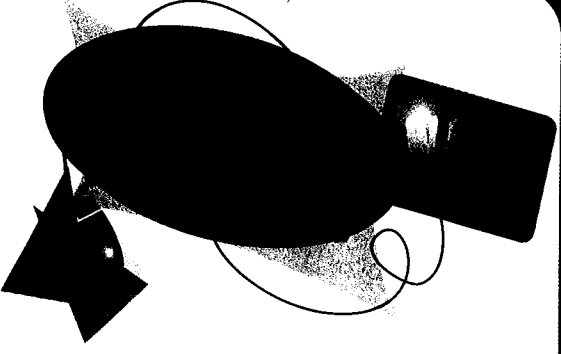



provide services and the relationship between each TIC Owner, the lender, and any lessee. The actual economic terms of the investment itself may get buried in the inches of legal documentation.

14. Regulation D, Securities Act of 1933, 17 C.F.R. §§ 230.501-.508.
15. See also Securities and Exchange Commission Rule 505 and 506.
16. See discussion *infra* Section V(J) Voting Rights.
17. See discussion *supra* Section V(I) Management Agreements.
18. Section 6.15 of Rev. Proc. 2002-22.



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Take This! A Roadmap Through a Regulatory Takings Claim

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I. OVERVIEW

Both the United States and California Constitutions prohibit the taking of private property for public use without payment of just compensation to the property owner.¹ The courts have identified two primary types of takings that require two different analyses: (1) a *per se* taking that occurs when there is a permanent physical taking of, occupation of, or damage to real property, and, (2) a *regulatory* taking that occurs when a statute or regulation deprives a property owner of substantially all economically viable use of his or her property. It is this second type of taking that has generated the bulk of the case law in this area, and the case law is anything but clear or consistent. Nevertheless, certain threads and trends are emerging that provide a framework for analyzing a regulatory takings problem.

The United States Supreme Court has historically applied the categorical, or *per se*, analysis to physical invasions of *real property*. If the government takes, occupies, or damages privately owned real property, the government must, in accordance with applicable state and federal constitutions, pay just compensation for the taking, occupation, and/or damage on (with very limited exceptions) a strict liability basis.² In contrast, the Supreme Court has traditionally applied the *ad hoc* analysis to regulatory takings claims. The *ad hoc* analysis is a case specific *balancing* test, measuring the public interest gained against the private harm suffered as a result of the regulatory taking.³ In addition to controlling United States Supreme Court jurisprudence on the subject, there is also an impressive library of California cases to help guide the discussion.

First, a disclaimer: As a result of the thousands of takings cases, from multiple jurisdictions, addressing a variety of “take” scenarios – physical and regulatory, real property and personal property, permanent and temporary – takings jurisprudence, especially regulatory takings jurisprudence, is evolving as quickly as public agencies contrive of new and different ways to regulate the use of private property. Not surprisingly, each new regulatory takings case often raises additional questions that the next court is left to resolve.

As one commentary laments: “[T]here is an inherent complexity which renders a simple definition [of the law of eminent domain] difficult and possibly misleading. It has been hedged in many exceptions, qualifications and limitations.”⁴ This observation is especially appropriate to regulatory takings jurisprudence. The purpose of this article is to simplify the “inherent complexity” of regulatory takings jurisprudence by providing a practical overview of the current state of this area of law in California and a framework for analysis of such claims. Because regulatory taking issues typically arise in the context of inverse condemnation cases, that will be the procedural posture this article assumes. The main difference between an inverse condemnation case and a direct eminent domain action is who brings the action. In the

former case, it is the property owner, in the latter, the condemning agency. It is well settled that with certain procedural exceptions, the rules governing direct condemnation cases and inverse condemnation cases are generally the same.⁵

II. WHO IS THE APPROPRIATE DEFENDANT?

In assessing or evaluating a claim for inverse condemnation, whether physical or regulatory, the first inquiry is determining the proper defendant. The question of who is a proper defendant arises more frequently in the physical takings context, as multiple agencies are often involved in public projects. In the regulatory takings context, the appropriate defendant is usually the agency that enacted the particular land use regulation. A private party is not a proper defendant in an action based upon a claim of inverse condemnation.⁶ While public agencies' power of eminent domain explains why they are liable in an inverse condemnation action, it does not follow that public agencies that lack the power of eminent domain are immune from an inverse condemnation claim. To the contrary, any public agency is a proper defendant in a claim for inverse condemnation.⁷ Moreover, a privately owned public utility can be held liable in inverse condemnation if the damage results from a public undertaking such as the transmission of electrical power.⁸ This liability exists because of the rationale underlying inverse condemnation, which holds that the government – whether or not it has the formal power of condemnation – should not force “some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.”⁹

A subsidiary question is which public agency or agencies should be named in an inverse condemnation action. The answer is to name any agency that has participated in the regulation or taking. The California Court of Appeal has recently confirmed that any public agency that is a “substantial participant” in the cause of the damage, is jointly and severally liable for the damage.¹⁰ A public agency cannot avoid liability even though it *only* approved the plans for the development of a private project involving a taking.¹¹

