

**IN THE SUPREME COURT, STATE OF FLORIDA**

**HOULIHAN’S RESTAURANTS, INC.,  
D/B/A DARRYL’S,**

**Petitioner,**

**CASE NO. SC05-1964**

**v.**

**APAC-FLORIDA, INC., A DELAWARE  
CORP., ET AL.,**

**Respondent.**

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**PETITIONER’S REPLY BRIEF**

ALAN E. DESERIO  
Florida Bar No. 155394  
Post Office Box 1485  
Brandon, Florida 33509  
Phone: (813) 335-2241  
Fax: (813) 684-7973

Of Counsel

M. STEPHEN TURNER, P. A.  
Florida Bar No. 095691  
CHARLES S. STRATTON, P.A.  
Florida Bar No. 221589  
GINO LUZIETTI  
Florida Bar No. 310130  
MARTIN A. FITZPATRICK  
Florida Bar No. 0032107  
BROAD AND CASSEL  
215 S. Monroe Street, Suite 400  
Post Office Drawer 11300  
Tallahassee, Florida 32302  
Phone: (850) 681-6810  
Fax: (850) 681-9792

Attorneys for Petitioner, HOULIHAN’S

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## REPLY ARGUMENT

### **THE DECISION BELOW DID NOT FULLY COMPENSATE HOULIHAN'S FOR THE VALUE OF ITS LEASEHOLD INTEREST, AND DID NOT PROPERLY CONSIDER THE VALUE OF CNL'S REVERSIONARY INTEREST IN APPORTIONMENT OF THE CONDEMNATION PROCEEDS**

#### I. Case Overview

The briefing in this case has established that equitable apportionment did not occur.

The value of Lessor CNL's reversionary interest at the end of the lease term was not considered. This contravened the holdings in *Trump Enterprises v. Publix Supermarkets, Inc.*, 682 So. 2d 165 (Fla. 4<sup>th</sup> DCA 1996), and *Parker Building Inc. v. Palm Beach County*, 144 So. 2d 830 (Fla. 2<sup>nd</sup> DCA 1962), that the value of the lessor's reversionary interest should be determined for purposes of apportionment between lessor and lessee. The reversionary interest and contract rent compose the maximum value of the lessor's interest. This amount should be subtracted from the before-taking value of the property to determine the value of the lessee's interest.

Here, the maximum amount of CNL's landlord interest was \$1,215,285, which is the total of \$903,737 for the contract rent and \$311,548 for the reversionary interest. Subtracting this from the before-taking value

of the property leaves a value of \$891,848 for Houlihan's leasehold interest before adjustment for the settlement shortfall. The condemnation settlement proceeds were \$1.1 million and the remainder value was \$625,000, for a total realized value of \$1.725 million. The before taking value of the entire property was \$2.2 million. The shortfall in settlement had to be shared in proportion to the respective property interests. This should have resulted in values of \$730,169 for Houlihan's leasehold, and \$994,891 for CNL's interest. Since CNL got the remainder property worth \$625,000, CNL should have been apportioned \$319,891 to compensate its landlord interest.

The same result would be reached even if Houlihan's lease was valued first, and the balance of the property's value allocated to CNL. However, Houlihan's lease was not correctly valued consistent with the controlling lease provisions and operative law. CNL's expert, Stephen Matonis, testified based on his faulty legal conclusion that a lease could only have value to the extent a sublease would produce bonus rent. This ignored that the lease required valuation of the parties' interests at the time of taking. There was no existing sublease and no plan to sublease at that time. Failure to give full effect to a lease provision for apportionment of condemnation proceeds contravenes holdings of such decisions as *Elmore v. Broward*

*County*, 507 So. 2d 1220 (Fla. 4<sup>th</sup> DCA 1987)(lessee's interest before lease is terminated as a result of the taking was agreed to be compensated).

Moreover, the law recognizes that the bonus value to the lessee of a possessory lease interest properly measures lease value. Houlihan's enjoyed a substantial rent advantage in its occupancy. Such value would enable Houlihan's to be compensated for the substantial rent savings built into the lease from the prepayment of rent as a result of the 50% discounted sale-leaseback a few years before the taking.

