OREGON REAL ESTATE AND LAND USE DIGEST

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CLE Announcement

Stop Predatory Mortgage Lending

A CLE sponsored by the Consumer Law Section of the Oregon State Bar, the Oregon Department of Justice Civil Enforcement Division and the Oregon Consumer League is presented by experts from the National Consumer Law Center on June 6th and 7th, 2002 at the Oregon State Bar Center in Lake Oswego. CLE materials include NCLC's "Stop Predatory Lending" manual and CD-ROM (239 pages, published March 2002), a $50 value. Cost: $275, advance registration $250; Space is limited, advance registration is encouraged. The day and a half agenda includes 10 general CLE credits, 1 ethics credit (applied for, not yet approved).

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Article

New Reverse-Exchange Revenue Procedure

On September 15, 2000, the Internal Revenue Service issued Revenue Procedure 2000-37. The new procedure provides a safe harbor for taxpayers in structuring a reverse tax-free exchange. The new revenue procedure embodies a liberal approach but may force taxpayers who are not sure whether they can sell their relinquished property within Rev. Proc. 2000-37's restrictive timelines to choose between the new safe harbor or a traditional (but riskier) reverse exchange.

Background

In a reverse exchange, the replacement property is acquired before the relinquished property is sold. By contrast, in a deferred-forward exchange structured under Section 1031 of the Internal Revenue Code, the relinquished property is exchanged and sold first, and the replacement property is acquired within 180 days of the sale. In most reverse exchanges an accommodator will hold either the relinquished property or the replacement property. This is known as "parking" the property.

There are two types of reverse exchanges. In one type of reverse exchange, the accommodator holds the replacement property until after the relinquished property is sold. When the relinquished property is sold, the taxpayer transfers the relinquished property to the accommodator (or by direct deed to the buyer), who simultaneously transfers the replacement property to the taxpayer. In the other form of reverse exchange, the accommodator immediately exchanges the relinquished property for the replacement property. The accommodator holds the relinquished property (as opposed to the replacement property) until it is sold.

From the perspective of tax practitioners, traditional reverse exchanges have always been considered riskier than forward exchanges. In a forward-deferred exchange there are safe-harbor regulations to protect the taxpayer, but until now there were no IRS pronouncements approving a reverse exchange (see Treas. Reg. § 1.1031(k)-1(a)). Further, only a few cases support reverse exchanges. The most commonly cited are *Biggs v. C.I.R.*, 69 T.C. 905 (1978), aff'd, 81-1 U.S.T.C. (CCH) ¶ 9114 (5th Cir. 1980), *J. H. Baird Publ'g Co. v. C.I.R.*, 39 T.C. 608 (1962), and *In re Exchanged Titles, Inc.*, 159 B.R. 303 (Bankr. C.D. Cal. 1993). In order to complete a reverse exchange, tax lawyers have traditionally attempted to give the accommodator the majority of the benefits and burdens of ownership with respect to the parked property and have attempted to structure transactions using arm's-length provisions in purchase agreements, puts, calls, leases, and management agreements.

Qualifying Arrangement

Rev. Proc. 2000-37 now provides a safe harbor to a taxpayer who wishes to complete a reverse exchange. If the following six requirements are met, the IRS will not challenge (thus creating a "safe harbor") the characterization of property as relinquished property or replacement property in a tax-free exchange.

(1) Ownership. The property must be owned by an "exchange accommodation titleholder" who is not the taxpayer or a disqualified person as defined in Treas. Reg. § 1.1031(k)-1(k). In general, a disqualified person is a person who is not related to the taxpayer. As discussed below, the exchange accommodation titleholder can also be a qualified intermediary under Treas. Reg § 1.1031(k)-1(g)(4). For simplicity, this article will refer to the title-holding entity, which will often be the qualified intermediary, as the accommodator. The accommodator must either hold a deed to the parked property or be a purchaser under a real estate contract. The revenue procedure also requires that the accommodator either be a taxpaying entity or, if it is a partnership or an S-corporation, have a 90 percent of its interests owned by a taxpaying entity. Rev. Proc. 2000-37 makes it clear that it is permissible for the accommodator to own the property through a single-member limited liability company, which is a disregarded entity for tax purposes under Treas. Reg. § 301.7701-3(b)(1).

(2) Intent. The taxpayer must have a bona fide intent that the property held by the accommodator be used as either relinquished property or replacement property in a tax-free exchange. This requirement is the same as the requirement found for a traditional forward exchange. Treas. Reg. § 1.103(k)-1(j)(2)(iv).

(3) Required Contract Provisions. The accommodator and the taxpayer must enter into an agreement providing that the accommodator is "holding the property for the benefit of the taxpayer in order to facilitate an exchange under section 1031" and Rev. Proc. 2000-37. The agreement must also provide that the accommodator will be treated as the owner of the parked property for federal income tax purposes and that both parties will report the transaction in a manner consistent with the agreement. This agreement must be entered into no later than five business days after the parked property is transferred to the accommodator.

Accordingly, accommodators must file tax returns that report lease income and deduct interest expenses, depreciation, and other costs of operating the parked property. Accommodators who are alarmed at the increased bookkeeping requirements may be able to avoid being forced to claim depreciation by providing in the lease agreement that the taxpayer-tenant has the obligation to restore the value of the property at the expiration of the lease term. *Terre Haute Elec. Co. v. Commissioner*, 21 AFTR 118, 38-1 USTC 9228, 96 F.2d 383 (7th Cir 1938); *Hibernia Nat'l Bank v. United States*, 54 AFTR 2d 84-5868, 740 F.2d 382 (5th Cir. 1984).

(4) Identification Requirement. Within 45 days after the accommodator acquires title to the parked replacement property, the relinquished property must be identified. The "identification must be made in a manner consistent with the principles described in section 1.1031(k)-1(c)." It is not clear whether this reference to the "principles" of the regulations refers only to issues such as signing and delivery of the designation, or whether it also refers to the number of replacement properties that can be designated. If so, one of three tests would have to be met: (1) not more than three relinquished properties can be designated, or (2) more than three relinquished properties can be designated if their value does not exceed 200 percent of the value of the replacement property, or (3) more than three relinquished properties can be designated if 95 percent of the value of all the relinquished properties designated are actually used as relinquished property in the tax-free exchange.

(5) Receipt Requirement. Within 180 days after the accommodator acquires title to the parked property, the property must be transferred to the taxpayer as replacement property or to a buyer as relinquished property in a tax-free exchange. The revenue procedure provides that if the property is not transferred to the taxpayer as replacement property, it cannot be transferred to a disqualified person. Therefore, the revenue procedure cannot be used in a related-party exchange under Section 1031(f) if the purchaser of the relinquished property is a related party. The identification requirement and receipt requirement for reverse exchanges were first suggested by the American Bar Association in 1993. *See ABA Section of Taxation, Report on the Application of Section 1031 to Reverse Exchanges*, 21 J. Real Est. Tax'n 44 (1993).

The receipt requirement is worded in such a way that all the parked property must be transferred to the taxpayer. It provides that no later than 180 days after receipt by the accommodator, "the property is [either] transferred . . . to the taxpayer as replacement property; or . . . transferred [to a buyer] as relinquished property." The language appears to preclude bifurcating a single reverse exchange into a safe-harbor reverse exchange and a traditional reverse exchange. The taxpayer, for example, cannot use 50 percent of the replacement property within the 180-day replacement period as replacement property for relinquished property Blackacre, while using the remaining 50 percent of the replacement property outside of the 180-day replacement period as replacement property for relinquished property Whiteacre.

It also appears that the language of the revenue procedure prevents a single parcel of property from being used as replacement property for two taxpayers. For example, a single accommodator cannot hold replacement property and then transfer 50 percent to taxpayer X as replacement property and the remaining 50 percent to taxpayer Y as replacement property. This problem could be solved if taxpayer X and taxpayer Y each had a separate accommodator and each accommodator purchased only an undivided one-half interest in the parked replacement property. The revenue procedure does not specifically provide that two taxpayers who co-owned the relinquished property and were both parties to the same exchange agreement (as would be the case with most husband-and-wife transactions) would be treated as the "taxpayer," but it is doubtful that the IRS intended to preclude this very common situation.

It should also be pointed out that if a reverse exchange is converted into a forward exchange, the identification and replacement requirements must be adhered to. For example, a taxpayer may wish to complete improvements to the replacement property held

by the accommodator after the relinquished property is sold. If so, the taxpayer must also comply with the forward-exchange requirements for identification of the replacement property within 45 days and receipt of the replacement property within 180 days after the taxpayer conveys the relinquished property.

(6) Total Holding Period. The combined period that the accommodator holds any parked property (relinquished property or replacement property) cannot exceed 180 days. This requirement is somewhat problematic. Traditionally, a reverse exchange was often used to extend the 180-day period for completing improvements to replacement property, thus avoiding taxable boot to the taxpayer. This strategy will not be available for a taxpayer who elects to take advantage of Rev. Proc. 2000-37's safe harbor.

