

ESSAY QUESTION NO. 3

Answer this question in booklet No. 3

In January 2012 Oren purchased a river-front property with an existing finished single-family home within Alaska City, Alaska. His offer of \$500,000 prevailed over three other offers pending on the property. To buy the property, he paid \$100,000 cash and borrowed \$400,000 from Local Bank. Oren executed a deed of trust in favor of Local Bank to secure his promissory note. Oren and Local Bank properly recorded their respective interests. Oren purchased the property with the intent of capitalizing in the strong rental market by constructing an apartment over the existing garage and then applying the rental income to his loan. Immediately after the purchase Oren engaged an architect to design the rental apartment.

In February 2012 the Urban Access Commission (UAC) — an Alaska City commission tasked with identifying three potential access routes to a proposed River Span Bridge — defined the boundaries of the Proposed Bridge Access Area (PBAA). The UAC followed proper public notice procedures for its meeting and decision. In March of 2012, the Alaska City council passed city ordinance AC86 which, for the next 12 months, prohibited all new construction on properties within the PBAA. The Alaska City council stated that the purpose of AC86 was: “to save the city money on condemnations in the event that the State of Alaska funds the proposed River Span Bridge and it becomes necessary for Alaska City to construct an access road of a yet-to-be-selected route through the PBAA to the bridge site.”

In June of 2012, Alaska City denied Oren a routine building permit for the construction of the apartment stating that his property was within the PBAA and citing to AC86. Unable to capitalize on the still-strong rental market, Oren attempted to sell his property for the next two months but could not find a willing buyer. In September of 2012, Oren defaulted on his loan with Local Bank. Oren then filed suit against Alaska City alleging a taking and seeking compensatory damages.

1. Discuss the merits of Oren’s taking claim under Alaska law against Alaska City.

2. For the purposes of this question assume that Oren’s taking claim against Alaska City fails. Discuss Local Bank’s recovery options against Oren for his default on the loan.

GRADERS' GUIDE
***** QUESTION NO. 3 *****
REAL PROPERTY

1. Discuss the merits of Oren's taking claim under Alaska law against Alaska City. (70 total points)

The Alaska Constitution provides: "Private property shall not be taken or damaged for public use without just compensation." Alaska Const., Art. I, § 18. Further, Article I, section 18 is liberally construed in favor of the property owner. Bakke v. State, 744 P.2d 655, 657 (Alaska 1987). Moreover, "the requirement that the condemner pay just compensation when property is damaged provides broader protection for private property rights than the Fifth Amendment to the United States Constitution." Homeward Bound, Inc. v. Anchorage School District, 791 P.2d 610, 614 (Alaska 1990) (citing Bakke, at 655 and State v. Doyle, 735 P.2d 733, 736 (Alaska 1987)).

In Alaska, a property owner may recover damages through an inverse condemnation action if there has been a *per se* taking whereby the State (1) physically invades private property without instituting formal eminent domain proceedings or (2) otherwise employs land use regulations which deprive a property owner of all economically valuable use of the land. R & Y, Inc. v. Municipality of Anchorage, 34 P.3d 289, 293 (Alaska 2001)(citations omitted). When a case does not fall into either of these categories, courts must engage in a case-specific inquiry to determine whether governmental action effects a taking. Municipality of Anchorage v. Sandberg, 861 P.2d 554, 557 (Alaska 1993).

Here there are no facts to support the argument that Alaska City exercised formal eminent domain proceedings or physically invaded Oren's property. However, Oren may prevail on inverse condemnation by showing either (A) the PBAA designation deprived him of all economically valuable use of the land or (B) the enforcement of AC86 constitutes a compensable taking under Sandberg.

A. Inverse Condemnation: PBAA Designation

The facts state that the reason given by the Alaska City council for AC86 is "to save the city money on condemnations in the event that the State of Alaska funds the proposed River Span Bridge and it becomes necessary for Alaska City to construct an access road of a yet-to-be-selected route through the PBAA to the bridge site." Thus, Oren may argue that the inclusion of his property within the PBAA designation constitutes a declaration by the city of its intent to condemn his land at some future date and thereby has deprived him of all economically valuable use.