III. WHAT IS THE APPROPRIATE TEST TO APPLY?

A. The *Per Se* Test Applies Physical Takings

The simplest form of inverse condemnation is that of a physical taking by the government. The landmark case of *Loretto v. Teleprompter Manhattan CATV Corp.* set forth the rule that “a permanent physical occupation is a government action of such a unique character that it is a taking without regard to other factors that a court might ordinarily examine.”¹² In other words, when the government intrudes on property in a physical manner, there is no need to consider other factors to determine if compensation is due. *Loretto* further notes “that when the physical intrusion reaches the extreme form of a permanent physical occupation, a taking has occurred. In such a case, ‘the character of the government action’ not only is an important factor in resolving whether the action works a taking but also is determinative.”¹³ The *Loretto* court held that New York’s law requiring landlords to allow television cable companies to install cable access boxes and lines in their apartment buildings was a physical occupation that constituted a *per se* taking.¹⁴

Some other examples of government actions that have been deemed physical takings included the withdrawal of lateral support causing physical damage to a building,¹⁵ measurable reduction in the market value of property due to noise from an airport that interfered substantially with the use and enjoyment of real property,¹⁶ and the posting of security guards on private property by a city.¹⁷ Government actions that have not been deemed physical takings generally include physical intrusion on property to enforce valid land-use regulations or to preserve the public’s health and safety.¹⁸

To summarize: If the government has occupied, damaged, or destroyed private property, and it cannot clearly justify the intrusion on police power (i.e., health and safety) grounds, chances are good that a taking has occurred.

B. The Categorical (*Per Se*) Test Applies to Regulatory Takings That Deny All Economically Viable Use

The modern history of *regulatory* takings jurisprudence was born 80 years ago with the case of *Pennsylvania Coal Co. v. Mahon*.¹⁹ In *Mahon*, the issue before the United States Supreme Court was whether a statute that prohibited coal mining that would “cause the subsidence of ... any structure used as a human habitation” constituted a regulatory taking in violation of the takings clause.²⁰ Pennsylvania Coal Company argued that the statute destroyed its previously existing rights of property and contract arising from a reservation for mining in the deed transferring ownership of the property to the present owners.²¹ The Supreme Court framed the issue as follows: “As long recognized, some values are enjoyed under an implied limitation and must yield to the police power. But obviously the implied limitation must have its limits or the contract and due process clauses are gone.”²²

In *Mahon*, the Supreme Court determined that when deciding whether the exercise of police power had gone too far, the amount of the diminution in value resulting from the regulation should be considered and that this should be weighed against the public interest served by the exercise of the police power.²³ The *Mahon* Court concluded that the statute was unconstitutional by reasoning that the public interest served was outweighed by the impact on private property because the statute did not apply to situations where the property and the right to mine the coal were held by the same owner, and the statute negated existing property and contract rights otherwise binding between the parties.²⁴

Fifty-eight years later in *Agins v. Tiburon*,²⁵ the United States Supreme Court addressed the constitutionality of a zoning ordinance that limited property to certain uses.²⁶ In *Agins*, the Supreme Court enunciated a two part test to determine if a regulation constitutes a taking.²⁷ Citing *Nectow v. Cambridge*,²⁸ the Supreme Court stated that the first part of the test is whether the ordinance substantially advances a legitimate state interest.²⁹ The second part of the test requires a determination as to whether the ordinance denies an owner economically viable use of his or her property.³⁰ The Supreme Court determined that the legislature’s purpose in implementing the zoning ordinance was to prevent the ill effects of urbanization and that this was a legitimate state interest.³¹ The Supreme Court concluded that while the zoning ordinance limited development of the property, it neither prevented the best use of appellants’ land nor “extinguished a fundamental attribute of ownership.”³² Therefore, the zoning ordinance was held to be constitutional.³³

Twelve years after *Agins*, in 1992, the United States Supreme Court again took the opportunity to address the issue of regulatory takings in *Lucas v. South Carolina Coastal Council*.³⁴ Lucas had purchased two residential lots on a South Carolina barrier island and following the purchase, the state legislature enacted a law that barred Lucas from building any permanent structures on such land.³⁵ The Supreme Court concluded that regulations that denying the property owner *all* "economically beneficial or productive use of land" constitute one of the discrete categories of compensable regulatory deprivations that do not require the usual case-specific (i.e., ad hoc) inquiry into "the public interest advanced in support of the restraint."³⁶ Therefore, the *Lucas* Court enunciated a *per se* category of regulatory takings that applies when a property owner is denied *all* economic use of his or her property. The Court's rationale for this conclusion was that regulations of this nature "carry with them a heightened risk that private property is being pressed into some form of public service under the guise of mitigating serious public harm."³⁷

In summary, a regulation that results in the deprivation of all economic use of property is treated as a "*per se*" taking in the same way that a physical occupation or intrusion is treated as a "*per se*" taking. Short of denial of all economic use, however, each case requires a balancing of certain factors, usually the degree of deprivation of the property right considered in light of the public policy objectives of the legislation or regulation. The *Lucas* case is the leading case on the *per se* or *categorical* rule in the context of a *regulatory* taking, and its reasoning applies in those relatively rare instances where a regulation deprives the owner of all economically viable use of his or her property.