Permissible Agreements

In addition to laying out the six requirements necessary to fall within the safe harbor, Rev. Proc. 2000-37 approves seven different types of legal relationships regardless of whether such arrangements, such as leases, purchase agreements, puts, and calls, include "arm's length" terms.

(1) Title Holder as Qualified Intermediary. The accommodator who holds title to the parked property may act as a qualified intermediary under Treas. Reg. § 1.1031(k)-1(g)(4). Thus, the title-holding accommodator can also act as the exchange accommodator if the title-holding accommodator can meet the requirements of a qualified intermediary.

(2) Guaranty Arrangements. The taxpayer may guarantee the obligations of the accommodator to purchase the parked property. The taxpayer may also indemnify the accommodator against costs and expenses.

(3) Loans. The taxpayer may loan funds to the accommodator or guarantee a loan to the accommodator. The revenue procedure allows all of the permissible agreements to contain terms that are not at arm's length. Thus, no interest need be charged on the loan to keep it within the revenue procedure's safe harbor. However, failing to charge interest may cause the loan to be treated under the imputed interest rules under Section 7872.

(4) Leasing Arrangements. The parked property can be leased to the taxpayer. Leasing the property from the accommodator to the taxpayer is very common in reverse exchanges. Under Rev. Proc. 2000-37, taxpayers need not be concerned about being charged market lease rates. For example, the lease amount might be set an amount equal to the mortgage payments against the parked property plus all other costs of holding the parked property.

(5) Taxpayer as Contractor. The taxpayer can manage the parked property or act as a contractor or supervisor to improve the parked property. These activities are also routinely done in traditional reverse exchanges that involve improvements to the replacement property. The benefit of the new Rev. Proc. 2000-37 is that these activities are now approved. But a taxpayer should not act as a contractor and receive a profit because that might be seen as a violation of the G6 rules. The G6 rules (from Treas. Reg. § 1.1031(k)-1(g)(6)) provide that a taxpayer cannot withdraw funds held by an accommodator until the exchange is completed.

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(6) **Purchase Agreements, Puts, and Calls.** The taxpayer and the accommodator may enter into purchase agreements, puts, and calls with respect to the parked property as long as they are for a period of not more than 185 days (5 days past the 180-day replacement period) from the accommodator's acquisition of the parked property. Purchase agreements, puts, and calls can be at a fixed or formula price, thus freeing tax lawyers from attempting to fashion market-rate provisions in such agreements. Thus, a taxpayer who wishes to take advantage of Rev. Proc. 2000-37, but is not sure that the sale of his relinquished property can close within the 180-day replacement period, cannot automatically convert to a traditional reverse exchange. Such a conversion cannot be accomplished because the applicable legal documents must provide that the right to force the accommodator to transfer the parked property to the taxpayer must cease after 185 days! Further, the leases and options may not have been structured using arm's length terms that are not required under Rev. Proc. 2000-37. If the taxpayer realizes that he will not be able to sell the relinquished property within the 180-day replacement period, he could seek to extend the date of the call or option agreement to a period beyond the 185-day deadline. Obviously, the accommodator would have to consent to such an extension.

(7) **Arranging for Parking Relinquished Property.** In a parking arrangement where the relinquished property is parked, it has always been very difficult to structure the documentation so that if the relinquished property is ultimately sold for more than the amount envisioned by the taxpayer, the taxpayer could recover the excess. This problem generally occurred only if the amount owed by the accommodator on various loans secured by the parked relinquished property was less than the sales proceeds from the sale of the relinquished property. If such an outcome was a possibility, this structure was usually not recommended. If the agreements provided that the taxpayer could recover the excess proceeds from the accommodator, it would be easy for the IRS to argue that the taxpayer and not the accommodator had most of the benefits and burdens of ownership with respect to the parked relinquished property. Rev. Proc. 2000-37 now makes it clear that such arrangements will not cause the exchange to be taxable. Of course, unless such excess cash was used to purchase additional replacement property, the cash would be distributed to the taxpayer in the form of taxable boot.

Conclusion

The new rules make it clear that a taxpayer can choose to either use Rev. Proc. 2000-37 or structure a reverse exchange using the traditional method with its inherent tax risks. If the taxpayer is sure that a particular relinquished property can be sold to a buyer within the 180-day period, Rev. Proc. 2000-37 provides a risk-free approach to structuring the exchange. But many taxpayers are unsure which of several possible relinquished properties will eventually be sold and, even if a particular replacement property is under contract to sell, whether in fact the transaction will close within the 180-day replacement period. In this situation, the taxpayer may want to structure the transaction under Rev. Proc. 2000-37, with the possibility of converting the transaction to a traditional reverse exchange. If conversion is a possibility, the entire transaction must be structured using the more conservative arm's length terms in leases, purchase agreements, puts, and calls so that the majority of benefits and burdens of the parked property reside with the accommodator, and the taxpayer must also obtain the consent of the accommodator to extend the period to acquire the parked property beyond 185 days.

Rev. Proc. 2000-37 is a welcome arrow in the quiver of taxpayers attempting to structure tax-free exchanges. The new safe-harbor procedure is a refreshingly practical approach by the IRS to completing reverse exchanges. It will undoubtedly be used by many taxpayers.

Ronald A. Shellan

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Appellate Cases—Land Use

ORS 687.195 Held Inapplicable to Seasonal Farm Worker Housing on EFU Land

Durig v. Washington County, 177 Or. App. 227 (2001), involved a challenge to LUBA's interpretation of ORS 197.685, which discusses consideration for the establishment of seasonal farm worker housing. This was the second time that the Court of Appeals heard this case. In its first opinion, the court affirmed LUBA's remand of Washington County's decision to approve the requested farm worker housing. *During v. Washington County* (Durig I), 158 Or. App. 36, 969 P.2d 401 (1999).

In this case, Washington County approved respondent Townsend Farms, Inc.'s application to site housing for approximately 391 seasonal farm workers (a slightly reduced number) on the same 33-acre site zoned exclusive farm use (EFU) at issue in *Durig I. Durig v. Washington County (Durig II),* 177 Or. App. 227, 229 (2001). The housing was to consist of 33 manufactured dwellings as well as various buildings already on the site. Water was to be provided by an existing well, and parking, lawn areas, lighting, utilities, and other amenities were to be provided. Petitioners were neighbors of the property who sought to block this development on the grounds that there was not a need for the housing, Townsend Farms failed to consider alternative sites for the housing, and the housing would constitute an urban use in a rural area.

In their first assignment of error, petitioners argued that Townsend Farms failed to establish a need for the workers or that the proposed site was the only site where the workers could be housed. The Court of Appeals addressed these arguments in reverse order. First, the court addressed whether ORS 197.685(2) requires that an applicant for seasonal farm worker housing on EFU land undertake an analysis of whether the housing could be sited on other nonresource land. *Id.* at 230. ORS 197.685(2) states:

> When a need has been shown for seasonal farm-worker housing within the rural area of the county, needed housing shall be permitted in a zone or zones with sufficient buildable land to satisfy that need. Counties shall consider rural centers and areas committed to nonresource uses in accommodating the identified need.

LUBA decided in *Durig I* that ORS 687.195(2) required counties to consider alternatives such as rural centers and committed areas. However, in *Durig II*, LUBA reversed itself, saying that ORS 687.195(2) was unclear as to whether the obligation to consider alternatives was to be imposed on counties at the legislative level or by individual applicants. LUBA concluded that ORS 687.195(2) imposed a legislative duty on counties only. *Id.* at 230–31.

The court analyzed ORS 687.195(2) in the context of various other statutes addressing seasonal farm worker housing, including ORS 215.213(1)(r) and ORS 215.283(1)(r). The court found that whereas ORS 215.213(1)(r) and ORS 215.283(1)(r) list seasonal farm worker housing as an outright permitted use on EFU land, ORS 687.195(2) directs consideration of placement of such housing on nonresource land. The court also noted that ORS 687.195(3) protects counties' authority to set approval standards for such housing and the statute as a whole permits counties to site seasonal farm worker housing on nonresource land. *Id.* at 233. However, ORS 197.685(4) prohibits counties from imposing approval standards that discourage seasonal farm worker housing. The court found that this provision prohibits counties from imposing standards on such housing on EFU land. *Id.*

The court ruled that ORS 687.195 was inapplicable to seasonal farm worker housing on EFU land and did not require an analysis of alternative nonresource sites when such housing is requested. *Id.* at 234. The court cited as authority the Oregon Supreme Court's decision in *Brentmar v. Jackson County*, 321 Or. 481, 496, 900 P.2d 1030 (1995), wherein the court found that the uses listed in ORS 215.213(1) and ORS 215.283(1) were permitted as of right and could not be subject to additional local criteria. *See Durig II*, 177 Or. App. at 233.

In a footnote to its opinion, the Court of Appeals noted that ORS 197.685 might apply in both a legislative context as well as in the analysis of individual applications. Specifically, the court stated that whereas here the statute applied to Washington County in a legislative sense because the County had already established a Community Development Code (CDC) to address the siting of seasonal farm worker housing, it may apply directly to individual applications in counties that had not adopted such a code. *Id.* at 233 n.6.

