Comment

Multiple Permits, Temporary Takings, and Just Compensation*

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I. Introduction

NOWADAYS IN THE UNITED STATES, a building entrepreneur needs to get the approval of a number of public agencies before putting its project on the market. Zoning laws, subdivision regulations, building codes, safety rules, and environmental standards all must be satisfied. The projector is required to get multiple permits.

American local governments are well aware of the bargaining power that inheres to their ability to veto private projects. Some have undertaken to "leverage their police power"[1] by exacting favors, demanding discounts, and requiring kickbacks. The U.S. Constitution places limitations on the legality of such practices. As Justice Holmes said long ago in *Pennsylvania Coal Co. v. Mahon*,[2] when public demands go "too far," they constitute a taking of property in violation of the fourteenth amendment.[3]

In theory this constitutional prohibition against excessive regulation protects developers from overzealous regulators. In practice it affords little protection. A California city attorney speaking to the National Institution of Municipal Law Officers in 1974 described why.[4] He explained how cities could defend against attacks on land-use regulations, one at a time, and one after another, and "IF ALL ELSE FAILS, MERELY AMEND THE REGULATION AND START OVER

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1. Justice Scalia coined the phrase "leverage their police power" in Nollan v. California Coastal Comm'n, 483 U.S. 825, 836–37 n.5 (1987) (Scalia, J.).

2. 260 U.S. 393 (1922).

3. *Id.* at 415.

4. *See* San Diego Gas & Electric Co. v. City of San Diego, 450 U.S. 621, 655–56 n.22 (1981) (Brennan, J., dissenting).

AGAIN.''[5] The locality could ''lose the battle and still win the war.''[6]

The city attorney's unlawyer-like burst of candor galvanized Justice Brennan to dissent in *San Diego Gas & Electric Co. v. City of San Diego*.[7] Brennan opined that once a court found a police power regulation had effected a ''taking'' then ''the government entity must pay just compensation for the period commencing on the date of regulation first affecting the 'taking' and ending on the day that the government entity chooses to rescind or otherwise amend the regulation.''[8] He explained why: ''Such liability might . . . encourage municipalities to err on the constitutional side of police power regulations, and to develop internal rules and operating procedures to minimize overzealous regulatory attempts.''[9]

Brennan's trial balloon rendered the land regulation lobby aghast. Self-styled ''police power hawks'' condemned the award of damages for temporary regulatory takings as ''a seductively simplistic notion'' and prophesied doom as the chilling prospect of dollar responsibility deterred local officials from making hard but necessary choices.[10] Notwithstanding these criticisms, just six years later Brennan's view was embraced by a majority of the Supreme Court in *First English Evangelical Lutheran Church v. County of Los Angeles*.[11]

This paper considers who has the better of the argument. It looks at two fictions from the American land control scene. The moral of these tales may provide a good answer to the questions of *whether* and *when* compensation should be awarded for temporary takings.

II. The Avalon City Story

Avalon City is an old rustbelt port in the northeastern United States. Under the leadership of its cantankerous mayor, Meyer Mayer, it has undergone a renaissance of sorts. A festival marketplace has been created in the old harbor area which attracts more tourists per square foot, per year, than Disneyland. Another of Mayor Mayer's built-in successes is a meticulous historic restoration of the old City Hall.

As the City Hall restoration was proceeding in 1983, Bertram Builder, a politically well-connected contractor acquired for the price of

5. *Id.*
6. *Id.*
7. *Id.* at 636.
8. *Id.* at 658.
9. *Id.* at 661 n.26.
10. *See* Williams, Smith, Siemonn, Mandelker & Babcock, *The White River Junction Manifesto*, 9 VT. L. REV. 193 (1984).
11. 482 U.S. 304 (1987).

$500,000 the old Avalon Hotel that stood catty-corner across the street. The Avalon had seen better days and was then a hotel for transients standing as a buffer between the municipal buildings and the adult entertainment district. Structurally it was a sound masonry structure of some architectural interest, but Builder, by moving fast and using his political clout, was able to raze the building before the architectural preservationists could mount a defense.

In 1983, once the building lot was vacant, Builder surveyed his options and determined to build a six-story office building with 50,000 net rentable square feet. Builder's plans were consistent with existing zoning laws; accordingly he was given a building permit by the city's Department of Housing. During the 1983-84 period of construction, building inspectors visited the site daily and approved the construction practices. Construction of the new office building cost $5.5 million.

