2010-5100, -5101

IN THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

CCA ASSOCIATES,

Plaintiff-Cross Appellant,

v.

UNITED STATES OF AMERICA,

Defendant-Appellant.

Appeal from the United States Court of Federal Claims in 97-334C,
Judge Charles F. Lettow

PRINCIPAL AND RESPONSE BRIEF OF PLAINTIFF–CROSS APPELLANT CCA ASSOCIATES

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September 16, 2010

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CERTIFICATE OF INTEREST

Counsel for Plaintiff Cross-Appellant CCA Associates certifies the following:

1. The full name of every party or amicus represented by me is: CCA Associates.

2. The names of the real parties in interest represented by me are:
   - Ernest B. Norman III
   - John H. Norman Jr.
   - Margaret H. Norman
   - Ernest B. Norman Jr. & Emma Couret Norman Grandchildren's Trust:
     - John H. Norman Jr.
     - Caroline Norman
     - John H. Musser V
     - Christopher H. Musser
     - David Musser
     - Susan Gaines
     - Ernest B. Norman IV
     - Chesley A. Norman

3. All parent corporations and any publicly held companies that own 10% or more of the stock of the party or amicus curiae represented by me are: None.

4. The names of all law firms and the partners or associates that appeared for the party or amicus now represented by me in the trial court or agency or are expected to appear in this court are:

   Elliot E. Polebaum and Eugene N. Hansen, of the law firm Fried, Frank, Harris, Shriver & Jacobson LLP; Albert S. Iarossi, of the law firm Akin, Gump, Strauss, Hauer, & Feld LLP

Date: September 16, 2010

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TABLE OF CONTENTS

<u>TABLE OF AUTHORITIES</u>

CASES

STATUTES

REGULATIONS

MISCELLANEOUS

STATEMENT OF RELATED CASES

This case previously was before the Court in *CCA Associates v. United States*, 2007-5094, decided July 21, 2008.

Counsel is not aware of any related cases currently pending in this Court; however, as reflected in the government's opening brief, page ix, numerous takings claims pending in the Court of Federal Claims may be affected by the disposition of this case.

JURISDICTIONAL STATEMENT

This Court has jurisdiction to consider the cross appeal of Plaintiff-Cross Appellant CCA Associates ("CCA") pursuant to 28 U.S.C. § 1295(a)(3). CCA cross appeals from a final judgment.

COUNTER-STATEMENT OF ISSUES

A. Did the Court of Federal Claims ("COFC") properly conclude that CCA suffered a regulatory taking, requiring the government to pay just compensation under the Fifth Amendment, particularly where:

   (1) ELIHPA and LIHPRHA, the statutes at issue, effected a taking comparable to a forced physical occupation, conscripting CCA to house HUD-approved low- and moderate-income tenants;

   (2) The COFC made express findings of fact that the confiscated prepayment right formed the primary investment expectation both for any reasonable investor in Chateau Cleary and for CCA; and

   (3) CCA suffered a financial loss of more than $700,000 (an 80% loss concentrated over the 5-year takings period, corresponding to an 18% loss in the property's lifetime value), a severe financial loss for a family-owned, 104-unit apartment complex?

B. Did the COFC properly determine just compensation by awarding CCA lost rental income?

STATEMENT OF ISSUE ON CROSS APPEAL

Did the COFC err in concluding that it was bound to dismiss CCA's breach of contract claim for lack of contractual privity because of *Cienega Gardens v. United States*, 194 F.3d 1231 (Fed. Cir. 1998)?

COUNTER-STATEMENT OF FACTS

This case, commenced in 1997, returns to this Court after a second trial and a second judgment in favor of CCA. The issues presented are familiar. In several decisions, this Court has addressed whether enactment of the Emergency Low Income Housing Preservation Act of 1987 ("ELIHPA")[1] and the Low-Income Housing Preservation and Resident Homeownership Act of 1990 ("LIHPRHA")[2] either breached owners' contractual rights or, alternatively, effected a compensable taking of the owners' right to prepay mortgages and exit Department of Housing and Urban Development ("HUD") programs, including the Section 221(d)(3)[3] program pertinent to this case. The COFC here, in a second detailed opinion, followed this Court's instructions on remand, JA1747, properly applied Supreme

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1 101 Stat. 1877 (1988) (codified at 12 U.S.C. § 1715*l* note).

2 104 Stat. 4249 (1990) (codified at 12 U.S.C. § 4101 *et seq*.).

3 Codified as amended at 12 U.S.C. § 1715*l*(d)(3).

Court and Federal Circuit precedents, again found a taking in violation of the Fifth Amendment, and again awarded CCA just compensation.

The facts recounted below are taken from both the COFC's 2010 and 2007 decisions, published at 91 Fed. Cl. 580 and 75 Fed. Cl. 170, respectively, unless otherwise noted.[4]

Chateau Cleary Transaction

The property at issue in this case is Chateau Cleary Apartments ("Chateau Cleary"), a 104-unit apartment complex in West Metairie, Louisiana, a suburb of New Orleans. A11. In October 1969, at the urging of HUD employees, Ernest B. Norman, Jr. and J. Robert Norman (the "Norman Brothers"), the predecessors-in-interest to CCA, purchased the land on which Chateau Cleary is located and agreed to construct and operate Chateau Cleary under HUD's Section 221(d)(3) program. A11. In pressing the Norman Brothers to invest in low-income housing, and thus to accept years of minimal returns, HUD representatives touted the program's so-called "prepayment right," which effectively limited the duration of use restrictions on the property to a 20-year term. 75 Fed. Cl. at 192. Chateau Cleary

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[4] In its 2010 decision, the COFC adopted the factual findings set forth in the 2007 decision, with a few limited exceptions. A9 n.2. Citations to the 2010 decision are to the addendum to the government's brief. Citations to the 2007 decision are to the Federal Claims Reporter. The government's addendum is cited as "A__," the Joint Appendix as "JA__" and the government's brief as "Br."

would house qualifying tenants and be subject to HUD regulations, restrictions, and oversight for 20 years; after 20 years, the Norman Brothers could exit the HUD program and operate the property however they saw fit, including by evicting all tenants, tearing the complex down, and building a movie theater.

Three core documents, executed contemporaneously, set forth the transaction: a regulatory agreement between HUD and the Norman Brothers; a mortgage between the Norman Brothers and the lender; and a note between the Norman Brothers and the lender, which note HUD endorsed. A17-19; JA611-24. HUD's endorsement of the note provided mortgage insurance, which in turn facilitated a low-interest 40-year mortgage in favor of the Norman Brothers and, additionally, reduced their initial cash outlay. A11. In consideration for this mortgage insurance, the Norman Brothers signed the regulatory agreement and thereby agreed to house low- and moderate-income tenants at Chateau Cleary for as long as HUD insured the mortgage. A11.

The regulatory agreement sharply restricted the Norman Brothers' use of Chateau Cleary. *Inter alia*, the Norman Brothers agreed to:

- limit the occupancy of Chateau Cleary to low- or moderate-income families;
- charge rents according to a HUD-approved schedule;

- manage the property "in a manner satisfactory to [HUD]," which meant compliance with HUD regulations and manuals (JA1063) (Tr.15:9-23) (Norman);
- obtain HUD approval for any conveyance of the property;
- submit to HUD audits and furnish annual financial reports to HUD; and
- limit their annual return to 6% of their initial equity investment.

JA611-16; 75 Fed. Cl. at 173.

The Norman Brothers first executed the transaction documents on November 7, 1969. A11. However, the Norman Brothers later requested, and HUD approved, an increase in the loan amount. The Norman Brothers therefore signed a second secured note and mortgage on May 17, 1971. A12 n.7; JA750-57. The second mortgage incorporated by reference the 1969 Regulatory Agreement. A12 n.7; JA753.

HUD – not the lender or Norman Brothers – structured the entire transaction. All of the transaction documents appeared on pre-printed HUD forms. A18. In both 1969 and 1971, the parties signed the transaction documents contemporaneously at HUD's office in New Orleans. A18. Subsequent to the transaction, the lender, Pringle-Associated Mortgage Company, sold the loan to Ginnie Mae, a HUD-administered government corporation. A10 n.3.

In March 1985, Ernest B. Norman, Jr. formed CCA Associates ("CCA"), a general partnership. A12; JA775-86. The partners then included himself, his children, and a trust for his grandchildren. A12. In April 1985, J. Robert Norman sold his 50% interest in Chateau Cleary to CCA for $677,550, and CCA assumed the Chateau Cleary mortgage. A12; JA761-65. HUD approved the transaction and required CCA to sign a new regulatory agreement. A12. The 1985 regulatory agreement mirrored that signed in 1969. A12; JA766-74. In December 1985, Ernest B. Norman, Jr. transferred his one-half interest in Chateau Cleary to CCA, thus giving CCA the full ownership of the property. A12.

Chateau Cleary always has been a family business. Members of the Norman Family presently and always have owned and operated Chateau Cleary. Ownership never has been syndicated.

The Primacy of the Prepayment Right

Significant for present purposes, both the 1969 and 1971 notes included express language guaranteeing the Norman Brothers the right to prepay the mortgage after 20 years (or on May 17, 1991). JA618, 750. Thus, as of May 17, 1991, the Norman Family could recapture its property in fee simple and cease housing qualifying tenants. The same prepayment right was embodied in HUD's regulations: The "mortgage indebtedness may be prepaid in full and the Commissioner's controls terminated without the prior consent of the

Commissioner where . . . the prepayment occurs after the expiration of 20 years from the date of final insurance endorsement of the mortgage . . . ." 24 C.F.R. § 221.524(a)(1)(ii) (1970); *Cienega Gardens v. United States*, 331 F.3d 1319, 1330 (Fed. Cir. 2003) ("*Cienega VIII*") ("Owners had unequivocal contractual rights after twenty years to prepay their mortgages[.]").

This prepayment right formed the *primary* investment-backed expectation in the decision to proceed with the Chateau Cleary project, not only for the Norman Brothers but also for any reasonable investor. A39. The reason is simple: At the time of the transaction, the land on which Chateau Cleary was to be built sat in the path of anticipated middle-class development in the New Orleans metropolitan area. 75 Fed. Cl. at 192. The Norman Brothers thus could construct a quality complex, maintain it well, and then convert the property to conventional housing at year 20 – at the time when development would reach Chateau Cleary and when conventional housing would be in high demand. *Id*. at 194.

The Norman Brothers executed this plan, and development reached Chateau Cleary just as anticipated. By 1991, Metairie had the benefit of two large popular shopping malls, one of the area's premier medical complexes, good public schools, low crime, a new regional library, easy access to Interstate 10, and proximity to downtown New Orleans. *Id*. at 193. Moreover, the complex was ideally positioned for the conventional market. The Norman Brothers used quality construction, building Chateau Cleary for the long run, and the Norman Family maintained the property in fine condition. Chateau Cleary consistently received superior ratings during HUD-required inspections and was praised as being “a model complex” by HUD’s own inspectors. JA01, 796. Well into its fourth decade of operation, Chateau Cleary sustained minimal physical damage from Hurricane Katrina in August 2005 – a testament to the quality of its construction and maintenance. 75 Fed. Cl. at 193. The property recently appraised at $5 million, A39, a more than $3 million appreciation since 1991. JA556.

That the Norman Brothers’ strategy looked ahead to achieve substantial economic gains after 20 years is further confirmed by their decision not to syndicate the ownership of Chateau Cleary. Syndication would have meant relinquishing most of the ownership in the property and sacrificing the up-side benefit that the family expected to achieve upon prepayment. JA969 (Tr.92:13-22) (Norman).

