

# Memorandum

To: CHAIR AND COMMISSIONERS

CTC Meeting: March 15-16, 2006

Reference No.: 2.4d.(3)  
Action Item

From: CINDY McKIM  
Chief Financial Officer

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Division Chief  
Right of Way and Land Surveys

Ref: DIRECTOR'S DEEDS

## RECOMMENDATION:

The Department of Transportation (Department) recommends the California Transportation Commission (CTC) authorize the execution of a Director's Deed and an Assignment of Contract of Sale. The conveyance of excess State-owned real property, including exchanges, is pursuant to Section 118 of the Streets and Highways Code. The items included on this agenda involve a current value of \$4,050,000. The net proceeds will be divided approximately 56% to the State and 44% to the local agency in proportion to the respective contributions of the parties to the acquisition cost of the exchange parcels. A recapitulation of the items presented follows. Maps and photographs are attached.

01-04-Mrn-101 PM 10.1	San Rafael
Disposal Unit DD 054600 01 01	57,780 sf
(054599 X1 X1)	73,883 sf
Convey to Francisco Boulevard Investors, LLC	\$4,050,000 (Appraisal \$4,050,000)

The State is acquiring Parcel 54598 containing 12,443± square feet from Francisco Boulevard Investors LLC (aka, Sonnen Motorcars, hereinafter "Sonnen" referenced herein as an individual) for the State Route (SR) 101 HOV lane project in the City of San Rafael. This area was used for automobile display and customer parking as illustrated on attached Exhibit A. Sonnen has two and one-half acres in his current facility and he previously operated three automobile dealerships on this property. He asserts he was grandfathered into the existing facility with Audi, Volkswagen, and Porsche dealerships, having obtained these franchises in the early 1990's and having operated them successfully for a number of years.<sup>1</sup> Because the acquisition triggers new site requirements by the franchisers to accommodate current marketing strategy, Sonnen relocated the Porsche operation to

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<sup>1</sup> This acquisition is currently in litigation with trial pending in the Marin County Superior Court. The issues are therefore presented in the context of Sonnen's claims or allegations and by this document the State does not concede or acknowledge the validity thereof. The issues are presented so that the Commission may assess the potential legal and monetary exposure relative to the exchange and assignment of the subject excess parcels.

Mill Valley in anticipation of the State's pending project. He has asserted that the move was required in order to partially mitigate damages caused by the State's acquisition.

Based on the opinion of District legal counsel and the State's appraiser, the best approach to the mitigation of the loss of business goodwill and severance damages resulting from the post acquisition non-conforming status of the franchises would be to convey Parcel 054600-01-01 to Sonnen, along with the assignment of the State's rights to the remainder of Parcel 054599-X1-X1, as an exchange for State's requirements from Parcel 54598. Under the proposed exchange, the State will convey Parcel 054600-01-01 (57,780 square feet) to Sonnen and assign its rights to Parcel 54599-X1-X1 (73,883 square feet), for a total transfer of 131,663 square feet, or approximately three acres.

The following key points summarize the extensive and compelling support for this exchange:

- The area of the State's acquisition was primarily used for pre-owned automobile display, which comprised a substantial portion of Sonnen's revenue.
- The State's acquisition has left Sonnen at well below the franchisers' space requirements for the dealerships. Though previously grandfathered in with lesser space requirements, a decrease in land area triggers new franchise lot and space requirements and would allow the cancellation of the existing franchise agreements.
- Under existing hazardous waste mitigation plans, Parcel 054599-X1-X1 cannot be developed for up to six and one half years because of Department of Toxic Substance Control (DTSC) mandatory cleanup requirements.
- An existing easement in favor of Sonnen, DTSC clean-up requirements, and City of San Rafael parcel development and land use restrictions are significant factors limiting the State's likelihood of success in obtaining full fair market value for the excess parcels at a public auction.
- Without the exchange and assignment, the State will be subject to extensive, costly claims for severance damages and loss of business goodwill. Sonnen is claiming in excess of \$10 million for these and other damages and is expected to claim up to \$12 million should the matter proceed to trial.
- In the event of trial, a jury verdict could be in the \$8-10 million range.
- Pre-trial litigation costs are estimated to range from \$300,000 to \$600,000 for each party. If the matter proceeds to trial and the State is unsuccessful in defending the action, it could be subject to an estimated additional \$800,000 to \$1,350,000 for Sonnen's attorneys' fees and other recoverable costs.
- The settlement saves the State several million dollars in severance damages and loss of business goodwill claims.

