

Memorandum 73-30

Subject: Study 36.175 - Condemnation (Compensation for Loss of Goodwill)

Background

At the March 1973 meeting, the Commission requested the staff to prepare a statute that would compensate for business losses along the lines of the Vermont statute that authorizes the awarding of business losses generally, without provision for specific standards and procedures, leaving it to the courts to implement. Such a provision is attached as Exhibit I. This memorandum is intended to point out some of the issues that will undoubtedly arise under a provision such as this. The staff concludes that such a broad provision is not desirable and suggests some general limitations to shape the business loss statute. A copy of the earlier memorandum containing sample business loss statutes is attached.

Problems Under the Vermont Statute

The Vermont statute that authorizes compensation for business losses generally is Vermont Statutes Annotated, Title 19, Section 221(2):

Damages resulting from the taking or use of property under the provisions of this chapter shall be the value for the most reasonable use of the property or right therein, and of the business thereon, and the direct and proximate lessening in the value of the remaining property or right therein and the business thereon.

This provision was enacted in 1957 to change the common law which allowed no recovery for business losses; it has stood unamended. Since 1957 there have been at least eight cases before the Supreme Court of Vermont requiring clarification and application of the business loss portion of the statute:

Record v. Vermont Highway Board, 154 A.2d 475 (1959)
Penna v. State Highway Board, 170 A.2d 630 (1961)

Colson v. State Highway Board, 173 A.2d 849 (1961)
O'Brien v. State Highway Board, 190 A.2d 699 (1963)
Fiske v. State Highway Board, 197 A.2d 790 (1964)
Flake v. State Highway Board, 209 A.2d 482 (1965)
Gibson Estate v. State Highway Board, 258 A.2d 810 (1969)
Young v. State Highway Board, 290 A.2d 29 (1972)

Of the numerous issues raised in these cases, the following are noteworthy:

(1) What are the elements composing business loss: Do they include temporary disruption of the business, moving costs, cost of replacing equipment, lost profits?

(2) If lost profits are to be included, for what length of time should they be extended?

(3) Should the business losses be offset by benefits to be conferred by the project, the reasonable rental value of the land on which the business was located, the services of an owner-manager, the reestablishment of the business elsewhere?

Lessons of the Vermont Experience

A general statute such as the Vermont statute or the draft statute attached as Exhibit I requires substantial interpretation by the appellate courts. Based on the Vermont experience, the enactment of such a statute in California would be bound to generate a great amount of litigation and, without a doubt, many cases that can now be settled would be tried in the courts.

The staff believes that it is poor legislative draftsmanship as well as poor public policy to draft a general rule that must be implemented in toto by the process of trial and appeal.

If the Commission desires nonetheless to provide a general business loss statute without imposing much detail, the staff believes that there are only two practicable alternatives. One is to enact a general statute that provides

some sort of framework to indicate the broad outlines of the right to recover for business losses. For instance:

(1) Where a business is located on the property taken and is relocated, damages for temporary disruption and for lost profits should be limited to a period of time reasonably necessary to reestablish the business; goodwill should be awarded only to the extent it is not transferable to a new location.

(2) Where a business is located on the property taken and is not relocated, business losses should be offset by amounts received on liquidation of assets; perhaps in this situation lost profits should be limited to a reasonable period of time, e.g., seven years.

(3) Where a business is located on the remainder, the business loss should be offset by any benefits to the business conferred by the construction of the project. Consideration should be given to limiting recovery for lost profits in this situation to a reasonable period of time.

(4) It may be helpful in any of the above cases to indicate more specific rules for computing business loss, including deductions for the reasonable rental value of the land and the services of the manager-owner.

An alternative to this scheme that would be much simpler and provide a somewhat more certain standard would be simply to allow recovery for loss of "goodwill." Goodwill is measurable and limited; a general statute could accomplish this.

We will defer preparation of a more detailed statute pending further direction from the Commission. We have also attached a copy of the earlier memorandum (Memorandum 73-22) containing sample business loss provisions for the Commission's further consideration.

Respectfully submitted,

Nathaniel Sterling
Staff Counsel

EXHIBIT I

§ 1245.640. Business losses

1245.640. (a) Where a business is conducted on property acquired by eminent domain or on the remainder if such property is part of a larger parcel, the owner of the business shall be compensated for any damage to the business caused by the taking.

(b) Compensation shall be allowed under this section only to the extent the damage to the business is not compensated under Section 7262 of the Government Code.

Comment. Section 1245.640 is new to California eminent domain law. Under prior court decisions, compensation for business losses in eminent domain was not allowed. See, e.g., Oakland v. Pacific Coast Lumber & Mill Co., 171 Cal. 392, 153 P. 705 (1915). Section 1245.640 is based upon Vermont Statutes Annotated, Title 19, Section 221(2).

Section 1245.640 compensates for business losses only to the extent those losses are not compensated by Government Code Section 7262 (moving expense and moving losses for relocated business or farm operations; in lieu payments for business or farm operation that cannot be relocated without a substantial loss of patronage).