C. The Non-Categorical (*Ad Hoc*) Test Applies to Regulatory Takings That Leave Some Economically Viable Use Available

In *Penn Central Transportation Co. v. New York City*, the United States Supreme Court considered whether the application of the New York City Landmark's Law constituted a taking of Penn Central's property because it denied Penn Central the right to develop a building on top of the existing Grand Central Terminal building.³⁸ The *Penn Central* Court established a three-factor "ad hoc" test to determine when a *regulation* goes too far, and constitutes a taking.³⁹ The three basic factors are: (1) the economic impact of the regulation on the person affected, (2) whether the regulation has interfered with a distinct investment backed expectation of that person, and (3) the character of the government action.⁴⁰

As to the first two factors, the Supreme Court dismissed Penn Central's argument that it was deprived of the airspace above the terminal on the grounds that a taking claim cannot be based on a speculative property interest that the parties "believed was available."⁴¹ With respect to the third factor – the character of the government action – the Court held that "a 'taking' is more readily found when the interference with the property can be characterized as a physical invasion by government than when interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good."⁴² Applying the three factors, the Court concluded that the proscription on development set forth in the City's Landmark's Law did not constitute a taking.⁴³

Thus, it is now settled that a regulation that does not leave the property economically idle should be analyzed under the *Penn Central*

test, rather than the *Lucas* test.⁴⁴ The question of whether or not the claim should be analyzed under the *Lucas* framework or under the more difficult to satisfy *Penn Central* framework is often a contentious and dispositive question in takings litigation. Because most regulations leave some arguable economic use available, the "*per se*" *Lucas* test is not frequently available. More often, the ad hoc factors identified in *Penn Central* apply, resulting in case specific inquiries.

IV. APPLICATION OF THE AD HOC TEST IN PARTICULAR CONTEXTS

A. Conditions and Exactions

Further elaboration on the law of regulatory takings came in *Nollan v. California Coastal Commission*⁴⁵ and *Dolan v. City of Tigard*,⁴⁶ both of which involved the government attempting to condition approval of development of property on concessions from the landowners. The question presented was how such regulations should be scrutinized.

In *Nollan*, the landowners wished to enlarge their oceanfront home.⁴⁷ The California Coastal Commission allowed them to do so only if they would agree to grant the public an easement over the front of their property for access to the beach.⁴⁸ The United States Supreme Court held that the Coastal Commission could not require such an easement without compensation, because the condition placed on development was not related to the stated goal of the commission – to prevent oceanside buildings from blocking freeway views of the ocean.⁴⁹ In other words, there was a "lack of nexus between the condition and the original purpose of the building restriction."⁵⁰

In *Dolan*, as in *Nollan*, the property owner was granted permission to enlarge her property only if she fulfilled certain conditions.⁵¹ Dolan wished to expand her business and the City required that she grant land adjacent to the business to the city so it could build a bike path and additional storm drainage.⁵² The United States Supreme Court held that this requirement did have a "nexus" to a legitimate public purpose (as required by *Nollan*), but that the burden on Dolan did not "bear the required relationship to the projected impact of proposed development."⁵³ *Nollan* and *Dolan* together hold that (1) a proposed condition or exaction imposed in connection with a development approval must have a sufficient relationship (i.e., nexus) to the legitimate public purpose sought to be furthered, and (2) the extent of the condition or exaction must be tailored to fit the impact of the proposed development.

B. Development Fees

Development fees are monetary exactions imposed as a condition of development approval. The California Supreme Court has recently clarified the appropriate analysis to be applied to development fees imposed by a public entity as a condition of development approval.⁵⁴ The *Nollan/Dolan* "nexus" and rough proportionately analysis only applies to development fees that are project specific and not generally applicable through legislative action.⁵⁵ In other words, if a monetary exaction results from generally applicable legislation not targeting or impacting a specific project, the courts will apply a more deferential standard of review. If the fee targets a specific development, the more rigorous *Nollan/Dolan* analysis applies.

In *San Remo Hotel v. City and County of San Francisco*, the hotel conversion fee at issue was imposed through legislative

action, and was ostensibly generally applicable to all projects within its scope.⁵⁶ The California Supreme Court held that because the fee was not specific to one project, the fee deserved a more deferential standard of review.⁵⁷ The fee in *San Remo*, a use-conversion fee, was non-discretionary with respect to application and amount.⁵⁸ The fee was extracted to help fund the construction of low and moderate income housing in the City of San Francisco.⁵⁹ Accordingly, the court merely determined whether a reasonable relationship exists between the exaction and the public purpose of the exaction. Applying this deferential standard, the California Supreme Court held that there was a reasonable relationship between the fee and the purpose underlying the fee.⁶⁰

It is important to note that Judge Baxter, in a concurring and dissenting opinion, focused on the causal link between the fee and its purpose and suggests the following recasting of the applicable standards: "The in-lieu fee does not violate the takings clause so long as (1) there is a cause and effect relationship between the owner's desired use of the property and the social evil that the fee seeks to remedy, and (2) the fee is reasonably related in both intended use and amount to that social evil."⁶¹ This proposed standard of review will no doubt be raised by property owners as appropriate in future fee-exaction cases.

