

Through a Glass Darkly: Measuring Loss Under Oregon's Measure 37

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"For now we see through a glass, darkly"
—1 Corinthians 13:12:

"I am half sick of shadows"
—"The Lady of Shalott," Alfred Lord Tennyson

I. Introduction

JUST AS TENNYSON'S *LADY OF SHALOTT* had yet to see the reality of Camelot, Oregonians have yet to experience the full reality of Measure 37. This is true, not only with respect to the impact that Measure 37 will have on land use patterns in the state, but also with respect to the correct interpretation of the Measure itself. While the contours of the Measure may be relatively clear, ambiguities abound in the details, as the lack of a clear law or precedent obscures the impact of the Measure and confounds those framing responses to it.

The planning process in Oregon, however, has clearly been transformed by the passage of Measure 37.¹ After the failure of multiple constitutional challenges to its enactment,² Measure 37 is now part and parcel of the Oregon planning program and, as a political matter, is not likely to be excised completely any time in the near future.³ Oregonians have now twice voted for government payments for regulation, and the argument that the voters did not understand the

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1. The Measure, codified at OR. REV. STAT. § 197.352 (2005), was enacted through the initiative process on November 2, 2004, and took effect on December 3, 2004.

2. *MacPherson v. Dep't of Admin. Servs.*, 130 P.3d 308 (Or. 2006) (involving a series of facial challenges to Measure 37 under the Oregon and federal constitutions). After the Measure was declared unconstitutional in the trial court, the Oregon Supreme Court reversed that decision.

3. At the time of the preparation of this article, the Oregon legislature had proposed a number of changes to the Measure. Oregon voters will act on this proposal, known as Measure 49, at a special election to be held on Nov. 6, 2007. *See* H.B. 3540-6, 74th Leg. (Or. 2007).

impacts of these ballot initiatives seems unavailing. It is more likely that changes to the Measure will be discussed in legislative proceedings.⁴ In the meantime, and even after further modifications to the Measure, Oregonians likely will live with at least some of its effects.

Very broadly, the Oregon planning program seeks to provide a participatory, coherent, and enforceable planning policy applicable to all nonfederal lands in the state, preserve resource lands for resource use, separate rural and urban lands, and concentrate growth within urban growth boundaries. Adopted by initiative, Measure 37 is an amendment to that program. The Measure operates so that if a parcel of land has been in the hands of a family member before a particular land use regulation was enacted, the current owner may bring a monetary claim against the public body that imposed the land use regulation, provided the regulation reduces the use of the property and “has the effect of reducing the fair market value of the property.” If the public body does not have the funds for payment of the claim (which is nearly always the case),⁵ that body has the option to “modify, remove, or not to apply”⁶ those regulations so as to replace them with those in place at the time the current owner acquired the land.⁷

Although the state land use program⁸ remains, the continued existence of Measure 37 could undermine these public policy objectives by allowing land tenure to trump state policy. A system of exemptions based on length of ownership creates a checkerboard pattern of land use regulations. The extent of this checkerboard will depend on whether the state, local governments, and the public as a whole are scrupulous and diligent in requiring uniform application and compliance with the language of the Measure.

4. This author predicted efforts to rationalize the inconsistencies, vagueness, and unintended consequences of the Measure. See Edward J. Sullivan, *Year Zero: The Aftermath of Measure 37*, 38 URB. LAW. 237, 256–60 (2006).

5. As of March 1, 2007, the City of Prineville was the only jurisdiction within the state offering to pay public funds in lieu of granting a waiver of the land use regulations. The city offered the property owner \$47,000 to prevent the construction of a residence on a property. Notwithstanding the offer, the owners subsequently filed a secondary Measure 37 claim for the same property seeking over \$5 million dollars or waiver to construct a restaurant or other commercial use. See *Prineville Couple Raise Ante on Measure 37 Claim*, THE OREGONIAN, Dec. 1, 2006, available at <http://www.oregonlive.com/news/oregonian/index.ssf?/base/news/116493813427660.xml&coll=7>.

6. OR. REV. STAT. § 197.352(8) (2005).

7. In common parlance in Oregon, this triad is referred to as “waiver,” which is the term used in this article.

8. See generally OR. REV. STAT. § 197; Sullivan, *supra* note 4, at 242–44.

Valuation is an issue of particular ambiguity—and, hence, controversy—within Measure 37. The Measure says very little on the subject (aside from creating a statutory right to “just compensation” if the fair market value of land is devalued by a land use regulation).⁹ Its discussion of valuation is largely confined to the following statement found in subsection (2):

Just compensation shall be equal to the reduction in the fair market value of the affected property interest resulting from enactment or enforcement of the land use regulation as of the date the owner makes written demand for compensation under this section.¹⁰

In eminent domain law the words “just compensation” mean the price a willing buyer would pay for land from a willing seller with both parties having knowledge of the marketplace.¹¹ Measure 37, however, uses this eminent domain term to establish the obligation of a public body to pay for regulation, even though that public body is not seeking to acquire property for public use, as it would be under eminent domain law.¹² Indeed, the appearance of these words in the ballot title and caption may well have been a significant reason for the passage of the Measure. However, it should not be assumed that the valuation methodology utilized in eminent domain law can be transposed to Measure 37 claims. Nor should it be assumed that the valuation methodologies ought to be analogous: the correct valuation methodology for Measure 37 claims is a normative question, which calls for an in-depth analysis of the text, context, and legislative history of the measure, as well as a critical review of the economic arguments.

This article is divided into six parts. Following this introduction, Section II discusses the structure of the Measure itself and current practice in administering Measure 37 claims. Section III illustrates the importance of assessing the *exact* quantification of the alleged loss in each Measure 37 claim, prior to any decision whether to pay or waive on behalf of the local governments. Section IV provides a review and critical analysis of proposed valuation methods. Section V assesses each of the valuation methodologies against the text, context, and legislative history of Measure 37 to determine its legal validity. Finally, the best of these valuation methods is selected and explained in terms of the Measure.

9. OR. REV. STAT. § 197.352(1) (2005).

10. *Id.* § 197.352(2).

11. *See, e.g.*, *State v. Lundberg*, 825 P.2d 641, 644–45 (Or. 1992).

12. *See, e.g.*, OR. REV. STAT. § 197.352(1)–(2).

II. The Structure of Measure 37 and the Use of Appraisals in Measure 37 Claims

As relevant, Measure 37 creates a statutory, rather than constitutional, cause of action in the event a “land use regulation”¹³ “has the effect of reducing the fair market value of the property.”¹⁴ That cause of action provides either for payment from the public agency of “just compensation” under subsection (2) or, alternatively, a waiver of the applicable regulations up to the date of the property’s acquisition by “the owner” under subsection (8).¹⁵

Filing a written claim with the public agency adopting the land use regulation triggers the “pay or waive” process: the claim must be granted or denied within 180 days.¹⁶ After that time, the landowner may bring a claim in the circuit court to enforce the public payment and, if successful, is entitled to “attorney fees, expenses, costs and other disbursements.”¹⁷ If a claim has not been paid within two years from the date of filing, “the owner shall be allowed to use the property as permitted at the time the owner acquired the property.”¹⁸

The lack of discussion of the payment alternative, and the relative precision of the waiver alternative, indicates the direction contemplated by the drafters of the Measure. The State of Oregon, the Portland Metro Regional Government (“Metro”), and cities and counties adopting and enforcing land use regulations have a choice, clearly granted to them by the language of the Measure, either to pay or waive valid claims. That choice is not made in a vacuum, but against the remaining provisions of Chapter 197 of the Oregon Revised Statutes, to which the Measure was added. These provisions—resource conservation,¹⁹ needed housing,²⁰ and implementation of existing state policy in the statewide planning goals and administrative rules²¹—continue to apply. Before a decision to pay or waive is made, an evaluation of the alternatives must be undertaken

13. Under subsection 197.352(11)(B) of the Oregon Revised Statutes, this term “includes” statutes, or goals and administrative rules of the Land Conservation and Development Commission, the state’s land use agency, or local government comprehensive plans, zoning, land division, or transportation ordinances. The term also applies to planning and regulatory exercises by the Portland Area Metropolitan Service District, as well as statutes and administrative rules regulating farm and forest practices. OR. REV. STAT. § 197.352(11)(B)

14. In full, this reduction may affect any interest in property. *Id.* § 197.352(1).

15. “Owner” is defined for purposes of the section as “the present owner.” *Id.* § 197.352(11)(C).

16. *Id.* § 197.352(4).

17. *Id.* § 197.352(6).

18. OR. REV. STAT. § 197.352(10) (2005).

19. *Id.* §§ 215.203, .243.

20. *Id.* §§ 197.303–.309.

21. *Id.* § 197.829(1).

in the light of state policy. The amount of payment due must be weighed against the alternative of waiving the regulation. While the discussion of the valuation methodology is hardly academic, most local governments unfortunately have treated it as such.

Local governments have reacted to Measure 37 claims paralyzed like a deer caught in the headlights: usually apply a planning policy to waive land use regulations in favor of any potentially eligible Measure 37 claimant. Indeed, the term “planning policy” in this context is at best misleading, and at worst oxymoronic. Local governments have neither adopted strategic approaches to Measure 37 to limit the detrimental effects of waiver, nor considered whether paying all or some of the eligible claims may actually be in the public interest.²² Instead, cowed by inaccurate, hyperbolic estimations of the cost of land use regulations, having a short time to decide claims, and facing possible judgments and attorney fees, local governments have largely abrogated any responsibility for protecting the Oregon land use program from the effects of Measure 37 claims.

Few governing bodies engage in a rigorous review process of the asserted loss, with a number routinely approving claims on the mere possibility that there has been some loss.²³ While there is no uniform system for assessing Measure 37 claims—the length and content of the staff reports, as well as the required evidential basis, varies quite dramatically among state, metropolitan, and local governments—the following paragraph is indicative of the superficial assessment that the state engages in when quantifying losses:

The claim asserts that the existing state land use regulations enforced by the Commission or the department have the effect of reducing fair market value of the subject property by \$115,000. However, without additional relevant evidence demonstrating that the land use regulation[s] . . . reduce[d] the fair market value of the subject property, a specific amount of compensation cannot be determined. In order to determine a specific amount of compensation due for this claim, it would also be necessary to verify whether or the extent to which the claimants’ desired use of the property was allowed under the standards in effect when they acquired the property. *Nevertheless, based on the record for this claim, the department has determined that the laws on which the claim is based have reduced the fair market value of the subject property to some extent.*²⁴

22. Generally an eligible applicant is one who can demonstrate that: (1) the applicant or a family member owned the property prior to the enactment of the land use regulation, (2) there is evidence that the land use regulation challenged has been enacted or enforced, (3) the regulation in question has “restricted the use” of the property, and (4) the fair market value of the property has been reduced as a result of the enactment or enforcement of the regulation. *Id.* § 197.352.

23. This is despite a number of local governments superficially requiring an assessed demand for compensation at a specific dollar amount.

24. *In re Nice*, Claim No. M124351, before the Or. Dep’t of Land Conservation & Dev., 6 (Sept. 11, 2006) (emphasis added), available at http://www.oregon.gov/LCD/MEASURE37/docs/finals2006/M124531_Nice_Lane.pdf.

Although the burden rests on the claimant to prove, *inter alia*, that the regulation challenged reduced the fair market value of her property, the state appears to assume that, so long as the preceding criteria are satisfied and there has been *some possible loss* (regardless of the amount), prudence dictates the regulations be waived. Indeed, even if claimants fail to provide detailed assessments of loss, Department of Land Conservation and Development (DLCDC) staff reports evaluating Measure 37 claims for the State of Oregon commonly and perfunctorily conclude with the statement “[n]evertheless, based on the record for this claim, the department has determined that the laws on which the claim is based have reduced the fair market value of the property to some extent.”²⁵

The State of Oregon is not the only one guilty of gingerly retreating under the threat of Measure 37 compensation claims. The DLCDC is the agency chiefly responsible for determinations of payment or waiver and uses a fairly low threshold in evaluating claims. The standard of review invoked by the majority of local governments is, if anything, less intense than that applied by the state. The claimant must merely show that it is “more likely than not” that there has been some reduction in the value of her property in order to obtain a waiver.²⁶ There have even been cases where the local government has determined—without reference to any evidence submitted by the claimant—that the land use regulation caused loss. In the City of Portland, for example, a staff report assessing a Measure 37 claim stated:

Staff can find *no basis for the estimated loss* of value claimed by Mr. Grudzinski. The change in Comprehensive Plan designation did not change the density to which he would be able to develop his property. The current zoning, R20, has remained the same since he purchased his property and the number of units he can lawfully have on the property has not changed.²⁷

Yet the planning staff went on to conclude:

That said, staff estimates that it is more likely than not that the value of the subject property has been reduced by at least one dollar as a result of changing the comprehensive plan designation from R10 to R20.²⁸

25. *See id.*

26. *See id.* The phrase repeatedly used by local governments is: “Nevertheless, based on the submitted evidence, the department determines that it is more likely than not that there has been some reduction in the fair market value of the subject property.” *Id.*

27. *In re Grudzinski*, Ballot Measure 37 Claim for Compensation (OR. REV. STAT. § 197) Staff Report and Recommendations, Claim No. 05-126994 PR, 13 (Nov. 23, 2005) (emphasis added), available at <http://www.portlandonline.com/shared/cfm/image.cfm?id=100361>.

28. *Id.*

Thus, despite failing to supply any relevant proof that the fair market value of his property was reduced by land use regulations, the claimant was granted a waiver of the existing zoning.²⁹ Such reasoning clearly undermines the statement in the “Voters’ Pamphlet,” which declared that, “if a property owner proves that a land use regulation restricts the use of the owner’s property, and reduces its value then the government responsible for the regulation will have . . . [to] pay the owner of the property an amount equal to the reduction in value.”³⁰

Thus, the level of proof required by at least some local governments is negligible: in the *Grudzinski* case the claimant did not even have to establish loss on the balance of probabilities.³¹ However, a number of local governments have begun to assess the amount of compensation claimed with greater scrutiny. Both the Metro and Multnomah County authorities analyze each claim in considerable depth, and both have rejected a number of otherwise eligible claims *purely* on the basis that the land use regulation did *not* result in the reduction in fair market value of the affected property.³² Applicants in these jurisdictions have had their claims denied on this basis, despite producing far more evidence to support their claim than that provided in the Portland case. Moreover, Metro has decided to employ a more rigorous valuation methodology than other local governments, rejecting the notion, seemingly apparent elsewhere, that enactment or enforcement of any land use regulation that restricts the claimants’ use of the property has “more likely than not” reduced the fair market value of the affected land.³³

29. *In re Grudzinski*, Order of Portland City Council, Claim No. 05-126994 PR (Nov. 2005), available at <http://www.portlandonline.com/index.cfm?c=40047>.

30. OR. SEC’Y OF STATE, 2004 GENERAL ELECTION VOTERS’ PAMPHLET 104 (2004) available at <http://www.sos.state.or.us/elections/nov22004/guide/pdf/vpvol1.pdf> (the explanatory statement is an impartial statement explaining Measure 37).

31. It was the local authority that concluded there was a possibility of some loss, with Mr. Grudzinski’s evidence providing no basis for the loss claimed. It comes as little surprise that the repetition of decisions based on similar paucity of evidence has resulted in a writ of review challenge by claim opponents on the basis that “the State’s findings and conclusions . . . are not supported by substantial evidence.” *In re Grudzinski*, Order of Portland City Council, Claim No. 05-126994 PR (Nov. 2005), available at <http://www.portlandonline.com/index.cfm?c=40047>. Indeed, as the only evidence regarding reduction in value on the record in Grudzinski’s case is the claimant’s own statement, it is hard to argue with the petitioner’s contention that the agency’s valuation appraisal was based on no more than guesswork.