The court's decision is interesting because of the weight it gave to the sanctity of ORS 215.213(1) and ORS 215.283(1) uses, as well as for its strengthening and extension of *Brentmar*, 321 Or. at 496. While *Brentmar* made it clear that ORS 215.213(1) uses could not be limited by local governments, the courts decision in *Durig II* seems to imply that even the legislature cannot limit an ORS 215.213(1) or ORS 215.283(1) use. *See Durig II*, 177 Or. App. at 232–34. The parties in *Durig II*, while disagreeing on the import of ORS 197.685, appeared to agree that ORS 197.685 was an example of the legislature qualifying an ORS 215.213(1) or ORS 215.283(1) use. Yet, the court went out of its way to read ORS 197.685(2)'s language that "needed housing shall be permitted in a zone or zones" to mean in a zone or zones other than an EFU zone. *Id.* Moreover, the court found the statutory language unambiguous on this point.

Neither of the parties in *Durig II* argued that ORS 197.685 was inapplicable to EFU lands; they simply disagreed over the way in which it should apply. *See Id.* at 232–34. The conclusion to be drawn from the court's analysis of ORS 197.685 is that, as was decided in *Brentmar,* ORS 215.213(1) and ORS 215.283(1) uses cannot be limited by local governments. The question is whether there are any limitations on *Brentmar's* rule. If nothing else, local government now bears a great burden to justify any limit an ORS 215.213(1) or ORS 215.283(1) use.

The court went on to reject petitioner's challenge to Townsend Farms' showing of need for requested seasonal farm workers. *See Id.* at 235–38. Specifically, the court found that CDC section 430-37.2(D) merely requires a showing of need for a particular number of workers, but it does not require a showing of a need for the workers to be housed on the site at issue. *Id.* at 237–38.

The court also rejected petitioners' argument that LUBA

incorrectly affirmed the Hearing Officer's imposition of conditions on Townsend Farms' use of an existing well to ensure water availability rather than a showing that there was sufficient available water. *See Id.* at 238–40.

Finally, the court rejected petitioners' argument that because the seasonal farm workers were to be housed in a de facto mobile home park it constituted an impermissible urban use on EFU land, and Washington County's mobile home and manufactured dwelling park standards should be applied prior to approval. The court found that the applicable statutes were intended to ensure that sufficient housing existed for seasonal form workers, but did not address what type of housing needed to be provided. *Id.* at 240–43. Moreover, the court found that the mobile home and manufactured dwelling park standards were meant to be applied to year-round residential housing, whereas the seasonal farm worker housing at issue was not year-round or typically residential. Finally, the court ruled that Townsend Farms had established that it nevertheless could meet certain yard setback and safety requirements imposed by these regulations. *Id.* at 242–43.

William Joseph

Durig v. Washington County, 177 Or. App. 227 (2001).

Dotting the i's and Crossing the t's on the UGB, or "How I Learned to Love Form for the Sake of Substance"

1000 Friends of Oregon v. Metro (Ryland Homes), 174 Or. App. 406, 26 P.3d 151 (2002), follows in the footsteps of *D.S. Parklane Development, Inc. v. Metro*, 165 Or. App. 1, 994 P.2d 1205 (2000) and *Residents of Rosemont v. Metro*, 173 Or. App. 321, 21 P.3d 1108 (2001) (see 23:5 RELU Digest 1 (October, 2001)). In *Parklane*, the court affirmed LUBA's remand of Metro's 1997 decision to designate

18,579 acres of land as urban reserves pursuant to OAR 660-21, agreeing with LUBA, inter alia, that Metro had not followed the statutory priorities in designating urban reserves. In *Rosemont*, the court affirmed LUBA's remand of Metro's 1998 decision to amend the Urban Growth Boundary (UGB) to include 830 acres of land. The court agreed with LUBA that a decision to amend the UGB could be based, in part, on a showing of need for more urban land in a subregion, but differed with LUBA about whether Metro had done an adequate job of articulating the need in that case and about whether Metro was required to address the potential for meeting that need in the region as a whole.

In *1000 Friends of Oregon v. Metro (Ryland Homes)*, the court again considers a remand by LUBA of a decision by Metro to amend the UGB; this time a 1999 decision adding to the UGB 109 acres of EFU land. Once again LUBA accepted the concept of amending the UGB to meet a subregional need for urban land. And, this time, it found Metro showed the subregional need could not be met elsewhere in the region generally. However LUBA concluded that Metro's findings under Goal 14, factors 5, 6 and 7, were inadequate, because Metro did not *directly* address certain aspects of those factors, did not undertake a sufficient analysis of alternative sites where the need could be met, and did not explain how it balanced the Goal 14 factors.

On appeal, Ryland Homes argued Metro's findings went far enough. Ryland argued LUBA and the Court of Appeals should have found the decision was adequate when viewed "as a whole" and "given the totality of the findings" even if it failed to do so point by point, inviting the court to do a little Monday morning quarterbacking. LUBA and the court declined the opportunity "to divine Metro's unexpressed reasoning." In so doing, the court described, what should be a familiar rubric, that the findings must show the local government considered the Goal 14 factors and balanced them. It said Metro's failure to do so "regarding each of the locational factors and its reasons explaining how it balanced the factors makes it impossible to conduct a meaningful review of Metro's decision." *See Sunnyside Neighborhood v. Clackamas Co. Comm.*, 280 Or. 3, 569 P.2d 1063 (1977); ORS 197.732(4); OAR 660-004-0010(1)(b)(B), -0020(1).

Regarding factor 6, which requires changes in UGB boundaries to be based on consideration of retention of agricultural land, Ryland argued the findings made pursuant to ORS 197.298 should have sufficed for factor 6, because they address the same issue, i.e., retention of agricultural land. However, LUBA and the court said factor 6 and ORS 197.298 are not identical, and this is not a game of horseshoes. ORS 197.298 requires Metro to evaluate potential expansion sites and to assign them priority for inclusion in the UGB, with higher priority being given to land of lower soil capability, subject to certain exceptions. Factor 6 does not contain such exceptions and does not contain the same priority scheme as ORS 197.298. The differences mean that the findings Metro made with regard to one of the standards do not suffice for the other standard.

Regarding other lands where the need for more urban land could be met, Ryland argued Metro made findings from which the court could infer that other agricultural lands in the area are unsuitable. For instance, Metro found that no other non-urban land could be serviced until the site in question is developed. Given this, a remand to address this issue would be superfluous. The court disagreed, because specific findings are required when "a relevant legal requirement calls for findings addressing a particular criterion ... ."

Under factor 5, Metro must consider the ESEE (environmental, social, energy and economic) consequences of expanding the UGB to include the proposed site as compared to other sites. LUBA and the court found Metro's ESEE analysis was inadequate, because it focused on the site in question.

For substantially the same reason, LUBA and the court rejected Metro's response to factor 7, which requires consideration of the "compatibility of the proposed urban uses with nearby agricultural activities." Although Metro found that including the subject site in the UGB would not be incompatible with agricultural activities in the area, it had to consider the consequences of including other properties. "Metro has an obligation to consider each of the locational factors and to articulate its thinking regarding the factor and the role each factor played in its balancing of all of the factors ... even though, at times, those steps may seem to be formalistic."

The Court of Appeals also addressed a cross-petition disputing what document Metro can use to establish whether there is a need for more urban land. Cross-petitioners argued Metro had to use the Urban Growth Management Functional Plan (UGMF Plan). Instead Metro used a 1997 Urban Growth Report (UGR). Using the UGR results in a need for 4000 acres more urban land than does the UGMF Plan.

This last issue had been before the court in the *Parklane* and *Rosemont* cases. In those cases the court held that Metro had to use the UGMF Plan to compute need for more urban land, because the UGR was "not a plan or a planning document of the kind that Goal 2 contemplates" as the basis for a planning decision. Following the *Parklane* and *Rosemont* decisions, Metro amended its Regional Framework Plan (RFP) to include the numbers from the UGR. LUBA and the court held that, with this amendment, the UGR capacity numbers in the RFP provide a suitable basis for planning decisions.

However, the "target capacities" in the UGMF Plan are different from the UGB 20-year capacity in the amended RFP. Metro and Ryland argued the two plans are not inconsistent, because they serve different functions. But neither LUBA nor the court bought that argument. The UGMF Plan clearly says its target capacities are mandatory. In contrast, the RFP says nothing about the role of the different capacity numbers it contains. The result is not coordinated, and it violates Goal 2, Part I, at least without a more detailed explanation of how the two inconsistent plans can be squared.

Larry Epstein

1000 Friends of Oregon v. Metro (Ryland Homes), 174 Or. App. 406, 26 P.3d 151 (2002).

As Washington County hearings officer, Larry Epstein approved a rezone to an urban residential zone for the 109-acre site, subject to approval of the ill-fated UGB amendment discussed above.

Court of Appeals Affirms LUBA's Interpretation of When an Amendment "Significantly Affects" a Transportation Facility

Department of Transportation v. City of Klamath Falls, 177 Or. App. 1 (2001), involved a challenge to LUBA's interpretation of OAR 660-12-0060, which requires that amendments to functional plans, acknowledged comprehensive plans, and land use regulations that significantly affect a transportation facility are consistent with the function, capacity, and performance standards for the facility. OAR 660-12-0060(1). The Court of Appeals affirmed LUBA's interpretation that an amendment significantly affects a transportation facility, although the facility would have failed even without the amendment.

