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DOES A WILLIAMSON ACT CONTRACT HAVE CONSTITUTIONAL STATUS?

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"Nowhere is the confusion between legal and moral ideas more manifest than in the law of contract."[2]

J. Oliver Wendell Holmes

I. INTRODUCTION

This Article will explore the legal nature of contracts made between California counties and landowners ("Act Contracts") pursuant to the Land Conservation Act of 1965 ("Williamson Act" or the "Act").[3] By analyzing the different ways Act Contracts are modified, cancelled, rescinded, or breached, this Article will show that Act Contracts are exactly what they claim to be – mere contracts. Accordingly, they neither have nor deserve a higher status than ordinary contracts and do not enjoy

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[2] 2-7 CORBIN ON CONTRACTS § 7.12, IS A CONTRACTUAL DUTY ALWAYS ALTERNATIVE? (*citing* Oliver W. Holmes, Jr., *The Path of the Law*, 10 HARV.L.REV. 457, 462 (1897)).

[3] CAL. GOV. CODE, §§ 51200 et seq.

a "Constitutional status" sometimes claimed by participating public agencies and the California Department of Conservation ("Department").[4] This Article will show the original intent of the Act was not to impart Constitutional status on Act Contracts and that the purposes of the Act are not served by claiming otherwise.[5]

Section II of this Article begins with a discussion of the intent of the drafters and dual purposes of the Act: conservation of farmland and subsidization of farming. Section III discusses the nature of the Act Contract and the 1966 Constitutional amendment and subsequent case law, which is the origin of the erroneous claim of Constitutional status. Section IV considers the consequences to the landowner if the Act Contract has Constitutional status. First, subsequent legislation by the participating public agency modifying the Act Contract may violate the Contracts Clause of the United States Constitution absent a high showing of public necessity. Second, manipulating the cancellation criteria in Government Code Section 51282 to prevent legitimate cancellations is unreasonable. Third, the definition of material breach in Government Code Section 51250 is arbitrary and overbroad. Fourth, the liquidated damages specified by Government Code Section 51250 in the event of material breach are grossly unreasonable. Fifth, the alleged egregious violations which provided the motivation to enact Government Code Section 51250 are actually trivial. Finally, Section V discusses the danger of confusing contract with tort and the consequences that result.

II. INTENT OF THE DRAFTERS AND PURPOSES OF THE ACT: CONSERVE AGRICULTURAL LAND AND SUBSIDIZE FARMING

The Act meets two societal objectives: the express purpose of conserving open and agricultural land, and the farmer's need for financial

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[4] James Faulk, *County declares ruling could make act 'unworkable'*, EUREKA TIMES STANDARD, Nov. 6, 2005, at 1.

[5] A number of articles have been written on Williamson Act issues, including two in recent years from the San Joaquin Agricultural Law Review. In 1997, Kathleen A. McGurty described the Fresno County battle over an attempted rezone of 340 acres of Act land into 20 acre parcels. McGurty considers the attempted rezone in light of the Agricultural Land Stewardship Program, which provides additional funding for conservation easements, and whether they may be a more effective solution. *See* Kathleen A. McGurty, Comment, *The State of Agricultural Land Preservation in California in 1997: Will the Agricultural Land Stewardship Program Solve The Problems Inherent in the Williamson Act?* 7 S.J.AGRI.L.REV. 135 (1997). In 1999, former Staff Counsel for the State of California Department of Conservation Dale Will discusses S.B. 1240 and S.B. 1182, in the context of an overview of the Act, its Constitutional roots and need for enforcement. *See* Dale Will, *The Land Conservation Act at the 32 Year Mark: Enforcement, Reform, and Innovation*, 9 S.J. AGRI. L. REV. 1 (1999).

assistance. Subsidizing farmers is not an express purpose of the Act, but the practical effect of assisting farmers is an important state interest that cannot be ignored. At its essence, the Act Contract is merely an agreement between the state, via a county or city, and the landowner to mutually meet the above objectives for a ten-year term. Unfortunately, solutions to these farming and environmental problems, creates problems in housing supply and housing costs.