32. See Attachment 2 to Report of the Metro Chief Operating Officer; In Consideration of Council Order No. 07-018 For the Purpose of Entering an Order Relating to the Measure 37 Claim of Richard L. and Sharon K. Kurtz (Jan. 2007), entitled Metro Memorandum to Ray Valone and Richard Benner from Sonny Conder and Karen Hohndel (Jan. 25, 2007), available at http://www.metro-region.org/library_docs/land_use/cooreport07_018.pdf.

33. The Metro-Region employs the so-called Jaeger/Plantinga method. See *infra* note 105.

Before moving to analyze the importance of establishing a valuation method, we must first consider the factors which have led to the local governments' reluctance to scrutinize the declared loss to any great degree, and which has resulted in their largely eschewing the need to establish an accurate valuation method.

Judging from the evidence highlighted above the majority of local governments appear to be risk-averse when dealing with Measure 37 claims, and the statute gives them good reason to be so. Subsection (6) of the Measure contains a one-sided attorney fee provision. Thus, if a court rules that a local government has improperly denied a claim (and therefore that "the land use regulation continues to apply"), the claimant is entitled to "reasonable attorney fees, expenses, costs, and other disbursements reasonably incurred."³⁴ Without the certainty a *court-approved* valuation method would bring, and due to the fact that claimants only need to prove a minimum loss of one dollar, many local governments are understandably nervous about rejecting a claim when there is even a remote chance that the land use regulation has caused a reduction in a property's value. This difficulty is compounded by the short time frame that local governments are afforded for decision making,³⁵ the lack of any requirement that the claimant provide specific details to support a claim, and the fear that any procedure they may establish will be made invalid by subsection (7) of the Measure.³⁶

Despite these factors, the blanket "planning policy" which dictates that all eligible claims shall be remedied by the waiver of all of the challenged land use regulations is the greatest inhibitor to local governments' close scrutiny of the accuracy of Measure 37 claims. The reasoning behind this proposition may not be immediately obvious, however its logic runs as follows: the governing body's legal power to "modify, remove, or not to [sic] apply the land use regulation," granted in subsection (8) of the Measure, is "in lieu of [monetary] compensation."³⁷ Importantly, the prevailing interpretation of the language "in lieu of compensation" is not that the waiver must be "comparable to," or "equivalent in financial terms to," the

34. OR. REV. STAT. § 197.352(6) (2005).

35. *Id.* § 197.352(6); Press Release, Or. Joint Special Comm. on Land Use Fairness (Jan. 19, 2007), available at http://www.leg.state.or.us/press_releases/courtney_011907.pdf (noting that "180-day approval period prevents a thorough case-by-case review and instead forces local governments to make snap decisions to comply with the law").

36. OR. REV. STAT. § 197.352(7).

37. *Id.* § 197.352(8).

amount of compensation payable, but rather that the waiver is “instead of” monetary compensation.³⁸

Combining this interpretation of subsection (8) with the “waiving regulations for all eligible claims” policy ensures that once the claimant has proven that there has been a devaluation in the fair market value of the property caused by the land use regulation (or more accurately that the local government has accepted her assertion that there has been devaluation), the magnitude of that loss is entirely irrelevant. There is little incentive for local governments to engage in a complex, time-consuming valuation report in order to determine the exact dollar amount of loss when the magnitude of the loss ultimately will have no bearing on the remedy. The only cases in which local governments would have an incentive to scrutinize the alleged compensation carefully are borderline cases, where the question of whether there was any devaluation is at issue. However, as seen from the examples given above, there appears to be a widespread belief among most public agencies that any land use regulation that restricts the use of a property must also have resulted in a net loss to the value of the property, if only “by at least one dollar.”³⁹ That is, once the applicant has demonstrated the relevant antecedent formalities, including a demonstration that the regulation in question has “restrict[ed] the use of [the] property,”⁴⁰ the question of whether there has been *any* devaluation is, for many local authorities, as redundant as the question of magnitude of loss.

III. Why Quantification Matters

A discussion of the quantification of loss pursuant to Measure 37 claims may be deemed somewhat inconsequential considering that there is only one instance of an offer for payment of a monetary claim.⁴¹ With a

38. This interpretation of “in lieu of” has been confirmed in the recent partial summary judgment by Judge Don Dickey, Circuit Court of Marion County, Oregon. *Vanderzanden v. Land Conservation & Dev. Comm’n*, Case No. 05C19565 (Marion County, Or. Cir. Ct. Jan. 2007); *Hood River Valley Residents v. State*, Case No. 06C17267 (Marion County, Or. Cir. Ct. Jan. 2007); *Messer v. Land Conservation & Dev. Comm’n*, Case No. 06C18036 (Marion County, Or. Cir. Ct. Jan. 2007).

39. *See, e.g., In re Grudzinski*, Ballot Measure 37 Claim for Compensation (OR. REV. STAT. § 197) Staff Report and Recommendations, 13 (Nov. 23, 2005) (emphasis added), available at <http://www.portlandonline.com/shared/cfm/image.cfm?id=100361>.

40. OR. REV. STAT. § 197.352(1).

41. As of January 23, 2007, Portland State University’s Institute of Metropolitan Studies has documented that over 7,500 Measure 37 claims have been filed, including over 750,000 acres. The total cost in compensation claimed totals \$10,448,335,417. SHEILA A. MARTIN, ET AL., *WHAT IS DRIVING MEASURE 37 CLAIMS IN OREGON* (2007), available at http://www.pdx.edu/media/i/m/ims_M37pptApril07UAAppt.pdf.

plethora of legal uncertainties surrounding Measure 37, one could argue that there is little practical benefit to more attention and debate on this issue. Furthermore, for those who wish to limit the detrimental effects of Measure 37, the issue of valuation may seem ethereal; an academic nicety the resolution of which will do little to prevent the threat of piecemeal development, loss of farmland, and further sprawl, given local governments' policy of granting waivers for any arguably eligible claim.

But nothing could be further from the truth. Establishing a comprehensive and understandable method of valuing alleged loss under Measure 37 is of paramount importance. Such a method is necessary to ensure all governing bodies apply the Measure in a manner that is not only comprehensible and accurate, but also consistent with its text, context, and legislative history, thereby ensuring payment only to those who have suffered a *true loss*, as defined by the statute. A valuation methodology for Measure 37 claims that does not fit with a justifiable (and justified) interpretation of the statute undermines both legislative and voter intent.

Most critically, public agencies need a sound valuation methodology to ally a functional planning system with the realities of the payment scheme set out in Measure 37. This is true both retrospectively—managing those claims pursuant to pre-Measure 37 land use regulations—and prospectively—ensuring future land use regulations are not rendered wholly impotent. For those dedicated to protecting Oregon's land use planning system, the establishment of an accurate valuation method is one of the first of many steps that will lead to the re-establishment of effective planning policy, the limitation of piecemeal development, and the prevention of planning sclerosis.

In waiving applicable land use regulations, Measure 37 allows for haphazard development of land based solely on the longevity of land tenure, and threatens to undermine the last three decades of careful, detailed planning policy in Oregon. However, if an accurate valuation of loss in each claim can be established, local governments may be able to take a more strategic approach to Measure 37 claims and pay at least some of the monetary claims. For instance, a local government could adopt a policy to pay all claims in a certain geographical area or pay all claims with regard to certain land use regulations, thereby ensuring that at least some of the land use regulations enacted prior to Measure 37 are kept wholly intact. The lack of any dedicated funding source most likely precludes the payment of *all* eligible claims. But by prioritizing particular regulations or geographical areas for enforcement, and balancing the

net benefits of enforcement (the benefits of the regulation less the cost of compensation) against the net costs of waiver (the losses induced by having exemptions to the land use regulation), haphazard development, and the general disintegration of current planning policy can be prevented.

Remembering that the decision to pay or waive is not taken in a vacuum, but must be made against the background of state policy on land use, and that any decision must be justified by reference to this policy, the notion that local governments should adopt such a “damage-limitation” procedure is reinforced.⁴² As one commentator has noted, the “inconsistent uses [created by local governments waiving land use regulations] can frustrate many aspects of the comprehensive plans, including those that were intended to implement [urban] statewide planning goals. . . .”⁴³

However, the sclerotic effect that Measure 37 will have on the future of planning in Oregon is potentially more serious than the lack of strategic policy by public agencies to deal with past claims. When attempting to make light of the impact of the Measure on Oregon planning law, Measure 37 supporters tend to overlook the chilling effect the Measure has on future planning policy.⁴⁴ The chilling effect results from the fact that all new regulations or amendments to plans, so long as they cannot be squeezed into the relatively narrow exceptions contained within subsection (3) of the Measure, will be de facto inapplicable with regard to all the affected Oregon residents—at least if the regulation causes a devaluation in the fair market value of their property. Indeed, a commentator notes that the paralytic effects are already being felt with, “many cities hav[ing] postponed or abandoned initiatives to amend their comprehensive plans and land use regulations.”⁴⁵

42. Indeed, Measure 37 was specifically made part of chapter 197 of the Oregon Revised Statutes by its terms. OR. REV. STAT. § 197.352(1) (2005).

43. GLENN KLEIN, MEASURE 37: (UN)INTENDED CONSEQUENCES ON LAND USE PLANNING (2006) (report distributed at the 2006 International Municipal Lawyers Association Annual Conference) (on file with author).

44. See Leonard Gilroy, *Statewide Regulatory Taking Reform: Exporting Oregon's Measure 37 to Other States*, REASON FOUND., Apr. 2006, at 34. In his paper Mr. Gilroy attempts to dismiss the myth that Measure 37 “decimates land use regulation,” however he restricts his comments on the effects of the measure on prospective planning policy to the notation that “Measure 37 . . . does not prohibit the State of Oregon and/or local governments from adopting laws that regulate public health and safety,” before going on to list some of the other exceptions found in subsection (3). Gilroy does not discuss the very factor that threatens to decimate land use regulation: the impact of Measure 37 on those land use regulations which do not fit within one of the listed exemptions. *Id.*

45. KLEIN, *supra* note 43. Indeed, the Metropolitan Service District in Ordinance 05-1077, adopted on September 29, 2005, took a less regulatory and more educational and

This author has already suggested that planners in Oregon may attempt to use the exceptions listed within the measure creatively, and has stressed that any such creativity would likely be shown substantial deference by the courts, due to separation of powers considerations.⁴⁶ There are undoubtedly amendments and land use regulations, however, that cannot be squeezed within the exceptions listed. Again the issue of valuation is of paramount importance: establishing an accurate, practicable method of quantifying loss would at least allow local government planners to produce cost estimates for future planning regulations, and force local governments to think about how to deal with these costs. For instance, if a regulation fell outside one of the statutory exceptions, then the planner could establish the total cost, assuming all current landowners are likely to make Measure 37 claims that the local government would have to bear to ensure the regulation was fully potent. From this quantification it would again be possible to perform a cost-benefit analysis, factoring in the added costs of the Measure 37 claims, to determine whether the proposed regulation should be enacted or enforced.

Finally, establishing a comprehensive and comprehensible valuation methodology is necessary to ensure uniformity. Uniformity is important for two reasons: first, it ensures the fair and equal application of the Measure 37 procedure between claimants, and second, it creates consistency and predictability.

Despite the lack of a dedicated centralized database of Measure 37 claims,⁴⁷ it is apparent that valuation methodologies are inconsistently employed.⁴⁸ While some local governments must be commended for taking a more proactive stance by challenging the presumption that land

site acquisition through purchase approach in dealing with natural resources in the Portland Metropolitan area. Whether that approach is more successful is yet to be determined. In addition, the use of the Endangered Species Act and the various federal acts relating to air and water quality provide a fairly comprehensive backup for the regulatory approach in any event. *Id.* (citing Endangered Species Act of 1973, 16 U.S.C. § 1531-44 (2000)).

46. See Sullivan, *supra* note 4, at 157.

47. See Portland State University Institute of Portland Metropolitan Studies, Measure 37: Database Development and Analysis Project, <http://www.pdx.edu/ims/m37database.html> (last visited May 22, 2007). This database, however, depends on self- or third-party reporting and is neither especially detailed nor comprehensive.

48. The disparities have been noted by the main proponents of Measure 37. See Oregonians in Action, Ballot Measure 37 "Implementing" Ordinances, http://measure37.com/measure%2037/local_ordinances.htm (last visited May 22, 2007) (classifying local governments into categories: "Good" (i.e., very little scrutiny), "Bad" (i.e., those that demand some evidence, and assess claims to a certain degree) and "Multnomah County" (which, Oregonians in Action suggests, is "clearly . . . intend[ing] to deprive its citizens of the rights secured by Measure 37")).

use regulations axiomatically result in the devaluation of the affected property, the disparity in assessment processes results in an arbitrary and unfair application of Measure 37.

While uniformity is an important safeguard for claimants, it also has a wider benefit in the form of predictability. If one valuation method is agreed-upon or mandated by the court, it will benefit all interested parties. Prospective Measure 37 claimants will be able to assess informally their chances of succeeding on the question of loss, prior to making the claim. More significantly, the state and local governments will be less cowed by the attorney fees provision; so long as they correctly apply any court-approved or uniformly agreed upon method of valuation, there should be little opportunity for claimants to argue that their claims have been improperly denied, at least with regard to the “reduction in fair market value” criterion.

Establishing a comprehensive, understandable method for quantifying the devaluation in the fair market value of properties affected by the land use regulation is imperative, both to ensure uniformity of application, and also to begin formulating a strategic response to the threat Measure 37 poses to Oregon’s land use system. Public agencies must now step out of the headlights and consider how to evaluate the validity of Measure 37 compensation claims.

The 2007 Oregon Legislature established a Joint Committee on Land Use Fairness to resolve the many difficulties of the Measure. Among much other testimony, the Joint Committee heard a *Measure 37 Report and Recommendations* from former Governors Victor Atiyeh and Barbara Roberts and prominent resort developer John Gray, dated March 21, 2007.⁴⁹ That report formed one basis for a bill passed by the legislature and sent to Oregon voters to “fix” Measure 37.⁵⁰ By its terms, the “fix” was referred to Oregon voters for their approval or rejection at a special election to be held in November, 2007.⁵¹ A companion bill extended the time in which the state or local governments were required to decide Measure 37 cases by another 360 days.⁵² The effect of the extension is to allow additional time to determine the glut of claims filed shortly before the December 4, 2006, deadline for filing claims

49. Measure 37 Report and Recommendations: Hearing on H.B. 3540, 74th Leg. (Or. 2007) (statement of Victor Atiyeh, former Governor and Barbara Roberts, Developer) (on file with author).

50. 2007 Or. Laws ch. 424 (Enrolled House Bill 3540).

51. 2007 Or. Laws _____ (Enrolled House Bill _____) (otherwise known as ballot Measure 49).

52. 2007 Or. Laws ch. 133 (Enrolled House Bill 3546).

without having to include those claims with a land use application of some sort. If not granted, those claims would be required to have been decided within 180 days of filing.⁵³

Among many other things, the “fix” requires that valuation issues be the subject of appraisals by licensed appraisers,⁵⁴ changes the definition of “market value” for Measure 37 purposes,⁵⁵ establishes a minimum threshold for most claims,⁵⁶ limits nonmonetary compensation to home sites only,⁵⁷ and uses the difference in value one year before and after enactment of the regulation that is the basis for the claim.⁵⁸ However, for all claims not determined and adjudicated, the issues set out in this article remain. Moreover, if the revisions do not receive voter approval, the regime described in this article will continue to apply.