### **STATE'S ACQUISITION**

The property being acquired from Sonnen by the State is as follows:

- 12,443 square feet in fee from the front of the automobile dealership.

- 1,334 square foot permanent easement for utility purposes across the front of the remaining property.
- 1,334 square foot temporary construction easement for a term of one year in the same area as the permanent utility easement.

The State's 12,443 square foot fee acquisition from the front of the dealership consists of a paved and landscaped area divided into four rows of mixed-use automobile display and customer parking. This was the only area available for customer parking. Because of the configuration of the lot and the location of the existing building, the fee acquisition reduces the front display and parking area of the property by approximately 50 %.

The loss of the automobile display area potentially impacts Sonnen in two ways. The franchise agreements require the dealer's property be of a size sufficient to sell pre-owned automobiles. The agreements base the number of new automobiles provided to the dealership on both the overall size of the property and the number of pre-owned automobiles sold. The State's acquisition places Sonnen in non-compliance on both points.

#### **ELEMENTS OF COMPENSATION IN THE PENDING EMINENT DOMAIN ACTION RELATIVE TO THE EXCHANGE AND ASSIGNMENT**

A partial acquisition of property on which an ongoing, profitable business is being conducted entails various elements of compensation. In the action to acquire the Sonnen property, the State is facing several claims of compensation, including compensation for the real property interests being acquired, severance damages to the remaining land and buildings, and loss of business goodwill. The estimated total value of these claims range from the State's low-end estimate of \$3.75 million to Sonnen's high-end estimate of \$10.41 million. A summary comparison of the State's values and those of Sonnen for the various elements of compensation is illustrated in Exhibit B, attached.

The proposed settlement involves the exchange and assignment of the two excess parcels to mitigate the severance damage and loss of business goodwill claims. In brief, the settlement provides that Sonnen will be compensated \$3,000,000 for the State's acquisition, inclusive of all claims of severance damage, loss of business goodwill, costs, fees and interest. Sonnen will pay \$4,050,000 for the acquisition of State's excess Parcel 054600-01-01 and the assignment of the State's contract of sale to Parcel 054599-X1-X1. The settlement terms also include a dismissal of all pending lawsuits and a waiver of Sonnen's \$750,000 claim for reimbursement of costs associated with relocating the Porsche dealership. Settlement on this basis avoids costly and time-consuming litigation and exposure to a jury verdict, which could be in the \$8 to 10 million range.

Exchange and assignment of both excess parcels is necessary in order to restore the "before" functionality of the Sonnen operation. As previously indicated, Sonnen operated three automobile dealerships on the property by virtue of being grandfathered into lesser space requirements. However, Sonnen asserts that pursuant to the governing franchise agreements, any alterations to the dealerships, particularly with respect to the physical space, can result in termination of the existing franchise agreements and imposition of new lot and space requirements.

Although there is some disparity between the parties as to the compensation due for the fee and easement interests being acquired, the main areas of disagreement concern the amount of damages arising from severance and loss of business goodwill. Both are based on Sonnen's inability to satisfy the lot and space requirements that he claims would be imposed as a result of the State's acquisition. The State's appraiser has estimated severance damages in the range of \$735,000 to \$1,315,000. This is because, as previously discussed, without the exchange of Parcel 054600-01-01 and the assignment of the State's interest in Parcel 054599-X1-X1, Sonnen would no longer satisfy franchise dealership requirements and the remaining land and improvements could only be used for independent, unaffiliated automobile sales.