CCA’s expectations in 1985, when it acquired Chateau Cleary, mirrored those of the Norman Brothers in 1969, except the realization of those expectations was then only six years away. 75 Fed. Cl. at 192. The price CCA paid for J. Robert Norman’s one-half interest in Chateau Cleary reflected the growing value in the property as the prepayment date (and therefore the market conversion date) neared. *Id*. If CCA had known in 1985 that it would be forced to continue operating under HUD regulations until the 40th anniversary of the mortgage, thus incurring years of minimal or no returns, the transfer to CCA in all likelihood would not have happened at any price because, essentially, "there would have been nothing to buy." JA1017 (Tr.175:22-25) (Norman). The prepayment right thus formed not only the primary, but the sole, investment-backed expectation for CCA.

Benefits of Entering the Section 221(d)(3) Program

The limited available returns in operating a Section 221(d)(3) property further demonstrate the significance of the prepayment right and realization of the property's unrestricted value after 20 years. The regulatory agreement limited the Norman Brothers to a *maximum* annual dividend of 6% of the initial equity investment, or a maximum return of $12,952. 75 Fed. Cl. at 180. At year 1, year 20, or year 40, the Norman Family never could hope to earn more than $12,952 in the HUD program. In fact, the Norman Family often did not enjoy even this minimal dividend. The Norman Family received no cash distribution at all – and hence no profit – during the first *12 years* of the project. A35. By 1990, the Norman Family had received less than one-half of the potential returns allowable. A35.

The government nonetheless argues that "tax benefits" formed the primary investment-backed expectation. *But the COFC found otherwise.* In fact, the tax benefits – *i.e.*, the ability to deduct accelerated depreciation from ordinary income – applied across the board to conventional and HUD properties alike. A36. Moreover, Congress could revoke the then-existing tax shelter at any time – *and did revoke it* as part of tax reform in 1986. A38. In addition, the value of any tax benefit hinged on marginal tax rates (which could change at any time, and did, in fact, decline substantially in 1981), as well as, obviously, the taxpayer's income (which also could decline and diminish the value of any tax shelter). JA988 (Tr.1254:3-10) (Malek) (admitting that tax benefits decreased in 1981 with reduction in marginal tax rates). In short, any number of unknown and unknowable contingencies impacted the value of the tax shelter.

Further confirming the primacy of the prepayment right, the Norman Brothers did not even take the available accelerated depreciation. A36. As found by the COFC, "[a]ccelerated depreciation, inherently by its nature, throws off greater tax benefits in the early years, but it eventually generates a tax detriment later. . . ." A36. Thus, in contrast to many limited partners in syndicated properties, who sought a temporary tax shelter, the Norman Family planned for the long run. A36 ("Accelerated depreciation as a result was favored for syndication to purchasers who wanted a short-term shelter for ordinary income and were not interested in long-term benefits.").[5]

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[5] The government's *argument* that CCA received tax benefits from 1972 to 1975 "exceed[ing] the amount of the Normans' initial investment," *see* Br. 13,

Footnote continued

Tax benefits manifestly did not motivate CCA's decision to acquire Chateau Cleary in 1985, a mere 6 years before CCA's prepayment date. By this time, any tax benefit already had expired. JA987 (Tr.1253:19-20) (Malek) (admitting tax shelter no longer available). The price paid by CCA reflected the expectation that the property's residual value shortly would be realized. 75 Fed. Cl. at 192.

<u>The Preservation Statutes</u>

1. <u>Confiscation of CCA's Right to Exclude</u>

The Norman Family satisfied its end of the bargain. The government did not. When Congress believed in the late 1980s that thousands of low-income housing units might be lost to mortgage prepayments, Congress simply outlawed

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Footnote continued from previous page

distorts the record and ignores the COFC's findings of fact. In making this argument, the government apparently assumes an initial cash investment of $31,877. Br. 13. But this assumption is wrong, and the other assumptions apparently employed by the government (e.g., hypothetical income and marginal tax rates) find no support in the record, let alone in the findings of the COFC. In fact, HUD (and the COFC) determined the Norman Brothers' initial equity investment to be $215,867, not $31,877. 75 Fed. Cl. at 180.

The government nonetheless may contend in Reply, as it has previously, that the Norman Brothers' cash outlay was less than $215,867 because the Norman Brothers received a Builder's and Sponsor's Profit and Risk Allowance ("BSPRA") for constructing and managing the project, which counted toward a determination of the initial equity. But the BSPRA represented the Norman Brothers' profit for building Chateau Cleary, not a contribution by the government. 75 Fed. Cl. at 174 n.4. A subcontractor similarly would have demanded a profit on its labor.

prepayment, first through ELIHPA, a temporary measure, and then permanently through LIHPRHA (collectively, the "Preservation Statutes"). Congress thus placed the burden of providing low-income housing squarely on then-existing owners rather than by funding new construction or providing payment vouchers to tenants.

Congress knowingly and intentionally abrogated the owners' contractual rights. Senator Armstrong observed with irony that HUD had "enter[ed] into contracts with owners and developers" and that the owners "probably had the mistaken notion that the Federal Government was going to honor its word." 136 Cong. Rec. 26,382-83 (1990). Senator D'Amato admitted that the legislation penalized "[o]wners of projects, who have lived up to a 20-year agreement with the Federal Government." 133 Cong. Rec. 22,209 (1987). Senator Heflin acknowledged that "unilaterally abrogating a contract, which has been adhered to by one party for 20 years, flies in the face of the law." 136 Cong. Rec. 26,372 (1990). And Representative Joseph Kennedy justified the legislation by explaining that "some fine print allowing prepayment" should not defeat the goal of providing low-income housing. *Preservation and the Loss of Subsidized Housing Stock*, Hearing Before Subcomm. on Housing and Community Dev. of H. Comm. on Banking, Finance and Urban Affairs (Feb. 28, 1990) at 6.

The "Preservation Statutes" thus achieved the desired end: They "preserved" affordable housing by compelling owners, including CCA, to continue renting units to qualifying tenants. CCA lost completely the right to exclude these tenants and make some other use of the property.

2. <u>ELIHPA and LIHPRHA Compensation Scheme</u>

The Preservation Statutes presented owners with certain "options" which, in theory, had the potential to partially compensate for confiscation of the prepayment right. In reality, the options required an owner to suffer a multi-year bureaucratic process with no assurance of a specific outcome, except that the owner would be far worse off than if ELIHPA and LIHPRHA had not been enacted.

One option required the owner to sign a "use agreement" and maintain the property as affordable housing in exchange for financial incentives. ELIHPA § 224; 12 U.S.C. § 4109 (LIHPRHA). However, any owner seeking these incentives was required to maintain the property for very-low, low-, and moderate-income tenants "for the remaining useful life" of the property, which HUD deemed was at least *50 years*. 12 U.S.C. §§ 4112(a)(2)(A) & (c)(3). But even these incentives proved illusory for many owners because Congress ceased funding them. A48. None of the properties in New Orleans that had approved plans of action for incentives under LIHPRHA received funding and, thus, none of the plans was implemented. A48.

A second option, available only under LIHPRHA, provided for the sale of the subject property through an artificial process at a HUD-approved price to a HUD-approved purchaser. But the prospective purchaser, if one could be found, had to agree to maintain the low-income affordability restrictions *for the remaining useful life of the property*. 12 U.S.C. § 4121(a)-(b). Thus, the "sale option," too, depended upon HUD's provision of incentives and funding by Congress. Br. 10; JA1082 (Tr.93:1-5) (East). No buyer would pay fair-market value for a property which had to be dedicated to low-income housing *for its remaining useful life*. JA984 (Tr.640:13-18) (Alexander) (admitting LIHPRHA sale process "very different" from fair-market process).

Moreover, no owner even could commence the sale process until, at the earliest, April 1992, when HUD first enacted interim regulations implementing LIHPRHA. A44; 57 Fed. Reg. 11,992 (Apr. 8, 1992). According to HUD guidance, the "sale option" took 41 months to complete. JA1901-08. Thus, the earliest that any party could expect to complete a sale under LIHPRHA would have been around *September 1995*, or *4.5 years after CCA's prepayment date* of May 1991 (assuming that a willing buyer could be found, that the parties could obtain a position in the funding queue sufficiently early to obtain the incentives, that the buyer would not back out of the transaction, and that HUD timely would process the transaction).

CCA exercised its statutory option *not* to seek either the sale or incentive "benefits." The Norman Family did not want to sell its property, and it certainly did not want incentives and another 50 years of HUD regulation.

<u>The HOPE Act and Restoration of the Right to Prepay</u>

By its terms, LIHPRHA *permanently* confiscated CCA's prepayment right, meaning that CCA had no choice but to house HUD-approved tenants for an additional 20 years, or until May 2011 when its 40-year mortgage would be paid in full. However, on March 28, 1996, Congress reversed course and enacted the Housing Opportunity Program Extension Act of 1996, Pub. L. No. 104-120, 110 Stat. 834 (1996) ("HOPE"). HOPE permitted owners to prepay their HUD-insured mortgages, but mandated a 60-day moratorium on rent increases. A14.

Following the passage of HOPE, CCA took steps to pursue prepayment, including seeking financing and obtaining an appraisal. A15-16. After months of HUD-related delays, CCA finally was able to complete the prepayment process in September 1998. A16.

All parties agree that the takings period in this case lasted 5 years, from CCA's original prepayment date of May 17, 1991, until May 27, 1996, the day CCA ostensibly could rid itself of the HUD restrictions. A30.

<u>**SUMMARY OF ARGUMENT**</u>

The COFC concluded not once, but twice, that ELIHPA and LIHPRHA went "too far" and effected a regulatory taking of CCA's property. *Penn. Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922) ("The general rule at least is that while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking."). The court reached the correct result both times.

The fundamental questions before this Court are simple: Are the effects of the regulations here comparable to a traditional taking? Do justice and fairness require the payment of just compensation? *See, e.g.*, *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 528, 539 (2005) (O'Connor, J., concurring) (purpose of court's inquiry is to identify "regulatory actions that are functionally equivalent to the classic taking in which government directly appropriates private property or ousts the owner from his domain"); *Penn Cent. Transp. Co. v. New York City*, 438 U.S. 104, 123 (1978) (court must determine whether "justice and fairness" require payment of compensation). These questions must be answered in the affirmative.

<u>First, ELIHPA and LIHPRHA effected an outcome comparable to a forced-physical occupation of land</u>. ELIHPA and LIHPRHA compelled CCA *to house* HUD-approved tenants against its will. The legislation wholly deprived CCA of its fundamental right to exclude others, tear down the apartment complex, and make some other use of the property. In cases like this one, implicating the

fundamental right to exclude others, Supreme Court precedent *requires* the finding of a taking and the payment of just compensation. *Kaiser Aetna v. United States*, 444 U.S. 164, 179-80 (1979) (applying *Penn Central* factors) ("[W]e hold that the 'right to exclude,' so universally held to be a fundamental element of the property right, *falls within this category of interests that the Government cannot take without compensation*.") (emphasis added).

<u>Second, justice and fairness require the payment of just compensation</u>. Through ELIHPA and LIHPRHA, Congress unfairly shifted the burden of providing affordable housing to CCA, rather than appropriate funds to construct new affordable housing units or to provide vouchers for low-income tenants. Not only did the statutes single out CCA for disparate treatment, but they also took CCA's primary investment-backed expectation. The end result was that CCA, a family business, lost hundreds of thousands of dollars over a 5-year period, a more than 80% diminution during that period.