IV. Literature Review of Economic Analyses

This section reviews the current economic literature on valuation of Measure 37 claims and, in particular, focuses on the variety of methods which have been proposed for quantifying loss caused by land use

53. See Edward J. Sullivan, *Betting the State*, PORTLAND DAILY J. OF COM., May 10, 2007.

54. 2007 Or. Laws _____ § 20 (Enrolled House Bill 3540)

55. 2007 Or. Laws _____ § 21b (Enrolled House Bill 3540) provides:

For the purposes of subsections 5 to 22 of this 2007 Act, the fair market value of property is the amount of money, in cash, that the property would bring if the property was offered for sale by a person who desires to sell the property but is not obligated to sell the property, and if the property was bought by a person who was willing to buy the property but not obligated to buy the property. The fair market value is the actual value of property, with all of the property’s adaptations to general and special purposes. The fair market value of property does not include any prospective value, speculative value or possible value based upon future expenditures and improvements.

56. *Id.* §§ 4(1)–(2). These sections use the term “unfairly reduces the value.” *Id.* § 12(2) sets the standard and provides:

- (2) The enactment of one or more land use regulations has the effect of unfairly reducing the fair market value of property if the regulation or regulations cause:
 - (a) Any reduction in the fair market value of the property by reason of the enactment of a farming or forest practice regulation;
 - (b) A reduction of 10 percent or more in the fair market value of the property by reason of the enactment of one land use regulation, other than a farming or forest practice regulation;
- or
- (c) A reduction of 25 percent or more in the fair market value of the property by reason of the enactment of two or more land use regulations that are not farming or forest practice regulations during any five-year period.

57. *Id.* §§ 7(2)(c), 7(5)(g), 9(c).

58. *Id.* §§ 7(b), 7(7), 8(4), 9(6), 9(7), 12(3).

regulations. Each of these valuation methods is analyzed against the criterion of the accuracy of that method in quantifying the loss caused by the land use regulation in question.

A. *The Exemption Method*

The majority of applications under Measure 37 employ the so-called “exemption method” to quantify the loss in value of their properties resulting from the “enactment or enforcement” of the land use regulation. While it has not been advocated in any academic literature, the exemption method is also currently accepted by most local governments as a valid means of loss quantification.⁵⁹ The attraction of this method lies both in its simplicity, and, from the claimant’s viewpoint, its propensity to result in high loss estimates. As Professors Jaeger and Plantinga explain, the method assumes that:

“[J]ust compensation” under Measure 37—that is, a government making up for the reduction in value of a property resulting from a land-use regulation—is equal to the increase in value if the regulation is waived for that property alone.⁶⁰

The Measure 37 claim made in the City of Portland by Augustine and Lorraine Calcagno serves as a valuable illustration of how the exemption method works.⁶¹ The Calcagnos owned two parcels of land, totaling 19,400 square feet. A single residential dwelling was situated on each parcel. The property was rezoned sometime after their purchase, effectively reducing the number of units which could potentially be developed on the site by two-thirds.⁶² According to the authors of a report documenting their claim, the Calcagnos claimed “that land use regulations have decreased the value of their North Portland property by

59. Libby Tucker, *A Method in the Madness*, DAILY J. OF COM., July 13, 2006, available at <http://www.friends.org/issues/M37/documents/M37-DJC-2006-07-13.pdf>.

60. See W.K. Jaeger & A.J. Plantinga, *The Economics Behind Measure 37*, EM 8925 OR. STATE UNIV. EXTENSION SERV. 1–4 (2007), available at <http://extension.oregonstate.edu/catalog/pdf/em/em8925.pdf>.

61. See SHEILA A. MARTIN & KATIE SHRIVER, DOCUMENTING THE IMPACT OF MEASURE 37: SELECTED CASE STUDIES (2006) [hereinafter MARTIN & SHRIVER]. The Calcagno claim is the basis of *Case Study 2: The Role of Community Planning in North Portland*. *Id.* at 22. Their compensation claim is considerably smaller than the majority of other claimants in the remaining nine case studies. The Calcagnos claimed \$500,000 in loss, while the average public payment claimed over the ten claims nears the \$3 million mark. *Id.*

62. *In re Calcagno*, Ballot Measure 37 Claim for Compensation (OR. REV. STAT. § 197) Staff Report and Recommendations, Claim No. 05-117098 PR (Aug. 12, 2005) [hereinafter Calcagno Staff Report], available at <http://www.portlandonline.com/shared/cfm/image.cfm?id=96464>.

\$500,000. . . . They based their estimate on the assumption that the property can be sold for \$10,000 per allowed unit; thus, the loss of fifty-six units brought him [*sic*] to approximately \$500,000.”⁶³

Although there was some disagreement about the exact amount, the Portland City Council concluded that it was “more likely than not that the challenged regulations have reduced the fair market value of the property.”⁶⁴ Despite the discrepancy in the exact figures, it is quite clear that the Calcagnos *and* the city council both utilized the exemption method to quantify the loss caused by the regulation in question. Using the Calcagnos’ figures the calculation is as follows⁶⁵:

$$\begin{aligned} \$500,000 &= \$700,000 \text{ (approx. 60–70 units at } \$10,000/\text{unit)} \\ &\quad - \$200,000 \text{ (approx. 20 units at } \$10,000/\text{unit)} \end{aligned}$$

$$\text{Public payment} = \text{Value of Land with an exemption from the regulation} - \text{Value of Land with the regulation}$$

As with the majority of successful claims thus far, the city council decided to invoke subsection 197.352(8) of the Oregon Revised Statutes and, “in lieu of payment of just compensation,” waive the offending regulation (i.e., rezoning to a less intensive use) in favor of the Calcagnos.⁶⁶

63. MARTIN & SHRIVER, *supra* note 61, at 22. The claimants assessed the value of the land with only twenty units on at \$200,000 (20 x \$10,000). The staff at the city council assessed the current value significantly higher. *Id.*

64. Calcagno Staff Report, *supra* note 62, at 8.

65. The calculation uses the approximate figures asserted by the Calcagnos as per the Staff Report. Calcagno Staff Report, *supra* note 62, at 8. The calculation assumes, as presumably the Staff report did, that both the value with the regulation, and the value without the regulation, reflects the “highest and best use” of the property. If the regulation in question did not restrict the “highest and best” use (say, as farm land, the property would be valued at \$1 million), then the owner would not have suffered any loss from the regulation, as the value would be unaffected. Alternatively, if the regulation caused a change in the highest and best use (say, as farm land, the property would be valued at \$400,000) the loss would be less than that claimed (\$300,000 = \$700,000 – \$400,000). It also assumes a constant price-per-unit, which is a questionable assumption as one would expect the price to increase as the quantity is reduced.

66. The offending regulation was the R1 (Residential 1000) zoning regulations, and the waiver enabled the Calcagnos to use the property as under the RH (High Density Residential) zoning regulations, which were in effect at the time of acquisition. However the “d” overlay (Design Overlay Zone) is to remain in force as it did not restrict the use of the subject property. Calcagno Staff Report, *supra* note 62, at 7.

B. Criticisms of the Exemption Method

1. AN ARBITRARY VALUATION METHOD

Land use regulations operate to demark regulated land from unregulated land.⁶⁷ The effect of land use regulations on land values, therefore, affects two variables: the value of the regulated land and the value of the unregulated land. The effects of the regulation may have *differing* consequences on the value of unregulated and regulated land. As Jaeger explains:

[I]n both of these land markets, price adjustments will occur as a result of the regulation . . . [and] these changes will give rise to market adjustments and a price differential, or price wedge, between the two land markets—one that will equal the negative price adjustment (if any) in one market plus the positive change in the other market.⁶⁸

The exemption method is not an accurate method of quantifying loss caused by land use regulations simply because, while purporting to capture *only* the loss to regulated land, in truth, it captures the price wedge between these two variables. In his paper Jaeger draws an analogy with a boat tied to a costal pier, and suggests that, “[if] we notice, after a period of hours, that the level of the boat is now below the level of the pier, we are unlikely to ask: did the pier move up or did the boat move down?”⁶⁹

In such a scenario we intuitively appreciate that we are dealing with one constant, the pier, and one variable, the boat. Therefore to measure variance of one variable—or the extent to which the boat has fallen—one merely has to measure the current difference (in length/distance) between the two. However, such intuition cannot be applied to the loss caused by land use regulations. As we have two variables, *both potentially affected by the relevant regulation*, we must question whether the price differential is due to an increase in value of one of the land markets, a decrease in value of the other land markets, or a combination of both.⁷⁰ To determine the “reduction in the fair market value” of the affected property it is essential to be able to separate the “effect . . . [of the regulation] on prices of the regulated lands from the effect on prices for unregulated lands.”⁷¹

67. Of course land regulations do not operate in a vacuum and the “unregulated” land is likely to be regulated in the sense that it is covered by some regulations. The point is the unregulated land it is not regulated by the regulation in question.

68. William K. Jaeger, *The Effects of Land Use Regulations on Property Values*, 36 ENVTL. L. 105, 109 (2006).

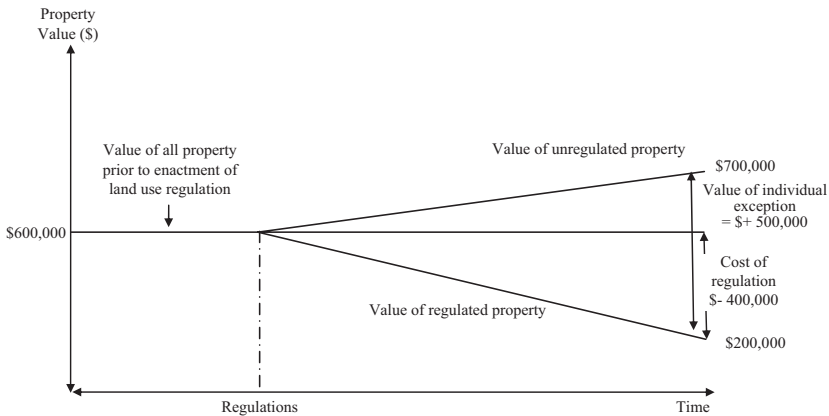
69. *Id.*

70. The effects of a regulation, of course, are only one of a number of components which make up the land’s value. In the following analysis, to highlight the effect of land use regulations, it is assumed that the regulation in question is acting in a vacuum and that the increase or decrease in land value is entirely derivative of the regulation.

71. Jaeger, *supra* note 68, at 12.

If we return to the Calcagnos case, it is patent that the employed method of valuation did not attempt to distinguish between the loss in value of regulated property (the Calcagnos property with the regulation) and any increase in price of unregulated land (the Calcagnos property with the exemption from the regulation) caused by the regulation. It is asserted that the Calcagnos property *unregulated* is worth \$700,000, and that *regulated* it is worth \$200,000. However, we do not know—and *cannot know* from using the exemption method—whether the price differential has been caused by an increase in the value of unregulated property, a decrease in value of regulated property, or a combination of both. The regulation in question might have caused a significant decrease in the value of the regulated land, and only marginally increased the value of the unregulated land.⁷² Such a scenario is demonstrated in the following diagram:

Diagram 1



NB 1: Graph not drawn to scale

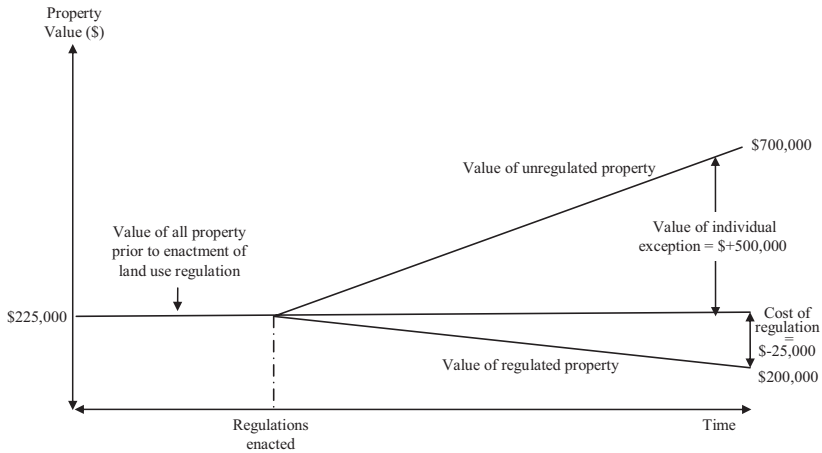
NB 2: Graph only takes into account the effects of the land use regulation on property values, and not other variables (inc. inflation)

However, it is equally possible that the effect of the regulation was to increase the value of unregulated land dramatically, while having little or no effect on the value of the regulated land.⁷³

72. Suppose the value prior to the regulation was \$600,000. The increase in value of the unregulated land would account for \$100,000, and the Calcagnos' land would have decreased in value by \$400,000.

73. Suppose the value of the property prior to the regulation was \$225,000. The increase in value of the unregulated land would account for \$475,000, and the Calcagnos' land would only be decreased in value by \$25,000.

Diagram 2



NB 1: Graph not drawn to scale

NB 2: Graph only takes into account the effects of the land use regulation on property values, and not other variables (inc. inflation)

In both scenarios the figures (\$700,000 – \$200,000) employed by the exemption method would remain the same, and thus the assessment of the loss would remain at \$500,000.

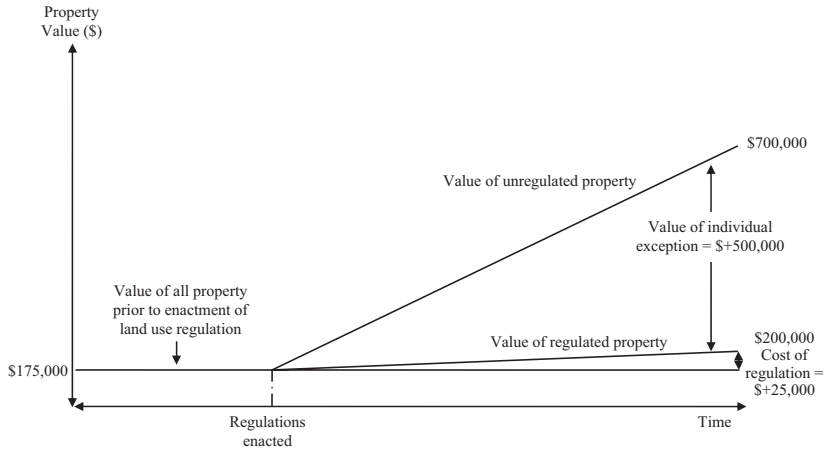
There is also a third possibility: that the regulation in question causes an increase in value to both the regulated *and* unregulated properties. This could potentially occur when the value of the neighborhood or amenity effects (e.g., extended tree cover, proximity to lakes, and the like), which was preserved or increased by the regulation, outweighs any loss incurred by the regulated property (e.g., the prevention of highest and best use).⁷⁴ In such a case, the unregulated property is also likely to benefit from the regulation (the increase being due to both amenity effects and the increased scarcity of land).⁷⁵ Let us assume in the Calcagnos case that the price prior to the enactment of the regulation was \$175,000. In this case both the regulated property (at \$200,000) and the unregulated property (at \$700,000) have increased in value due to the “enactment and enforcement” of the land use regulation. One would therefore expect that an accurate calculation of the “reduction in the fair market value of the

74. See, e.g., Noelwah Netusil, *The Effect of Environmental Zoning and Amenities on Property Values: Portland, Oregon*, 81 LAND ECON. 227 (2003).