In June 1984, when the building was substantially completed but still not finally approved for occupancy, Builder sold it for $6.5 million to Russell Rentier who owned and leased out a number of downtown commercial properties.

Pursuant to the terms of the contract of purchase, Rentier was responsible for obtaining all final permits necessary for the occupancy of the new building. However, he was not terribly concerned because his lawyers and engineers indicated that it substantially met all legal requirements. His reasonable expectation was that within six months (by January 1, 1985) he would obtain these approvals and have leased the space at $20 per square foot so as to produce gross income of $1 million per year.[12] After subtracting operating expenses, maintenance costs, taxes, and setting aside a reserve for depreciation, Rentier reasonably expected to receive $700,000 in net income per year.

Mayor Meyer Mayer had watched the building go up with pride and satisfaction. He counted it as yet another example of Avalon's renaissance. In the fall of 1984 he developed a more particular interest in the building. It occurred to his Honor, the mayor, that it was just the place in which to expand overcrowded city offices. Accordingly, he directed the acquisition agent in the City Solicitor's office to begin negotiation with Rentier with a view towards acquiring the building.

Negotiations bogged down; the parties were far apart in price. Rentier felt that capitalization of his net income projections for the building at a rate of 10 percent suggested a fair market value of at least $7 mil-

12. 50,000 sq. ft. × $20 = $1,000,000.

lion.[13] The city, aware of Bertram's investment[14] and the recent sale price to Rentier,[15] was unwilling to pay more than $6.7 million. Rentier proceeded with his plans to put the office space on the private market. At a staff meeting with his department heads in September of 1984, Mayor Meyer Mayer described the breakdown in negotiations and expressed his displeasure.

Several weeks later Rentier went to the Department of Housing to obtain an occupancy permit. The City Code required that, in order for an occupancy permit to be issued, the building inspector first make a determination that the building complied with all city ordinances and regulations. A procedure existed whereby applications were circulated to the fire department, the water and sewer division, and the chief building inspector to determine compliance.

Rentier's occupancy permit met a series of obstacles. The application was first sent to the fire marshall. It took him six months to reach a decision. After inspecting the premises and finding them in complete compliance with the requirements for a "fire proof" building, he nonetheless denied approval. In an April 1985 letter to the Department of Housing, he explained that approval was denied because the fire department was inadequately funded by the city council. He allowed that unless there was a 25 percent increase in the department's operating budget that the building could not be safely occupied. Rentier was notified of the grounds upon which his application for an occupancy permit was refused.

In May of 1985, Rentier brought suit in the Circuit Court for Avalon City and sought a writ of mandamus ordering the fire marshall to give his approval to the application for an occupancy permit. When the case came to trial, a year later in May of 1986, the court so ordered, holding that it was *ultra vires* to deny approval based upon the fire department's shortage of operating funds over which the applicant had no control or responsibility.

In June of 1986, Rentier's application for a occupancy permit was sent to the water and sewer division to determine whether the building would be provided with water and sewer hookups. In reviewing the application, the division head found that it had sufficient available capacity to provide water and sewer service for the building. The division head determined, however, to impose a condition on the hookups pursuant to the provisions of the newly-enacted Avalon City Ordinance § 2115 (1986), which provided, *inter alia*: "[A]gencies of Avalon City

13. 700,000 ÷ .10 = 7,000,000.
14. Land—$500,000 + Building—$5,500,000 = $6,000,000.
15. $6.5 million.

may condition exercises of their police power on the willingness of the regulated parties to agree to serve the *pro bono publico.*''

In December 1986, the division head notified the building engineer who in turn notified Russell Rentier that water and sewer service would be provided only if Rentier was willing to enter into a ten-year lease with the city pursuant to which a ground floor suite in the building would be leased at $4 per square foot for use as a day care center for the children of city employees.

Rentier refused to enter into such a lease, publicly attacking it as ''outright extortion,'' and the occupancy permit was withheld. When efforts to resolve the deadlock broke down in June of 1987, Rentier brought a suit in the Circuit Court for Avalon City in which he sought an injunction ordering the division of water and sewer to remove the condition. Because of a judicial backlog, the case took nine months to come to trial. In April of 1988, the court ordered removal of the condition because there was no ''rational nexus between the exaction and the burden which the new office building would impose on the community.''