The Alaska Supreme Court has adopted a “four-part test to determine whether a government agency’s declared intent to condemn land at some future date is sufficient to deprive landowners of the full, beneficial use of their land. . . . (1) Is the land’s marketability substantially impaired? (2) Has the condemning authority evidenced an unequivocal intention to take the specific parcel of land? (3) Has the owner acquired and held the property for subsequent development and sale? and (4) Has the owner taken active steps to accomplish this purpose?” City of Kenai, Alaska v. Burnett, 860 P.2d 1233, 1240 (Alaska 1993)(citations omitted). Here the facts support a finding in favor of Oren on all factors except factor number two, which is discussed last.

Here Oren would argue that the marketability of his property is substantially impaired by the inclusion of his property within the PBAA designation by the UAC. The facts state that in January of 2012 when Oren purchased the property his offer bested three others. Four potential buyers vying for a property indicates a strong market demand. In July and August Oren attempted to sell the property but was unable to find a willing buyer which strongly suggests that the PBAA designation in February impaired the marketability of his property. Further, the facts indicate that Oren acquired the property for future development; he purchased the property with the intent to construct a new apartment for the purpose of supplementing his income. Moreover, Oren has demonstrated active steps toward accomplishing his development plan by way of immediately engaging an architect and applying for a building permit.

However, there is a question of whether the condemning authority evidenced an unequivocal intention to take Oren’s land. In Homeward Bound, the Alaska Supreme Court stated that “where the alleged taking is based on pre-condemnation decisions concerning the subject property, the objective manifestations of the government’s intention to take the property are critical to the decision whether there was a taking. This is because the government’s indications of its intention to condemn the property are the source of the owner’s claimed damages.” 791 P.2d at 614.

In Homeward Bound, the property owner claimed that a designation by the city assembly of the property as a potential school site constituted an unequivocal intention to condemn the property. 791 P.2d at 613. The Alaska Supreme Court rejected the property owner’s designation argument reasoning that whether the city assembly would condemn the property depended upon the decision of the school board, an independent agency, and that agency had never manifested an intention to select the property as a school site. Id. at 614. The court cited favorably to the California Supreme Court’s reasoning in Selby Realty Co. v. City of San Buenaventura, where “the court held that the mere enactment of a general plan showing proposed streets extending through private property did not constitute a taking because there was ‘no present concrete indication that the county either intended to use plaintiff’s property

for the proposed streets or that it intends to acquire the property by condemnation.” Id. (quoting 514 P.2d at 117 (Cal. 1973)(en banc)). Thus, the court in Homeward Bound held that “the Assembly’s mere designation of the property as a school site was not a concrete indication that the Municipality intended to condemn the property.” Id. at 615.

Here Oren may argue that the inclusion of his property within the PBAA designation constitutes intent to condemn his property at some future date. However, while the facts state that Oren’s property is within the PBAA there are no facts to suggest that Oren’s property is within any of the proposed access routes nor are there any facts to suggest that UAC or the Alaska City Council had selected a particular route. Moreover, condemnation of those properties along the yet-to-be-selected route by Alaska City is contingent upon the decision of the State of Alaska funding the River Span Bridge.

Therefore, Oren’s case is analogous to Homeward Bound and the PBAA designation probably does not constitute a concrete indication that Alaska City intended to condemn Oren’s specific property.

B. Inverse Condemnation: AC86 Enforcement

If Oren is unable to prove a loss of all economically valuable use due to the PBAA designation, he may, in the alternative, argue that he suffered a compensable taking through the enforcement of AC86. In R & Y, the Alaska Supreme Court stated the relevant inquiry:

[I]f there has been no per se taking – either through physical invasion of land or regulation that has deprived the landowner of all economically valuable use of the land – case-specific analysis is necessary to determine whether a compensable taking has occurred. Alaska courts engaging in this case-specific analysis consider four factors: (1) the character of the governmental action; (2) its economic impact; (3) its interference with reasonable investment-backed expectations; and (4) the legitimacy of the interest advanced by the regulation or land-use decision. These are known as the Sandberg factors.

