. Sales Tax Asset Receivable Corp.*, in an opinion by Judge George Bundy Smith (Judge Robert S. Smith taking no part), unanimously held that the MAC Refinancing Act (the "Act"), enacted as part of the State's 2003 budget bill when the Legislature overrode the Governor's veto, did not violate the State or Federal Constitutions.

The 2003 legislation was spawned by a looming financial crisis in New York City. The crisis resulted from the City's obligation to pay $2.5 billion over the ensuing 5 years in debt service on Municipal Assistance Corporation ("MAC") long-term bonds coming due in 2008. The Act permitted the City to receive State sales tax revenues previously paid directly to MAC, thereby covering the City's debt service obligation. At the same time, the Act required the State, through the Local Government Assistance Corporation ("LGAC"), to make 30 annual payments of $170 million each to the City ($5.1 billion). These payments were to be used to finance bonds issued by a public benefit corporation, the proceeds of which would be used to pay off the City's MAC debt. LGAC brought an action in the Supreme Court, Albany County, to declare the Act unconstitutional. All in all, a political, legislative and judicial *tour de force*, to say the least.

MAC REFINANCING ACT

LGAC was created in 1990 as part of a State fiscal reform program and issued $4.7 billion of its own bonds to provide funding for public services. Under that legislation, the bondholders of LGAC were given first priority on State sales and use tax collections from which the bonds were to be paid. They also received pledges that no equal or prior lien could be created to impair their rights, and that the State would not change LGAC's right to carry out its obligations to the bondholders or do harm to the bondholders' rights.

The Chairperson of LGAC each year certifies to the Governor and Comptroller how much LGAC needs to cover debt service and other expenses. Under what has been aptly described as the "trapping mechanism" in the legislation creating LGAC, only after LGAC gets from the Legislature the certified amount can money in the State Tax Fund go into the State's Treasury. While the Legislature is not required to appropriate the amount LGAC certifies it requires, under the circumstances the Legislature has always provided LGAC with that amount.

The 2003 Act required LGAC to make annual payments to the City of $170 million until 2034 and to include the $170 million payment in its annual certification to the Governor and Comptroller. The legislation also permitted the Mayor of the City to assign the $170 million payments to a not-for-profit public benefit corporation.

After the Act was passed, Mayor Blumberg made an irrevocable assignment to Sales Tax Asset Receivable Corporation ("STARC"), a not-for-profit corporation, and LGAC was therefore obligated to make the $170 million annual payment directly to STARC. STARC would then issue bonds financed by the $170 million payments, and the proceeds from the bonds would be used to pay off the City's $2.5 billion MAC debt.

In its lawsuit, LGAC asserted that the Act violated the State Constitution by imposing upon the State a multi-year payment obligation without a referendum for a legislative appropriation, and because the City's assignment to STARC represented the contraction of debt by the City without a pledge of its full faith and credit. LGAC also claimed that the Act violated the United States Constitution by impairing the contract rights of the LGAC bondholders.

After the Act became law, LGAC sought a preliminary injunction to prevent STARC from issuing its bonds. The motion was denied in the motion court, but the Appellate Division, Third Department, reversed and issued a preliminary injunction pending an appeal to the Court of Appeals. STARC and the City then moved in the motion court for summary judgment declaring the Act constitutional and LGAC cross-moved to declare the Act unconstitutional. STARC and the City's motion was granted; the Appellate Division, with one Justice concurring in part and dissenting in part, *inter alia*, modified in part the order below and held that the portion of the Act that eliminated the need for an annual legislative appropriation violated the State Constitution. Both sides appealed to the Court.

The Court, in reinstating the order of the motion court declaring the Act constitutional, noted at the outset the heavy burden on LGAC to (1) overcome the presumption of constitutionality which attaches to every statute, particularly those concerning public financing programs, and (2) "prove beyond a reasonable doubt" that the Act suffered "wholesale" constitutional impairment.

The Court in a detailed opinion then proceeded to describe the Act as an expression of the Legislature's intention to enact a constitutionally sound statute under which the State would assist the City in meeting its MAC obligations. It held that the annual payments to be made by LGAC were in fact made through annual legislative appropriations and therefore the Act did not violate the State constitutional prohibition against incurring debt without a public referendum.