* * *

Separately, on CCA's cross appeal, the Court should conclude that the government breached its contractual commitments in enacting ELIHPA and LIHPRHA and thus prohibiting prepayment. The transaction documents executed first in 1969 and then in 1971 formed three parts of one overall agreement, binding on the government, including CCA's contractual right to prepay. The COFC reached this conclusion but "reluctantly" held that it had to dismiss CCA's contract claim because of this Court's decision in *Cienega Gardens v. United States*, 194 F.3d 1231 (Fed. Cir. 1998) ("*Cienega IV*"). In fact, the facts in this case are distinguishable from those in *Cienega IV*. In all events, *Cienega IV* conflicts with longstanding precedent and deserves to be overruled by this Court *en banc*.

ARGUMENT

I. THE COFC PROPERLY DETERMINED THAT CCA SUFFERED A REGULATORY TAKING

Determining when a regulation "goes too far" and effects a compensable taking requires an "*ad hoc*, factual inquir[y]" by the trial court. *See Penn Cent.*, 438 U.S. at 124. "[T]here is no set formula." *Cienega Gardens v. United States*, 503 F.3d 1266, 1278 (Fed. Cir. 2007) ("*Cienega X*") ("The focus of the regulatory takings analysis is on fundamental fairness . . . .").

Notwithstanding the flexible *ad hoc* nature of the inquiry, courts typically focus on three guideposts identified in the *Penn Central* decision: (i) the character of the governmental action, (ii) the investment-backed expectations of the claimant, and (iii) the economic impact of the regulation on claimant. *Id*. at 1279. Consistent with the mandate of this Court, JA1747, the COFC here analyzed each *Penn Central* factor in light of the *Cienega X* decision and determined that Congress unfairly burdened CCA with the cost of providing affordable housing.

The COFC properly applied the law, and its judgment finding a taking must be affirmed.[6]

A. The Character Of The Preservation Statutes Singularly Supports The COFC's Finding Of A Taking

The "character" factor may be informed by either of two inquiries. The first inquiry asks whether the governmental action is comparable to a physical occupation, implicating the fundamental right to exclude others. *Penn Cent.*, 438 U.S. at 124 ("A 'taking' may more readily be found when the interference with property can be characterized as a physical invasion by government . . . .") (citation omitted). Where the effect of the regulation is to diminish a property holder's fundamental right to exclude, courts have found compensable takings as a matter of course. *See Kaiser Aetna*, 444 U.S. at 179-80.

The second inquiry concerns whether the regulation unfairly forces a subset of the population to bear the burden of providing a public good, as opposed to having the public at large bear that burden. "The Fifth Amendment's guarantee that private property shall not be taken for a public use without just compensation was designed to bar Government from forcing some people alone to bear public

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[6] The government's argument that the COFC somehow erred in also considering the length of the restriction, Br. 27, overlooks not only the flexible *ad hoc* nature of the *Penn Central* inquiry but also this Court's precedent. *See Cienega X*, 503 F.3d at 1287 ("We believe existing takings law requires consideration of the duration of the legislation as part of the takings analysis.").

burdens which, in all fairness and justice, should be borne by the public as a whole." *Armstrong v. United States,* 364 U.S. 40, 49 (1960).

Both inquiries overwhelmingly support the finding of a taking in this case. Taken together, these inquiries compel affirmance; the effects of the statutes here compare in every respect to the traditional expropriation of property for public use.

1. <u>ELIHPA And LIHPRHA Effected A Taking Comparable To A Forced Physical Occupation</u>

ELIHPA and LIHPRHA resulted in the forced occupation of Chateau Cleary by HUD-qualifying tenants. On this point, there can be little debate: *The entire point of the legislation* was to compel owners' continued participation in the HUD programs and thereby "preserve" units for low- and moderate-income tenants.

The Preservation Statutes conscripted CCA to house tenants against CCA's will for 20 additional years. CCA lost completely the right to exclude from Chateau Cleary an entire class of individuals, *i.e.*, low- and moderate-income tenants. CCA lost completely the right to tear down Chateau Cleary and make some other use of the land. CCA lost the right to assign its interest in Chateau Cleary to another party without HUD approval. CCA lost the right to sell the property at a price of its choosing to a buyer of its choosing without HUD approval. And CCA lost the right to rent units at market rates. When one low- or moderate-income tenant left, CCA had no choice but to rent to some other low- or moderate-income tenant at a HUD-approved rate. *See* JA613 ¶6 (regulatory agreement).

CCA nonetheless expects the government to argue in its Reply, as it did below, that CCA retained the discretion to reject the applications of *prospective* tenants on a case-by-case basis and, consequently, could have exercised some right to exclude by letting Chateau Cleary go vacant over time. The government's presumed argument is flat wrong, even putting aside the Morton's Fork nature of it.[7]

First, this Court already has recognized the contrary. In *Cienega VIII*, the Court explained that ELIHPA and LIHPRHA "*intentionally defeated* the Owners' real property rights *to sole and exclusive possession* after twenty years and to convey or encumber their properties after twenty years." 331 F.3d at 1328 (emphasis added). This Court went on to compare the government to a *holdover tenant* and stated that "[w]e agree that the enactment of ELIHPA and LIHPRHA could fairly be characterized as *akin to this type of physical invasion*." *Id*. at 1338 (emphasis added); *see also Palmyra Pacific Seafoods, LLC v. United States*, 561

[7] If CCA had exercised this supposed right to exclude, it *still* could not have put the property to other uses (such as tearing down the complex and building a shopping center). The property would have sat vacant and useless, with no income generation to CCA. According to the government, then, CCA had the right either to forfeit all income from the property or forfeit its fundamental right to exclude others.

F.3d 1361, 1368 (Fed. Cir. 2009) (Preservation Statutes "authorized what amounted to a traditional appropriation of real property rights.").

Second, CCA did not have the ability after enactment of ELIHPA and LIHPRHA to evict all then-existing tenants, place plywood over the windows, and let Chateau Cleary sit vacant and unused for 20 years. Had CCA evicted all tenants and boarded up the complex, such action would have defeated the entire purpose of the transaction between the Norman Brothers and HUD and breached both express terms of the parties' agreement as well as the implied covenant of good faith and fair dealing. This explains why Congress stated that it had "preserved" affordable housing through enactment of ELIHPA and LIHPRHA.

More particularly, *CCA had no ability* to exclude then-existing tenants after enactment of the Preservation Statutes. In this respect, the regulatory agreement required CCA to operate Chateau Cleary "in a manner satisfactory to [HUD]." JA768 ¶ 8(a). Operating Chateau Cleary "in a manner satisfactory to [HUD]" meant, in turn, that CCA had to comply with the panoply of HUD regulations and guidance for affordable housing. JA1063 (Tr.15:14-19) (Norman) (regulatory agreement bound CCA to follow requirements set forth in HUD Handbook). *Inter alia*, through these mandatory rules and requirements:

- HUD compelled CCA to renew the lease of any tenant in good standing. JA1066 (Tr.29:11-13) (Norman); JA1842.

- HUD barred CCA from evicting tenants for minor lease infractions. JA1067 (Tr.30:19-22) (Norman); JA1842-43.
- HUD barred CCA from evicting tenants who refused to pay late charges. JA1066 (Tr.28:24-25–29:1-2) (Norman); JA1840.

ELIHPA and LIHPRHA thus had the effect of abrogating CCA's fundamental right to exclude others. The legislation compelled CCA's continued participation in HUD's affordable housing program and compelled CCA to continue boarding low- and moderate-income tenants.

This physical occupation and abrogation of the right to exclude singularly supports the COFC's finding of a taking. In *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982), the Supreme Court held that the government effected a taking by forcing a landlord to acquiesce in the installation of a small cable box in the apartment building. The law cannot be that a landlord compelled to accommodate one 30-foot cable and two small cable boxes has a compensable takings claim, but a landlord compelled *to house* hundreds of low-income tenants for 20 years does not.[8]

[8] In *Cienega VI*, this Court rejected the argument that ELIHPA and LIHPRHA could result in a *per se* taking under *Loretto*. *Cienega Gardens v. United States*, 265 F.3d 1237, 1248 (Fed. Cir. 2001). However, on appeal, CCA proceeds under *Penn Central*, not a *per se* theory. ELIHPA and LIHPRHA, if not effecting an actual invasion, resulted in something comparable to a physical invasion and confiscated CCA's right to exclude.

And this is not the law. The Supreme Court has made clear that where the character of the governmental action is extraordinary, such as where it implicates fundamental property rights, a taking will be found. Thus, in *Hodel v. Irving*, 481 U.S. 704 (1987), the Court found a regulatory taking where Congress through legislation had restricted claimants' fundamental right of devise. The Court so held notwithstanding the miniscule economic impact to claimants and absence of investment-backed expectations. *Id.* at 714-15; *E. Enterprises v. Apfel*, 524 U.S. 498, 543 (1998) (Kennedy, J., concurring in judgment) (noting the "insignificant economic impact" in *Hodel*). Indeed, after discussing the "dubious" nature of any investment-backed expectations and the insignificant loss of income, the Court stated that it "might well find [the regulation] constitutional" if the Court "were to stop [its] analysis at this point[.]" *Hodel*, 481 U.S. at 716. "But," according to the Court, "the character of Government regulation here is extraordinary." *Id*. "[T]he regulation here amounts to virtually the abrogation of the right to pass on a certain type of property – the small undivided interest – to one's heirs. In one form or another, the right to pass on property – to one's family in particular – has been part of the Anglo-American legal system since feudal times." *Id*.

Here, the right to exclude implicated by ELIHPA and LIHPRHA is even more fundamental than the right of devise at issue in *Hodel*.[9] *See, e.g., Lingle*, 544 U.S. at 539 (right to exclude is "perhaps the most fundamental of all property interests"). As explained in *Kaiser Aetna*, a regulatory takings case applying the *Penn Central* rubric, abrogation of the right to exclude *requires* just compensation. *Kaiser Aetna*, 444 U.S. at 179-80 ("[W]e hold that the 'right to exclude,' so universally held to be a fundamental element of the property right, *falls within this category of interests that the Government cannot take without compensation*.") (emphasis added).[10] *See also Hendler v. United States*, 952 F.2d 1364, 1374 (Fed.

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[9] The prominence that case law has accorded to the right to exclude stands to reason: The right to exclude is basic and fundamental to all other property rights; property cannot be understood in the absence of a right to exclude others from it. *See, e.g., White-Smith Music Publ'g Co. v. Apollo Co*., 209 U.S. 1, 19 (1908) (Holmes, J., concurring) ("The notion of property . . . consists in the right to exclude others from interference with the more or less free doing with it as one wills."); *In re Etter*, 756 F.2d 852, 859 (Fed. Cir. 1985) ("The essence of all property is the right to exclude. . . ."); Shyamkrishna Balganesh, "Demystifying the Right to Exclude: Of Property, Inviolability, and Automatic Injunctions," 31 Harv. J. L. & Pub. Pol'y 593, 627 (2008) (right to exclude "remains a manifestation of the norm of inviolability, on which the entire institution of property is centered").

[10] CCA anticipates that the government will attempt to rely upon *PruneYard Shopping Center v. Robins*, 447 U.S. 74 (1980). There, a shopping center, frequented by 25,000 customers each day, prohibited high school students from distributing political pamphlets. Significantly, the shopping center's prohibition of this pamphleteering violated the California State Constitution, which protects such speech. 447 U.S. at 77-79. The shopping center nonetheless argued that its rights under the First and Fifth Amendments of the Federal Constitution had been violated. Pertinent here, with respect to the shopping center's Fifth Amendment

Footnote continued

Cir. 1991) ("The Government does not have the right to declare itself a co-tenant-in-possession with a property owner. . . . In the bundle of rights we call property, one of the most valued is the right to sole and exclusive possession – the right to exclude strangers, or for that matter friends. . . .").