75. See Jaeger, *supra* note 68. Indeed, land use regulations have positive economic effects on land values through the use of amenity and scarcity effects. The difficulty with the exemption method is that it allows a claimant to point to the negative impacts of the regulation as if she were the only one affected, but not to look at the value-enhancing effects of the regulations as a whole.

affected property” to be zero. However employing the exemption method in such a scenario would still result in the loss to the regulated land being quantified at \$500,000, as the following diagram illustrates:

Diagram 3



NB 1: Graph not drawn to scale

NB 2: Graph only takes into account the effects of the land use regulation on property values, and not other variables (inc. inflation)

Under the exception method, the analysis shows a “loss” despite the fact that the appreciation in the value of the regulated land is entirely due to the land use regulation which is challenged.⁷⁶ It must be concluded that assessing the difference between the current fair market value of the unregulated property (that is, the value of the property in question *without* the regulation applied) and the current fair market value of the regulated property (the value of the property in question *with* the regulation applied) has absolutely no connection with the effect of a land use regulation on a property’s fair market value.

2. PROPENSITY FOR HYPER-INFLATED VALUATION

The exemption method is not only entirely arbitrary in its assessment of loss; in the majority of cases its employment will tend to inflate the claim above any true loss.⁷⁷ The hyper-inflated claim is produced by the

76. These examples assume, for the purposes of highlighting the fallacies inherent in the exemption method, that the land use regulation is the only component which affects the value of land.

77. This is consistent with the findings of Hascic and Wu: in the vast majority of cases the Value of an Exemption (VIE) was greater than the Cost of Regulation (CR). Hascic & Wu, *Essays on Land Use Regulation*, ch. 3, *The Reduction in Value Due to*

exemption method, because it allows individuals to claim that if they, and they *alone*, were granted an exemption to the land use regulation they could sell their property for the fair market value of unregulated property. However, in doing so, the landowner is often (perhaps unconsciously) attempting to “have their cake and eat it too”: claiming a particular land use regulation resulted in a *loss* in the *regulated* land’s value by reference to the *increase* in value of *unregulated* land *which that very regulation brought about*. This is because increasing the scarcity of a particular land use (by prohibiting, or limiting, the particular land use in the regulated zone) often drives up the value of land where the particular land use is still permitted (or unlimited).⁷⁸ The effects of the land use regulation will shift or constrain the supply of land in a way that affects both . . . [regulated and unregulated] land markets. As this occurs, the market price for land put to use A may differ from the market price for land put to use B. For a land use regulation that limits the amount of land that can be put to use B, or one that requires that certain lands be put to use A, the effect of this land use regulation will be to increase the price of B land and decrease the price of A land.⁷⁹

In essence, the “exemption” method puts the claimant in a monopolistic position, at least with reference to the other regulated landowners. It allows her to reap the benefits, in common with other landowners in the vicinity, of any amenity value which has been preserved or even enhanced by the land use regulation. But the successful Measure 37 claimant is also able to benefit from the fact that the regulation in question will have increased the scarcity (and hence the value) of land where the land use prohibited by the regulation is permitted. In both cases the relevant increase in value *may not have occurred if the land use regulation had not been “enacted or enforced.”*

Returning to the Calcagnos case for illustration of the monopolistic effect, let us assume all comparable land in this case was subject to the same R1 zoning regulations, which restricted the number of properties which could be developed on the property. Discounting variables such

Land Use Regulation vs. the Value of Individual Exemptions: An Exploratory Analysis of Oregon’s Measure 37, 57-121 (June 21, 2006) (unpublished Ph.D. dissertation, Oregon State University) (on file with author).

78. Assuming a constant level of demand, the decrease in supply of land where such a land use is permitted (or unregulated land), will generally result in an increase in value. Jaeger notes that this may not be the case in all scenarios. See Jaeger, *supra* note 68.

79. Jaeger, *supra* note 68, at 110. He notes however that such a phenomenon does not occur in all scenarios; for instance, an increase in supply of farm or forest lands may not cause their prices to decline, because their price depends primarily “on their productivity, and on the value of what they produce in the marketplace.” *Id.* at 127–29.

as view, proximity to amenities, and assuming the highest and best value of each plot of land was residential property; the value of each plot (and plots in the surrounding area) would be directly connected to the number of units which could be developed on the property.⁸⁰ The restriction of the number of properties that can be developed per acre in the area by the “enactment and enforcement” of the residential zoning classification will drive up the price per unit. Thus, by granting to the Calcagnos an exemption from R1—so that they are able to develop more properties per unit than their comparables/neighbors—the exemption will result in an increase in the value of their land. Yet the high value of the units “per unit” is due only to the restriction in number of units in the area *brought about by the regulation*. If the exemption were applied to all property owners in the vicinity, or had the regulation never been enacted, the increased competition would have driven down the value per unit. Moreover, the land use regulation, by restricting the maximum number, density, and height of the units, is likely to have maintained or increased the amenity value—such as the unrestricted view, the prevention of the levels of traffic which would have resulted from higher density, and the like—from which the Calcagnos’ land, and consequently its value, would have benefited.

Exposing the failings of the exemption method is not a purely negative exercise: it will be used to inform the analysis of alternative valuation methodologies. The fallacy of the exemption method, at least in conceptual terms, is that it targets the wrong differential. As seen, it attempts to capture the price wedge between the current value of properties not regulated by the land use regulation and the current value of those properties that were regulated. This differential lacks any correlation with the “loss” suffered by the owner of the regulated land.

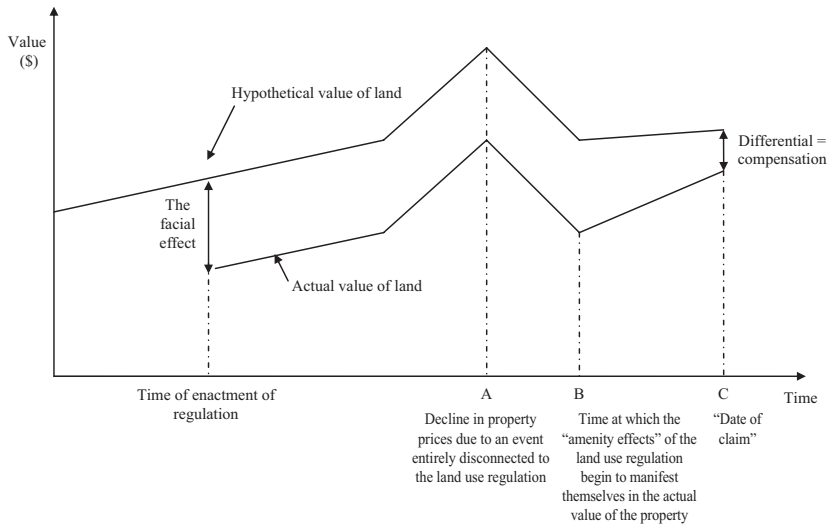
In contrast, the differential at which any valuation method should be targeted to establish the true cost of the regulation is “the difference between the current value of the property and the value of the property that would have existed if the regulation had not been imposed in the first place.”⁸¹ This differential is illustrated in the following diagram⁸²:

80. Even if the extraneous variables were included, the land use regulation restricting the density of urbanization would have a significant impact on the value of the affected land.

81. Hascic & Wu, *supra* note 77, at 3.

82. The only factors which should affect the differential between the hypothetical value and the actual value, and hence the compensation payable, are those factors which are caused by the land use regulation. In this much-simplified example the effects of the regulation are manifested at two points, the time of enactment—when the facial devaluation occurs, and at point B, when the amenity effects flowing from the *enforcement* of

Diagram 4



This differential, which all of the following valuation methods arguably attempt to target, is easy to state in conceptual terms. However, due to the acute difficulty in establishing the hypothetical value (the value of the property had the regulation never been imposed, which is also referred to as the “counterfactual”), it is undoubtedly less easy to apply in practice.⁸³ Jaeger summarizes the difficulties:

The influence of land use regulations on the markets for alternative land uses will generally occur gradually over time. As a land use regulation becomes binding, it will begin to influence land prices and land uses, and it may also influence other private and public land use decisions, other public and private investments, other government policies such as taxation, and decisions about infrastructure. These changes will, in turn, cause feedback effects on land markets, land use decisions, and even on demographic changes and economic growth. Over a period of years, this complex, interdependent pattern of changes that may occur *with* a land use regulation will make it very difficult—if not impossible—to ascertain what would have happened *without* the land use regulation.

The remaining analysis in this section focuses primarily on the ability of the respective valuation methodologies to establish the hypothetical value—the value without the land use regulation—and thereby accurately quantify the loss suffered by the applicant landowner.

the land use regulation begin to have an effect on the actual property’s value. Note that at point A, events wholly extraneous to the land use regulation do not have an effect on the differential.

83. For an economist’s perspective of the difficulty in establishing the hypothetical, see generally Hascic & Wu, *supra* note 77; see also Jaeger, *supra* note 68, at 27.

C. *Hascic and Wu—The Economic Simulation Model
and the Elusive Counterfactual*

Perhaps an ideal methodology for measuring “loss” under Measure 37 is that which is the most difficult to undertake. Ivan Hascic and Junjie Wu developed a model that appears to meet the words of Measure 37, but which is controversial and difficult to apply. The method was developed as part of Hascic’s doctoral dissertation work in collaboration with Professor Wu, one of his supervisors, as part of a series of essays on the economic impacts of land use regulations on land values.⁸⁴ The authors developed what they termed an “empirical method” to measure such effects, using a portion of the Eugene-Springfield Metropolitan Area of Lane County at the southern end of the Willamette Valley, as well as certain adjacent rural lands, as their study area.⁸⁵

Hascic and Wu concluded that the exemption method of valuation is flawed because it considers the application, or not, of the regulation only to the property of the claimant, as opposed to the presence or absence of the regulation itself.⁸⁶ Because the presence or absence of the regulation affects many parcels, even those that it does not regulate,⁸⁷ and the effects of that presence or absence on land value are not clear, their methodology becomes somewhat complex.⁸⁸ While it is comparatively easy to ascertain

84. See Hascic & Wu, *supra* note 77.

85. The boundaries and use of this study area is not justified in the text; however, the authors noted that there was an abundance of knowledge of both land use regulations and land prices for this area, where the local governments have had the authority to impose land use regulations since 1948. Hascic & Wu, *supra* note 77, at 99 n.22.

86. *Id.* at 60.

87. *Id.* at 61. Professor Jaeger used the fact that a regulation affected many properties to distinguish the use of the “single exemption” method from the “with and without” approaches to valuation. He argues that if 20,000 single-family residential properties were condemned in a city, the fact that the market for those properties would skyrocket would not entitle each individual property owner of the condemned sites to the higher value of the property after the condemnation action began. Jaeger concludes:

Estimating “reductions in value” when one property is involved is fundamentally different from situations where many properties are involved. It follows that because land use regulations affect many properties, we cannot rely on standard appraisal methods to estimate reductions in value.

Letter from William K. Jaeger, Associate Professor, Oregon State University, to Larry George, Oregon State Senator (Mar. 2, 2007) (on file with author).

88. In fact, Hascic & Wu claim:

We show that the increase in value of a parcel when it is solely exempted from a regulation does not equal the reduction in value due to the regulation to the owner. The reduction in value due to the regulation equals the difference between the current value of the property and the value of the property that would have existed if the regulation had not been imposed in the first place. A landowner may benefit from a waiver because the regulation has been applied to other properties. Since the price of a parcel depends on the land use in its surrounding parcels, which in turn depends on

the value of a parcel *with* a certain land use regulation, it is less easy to deal with the hypothetical or counterfactual case, i.e., the value of a parcel as if the regulation had never been adopted.⁸⁹ However, that is Hascic and Wu's analytical project, perhaps oversimplified in the description that follows.

Following an inventory of those urban and rural lands in the study area,⁹⁰ Hascic and Wu move to their two-part model. The first part measures the economic impacts of the various existing land use regulations on land values in the study area.⁹¹ The second part presents a simulation model that predicts land use choice and value for each property under alternative regulatory scenarios.⁹² This model is used to predict land values as if some or all of the currently applicable land use regulations are removed.⁹³ In addition to this speculation, the model also purports to accommodate further variables, i.e., the spatial and temporal variation

their surrounding land use, it is necessary to predict the land use patterns and prices that would have existed on the whole landscape in the absence of regulation.

Hascic & Wu, *supra* note 77, at 60.

89. *Id.* at 94.

90. Hascic & Wu find eight zoning categories (described below) apply. *See supra* note 77, at 67 tbl.3.1.

91. In the urban areas, those classifications include urban low-, medium-, and high-density residential, and commercial and industrial categories. In rural areas, those classifications include rural residential, agricultural, and forestry categories. The economic impacts are further broken down, *see id.* at 71–72 tbl.3.2, to deal with additional variables, such as size, location, and proximity to highways. Hascic & Wu, *supra* note 77, at 70–75.

92. Hascic & Wu, *supra* note 77, at 68–69. The authors describe this part of their model as follows:

The land price equations serve as the foundation of the empirical framework. They are estimated by regressing parcel-level land prices on a vector of socioeconomic, location, and neighborhood characteristics. Spatial interdependencies between parcels are assumed to take two forms in these land price equations. First, each land price equation is specified as a function of variables summarizing the spatial information. These variables include location characteristics such as the distance of the parcel to certain natural or man-made features (e.g., the city center and highway) and neighborhood characteristics such as the proportion of land in different uses in the neighborhood. Second, the land price equations are specific as spatial autoregression models (Anselin 2002) to explicitly deal with the spatial dependency between unobserved variables affecting various land uses. Formally, each land price equation is specified as

$$\gamma = X\beta + \mu \quad \text{and} \quad \mu = \lambda W\mu + \varepsilon$$

where λ is a vector of the observed land prices, X is a matrix of observations of explanatory variables, β is the parameter vector, and μ is a vector of the autoregressive error terms. Parameter λ represents the spatial autoregression coefficient which is estimated simultaneously with λ , W is the $n \times n$ spatial weights matrix, and ε is a vector of error terms that are independently normally distributed with a mean of zero. Spatial autocorrelation may arise in the land price equations as a consequence of omitted variables. It is quite likely that parcels located near each other are affected by the same omitted variables, leading to spatial autocorrelation. . . . The spatial error specification has been widely used in previous hedonic studies of land values.

Id. at 69.

93. Hascic & Wu, *supra* note 77, at 75–78.

of land use patterns that were influenced by the removal of some or all of these land use regulations.⁹⁴

In their simulation model, Hascic and Wu considered two baselines: one is as if there were no land use regulation over the period under consideration, while the other is an “all-but-the-selected-regulation” baseline in which the land price is considered under all land use regulations but the one evaluated.⁹⁵ The authors concluded that owners of properties zoned for natural resource use (i.e., farm and forest designations) lost value, as opposed to a no-regulation scenario, although other properties gained in value by these restrictions.⁹⁶ The “all-but-the-selected-regulation” scenario demonstrated a similar, but less profound impact on land values, because it emphasized a lifting of a single restriction, while remaining regulations that reinforced the excluded regulation remained in place.⁹⁷

The choice of the “all-but-the-selected-regulation” method over the exemption method results is a significant change in the calculation of “loss,” particularly with respect to lands in natural resource zoning classifications.⁹⁸ The authors conclude:

These results suggest that landowners seeking exemption under Measure 37 would overstate the reduction in value due to regulation because an estimate obtained using

94. The model simulates land values every ten years, beginning in 1950, based on historical income and population data, as well as urban boundaries. The authors used the ten-year periods “because of data and computational constraints.” Hascic & Wu, *supra* note 77, at 77. For example, income data is collected only on a ten-year basis by the United States Census Bureau. *Id.* at 99 n.18.

95. Hascic & Wu, *supra* note 77, at 77–78 tbls.3 & 4, 85–97 tbls. 3 & 5.

96. Hascic & Wu, *supra* note 77, at 84–88, 95. Similarly, the greater choice of land uses under the “no regulation” scenario tends to lower land values.