In 1979, the City of Klamath Falls approved Southview Property Development, LLC's PUD consisting of 560 acres in the southwest quadrant of the city. At the same time, the City also zoned 40 nearby acres for single-family residential use, but this property was not part of the PUD. Both properties were brought within the Urban Growth boundary (UGB). The 560-acre property is partially bordered by Highway 140, where access was proposed at the intersection of Orindale Highway. Klamath Falls adopted its Comprehensive Plan in 1981, rewrote its Community Development Ordinance in 1995, and adopted its Transportation System Plan (TSP) in 1998, but still maintained its approval of the PUD. The City's TSP assumed no population growth in the southwest quadrant of the city. *Dep't of Transp.*, 177 Or. App. at 3.

In 1999, Southview applied for a plan amendment to add the nearby 40 acres to the PUD. Doing so would substantially alter the traffic patterns and uses within the PUD, including eliminating certain road connections, and would result in 1,690 more daily trips than the 1979 version. *Id.* at 4, 6. Because a state highway was involved, the applicable TSP was determined to be the Oregon Highway Plan (OHP). The OHP seeks to avoid further degradation of the performance of highways that are currently operating in excess of their capacity where improvements are infeasible. It also states that an amendment to a TSP, acknowledged comprehensive plan, or land use regulation "significantly affects" a transportation facility, as that term is used in OAR 660-012-0060(1), if it increases volume but not capacity. *Id.* at 5 (quoting OHP at 79 (1999)).

The City approved the amendment in part relying on improvements to the intersections at issue that were not listed in the application. The Department of Transportation appealed to LUBA. LUBA noted the significant increase in volume that would result from approval of the application and the City's reliance on what it termed "entirely speculative" improvements to the affected transportation facilities. As such, LUBA remanded for a determination of whether the specifically listed improvements would increase capacity such that approval of the amendment would not "significantly affect" the transportation facilities at issue. LUBA further noted that if the proposed amendment would cause the affected transportation facilities to exceed their capacities sooner than they otherwise would, this would fall within the "significantly affects" language of OAR 660-012-0060(1). *Id.* at 6.

Southview appealed to the Court of Appeals arguing that LUBA erroneously interpreted OAR 660-012-0060(2)(d) in deciding that an amendment to a land use regulation "significantly affects" a transportation facility where the facility would fail anyway within the relevant planning period. Southview's argument was two-pronged: First, Southview argued that the determination of whether an amendment "significantly affects" the intersections at issue must be made at the end of the 20-year planning period, and because the intersections could exceed their capacity anytime within that 20 years even without the proposed amendment, it is impossible to determine whether the amendment itself would cause them to fail sooner than they otherwise would. Second, Southview argued that the amendment must be the sole cause of the failures for it to "significantly affect" the intersections. *Id.* at 7–8.

Relying on the language in context of OAR 660-012-0060, the Court of Appeals rejected both of Southview's arguments. First, the court found no support for the proposition that the effects of an amendment can only be measured at the end of the planning period. To do so, would nullify the other provisions of OAR 660-012-0060 that provide alternative means for ensuring that an amendment is consistent with the performance standards of the affected transportation facility. Second, the court found no support for Southview's argument that the amendment must be the sole cause of the failure for it to "significantly affect" the facility. Specifically, the court rejected Southview's reliance on *Dept of Transp. v. Coos County*, 158 Or. App. 569, 976 P.2d 68 (1999), which was decided under a previous version of the OHP. *Id.* at 8.

While noting that the intersections in question would likely exceed their capacities within the 20-year period even without the amendment, the court affirmed that, if the amendment will cause the intersections to exceed their capacities sooner than they otherwise would, it will "significantly affect" the intersections, thereby triggering the provisions of OAR 660-012-0060. *Id.* at 9.

The court also rejected Southview's argument that where a transportation facility will fail within the planning period, the TSP must have been based on faulty predictions, thereby triggering periodic review of the TSP due to a change in circumstances rather than implementation of the provisions of OAR 660-012-0060(1). *Id.* at 9 (citing ORS 197.628(3)(a)). The court ruled that the amendment does not constitute a "change in circumstances" and that periodic review is triggered by the Department of Land Conservation and Development (DLCD). *Id.* at 9-10.

The court also rejected Southview's argument that imposition of the provisions of OAR 660-012-0060(1) where the affected transportation facility would fail even without the amendment results in a *de facto* moratorium on development. The court stated that although Southview may not prefer the alternatives listed in OAR 660-012-0060(1), they must be applied and doing so does not result in a moratorium. The court ruled that LUBA's reversal was based on the fact that the proposed amendment did not meet the OHP; that does not constitute a moratorium. *Id.* at 10–11 (citing ORS 197.524(2)). Finally, the court rejected Southview's remaining arguments as premature. *Id.* at 11–12.

William Joseph

Dep't of Transp. v. City of Klamath Falls, 177 Or. App. 1 (2001).

Decision Under a County Code About Expiration of an Approval Is a "Land Use Decision"

State ex rel Coastal Management v. Washington County, 178 Or. App. 280 (2001), presents the recurring question whether the circuit court or LUBA has jurisdiction to review a local decision. As is usually the case, the Court of Appeals held LUBA had jurisdiction, and reversed the circuit court's issuance of a peremptory writ of mandamus.

In 1996, Coastal filed a 120-day mandamus action against the county, asking that the circuit court order the county to approve its subdivision application. The trial court issued the requested peremptory writ of mandamus, and on January 28, 1997, the county approved Coastal's preliminary subdivision plat. At the same time, the county appealed the issuance of the writ, which was ultimately affirmed by the Court of Appeals in April 1999.

The Washington County Community Development Code provides that plat approvals expire after two years unless development is commenced or a time extension granted. During 1997 and 1998, Coastal did not commence development or receive final plat approval, allegedly relying on what they understood to be the county's practice of tolling the two-year time limit during an appeal. The county code, however, contains provisions that imply, if not clearly state, there is no such tolling.

In December 1998, while the original mandamus case was still on appeal, the Board of County Commissioners issued an interpretation that the preliminary plat time limit was not tolled by an appeal. Shortly thereafter, an assistant county counsel advised Coastal's attorney that their approval would soon expire. On January 7, 1999, Coastal's counsel requested that the county either confirm that the clock stopped running during the appeal or extend the preliminary approval until the appeal was concluded. In an exchange of correspondence during January 1999, the county maintained its position that the approval expired on January 28, and suggested the possibility of Coastal seeking an extension of the time limit, as provided for in the code. Coastal did not request an extension under this code provision, but instead filed this new mandamus action, seeking a writ compelling the county to extend the plat approval for two years after the conclusion of the county's appeal of the prior mandamus. The circuit court so ordered, and the county filed this appeal.

The Court of Appeals commenced its analysis with a general statement that a decision under a county code about the expiration of an approval is a "land use decision," subject to LUBA's jurisdiction. Coastal argued, however, that in this circumstance the county's action (or inaction) actually "amounted to a procedurally flawed attempt to subvert the prior mandamus judgment." It was therefore not a land use decision reviewable by LUBA, but rather subject to the circuit court's inherent authority to enforce its judgments during an appeal.

The court rejected all of Coastal's arguments in support of this position. Amendments to the 120-day mandamus statute enacted after the circuit court's decision in this case were not relevant. Neither were the facts that Coastal may have only been alerted to the pending expiration a short time before it occurred and that there was no formal written denial of their time extension request; such procedural flaws were within LUBA's jurisdiction. *Murphy Citizens Advisory Comm. v. Josephine County*, 325 Or. 101 (1997), did not apply where the county had taken the action ordered by the writ of mandamus, and the issue was simply the expiration date of that approval. Similarly, ORS 19.270(1)(b), authorizing a circuit court to enforce its judgments during appeal, did not apply because the county had in fact followed the judgment by issuing the preliminary plat approval. The county's action was a land use decision, subject exclusively to LUBA's jurisdiction, and the mandamus was reversed.

Mike Judd

State ex rel Coastal Management v. Washington County, 178 Or. App. 280 (2001).

When Must Local Governments Consider the Legality of Existing Lots of Record

In *Maxwell v. Lane County*, 178 Or. App. 210 (2001), the Court of Appeals revisited the circumstances under which a local government must evaluate the legality of a unit of land (a tract or parcel, but hereinafter referred to as a lot) in connection with a subsequent land use decision. The Court expanded the existing rule that a local government need only find that an existing lot was legally established if the applicable land use criteria expressly requires such a finding. *See McKay Creek Valley Ass'n v. Washington County*, 188 Or. App. 543, rev. den'd 317 Or. 272 (1993) (holding that Washington County was not required to determine the legality of a lot when it approved a land use decision authorizing construction of a dwelling on the EFU zoned lot because the County ordinance did not expressly require such a determination).