Sonnen's claim for loss of business goodwill is based upon his verified claim that he would lose one, if not both, of his remaining franchises due to failure to meet the minimum space requirement. He has asserted that representatives from Audi, Volkswagen and Porsche, along with other industry representatives, will support his claim. In discovery, the State determined that Sonnen's claim could potentially be construed as consistent with the provisions of the franchise agreements. Sonnen's appraiser estimated the value of business goodwill to be at least \$5,000,000 and claims that, without mitigation provided by the excess parcels, all of the business goodwill value will be lost as a result of the State's acquisition. The State's business goodwill appraiser agreed that because the front display area is a substantial component of the business, a reduction in that area would result in a reduction in the overall gross income of the business. A reduction in automobile sales in excess of 10% resulting from the acquisition of the automobile display and customer parking spaces could potentially cause a total loss of business goodwill.

### **THE EXCHANGE PARCELS**

#### **Parcel 054600-01-01**

The State acquired this parcel, which is contiguous to Sonnen on the northwesterly side, in 2002 with the intent to use it to mitigate a portion of Sonnen's severance damage and loss of business goodwill claims. Under the terms of the proposed settlement, it is to be conveyed to Sonnen for \$34 per square foot for 57,780 square feet, totaling \$1,964,520. A small portion of the parcel requires remediation under the DTSC action on the adjoining property (Parcel 054599-X1-X1). Under the proposed settlement, the State will convey this parcel to Sonnen in partial mitigation of severance damage and loss of business goodwill claims.

- Parcel 54600-01-01 is approximately 113 feet wide. If it were divided laterally, allowing for the required minimum 60-foot width required for independent development under the current zoning (General Commercial/Francisco Boulevard West Commercial District), the remaining 53± foot wide parcel would be of minimal value to the adjoining property on the north. Parcel 54601, is fully developed with buildings sited away from Parcel 054600-01-01 and the additional property would create a maintenance and security concern on the isolated south side of the existing building.

If the parcel were divided parallel to Francisco Boulevard West, with a portion retaining full frontage on Francisco Boulevard West, the following considerations would apply:

- The total parcel area is 57,780 square feet. The parcel dimensions are approximately 113 feet wide, by 510 feet long. This parcel's shape presents development difficulties in that it is long and narrow. Retail commercial properties depend on frontage and width for optimum building identification and adequate parking and circulation. If the site were divided, an access road to Francisco Boulevard West must be preserved for the parcel to the rear. The rear parcel would be a small commercial flag lot and would have limited value. A parcel without frontage in this area would most likely be used for vehicle storage. Judging from contemporaneous paired sales of former railroad right of way located to the rear of Francisco Boulevard West and a frontage sale on Francisco Boulevard East (I-580), this rear parcel may sell in the range of 40% to 60% of fee value.
- Compounding this physical impediment to development is the fact that Parcel 54600-01-01's location within the Central San Rafael Redevelopment Area would require any new development or renovation plans to obtain Project Selection Process approval before permits could be granted.
- The Project Selection Process would grant approval only to those projects that are determined to be 'high priority' i.e., those projects that would produce limited traffic capacity on the load-strained city streets. The criteria for determining 'high priority' are defined as high tax generating uses, affordable housing projects, and community service or public benefit projects. The subject site would be most suited to a high tax-generating user in this location. However, the size of the frontage parcel would preclude high tax generating businesses from considering the site.
- The City's highest tax revenue generators are Sonnen Motorcars II, LLC, Home Depot and RAB Motors, Inc. Interviews with brokers, buyers, sellers, and City Planning staff painted a clear picture of the City's preference for automobile dealerships in this area. The Lexus site, located across SR 101 from the subject on Francisco Boulevard East, was presented to the City as a big-box retail site twice and refused approvals until a car dealership was proposed and approved in 1999. The likely requirement that a business generate over \$300,000 in annual sales tax revenue to the City restricts smaller retail businesses and favors those businesses with a regional draw such as big-box retailers and automobile dealerships.
- The most recent developments on Francisco Boulevard West are big-box retail and automobile related sales. With one acre or less, the parcel could languish indefinitely in a planning limbo. A buyer would most likely try to option the property while attempting to obtain development permits or would expect a heavily discounted sales price to reflect the high risk of development.