The Eleventh Circuit's decision in *Cable Holdings* is instructive. *Cable Holdings of Ga., Inc. v. McNeil Real Estate Fund VI, Ltd.*, 953 F.2d 600 (11th Cir. 1992). The issue there concerned whether the Cable Communications Policy Act permitted a cable company to place cable in a multi-unit apartment complex together with already existing video, telephone, and electric wires and cables. The cable company argued that the legislation permitted it to "piggyback" on these other cables and wires based on the owner's prior invitation. The court disagreed. Noting the maxim that legislation should be interpreted so as to avoid

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claim, the Supreme Court emphasized that the shopping center's right to exclude others was only *limited*, not abrogated. In this respect, the shopping center had the right under the California Constitution to limit the students' speech by time, place and manner. *Id*.

In contrast to *PruneYard*, ELIHPA and LIHPRHA eviscerated, not merely limited, CCA's right to exclude others. During the takings period, CCA had no ability to impose time, place, and manner restrictions on its government-imposed tenants. Supreme Court case law has distinguished *PruneYard* on this very ground. *See Dolan v. City of Tigard*, 512 U.S. 374, 393-94 (1994) (distinguishing *PruneYard* because right to exclude was only regulated in that case, not extinguished, and explaining that deprivation of right to exclude established taking).

constitutional difficulties, the court explained that the apartment owner's prior invitation to the other video and utility companies did not mean that the owner somehow had forfeited its right to exclude. *Id*. at 605 ("A property owner's right to exclude another's physical presence must be tenaciously guarded by the courts.").

Here, just like the cable company in *Cable Holdings*, the government wants to piggyback on CCA's *initial invitation* to house HUD-approved tenants. The government would have this Court conclude that it somehow matters that the government is *extending* a physical occupation versus *commencing* an occupation.

There is no principled difference. CCA extended its invitation for a period of 20 years, until it could prepay its mortgage and exit the HUD program, and no longer. The government unilaterally, and in breach of its agreement with CCA, stayed for years after the invitation had expired. This was a physical invasion, and an abrogation of the right to exclude, the same as if Congress had enacted legislation directing landlords of existing conventional properties to henceforth lease units only to HUD-approved low-income tenants, evict all non-qualifying tenants, charge tenants a below-market rate, forbid any other use of the property, and comply with the panoply of HUD regulations. Indeed, this case presents exactly the "different case" noted by the Supreme Court in *Yee v. City of Escondido*. *See* 503 U.S. 519, 528 (1992) (finding rent control ordinance did not effect taking because landowner had the option of using the property for purposes other than a mobile home park but noting that a "different case" would be presented if the government "compel[led] a landowner over objection to rent his property or to refrain in perpetuity from terminating a tenancy").

The bottom line is this: The Preservation Statutes effected, at a minimum, a result comparable to a physical invasion. The Preservation Statutes eviscerated CCA's right to exclude. Under these circumstances, following both *Hodel* and *Kaiser Aetna*, the COFC's finding of a taking must be affirmed.

2. <u>The Preservation Statutes Unfairly Shifted The Burden Of Providing Low-Income Housing To CCA</u>

Separately, the Preservation Statutes had the character of a taking because they unfairly forced CCA, instead of the public as a whole, to bear the cost of affordable housing. "Rather than distributing the burden of providing subsidized housing for thousands of low- and moderate-income families on taxpayers as a whole, the [P]reservation [S]tatutes placed the burden on CCA and other owners who were participating in the HUD programs." A30.

The Preservation Statutes thus effected the classic taking. Congress took the easy route. Rather than appropriate funds for new construction or vouchers, Congress singled out owners to bear this societal cost. *See, e.g., Pennell v. City of San Jose*, 485 U.S. 1, 22 (1988) (Scalia, J., dissenting) ("The fact that government acts through the landlord-tenant relationship does not magically transform general public welfare, which must be supported by all the public, into mere 'economic regulation,' which can disproportionately burden particular individuals."); *Property Owners Assn. v. North Bergen*, 378 A.2d 25, 31 (N.J. 1977) ("A legislative category of economically needy senior citizens is sound, proper and sustainable as a rational classification. But compelled subsidization by landlords . . . is an improper and unconstitutional method of solving the problem.").

3. The Government's Arguments Lack Merit

The government nonetheless argues that ELIHPA and LIHPRHA lacked the character of a taking because the LIHPRHA legislation contained certain "benefits" for owners, and President George H.W. Bush in a signing ceremony described these "benefits" as "generous." Br. 36-37. According to the government, these "generous" benefits indicate that the Preservation Statutes did not unfairly burden owners.

The government's theory ignores that the Preservation Statutes effected a physical invasion and otherwise fails both in law and in logic. This Court already has held that "[t]he character of the government's action [in enacting the Preservation Statutes] is that of a taking" because "the expense [of providing affordable housing] was placed disproportionately on a few private property owners." *Cienega VIII*, 331 F.3d at 1338. According to this Court: "We conclude, *as [a] matter of law*, that the government's actions in enacting ELIHPA and LIHPRHA . . . *had a character that supports a holding of a compensable taking*." *Id*. at 1340 (emphasis added).[11]

Further, the government's reference to statutory benefits only confirms that the Preservation Statutes worked a taking. Congress provided the possibility of "benefits" precisely because it understood that abrogation of prepayment rights unfairly burdened owners with societal costs. *See Whitney Benefits, Inc. v. United States*, 926 F.2d 1169, 1176 (Fed. Cir. 1991) ("An offer to pay would make no sense if nothing were taken."). This Court stated as much in *Independence Park Apartments v. United States*, 449 F.3d 1235, *on reh'g*, 465 F.3d 1308 (Fed. Cir. 2006), a case similarly involving a taking effected by ELIHPA and LIHPRHA. The Court there described the opportunity to receive incentives as "*analogous to a physical taking* in which the government appropriates a plaintiff's property at the outset and then takes steps to mitigate the financial impact of the taking, rather than returning the property to the plaintiff." 449 F.3d at 1247 (emphasis added).

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11 This Court's later decision in *Cienega X* did not overrule the *Cienega VIII* holding (nor could it). As noted by the COFC, this Court in *Cienega X* "did not alter or even address the application of the character factor of the *Penn Central* test." A29. The existence of statutory benefits is not some new fact distinguishing *Cienega X* from *Cienega VIII*.

The government's remaining argument – that the character of the Preservation Statutes is "akin to standard rent control measures," Br. 38 – similarly is foreclosed by Circuit precedent. The Preservation Statutes did not merely restrict the rents charged; they forced CCA to house tenants against its will, abrogating CCA's fundamental right to exclude. This was the entire purpose of the legislation. In *Cienega VIII*, the Court analogized the government to a holdover tenant and stated that "the enactment of ELIHPA and LIHPRHA could fairly be characterized as akin to this type of physical invasion." 331 F.3d at 1338. Rent control statutes do not "require[] the landowner" to continue "rent[ing] [his] land" to tenants. *Yee*, 503 U.S. at 527-28.[12]

* * *

In short, the character of the governmental action overwhelmingly, if not singularly, supports the COFC's conclusion of a taking. The governmental action here was extraordinary. Through ELIHPA and LIHPRHA, the government forced CCA *to house* tenants for a period of 20 additional years, thereby abrogating

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12 Standard rent control statutes do not constitute a taking because such statutes address market failures producing extra-competitive rents. *See Pennell*, 485 U.S. at 20 (1988) (Scalia, J., concurring in part and dissenting in part) ("Since the owner's use of the property is . . . the source of the social problem, it cannot be said that he has been singled out unfairly."). That factor obviously is missing here because ELIHPA and LIHPRHA were enacted to ensure below-market housing for low-income families who cannot afford market rents. Nothing suggests that CCA somehow contributed to the problem of the lack of affordable housing.

CCA's fundamental right to exclude others, and placed the burden of providing affordable housing on owners such as CCA, rather than on the public as a whole. In every respect, the governmental action here had the character of a taking.

B. ELIHPA And LIHPRHA Interfered With CCA's Reasonable Investment-Backed Expectations

The second *Penn Central* guidepost – whether ELIHPA and LIHPRHA interfered with CCA's investment-backed expectations – further confirms that the COFC properly found a taking. In arguing otherwise, the government tellingly avoids any discussion of the appropriate standard of review.

1. <u>This Court Previously Has Addressed The Investment-Backed Expectations Factor In The Context Of The Preservation Statutes</u>

In *Cienega VIII*, this Court made a number of important determinations in holding that the model plaintiffs had reasonable investment-backed expectations. First, the Court rejected the government's argument that a reasonable owner would have expected Congress to abrogate prepayment in the face of a housing shortage. The Court noted that "no pre-existing legislation suggested that prepayment was limited in any way or even that Congress would consider the termination of individual developers' participation in the programs a problem." 331 F.3d at 1352. Second, the Court explained that the relevant documents signed by the government reflect contractual terms that "would be presumptively material for any housing program participant with similar documents." *Id*. at 1349. Third, the Court observed that the "prepayment rights provided, *from all objective analyses*, the *crucial economic incentive* here." *Id*. at 1352 (emphasis added).

The Court addressed investment-backed expectations again in *Cienega X*, questioning in part the Court's prior conclusion that the prepayment rights had been, "from all objective analyses, the crucial economic incentive here." In particular, the Court noted the importance of determining whether the prepayment right was, in fact, "investment backed." *Cienega X*, 503 F.3d at 1289. The Court thus ruled that the COFC on remand should consider whether the prepayment right abrogated by the Preservation Statutes formed "the primary or 'but for' cause of the investment." *Id*. at 1290. The Court also instructed that "[i]n determining whether expectations of prepayment were reasonably investment backed, it is necessary to inquire as to the expectations of the industry as a whole." *Id*.

2. <u>The COFC Properly Followed This Court's Guidance In Determining That The Preservation Statutes Interfered With CCA's Investment-Backed Expectations</u>

The COFC did precisely as this Court had instructed. The COFC made extensive findings of fact in determining that (i) CCA had a subjective expectation to prepay, (ii) this expectation was objectively reasonable, and (iii) the prepayment expectation would have formed the "but for" *and* primary expectation for any reasonable investor in Chateau Cleary. A31-39; 75 Fed. Cl. at 191-94. The COFC addressed each investment expectation and determined that "the prepayment right was paramount" both for CCA *and any reasonable investor* in Chateau Cleary, A33, because, *inter alia*:

- **<u>Cash distributions were minimal, capped, and unpredictable</u>**.

CCA had a right to a *maximum* annual cash distribution of just $12,952, representing 6% of its initial equity investment, for as long as the property remained in the HUD 221(d)(3) program. 75 Fed. Cl. at 180. But, as the COFC found, even this limited distribution was far from a sure thing. Section 221(d)(3) projects such as Chateau Cleary "entailed considerable risk." A34. This risk included the risk that HUD would not grant rent increases corresponding to inflation, as well as the risk of general economic declines. A34.

In fact, *CCA did not receive any cash distributions at all* for the first 12 years of operation, from 1971 until 1983. A35. By 1990, CCA had "received less than half of the potential amount it could receive." A35.

- **<u>The opportunity for a tax shelter was the primary expectation for some, *but not all*, investments in Section 221(d)(3) and Section 236 properties</u>**.

The COFC determined that, while the tax benefits may have driven the investment for *some* properties, in particular for limited partners in certain syndicated properties, tax benefits did not drive all (or anywhere close to all) Sections 221(d)(3) and 236 investments.

The so-called tax benefits refer to the leveraged nature of a Section 221(d)(3) or 236 investment and the ability to take accelerated depreciation to offset other income.[13] A36. However, as found by the COFC, the ability to deduct accelerated depreciation against earned income presented its own risks, including the risk that Congress would change the Tax Code (which it did in 1986, resulting in the foreclosure of several properties, A38), as well as the fact that the tax benefits would disappear in the long term, thereby diminishing long-term gains, A36. "Accelerated depreciation, inherently by its nature, throws off greater tax benefits in the early years, but it eventually generates a tax detriment later, with the tipping point ordinarily coming between years 19 and 22." A36. Other unknown and unknowable factors also influenced the value of any tax benefit, including marginal tax rates (substantially reduced in 1981) and income. JA1069 (Tr.39:19-20) (Norman).