In *Maxwell*, the Court revisited the legal lot of record rule. In expanding the existing rule, the Court held:

> "A local government entity must determine the legal status of a unit of land in connection with a current proceeding involving that unit of land if required to do so by applicable legislation. ***Applicable legislation includes*** not only the local enactment governing the particular proceeding at issue, but also ***related enactments.*** In addition, ***the requirement that the local government determine the legal status of a unit of land*** in connection with a particular proceeding need not be expressly stated in the relevant enactment, but ***may be derived from its text in context or by consideration of its purpose or policy***."
>
> *Id.* at 230 (emphasis added).

The facts in *Maxwell* are complicated and convoluted. They can be summarized as follows. Three lots, each about ten acres, were converted to four lots, two of which were about five acres in size. Originally, two of the three lots had houses on them. After the new lot was created, an additional house was added to the new lot. The three lots were converted to four lots via lot line adjustments and an informal county policy that treated a single lot that is divided by an unimproved but rededicated right of way as two lots.

All of the lots were zoned Rural Residential 10 (ten acre minimum lot size). After the fourth lot was created and the house was added, Maxwell applied to rezone the property to Rural Residential 5 (five acre minimum lot size). Approving the rezone was dependent on a calculation of the average lot size and density of the property that was subject to the rezone. If the county was able to consider the lot size of the four parcels that existed when the rezone application was filed, the average lot size and density calculation supported the county's decision to rezone the property. If the four parcels were not legally established and thereby only consisted of three parcels in their original configuration, the average lot size and density calculation did not support the county' decision to rezone the property and it should have been denied.

Lane County and LUBA held it was unnecessary to evaluate whether the lots were legally established, relying on the rule in *McKay*. The applicable county regulations and comprehensive plan policies did not expressly require a determination that the parcels were legally established. The Court of Appeals disagreed. The court reasoned that the context of the applicable approval criteria required consideration of lots that were legally established, and therefore, the county had to determine that the lots were legally established. Since the county did not make that determination, the case was remanded.

Marnie Allen

Maxwell v. Lane County, 178 Or. App. 210 (2001).

20-Day Notice Required for LUBA Remand Hearings

Hausam v. City of Salem, 178 Or. App. 417 (2001), addresses the issue of whether the procedural requirements of ORS 197.763 apply to local hearings held on remand from LUBA. In reversing LUBA, the Court of Appeals held that at least the 20-day hearing notice requirement applies in that situation.

In an earlier appeal by Hausam, LUBA remanded a subdivision approval that he opposed, finding that decision not supported by substantial evidence. After the applicants amended their subdivision proposal, a new hearing was scheduled before the planning commission for February 6, 2001. Notice of that hearing was mailed to Hausam on January 25, 2001. LUBA estimated he received the notice on January 27. Hausam did not attend the February 6 hearing, at which the subdivision was again approved. On February 20, 2001, he asked the planning commission to reconsider the application, arguing that he was out of town on February 6 and, because of the inadequate notice, did not have time to make other arrangements to present testimony. The planning commission denied the request, and that denial was appealed.

At LUBA, Hausam argued that the city violated the requirement of ORS 197.763(3)(f) that notice be mailed "twenty days before the evidentiary hearing," and that he was substantially prejudiced by this procedural error. LUBA did not rule on whether the notice requirement applied, instead deciding that, even if it did, the fact Hausam received only 10 days' notice of the hearing did not prejudice his substantial rights; he had "adequate time to make arrangements to appear in person, in writing or through a representative," notwithstanding the fact he was out of town for at least some of the relevant period.

The Court of Appeals reversed LUBA and held the 20-day notice requirement applied to this hearing. The court rejected the theory of the applicant and the city that the remand hearing should be viewed as the second evidentiary hearing in a continuing case, so the notice provision had already been satisfied. The court distinguished this case from the situation where at the end of a local hearing a continuance to a date certain is announced, which is permissible. It also noted it was expressing no opinion on notice requirements where LUBA remands on issues of law, rather than for a further evidentiary hearing. The court then held that, under the particular circumstances of this case, giving notice only 10 days before the hearing, rather than 20 days, resulted in Hausam having an "inadequate opportunity to participate" and, therefore, was prejudicial.

The court's holding that the 20-day notice provision of ORS 197.763(3) applies to a remand proceeding is new law. It appears contrary to a number of LUBA decisions holding that the procedural requirements of ORS 197.763 do not apply to hearings on remand from LUBA (*e.g., Noble v. City of Fairview, 30 Or LUBA 180 (1995)*). While this decision only deals with the 20-day notice requirement, the court's approach to this issue would seem to apply to many, if not all, of the ORS 197.763 requirements.

Mike Judd

Hausam v. City of Salem, 178 Or. App. 417 (2001).

Goal 5 Rule Applies to PAPA Affecting Goal 5 Resource.

In *Rest-Haven Memorial Park v. Eugene*, 175 Or. App. 419 (2001), the Court of Appeals affirmed LUBA's determination that Eugene was required to apply Goal 5 before adopting a waterway ordinance. The City of Eugene adopted an ordinance that prohibits placing fill or pipes in waterways and drainageways in the city "to establish interim protection for…waterways that provide multiple stormwater benefits to the entire community…until the city completes its Goal 5 process… ." The city did not apply Goal 5 when adopting the ordinance.

Owners of property containing drainageways appealed, alleging a violation of OAR 660-023-0259(3), which requires local governments to apply Goal 5 if a post-acknowledgement plan amendment (PAPA) affects a Goal 5 resource, e.g., by protecting such a resource.

The city argued it was not required to apply Goal 5 because the ordinance was not intended to protect Goal 5 resources. It served other purposes. LUBA disagreed, holding that the ordinance regulated all waterways more stringently than before its adoption, and some of those waterways are listed by the city as significant Goal 5 resources.

On appeal, the city argued Goal 5 applies only if an ordinance is adopted specifically to protect a significant Goal 5 resource or to address a specific requirement of Goal 5. The city insisted its ordinance was not intended to protect Goal 5 resources, but was

adopted to protect the stormwater conveyance function that the waterways served. Protection of Goal 5 resources was an incidental effect of the ordinance, not its purpose.

The Court of Appeals agreed with LUBA for two reasons: the ordinance protects Goal 5 resources, and one of the stated purposes of the ordinance was to protect open waterways, some of which the city has identified as Goal 5 resources. Therefore the city was required to apply Goal 5 before adopting the ordinance.

Larry Epstein

Rest-Haven Memorial Park v. Eugene, 175 Or. App. 419 (2001).

Appellate Cases—Real Estate

An Easement By Any Other Name

R&C Ranch, LLC v. Kunde, 177 Or. App. 304 (2001), is a study in litigation strategy, more than novel case law. Plaintiff-respondent lost the appeal, won on cross-appeal, and ended up owing attorneys fees to defendant-appellant. The case involved adjacent ranches in Gilliam and Wheeler counties near the John Day River. The trial court had rejected plaintiff's claim of a prescriptive easement, but found plaintiff was entitled to a statutory way of necessity. Defendant appealed and plaintiff cross-appealed, citing an error in failing to find it had a prescriptive easement, among other grounds.

The ranches had a variety of owners over the 70 years prior to the suit, but were never under common ownership. The dispute arose from the unusual configuration of plaintiff's ranch—one parcel, 200 acres of low ground, is separated from the rest, more than 5,000 acres of high ground, by 2,000-foot cliffs, which are passable only by goats. Plaintiff's predecessors used a little-developed trail located primarily on defendant's ranch to access the high ground. Defendant barred plaintiff from using the trail and plaintiff sued.

At trial, plaintiff introduced testimony from several witnesses stating that plaintiff's predecessors had considered use of the trail to be their right and that they had consistently used the route, although the intensity of the use varied over the years. One witness testified that his father had foiled an attempt by defendant's predecessor to farm across the trail. The appeals court found plaintiff's testimony sufficient to invoke a presumption of adversity. The Court of Appeals reversed the trial court's ruling on the prescriptive easement. In doing so, the court rejected defendant's argument that it should benefit from a presumption that the use of the trail was permissive; the court concluded that the trail was not sufficiently developed and that plaintiff's use was adverse, so the presumption was inappropriate. Having concluded that plaintiff was entitled to a prescriptive easement, the appeals court reversed the trial court's judgment for a statutory way of necessity. Accordingly, defendant was entitled to recover attorney fees for defense costs related to that claim.

Tod Northman

R&C Ranch, LLC v. Kunde, 177 Or. App. 304 (2001).

Cases From Other Jurisdictions

Connecticut Federal Court Enjoins Local Regulation of Religious Activity

In *Murphy v. Zoning Commission of the Town of New Milford*, 148 F. Supp. 2d 173 (D. Conn. 2001), plaintiffs held religious meetings in their single family home and claimed enforcement efforts by defendant violated their constitutional rights to free exercise, free association, peaceable assembly, privacy, speech, due process, and equal protection. Plaintiffs also alleged the defendant's enforcement activities constituted a taking and violated both the establishment clause and the Religious Land Use and Institutionalized Persons Act (RLUIPA). The court issued a temporary restraining order and, in this case, considered a preliminary injunction.