The application for a occupancy permit was next considered by the building engineer to determine whether it complied with all provisions of the building code. Under an antiquated provision still on the books, all plumbing was required to be of either copper or galvanized pipe. For the past ten years, however, the housing department has permitted the use of plastic pipe which is generally viewed in the trade as a cheaper and better substitute. During the course of construction, the office of the building inspector had given informal approval to building plans calling for the use of plastic pipe and, on weekly inspections, the building inspector had made no complaint.

In July of 1988 the building engineer determined to require a literal compliance with the Code after all. He turned down Rentier's permit on the grounds that the plumbing was in noncompliance. It would have cost approximately $100,000 for Rentier to redo the plumbing in the office building. Instead he brought suit in the Circuit Court for Avalon City challenging the denial of the building permit. In September of 1989, after a one year delay, the court decided for Rentier finding that literal compliance with the Building Code's requirement that copper or galvanized pipe be used had been waived, and issued an order of mandamus ordering issuance of the permit.

Finally, Rentier's tenacity was rewarded. In October of 1989, he was given an occupancy permit and, on January 1, 1990, the building had a formal opening with all the space rented out at $20 per square feet, exactly five years later than he had originally expected.

This cautionary tale of the risks which developers face when dealing with a city intent on muscling its police power creates a compelling case for relief under the fourteenth amendment. The threshold question is whether it ought to come under the "due process" clause or the "taking clause." Some courts and commentators have argued that unprincipled regulatory behavior should be redressed as a violation of due process.[16] They argue that the gravamen of the landowner's complaint is unprincipled bureaucratic behavior—quite literally a denial of the process to which they are due, and put down a theory of regulatory takings as novel and mischievous.[17] But for substantive and procedural reasons, the disappointed developer is better served by the "taking" clause.

In some respects, the choice of theory is immaterial. Regardless of whether relief is sought on due process or taking grounds the standard of review is the same: "When a court passes judgment on the municipalities' conduct" it does not "seek to second-guess the 'reasonableness' of the city's decision nor to interfere the local government's resolution of competing policy considerations."[18] In both cases, the aggrieved party must prove by a preponderance of the evidence that the municipality has failed to conform to "the requirements of the Federal Constitution."[19]

It is in other respects that the "taking" clause is the less burdensome. Under a due process approach, the aggrieved party must establish that the municipal actions were "clearly arbitrary and unreasonable, having no substantial relation to the public health, safety, morals, or general welfare."[20] Russell Rentier could attempt to satisfy this burden with evidence that he was the victim of a conspiracy to depress the value of his land so the city could acquire it at a discount—a proposition likely to be true but virtually impossible to prove. Rentier is out of court.

When the landowner is protected from overzealous regulation under the "taking" clause, however, the focus of the inquiry shifts to the objective issue of whether the land-use regulations deny all economically viable use of his land.[21] Russell Rentier and his accountant have the necessary facts at their disposal. They can prove "the extent to which the regulation has interfered with distinct investment backed expecta-

16. *See, e.g.*, Fred F. French Investing Co. v. City of New York, 39 N.Y.2d 587, 350 N.E.2d 381, 385 N.Y.S.2d 5 (1976); F. BOSSELMAN, D. CALLIES & J. BANTA, THE TAKING ISSUE 238 (1973).

17. *See* sources cited in *supra* note 16.

18. Owen v. City of Independence, 445 U.S. 622, 649 (1980).

19. *See id.*

20. Euclid v. Ambler Realty Co., 272 U.S. 365, 395 (1926).

21. *See* First English Evangelical Lutheran Church v. County of Los Angeles, 482 U.S. 304 (1987).

tions.''[22] While the landowner's claim is certainly enhanced by proof that he was ''singled-out'' for disfavored treatment, that is not a necessary element of his case. A magnitudinous loss combines with a hint of bias to make the case.[23]

Moreover, landowners have an important procedural stake in a guarantee of redress under the ''taking'' clause. When seeking damages for unconstitutional misconduct by state or local officials, litigants feel a particular need for federal protection. The Warren Court met this need by reinterpreting 42 U.S.C. § 1983 to provide both declaratory and monetary relief against state and local deprivations of ''due process'' and other federal rights.[24] But the Supreme Court seems to be having some second thoughts about allowing monetary relief. Recently it immunized the state government, itself, against any liability for damages under section 1983 in both federal and state courts.[25] Moreover, the Court determined that local governments would only be liable in damages under section 1983 for acts ''officially sanctioned or ordered.''[26] No redress is afforded against an informally encouraged pattern of overzealous behavior of the sort described in the Avalon City story. When pursuing a due process claim for damages under section 1983, the aggrieved party is no longer guaranteed a day in court.