In determining investment-backed expectations, then, geography matters. The then-available tax shelter undoubtedly motivated investments in HUD properties in struggling neighborhoods with little prospect of economic development. But, for those properties with long-term potential, in middle class

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[13] The tax treatment was the same for both conventional and subsidized properties. A36. "The reason the tax benefits were potentially more advantageous for owners in the HUD programs was because of the proportionately lower initial cash investment, which gave the equity owner more leverage." A36.

neighborhoods, the temporary and uncertain nature of the tax shelter (which depended on the vagaries of Congress) presented only a secondary, not a primary, benefit. For these properties, realizing the residual value in the land after 20 years presented the primary investment focus. A37-38.

In making this factual finding, the COFC relied upon, *inter alia*, an industry treatise and prospectuses for syndicated properties. The treatise, a 1972 guide to low- and moderate-income housing, notes that a tax shelter forms "one" of the benefits of ownership of Sections 221(d)(3) and 236 housing. A35. The treatise goes on to state, however, that "[w]here a project is located in a growing suburban or exurban area, it may increase in value over the years, thus creating *substantial residual profits* to the investors upon sale or other disposition." A38.

The prospectuses introduced at trial confirm that, depending on the property, the realization of the residual value after 20 years may have had substantial value for the reasonable investor. At first blush, many of the prospectuses appear not to assign any weight to the prepayment right, listing the nominal value of the subject properties as $1 after 20 years. A36. However, "the details of the prospectuses indicate that the possibility of prepaying the mortgage after 20 years and of realizing an increase in equity was a *considerable benefit*." A36-37 (emphasis added). In this respect, the general partners often retained an interest in the residual proceeds of any refinancing, sale, or other disposition of the property.

"These reallocation provisions suggest that the general partners in three of the six instances were willing to sell short-term tax benefits and dividends *but wanted to retain a significant portion of the long-term benefits* from property appreciation, particularly those following the prepayment date." A37 (emphasis added).

In short, the COFC determined that there was no single investment expectation for the industry. "The evidence thus shows that it is not possible to derive investment expectations of participants in the Section 221(d)(3) and Section 236 programs as a whole." A38. For some properties, the opportunity to obtain a short-term tax shelter drove the decision to invest. For other properties, particularly those located in middle-class areas with potential for growth, the ability to prepay and realize the residual value primarily motivated the investment decision.

- **Any reasonable investor in Chateau Cleary would have focused on recognizing the residual value of the property after 20 years, not temporary and uncertain tax benefits**.

Looking at the Chateau Cleary transaction, then, the COFC found that (i) the Norman Brothers' primary investment expectation was to prepay after 20 years and realize the residual value in the property and (ii) any reasonable investor, just like the Norman Brothers, would have looked to the prepayment right after 20 years and the realization of residual value as the primary investment expectation. Most significant in this regard, the land on which Chateau Cleary was to be built stood straight "in the path of future development in the New Orleans area and an emerging middle-class neighborhood" and "the potential returns very much depended on its geographical location." A37. Supporting this conclusion, the COFC found, *inter alia*:

- HUD touted and sold the prepayment right to the Norman Brothers, therefore selling the ability to recognize residual value in Chateau Cleary after 20 years. 75 Fed. Cl. at 192.
- "[T]he ability to prepay the mortgage after twenty years was an integral part of a long-term strategy." *Id*.
- "The objective reasonableness of the Norman brothers' and CCA's expectations was also evident from the site visit. . . . The property is located in a largely residential neighborhood made up of well-maintained homes. . . . Regional shopping centers and major hospitals are readily accessible. Schools are good, and the area has a relatively low incidence of crime." *Id*. at 193.
- "Chateau Cleary was well built and is well maintained, the structural integrity of its construction having been demonstrated by, among other things, the fact that it suffered virtually no damage as a result of Hurricane Katrina in 2005." *Id*.

- "The Chateau Cleary complex is well positioned to be, and is, a viable competitor in the conventional rental housing market, reflecting its favorable location, design, and construction." *Id*.
- Chateau Cleary recently appraised at $5 million, A39, meaning that the property has more than doubled in value since 1991, appreciating some $3 million, JA556.

Thus, after examining and weighing all of the potential investment benefits, including the availability of cash distributions and tax benefits, the COFC concluded that "Chateau Cleary was similar to properties where long-term results, not short-term gains, were the basis of the owners' expectations." A39. The COFC found that CCA had an investment-backed expectation regarding the right to prepay, and this expectation constituted both the "but for" and "primary" reason for the investment. A39.

3. The Government Improperly Seeks To Have This Court Revisit The COFC's Factual Findings

In the face of the COFC's detailed factual findings, the government improperly attempts to reargue its case in this Court, rather than address the proper standard of review. The government ignores the clear error standard and ignores evidence in the record supporting the COFC's factual findings. *Anderson v. Bessemer City*, 470 U.S. 564, 574 (1985) (appellate court may not disturb trial court's findings of fact even if "convinced that had it been sitting as the trier of fact, it would have weighed the evidence differently"); *id*. ("where there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous").

Rather than establish or explain how the COFC clearly erred in making its detailed factual findings, the government offers unsupported rhetoric. For example, the government remarkably argues that no record evidence supports the COFC's finding that different owners had different expectations, depending on the location of the property. Br. 33. However, as noted above, extensive evidence supports the COFC's factual finding, including the very treatise and prospectuses cited by the government. A36-38 (discussing prospectuses and Edsel & Lane Treatise). The government just overlooked these pages of the COFC's opinion.[14]

The government goes so far as to describe the COFC's findings as "nonsensical," postulating that, if the prepayment right had been "primary," then owners like CCA would have "declined to participate in the section 221(d)(3) program [and] would have been eligible to prepay [the] mortgage from day one –

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14 Common sense also confirms the COFC's findings. Location matters. Maintaining a property as a HUD property may make perfect sense in one neighborhood but not in another neighborhood. Indeed, Mr. Norman explained that he continues to operate another apartment complex as a HUD property because "you could . . . put the Taj Mahal there and you still couldn't get much higher rents . . . ." JA1078 (Tr.76:1-3). Construction and maintenance also matter. Chateau Cleary was well built and well maintained and therefore "well positioned" for the conventional market at year 20. 75 Fed. Cl. at 193.

not after a 20 year wait." Br. 35. This rhetoric underscores that the government has failed to appreciate the COFC's decision, the decisions of this Court, and the record in this case.

Owners in up-and-coming areas – like the area around Chateau Cleary – agreed to participate in the HUD program because of the realization of the residual value after 20 years, when development of the surrounding area could be expected to "catch up" with the apartment complex. For these properties, the HUD programs made perfect sense. The owners could receive more favorable financing (versus operating a conventional property), and a HUD property promised a ready pool of tenants and correspondingly less risk. For properties in economically depressed areas, without substantial prospects for development, the prepayment right had less value. In short, the significance of the prepayment right "very much depended on . . . geographic location," A37, with investors in areas of projected development and neighborhood enhancement assigning primary significance to the prepayment right. A37-38.

Far from being "nonsensical," the COFC's factual findings fit squarely within this Court's precedents. In *Cienega X*, the Court *remanded* for further findings; it did not prejudge any particular conclusion. Far from it, the Court noted testimony in the record from the former Deputy Assistant Secretary of HUD that "the ability to discuss an exit strategy in 20 years . . . was a reason why people would undertake to do [HUD] programs and a reason why people would invest in the programs." *Cienega X*, 503 F.3d at 1290. Similarly, in *Cienega VIII*, the Court explained that the prepayment right formed "from all objective analyses, the crucial economic incentive here." 331 F.3d at 1352.

The government's remaining contention likewise misses the mark. Ignoring the Supreme Court's admonition that "there are no set rules," the government contends that judgment should be vacated because the COFC did not make a specific finding that "a reasonable owner would have declined to participate in the section 221(d)(3) program if the option to prepay first arose after 25 years – rather than after 20 years." Br. 31. The government argues that Congress's restoration of the prepayment right (through HOPE in 1996) somehow has relevance in determining investment-backed expectations in 1971.

Regardless, the record unquestionably supports the conclusion that CCA would *not* have gone forward with the Chateau Cleary transaction had it somehow known that its right to prepay would have been taken by the government for a 5-year period. The evidence at trial indicated that development was expected to reach Chateau Cleary in years 15-20, meaning that losses associated with extending the HUD restrictions another 5 years would have been material. JA1070 (Tr.42-43); JA1069 (Tr.40:11-13). Equally significant, and overlooked by the government, CCA acquired its interest in Chateau Cleary in 1985, a mere 6 years before the anticipated prepayment date in 1991. CCA unquestionably would not have paid the price that it did had it known that the restriction period nearly would be doubled, from 6 years to 11 years. 75 Fed. Cl. at 192.

C. CCA Suffered A Severe Economic Loss

1. CCA Lost More Than $700,000 In Income

The third *Penn Central* factor – economic impact – finally supports and confirms the COFC's finding of a regulatory taking. In *Cienega X*, this Court instructed the COFC to determine economic impact in reference to diminution in the lifetime value of the property. 503 F.3d at 1282. The COFC did precisely this, finding that the Preservation Statutes confiscated fully 18% of the lifetime value of Chateau Cleary. A42. As explained by the COFC, "an 18% economic loss concentrated over approximately five years constitutes a 'serious financial loss.'" A49 (citation omitted).

The COFC unquestionably reached the correct conclusion. In total, CCA lost more than $700,000 in income during the 5-year takings period. This $700,000 loss translates to an economic impact of greater than 80% considering the "return-on-equity" methodology expressly endorsed by this Court in both *Cienega VIII* and *Chancellor Manor*.[15] A40; *see also Rose Acre Farms, Inc. v.*

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[15] *Cienega VIII*, 331 F.3d at 1343 ("loss of return on equity *offers us a way to understand* that . . . the abrogation of the Model Plaintiffs' prepayment rights had

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United States, 559 F.3d 1260, 1275 n.7 (Fed. Cir. 2009) (fact finder may consider different measures of economic impact). More than $700,000 in lost income concentrated in a 5-year period, reflecting an 80% loss for that period (corresponding to an 18% loss in the lifetime value of the property), for a single 104-unit apartment complex, can only be described as a severe loss.

2. The Government's Attempt To Erect *Per Se* Barriers Must Be Rejected

The government nonetheless contends that an 18% loss in the *lifetime value* of Chateau Cleary cannot be deemed serious and, of itself, defeats CCA's takings claim. Br. 19-20. This contention must be rejected for any of several reasons.

First, the case law cited by the government is inapposite. The cited cases, Br. 19-20, all concern *permanent* use restrictions. In the context of a *permanent* restriction, and without considering the character of the regulation or the claimant's investment-backed expectations, an 18% diminution in value may not support a taking. However, in the context of a *temporary* restriction of an *income-producing* property, as here, an 18% diminution in lifetime value, which corresponds to an 80% economic loss during the 5-year period of the taking, fully

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sufficient economic impact to merit compensation") (emphasis added); *Chancellor Manor v. United States*, 331 F.3d 891, 905 (Fed. Cir. 2003) (instructing trial court on remand to "calculate the *rate of return on invested capital* under [LIHPRHA] as implemented by HUD and the reasonableness of that return") (emphasis added).

supports a taking. A49 ("[A]n 18% economic loss *concentrated over approximately five years* constitutes a 'serious financial loss.'") (emphasis added) (citation omitted).