34 P.3d at 293.

With regard to the first factor – the character of the government action – the Alaska Supreme Court has looked to whether the government’s action directly or indirectly affects the property owner’s use. R & Y, 34 P.3d 294. Here the character of the governmental action is direct: AC86 directly prohibits new construction within the PBAA. The direct nature of the character of the government’s action weighs in favor of a compensable taking.

With regard to the second factor – the economic impact of the government action – Oren must show that he suffered an economic harm but need not prove that the regulation constitutes a deprivation of all economically valuable use. Arguably Oren has been economically injured by the prohibition on new construction. The Alaska Supreme Court has expressed a preference for a “fair market value” approach to takings and employed a before and after valuation method of determining economic harm alleged by regulation. See Burnett, 860 P.2d at 1241-2. Here the relevant inquiry is the value of Oren’s property before and after the restriction. Arguably the property was worth \$500,000 before AC86 and, since Oren could not find a willing buyer, may be now worth \$0. On the other hand, the City would argue that the economic impact of AC86 is either nonexistent or de minimis since it is a temporary restriction and does not impact Oren’s use of the property as a residence. Further, Oren may also argue that he reasonably relied upon his ability to construct the apartment and his inability to do so cost him lost rental income and caused him to default on his loan with Local Bank and therefore the costs associated with any recovery proceeding by Local Bank also constitute an economic harm. In Alaska, the fundamental goal of “just compensation” is to make the property owner whole. State v. Hammer, 550 P.2d 820, 826 (Alaska 1976) (holding that while a business owner may recover for loss of profits resulting from a temporary interruption of the business due to the state’s exercise of eminent domain power, lost profits must be proven by a preponderance of the evidence to be a direct result of the taking and must meet reasonable certainty with regard to the amounts). Here, the direct economic impact of the default may fall within the scope of just compensation. On the other hand, Oren’s rental efforts may be speculative and his alleged lost profits may fail to meet the certainty standard since there are no facts to support a history of rental income or profits specific to Oren’s property.

The third Sandberg factor considers the interference of the regulation with reasonable investment-backed expectations. Here the facts state that Oren purchased the property with the intent to make the apartment addition specifically to capitalize on a strong rental market and to supplement his income. In State, Dep’t of Natural Resources v. Arctic Slope Regional Corp., the Alaska Supreme Court stated that for taking purposes “a reasonable investment-backed expectation must be more than a unilateral expectation or an abstract need.” 834 P.2d 134, 140 (Alaska 1991) (internal quotation omitted). Further, in Sandberg the court found that the plaintiff did not show evidence of a reasonable investment-backed expectation, “but rather, a business gamble.” 861 P.2d at 560 (citing Habersham at Northridge v. Fulton County, 632 F. Supp. 815, 823-24 (N.D. Ga. 1985)(holding that the county board’s refusal to change a property’s zoning from residential to commercial did not constitute a taking). Here Oren would argue that, unlike in Sandberg and Northridge, but for AC86, his proposed apartment addition would have required only the routine and well-established Alaska City permitting process and was, therefore, a reasonable investment-backed expectation and not

merely a “business gamble”. Oren’s position is further supported by the fact that the Alaska City rental market was strong before AC86 and continued to be strong after the AC86 restriction. Thus, Oren’s expectation of constructing the apartment to capitalize on a strong rental market is reasonable.

With regard to the fourth factor, the legitimacy of the interest advanced by the regulation or land-use decision, the City would argue that the AC86 restriction is temporary – limited to 12 months – and serves a public policy of reducing economic waste by prohibiting new construction that may be condemned. The Alaska Supreme Court has held that “the financial stability of a governing body is a legitimate governmental purpose in the regulatory takings arena.” Sandberg, 861 P.2d at 561 (citing Arctic Slope, 834 P.2d at 143).