Under either scenario, Parcel 54600-01-01 has very limited appeal and value as a stand-alone parcel. It is approximately four-feet below grade, narrow, relatively small, would require an access easement to the rear parcel under one proposed development scheme, and is unlikely to receive development permits. For these reasons, in terms of a hypothetical value, the parcel may sell in the range of 40% to 60% of fee value.

**Parcel 054599-X1-X1**

In 2004, the State was able to negotiate a contract, which included the right to acquire the excess remainder of Parcel 054599-X1-X1. Under the terms of the proposed settlement, Sonnen is to pay \$28.23± per square foot, for 73,883 square feet for a total of \$2,085,480 for the assignment of the State's rights under the contract of sale for Parcel 054599-X1-X1. As previously discussed, the parcel has extensive contamination and, in addition to the extensive and time-consuming DTSC ordered hazardous waste cleanup, is below grade and requires approximately four feet of fill. The parcel is further encumbered by a 20-foot easement for ingress and egress in favor of Sonnen, which divides the parcel perpendicularly to Francisco Boulevard West and then across the rear to connect to Sonnen's parcel behind its major existing improvements, as illustrated on the attached parcel map.

Under the settlement, the State will assign its rights to the immediately adjacent Parcel 054599-X1-X1 to Sonnen in further mitigation of severance damages and loss of business goodwill claims. Parcel 054599-X1-X1 is subject to DTSC enforcement due to extensive contamination. The owners of title are currently conducting the cleanup. In assigning the contract of sale to Sonnen, the State is released and discharged from any liability for Parcel 054599-X1-X1.

Under the timeline for the cleanup of Parcel 054599-X1-X1, it is possible that the State would not be able to acquire title and sell this property at a public auction until December 2010. The property would be sold with a recorded deed restriction that may prohibit any subsurface excavation. This would likely reduce the open market value of the property by as much as 50%. In addition, the property is subject to the Sonnen easement and is located in the City of San Rafael's Francisco Boulevard West Commercial Zone District and is subject to the same development constraints as Parcel 054600-01-01.

**SUMMARY**

There is little dispute that the State's acquisition of the front display space from the Sonnen property will have an adverse impact on the operation of the business as currently conducted, with the extent of the loss to be determined by a jury. A review of eminent domain verdicts over the past ten years shows that juries have rendered numerous verdicts for businesses in similar factual situations in the \$8 to \$10 million range. Without the exchange of the excess parcels, which mitigate his damages, as illustrated in attached Exhibit B, Sonnen has claimed losses in excess of \$10 million and is expected to claim even higher losses in the event of trial.

Settlement of this action came after extensive negotiations and eight mediation sessions with the Honorable Richard Patsey (Retired). Judge Patsey recently retired from Contra Costa County Superior Court with over 30 years of experience. He is familiar with eminent domain law and has a reputation for fairness. He understood the need to deal with the intangible claims asserted by Sonnen and refuted by the State. Both parties agreed that the settlement saved each of them potential pre-trial litigation costs in the range of \$300,000 to \$600,000 for the eminent domain action. In addition to these costs, if this matter proceeded to a jury trial and the State was unsuccessful in defending the

action, it would have to pay attorney's fees and other recoverable costs to Sonnen. These fees and costs are estimated to be in the range of \$800,000 to \$1,350,000.