Accordingly, CNL's expert testimony could not support the erroneous apportionment approved by the decision below.

The severity of the legal error is manifest in the egregious inequity of the apportionment result. Respondent CNL was awarded \$932,381 of the condemnation proceeds and controls the remainder property (post-taking) valued at \$625,000. Thus CNL realized a total benefit of \$1,557,381. Yet the value of its interest at the time of taking could not possibly exceed \$1,215,285, considering the rent reserved under the lease and value of its reversionary interest. Of course the shortfall adjustment would reduce this amount even further.

From the obverse perspective, Houlihan's received only \$167,619 for its terminated lease interest. This amount must compensate its exclusive

occupancy right enjoyed for 50% of market rent. This amount is all the compensation Houlihan's received despite having effectively prepaid \$1,000,000 in rent, and admittedly owning about 50% of the value of the entire property interest at the time of taking. Upon proper valuation and apportionment, Houlihan's should be awarded \$730,109 of the condemnation proceeds to compensate its interest as a property owner entitled to full compensation.

## II. Answer Brief Rebuttal

In its Answer Brief, Respondent CNL admits two important facts which confirm the erroneous valuation of Houlihan's leasehold interest at the time of the taking. First, there is no dispute that the lease had value to Houlihan's because the agreed-upon rent was one-half of the market rent for the property. Answer Brief pp. 4, 11 and 22. Second, Houlihan's created this market advantage by prepaying half of the rent it was to be charged during the life of the lease by reducing the purchase price from Respondent CNL as part of the sale-leaseback transaction. Answer Brief pp. 11-12, 23-24. Houlihan's compensation must necessarily include these lost benefits.

Respondent's expert, Stephen Matonis, believed that Petitioner could only benefit from its rental advantage if it was able to sublease the property. According to Mr. Matonis, valuation of the leasehold had to be based on a

future hypothetical sublease, including a substantial reduction in value for the cost of conversion for a new subtenant<sup>1</sup> and sharing incremental income with CNL. This “sublease value” would then be subtracted from the value of the entire property to yield the value of CNL’s interest. The value of both interests would then be prorated to account for any shortfall in settlement.

Mr. Matonis testified based on a false premise. A lessee’s advantageous possessory use at the time of taking is correctly measured by its bonus value (“market advantage”), or by the amount remaining after the lessor’s contract rent and reversionary interest is subtracted from the value of the entire property.

In his analysis, Mr. Matonis’ failed to value the respective interests as they existed at the time of the taking. There is no support or any rational explanation as to why a future sublease is required for Houlihan’s lease to have value. *See* Answer Brief p. 15. Mr. Matonis’ ignores the fact that a tenant who retains the right to pay below-market rent experiences a cost savings with each month that passes. This necessarily results in a compensable benefit. The fact that Petitioner will lose that cost savings and

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<sup>1</sup> It is questionable whether costs of conversion could be attributed to the lessee, even hypothetically. The lease provides for the cost of conversion to be paid by the subtenant, not by the lessee. Answer Brief p. 18 (quoting the lease requirement that the subtenant have the financial capability to “pay all debt service obligations, conversion costs and rent payments”).



be required to pay higher rent as a result of the taking represents the compensable value of its interest. Moreover, if Respondent's position is accepted, a lease without an enforceable sublease provision would be rendered valueless, contrary to the well-established principle that a lease has value protected from condemnation by the Constitution. *See Trump Enterprises Inc.*, 682 So. 2d at 169 (“[i]n the law of eminent domain, a lessee for years under a written lease is an owner of property in the constitutional sense, and is entitled to share in the compensation when all or a part of the leased property is taken during the period of the lease”).

In short, the opinion of Respondent's expert was based on a false legal premise and ignored the inherent value in a below-market rent lease. Such testimony cannot support the apportionment. *See Dept. of Trans. v. Nalven*, 455 So. 2d 301, 308 (Fla. 1984) (holding that expert testimony based on erroneous legal premise should not be allowed); *Fixel v. Rosenthal & Rosenthal, Inc.*, 921 So. 2d 43, 47 (3<sup>rd</sup> DCA 2006) (holding that expert opinion based on totally incorrect premise should be excluded). Under the language of the lease and well-established principles of condemnation law, the apportionment should not have proceeded on the false premise that Houlihan's leasehold had to be valued as a hypothetical sublease, where no

sublease was in existence or contemplated by the parties at the time of the taking.

