New Eminent Domain Case Clarifies "Good Faith" Test for Determining Litigation Expenses

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In California eminent domain cases, government agencies must take care in formulating the final offer of compensation they make before trial. If the court concludes after trial that the agency's offer was unreasonable – and that the property/business owner's final demand was reasonable – the property/business owner is entitled to an award of litigation expenses, including attorneys' fees. (See Code Civ. Proc. § 1250.410.)

How one analyzes "reasonableness" once the jury issues its verdict has been the subject of myriad court opinions. An October 29 decision from the California Court of Appeal, *Tracy Joint Unified School Distract v. Pombo*, adds to that body of law. *Pombo* makes clear if the final offer misses the mark, the agency is subject to an award of litigation expenses unless it can show that exceptional circumstances led to the disparity between the final offer and the verdict. Mere good faith belief in the agency's appraiser's conclusion will not suffice.

Background

In *Pombo*, the school district filed an eminent domain action to acquire 61.6 acres in the middle of a 231-acre parcel of raw land. The agency's appraiser valued the taking at about $3 million. The property owner's appraiser valued it at more than $12 million. The discrepancy arose largely from different opinions as to the property's development potential.

When it came time to exchange the final offer and demand, the agency stuck to its guns, offering only $100,000 more than its appraiser's value. The property owner, on the other hand, split the difference, making a demand of around $8 million. The jury returned a verdict nearly matching the owner's final

demand. The owner then sought a $574,000 award of litigation expenses, contending its final demand was reasonable and the agency's offer was unreasonable.

The trial court focused on the standard, three-factor test:

1. The amount of the difference between the offer and the compensation awarded;
2. The percentage of the difference between the offer and the award; and
3. The good faith, care and accuracy in how the amount of the offer and amount of demand, respectively, were determined.

(See, e.g., *Los Angeles County Metropolitan Transportation Authority v. Continental Development Corp.* (1997) 16 Cal.4th 694, 720; *People ex rel. Dept. of Transportation v. Acosta* (2009) 178 Cal.App.4th 762, 773.) The trial court easily concluded that the agency failed the first two factors. The verdict was nearly $5 million more than the agency's offer, and the offer represented only 39 percent of the jury's verdict.

However, the court concluded that the agency was saved by the third factor, concluding that the good faith, care and accuracy it exhibited insulated it from an award of litigation expenses. The trial court particularly focused on (1) the difficulty of the appraisal assignment given the rapidly changing real estate market, and (2) difficulty in predicting which expert would be more credible before the trial began.

The Appeal

The Court of Appeal reversed. As to the first factor, the Court noted that the gross dollar disparity between the agency's offer and the jury's verdict "is striking – and ‘certainly indicative of an unreasonable offer,'" especially given that the agency only offered a token amount above its appraiser's value conclusion.

With regard to the second factor, the Court explained that while no precise mathematical formula exists, precedent suggests that offers of less than 60 percent of the verdict are usually unreasonable, while offers more than 85 percent are usually reasonable. In *Pombo*, the agency's offer amounted to less than 40 percent of the compensation awarded, a stark contrast with the owner's demand, which was virtually identical to the verdict.

Turning to the third factor, the Court distinguished the cases that had found against the agency on the first two factors but nonetheless denied recovery of litigation expenses. In each of those cases, the parties were confronted with a significant legal issue or an issue of first impression that ultimately swayed the courts to conclude that the condemning agency had acted reasonably in making its offer despite what the numbers suggested.

For example, in *Escondido Union School Dist. v. Casa Sueños De Oro, Inc.* (2005) 129 Cal.App.4th 944, the agency missed badly in its final offer (the verdict was more than double the offer and higher even than the owner's final demand). The Court of Appeal nonetheless upheld the denial of litigation expenses since the discrepancy arose largely from an issue of first impression; namely, whether mobile homes qualify as "improvements pertaining to the reality," making their loss compensable under the law.

Similarly, in *Moulton Niguel Water Dist. v. Colombo* (2003) 111 Cal.App.4th 1210, the court upheld the denial of litigation expenses where the agency's refusal to credit the owner's appraisal reflected a good faith (but ultimately erroneous) belief that the owner was not eligible for an award of severance damages.

Here, however, "[t]here was no tricky legal issue or unusual circumstance that made the offer difficult to formulate. The jury was confronted with a straightforward conflict between two appraisers who advocated vastly different approaches to the appraisal process." The Court concluded that agency evinced an "arrogant and unyielding approach to settlement negotiations" by "audaciously" assuming that the jury would totally reject the owner's appraisal.

In the absence of a "tricky legal issue or unusual circumstance," the Court of Appeal had no difficulty concluding that a fee award was warranted:

> [T]he monetary difference between the offer and the award was enormous, the property owners' offer was extremely reasonable and the [agency] made no effort to show good faith by tendering an offer that gave serious consideration to an adverse appraisal that was several times larger than that of its expert.

Conclusion

Agencies should have confidence in their appraisals. However, where a substantial difference between the appraisals exists, strictly adhering to the agency's appraisal figure in making the final offer does not evince the good faith spirit of compromise that should be expected of a reasonable condemnor.

In the past, some agencies have escaped liability for litigation expenses through citation to *Casa Sueños* and others like it, claiming their "good faith, care and accuracy" trumped the mathematical results. *Pombo* provides an important cautionary tale: cases like *Casa Sueños* do not provide protection where the agency's claim of "good faith" amounts to even well-intentioned reliance on the agency's own appraisal, where that reliance is coupled with a disregard of the owner's appraisal and a general unwillingness to consider the possibility that the jury might view the case through eyes different than its own. If the agency wants to "stick to its guns," it better (1) have a weighty issue of law behind its decision, or (2) expect to pay litigation expenses along with a higher-than-anticipated verdict if it rolls the dice and loses.

Rick E. Rayl is the Chair of Nossaman's Eminent Domain and Valuation Practice Group and a member of the Firm's Real Estate Practice Group. Mr. Rayl is an experienced trial attorney dealing with eminent domain, inverse condemnation, and other real estate and business disputes. He is also editor of the blog, "California Eminent Domain Report." He can be reached at rrayl@nossaman.com or 949.833.7800.

Bradford B. Kuhn is a member of Nossaman's Eminent Domain and Valuation Practice Group and specializes in real estate and business litigation with an emphasis on eminent domain, inverse condemnation, and other real estate disputes. He can be reached at bkuhn@nossaman.com or 949.833.7800.