C. Temporary Moratoria

In *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*,⁶² the United States Supreme Court addressed whether a temporary development moratoria is a categorical taking under *Lucas* or whether it requires an *ad hoc* analysis under *Penn Central*.⁶³ The Supreme Court framed the issue as whether "the mere enactment of a temporary regulation that, while in effect, denies a property owner all viable economic use of her property gives rise to an unqualified constitutional obligation to compensate her for the value of its use during that period."⁶⁴ The Court struggled with the concepts of the "parcel as a whole" and concluded that a total taking cannot be temporary because there may be value in future uses of the property.⁶⁵ The majority viewed the property rights at issue as both temporal and geographic in nature and concluded that courts must consider the economic use of the entire temporal parcel, just as they must consider the economic use of the entire geographic parcel.⁶⁶ In answer to the question whether a regulatory taking that results in the loss of all economic use of property for a temporary period is a *per se* taking under *Lucas*, the Court answered: "No. In our view the answer to the abstract question whether a temporary moratorium effects a taking is neither 'yes always' nor 'no, never'; the answer depends upon the particular circumstances of the case." Therefore, the *Penn Central* test is appropriate.

Applying the *Penn Central* factors, and rejecting the landowners' *Lucas*-based "conceptual severance argument," the Court found that there had not been a taking as a result of the temporary moratorium.⁶⁷

D. Development Delay

In *Loewenstein v. City of Lafayette*, the First District Court of Appeal held that there had been no wrongful taking in denying a lot-line adjustment since the city was promoting the legitimate interest of monitoring density and slope requirements.⁶⁸ The court was guided however, not by the *Penn Central* factors,

but by the California Supreme Court case *Landgate, Inc. v. California Coastal Commission*.⁶⁹ The *Landgate* analysis negates the *Penn Central* factors in cases involving regulatory delay.⁷⁰ In other words, a non-categorical, *per se* taking still may occur even where there has not been a full deprivation of economic use,⁷¹ if there is regulatory delay motivated not by a legitimate governmental interest, but rather by an effort to delay the development for the sake of delays.

Under *Landgate*, "a government agency may not evade the takings clause by fabricating a dispute over the legality of a lot, or by otherwise arbitrarily imposing conditions on development in order to delay or discourage that development. The government agency's assertion of authority, whether or not legally erroneous, must advance some legitimate government purpose."⁷² Because the regulation in *Loewenstein* was advancing a legitimate state interest, and there was no evidence that the City's position "was so unreasonable from a legal standpoint as to lead to the conclusion that it was taken for no purpose other than to delay the development project," the court of appeal determined there was no taking.⁷³

E. Rent Control

Rent control has been a thorn in the side of property rights activists and counsel for years. Two California decisions in the past six years have weakened future takings claims based upon rent control regulations.

In *Galland v. City of Clovis*,⁷⁴ the Gallands filed a complaint for inverse condemnation and for statutory federal civil rights violations under section 1983, the court held that a property owner's damage claims against the city for blatant violations of due process in administering its rent control ordinance may be denied without compensation if the city, after years of litigation, considered a rent adjustment to avoid a "confiscatory" result.⁷⁵ In effect, the court held that the city's procedural delays and abuses did not constitute takings if the city, after the fact, permitted a non-confiscatory rent increase.

The court based its decision on its holding in *Kavanau v. Santa Monica Rent Control Board*.⁷⁶ The *Galland* court described the *Kavanau* decision as one where the court "decided that under rent control, adjustment of future rents was generally sufficient to compensate for prior rent ceilings that were set so low as to be confiscatory."⁷⁷ The city argued that before paying damages to the Gallands, it must be given the opportunity to rectify confiscatory rent ceilings with a *Kavanau* adjustment.⁷⁸

The California Supreme Court sent the dispute back to the trial court to determine whether a *Kavanau* adjustment would be adequate "to prevent constitutional injury by compensating for previous excessive low rent ceilings."⁷⁹ The trial court could impose liability under section 1983 only if one of two conditions were present: "(1) the costs imposed are part of a government effort to deliberately flout established law, e.g., deliberately obstruct legitimate rent increases; or (2) the landlord suffers confiscation as a result of the imposition of such costs."⁸⁰

In the area of rent control, the California Supreme Court has made it very difficult to prove an unconstitutional taking. It must be shown that the government has grossly, intentionally, and arbitrarily regulated the use of the claimant's property. The *Galland* case illustrates the difficult and often financially devastating burden imposed on property owners to prove a takings claim based on rent control ordinances.

R. Interest on Lawyer Trust Accounts (IOLTA)

The United States Supreme Court recently addressed whether a categorical or non-categorical test should be applied in a regulatory takings case involving a Washington state law requiring that interest on lawyer trust accounts be “given” to state legal aid programs.⁸¹

In *Washington Legal Foundation v. Legal Foundation of Washington*,⁸² the ninth circuit, sitting *en banc*,⁸³ applied the *ad hoc*, fact specific analysis of *Penn Central* to the question of whether the State of Washington’s IOLTA (interest on lawyer trust accounts) program violated the takings clause.⁸⁴ The *Washington Legal Foundation* ninth circuit majority not only believed that it was “entirely appropriate to apply *Penn Central*’s *ad hoc* takings analysis to the IOLTA program, but that such an analysis [was] compelled.”⁸⁵ The majority also noted that the fact that IOLTA programs are regulated by the banking industry “counsels against the application of the *per se* analysis to the regulation of the use of money at issue.”⁸⁶ Lastly, the majority reasoned that the *per se* analysis “has almost exclusively been employed in situations involving real property.”⁸⁷