Plaintiffs' home is a single-family residence where plaintiffs live with their six children. They hold weekly Sunday afternoon prayer meetings from 4:30 p.m. to 6:00 p.m. People park where they can in the neighborhood and, while there has never been less than ten to twelve visitors; attendance at the meetings often ranges up to forty people. Plaintiffs have not limited the total attendance although the meetings are not open to the public. When the town began to receive complaints, it examined whether there were violations of zoning or other ordinances. Most of the complaints dealt with parking congestion. Defendant commission was asked whether the meetings violated the zoning ordinance. The commission responded that they did because they were not customary accessory uses and plaintiffs could not use their property for a parking lot to accommodate those meetings. The zoning enforcement officer then issued a cease and desist order, which plaintiffs did not appeal. Instead, they brought this suit.

To receive a preliminary injunction, a plaintiff must demonstrate irreparable harm and either a likelihood of success on the merits or "sufficiently serious questions going to the merits." However, case law requires that, if a governmental action in the public interest pursuant to a regulatory scheme is at issue, plaintiff must meet the more rigorous likelihood of success standard. The court found the irreparable harm standard met, as there were first amendment rights involved, particularly with the RLUIPA claim. The court noted that plaintiffs also demonstrated the enforcement action has had a chilling effect and some participants have stopped attending over fears of being arrested.

The court then turned to the jurisdictional questions raised by defendant and held that plaintiffs were not required to exhaust their remedies before seeking judicial relief. However, the court noted that case law still requires a showing of inadequate legal remedies before equitable jurisdiction may be invoked. The court next considered the ripeness issue. Defendant contended that the case was not ripe because there was no final action (plaintiff could still appeal) and no enforcement action had been formally taken. The court said the case was ripe, as there was a final decision on the alleged violation that was formalized and has practical effects the

plaintiffs would feel in a concrete way, at least with respect to the RLUIPA claim. The court determined that plaintiffs were not required to appeal the cease and desist order or seek a permit to bring their RLUIPA claim. Following an extensive discussion of case law and the facts of this particular case, the court found the RLUIPA issue ripe for adjudication, but invited defendant to test the ripeness of other issues by a motion to dismiss.

As to the likelihood of success on the merits of the RLUIPA claim, once plaintiffs make out a prima facie case that a local regulation imposes a substantial burden on their constitutionally protected rights, the burden shifts to defendant to show the regulation furthers a compelling state interest and the local government has used the least restrictive means to advance that interest. The court found the substantial burden standard was met by the testimony of those who had not attended more recent meetings out of fears of arrest. These actions showed the enforcement activities imposed pressure on participants to modify their behavior and violate their beliefs, which was sufficient to establish a prima facie case. The court agreed traffic safety was a compelling state interest, but concluded the commission failed to consider alternative forms of regulation that would accommodate the religious uses. In this case, defendant did not address traffic congestion, but rather the number of people who attended the meetings. In fact, barring use of plaintiffs' driveway for parking appeared inconsistent with the traffic congestion concerns expressed by defendant. The court noted the inconsistency between plaintiffs' stated concerns and its actions.

> "In passing RLUIPA, Congress required local governments to be sensitive to the values of religious freedom and expression. It directed that substantial burdens be placed on the exercise of religion only to the extent necessary to accomplish compelling governmental interests. Even absent a federal statute, one would expect that, before banning an ongoing private religious gathering, public officials in a free and tolerant society would enter into a dialogue with the participants to determine if the legitimate safety concerns of the neighbors could be voluntarily allayed. Particularly where the participants are enjoined by religious teachings to "do unto others" as they would have done unto them, it is not unreasonable to expect the parties to be able to agree on means of reducing the impact of weekly prayer meetings on this small cul-de-sac without undermining the benefit that participants seek to derive from the practice of their faith." *Murphy*, 148 F. Supp. at 191 (footnote omitted).
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> The court thus issued the preliminary injunction.

This is one of the first RLUIPA cases to deal with land use regulation. The town noted it would contest the constitutionality of the legislation at a later stage of the proceeding; however, if the Act is constitutional, the decision in this case appears to have carried out the legislative intent of Congress.

Edward J. Sullivan

Murphy v. Zoning Commission of the Town of New Milford, 148 F. Supp. 2d 173 (D. Conn. 2001).

Federal Circuit Court of Appeals Denies Rehearing in Surface Mining Takings Case

In *Rith Energy, Inc. v. United States*, 270 F.3d 1347 (Fed. Cir. 2001), plaintiff asked the federal circuit to reconsider its affirmance of the Court of Federal Claims' denial on of plaintiff's takings claim. Plaintiff's surface mining permit at leased sites was suspended and plaintiff sought to revise it. When that revision was denied, plaintiff brought a takings claim in the Court of Federal Claims and lost. In the previous case of the same name at 247 F.3d 1355, that denial was affirmed. Plaintiff sought reconsideration in light of the United States Supreme Court's decision in *Palazzolo v. Rhode Island*, 121 S.Ct. 2448 (2001). Plaintiff argued that Palazzolo was contrary to the court's analysis in the original opinion and required the judgment to be changed. The Federal Circuit disagreed.

Plaintiff suggested the court was incorrect in holding that the "taking" at issue was not categorical. The court had based that decision on its finding that the plaintiff had not lost all value in its coal leases because it was able to mine 35,700 tons of coal, or about nine percent of what it hoped to mine if the permit had not been suspended and ultimately revoked. The court found *Palazzolo* "distinctly unhelpful" to plaintiff because, if there was some economic value in the regulated property, there was no categorical taking. *Palazzolo* involved about $200,000 of development value, which would be available even with the state's wetlands regulations in that case, or about six percent of the original value. The court characterized the situation as a "mere diminution" in property value.

Plaintiff also contended that the taking must be measured by the economic value remaining in the coal leases at the time the permit was revoked and, because the revocation prevented any further coal from being taken, this action constituted a categorical taking of 100 percent of the coal that was left in the ground. The court specifically rejected this argument, saying that it is "artificial" to divide the interests in the coal lease, i.e., comparing that which was mined before and after the suspension, which effectively disregarded the coal that had already been mined before the revocation. The court concluded that the effect of the regulatory action was to permit plaintiff to take some coal from the property and then to prohibit it from taking any more. Such a course of regulatory action, viewed as a whole, did not deprive plaintiff of all economic value in the coal leases and, therefore, did not constitute a categorical taking.

More interesting was the plaintiff's suggestion that no weight should be given to the regulatory scheme established by the Surface Mining Control and Reclamation Act of 1977 (SMCRA) as an element of investment-backed expectations. The court noted that *Palazzolo* had rejected the argument that, when government action regulates the use of property, a person who purchased property after the date of the regulation may never challenge the regulation under the takings clause. However, the court also said that the Supreme Court did not find that the reasonable expectations of persons in a highly regulated industry are irrelevant to determining whether the regulatory action constitutes a taking, noting in particular Justice O'Connor's position on this point, which was apparently joined by a majority of the Supreme Court. The court pointed out that in *Eastern Enterprises v. Apfel*, 524 U.S. 498 (1998), the four-justice plurality reaffirmed the role of investment-backed expectations in

regulatory takings analysis, indicating that they were entitled to "particular significance" in that analysis. Similarly, the court found no comfort for plaintiff in *Nollan v. California Coastal Commission*, 483 U.S. 825 (1987).

The court concluded:

> "In this case, which involves a business engaged in a highly regulated industry, the plaintiff's reasonable investment-backed expectations are an especially important consideration in the takings calculus. A party in [plaintiff's] position necessarily understands that it can expect the regulatory regime to impose some restraints on its right to mine coal under a coal lease. The leases themselves notified [plaintiff] of the uncertainty of obtaining permits to mine, and the low price that [plaintiff] paid for the leases may well reflect the widely understood risk that [plaintiff] would not be permitted to extract as much coal as it hoped for from the leased properties. The likelihood of regulatory restraint is especially high with regard to possible adverse environmental effects, such as potentially harmful runoff from the mining operations, which have long been regarded as proper subjects for the exercise of the state's police power."

The court concluded that reasonable investment-backed expectations play an important role in regulatory takings analysis and did not find that conclusion undermined by either Nollan or *Palazzolo*, even though the federal Supreme Court in *Palazzolo* concluded that, by itself, notice of the regulatory scheme did not prevent a takings claim from being advanced.

Turning to the character of government action, the court said the revocation of the permit was an exercise of the "police power" directed at safety, health, and welfare of the communities surrounding plaintiff's mine site so as to prevent the harmful runoff. Such harm-preventing legislation usually does not trigger a right to compensation for burdens it imposes on landowners who are affected by the regulations.

Finally, plaintiff suggested that the federal government's decisions in this case were driven by political pressure, that its activities were not significantly harmful, and that it was unfair to be singled out for disparate treatment. The court said these were claims that plaintiff either raised or could have raised in the administrative and judicial challenges to the denial of the permit at issue. Further the claims are contrary to the administrative law judge's determination that mining in this geographical area had a high propensity to produce acid mine drainage and that plaintiff's proposed abatement plan would not undertake the necessary reclamation of this site or prevent damage to hydrologic balance. The court thus denied reconsideration.