The government's argument that an 18% diminution in lifetime value defeats a takings claim would, if adopted by this Court, do away with virtually all temporary regulatory takings. Because real property has an infinite life, and therefore infinite income potential, a 5-year regulatory taking will seldom cause an economic impact of more than 18% and can *never* cause a lifetime economic impact on the order of 80% or 90%. *See* David W. Spohr, "What Shall We Do with the Drunken Sailor?: The Intersection of the Takings Clause and the Character, Merit, Or Impropriety of Regulatory Action," 17 S.E. Envtl. L.J. 1, 87 (2008) ("[A]pplying even a very high (property-owner friendly) annual discount rate of 15 percent, reaching the 75 percent diminution in value point would require a full decade of delay.").

Supreme Court precedent confirms the fallacy of the government's position. In *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, the Court stated that a 32-month *temporary* moratorium on construction on real property might establish a regulatory taking. 535 U.S. 302, 334 (2002) (plaintiffs "might have prevailed under a *Penn Central* analysis"). Yet, a mere 32-month moratorium on construction would not, under any circumstance, have deprived plaintiffs of 80% or 90% of the lifetime value of their properties.

Moreover, because the government has the power to make any "permanent" taking a "temporary" taking by rescinding the regulation (as was done here, by enactment of HOPE), the government's proposed rule that a plaintiff always must establish an economic loss on the order of 80% or more of the lifetime value of the property would license the government to avoid paying just compensation *in every case*. The government need only withdraw the offending regulation. *Cf. First English Evangelical Lutheran Church of Glendale v. County of Los Angeles*, 482 U.S. 304 (1987) (government may not escape paying just compensation by rescinding regulation).

Second, the notion that an 18% loss in lifetime value *ipso facto* defeats a regulatory takings claim runs contrary to the Supreme Court's decisions in *Hodel* and *Kaiser Aetna*. These cases make clear that the character of the governmental action alone may establish a taking, without regard to the specific quantum of economic impact. *Supra* at 23-26.

The government's argument also runs headlong into various other Supreme Court precedents, concerning regulatory takings, in which the Court never even addressed diminution in lifetime value. *See, e.g., E. Enterprises*, 524 U.S. at 529-31 (plurality) (finding company's potential liability of $50-$100 million a "considerable financial burden" supporting a regulatory taking notwithstanding company's potential right to pursue indemnification and without any discussion or analysis regarding loss in value); *Fed. Power Comm'n v. Hope Natural Gas*, 320 U.S. 591 (1944) (regulations resulting in a confiscatory rate of return require the payment of just compensation, without inquiry into diminution in the lifetime value of the utility); *Penn Cent.*, 438 U.S. at 136 (declining to find a regulatory taking, *inter alia*, because the plaintiff continued "to obtain a 'reasonable return' on its investment," without inquiry into loss in lifetime value).[16]

Third, the government's proposed 18% bar ignores that the *Penn Central* test is "flexible," "*ad hoc*," and concerned with achieving "justice and fairness." 438 U.S. at 124; *see also, e.g., Rose Acre*, 559 F.3d at 1282 (explaining that a court's "objective is to ascertain whether . . . it is unfair to force the property owner to bear the cost of the regulatory action"). Here, the extraordinary character of the governmental action alone compels the finding of a taking. That CCA had

[16] The Supreme Court's focus on a rate-of-return analysis stands to reason: In measuring the economic impact of a regulation on an *income-producing property*, a court should look to the *loss of income* during the period of the challenged regulation. As the COFC astutely observed, the government's position, if allowed to stand, "could allow the government to take an owner's $10 million annual income stream from a $100 million property for four and a half years – yielding the government $45 million – and then assert that the owner had not suffered a severe economic impact because he or she had only been deprived of 45% of the value of his property." 75 Fed. Cl. at 197.

reasonable investment-backed expectations regarding the right to prepay, which expectations formed the primary reason for the investment, only bolsters this conclusion.

Finally, the case law uniformly rejects the proposition that there is some "magic number" of economic impact. *See, e.g., Rose Acre*, 559 F.3d at 1282 ("[T]here is no magic number or formula in takings cases.").

The Court's recent decision in *Rose Acre* is instructive. The Court there determined the economic impact to be 10%. *Id*. at 1275. Yet, the Court did not rule against plaintiff out-of-hand and find that this economic impact was too "small" to support a taking. Instead, the court explained that this degree of economic impact simply did not "favor[]" plaintiff's position. *Id.* at 1283. The court then took pains to address both the character of the governmental action and plaintiff's investment-backed expectations, *id*. at 1275-83, finding that the investment-backed expectations factor supported a taking but that "the character of the government's regulations strongly favor[ed] a non-taking." *Id*. 1283. In balancing all three factors, the court noted that, while plaintiff's investment-backed expectations "favor[ed]" plaintiff, "they [were] not strong enough to be dispositive." *Id*. Thus, the court had to conclude that there was no taking. *Id*. at 1283-84.

Rose Acre categorically defeats the government's proffered bright-line rule that an 18% diminution in value over the *lifetime value* of the property cannot support a taking. The court indicated it might have ruled *in favor* of plaintiff had there been stronger investment-backed expectations, notwithstanding the 10% economic impact *and* the fact that the character of governmental action "strongly favor[ed] a non-taking." *Id*. at 1283. Here, where the character of the governmental action *overwhelmingly* supports a taking, and where CCA had reasonable, investment-backed expectations regarding the property right taken, there can be no doubt that an 18% diminution in the *lifetime value* of the property (equivalent to an 80% economic impact during the actual period of the taking) supports a taking.

3. Consideration Of The So-Called "Sale Option" In LIHPRHA Does Not Reduce The Economic Impact In This Case

The government's alternative contention that the economic impact is 5% after consideration of so-called "statutory benefits" must be rejected out of hand.[17]

[17] While CCA does not rely on this point, CCA respectfully notes that the *Cienega X* Court erred in holding that statutory "benefits" have relevance to the takings inquiry. *See Suitum v. Tahoe Reg'l Planning Agency*, 520 U.S. 725, 748 (1997) (Scalia, J., concurring) ("If money that the government-regulator gives to the landowner can be counted on the question of whether there *is* a taking . . . the government can get away with paying much less.").

More problematic, however, is the fact that here CCA only was presented with the *option* to receive statutory benefits, not an actual benefit (as the plaintiffs

Footnote continued

a. The Government Had The Burden Of Proving Any Value Associated With The Statutory Options

In the first instance, the COFC properly held that the government had the burden of proving any value associated with the ELIHPA and LIHPRHA statutory options. A43; *see also Rose Acre*, 559 F.3d at 1275 (refusing to consider offsetting economic benefits because "the government points to no economic data in the record to support its assertion of offsetting benefits"); *Whitney Benefits*, 926 F.2d at 1175 (rejecting government's argument that coal exchange should be considered in assessing economic impact) ("Though the government asserts that the possibility of an exchange represented a post-SMCRA value, it offered no evidence thereof at

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Footnote continued from previous page

in *Penn Central* actually received the benefit of transferable development rights, *see* 438 U.S. at 137). Here, CCA received no benefit at all. CCA never wanted to sell Chateau Cleary (or agree to further HUD regulation), and therefore CCA exercised its right *not* to sell the property or to seek incentives.

The erroneous nature of the rule set forth in *Cienega X* is best demonstrated by analogy. Suppose CCA sues the United States for $1.0 million in damages. The United States then offers to settle the case for $800,000, but CCA rejects this settlement "option" because it believes that it is entitled to $1.0 million, not $800,000. CCA then establishes liability at trial and proves damages of $1.0 million. Under the logic of *Cienega X*, the economic impact on CCA would only be $200,000 because CCA had the prior "option" of settling the case for $800,000. Of course, this logic cannot be correct because CCA never received (or benefited from) the $800,000 offer. Likewise here, CCA never benefited from the "sale option," and the economic impact should not be reduced. The *actual* economic impact on CCA has no relation whatsoever to the *non-exercised* statutory options.

trial and the segment of its brief devoted to the exchange provision contains not a single record citation.”).

Even if it could be argued, contrary to law and common sense, that CCA had the burden of proving how much any supposed benefit reduced the economic impact in this case, CCA satisfied this burden. CCA’s position throughout has been that the value of these statutory “options” cannot be quantified because, *inter alia*, CCA never availed itself of any options, and therefore to quantify the “value” of the options would be an exercise in speculation.[18] The government’s own expert witness in the first trial testified that any attempt to quantify the value of these options would be “speculative.” JA1005 (Tr.1756:9-17) (Dickey). As a result of this testimony from the government’s own witness, CCA had no need to introduce additional evidence on the speculative nature of statutory options during the trial on remand. JA1055 (incorporating prior trial record).

b. LIHPRHA Did Not Provide CCA With The Opportunity For A Fair-Market-Value Sale At Or Near Its Prepayment Date

On remand, the government’s expert, Dr. Dickey, testified that LIHPRHA and ELIHPA, two different statutes, *collectively* provided an opportunity for CCA

[18] There is no way to quantify the value of “incentives” without knowing, *inter alia*, what incentives HUD was willing to provide, when those incentives would be provided, in what amount, and whether CCA would have been able to get in the funding “queue” before Congress ceased funding all incentives.

to realize a sale of Chateau Cleary in November 1992, or about 18 months after CCA's prepayment date of May 1991. JA1537. Neither Dr. Dickey nor any other government witness attempted to quantify the value of the so-called statutory incentives (which exercise would have been impossible, *see supra* note 18). According to Dr. Dickey, the supposed ability of CCA to sell Chateau Cleary in November 1992 meant that (i) the Preservation Statutes restricted the use of Chateau Cleary for 18 months and (ii) this 18-month restriction period yields an economic impact of 5%. JA1541-42.

Dr. Dickey conflated LIHPRHA and ELIHPA for good reason: He could not otherwise attempt to support the conclusion that CCA suffered an economic impact of just 5%.

LIHPRHA provided zero opportunity for CCA to sell Chateau Cleary at any date at or near CCA's prepayment date of May 17, 1991. The government's own witness, Mr. Kevin East, made this point abundantly clear. According to Mr. East – the former Chief of the Affordable Housing Branch of HUD and Director of the Preservation Division – no property owner could even commence the LIHPRHA sale process until, at the earliest, *April 1992*, when HUD first enacted interim regulations implementing the legislation. A44; JA1088 (Tr.116:5-8); 57 Fed. Reg. 11,992 (Apr. 8, 1992).

Thus, under the rosiest of scenarios for the government – *i.e.*, assuming that CCA filed a notice of intent to sell Chateau Cleary on the very day HUD enacted LIHPRHA's interim regulations, assuming further that CCA actually could find a buyer, and finally assuming, as Dr. Dickey did, that the sale process could be completed in a mere 30 months, CCA would not have completed a sale under LIHPRHA until, at the earliest, *October 1994*, or 3.5 years after CCA's prepayment date of May 1991.

In fact, the restriction period if CCA had pursued the LIHPRHA sale option likely would have been much longer than 3.5 years. *HUD itself* provided an estimate of *41 months* to complete the sale process (11 months more than the 30 months Dr. Dickey assumed and rendering a nearly 4.5-year restriction). JA1901-08; JA1091 (Tr.129:15) (East). And this all assumes that a buyer would have surfaced and finished the transaction. Had CCA been unable to find a buyer, and thus been permitted to prepay, then CCA would have had to house its existing low- and moderate-income tenants *at HUD rents* for a period of *3 additional years* after the prepayment. 12 U.S.C. § 4113(c)(1).