# EXHIBIT A



PARTIAL TAKE AREA



PARTIAL TAKE AREA

## **EXHIBIT B**

### **COMPARISON OF VALUATION ESTIMATES AND COSTS**

	<b><u>STATE</u></b>	<b>TAKE</b>	<b><u>SONNEN</u></b>
<b><u>Real Estate:</u></b>			
Fee	\$ 530,000		\$ 740,000
TCE	\$ 5,000		\$ 10,000
PUE	\$ 15,000		Included in land value
Improvements	\$ 62,215		Included in land value
Relocation and repairs (paving, landscaping, sign)	\$ 102,221		\$ 160,000
Severance damages	\$ 735,000-\$1,315,000		\$3,150,000*
<b><u>Business Losses</u></b>			
Relocation of Porsche Dealership			\$ 750,000
Loss of Business Goodwill	\$1,200,000-\$2,400,000		\$5,000,000
<b><u>Litigation Costs</u></b>			
Pre trial	\$ 300,000-\$600,000		\$ 300,000-\$600,000
Potential Litigation Cost Award to Sonnen <sup>1</sup>	\$ 800,000-\$1,350,000		
<b><u>Total Financial Exposure</u></b>	<b>\$3,749,436 - \$6,379,436</b>		<b>\$10,110,000 - \$10,410,000</b>

\*Figure reflects assumption of Sonnen's appraiser that Sonnen would be able to acquire Parcel 054599-X1-X1

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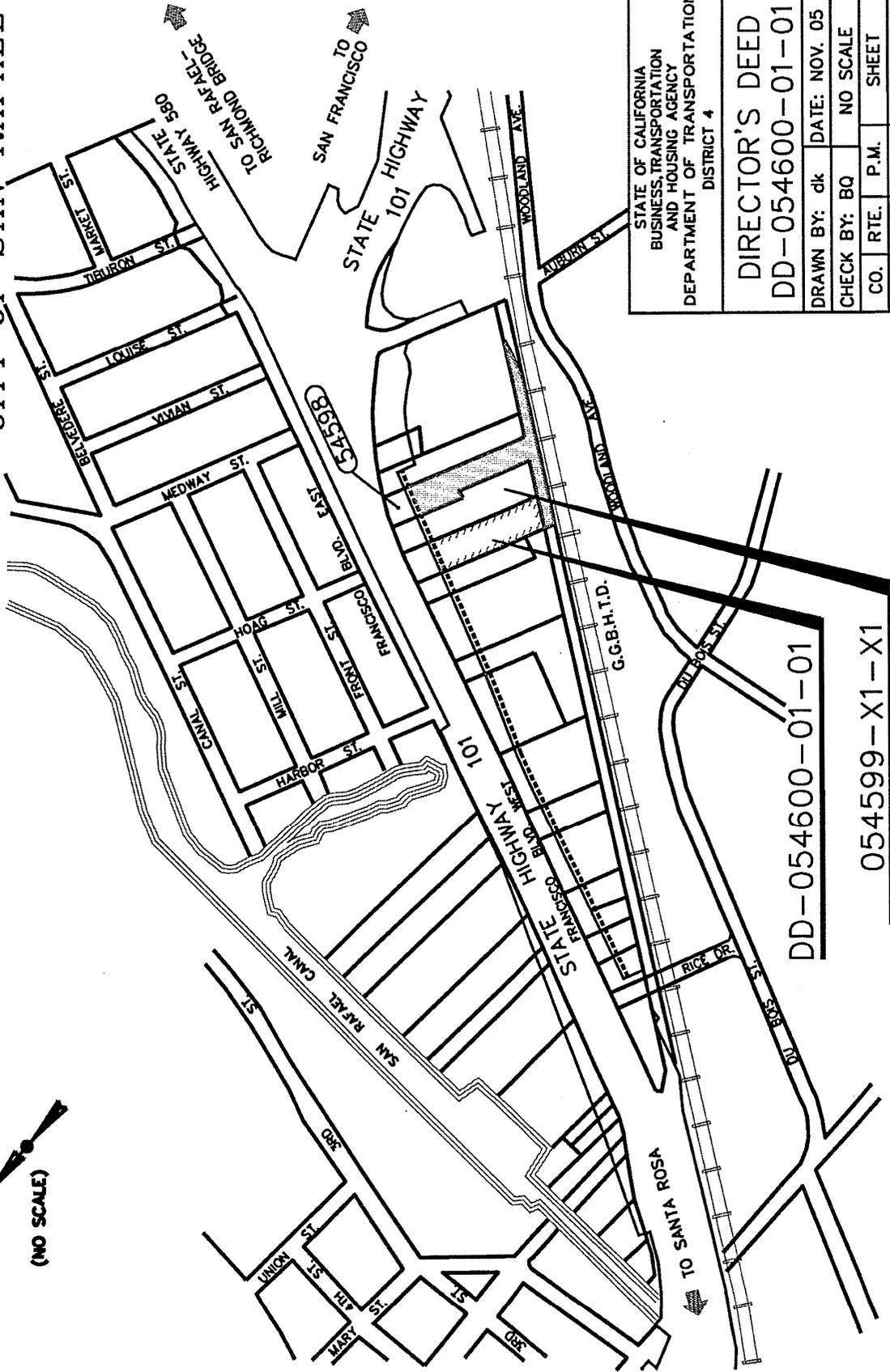
<sup>1</sup> If the jury's award is favorable to Sonnen, then Sonnen could collect litigation expenses, including attorneys' and expert witness fees, and costs from the State. These are estimated to be \$500,000-\$750,000 for attorneys' fees, \$300,000-\$600,000 for expert witness fees and costs resulting in the total potential award of \$800,000-\$1,350,000.