This case involves one of the first federal Court of Appeals' decisions interpreting *Palazzolo*. The court in this case viewed a takings claim as not necessarily defeated by notice of the existence of regulations at the time one purchased the property. Similarly, it did not eliminate consideration of investment-backed expectations from the takings analysis, but included it as a factor in the calculation of whether a taking had occurred.

Edward J. Sullivan

Rith Energy, Inc. v. United States, 270 F.3d 1347 (Fed. Cir. 2001).

California Supreme Court Says City Cannot Avoid Environmental Quality Act By Use of Council-Generated Initiative

In Friends of *Sierra Madre v. City of Sierra Madre*, 105 Cal. Rptr. 2d 214, 19 P.3d 567 (2001), defendant City, through its Council, placed an initiative measure on the ballot. The effect of the measure was to remove twenty-nine sites from a historic preservation list. Ordinarily, sites must be removed in accordance with the California Environmental Quality Act (CEQA), which requires the filing of an Environmental Impact Report (EIR) or a negative declaration (i.e., that there is no significant environmental impact). Those determinations may be challenged in court and may not be finally resolved for a long time. Plaintiff filed a mandamus action challenging the City Council's placement of the measure on the ballot as inconsistent with CEQA. The trial court and the California Court of Appeals found that including the measure on the ballot was invalid, although for different reasons. Defendant contended, *inter alia*, that noncompliance with CEQA was not a valid ground for contesting the measure and that plaintiff's Writ of Mandate could not overturn an election. In this case, the election resulted in passage of the measure and removal of the twenty-nine properties from the historic preservation list.

The trial court characterized the City Council's action as legislative, even though it affected twenty-nine discrete parcels. The City's original landmark legislation was adopted in 1987 and was strengthened in 1997. Even though the regulations were described as voluntary in nature (in that individuals either consented or requested that the properties be added to the landmarks preservation list), certain property owners disputed that their consent had been given and asked, following adoption of the 1997 amendments, for removal from the list. These owners complained that it would be complicated and expensive (i.e., $2,500 for each EIR) to undertake the removal individually and that such removal would be subject to CEQA. The City Council then decided to use the initiative process to undertake the removal. The Council heard testimony from the city attorney that a referendum would not work in such a situation because the referendum dealt with a City Council decision that was already made (and thus, subject to CEQA), whereas mere placement on the ballot through a council-generated process would not, in the opinion of the city attorney, be subject to CEQA. The city attorney noted that there was an exception to CEQA for initiative measures and thus an EIR or negative declaration would not be required and that placement of this measure on the next regular election ballot would not be expensive for the city.

Thus, in December 1997, the City placed a measure on the ballot that would delist the twenty-nine properties. When concern was raised as to whether the property owners would still be required to undergo the EIR process, the Council adopted a "clarifying ordinance," to take effect only if the initiative passed, that freed the twenty-nine properties from all general plan and city code requirements relating to historic preservation. The Council also sent a mailing to all property owners in the city indicating the same.

Plaintiffs challenged both the propriety of this election process,

as well as the alleged impropriety of circumventing CEQA through a council-generated initiative. The trial court granted relief only on the election law grounds, indicating that the amendatory ordinance was not before the voters, who may have been confused by the relationship of the two ordinances, and that the mailed notice was insufficient to notify they voters of the choices before them. The trial court denied the CEQA claim.

Conversely, the Court of Appeals found no election law violation, but did find CEQA violations. The Court of Appeals reasoned that the delisting was a "project" under CEQA for which an EIR was required and found that the only initiative measures that were exempt were those that were ministerial, i.e., those that had garnered sufficient voter signatures so that the City Council was required to place the measure on the ballot. Because this initiative was undertaken as a discretionary act of the Council, the Court of Appeals reasoned that it was subject to CEQA and the Council's failure to file an EIR invalidated the ordinance. The city then sought review of this case of first impression in the California Supreme Court.

Before the Supreme Court, the City contended that the council-generated initiative was not subject to CEQA because there was no post-election challenge available under California statutory law in these circumstances. The Court began its analysis by stating the broad scope of CEQA, which included preservation of historic resources among other things. The requirements and procedures of CEQA are triggered by any proposed public or private project that is not exempted by statute. CEQA assures that a public agency identifies significant environmental impacts and conditions approval on mitigation measures responding to those impacts. A "project" under statutory law is an activity that may cause either direct or indirect changes to the environment. The Supreme Court agreed with the Court of Appeals that an exception for placement of an initiative measure on the ballot was mandated by the state constitution when sufficient signatures are gathered. The Court noted that the legislative history of the exemption had its origins in the state constitutional requirements of the initiative process, so that when voters gather enough signatures, the measure must be placed on the ballot. The Court thus held that any project was subject to CEQA unless specifically exempted by law or mandated by other controlling law. Discretionary measures, such as the placement of this measure on the ballot, require an EIR or negative declaration under CEQA.

The Court also agreed that CEQA compliance was not a matter for an election contest; however, the validity of an ordinance adopted through this process may be challenged by a writ of mandate. The irregularities do not affect the will of the voters, which is the subject of separate declaratory, injunctive, or writ of mandate proceedings, as in this case. The Court ruled the writ of mandate would issue because the council failed to undertake a necessary step in a discretionary process that involved a "project" ordinarily subject to CEQA.

This case deals with the two 800 pound gorillas of California law—the popular control of government by the initiative referendum and recall process and a strong set of environmental regulations. In the event of a conflict, both must be given effect if possible. In this case, the initiative process may trump the environmental policies of the state only when required by the constitution to do so, such as in the event of sufficient voter generated signatures that require a local government to place the measure on the ballot. In the absence of such a requirement, the environmental regulations will prevail, and the council in this case could not circumvent those regulations by choosing to place a measure on the ballot without going through the EIR or negative declaration process.

Edward J. Sullivan

Friends of Sierra Madre v. City of Sierra Madre, 105 Cal. Rptr. 2d 214, 19 P.3d 567 (2001).

Third Circuit Decides Land Use Appeal from Bankruptcy Court

In *In re Four Three Oh, Inc.*, 256 F.3d 107 (3d Cir. 2001), Bochasanwasi Shree Akshar Purushottam Swaminarayan Sanstha (BAPS) applied to the North Bergen Board of Adjustment (Board) for a use variance to use a former nightclub as a temple for Hindu worship. BAPS intended to purchase the property from a trustee in bankruptcy for Four Three Oh, Inc., on condition that it receives a use variance. However, the variance process took two years to complete and resulted in a condition that the landowner hire off-duty police to direct traffic and assure that occupancy limits were met. The bankruptcy court held the condition unreasonable and enjoined it, whereupon the Board appealed to the district court, which affirmed. The Board then appealed the judgment of the district court to the Third Circuit, which also affirmed.

BAPS noted that the Board had repeatedly postponed the hearing, causing the bankruptcy court on plaintiff's motion to require the matter to be decided by a date certain. One of the major issues at the hearing was parking, which BAPS sought to deal with by limiting temple occupancy initially to 578 persons and 165 parking spaces. Later, BAPS reduced its proposal to a 505-person occupancy; however, the Board denied the application.

When BAPS appealed the denial to the bankruptcy court, that court remanded the case to the Board, finding that the Board had acted arbitrarily in failing to impose reasonable conditions. On remand, the Board imposed the off-duty police requirement. When BAPs discovered that there were no off-duty police available in the vicinity, it proposed using volunteers, which the Board rejected. BAPS appealed again. The bankruptcy court found the new condition arbitrary and unreasonable and voided it, allowing plaintiff's volunteers to monitor traffic and occupancy.

The Third Circuit reviewed the district court's affirmance of the bankruptcy court on a dual track—for factual matters, the standard was clear error, while on legal matters, it was a plenary review. The court said it would grant a state agency the same deference as that given to the agency by a state trial court. In this case, that deference would be substantial evidence on factual matters and "arbitrary, unreasonable or capricious" on legal issues. The court concluded that the bankruptcy court had used the correct standard of review,

but the district court erred in failing to exercise plenary review. Nevertheless, to avoid delay, the Third Circuit proceeded to decide the merits.

The court faulted the Board for failing to apply New Jersey variance law correctly, noting that the three negative grounds for denial (i.e., overuse of a parking facility in a similar temple elsewhere, the shortage of parking, and traffic problems) did not have support in the record and were, in fact, based on testimony that had been discredited. Moreover, the court held the Board had a duty to consider seriously conditions proposed to alleviate any negative impact flowing from the grant of the variance, and found that the Board had rejected the conditions proposed by BAPS for no apparent reason. Finally, the court determined that the Board unreasonably imposed the off-duty police condition, finding it to be arbitrary and unreasonable for the Board to state that plaintiff's volunteers were untrustworthy.

Judge Alito dissented, stating that the New Jersey variance standard was that a variance must be denied if it would result in a substantial detriment to public good. Such a decision is presumptively valid and reversible only if arbitrary, capricious, and unreasonable, as local boards of adjustment have knowledge of local conditions. The dissent said that the structure at issue could accommodate 1,500 to 1,600 people. After setting forth the testimony of the experts and others, the dissent said that a reasonable person would have accepted the Board's findings as sufficient under the substantial evidence test. Further, the dissent found the conditions proposed by BAPS to limit the intensity of the use were unreasonable and saw no bias against Hindus alleged or shown by BAPS. Finally, the dissent found the off-duty police condition was not properly before the court on appeal. In conclusion, the dissent said there was no abuse of discretion in this case merely because a majority of the court disagreed with the interpretations at issue.