Applying the three *ad hoc* factors, the ninth circuit court concluded that the program did not result in an unconstitutional taking of the interest earned on client trust accounts.⁸⁸ Applying the first factor, the economic impact of the regulation, the majority discussed the history of the IOLTA programs and ruled that there was no economic impact since “the IOLTA program, at worst, maintains the status quo and, at best, provides clients with interest they otherwise would not have earned.”⁸⁹ The Ninth Circuit majority employed similar reasoning in determining that the IOLTA did not interfere with the appellants’ investment backed expectation, the second *ad hoc* factor under *Penn Central*, since neither of the appellants “could have expected his principal to earn a net interest.”⁹⁰ Finally, addressing the nature of the regulation, the court of appeals deemed the IOLTA program to be simply a regulation affecting the use of the property and “not out of character for either the commercial industry [banking] or the professions [the practice of law] they affect.”⁹¹

The United States Supreme Court granted certiorari in *Washington Legal Foundation*, and rendered its ruling in March of this year.⁹² The two issues on review in *Brown & Hayes v. Legal Foundation of Washington et al.* (styled *Washington Legal Foundation v. Legal Foundation of Washington* in the ninth circuit proceedings) were (1) whether the *Penn Central ad hoc* test applied, and (2) whether Washington’s IOLTA program constitutes a taking.⁹³ These issues were highlighted by Justice Kozinski’s dissent in the ninth circuit *en banc* ruling, reciting the original three-justice ninth circuit panel’s appellate ruling verbatim. That original panel ruling (1) applied the *per se* test because the regulation deprives the property owners of *all* of its beneficial interest in the earned interest, and (2) held that the IOLTA program was an unconstitutional taking.⁹⁴

In the end, the United States Supreme Court agreed with the ninth circuit majority that there was no taking, but determined that the categorical *Lucas* and *Loretto* tests were applicable.⁹⁵ This was because the transfer of interest from the trust accounts to the legal services foundation was “more akin to the occupation of a small amount of rooftop space in *Loretto*.” The Supreme Court next held that while the interest on a lawyer’s trust account is a property right protected by the Fifth Amendment,⁹⁶ no compensation was due in connection with a state program to provide legal

services to the needy because the program did not result in a net loss to the owner of the interest, except in cases where the lawyer mistakenly put interest bearing funds in an IOLTA account.⁹⁷ “Because . . . compensation is measured by the owner’s pecuniary loss – which is zero whenever the Washington law is obeyed – there has been no violation of the just compensation clause of the Fifth Amendment in this case.”⁹⁸ In his dissent, however, Justice Scalia warned that: “To extend to the entire run of Compensation Clause cases the rationale supporting today’s judgment – what the government hath given, the government may freely take away – would be disastrous.”⁹⁹

V. WHEN IS THE CASE RIPE?

The ripeness doctrine is derived from the United States Constitution’s article III case or controversy requirement.¹⁰⁰ The doctrine protects agencies from judicial interference until an administrative decision has been formalized and its effects felt in a concrete way by parties challenging the decision.¹⁰¹

The ripeness of a regulatory takings claim is more difficult to show than the ripeness of a physical takings claim, because the damage from the physical taking usually is immediately apparent. In order for a regulatory takings claim to be ripe, there first must be a final and authoritative determination from the governmental agency involved regarding the application of its regulation to the land.¹⁰² Then there must be a determination of the type and intensity of development legally permitted on the subject property.¹⁰³ Furthermore, the landowner should have applied for and been denied a development permit, and it should have sought any appropriate variances.¹⁰⁴ If the claim is brought in federal court, the ripeness doctrine also requires a showing of inadequate state remedies, or exhaustion of available remedies.¹⁰⁵ In other words, if the alleged regulatory taking was committed by a state or local government agency, the claimant must first pursue his or her claim in state court before resorting to federal court.

In *Palazzolo v. Rhode Island*, the United States Supreme Court reversed a trial court’s determination that the claim was not ripe where the landowner had applied for and been denied four different permit applications over a 23-year period.¹⁰⁶ The Court held that in order for a claim to be ripe “the administrative agency [must have] arrived at a final, definitive position regarding how it will apply the regulations at issue to the particular land in question.”¹⁰⁷ The Court found that the requirement had been satisfied where there was no remaining uncertainty as to what the agency would and would not allow.

Notwithstanding the foregoing, there is a futility exception to the ripeness doctrine. At a minimum, the landowner is expected to have submitted one formal development plan and to have sought a variance from any regulation barring the development proposed in the plan.¹⁰⁸ Under the futility exception, if the landowner knows that resubmission of either a development plan or application for a variance would be futile, it is not necessary that the landowner go through the process.¹⁰⁹ The landowner bears the responsibility of showing the futility of resubmission.¹¹⁰ Futility can be shown in a number of ways, such as by showing that pursuit of the issue would cause excessive delay resulting in loss of use of the property, by the agency’s rejection of resubmissions, and, sometimes, after more than one separate plan has been submitted and rejected.¹¹¹

A related but different issue relates to the exhaustion of

administrative remedies.¹¹² In order to challenge an administrative action, the petitioner must show that he or she has exhausted all available administrative remedies.¹¹³ While ripeness involves a horizontal analysis of ensuring that all potential approaches to solve the problem have been undertaken, exhaustion is more of a vertical analysis, analyzing whether all appeals have been exhausted with respect to each approach attempted.