97. The authors note that zoning affects not only the value of the land zoned, but that of lands that are not subject to that restriction, concluding:

While the study’s limitations prevent any firm conclusions from being drawn, some tentative insights can be offered. In the absence of land use regulation individual landowners typically have little incentives to take into account the spatial externalities of their land use because benefits accrue to others in the neighborhood. This is where government intervention in land markets is warranted. Zoning ordinances and other forms of land use regulations aim to correct inefficient land use patterns by promoting provision of positive externalities and by limiting negative externalities of private decisions on others in the community. However, land use regulations are often blamed for causing reductions in property values. While zoning and various other land use regulations may indeed cause land prices to change, it is difficult to measure the direction and the magnitude of these changes because of difficulties in establishing a counterfactual.

Hascic & Wu, *supra* note 77, at 94–95.

98. Hascic & Wu estimate that use of the Exemption Method would result in a “loss” of \$104,855 per acre, compared with \$32,614 per acre under the “all-but-the-selected-regulation” methodology. Hascic & Wu, *supra* note 77, at 89–90 tbl.3.6. The authors suggest a similar result would occur through the use of forest land zoning and the use of the urban growth boundary.

the standard appraisal methods yields the value of an individual exemption rather than the reduction in value due to regulation. Given that some of the limiting factors in our analysis tend to overstate property values in the no-regulation scenario, it is not clear whether the change in value due to the regulation is positive. The estimates of reduction in value due to regulation are negative for unzoned land located outside the zoned district suggesting that the three resource protection zoning regulations increase the value of unzoned lands by \$1552 to \$156,116 per acre on average. Hence, while the resource protection policies may reduce the value of the regulated lands, these policies often increase the value of unregulated lands.⁹⁹

There are also those positive reinforcement roles of land use regulations in limiting spatial externalities of private unregulated land use activities, as well as providing benefits accruing from coordinating infrastructure installation and location of uses where they will have the greatest social effects (none of which are usually considered in the “loss” calculus under Measure 37). Hascic and Wu infer that a more sophisticated model would consider these calculations as well in determining any net “loss” of property value.¹⁰⁰ Such a model is both consistent with the wording of Measure 37 (as is suggested in the analysis below), but is also vastly more accurate than the prevalent exemption model most often used for calculations of loss in value throughout Oregon. The principle defect of the model is its impracticality of use,¹⁰¹ although it is also controversial in economic circles, as discussed immediately below.

D. *Criticism of the Hascic and Wu Method*

There are a number of criticisms from an economic standpoint that can be made of the Hascic and Wu method. The first and most potent economic criticism of their model is that their equation for establishing the hypothetical land value entirely ignores the effect of supply and demand relationships on the value of land. As we have seen, land use regulations can have a dramatic effect on land prices by increasing or decreasing

99. Hascic & Wu, *supra* note 77, at 89.

100. If the analysis were limited to an “all-but-the-selected-regulation” basis, the authors suggest the “loss” of value would be greatly reduced. However, the exemption method would place a premium beyond any actual reduction in value arising out of the use of natural resource zoning or the use of an urban growth boundary. Hascic & Wu, *supra* note 77, at 93.

101. William K. Jaeger, associate professor of agricultural and resource economics at Oregon State University, suggests the “with and without” selected regulation approach comes up with the correct result, but is “complex, costly[,] requires detailed economic model[ing] [and is] difficult to validate.” Jaeger and his academic colleague, Andrew Plantinga, proposed their own methodology, described herein, as a more easily administered process for evaluating claims, while acknowledging that it has only a 75% accuracy rate. See William K. Jaeger, *Three Methods for Evaluating Measure 37 Claims*, EM 8933-E OR. STATE UNIV. EXTENSION SERV. (2007), available at <http://extension.oregonstate.edu/catalog/pdf/em/em8933-e.pdf>.

the scarcity of the land use in question. Neglecting a variable which has such a great impact on land values and concentrating purely on the marginal effects on neighboring properties—in essence the amenity effects—must surely lead to the conclusion that the proposed model, in its application if not conception, is flawed.

Second, using the value generated by the simulation ($V_i^{\text{all zoning}}$) in order to establish one of the baseline figures,¹⁰² rather than merely assessing the value in actuality, may lead to inaccuracies in the valuation of loss. While the authors claim that the actual and simulated land use pattern generally correlate closely, the success of the model varies by land classification. Hascic and Wu attribute these inaccuracies, not to a deficiency in the model, but rather to “a result of noncompliance with zoning regulations.”¹⁰³ Assuming this to be the case, the simulated results still represent a counterfactual value: although the model predicts what the value of a property, with all regulations in force, *should* be, it does not assess what the value *is*. Nonconforming land uses do not cease to affect land values merely because they are unlawful. The one relatively certain variable is the current value of the property; however, in Hascic and Wu’s method this value is dispensed of, and replaced by yet another hypothetical.

Third, these economists appear to assume that each land use regulation, or segment thereof, is independent of the whole and that their effects can be calculated independently of each other, so that the omission of one would not have an effect on the whole. However, the non-implementation of one land use regulation would undoubtedly have an effect on the content of subsequent land use regulations. Moreover, the impact of non-implementation of a certain land use regulation would affect land markets in many intangible ways. As Jaeger recently noted:

[W]ould local government investments in roads, sewers, or other infrastructure have been [developed] different[ly] [had the land use regulation not been applied]? Would government services and property tax revenues differ significantly? If so, would other decisions have been different?¹⁰⁴

In the light of the telling economic criticisms of this model, we return to the pragmatic objections to this model—or for that matter any model of its kind, no matter how accurate its application may be. The complex economic equations involved in such a theory, coupled with the essentially unquantifiable nature of a large number of the

102. That is, the value of the property with all land use regulations in place.

103. Hascic & Wu, *supra* note 77, at 81. In essence, Hascic and Wu are asserting that if everybody complied fully with the land use regulations, then the actual acreage would be closer to the simulated results.

104. Jaeger, *supra* note 101, at 3.

variables necessarily included, ensures that to develop a model which is widely accepted as valid in economist circles (if at all possible) is likely to take a significant amount of time and money. To replicate such a model on a statewide basis and to utilize it in each and every Measure 37 claim would prove even more resource intensive. Thus, the prospect of using a complex economic model akin to that developed by Hascic and Wu to quantify Measure 37 claims, if at all possible, is certainly not achievable in the foreseeable future.

E. *Plantinga/Jaeger Method*

The eponymous valuation method was designed by Professors Plantinga and Jaeger as a corollary to their criticism of the exemption method.¹⁰⁵ In his paper, *Measuring Compensation Under Measure 37: An Economist's Perspective*, Plantinga explains what the term “fair market value” means.¹⁰⁶ He concurs with the definition found in the case law—that there must be some notion of a competitive market—but asks the question: “[W]hat does the price of property represent assuming it derives from a competitive market?” His answer, in short, is that:

Contemporary/Current price = Annual income ÷ Interest Rate (called “the Contemporary Price Formula”)¹⁰⁷

The Contemporary Price Formula enables the establishment of a fair market value for the property: both the current price, and, so long as the relevant annual income and interest rates are available, an accurate valuation of the property at any point in the past, the so-called Historical Fair Market Value (“Historical FMV”).

The Contemporary Price Formula, in turn, informs Plantinga and Jaeger’s valuation method for Measure 37 claims:

105. Although commonly referred to as the Plantinga/Jaeger method, there is no paper where Jaeger explicitly promotes this method of valuation.

106. Andrew J. Plantinga, *Measuring Compensation Under Measure 37: An Economist's Perspective* (Dec. 9, 2004) (unpublished manuscript, on file with Oregon State University), available at <http://arec.oregonstate.edu/faculty2/measure37.pdf>.

107. *Id.* Plantinga explains that a buyer should be indifferent between buying of land for \$y, and gaining an income stream of \$x; and giving up \$y—by investing it in the bank, and gaining an income of \$x. Moreover, in a competitive market the buyer would not buy the property at more than \$y because by investing his capital (>\$y) in the bank (and assuming the rate of interest remained the same) the buyer would generate an income of more than \$x. Conversely, a competitive market will push the price up to \$y, because by investing less than \$y in the bank, the buyer will generate an income of less than \$x. Plantinga adds the proviso that the formula would be more complicated if the income stream is expected to fluctuate. *Id.* at 4.

Public payment = Original Purchase Price (OPP) (“express[ing] prices in current dollars to account for inflation since the property was purchased”) – Price with Regulation (PWR)¹⁰⁸

Quantification of the Price with Regulation (PWR) is merely a question of executing the Contemporary Price Formula with regards to the *current* annual income and the current interest rate. Calculation of the Original Purchase Price (OPP) is also reasonably straightforward; it is the actual price that was paid in consideration for the property at the time of acquisition. The hypothetical value is achieved by inflating the OPP so it is equivalent to today’s dollar value, by reference to the Current Price Index (CPI).¹⁰⁹

The following is an example of a calculation using the Plantinga/Jaeger valuation method. Let us say that the landowner purchased the property in 1995 for \$1 million, that the annual income of the land *today* is \$45,000, and that the current interest rate is 5%.

Public payment = OPP (\$1 million in 1995 would have the price of \$1.34 million in current dollars¹¹⁰)
– PWR (\$45,000/0.05)

Public payment = OPP (\$1.34 million) – (PWR \$900,000)

Public payment = \$440,000

On its face the Plantinga/Jaeger method is a vast improvement on the exemption method. Indeed the rationale which appears to lie behind the methodology is correct: to determine loss caused by a land use regulation, the comparators must be (1) the value of the land in a world where the land use regulation has *never* been enacted or enforced, and (2) the value of the land with the regulation in force. The method also benefits both from its relatively straightforward calculation and, as in most cases the relevant values will be easily accessible, its utility and practicality.

Questions remain, however, about the accuracy of this method. In particular, there are questions regarding whether using the original purchase price, as expressed in current dollars, is an accurate means of reflecting the value of the land in a world where the regulation has never been enacted or enforced: the hypothetical value.

108. Plantinga, *supra* note 106, at 12. Plantinga suggests using the “inflation calculator” from the United States Dep’t of Labor, Bureau of Labor Statistics, Consumer Price Indexes, <http://www.bls.gov/cpi/home.htm> (last visited May 25, 2007).

109. In this instance, reference to the CPI is merely used to express the OPP in current dollars. For a different interpretation, see below.

110. This was calculated by using the inflation calculator, *supra* note 108, as suggested by Plantinga, and was correct at the time of writing.

The first concern is with regard to the assertion that the original purchase price reflects the “income stream that would have accrued to the land owner in the absence of the regulation.”¹¹¹ This assumes that the current owner will have paid a fair market price for the property. Of course, theoretically, and presuming a competitive market, the current owner *should* have paid a fair market price.¹¹² However, we know that people do not always act in the way economic norms would suggest, and this may well be the case when purchasing land. Often individual purchasers are not interested in calculating whether the investment is rational in economic terms—the purchaser may, for instance, derive an idiosyncratic value from the land which is indiscernible to economic analysis, and thus has no effect on the market value.¹¹³ Moreover, we well know the fallibility of human beings; when buying the property the purchaser may have simply made a mistake with his or her sums, or otherwise desire to acquire or alienate land other than on economic grounds. Whatever the reason, we know that the *actual* price paid will not always represent the fair market value at the time of purchase (the historical FMV), notwithstanding the fact that, at least in economic terms, the actual price paid (OPP) and the fair market value *should* be equal. Thus, by basing public payment on the *actual* price paid instead of the historical FMV, the Plantinga/Jaeger method has the potential to provide windfalls to those owners who paid “over the odds” for their property. Using the calculation above, the following example demonstrates how this happens.

Let us assume that the annual income in 1995 was \$47,000, and that the interest rate was 5%; employing the Contemporary Price Formula allows us to determine that the historical FMV in 1995 was \$940,000 (\$47,000/0.05). However, we know our buyer purchased the property for \$1 million; \$60,000 over the odds. If we are to quantify the *true* loss to the property/income caused *by the regulation*, we must use the historical FMV, rather than the OPP. In that case, the equation is as follows:

$$\begin{aligned} \text{Public payment} &= (\$940,000 \text{ in 1995 would have the price} \\ &\quad \text{of } \$1,255,000 \text{ in current dollars)} \\ &\quad - \text{PWR } (\$45,000/0.05) \end{aligned}$$

$$\text{Public payment} = \$1,255,000 - \$900,000$$

$$\text{Public payment} = \$355,000$$

111. Plantinga, *supra* note 106, at 12.

112. The economic logic behind this statement is explained in note 95, *supra*, and it forms the basis for Plantinga’s Contemporary/Current Price Formula.

113. Suppose, for instance, that the property brought back pleasant childhood memories.

Use of the fair market value at the time of purchase (historical FMV), rather than the actual price of purchase, reduces the public payment payable by \$85,000.¹¹⁴ This sum represents a windfall to the landowner; rather than merely compensating for the reduction in value of his property *caused by the land use regulation*, the utilization of the *actual* purchase price additionally “compensates” landowners for their irrational (in economic terms) overpayment at the time of purchase.

A potentially more serious challenge to the Plantinga/Jaeger method arises from the assumption, made in order to arrive at the hypothetical value, that the income stream from the property would have remained constant between the time of the original purchase and the date of the Measure 37 claim had the land use regulation not been enacted. While land markets are comparatively stable, this assumption undoubtedly detracts from the accuracy of their method.

To see why this is the case, it is important to revisit the lessons learned from the failings of the exemption method. It will be remembered that the exemption method was based on a fallacious rationale, and that, in light of the criticisms of its rationale, it was concluded that any accurate valuation method must at least purport to capture “the difference between the current value of the property and the [hypothetical] value of the property that would have existed if the regulation had not been imposed in the first place.”¹¹⁵

In order to capture this differential it is clearly vital to delineate those variations in land value which are attributable in some way to the land use regulation and those which are wholly extraneous. Unfortunately, there is an implicit assumption made by Plantinga and Jaeger that any variance in the actual income stream between the time of purchase and date of the claim is entirely due to the implementation of the land use regulation in question. While the value of the land may be reduced by any number of causes related *or* unrelated to the land use regulation, the value of the hypothetical land in the Plantinga/Jaeger method is impervious to any such variables. The method operates so as to insulate the hypothetical value from the vagaries of the property market, freezing the income stream at the date of purchase. In doing so, because the actual value of the property (and its income stream) is affected by the vagaries of the land market, so the “compensation”—the differential between the value of the hypothetical and value of the actual land—is affected by *all* causes since the property was purchased. Thus, the

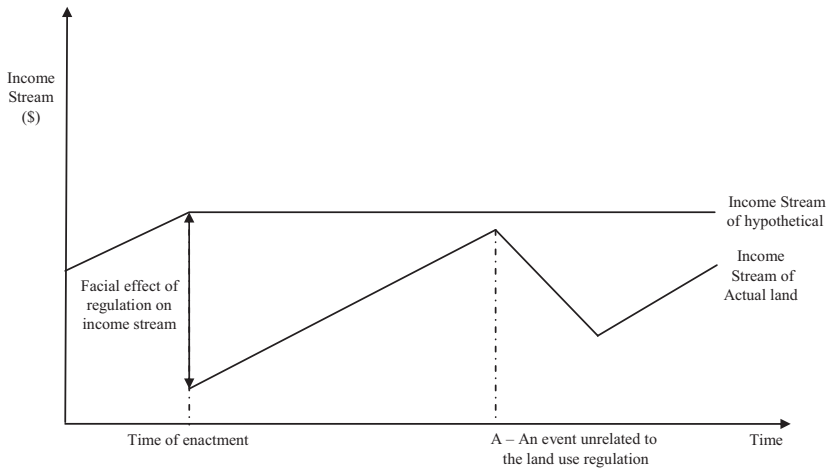
114. $\$440,000 - \$355,000 = \$85,000$.