LIHPRHA thus provided no possibility for a sale "at or near the original prepayment date" as required by this Court's precedent. *Cienega X*, 503 F.3d at 1285.

c. ELIHPA Had No "Sale Option"

ELIHPA likewise provided no opportunity for a sale at or near CCA's prepayment date. *ELIHPA provided no sale option at all*. This Court will read ELIHPA and the accompanying regulations in vain trying to find any procedure for an ELIHPA "sale."

The government plays fast and loose in arguing otherwise. According to the government, "ELIHPA and its implementing regulations identify 'actions to facilitate a transfer or sale of the housing' as one incentive available to project owners." Br. 26. The government cites ELIHPA § 224(b) and 24 C.F.R. § 248.231(g) (1990) as support. In fact, these provisions confirm the absence of any procedure for an ELIHPA sale. These provisions provide, in pertinent part:

> SEC. 224. INCENTIVES TO EXTEND LOW INCOME USE.
>
> (b) PERMISSIBLE INCENTIVES. Such agreements may include one or more of the following incentives that the Secretary, *after taking into account local market conditions*, determines to be necessary to achieve the purposes of this title . . . .
>
> (7) Other actions, *authorized in other provisions of law*, to facilitate a transfer or sale of the project to a qualified nonprofit organization, limited equity tenant cooperative, public agency, or other entity acceptable to the Secretary.
>
> * * * *
>
> § 248.231 Incentives to extend low income use
>
> The Commissioner may agree to provide one or more of the following incentives to induce the project owner to extend the low

> income use of the project, *if the Commissioner determines that such incentives are warranted* under the standards in § 248.233 of this part. . . .
>
> (g) Other actions to facilitate a transfer or sale of the housing to a qualified nonprofit organization, limited equity tenant cooperative, public agency, or other entity acceptable to the Commissioner, *such as expedited review of a request for approval of a transfer of physical assets* . . . .

(emphasis added.)

Quite obviously, *nothing* in either the statute or the regulation specifies any process or procedure for achieving a sale "under ELIHPA." To the contrary, the statute specifies that the Commissioner "may" attempt to "facilitate" a sale pursuant to "*other provisions of law*." There are no guidelines or procedures regarding how the Commissioner "may," in his or her discretion, "facilitate" such a sale except for the regulation's suggestion that HUD "may" be able to provide "expedited review" of the sale transaction (whatever "expedited review" means).[19]

The government's suggestion that ELIHPA provided some "sale option" comparable to LIHPRHA is false. In drafting LIHPRHA, Congress actually set forth standards and procedures, limited the discretion of HUD, and included safeguards to protect owners, such as multiple appraisals and timetables for HUD

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19 In fact, HUD *rejected* commenters' suggestions that the regulation provide for specific incentives to purchasers. 55 Fed. Reg. 38,944, 38,949 (Sept. 21, 1990).

to act on a plan of action to sell a property. *See*, *e.g.*, LIHPRHA §§ 213, 216-220, 222. ELIHPA contains none of this.

At trial, Mr. East testified that HUD had internal procedures for this supposed sale option. JA1088 (Tr.115:4-16); JA1095 (Tr.144:4-20). But, after the COFC requested, during the trial, the production of these internal HUD memoranda, JA1137, the documents disclosed no procedures whatsoever. JA1750-78; JA1779-1806. The memoranda do not even raise the *possibility* of selling a property under ELIHPA.

Equally significant, the HUD memoranda confirm that owners did not receive notice of any "sale option." Thus, the May 20, 1988 Memorandum attaches the form letter owners were to receive regarding ELIHPA. JA1757-58. The letter says nothing about an owner's ability to sell its property. Likewise, the form letter owners were to receive after they had submitted a notice of intent does not alert owners to any ELIHPA "sale option." JA1796-97. To the contrary, the letter suggests the absence of such an option. In this respect, an attachment to the letter purports to list all of the available incentives under ELIHPA. JA1804-05. The listed incentives do not include monies or other enticements designed to facilitate a sale, such as the provision of incentives to purchasers. A45 ("Remarkably, however, these memoranda do not even mention a sale option among the potential incentives, which the memoranda purported to set forth *in toto*.”).

The COFC properly concluded that “ELIHPA and its implementing regulations lack any defined procedures, standards, or guidelines for effecting such a sale [and] fail to put the property owner on notice of such a sale option.” A47.

d. *The COFC Properly Rejected The Government’s Evidence As Speculative*

In all events, the COFC did not clearly err in finding that the possibility of a fair-market sale prior to May 1996 (when CCA finally obtained the right to prepay under HOPE) was “too speculative to offset the economic loss imposed on CCA by the prepayment restrictions.” A48. Substantial evidence supported the COFC’s finding, including:

- Only speculation supported the conclusion that a buyer would, in fact, have surfaced. A46-47; A48 (“there was no reasonable certainty that a buyer would be available”).
- Had a buyer surfaced, there may not have been funding from Congress to support the transaction. A46; A48 (“A shortfall in funding for incentives under LIHPRHA also occurred. Three properties in the New Orleans area sought incentives under LIHPRHA and were approved by HUD, but could not be implemented because HUD lacked the requisite funding.”).

- Had a buyer surfaced and had incentives been available, that buyer may have refused to go forward with the transaction for any number of reasons.[20] A47 (noting testimony of Mr. East that "issues arising with a seller or buyer could delay or derail the process").
- "The absence of any defined sale process under ELIHPA also meant there was no assurance that the property owner would receive fair market value." A47.
- The government failed to account for changing land values in arguing that a fair-market transaction was possible. The government's expert, Dr. Dickey, readily acknowledged that property values can "change significantly" over the course of just 18 months. JA1132 (Tr.288:14-15). Yet, Dr. Dickey did not undertake to determine the trend in land values in the New Orleans region in the early 1990s timeframe. JA1132 (Tr.289:5-8). That Dr. Dickey refused to account for changing property values is particularly mystifying given that HUD estimated a period of

[20] If a buyer walked away or did not surface "under ELIHPA," CCA would have had no recourse whatsoever. Under LIHPRHA, CCA could have prepaid if a buyer did not surface or did not consummate the sale but still would have been forced to house existing tenants at HUD rates for a period of three additional years. 12 U.S.C. § 4113(c)(1).

approximately *3 years* (not 18 months) to complete a sale from the time of the appraisals. JA1902-08.

The government's mere disagreement with the COFC's findings, Br. 24-25, does not establish clear error. *King Instruments Corp. v. Perego*, 65 F.3d 941, 945 (Fed. Cir. 1995) (no clear error where trial court's "account of the evidence [is] plausible").

* * *

There are no "set rules" or "formulas" for determining a regulatory taking. The fundamental question is fairness. Here, Congress unfairly burdened CCA with the obligation to house tenants. Congress unfairly burdened CCA by confiscating its primary investment-backed expectation. And Congress unfairly burdened CCA by depriving it of more than $700,000 in income, an 80% diminution concentrated in the 5-year takings period. The Court should affirm the COFC's finding of a taking.

II. THE COFC PROPERLY DETERMINED JUST COMPENSATION

The government's challenge to the COFC's award of just compensation also must be rejected. The pertinent inquiry in assessing damages in any takings case is: "What has the owner lost?" *Boston Chamber of Commerce v. Boston*, 217 U.S. 189, 195 (1910); *see also Kimball Laundry Co. v. United States*, 338 U.S. 1, 6 (1949) ("this amount can be determined only by a guess, as well informed as possible, as to what the equivalent would probably have been . . ."). The loss in this case is evident: income during the 5-year period of the confiscation, from May 1991 through May 1996.

The COFC properly calculated this loss of income by comparing "the difference between the cash flow CCA would have received had it been allowed to prepay its mortgage and operate the property as a conventional apartment complex . . . and the cash flow CCA actually received from operating the property as a HUD-restricted property." A50 (quoting 75 Fed. Cl. at 200).

The government's challenge to this methodology cannot be squared with either the Supreme Court's or this Court's precedents. In *Kimball Laundry*, the Supreme Court utilized this exact approach to measuring just compensation in the context of a temporary taking. 338 U.S. at 7 ("[T]he proper measure of compensation [in a temporary takings case] is the rental that probably could have been obtained."). Likewise, this Court has observed that fair rental value, not diminution in lifetime value, is the proper method to determine just compensation. *Yuba Natural Res., Inc. v. United States*, 904 F.2d 1577, 1581 (Fed. Cir. 1990) ("The usual measure of just compensation for a temporary taking, therefore, is the fair rental value of the property for the period of the taking.").

Indeed, this Court has blessed the methodology employed by the COFC in the very context of ELIHPA and LIHPRHA not once, but twice. In *Cienega VIII*, the Court *directed* that the original damages award in *Cienega III* "be reinstated in the amount awarded therein for each of the four Model Plaintiffs." 331 F.3d at 1353. *Cienega III* awarded damages based on the Model Plaintiffs' lost rental income, just like the COFC did here. *Cienega Gardens v. United States*, 38 Fed. Cl. 64 (1997). Later, in *Independence Park*, the Court again approved of this methodology, directing the COFC to calculate damages based on lost income. 449 F.3d at 1247. In short, the government's contention that the COFC somehow erred by looking to lost rental income, rather than lost market value, finds no support in law. *United States v. Pewee Coal*, 341 U.S. 114, 119-120 (1951) (Reed, J., concurring) ("[I]n the temporary taking of operating properties, market value is too uncertain a measure to have any practical significance.") (citations omitted).

Further, the government fundamentally errs in supposing that the "time of the taking" was May 17, 1991. In fact, the government merely *commenced* the taking in May 1991; it *completed* the taking in May 1996. *Cf. Creppel v. United States*, 41 F.3d 627, 632 (Fed. Cir. 1994) (statute of limitations begins to run only at end of period of temporary taking); *Nemmers v. City of Dubuque*, 764 F.2d 502, 504 (8th Cir. 1985) ("[F]or a temporary taking, the government is responsible for compensating the owner *for the interim* during which it effected the taking.") (emphasis added).[21]

The government's alternative contention that it somehow would be "unjust" not to award just compensation based on the market-value loss as of May 1991 similarly misses the mark. Just compensation does not concern the government's ability *ex ante* "to estimate the cost to the public fisc," Br. 42, but whether the owner has received the "full and perfect equivalent" for the property taken. *Monongahela Navigation Co. v. United States*, 148 U.S. 312, 326 (1893). Here, the COFC took account of what happened during the takings period and compensated CCA for its actual loss – no more, no less.[22]

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[21] The cases cited by the government lack relevance. *See* Br. 40-41. The Supreme Court's decision in *First English* does not address *how* compensation for a temporary regulatory taking should be calculated; instead, the decision merely holds that the Constitution requires compensation for temporary takings. 482 U.S. at 321. This Court's decision in *Yancey v. United States*, 915 F.2d 1534 (Fed. Cir. 1990), likewise provides no support for the government's assertion that the "time of taking" in this case was May 17, 1991, when CCA would have been able to prepay but for enactment of the Preservation Statutes. *Yancey* does not concern or address compensation in the context of a temporary taking but rather a regulation requiring the destruction of healthy turkeys.

[22] To the extent that the government may be challenging the COFC's application of a 10% factor to adjust CCA's losses to the end of the takings period, Br. 43, that argument has been waived because it was not raised below. The argument lacks merit in all events. The COFC concluded that, based on the evidence before it, application of a 10% factor to adjust CCA's losses to the end of the takings period was the only way to make CCA whole. 75 Fed. Cl. at 203-04 ("The ten percent rate reflected a slight premium over the relatively riskless rate of

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<u>**CROSS APPEAL**</u>

I. THE COURT SHOULD HOLD THAT THE GOVERNMENT BREACHED ITS CONTRACTUAL OBLIGATIONS IN ENACTING ELIHPA AND LIHPRHA

CCA cross appeals the COFC's judgment dismissing CCA's separate contract claim for lack of subject matter jurisdiction. Considering itself bound by this Court's decision in *Cienega IV*, 194 F.3d 1231, the COFC held that CCA lacked privity of contract with the United States with respect to the prepayment right. A26 ("[T]he court reluctantly must conclude that the majority's view in *Cienega IV* is controlling.") The Court should find the facts in this case distinguishable from those in *Cienega IV* and vacate judgment for the government on CCA's contract claim. Alternatively, the Court should revisit the *Cienega IV* holding *en banc*.