In summary, landowners must make a complete effort to obtain development approvals, involving not only as many development approaches as feasible, but also appeal of any denials all the way up to the highest administrative body. It is crucial to evaluate whether a claim is ripe before a takings claim is asserted, because failure to ripen the claim may defeat it before the merits are reached.

VI. WHEN MUST A CLAIM BE FILED?

Generally, an inverse condemnation action that is based upon "damage" to property must be filed within three years of discovery of the damage.¹¹⁴ This is based on Code of Civil Procedure section 338, which provides a three-year statute of limitations for an "action to recover for physical damage to private property under Section 19 of Article I of the California Constitution."¹¹⁵ Section 19 of Article I of the California Constitution is the section guaranteeing the right to just compensation.¹¹⁶ The three-year time period starts to run once the damage has stabilized.¹¹⁷ Actions based upon a "taking" of property, however, generally must be filed within five years of the taking.¹¹⁸

In a case decided earlier this year, a California court of appeal applied a five-year limitation period in Code of Civil Procedure section 318 to an inverse claim brought by a sublessee who was not named or compensated in the direct condemnation action.¹¹⁹ Because the taking in question was "possessory" and not a result of physical damage, the court of appeal applied the five-year statute of limitations applicable to actions based on the possession of real property – in other words, this was a physical "takings" claim and not a physical "damage" claim.¹²⁰ The five-year time period begins to run as of the time the government takes possession.¹²¹

Notwithstanding these three and five-year statutes of limitations, the effective statute of limitations for a regulatory takings claim is often much shorter. This is because a timely challenge to the administrative decision complained of is a prerequisite to a regulatory takings claim, and the time period for such a challenge is typically very short. For example, a challenge to an administrative decision in the land use context must, in most cases, be made within 90 days from the date the decision is final. Therefore, the effective limitation period for a regulatory takings claim would be 90 days.¹²²

VII. WHAT DAMAGES ARE RECOVERABLE?

A. The General Standard – Fair Market Value

The United States Supreme Court has often stated that the just compensation required by the Fifth Amendment is measured by the property owner's loss rather than the government's gain. "The property owner is entitled to be put in as good a position pecuniarily as if his property had not been taken. He must be made whole but is not entitled to more."¹²³

The concept of fair market value, along with other direct condemnation principles, applies equally to inverse condemnation cases.¹²⁴ Thus, the first place to look in determining recover-

able compensation is to the statutory and case law definition of fair market value.¹²⁵ By statute, fair market value is "the highest price... that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obliged to sell, and a buyer, being ready willing and able to buy, but under no particular necessity for so doing, each dealing with the other with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available."¹²⁶ The determination of fair market value cannot take into account the value depressing effect of the regulation resulting in the taking.¹²⁷

B. Compensation for Less Than Fee Interest

The taking or damaging of an interest in real property that constitutes less than the fee is compensable in inverse condemnation law. For illustration, some less than fee interests that have been deemed compensable include leaseholds,¹²⁸ easements,¹²⁹ and rights-of-way.¹³⁰

A recent decision from the second district suggests, but does not hold, that an expectancy of lease renewal based on a lease clause permitting a tenant to holdover following the expiration of the term may be a compensable property interest.¹³¹ This dicta is in contrast to the holding in *San Diego Metropolitan Transit Development Bd. v. Handlery Hotel*.¹³² In that case, the Fourth District Court of Appeal held that the expectation of a lease renewal based on the length of the tenancy, and the relationship between the tenant and landlord is not a compensable property interest.¹³³ The second district's approach would appear to be more in accord with established United States Supreme Court precedent on this issue.¹³⁴

C. Recovery of Expenses in Mitigating Potential Damage

A property owner who acts reasonably in expending sums for mitigation of anticipated future damage is entitled to recovery of the mitigation costs on an inverse condemnation basis, regardless of whether hindsight reveals that the mitigation measures were unnecessary.¹³⁵ This approach has been characterized as consistent with the basic notion of making the property owner whole for damages incurred by reason of a "taking". It would be counterproductive to require actual damage in order to receive compensation for mitigation measures reasonably adopted because such a policy would severely reduce the incentive of property owners to act responsibly when faced with potential damage from a public project.

D. Recovery for Loss of Business Goodwill and Unreasonable Precondemnation Conduct

A business owner may assert a claim for loss of business goodwill under Code of Civil Procedure section 1263.510 as part of an inverse condemnation claim.¹³⁶ This is based on well-established authority applying direct condemnation principles to inverse condemnation claims.¹³⁷

A property owner is also permitted to recover damages resulting from unreasonable agency conduct prior to initiating condemnation, so long as the necessary prerequisites are established.¹³⁸ Such a claim is often made when an agency's precondemnation announcements or actions cause the value of a property targeted for acquisition to decline or tenants to be lost. However, there does not exist a separate cause of action for

unreasonable precondemnation conduct; it is simply a category of damages in an inverse cause of action.¹³⁹