The Court also concluded that the Act did not violate the State Constitution by permitting the City to assign to STARC its right to receive LGAC's annual $170 million payment. The assignment, in exchange for the proceeds of the sale of the STARC bonds, the Court found, was not a debt of the City that would require the City to support the obligation with a pledge of its full faith and credit; the City had not undertaken any legal obligation to fund STARC's debt service to its bondholders in the event of STARC's default.

Finally, the Court held that the Act did not violate the United States Constitution (Article 1, § 10) by "impairing the Obligation of Contracts." LGAC argued that the Act impaired the priority given to the bondholders of LGAC under bond resolutions and the pledge by the State that it would do nothing to impair the bondholders' rights. The Court rejected this assertion because there was no expression by the Legislature in passing the Act of any intent to modify the State's pledge to the LGAC bondholders and it would be inappropriate to find an implied repeal or modification of the pledge. The Court also found no expression of intent by the Legislature to give STARC bondholders an equal or greater priority than LGAC bondholders, an issue that was conceded by STARC in the offering documents for the sale of its bonds.

It is surely noteworthy that at several points in the Court's opinion it made clear it was not passing judgment on the "wisdom" of the Act, but only its legality.

POTHOLE LAW

The Court resolved two open issues of interpretation of NYC Admin. Code § 7-201[c], the so-called Pothole Law, and reversed the verdict for plaintiff due to the trial court's refusal to give a comparative negligence charge, in *Bruni v. City of New York.*

Joseph Bruni left his home before sunrise one morning to go to a local grocery store. On his way home from the store, Bruni took a route that he had never taken before because it was shorter than his usual route, and looking straight ahead while walking stepped in a hole in the street caused by a defective catch basin. He sustained injuries, including a broken jaw. The New York City Department of Transportation ("DOT") did not have notice of the hole. Instead, a complaint had been received by the Department of Environmental Protection (DEP), which is responsible for catch basins. A DEP foreman inspected the site, blocked off the hole with sawhorses and traffic cones, and completed a report and repair work order form. When Bruni fell 39 days later, the sawhorses and cones had been removed.

The Pothole Law provides three alternative prerequisites to maintaining a property damage or personal injury claim against the City arising out of a street or sidewalk being out of repair, unsafe, dangerous or obstructed. The condition must have at least 15 days earlier been the subject of: (1) written notice to the DOT; (2) previous injury to property or a person with written notice to a City agency; or (3) "written acknowledgement from the city." The claim at issue involved the third alternative.

The Court first answered whether the acknowledgement must come from the DOT, a question it had left open in *Laing v. City of New* York, 71 N.Y.2d 912 (1988). In *Laing,* the Court had found that a Parks Department report noting a crack in the sidewalk but generated in connection with tree-pruning and not sidewalk repair, did not constitute "acknowledgement from the city." In *Bruni,* by contrast, the DEP reports were generated in connection with the street repair. The Court held that written acknowledgement can come from an agency other than the DOT "where, as here, that other agency is performing the function (normally performed by DOT) of remedying an unsafe condition in the roadway."

The Court also rejected the City's argument that internal documents cannot constitute acknowledgements. In its unanimous decision by Judge Robert S. Smith, the Court looked to the purpose of the relevant subdivision of the law - to eliminate written notice to the DOT "where there is documentary evidence . . . to demonstrate that the responsible City agency knew of the hazard and had an opportunity to remedy it." The DEP foreman's two reports here served that purpose.

Finally, the Court reversed the $1.6 million plaintiff's verdict, without deciding whether the award was excessive, because the jury had not been given a requested comparative negligence charge. Comparative negligence, an issue of fact, should be submitted to the jury "if there is a valid line of reasoning and permissible inferences from which rational people can draw a conclusion of negligence on the basis of the evidence presented at trial." The Court found "at least" two ways in which a jury could have found plaintiff failed to exercise due care, either by taking an unfamiliar route in the dark or by looking straight ahead while walking rather than at the ground in front of his feet.