The taking clause on the other hand is self-executing.[27] Regardless of the interpretation of section 1983, litigants are constitutionally assured an opportunity to recover damages if a regulation ''goes too far.''[28] The eleventh amendment to the U.S. Constitution prohibits federal courts from hearing suits against a state, but the aggrieved party is guaranteed access to state court.[29] If the suit is against a local government, both state and federal courts have jurisdiction.[30]

Therefore, under a taking theory, Russell Rentier would have a

22. Penn Central Transp. Co. v. City of New York, 438 U.S. 104 (1978). This is the key factual question in determining whether there is a regulatory taking. Under either a taking or due process challenge the claim of the plaintiff is advanced if he can show that he has been ''singled out'' for adverse treatment. *See id.* at 132–34. Since this is an equal protection notion the three strands of the fourteenth amendment become even more intertwined.

23. *See, e.g.*, Vernon Park Realty v. City of Mount Vernon, 307 N.Y. 493, 121 N.E.2d 517 (1954).

24. *See* Owen v. City of Independence, 445 U.S. 622 (1980); Monell v. Department of Social Servs., 436 U.S. 658 (1978); Monroe v. Pape, 365 U.S. 167 (1961).

25. Will v. Michigan State Police, 491 U.S. 58 (1989).

26. St. Louis v. Praprotnik, 485 U.S. 112, 123 (1988).

27. United States v. Clarke, 445 U.S. 253, 257 (1980).

28. *See* Pennsylvania Coal Co. v. Mahon, 260 U.S. 393, 415 (1922).

29. Lake Country Estates v. Tahoe Regional Planning Agency, 440 U.S. 391, 400–01 (1979).

30. *See* 260 U.S. at 419–20.

lighter burden of proof and better access to an unbiased tribunal. The "taking" theory does have its downside, however. In order to qualify for relief, the claimant must satisfy the court that he has pursued his administrative remedies to the point that the taking of the property interest has ripened.[31] Omnipresent is the argument that the local officials might have deregulated if the landowner had only exhausted one more state remedy.[32] But Russell Rentier has met even the most rigorous requirements of ripeness and exhaustion of state remedies. Through extensive and expensive litigation he has finally freed his land from the unlawful restraints.

The question remains as to whether the fact that these restraints proved temporary ought to disqualify Rentier from recovering the value of the property taken. To this question, our sense of justice and economics provide an easy answer: Of course not! Unlawful regulations took from Rentier a stream of gross income in the amount of $1 million per year, for five years. The fact that unlawful regulations were eventually overturned sensibly relates only to the measure of Rentier's loss, not whether it ought to be compensable.

The U.S. Supreme Court has recognized in condemnation cases that the "rental that probably could have been obtained" is the proper measure of compensation.[33] The same measure seems appropriate in inverse condemnation cases such as this one. The first step is to determine Rentier's net rental loss. Such a determination might disclose, for example, that while Rentier was denied $1 million in annual gross rents, he saved $280,000 in annual operating expenses for a net revenue loss of $720,000 per year, or $60,000 per month.

Therefore, assuming that Russell Rentier lost a stream of net rent of $60,000 per month for five years, he is entitled to recover $3.6 million[34] along with compound interest from the date when each rent payment was due. A financial table is available to capitalize the measure of compensation.[35] If we assume that rent in the amount of $60,000 would have been paid at the end of each month, and assume an interest rate of 10 percent (which appears to an accurate estimate of the market rate of return which Rentier is able to achieve on his investments), then mathe-

31. *See* Williamson County Regional Planning Comm'n v. Hamilton Bank, 473 U.S. 172 (1985).

32. *See* First English Evangelical Lutheran Church v. County of Los Angeles, 482 U.S. 304 (1987).

33. Kimball Laundry Co. v. United States, 338 U.S. 1 (1949).

34. $60,000 × 60 = $3,600,000

35. *See* P. GOEBEL & N. MILLER, HANDBOOK OF MORTGAGE MATHEMATICS & FINANCE TABLES 79–81 (1981).

matical analysis tells us that the measure of Rentier's loss on January 1, 1990, was $4,646,224. This amount would continue to grow at a compound rate of 10 percent until payment is actually made.