VIII. CONCLUSION

Recent decisions from state and federal courts have provided further insight, but not necessarily clarity, into the muddy waters of regulatory taking and inverse condemnation law. The constitutional controversies generated by the tension between the government's need to condemn property for the greater good, on the one hand, and the individual's right to own and enjoy private property free from governmental interference, on the other, bring property law to life and implicate a central tenet of constitutional democracy. As our Supreme Court has said: "The dichotomy between personal liberties and property rights is a false one. Property does not have rights. People have rights. The right to enjoy property without unlawful deprivation, no less than the right to speak or to travel, is in truth a 'personal' right....A fundamental interdependence exists between the personal right to liberty and the personal right in property. Neither could have meaning without the other."¹⁴⁰

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ENDNOTES

1. U.S. Const. amends. V, XIV; Cal. Const. art. I, § 19.
2. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 426 (1982)[hereinafter *Loretto*].
3. See, e.g., *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 122 S.Ct. 1465, 1479-80 (2002); *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1015-16 (1992); *Penn Central Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).
4. 1 Nichols on Eminent Domain, § 1.1, p. 1-6 (rev. 3d ed. 2002).
5. *Barham v. S. Cal. Edison Co.* 74 Cal. App. 4th 744, 751 (1999); *Chlour v. Community Redevelopment Agency*, 46 Cal. App. 4th 273, 279-80 (1996).
6. *Oliver v. AT&T Wireless Serv.*, 76 Cal. App. 4th 521, 530 (1999).
7. *Marshall v. Dep't of Water & Power of City of Los Angeles*, 219 Cal. App. 3d 1124, 1139 (1990).
8. *Barham v. Southern Cal. Edison Co.*, 74 Cal.App.4th 744 (1999).
9. *Armstrong v. United States*, 364 U.S. 40, 49 (1960).
10. *Arreola v. County of Monterey*, 99 Cal. App. 4th 722, 761 (2002).
11. See *Aaron v. City of Los Angeles*, 40 Cal. App. 3d 471 (1974)[hereinafter *Aaron*].
12. *Loretto*, *supra* note 2, at 432.
13. *Id.* at 426.
14. *Id.* at 421.
15. *Holtz v. San Francisco Bay Area Rapid Transit*, 17 Cal. 3d 648, 651 (1976).
16. *Aaron*, *supra* note 11, at 483-84.
17. *Ali v. City of Los Angeles*, 77 Cal. App. 4th 246, 249-50 (1999). The trial court had found that the placement of security guards on the property constituted a physical taking. This decision was rendered moot by the appellate court's holding that there was a temporary taking of the property under the Ellis Act.
18. See *Hoeck v. City of Portland*, 57 F.3d 781, 787 (9th Cir. 1995) (listing examples where government presence was temporary and the entry could have been avoided if the land owner had complied with laws to begin with).
19. 260 U.S. 393 (1922).
20. *Id.* at 412-13.
21. *Id.* at 412.
22. *Id.* at 413.
23. *Id.* at 419.
24. *Id.* at 413-14.
25. 447 U.S. 255 (1980)[hereinafter *Agins*].
26. *Id.* at 257.
27. *Id.* at 260.
28. 277 U.S. 183 (1928).
29. *Agins*, *supra* note 25, at 260.
30. *Id.*
31. *Id.* at 261.
32. *Id.* at 262.
33. *Id.* at 262-63.
34. 505 U.S. 1003 (1992).
35. *Id.*
36. *Id.* at 1015.
37. *Id.* at 1018.
38. *Id.*
39. *Id.* at 124.
40. *Id.*
41. *Id.* at 130.
42. *Id.* at 124.
43. *Id.* at 138.
44. *Palazzolo v. Rhode Island*, 533 U.S. 606 (2001).
45. 483 U.S. 825 (1987)[hereinafter *Nollan*].
46. 512 U.S. 374 (1994)[hereinafter *Dolan*].
47. *Nollan*, *supra* note 45, at 828.
48. *Id.*
49. *Id.* at 837.
50. *Id.*
51. *Dolan*, *supra* note 46, at 377.
52. *Id.* at 379-80.
53. *Dolan*, *supra* note 46, at 388.
54. *San Remo Hotel L.P. v. City and County of San Francisco*, 27 Cal. 4th 643 (2002).
55. *Id.* at 668.
56. 27 Cal. 4th 643 (2002).
57. *Id.* at 668-69.
58. *Id.* at 668.
59. *Id.* at 676.
60. *Id.* at 673.
61. *Id.* at 687.
62. 535 U.S. 302 (2002).
63. *Id.* at 306.
64. *Id.* at 320.