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8.5 percent to account for the 'opportunity cost' CCA lost due to the preservation statutes. Mr. Norman testified that had CCA received the extra cash flows that market rents would have brought, it would have invested them with the goal of a fifteen to twenty percent annual return.") (citations omitted); *compare Anderson*, 470 U.S. at 574 ("where there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous").

A. The Secured Note, Mortgage, and Regulatory Agreement Constituted Three Parts Of One Single Transaction And Must Be Read Together

Three essential, mutually dependent documents comprised the transaction to operate Chateau Cleary as a HUD property: the secured note, mortgage, and regulatory agreement. A17-18; JA611-24. The secured note, executed between the lender and the Norman Brothers, provided CCA with an express prepayment right after 20 years. JA618-19. HUD endorsed and thereby insured the note. HUD's endorsement to the secured note states that HUD's provision of insurance is "under Section 221(d)(3) of the National Housing Act and Regulations thereunder of the Federal Housing Commissioner." JA619. The referenced regulations provided for prepayment by owners such as CCA after 20 years. *See* 24 C.F.R. § 221.524(a)(1)(ii) (1971).

The regulatory agreement, in turn, bound the Norman Brothers (and later CCA) to operate Chateau Cleary in accordance with HUD rules and regulations, per the Section 221(d)(3) program. For as long as the secured note and mortgage remained outstanding, the Norman Brothers (and later CCA) had to operate Chateau Cleary as a HUD property. JA611. The regulatory agreement expressly references HUD's provision of insurance, accomplished by HUD's endorsement of the secured note. JA611.

Finally, the mortgage, provided by the Norman Brothers to the lender, references and incorporates both the secured note and regulatory agreement. A19; JA620 ("Said Note and all of its terms are incorporated herein by reference."); JA621 ("[T]he Regulatory Agreement, executed by the Mortgagor and the Federal Housing Commissioner, which is being recorded simultaneously herewith, is incorporated in and made a part of this Mortgage.").

The documents on their face, by referencing and/or incorporating each other, thus indicate that they form essential parts of one integrated transaction, not three separate transactions, and must be read together as one agreement. Several points confirm this understanding.

First, HUD structured the entire transaction on pre-printed standard HUD forms. A18. The parties signed these HUD-generated documents *at the same time* in a conference room *in HUD's office* in New Orleans. A18.

Second, the lender sold the mortgage to the Government National Mortgage Association ("Ginnie Mae"). A10 n.3. Significant for present purposes, *HUD then controlled (and still controls) Ginnie Mae as a government-run corporation*. 12 U.S.C. §§ 1717(a)(2)(A), 1723(a). In practical effect, the lender merely acted as a placeholder for Ginnie Mae/HUD in the transaction.[23]

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[23] *See* A10 n.3 (citing authorities); Jerome I. Weinstein, "Housing Subsidies: An Overview," 51 J. Urb. L. 723, 735 (1973) ("These below market interest rate

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Third, "HUD officials highlighted the prepayment right as an inducement to convince the Norman brothers to accept the deal and enter the subsidized housing program." 75 Fed. Cl. at 192. The prepayment right formed the primary investment expectation for the Norman Brothers. A39.

Fourth, the Norman Brothers specifically understood that the note, mortgage, and regulatory agreement formed three parts of one single agreement. A25; JA1068 (Tr.35-37) (Norman).

These facts, coupled with the language of the documents referencing and incorporating the other documents, lead inexorably to the conclusion that the note, mortgage and regulatory agreement form one overarching contract. The Tenth Circuit's decision in *Aspenwood Investment Company v. Martinez*, 355 F.3d 1256 (10th Cir. 2004), considering indistinguishable HUD documents, is directly on point. According to that court, the documents formed "a single, overarching agreement" whereby HUD agreed "to be bound by the terms of all of the parts of the transaction." *Id*. at 1260.

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programs are based on direct loans from the federal government through an agency called [Ginnie Mae]."); Nathaniel S. Keith, "An Assessment of National Housing Needs," 32 Law & Contemp. Probs. 209, 214 (1967) ("The mortgage interest rate is limited to three per cent, the FHA mortgage insurance premium is waived, and the permanent mortgage is purchased by [Fannie Mae].").

The COFC likewise determined that the documents "should be read together to determine what contractual obligations the parties undertook." A21. According to the COFC, reading the documents together as one agreement "gives effect to the fact that the 20-year limit on prepayment contained in the secured note was a provision drafted by HUD that replicated HUD's regulations on prepayment and was used by HUD to induce participation in the program." A21. The government consequently breached the contractual term permitting prepayment after 20 years in enacting the Preservation Statutes. A25 ("[T]his court would find that Congress breached the government's contract with CCA with respect to its prepayment rights when it enacted ELIHPA and LIHPRHA.").

B. This Case Is Distinguishable From *Cienega IV*

The COFC nonetheless "reluctantly" considered itself bound to dismiss CCA's contract claim for lack of privity because of this Court's decision in *Cienega IV*. A19-26. Considering similar documents, and over a dissent by Senior Judge Archer, the majority in *Cienega IV* concluded that, while "part of the same transaction, each document stands alone and is unambiguous on its face." 194 F.3d at 1243. The majority therefore determined that "[t]he documents evidence separate agreements between distinct parties." *Id*. Reading the documents as "separate agreements," the majority held that the owners and the government could not have been in privity with respect to the prepayment right because the prepayment right appeared in the secured note, an instrument only *endorsed* by HUD. *Id*.

The facts in this case are distinguishable from those in *Cienega IV*. In determining whether documents that are part of the same transaction should be read together, the question is factually intensive and one of contract *formation, not interpretation*: Did the parties intend the documents to form one agreement? Here, the answer is a resounding "yes."

The COFC made factual findings not present in *Cienega IV*, including that HUD specifically lured the Norman Brothers to participate in the project by selling the prepayment right; that the Norman Brothers understood that the documents formed three parts of one agreement; that the lender sold the loan to Ginnie Mae, a HUD-run corporation; and, critically, that this prepayment right formed the *primary* investment-backed expectation for any reasonable investor in Chateau Cleary. The parties could not have intended that the United States, *a party to this transaction*, had an unfettered right to prevent the Norman Brothers, another party to the transaction, from enjoying its *primary* investment-backed expectation. As specifically found by the COFC: "[N]one of the documents taken alone would have sufficed to provide the parameters of the agreement." A18-19; *see* 6 Williston on Contracts § 863 (3rd ed. 1970) ("The essential test to determine whether a number of promises constitute one contract or more than one is simple.

It can be nothing else than the answer to an inquiry whether the parties assented to all the promises as a single whole, so that there would have been no bargain whatever, if any promise or set of promises were struck out.”).

C. Alternatively, This Court Should Revisit The *Cienega IV* Holding *En Banc*

In the event that the panel considers itself bound by *Cienega IV*, then the panel should recommend that this case be heard *en banc*. For reasons discussed in significant detail in the COFC’s decision, A19-26, Judge Archer’s dissent, 194 F.3d at 1247, and the Tenth Circuit’s decision in *Aspenwood*, 355 F.3d at 1260, *Cienega IV* deserves to be overruled for any of several reasons.

First, the documents here do not “stand alone.” The prepayment right was not a product of negotiation between the lender and the Norman Brothers but rather a term dictated and sold by HUD. The parties assented to all of the promises as a single whole. A18-19. Nonetheless, the *Cienega IV* majority apparently concluded that, with respect to HUD’s endorsement of the secured note, HUD merely acted as a surety, not as a contractual party. But no “surety” ever would bar its principal from paying a note in full, thereby extinguishing the surety’s liability, as the government did in this case. The government quite obviously had several interests in this transaction, and these interests only can be understood by reading the documents together as a single agreement. A25.

Second, *Cienega IV* conflicts with longstanding law, including Circuit precedent. The majority concluded that the relevant documents had to "stand alone," principally because they were unambiguous and executed by "distinct parties." *Cienega IV*, 194 F.3d at 1243. But this is not the pertinent question. The question is fact driven and asks whether, as a matter of contract *formation*, not interpretation, the parties intended the documents to form a single, overarching contract. *See, e.g., Joy v. St. Louis*, 138 U.S. 1, 38 (1891) (two tripartite agreements and a deed "constituted a single transaction, relating to the same subject matter, and should be construed together in such a way as to *carry into effect the intention of the parties*, in view of their situation at the time and of the subject-matter of the instruments") (emphasis added).

In determining whether different writings form a contract, the documents need not refer to the other documents or be signed by the same parties. 5 Corbin on Contracts § 24.21 (rev. ed.) ("[T]he [t]erms of agreement may be expressed in two or more separate documents . . . [regardless of] whether the documents are all executed by a single party or by two or more parties, and if some of the documents are executed by parties *who have no part in executing the others*.") (emphasis added). This Court expressly has held as much. *See Home Savings of Am., FSB v. United States*, 399 F.3d 1341, 1349 (Fed. Cir. 2005) (party in privity with government *notwithstanding the fact that the party did not execute the pertinent* *contract*) ("Although Ahmanson did not itself sign the Assistance Agreements, the [COFC] properly focused on a set of 'larger transaction[s].'").

Third, *Cienega IV* does not address the central role played by Ginnie Mae in these transactions. Ginnie Mae, *a HUD-administered government corporation*, typically entered into commitment agreements with the lenders to purchase the notes at issue, often long before the transaction closed. *See, e.g.*, David L. Krooth and Jeffrey G. Spragens, "The Interest Assistance Programs – A Successful Approach to Housing Problems," 39 Geo. Wash. L. Rev. 789, 794 (1971) ("BMIR loans were made by conventional lenders at a market rate during construction, but there was an advance commitment for the purchase of a three percent mortgage by [Ginnie Mae] upon the project's completion. The net effect was that *the federal government furnished mortgage funds* at an interest rate below the market. . . ."); (emphasis added). The lender thus had a "placeholder" role in the transaction, generating its fees and then selling the loan to Ginnie Mae/HUD, with HUD structuring the overall deal and agreeing to be bound by all of the deal documents. This explains why all documents appear on *HUD forms*, not on forms generated by the respective lenders.

For these and other reasons explained in detail by the COFC, the panel majority incorrectly decided *Cienega IV*, and the full Court should decide the contract issue in this case *en banc*.

CONCLUSION

For all the above reasons, the Court should affirm the COFC's judgment finding a taking and awarding just compensation. Separately, the Court should vacate the COFC's judgment dismissing CCA's contract claim. The Court should instruct the COFC to enter judgment for CCA on the contract claim.

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Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that, on this 16th day of September 2010, I caused twelve copies of the foregoing Principal and Response Brief of Plaintiff-Cross Appellant CCA Associates to be delivered by hand to:

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CERTIFICATE OF COMPLIANCE WITH TYPE-VOLUME LIMITATION, TYPEFACE AND TYPESTYLE REQUIREMENTS

I hereby certify that this brief complies with the type-volume limitation set forth in Federal Rule of Appellate Procedure 28.1(e). This brief contains 16,498 words, excluding the parts of the brief exempted by Federal Rule of Appellate Procedure 32(a)(7)(B)(iii) (according to the word count feature of Microsoft Word 2007). This brief utilizes 14-point, proportionately spaced, Times New Roman font and was prepared using Microsoft Word 2007.

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