115. Hascic & Wu, *supra* note 77, at 3.

failure to capture only those variations in land value which are attributable to the “enactment and enforcement” of the land use regulation is *potentially unfair to the public entity by making it responsible for actions not of its own doing*.¹¹⁶

The following diagram illustrates the over inclusive nature of the Plantinga/Jaeger method:

Diagram 5



To determine the true cost of the regulation, the income stream of the hypothetical should fluctuate simultaneously, and to the same degree, as the income stream in actuality in response to all variables (e.g. market for rent, natural disasters, etc.) *apart from* those caused by, directly or indirectly, the land use regulation in question. However, it is clear from the diagram above that this is not the case. While the initial decrease can be attributed to the facial effects of the enactment of the land use regulation, and thus it is right that the hypothetical income stream (in a world without that regulation) remains unaffected at this point, the income stream of the hypothetical *should* react to the occurrence at point A which is wholly extraneous to the enactment of the land use regulation.

The effect of assuming a constant income stream for the hypothetical is best demonstrated by way of example. We know from the examples given above that had a Measure 37 claimant purchased a parcel of land

116. *Id.*

for \$1 million in 1995, augmenting this value using the Consumer Price Index (CPI) (as the Plantinga/Jaeger formula requires) would provide us with a current hypothetical value of \$1,340,000.¹¹⁷ In the example above we suggested that the income stream at the date of the claim was \$45,000 per annum, with the current interest rate at 5%. This provided us with a price with regulation (PWR) of \$900,000, and a compensation package of \$440,000. However, let us assume instead that in the period intervening between the purchase of the property in 1995 and the date of the claim in 2006 an event wholly unrelated to the land use regulation¹¹⁸ occurred that dramatically reduced the property prices in Oregon. Let us also assume that this event causes the income stream at the date of the claim to lower by \$15,000 to \$30,000 per annum. In this case the PWR would be \$600,000 and the Measure 37 compensation package would stand at a massive \$740,000. This despite the fact that the additional loss is in no way connected with the land use regulation. It is surely impermissible that a measure designed to provide compensation for loss caused by the enactment or enforcement of land use regulations should ensure eligible claimants against all loss to their property since, regardless of the source of that loss.

Of course, it may well also have the opposite effect to that depicted in this scenario; that is, the Plantinga/Jaeger method is capable of obscuring losses caused by the implementation of the land use regulation by taking into account external events (which have no causal relationship with the land use regulation) that have a positive impact on the income stream of the land.

F. *An Alternative Interpretation of the Plantinga/Jaeger Method*

It may be countered that this is a misinterpretation of the Plantinga/Jaeger method, and that the use of the CPI as the multiplier is much more than merely a device to reflect the equivalent purchasing power of the OPP in today's dollars. It may be argued that the correct interpretation of their method would view the CPI as a multiplier, designed to plot the inflation and fluctuations in the price of the affected land in a world where the regulation was never enacted (the hypothetical). The multiplier, on such an interpretation, would operate so as to ensure that the hypothetical value of the land is affected by all the same variables/

117. Despite the reservations highlighted above, for reasons of consistency, the OPP and not the Historical FMA is utilized as the multiplicand.

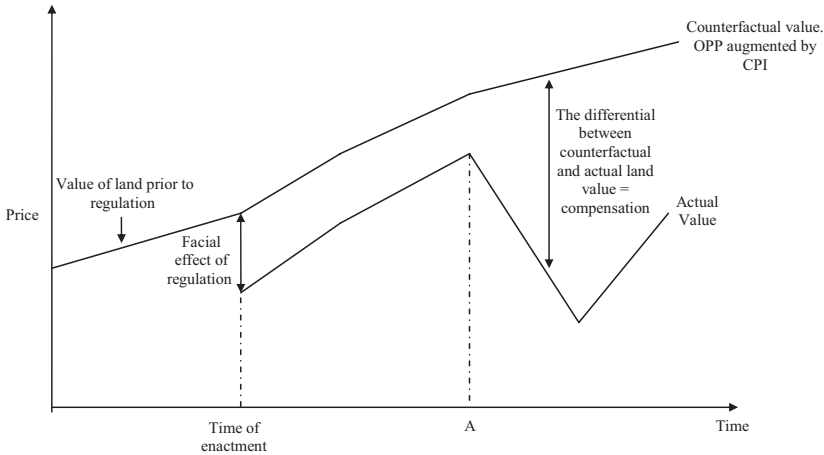
118. There are innumerable factors which affect land prices; however, for the sake of argument let us assume it was a natural disaster on the scale of the recent Hurricane Katrina tragedy.

components as the actual land value, *except* for those variables/components caused by, or resulting from, the “enactment or enforcement” of the specific land use regulation. While such an interpretation is contrary to the express intentions of the authors, analyzing the use of the CPI as a multiplier is useful in order to highlight the almost insurmountable difficulties one faces in establishing an accurate hypothetical value.

The difficulty in using the CPI as a multiplier is that it is necessary to make the assumption that, had the regulation *never* been “enacted or enforced,” the price of the property would have risen in direct correlation with the CPI. However this assumption is unlikely to be accurate. If the analysis takes place over an extended period on an institutional level,¹¹⁹ there is likely to be a rough correlation between the rise and fall of property prices and the rise and fall of the CPI. Yet the CPI is influenced by many different variables, only one of which is land price, and thus there is a potential divergence between the inflation rate set by the CPI and the inflation rate for land prices. This divergence is only exaggerated when analyzed on the individual level. It is possible that the rise in the CPI could bear absolutely no correlation to the fluctuation in the value of the affected land, or land in that particular area. For instance, what happens if the value of the affected land or the land in the particular area declined as a result of something entirely unconnected to the land use regulation, such as a natural disaster, years of bad harvest, or a drop in rental market? While the CPI may be affected by such happenings, it would *not* accurately reflect the loss in value that the affected land *actually suffered* (i.e., with the regulation), and importantly that the affected land *would have hypothetically suffered* in the hypothetical scenario (i.e., even if the regulation had never been enacted). The following diagram illustrates such a phenomenon¹²⁰:

119. That is, in relation to land prices as a whole.

120. The major problem with the Plantinga/Jaeger method is that the differential between the hypothetical and actual values (and hence the compensation) is affected by too many variables. In fairness, it should be noted that the “too many variables” problem is inherent in economic modeling. In the diagram, between the time of enactment and the time of A, the actual value rises at a faster rate than the hypothetical value; this presumes that there is an increase in price of the property *caused by* the “long term” effects of the regulation (amenity effects, etc.—there could quite easily have been a negative “long term effect”). The method is working correctly thus far, because it is taking into account only the effects that the land use regulation has on the differential. However, let us presume that at point A, a natural disaster (which is entirely disconnected to the land use regulation) occurs in the area, rapidly reducing the value of the affected land. While this would affect the actual value of the land greatly, the hypothetical value is, to an extent, insulated from the risk because it is augmented by the CPI, which is a national standard and likely only to be mildly affected by the disaster.

Diagram 6

The difficulties arise with the near impossibility of establishing a multiplier which will produce an accurate hypothetical value for the land. There is, for example, a flip side to the argument that the CPI is too far removed to accurately plot the fluctuation in property values in a particular area and/or of a particular variety. If a far closer comparator is used as the multiplier—let's say the increase in price of comparable land in the locality, expressed as a percentage and assessed from the time of regulation to the time of the claim—it will be difficult, if not impossible, to exclude from that comparator any effects which have been brought about, directly or indirectly, by the very land use regulation the hypothetical value is designed to eliminate.

G. Sercombe's Proposed Valuation Methodology

Following a request by Robert E. Stacey, Jr., the Executive Director of 1,000 Friends of Oregon, a prominent attorney, Timothy Sercombe, provided a detailed legal opinion on the meaning of "just compensation" under subsection 197.352(2) of the Oregon Revised Statutes. His valuation method differs from those considered above due to the fact his opinion is

The increase in the differential after A, and hence the increase in compensation for the Measure 37 claimant, is wholly unjustifiable: the land would have suffered from a radical drop in price after point A, whether or not the land use regulation was enacted. The reverse of this situation could also occur: if the CPI is positively affected by something wholly extraneous to the land use regulation in question (say the discovery a virtually finite source of oil in the United States, or the "dot-com boom"), the differential and hence the compensation payable to Measure 37 claimants would be unjustifiably increased.

a strict legal analysis; nevertheless, it is important to analyze Sercombe's valuation from an economic, as well as legal, perspective. The analysis is thoughtful and well-written and is the only comprehensive legal analysis of value. If it has flaws, it is because it attempts to reconcile the silence, the vagueness, and the contradictory provisions of the Measure itself.

Sercombe concludes that a court, following the statutory interpretation methodology set out in *Portland General Electric Co. v. Bureau of Labor & Industries*,¹²¹ and relying on the textual, contextual, and legislative history of Measure 37, should determine that "just compensation" under section 197.352 is equal to the "actual reduction in the fair market value of the property or comparable land before and after the enactment of the regulation. This value would be augmented or inflated to provide a rate of return on investment to the date of the claim [hereinafter known as 'interest']."¹²²

It is important to note that the reduction he refers to is the devaluation caused by the textual or facial effect of the land use regulation: in other words, the devaluation in the property value caused *immediately* by the enactment of the land use regulation, and *not* by any long-term, unpredictable, or indirect consequences that the regulation may have.¹²³ Fundamental to this methodology is the fact that both values are to be assessed *at the time of the enactment of the regulation*, and the differential then augmented by the interest that the owner would have received on the differential to the date of the claim.¹²⁴

Although Sercombe does not explicitly refer to a formula for calculating loss, the following formula can be inferred from the hypothetical scenario he provides in his memorandum.¹²⁵

$$\text{Public Payment} = \text{Lost Value} (1 + \text{Interest Rate})^n$$

121. 859 P2.d 1143 (Or. 1993).

122. Memorandum from Timothy J. Sercombe to Robert E. Stacy, Jr., Executive Director, 1000 Friends of Oregon, Meaning of "Just Compensation" under OR. REV. STAT. § 197.352(2) and Modification of Land Use Regulation under OR. REV. STAT. § 197.352(8) (June 15, 2006) (emphasis added) (on file with author).

123. If the highest and best value of a plot of land is as residential property, and a land use regulation rezones the land as farmland, the "facial devaluation" will equal the difference between the fair market value of the land as residential property and the fair market value of the land as farm land on the day the legislation took effect.

124. The rate of return can be seen to represent the interest on the compensation that the owner would have received up to the date of the claim had the compensation been paid to the owner at the date of the enactment of the regulation.

125. Sercombe, *supra* note 122, at 16 n.8. The literal interpretation of Sercombe's hypothetical scenario actually results in the formula Public Payment = Lost Value + Lost Value (1 + Rate of Return)ⁿ. However this formula does not appear to be

Suppose, as in the Calcagno case, a land use regulation was enacted which reduced the residential density allowance from medium to low density. Let us assume, as Sercombe does in his example, that the regulation was enacted in 1980 and its facial effect was to reduce the value of the land from \$40,000 to \$20,000.

$$\text{Public Payment} = (\$40,000 - \$20,000) \times (1 + \text{Interest Rate})^n$$

If we assume, again as Sercombe does, that the interest on the lost value was 5% (0.05), and that n equals 26 (twenty-six years between the date of enactment and the present day, i.e., 2006), the calculation is as follows:

$$\text{Public Payment} = \$20,000(1 + 0.05)^{26}$$

$$\text{Public Payment} = \$71,113 \text{ (to the nearest dollar)}$$

The essential flaw in Sercombe's method, at least from an economic viewpoint, is that it treats the effects of land use regulations as an extraordinary one-off event, when they are anything but. Indeed, even he recognizes that the continued enforcement of the regulation may cause a further "reduction in value, as distinct from, or perhaps in addition to, the value reduction by the facial effect of the law."¹²⁶

It takes time, often a great deal of time, for the effects of an individual land use regulation to become observable. Professor Jaeger notes that:

[i]n many cases when a land use regulation is enacted it does not have an immediate effect on land prices. In the case of environmental zoning it takes time for neighborhood effects to appear (or if they already exist, for them to be better protected from degradation than other neighborhoods). When urban growth boundaries are established they tend not to be binding on the land use decisions being made at that time, so they do not typically constrain the existing demands for the different land uses.¹²⁷

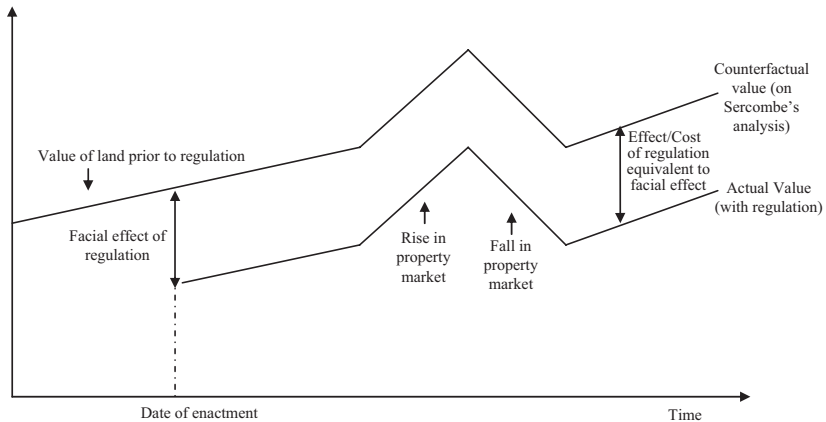
faithful to his stated methodology as it "double counts" the facial effect of the land use regulation. Augmenting the "facial devaluation" by use of the "rate of return" multiplier is ostensibly justifiable on Sercombe's interpretation of the statute, as it ensures that the landowner is compensated for the loss of return from the time of enactment to the "date of written demand." This is represented by the "Lost Value (1 + Rate of Return)ⁿ" part of the equation. However Sercombe, in his hypothetical scenario, adds to that equation the "Lost Value." With the greatest respect this makes no economic sense: the land owner has already been fully compensated, at least consistent with Sercombe's interpretation of subsection 197.352(2) of the Oregon Revised Statutes, for both the "facial devaluation" he suffered from the enactment of the land use regulation, and the loss of return he has suffered since the enactment. To then grant her an additional amount equivalent to the original facial loss, is to provide a windfall to the landowner. It is suggested that Sercombe may have simply made an error in his calculations and that the formula utilized is more consistent with Sercombe's overall analysis of Measure 37.

126. Sercombe, *supra* note 122, at 12.

127. Jaeger, *supra* note 68, at 9.

The continued enforcement of land use regulations can have both a positive impact and negative impact on property prices. For instance, the beneficial externalities of a land use restriction which both preserves trees, and encourages tree growth, may not be instantly observable. Indeed, tree canopy within a quarter mile of a property is estimated to represent between 2.77% and 7.41% of the mean sale price for properties within the city of Portland, Multnomah County.¹²⁸ Conversely, it is far from inconceivable that a regulation could have a more onerous effect on property prices than reflected in the facial devaluation. Jaeger gives the example of “a municipality zon[ing] more land for commercial or industrial use than the demand would support, [where the eventual impact would be that] the prices for these lands would decline.”¹²⁹ The Sercombe methodology, in effect, freezes the loss at the point of enactment, and in doing so fails to take into consideration such longer term effects of the regulation. The following diagram illustrates how on Sercombe’s analysis the differential, and thus the compensation, is frozen at the facial effect of the regulation.¹³⁰

Diagram 7



128. Netusil, *supra* note 74.

129. Jaeger, *supra* note 68, at 16.

130. Sercombe’s method assumes that the only effect that the land use regulation will have on the value of the affected land is a facial effect. Therefore the differential between the “Counterfactual” and the actual value of the land (with the regulation in force) is frozen at that point. It fails to take into account the ongoing effects that the land use regulation will have on property values (e.g., particularly through amenity or “neighborhood” values). Sercombe, *supra* note 122.