* * *

In other real estate contexts the question of whether a temporary taking requires compensation may be much in doubt. Consider the following:

III. The Avalon County Story

Avalon County is a growing county surrounding Avalon City on three sides. Today it is a sprawling mix of first and second-class houses, garden apartments, old business centers, high-rises, commercial strips, light industry, glitzy malls, and a few farms. But in 1960, when Rita Rustic bought fifty hardscrabble acres for $5,000, it was mostly rural. Rustic bought the vacant land, although it was unsuitable for agriculture, on the whimsical theory that someday it might be worth something. She paid the insignificant taxes and occasionally sent a man out to whack the bushes and kill the poison ivy.

In the 1980s, local officials began searching for a location for a sanitary landfill to accommodate the county's ever-growing supply of garbage. Rustic's fifty-acre tract was not among the preferred sites. As opposition mounted at other locations, however, it came under consideration. It appeared as one of several alternative sites in a planning document published by the county planning department in 1983.

Pursuant to state enabling legislation, the Board of Commissioners of Avalon County was empowered to place lands being considered for public acquisition in "reservation":

> to reserve for parks, playgrounds, and other public purposes provided that said reservation shall continue for no longer than five years and provide further that the properties so reserved shall be exempt from all State and county taxes during the period.

State legislation went on to provide:

> During the reservation period, no building or structure shall be erected upon the land so reserved. No trees, topsoil, or cover shall be removed or destroyed; no grading shall be done; nor shall any land so reserved be put to any use whatsoever, except upon written approval of the Board of County Commissioners.[36]

36. The quoted regulations are adapted from those in force in the Maryland-Washington Metropolitan District in Montgomery and Prince George's Counties, Maryland. *See* Maryland Nat'l Capital Parks & Planning Comm'n v. Chadwick, 286 Md. 1, 405 A.2d 1064 (1979).

On December 31, 1984, Rustic was notified by registered mail that her fifty-acre parcel had been placed "in reservation" until December 31, 1989.

Rustic was not averse to selling the property to Avalon County at a nice profit, but felt that the reservation left her land in limbo. Her lawyer advised her that although the reservation procedure was constitutionally suspect, the costs and delays involved in a challenge were too great to make it worth her while. She decided to wait and see what happened.

In 1988 Rustic lost an opportunity to make some money on the property when the Avalon Sand and Gravel Company offered to pay her $100 per ton for mining rights. The firm estimated that it would take approximately 5,000 tons. Pursuant to the terms of the reservation legislation, Rustic applied to the Board of Commissioners for permission to permit sand and gravel mining, but it was summarily denied.

December 31, 1989 came and went without the county ever acquiring Rustic's fifty acres. The five year reservation expired and Rita Rustic now reconsiders whether there has been a temporary taking of her property entitling her to just compensation.

Common law and common sense agree that there was a taking. The reservation legislation was designed to capture a public benefit not to prevent a public harm. She was deprived of all reasonable use of her property. Placing Rustic's land in reservation for five years amounted to a virtual freeze on the use of the property in its entirety.[37] The reservation legislation itself seems to recognize that there is a temporary taking since it exempts the property from real estate taxes for the duration.

The question of whether Rustic is constitutionally guaranteed compensation is a much more difficult one. It is not at all apparent that she has suffered any economic loss. Since she made an investment decision to hold nonproductive land we know of no income interest she lost. She lost a profit on the sale of the sand and gravel, but it is still in the ground to be sold another day. Furthermore, a proscription on its taking will probably be justified as a nuisance-prevention measure.

The events in Avalon County highlight another complication in the constitutional treatment of regulations which work a temporary taking of property. Where non-income producing property is involved the speculator may have suffered no loss. She has the burden of proof to establish that she was prevented from taking a speculative profit when

37. *Accord* Maryland-Nat'l Capital Park and Planning Comm'n v. Chadwick, 286 Md. 1, 405 A.2d 1064 (1979).

the market was up. In the absence of proof of a lost opportunity to seize a capital gain the measure of just compensation is zero.

IV. Conclusion

As our stories indicate, delay is endemic under the system of multiple permits presently used to regulate the use of land. Sometimes this delay can result in a taking of property under the Supreme Court's interpretation of the fourteenth amendment of the U.S. Constitution. The argument that temporary takings should not be compensated is misguided. Good economics and good government demand compensation. Time is money; cost internalization keeps the locals honest.

The "police power hawks" should prey instead on the issue of just compensation. Difficult analytical and factual questions must be answered. Distinctions between income-producing property and vacant land dictate different measures. Sometimes the government owes a lot, sometimes a little, and sometimes nothing. Only an eagle's eye assures that awards are neither too large or too small.