With respect to the prepayment of rents, CNL seems to argue that Houlihan's gave up those monies at the time of the sale-leaseback, which was prior to the time of the taking, and therefore Houlihan's is precluded from considering those amounts in the valuation of its interest. *See Answer Brief pp. 11-12, 23-24.* But these pre-payments were, in effect, being recovered by Houlihan's with each payment of below-market rent. It would be inequitable to allow CNL to retain the prepayments and not have them accounted for in the apportionment to compensate Houlihan's interest. *See Dama v. Record Bar, Inc.*, 512 So. 2d 206, 208 (Fla. 1<sup>st</sup> DCA 1987) ("In apportioning condemnation proceeds the court should divide the sum equitably between the parties to reflect the respective values of the encumbered fee and the leasehold interest"). Equity demands that Houlihan's be compensated vis a vis Respondent CNL for the loss of the benefit Houlihan's secured from CNL, including significant prepayments and discounted rent at the time of the sale-leaseback agreement.

The apportionment should also account for the "remaining value" of the property that reverted to Respondent CNL as a result of the taking and termination of the lease. The parties do not dispute that the "after taking"

value of the land in CNL's hands was \$625,000. R IV:475, 515. After the taking, and as a result of the termination of the lease, Respondent CNL had sole possession of the land, and could have sold the property for \$625,000 without further cost or improvement. As a result, Respondent CNL's reversionary interest (valued at \$311,000) was converted into a much more valuable present possessory interest in the condemned property (valued at \$625,000). Such benefit to CNL must be taken into account in apportioning the settlement proceeds.

To properly value the parties' interests in the condemned land at the time of the taking, the summation method, described in the Initial Brief at pp. 26-28, should have been used to value CNL's interest first, with the balance of the property value belonging to the lessee. This would assure that CNL would be compensated for the value of its interest at the time of the taking – that is, the amount of rent it was to receive over the term of the lease plus the value of the land to be returned to it fifteen years in the future, adjusted for the shortfall in settlement. There was no need to speculate regarding the benefit Houlihan's might have realized from a hypothetical sublease, since Houlihan's allocation would be the amount remaining from the \$1.1 million settlement proceeds (\$730,000) following the calculation of the amount to which Respondent was entitled (\$370,000). *Id.* at 28.

**CONCLUSION**

The decision below should be quashed with directions to remand for entry of a revised apportionment judgment.

Respectfully submitted,

ALAN E. DESERIO  
Florida Bar No. 155394  
Post Office Box 1485  
Brandon, Florida 33509  
Phone: (813) 335-2241  
Fax: (813) 684-7973

Of Counsel

/s/ Martin A. Fitzpatrick  
M. STEPHEN TURNER, P. A.  
Florida Bar No. 095691  
CHARLES S. STRATTON, P.A.  
Florida Bar No. 221589  
GINO LUZIETTI  
Florida Bar No. 310130  
MARTIN A. FITZPATRICK  
Florida Bar No. 0032107  
BROAD AND CASSEL  
215 S. Monroe Street, Suite 400  
Post Office Drawer 11300  
Tallahassee, Florida 32302  
Phone: (850) 681-6810  
Fax: (850) 681-9792

Attorneys for Petitioner, Houlihan's

**CERTIFICATE OF SERVICE**

I HEREBY CERTIFY that a true and correct copy of the Reply Brief has been furnished via U.S. mail to John T. Wettach, Esq., attorney for Respondent, CNL, APF Partners, L.P., 215 North Eola Drive, Orlando, Fl. 32802, this 14<sup>th</sup> day of July, 2006.

**CERTIFICATE OF COMPLIANCE WITH FONT SIZE**

I HEREBY CERTIFY that this Initial Brief complies with the font requirements of Rule 9.210 (a) (2), *Florida Rules of Appellate Procedure*, because it is prepared in Word using a 14-point, Times New Roman font.

/s/ Martin A. Fitzpatrick  
Attorney