The rate of return multiplier Sercombe uses in his formula does not affect this analysis. As further developed in the body of this article, the rate of return multiplier merely compensates the owner for the loss of revenue potential to the extent of the facial devaluation (e.g., if the facial devaluation were \$50, the rate of return multiplier would provide a return, say equivalent to the interest rate, on that amount) but it does not affect the differential between the counterfactual and actual values of the land itself. *Id.*

Some contend that the market will have anticipated *ex ante* the long-term effects of the regulation, and that this will be reflected in the facial reduction in price. If the land market could foresee that the regulation will have a positive effect in the long run, then the valuation after enactment will be higher than it otherwise would have been. However, while theoretically true, the ability of the land market to predict *accurately* by what sign (positive or negative), and to what extent an individual land use regulation will have an effect on property value is highly questionable.

V. Legal Analysis

The final section of the article analyzes the proposed valuation methodologies from a legal perspective; examining the aforementioned methodologies in order to determine which best fits the text, context, and legislative history of section 197.352 of the Oregon Revised Statutes.

It is possible to classify in a broad manner the valuation methodologies encountered in the previous section into three different conceptual categories¹³¹:

1. Just compensation is equal to the difference between the current fair market value, and the fair market value of the affected property if it is, alone, granted exemption from the land use regulation (e.g., “Exemption method”).
2. Just compensation is equal to the devaluation in the fair market value of the property at the time of enactment (or at the time it first bites on the property’s value) with this devaluation augmented to reflect the additional revenue which the differential (“taking”) would have generated up to the date of the written demand (e.g., Sercombe’s method).
3. Just compensation is equal to the differential, at the date of demand, between the fair market value, and the (hypothetical) fair market value of the property had the regulation never been enacted or enforced. (e.g., the Plantinga/ Jaeger method or the Hascic and Wu method).

Despite the difficulties faced in estimating the differential in practice, it is quite clear that the third conception clearly represents the best interpretation of section 197.352. The major difficulty of this doctrinally pure method is plotting the counterfactual scenario as to the value of a particular property if a regulation now in effect had never been adopted

131. This is a reference to the compensation the method attempts to capture, rather than the method’s accuracy in application.

or enforced. We have thus far considered the competing methods to determine which model is most accurate in establishing the counterfactual and, thus, best at assessing the devaluation caused by the enactment or enforcement of the land use regulation. Let us now review the competing methods to determine that which best fits the legal framework established by Measure 37.

A. *Conceptual Category One: The Exemption Method*

Those who defend the exemption method as the basis for evaluating Measure 37 claims have, in essence, resorted to two central arguments: first, that the proposed alternative valuation methods are “even more flawed [than the exemption method]”¹³² and second, that the “clear”¹³³ language of subsection (2) dictates the use of the exemption method regardless of its economic inaccuracies.

Both of these propositions are themselves inaccurate. As we have seen, while the alternative valuation methods have their own flaws, none are as inaccurate as the exemption method¹³⁴: a method, lest we forget, which is wholly unable to establish whether a particular land use regulation has had a negative effect, no effect, or indeed a positive effect on the affected land’s value. Nor is the language of subsection (2) clear: the *prima facie* plausibility of Sercombe’s interpretation demonstrates that the language is inherently ambiguous. Furthermore, controversial interpretative questions—such as whether the causative event in question is the enactment or enforcement of the land use regulation or, alternatively, whether both should be taken into account—abound.¹³⁵ However, the one proposition about which we can be relatively clear is that the exemption method has

132. See Letter from David Hunnicutt, Executive Director, Oregonians in Action, to the Joint Land Use Fairness Comm. (Mar. 2, 2007) (on file with author).

133. *Id.*

134. See Jaeger, *supra* note 101.

135. The assumption that the exemption method is valid is evident in the only case that has addressed the question of valuation. In *Vanderzanden v. Land Conservation & Development Commission*, Case No. 05C19565 (Marion County, Or. Cir. Ct. Jan. 8, 2007) (letter opinion) Circuit Judge Don Dickey stated that: “By virtue of the plain language of [subsection] 197.352(1) [of the Oregon Revised Statutes], public entities are required to consider whether the value of the property without the applicable regulation would be different from the value of the property with the regulation.” That may well be the “plain language” of the section; however, the judge assumed that the only method to determine this difference was to consider the magnitude of the increase in value should the applicable regulation be waived: “Necessarily, then, the public entity must consider what value the property might have if the requisite waiver were granted.” *Id.*

With due respect to the judge it is submitted that his conclusion as to the correct valuation method is far from necessitated by his premise. Indeed, this article goes to great lengths to explicate the various valuation methodologies which may plausibly lay claim to capture the differential the judge identifies as his premise.

absolutely no legal basis: it is both explicitly and implicitly contradicted by the text, and also runs contrary to the intentions of the voters, as demonstrated by reference to the legislative history.

The definition of just compensation in subsection 197.352(2) explicitly refers to the need for a “*reduction* in the fair market value of the affected property resulting from enactment or enforcement.” It is explicit, therefore, that any quantification method employed must be able to distinguish *reductions* in the value of the affected property resulting from the enactment or enforcement of the land use regulations from reductions in value resulting from extraneous variables.¹³⁶ This immediately undermines any textual basis for the exemption method, because it entirely lacks the ability to determine whether, or to what magnitude, the “affected property” has been reduced in value. Indeed, we have seen how employment of the exemption method can result in the calculation of loss when the regulation in question has instead resulted in an increase in value of the affected property.¹³⁷

It may be countered that the term “enforcement” within subsection 197.352(2) implicitly supports the exemption method. The argument being that the continued enforcement of the land use regulation *against the particular property* prevents that property from achieving a higher market value. This presumes that to negate the effects of the land use regulation, and thereby to compensate for any loss, it is simply necessary not to apply the regulation to the specific land. The exemption method is based on this presumption.

However, the text of subsection 197.352(2) implicitly contradicts such an interpretation. Subsection (2) envisages enforcement of a land use regulation on an all-or-nothing basis; that is, it envisages the devaluation of a property resulting from the enforcement of the regulation *in specie*. This is evident if one contrasts the language in subsections (1) and (2), which imply a generality of enforcement of land use regulations, with the language in subsections (4), (5), and (6), in which enforcement is clearly parcel specific. Although subsection (2) mentions the “affected property” it is specific to the calculation of the “reduction in the fair market value,” which “result[s] from” the *general* “enactment or enforcement of the land use regulation.” Compare this with the language in subsection (4), which states that just compensation

136. That is, variables wholly unaffected by the enactment or not of a land use regulation. As noted above, this is a problem common to economic modeling.

137. Albeit only where the unregulated comparable land has increased at a greater rate.

shall be due 180 days after the written demand is made “if the land use regulation continues to be enforced *against the property*.” Compare also the language in subsection (5), where the local government is to apply “the land use regulation as an approval criterion to an application submitted by the owner of the property,” or subsection (6), where a right of action in a trial court accrues in certain cases so long as “a land use regulation *continues to apply to the subject property*.”

The generality of the language contained within subsection (2) requires that any valuation method must assess the differential between the value of the land *with* the land regulation (enacted and enforced in its entirety) and the value of the land *without* the land regulation (where the land use regulation was never enacted or enforced). It does not allow for the exemption to be granted to a specific land parcel as required by the exemption method.

Finally, the legislative history of Measure 37 demonstrates that the voter intent was to rebalance the planning system in Oregon and to ensure landowners were treated in a “fair and just manner.” That the Measure was sold to voters with the emphasis firmly on “fair and just” compensation is apparent from many of the arguments for a “YES” vote on Measure 37 in the voters’ pamphlet; for instance, Dorothy English, the so-called “poster child” of Measure 37, called for the restoration of “fairness and balance to the system”; the Family Farm Association asserted that “Measure 37 . . . is about restoring fairness”; the Family Farm Preservation argued, “no-one should take property without *compensation*”; and the Oregon Cattlemen’s Association appealed for “a restored balance that is fair.”¹³⁸ Indeed the vast majority of the arguments make reference to a “fair and balanced system,” and all refer to the government payments as compensation.

Thus, it is imperative for any valuation method to be consistent with this legislative history, that it both accurately captures the loss suffered by the claimant so as not to produce windfalls, and also provides a “fair and balanced” methodology. As seen above, the exemption method fulfills neither of these requirements. It is not compensatory—it fails to capture the devaluation of the property caused by the land use regulation, and often results in hyper-inflated claims. Neither is it fair—any loss calculated will be more a function of the increase in value of comparable unregulated land than reflective of any loss actually suffered.

138. See OR. SEC’Y OF STATE, 2004 GENERAL ELECTION VOTERS’ PAMPHLET, *supra* note 30, at 105–07, 109–10.

B. *Conceptual Category Two: Sercombe's Analysis*

Sercombe's overarching thesis is that just compensation under subsection 197.352(2) should be based "on the value reducing effects of *enactment* of the land use restriction."¹³⁹ In other words, the compensation should be limited to the facial effect of the enactment of the land use regulation. The problem Sercombe faces in succeeding with this analysis is that the text of subsection 197.352(2) defines just compensation as the "reduction in the fair market value of the affected property interest resulting from enactment *or enforcement* of the land use regulation." The use of the term enforcement, as Sercombe admits, could infer that the "culpable governmental conduct" takes place at a date later than the enactment of the land use regulation and hence implies a different valuation methodology.

Sercombe readily admits that, *prima facie*, both the terms "enforces" in subsection(1) and "enforcement" in subsection (2) are contrary to the argument that he attempts to make, and therefore it is imperative that he explains their presence in the text, in order for his proposed methodology to have any force.

He does so by contending that the terms "enforces" and "enforcement" within subsections (1) and (2), respectively, mean merely a "failure to remove, modify or not apply the land use regulation." Such passive enforcement is, Sercombe asserts, contained within the statute in both subsections (4) and (6). These subsections create, respectively, a right to payment, and a cause of action in the trial courts, in cases where the land use regulation "continues to be enforced" and "continues to apply" despite a written demand under subsection (2) being made. He juxtaposes these examples of "passive enforcement" with "active enforcement" found in subsection (5), where the statute of limitations restricts claims to within two years of the local government "apply[ing] the land use regulation as an *approval criteria*. . . ."¹⁴⁰

Crucially, by reference to the fact that subsection (7) precludes the local government from establishing procedures that "serve as grounds for dismissal, abatement or delay of a compensation claim," he concludes that the term "'[e]nforces' under [subsection] 197.352(1) [of the Oregon Revised Statutes] likely means that the regulation 'continues to apply' after demands, as paraphrased by [subsection]

139. Sercombe, *supra* note 122, at 14 (emphasis added).

140. OR. REV. STAT. § 197.352(5) (2005) (emphasis added). Of course the statute of limitations is superficial; all a claimant has to do to "restart" her claim is to apply for a new land use permit with regards the regulation she wishes to challenge.

197.352(6). At a minimum, [he suggests] the word means something in addition to the ‘active enforcement’ of the use-restricting land use regulation.”¹⁴¹

In other words, were the local or state government, to require as a precondition for a Measure 37 claim, that a claimant have demonstrated active enforcement by making an application for a land use permit or the like, it would contravene subsection (7). Thus, by proving that “enforces” in subsection (1) must mean something more than merely active enforcement, Sercombe is able to establish that there is no requirement that the claim ripen in order for “compensation” to be payable.¹⁴²

So far, so good. However, as the active enforcement of a land use regulation is *not* necessary to bring a compensation claim,¹⁴³ Sercombe goes on to submit that “it is reasonable to construe subsection 197.352(1) to base the *remedy* on the facial effect of a land use regulation, and not its administration.”¹⁴⁴ It is this with this slight-of-hand, deducing from the premise that active enforcement is not necessary in order to bring a Measure 37 claim, to the proposition that compensation should be based on the facial effect of a land use regulation only, that his analysis becomes less transparent. In fact, the argument immediately appears counterintuitive: if the claimant is able to bring a claim without demonstrating active enforcement (i.e., there is no ripeness requirement analogous to a takings claim, therefore a claim can be brought *merely* after passive enforcement by the local government¹⁴⁵), why does this prevent the claimant from taking into account any value-altering effects flowing from the passive enforcement of the regulation (as well as its active enactment)? The presumption Sercombe appears to be making is that only enactment or/and active enforcement, and not passive enforcement, of land use regulations can have an effect on property values. Thus, without the need for active enforcement in order to bring a claim, all that is left to affect the property’s value is the facial effects of enactment. This allows Sercombe to assert that subsection 197.352(1) “hinge[s] a compensation claim upon the value reducing effects of a

141. Sercombe, *supra* note 122, at 13.

142. Under *Williamson County Regional Planning Commission v. Hamilton Bank*, 473 U.S. 172 (1985), a taking claim must be “ripe” for adjudication. In the context of takings law, “ripeness” means that a claimant must have sought all administrative remedies before resorting to a claim for damages. Such a process is not required in order to pursue a Measure 37 claim.

143. See OR. REV. STAT. § 197.352(7) (2005).

144. Sercombe, *supra* note 122, at 13.

145. See *Williamson County Reg’l Planning Comm’n*, 473 U.S. at 194.

restriction on use by enactment of a land use regulation or by action confirming that restriction on use.”¹⁴⁶

The solitary role reserved for the word “enforcement” within subsection 197.352(2) is for those cases where the land use restriction is applied to property in an unexpected or discretionary way. In such cases active enforcement, rather than the enactment itself, supplies the facial effect, and hence, causes devaluation in land value. Sercombe concludes his textual argument by saying: “The facial application of the regulation is what largely produces this market effect. Because of this, it is reasonable to construe the compensation formula under [subsection] 197.352(2) as based on the value reducing effects of enactment of the land use restriction.”¹⁴⁷

By referring to eminent domain law, Sercombe attempts to support his argument that the compensation should be confined to the facial effects on the property’s fair market value and the “losses from that reduction in value up to the point of the claim.”¹⁴⁸ Sercombe contends that a “compensation formula that updates the past reduction in value is consistent with the valuation awarded in regulatory takings cases.”¹⁴⁹ Drawing an analogy with the irregularly invoked doctrine of temporary regulatory takings, he highlights the use of a “market rate of return or interest rate as an acceptable measure of return on a use limitation and reliance on comparable sales as the measure of difference in value.”¹⁵⁰ Combining his interpretation of the words “enacts or enforces” in subsection (1) with the rate of return multiplier drawn from the regulatory takings analogy, Sercombe summarizes his valuation method as follows: “[T]he difference in fair market value of the property with and without the regulation, measured at the time of the ‘taking’ (enactment or implementation of the regulation) and a return on that loss between the time of the ‘taking’ and the demand for compensation.”¹⁵¹

C. *Conceptual Category Three: An Alternative Interpretation*

Although there is much that is convincing about Sercombe’s argument, his concentration on the reduction in fair market value resulting

146. Sercombe, *supra* note 122, at 14.

147. Sercombe, *supra* note 122, at 14 (emphasis added).

148. *Id.*

149. Sercombe, *supra* note 122, at 17.

150. Sercombe, *supra* note 122, at 20.

151. *Id.*

from the *enactment* of the land use regulation, or the facial effect, may not be as consistent with the text and context of the Measure as other explanations. A better and more accurate interpretation of the text, context, and legislative history of section 197.352 is one that captures the differential, *at the date of the claim*, between that current fair market value of the land (when the regulation has been both enacted and enforced) and the fair market value had the regulation never been enacted *or* enforced (the hypothetical). This is the differential which the valuation methodologies in the third conceptual category attempt to assess. In order to capture this differential accurately, the devaluation must be viewed in a more holistic manner than Sercombe proposes: not only should the facial effects of enactment be considered, but also the ongoing effects which flow from the passive enforcement of the land use regulation. In the following section each of the statutory interpretative reference points highlighted in *Portland General Electric Co.*—the text, context, *and* the legislative history—will be analyzed in turn to demonstrate how they provide support such for an interpretation.