**SUMMARY OF PROPOSED SETTLEMENT  
(WITH CONVEYANCE OF PARCEL 54600-01-01 AND ASSIGNMENT OF  
PARCEL 054599-X1-X1)**

	<u>STATE</u>	<u>SONNEN</u>
Payment by	\$3,000,000	\$4,050,000
Net to	\$1,050,000	

Data provided are estimates based on/or derived from information known to date. Due to the subject pending litigation, as well as other pending suits involving properties in the vicinity on the same project, additional detail is not provided.

MARIN COUNTY  
CITY OF SAN RAFAEL



STATE OF CALIFORNIA  
BUSINESS, TRANSPORTATION  
AND HOUSING AGENCY  
DEPARTMENT OF TRANSPORTATION  
DISTRICT 4

DIRECTOR'S DEED	
DD-054600-01-01	
DRAWN BY: dk	DATE: NOV. 05
CHECK BY: BQ	NO SCALE
CO. RTE. P.M.	SHEET
MRN 101	10.1
	1 OF 2

DD-054600-01-01

054599-X1-X1

STATE OF CALIFORNIA  
 BUSINESS, TRANSPORTATION  
 AND HOUSING AGENCY  
 DEPARTMENT OF TRANSPORTATION  
 DISTRICT 4

**DIRECTOR'S DEED**  
 DD-054600-01-01

DRAWN BY: DK	DATE: NOV 05		
CHECK BY: BQ	SCALE: 1"=120'		
CO.	RTE.	P.M.	SHEET
MRN 101	10.1		2 OF 2

# FRANCISCO BLVD.

DISTANCES SHOWN ARE ON THE CALIFORNIA  
 COORDINATE SYSTEM OF 1983, ZONE III. MULTIPLY DISTANCES  
 SHOWN BY 1.0000625 TO OBTAIN GROUND-LEVEL DISTANCES.

9.84' TCE  
 TERM 12/31/2006  
 9.84' PUE  
 RESERVED FOR C.T.