65. *Id.* at 331-32.
66. *Id.*
67. *Id.*
68. 103 Cal. App. 4th 718 (2002)[hereinafter *Loewenstein*].
69. 17 Cal. 4th 1006 (1998).
70. *Loewenstein*, *supra* note 68, at 736.
71. *Landgate, Inc. v. California Coastal Comm'n*, 17 Cal. 4th 1006.
72. *Id.* at 1029.
73. *Loewenstein*, *supra* note 68, at 736-37.
74. *Galland v. City of Clovis*, 24 Cal. 4th 1003 (2001)[hereinafter *Galland*].
75. *Id.* at 1018.
76. *Kavanau v. Santa Monica Rent Control Bd.*, 16 Cal. 4th 761 (1997).
77. *Galland*, *supra* note 74, at 1008.
78. *Id.* at 1021.
79. *Id.* at 1018.
80. *Id.* at 1009.
81. *Brown Hayes v. Legal Found. of Wash. et al.*, 123 S.Ct. 1406 (2003)[hereinafter *Brown*].
82. 271 F.3d 835 (9th Cir. 2001)[hereinafter *Washington*].
83. An 11 judge panel of the ninth circuit.
84. *Washington*, *supra* note 82, at 857.
85. *Id.* at 857.
86. *Id.* at 856.
87. *Id.*
88. *Id.* at 864.
89. *Id.* at 857-58.
90. *Id.* at 860.
91. *Id.* at 861 (explanation added).
92. *Brown*, *supra* note 81.
93. *Id.* at 1416-17.
94. *See Washington*, *supra* note 82, at 864.
95. *Brown*, *supra* note 81, at 1419.
96. *See Philips v. Washington Legal Found.*, 524 U.S. 156, 172 (1998).
97. *Brown*, *supra* note 81, at 1419-21.
98. *Id.* at 1421.
99. *Id.* at 1428.
100. U. S. Const. Art. III.
101. *Williamson County Reg'l Planning Comm'n v. Hamilton Bank of Johnson City*, 473 U.S. 172 (1985)[hereinafter *Williamson*].
102. *Palazzolo v. Rhode Island*, 533 U.S. 606, 618 (2001)[hereinafter *Palazzolo*].
103. *Calprop Corp. v. City of San Diego*, 77 Cal. App. 4th 582, 590-91 (2000).
104. *Id.* at 593.
105. *North Pacifica, LLC v. City of Pacifica* 234 F. Supp.2d.1053 (ND Cal. 2002).
106. *Palozzolo*, *supra* note 102.
107. *Williamson*, *supra* note 101, at 191 (1985).
108. *Del Monte Dunes at Monterey, Ltd. v. City of Monterey*, 920 F.2d 1496, 1501 (9th Cir. 1990).
109. *Id.*
110. *Id.*
111. *Id.*
112. Cal. Civ. Proc. Code § 1084 et seq.
113. *See, e.g., Briggs v. City of Rolling Hills Estates*, 40 Cal.App. 4th 637 (1996); *see also* Cal. Civ. Proc. Code § 1094.5(a).
114. Cal. Civ. Proc. Code § 338(j).
115. *Id.* § 338.
116. California Constitution Article I, Section 19 states, "Private property may be taken or damaged for public use only when just compensation, ascertained by a jury unless waived, has first been paid to, or into court for, the owner. The Legislature may provide for possession by the condemnor following commencement of eminent domain proceedings upon deposit in court and prompt release to the owner of money determined by the court to be the probable amount of just compensation."
117. *Lee v. LA County Metropolitan Transit Auth.*, 107 Cal. App. 4th 848, 858 (2003).
118. *Patrick Media Group, Inc. v. California Coastal Comm'n*, 9 Cal. App. 4th 592, 607 (1992).
119. *Kong v. City of Hawaiian Gardens Redevelopment Agency*, 108 Cal. App. 4th 1028 (2002)[hereinafter *Kong*].
120. *Id.* at 1047.
121. *Id.*
122. Cal. Gov. Code § 65009, subd. (c)(1)(A)-(F); *see also*, Cal. Civ. Proc. Code § 1094.6, subd. (b). An informative summary of limitation periods applicable to local land use decisions is contained in Longtin's California Land Use (2d ed. 1987, Supp. 2000) § 12.34.
123. *Brown*, *supra* note 81, at 1419.
124. *Barham v. Southern Cal. Edison Co.*, 74 Cal. App. 4th 744, 751 (1999); *Chlour v. Community Redevelopment Agency*, 46 Cal. App. 4th 273, 279-80 (1996).
125. Cal. Civ. Proc. Code § 1263.320.
126. *Id.*
127. *City of San Diego v. Rancho Penasquitos Partnership*, 105 Cal.App. 4th 1013 (2003); *see also* Cal. Civ. Proc. Code § 1263.330.
128. *San Francisco Bay Area Rapid Transit Dist. v. M. Keegan*, 265 Cal.App.2d 263 (1968).
129. *People v. Kubic*, 254 Cal.App.2d 470 (1967).
130. *City of Long Beach v. Pacific Elec. Ry. Co.*, 44 Cal.2d 599 (1955).
131. *Kong*, *supra* note 119, at 1041.
132. *San Diego Metropolitan Transit Development Bd. v. Handlery Hotel, Inc.*, 73 Cal. App. 4th 517 (1999).
133. *Id.* at 531.
134. *See, e.g., Alмота Farmers Elevator and Warehouse Co. v. United States*, 409 U.S. 470 (1973).
135. *CUNA Mutual Life Ins. Co. v. Los Angeles County Metro. Transp. Auth.*, 108 Cal. App. 4th 382 (2003).
136. *Kong*, *supra* note 119, at 1042.
137. *See supra* note 124.
138. *See Klopping v. City of Whittier*, 8 Cal. 3d 39 (1072); *City of Ripon v. Sweetin*, 100 Cal. App. 4th 887 (2002); *City of San Diego v. Rancho Penasquitos Partnership*, 105 Cal. App. 4th 1013 (2003).
139. *Kong*, *supra* note 119, at 1045.
140. *Lynch v. Household Finance Corp.*, 405 U.S. 538, 552 (1972).