D. Textual Analysis

1. “REDUCTION”

The term “reduction” within the first sentence of subsection 197.352(2) demands that, as a prerequisite to any successful claim, the property has, after adjustment for inflation, been reduced in value by the enactment or enforcement of the land use regulation. As we have seen this requirement has already undermined any support for the exemption method, however there are further ambiguities with the term “reduction.” One might argue, for instance, that the phrase “reduction in the fair market value of the affected property” implies that there has to be, as a precondition to a compensation claim, a *net* reduction in value of the property in real terms. In this case one would need to ask the antecedent question, “[H]as there been a *net* reduction in the property’s fair market value from the time of enactment of the land use regulation?” If the answer is no, then this automatically ends the claim; on the other hand, if the answer is yes, further analysis is required to determine whether the reduction in value “result[ed] from the enactment or enforcement of a land use regulation” or from some other source.¹⁵²

152. Sercombe, *supra* note 122, at 3.

However, such an interpretation is clearly erroneous when one considers the section in its entirety. The reduction aimed at by the regulation is *not* the net reduction in value of the property as compared with the time of enactment, but rather any reduction “resulting from the enactment or enforcement of the land use regulation.” This includes any reduction in value caused by the land use regulation, *notwithstanding* the property’s otherwise increase in value. The suggested interpretation could well result in a claim being denied where the land use regulation *has* had a large negative effect on a land’s value, but where this negative effect is masked by other factors or components having a correspondingly large (or larger) positive effect, so that the net outcome is either zero, or positive. It is arbitrary to restrict a claimant’s ability to make a claim by requiring that there has been a net devaluation in her property, as the validity of a compensation claim becomes contingent on factors entirely extraneous to the “value-reducing” or “value-enhancing” effects of the land use regulation.

To determine the reduction demanded by a literal interpretation of the text, “the *reduction* in the fair market value of the affected property *resulting from* enactment or enforcement of the land use regulation,” it is necessary to isolate the impact of the land use regulation, which is only one of a multifarious number of factors that affect land value. The assessment of loss should then focus on whether that component *alone* has brought about a reduction in value, and this analysis should be wholly unaffected by the question of whether the net value of the property in question has risen or fallen. Thus, to assess accurately the *reduction* in land value *resulting from* enactment or enforcement in isolation, the comparison must be between the current fair market value (with the regulation enacted and enforced), and the hypothetical fair market value of the land had the regulation in question *never* been enacted or enforced.

2. “ENACTMENT OR ENFORCEMENT”

The language “enactment or enforcement of the land use regulation” is pivotal to the meaning of the section. Sercombe recognizes this, and skillfully attempts to consign the importance of the term “enforces” with subsection 197.352(1) to those situations where the *enactment* has not had a facial effect on the value of the property.¹⁵³ However, the literal

153. Those situations in which it was not clear at the time of enactment that the land use regulation applied to the property.

interpretation of subsection 197.352(2) mandates that *both* the facial effects of the enactment and the continuing effects of the enforcement are taken into account when assessing whether (and/or the magnitude to which) the land use regulation has resulted in a reduction in the fair market value of the affected property. Indeed, Sercombe almost admits as much when commenting that “[t]he allowance of a claim when a jurisdiction ‘enforces’ the regulation suggests that the act of enforcement might cause the reduction in value, as distinct from, or perhaps in addition to, the value reduction by the facial effect of the law.”¹⁵⁴

Sercombe’s attempt to avoid the literal interpretation involves a distinction being drawn between what he has termed “active enforcement”—“appli[cation] [of] the land use regulation as an *approval* criteria [sic],” and what this author has termed “passive enforcement”—“failure to remove, modify or not apply the land use regulation.”¹⁵⁵ While the distinction drawn *itself* is insightful and accurate, it fails to explain why the “passive enforcement” of a regulation, which may have value-reducing or value-enhancing effects on properties, should be excluded from the valuation process. It has been suggested that Sercombe implicitly assumes passive enforcement of a land use regulation *does not* have an effect on the market value of the land, and that it is only active enforcement (whether in the form of enactment or the applying of the regulation as approval criterion) that causes devaluation. This assumption is indicated by his comment that “the facial application of the regulation . . . largely produces th[e] market effect.”¹⁵⁶

To an extent, Sercombe’s assumption is true: any effect on a land’s value that “passive enforcement” has is a result of the underlying threat of active enforcement. For instance, if a local government fails “to remove, modify, or not apply” (in other words, passively enforces) a land use regulation which restricts the number of properties that can be built on a property, then the only reason that the landowner complies with the regulation, and hence why the value of her land (and the value of her neighbors’ land) is affected by the passive enforcement, is the threat that should she not comply, the local government will apply the land use regulation as an approval criterion and deem the development an illegal or nonconforming use. While, in a sense, the reduction (or variance) in land values caused by passive enforcement flows indirectly from (at least the threat of) active enforcement, it is *not true* that the reduction is

154. Sercombe, *supra* note 122, at 12.

155. Sercombe, *supra* note 122, at 3.

156. Sercombe, *supra* note 122, at 14.

captured by assessing merely the facial effect. The value-altering effects of passively enforcing a land use regulation manifest themselves in a property's value in an entirely different manner to the immediacy of the facial effect flowing from enactment or active enforcement. The value-altering effects of passive enforcement secrete over a long-time period, and generally manifest as "amenity effects." For example, the beneficial effects of a large number of persons complying with a passively enforced land use regulation which restricts the type or density of property and thus preserves a beautiful pastoral setting will only appear over time. Jaeger also gives the example of environmental zoning, which may not have an immediate facial effect on a property's value as it takes time for neighborhood effects to appear (or if they already exist, for them to be better protected from degradation than other neighborhoods).¹⁵⁷

Sercombe's analysis, while correctly highlighting that passive enforcement of a land use regulation is all that is required under subsection 197.352(1) to bring a claim, fails to explain why the effects of that very (passive) enforcement should not be taken into account when constructing a compensation formula under subsection 197.352(2). The definition of "just compensation" in subsection (2) refers to both enactment and enforcement. The literal interpretation must be that both components—the facial effect of enactment or active enforcement *and* the continuing, longer term effects of passive enforcement—are to be taken into account. For a proposed valuation methodology to be consistent with the text of section 197.352, it must capture *both* components.¹⁵⁸

3. "AS OF THE DATE OF THE WRITTEN DEMAND"

The requirement that the reduction in the fair market value of the affected property be assessed "as of the date the owner makes written demand for compensation" demands that any "with" (current value) and "without" (hypothetical value) compensation formula be assessed *not* at the date of enactment, but rather at the date of demand. The exact reduction in the land's fair market value resulting from the enactment of the

157. Jaeger, *supra* note 68, at 113–14.

158. Some may contend that the use of the disjunctive "or" rather than the conjunctive "and" undermines the assertion that both the effects of enactment and enforcement should be taken into account. While this is certainly a plausible interpretation of the phrase, the concept of "or" in the English language is notoriously ambiguous, and can be applied either exclusively, so that if the effects of enactment are taken into account, the effects of enforcement cannot be, or inclusively, so that either, or both, can be taken into account. Analyzing the phrase in a vacuum can provide us with no clarity as to whether the use of the word "or" in subsections (1) and (2) of section 197.352 is inclusive. However, once the legislative history is taken into account, it becomes clear that the term "or" in this context is inclusive in nature.

land use regulation may well fluctuate over time, and the “date of demand” represents a statutorily defined cut off point at which compensation is to be assessed. This immediately appears at odds with Sercombe’s contention that compensation should be assessed at the earliest time the regulation “has the effect of reducing the fair market value of the property.”

In defense of Sercombe’s methodology, one can argue that augmenting the original devaluation by the interest that would have been earned between the date of enactment and the date of claim ensures that his formula assesses damages at the date of the written demand. This may well be true; however, it is contended that there is a distinction, albeit a fine one, between damages and “reduction in the fair market value.” In Sercombe’s method, the “reduction in the fair market value” is assessed purely on the basis of the facial effect *at the time of enactment*, which is then multiplied by an interest rate to equate to the loss suffered by the claimant. The reduction in the fair market value (the differential between the actual and hypothetical values) is therefore frozen at the time of enactment, and the interest component represents an attempt to compensate the landowner for any loss in revenue she has suffered from the loss of any income-producing potential. While the damages increase over time, the multiplicand—the *actual* reduction in fair market value (and hence the differential between the actual and hypothetical values)—remains static.¹⁵⁹

Such an interpretation contradicts the clear words of the statute. The language requires a calculation of just compensation—that is the differential between the hypothetical value (the value of the land had the regulation never been enacted) and the current value (the value of the land with the regulation enforced)—*as of the date of the written demand*. A valuation methodology which is consistent with the text of the statute must be able to account for any fluctuations in the reduction in fair market value (even to the extent that there may no longer be a reduction) right up to the date of the demand. Therefore, any multiplier used in a valuation method must attempt to establish a hypothetical value of the land at the date of the demand, and not merely update the reduction in value (assessed at the date of enactment) to account for lost revenue, as Sercombe does. The valuation methodologies of the third conceptual category are the only methods that aim at this differential.

159. Sercombe, *supra* note 122, at 15–16.

4. CONTEXT

As a measure adopted by the voters, the placement of the Measure in chapter 197 of the Oregon Revised Statutes is not clear. Certainly placement within that chapter with other statutes governing how state agencies and local governments are to implement land use policy including comprehensive planning, the preservation of agricultural lands, and the obligation to provide adequate needed housing throughout the state is significant. It may well be that the drafters desired inclusion in this chapter to require it to be part of the fabric of state land use regulation. If so, the lack of a frontal attack on the remainder of that chapter may represent a poisoned chalice to the drafters, who are left with arguing that the remaining portions must coexist with the Measure. If so, then the Measure must be read within the context of the remaining portions of the chapter.

E. Legislative History

The true intent of the legislation is to be compensatory in nature, and, therefore, the assessed loss should equal the entirety of the reduction in value caused by the land use regulation in question, and not just the facial devaluation. If the assessment of reduction in value is frozen at the level caused by the facial effect of enactment, then the amount payable has the potential either to over-compensate (if the effects of *enforcement* are found to increase the value of the property, and thus decrease the overall reduction in value of the property caused by the land use regulation), or under-compensate (if the effects of *enforcement* are found to further reduce the value of the property). Despite Sercombe's suggestions that his method is compensatory in nature, it will only be truly compensatory in those rare situations where the facial effect of enactment is the only effect that the land use regulation has on a property's value.

For a valuation methodology to be compliant with legislative history, and to ensure true compensation, it must capture both the facial effects of enactment or active enforcement and all of the ongoing, long-term effects of passive enforcement.

One of the strongest arguments that Sercombe makes in defense of his method is that Measure 37 is intended to be an extension of the takings doctrine, and as such the established valuation methodology in takings cases should form the basis of any compensation formula for Measure 37 claims. That the proponents of Measure 37, at least, saw this as an extension of the takings law is clear from their arguments in the "Voters' Pamphlet." Indeed Oregonians in Action went as far as to state:

Through the normal condemnation process, the state government and local governments have an efficient statutory procedure already used to determine just compensa-

tion. The process is quick, clean, and extremely efficient and will be the basis for determining just compensation under Ballot Measure 37.¹⁶⁰

Sercombe uses takings jurisprudence to buttress both his argument that the compensation be assessed at the earliest time the regulation “has the effect of reducing the fair market value of the property,” and his use of a rate of return as a multiplier to augment the assessed reduction.

However, as highlighted above, there is some tension between this intent and the clear terms of the statute. The tension arises because, in conceptual terms, Measure 37 claims and takings claims are very different creatures. A thought experiment illuminates the distinction between the concept of takings and the rationale of Measure 37 claims. Let us imagine that there are four properties all restricted by one land use regulation. But only one of these properties was so severely restricted that it constituted a taking under the *Penn Central*¹⁶¹ test. Assume that the taking was rescinded at the government’s request, so the taking was judged to be temporary in nature, and also that the loss caused by the taking was \$100,000. Should this \$100,000 compensation be reduced because of the fact that when the regulation was enforced it caused, through (long-term) amenity effects, an increase of \$5,000 in value to all four properties? Probably not: this is an effect of the *regulation* and not of the taking. Indeed, as the amenity effects accrue to all four properties, it logically cannot be a consequence of the taking (as there has only been a taking in one of the cases). In comparison, under the Measure 37 regime all four properties would be able to claim for the facial devaluation caused to their land by the enactment of the land use regulation in question (including the property that was so badly affected it constituted a temporary regulatory taking) *less* any appreciation in value of their properties (\$5,000) that the regulation had caused.

Moreover, in takings claims the government receives a property interest in the affected property; even in temporary regulatory takings the government has a quasi-proprietary right akin to an option on the affected property.¹⁶² With Measure 37 claims, the public pays, but gets no property right. A new right to payment accrues with any new

160. Sercombe, *supra* note 122, at 10.

161. See *Penn Cent. Transp. Co. v. New York City*, 438 U.S. 104, 131 (1978).

162. See generally *First English Evangelical Church v. County of Los Angeles*, 482 U.S. 304 (1987) (holding that the government had the option of keeping the regulation in place and paying compensation for the permanent taking, or rescinding the regulation and paying only compensation).

regulation that restricts land and arguably lowers property values. Thus, the method of calculation of payment becomes critical to any understanding of Measure 37. We now turn to the methodology that is most consistent with the Measure.

VI. Conclusion—The Measure 37 Methodology

The exemption method views only the land at issue and looks only at *its* value with and without the regulation. This methodology fails to address the effects of the regulations on other properties, and how those effects influence the value of the subject property.

The Hascic and Wu method has much to offer conceptually, but is expensive and difficult to apply. Moreover, it fails to deal with the complex interrelationships among regulations for economic analysis purposes.

The Plantinga/Jaeger method appears to come closest to the needs of practicality and relative ease of administration. It has the faults that may be seen as common for any non-economist, in that it does not deal with the non-economic actor who may deal with land for reasons besides economics. It assumes a relatively perfect market. It assumes the CPI is an appropriate multiplier. Finally, it attempts to deal with what is not known and may not be knowable—the effect of the land use regulation, in isolation, on the value of land. Even with these criticisms, however, the Plantinga/Jaeger analysis comes closest to the text and context of Measure 37 in terms of an easily applied methodology.

The Sercombe method attempts to reconcile the words of the Measure, to distinguish a cause of action as of the time of the bringing of the claim and the time when any cause of action that might otherwise accrue, i.e., at the time of the passage of the restrictive regulation. It then compounds the difference in value at the time of the passage of the restriction with an interest rate over the period of the imposition of the regulation. That compounding has the same difficulty as it does under the Plantinga/Jaeger method, i.e., it imposes a value on time, which may not be measurable nor reflect real world values. Unlike the Sercombe approach, it appears more consistent with the Measure to have the claim accrue when filed.

Thus, a methodology that looks to the date of the claim as the starting point, includes the total impact of the land use regulation, both positive and negative, and uses a rate of interest starting with the date of the claim, might be a better method of showing “loss” under Measure 37. Just as a statute must be interpreted in its text and context, so also must

the property value of a parcel be understood in the context of its surrounding area, and the applicable land use regulations.

The test must be the value of the land if the regulations were, and were not, applied to the area, rather than limiting consideration to the subject site. The economic impacts of the regulation at issue can be understood and quantified only when the enactment and enforcement of the regulation as a whole is the standard. Doing less contravenes the remedial purpose of Measure 37. Doing more results in an unjustified expenditure of public funds.