This is a most unusual case—a bankruptcy court deciding the propriety and lawfulness of a land use decision. The difficulty is compounded by New Jersey's muddled jurisprudence of review of local government decisions and an administrative law tradition that has an outcome dependent upon the manner of framing the question.

Edward J. Sullivan

In re Four Three Oh, Inc., 256 F.3d 107 (3d Cir. 2001).

LUBA

New Decision on Remand May Be Adopted Without a Hearing

Arlington Heights Homeowners Association v. City of Portland and Oregon Holocaust Memorial Coalition (LUBA No. 2001-099) involves a new decision by a city on remand from the Oregon Land Use Board of Appeals (LUBA). The fundamental issue is whether the petitioner is entitled to a hearing on remand where an interpretation is part of the new decision. LUBA's position is that, while a local government may either hold an evidentiary hearing or hear argument, or both, it does not have to, except in limited situations. The limited situations are set forth in a Court of Appeals case, *Gutoski v. Lane County*, 155 Or. App. 369, 963 P.2d 145 (1998). Gutoski holds that a new hearing or argument may be required (1) where the interpretation significantly changes an existing interpretation or where it is significantly beyond the range of interpretations that could have been reasonably anticipated at the time of the evidentiary presentation, and (2) the party seeking reversal must demonstrate that it can produce substantially different evidence that is directly responsive to the unanticipated interpretation. In deciding Gutoski, the Court of Appeals had limited *Morrison v. City of Portland*, 70 Or. App. 437, 689 P.2d 1027 (1984) to its facts. In applying the Court of Appeals decision, LUBA overruled two of its earlier decisions, *Collins v. Klamath County*, 28 Or. LUBA 553 (1995), and *Friends of the Metolius v. Jefferson County*, 28 Or. LUBA 591 (1995).

Another problem raised by this case is the level of deference to be given to interpretations. First, in the fact pattern involved, at issue was an interpretation of a set of siting policy approval criteria for memorials in Washington Park, a significant and long established park in Portland. LUBA pointed out that, in its earlier decisions on this matter, it had determined that these approval criteria are not comprehensive plan or land use regulation provisions (then, are they "land use decisions?"). It then said that, because the outer limits of the *Clark v. Jackson Co.*, 313 Or. 508, 836 P.2d 710 (1992), and ORS 197.829(1) standards are sufficiently unclear, it would not apply the Clark deference standard in this case. Further, the City's interpretation of such requirements was not entitled to more deference than that set forth in *Clark*. Rather, it was required to "some deference."

I found the view from the benches much different than that from the trenches. Specifically, the dialogue about interpretations in *Gutoski* was quoted in the LUBA opinion. In the LUBA version of *Gutoski*, LUBA had said, "Where the interpretation of a local provision is a matter of first impression for the local government, the participants should have realized that a variety of interpretations might be adopted, and should have presented their evidence accordingly." *Gutoski v. Lane County*, 34 Or. LUBA 219 (1998). In the Court of Appeals decision on *Gutoski*, also quoted by LUBA, the homily goes even further:

> "Generally, as in the trial court and the agency setting, interrelated questions of fact and law are 'tried' and decided simultaneously in the local land use hearing process. From the standpoint of both litigants and decision makers, questions of fact and of law can have reciprocal effects on the answers to one another, and the ability to deal with the two as part of the same exercise is an essential tool of the advocate's craft. Hence, what petitioners appear to perceive as a chicken-and-egg problem that is somehow unique to this case is, in our view, simply a variation of a standard practice in which lawyers and judges have been engaging for centuries."
>
> *Gutoski v. Lane County*, 155 Or. App. 369, 963 P.2d 145 (1998).

Four practices seem to be ignored in the above comments. First, a common practice with most boards is to decide the basic matter (i.e., are we for or against the proposal) and then ask that findings, which may well contain interpretations, be prepared. Second, is the common practice of having the advocate for the other side write the findings; predicting interpretations in this environment sometimes requires an Ouija board rather than rational anticipation. Third, in a major land use proceeding, there may be hundreds of standards possibly applicable; it is naive and irrational to assume that possible interpretations can be anticipated for this many standards. Finally, to meet the Gutoski requirement, one has to be able to find the existing standard, but unlike appellate courts, very few local governments have interpretations that are written down anywhere. It is not wrong for those sitting on benches to ask those working in trenches to do their jobs, but is fundamentally unfair to move the goal posts at the end of the game. *See Commonwealth Properties, Inc. v. Washington Co.*, 35 Or. App. 387, 582 P.2d 1384 (1978).

The ground is shifting on interpretations generally. Notwithstanding Portland General Elec. Co. v. Bureau of Labor and Industries, 317 Or. 606, 859 P.2d 1143 (1993), the 2001 legislature has mandated the consideration of legislative history in interpreting statutes. ORS 174.020 (Enr. HB 3677). The proposed Judicial Review of Governmental Actions bill (HB 2246 in the 2001 session), though it excluded land use decisions, attempted to codify *Springfield Educ. Ass'n v. Springfield School Dist.* No. 19, 290 Or. 217, 621 P.2d 547 (1980), and applied an express standard to state agency and other local government interpretations. Specifically, Section 17(7) of the bill provided:

> "To determine whether a government unit erroneously interpreted an enactment, the court shall interpret the enactment. The court shall accept a government unit's interpretation of technical terms of which the government unit has special knowledge and terms in the government unit's own enactment, unless the court independently determines that the interpretation is inconsistent with the enactment. The court shall accept a government unit's interpretation of terms the government unit is empowered to interpret and apply, if the court independently determines that the government unit's interpretation is consistent with the enactment. If the court concludes that the challenged government action is based upon an erroneous interpretation of an enactment and a correct interpretation compels a particular action, the court shall set aside the challenged action or modify the challenged action in accordance with the correct interpretation. If the correct interpretation does not compel a particular action or leaves the government unit with discretion that the government unit has not exercised, the court shall remand the challenged government action for disposition in accordance with the correct interpretation."

While the above is not law, it reflects that deep concern found in many fora about proper interpretations. I sense that LUBA's foray in this case will turn out to be a footnote rather than a substantial part of the evolving law of proper interpretations.

Steven R. Schell

Arlington Heights Homeowners Ass'n v. City of Portland & Oregon Holocaust Memorial Coalition (LUBA No. 2001-099).

UPDATE

Gorge Litigation Over Regional Planning

Last October, the Digest reported that the Washington Court of Appeals decided a case requiring the bi-state Columbia River Gorge Commission to apply Washington's common law of land use in Washington in the Columbia River Gorge National Scenic Area. The result of the case is that the National Scenic Area standards would be not be applied uniformly, as envisioned by the federal law creating the National Scenic Area. The Gorge Commission appealed the case up to the U.S. Supreme Court, which denied the Commission's petition for certiorari. The State of Oregon, the Delaware River Port Authority (another interstate compact agency), and former Senators Mark O. Hatfield (R-Or) and Daniel J. Evans (R-Wa) (co-sponsors of the National Scenic Area legislation) all filed amicus briefs in support of the Gorge Commission.

In the past decade, several interstate compact agencies have asked the U.S. Supreme Court to consider the question of when an interstate compact agency must comply with the conflicting law of the states that created it. Generally, the federal courts throughout the county have determined that state law applies to an interstate compact only when specifically reserved in the compact. See e.g. Seattle Master Builders Ass'n v. Pacific Northwest Elec. Power and Cons. Planning Council, 786 F.2d 1359, 1371 (9th Cir. 1992). State courts throughout the country have been more favorable to applying state law. For example, the New Jersey Supreme Court looks to whether the law of the states is "complementary and parallel" and which does not intrude on the mission of the compact agency. Ampro Fisheries Inc., v. Yaskin, 606 A.2d 1099, 1103 (N.J. 1992).

Hopefully, the Supreme Court will soon decide to bring clarity to this esoteric area of law.

Jeff Litwak

Skamania County v. Woodall, 16 P.3d 701, 104 Wash. App. 525, rev. denied en banc 34 P.3d 1232, 144 Wash. 2d 1021 (2001), cert. denied —- U.S. —-, No. 01-958 (April 1, 2002).

THANK YOU AND GOODBYE

Stacy Harrop, student editor during the past year for the Digest, is graduating from Northwestern School of Law and moving on to a clerkship with Oregon Supreme Court Justice Robert D. Durham. On behalf of the section, many thanks to Stacy for her extremely capable editorial work on the Digest and best wishes in her new position.

DIGEST WRITERS WANTED

The Digest is interested in hearing from lawyers willing to submit articles for publication on a regular basis. If you are interested in being published, please contact **Kathryn Beaumont, RELU Digest editor** at (503) 823-3081 or *kbeaumont@ci.portland.or.us.*

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