The Alaska Supreme Court in R & Y noted that “Alaska case law does not elaborate on how the Sandberg factors are to be weighed against each other. But it is helpful to consider the policies that animate the federal doctrine from which the Sandberg factors were adopted.” 34 P.3d at 296-7. The Court reasoned that “[a]lthough no precise rule determines when property has been taken, the question necessarily requires a weighing of private and public interests.” Id. at 297.

Here Alaska City has directly affected Oren’s use of his property by expressly prohibiting new construction within the PBAA. Further, with additional facts Oren may show an economic harm by way of a reduction in fair market value or, in the alternative, a measure of Oren’s economic loss by his lost rental income and associated costs of default. Moreover, Oren can probably demonstrate that AC86 interferes with his reasonable investment-backed expectation of apartment construction to capitalize on the strong rental market. Here, there are no facts to suggest that Oren’s rental project was highly speculative or contingent upon anything other than routine government permitting. Lastly, Alaska City’s stated interest of reducing its costs should condemnations be required is probably a legitimate governmental purpose. In weighing the private and public interests it is important that AC86 applies only to those properties within the PBAA and not to all properties within Alaska City. Thus, AC86 imposes a burden on only few for the benefit of all.

Applicants may reach any conclusion as to whether the enforcement of AC86 constitutes a compensable taking under Sandberg.

2. For the purposes of this question assume that Oren’s taking claim against Alaska City fails. Discuss Local Bank’s recovery options against Oren for his default on the loan. (30 total points)

This question requires the examinee to assume Oren’s taking claim against Alaska City fails. The effect of this assumption is to maintain the

original relationship between Oren and Local Bank since Oren remains the properly recorded owner of his property. Therefore, after Oren's default Local Bank may either: (A) sue Oren on the note, (B) initiate a judicial foreclosure, or (C) proceed with a non-judicial foreclosure. Fireman's Fund Mortgage Corp. v. Allstate Ins. Co., 838 P.2d 790, 793 n. 5 (Alaska 1992).

A. Sue on the Note

Local Bank may elect to bring suit against Oren on the note. Here the facts state that Oren executed a promissory note and a deed of trust. In Alaska the note is the primary obligation and a mortgage or deed of trust follows the note. In order for Local Bank to first sue on the note, the note must state that Local Bank has the option to sue directly on the note without foreclosure. AS 34.20.160. There are insufficient facts to determine whether this language is within the promissory note. However, if Local Bank has the option to sue and obtains a judgment, Local Bank may only thereafter pursue judicial foreclosure but may not non-judicially foreclose. Id.

B. Judicial Foreclosure

Should Local Bank pursue a judicial foreclosure it retains the right to a deficiency judgment but is subject to a statutory right of redemption for twelve months after the sale is confirmed. AS 09.35.250. This means that for this period Oren has the right to buy the property back for the amount paid at the sale, plus actual costs. Id.

C. Non-Judicial Foreclosure

In the alternative, Local Bank may elect to non-judicially foreclose with notice to Oren. AS 34.20.070(a); see Rosenberg v. Smidt, 727 P.2d 778 (Alaska 1986). Should it do so, Local Bank gives up the right to obtain a deficiency judgment but the debt is not extinguished. AS 34.20.100; see Fireman's Fund Mortgage Corp., 838 P.2d at 794 (holding that AS 34.20.100 "contemplates the survival of a loan 'obligation' following the sale, but precludes the lender from seeking any 'deficiency' on this obligation either from the debtor or from the debtor's guarantor"). Unless otherwise stated in the deed of trust, sale must be made by public auction at the front door of the courthouse of the superior court within the judicial district in which the property is located. AS 34.20.080. Local Bank is subject only to Oren's equitable right of redemption through payment of the amount due plus costs before sale. AS 34.20.070(b).