Congress has found that agricultural land and the ability to produce food is a natural resource and is necessary for the continued welfare of our country.[6] This is due in part to the irrevocable conversion of agricultural land to other uses which may threaten production, export ability, or the economic base of rural areas.[7] As a result, California's Williamson Act is not unique in our nation. Nearly every state has passed some form of tax-benefit legislation to alleviate development pressure on farmland.[8] Like the Act, most states attempt to tax farmland that would increase in value due to encroaching development according to its use, rather than its potential sale value.[9] Some think tanks and universities feel the tax breaks have been a welcome relief for working farmers, but have done little to slow the pace of development.[10] In light of the fact that California housing development falls over 100,000 units short of meeting the housing need, perhaps the Act is more successful at conserving agricultural land than critics would like to admit.[11]

A. Tension Between Agricultural Land for Food or Housing

In testimony before the Senate Agricultural and Water Committee in 2003, John Gamper, the Director of Land Use and Taxation for the California Farm Bureau Federation, stated that "farmers are struggling and they're frustrated by their rising costs and declining incomes."[12] Regulatory burdens, the collapse of international markets, trading sanctions, and fixed commodities prices prevent farmers from passing their costs to

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[6] 7 U.S.C. § 4201 (2007).

[7] *Id.*

[8] Allen G. Breed and Martha Mendoza, *Attempt To Save Farm Acres Aids Developers*, ASSOCIATED PRESS, Apr. 4, 2004.

[9] *Id.*

[10] *Id.*

[11] New Communities: A Strategy for Building California's Future – The Principles and Policies of California Homebuilders [hereinafter Policies and Procedures of CBIA] 3.

[12] *Ag Land Preservation: The Future Of Our Fields: Interim Hearing Before the Senate Agriculture Comm.*, 2005-2006 Sess. (Cal. 2005) (statement of John Gamper, Director of Taxation and Land Use, California Farm Bureau Federation).

consumers.[13] Clearly, "[t]he unwritten social contract that farmers can earn income in exchange for managing the environment to produce a safe and secure food supply is in grave jeopardy."[14]

The struggle to farm is not new. In addition to the conservation of open space and agricultural land, John Williamson and other drafters also intended to save farmers money.[15] Today, farmers directly benefit from the tax savings brought about by the Act. Over one-third of California's farmers would not be in business without the Act.[16] There are currently over 16 million acres of land enrolled in the Act, which generates about $40,000,000 in reimbursement funding from the state budget to participating counties.[17] This is the highest participation for the lowest cost of any state program.[18] As recently as 2003, enrollments in the Act were increasing and nonrenewals were slowing.[19] That same year, former Governor Gray Davis proposed cutting the Act reimbursement payments to counties from the state budget.[20] However, due to the relatively small amount spent compared to the overall budget and the emphatic opposition from farmers, the funding was left intact.[21]

Despite farmers' obvious enthusiasm for the Act, significant amounts of land are being converted to new uses. For context, consider that in 1946, more than 267,000 acres--54% of Orange County's entire land area--were devoted to farming and ranching.[22] In 2004, only 30,708 acres of Orange County's land was in agricultural production and a mere 13,482 acres of non-grazing land was available for production of agricultural goods.[23] Now that Los Angeles is knocking on the back door of Bakersfield, many San Joaquin Valley residents believe the area is ripe

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[13] *Id.*

[14] *Id.*

[15] Telephone Interview with Bill Geyer, Geyer and Associates Consulting, former aid to State Assembly member John Williamson (1964-1968), in Sacramento, Cal. (Feb. 15, 2008).

[16] Telephone Interview with John Gamper, Director of Taxation and Land Use, California Farm Bureau Federation, in Sacramento, Cal. (Dec. 21, 2005).

[17] *Id.*

[18] *Id.*

[19] Letter from Erik Vik, Assistant Director, California Department of Conservation, to Madera County Assessor, (July 14, 2003) (on file with San Joaquin Agricultural Law Review).

[20] Opinion, *Davis Must Make Cuts*, ALAMEDA TIMES STAR, Mar. 13, 2003, at 1.

[21] Jake Henshaw, *Budget Raises Sales Tax*, VISALIA TIMES DELTA, May 15, 2003, at 1.

[22] Gary Jarlson, *Plowed Under By Development - Farming Fading in Orange County*, LOS ANGELES TIMES, June 23, 1985, at 1.

[23] California Department of Conservation Division of Land Resource Protection Orange County 2004-2006 Land Use Conversion, *available at* http://www.conservation.ca.gov/DLRP/fmmp/pubs/2002_2004/conversion_tables/ora0204_web.xls.

for wide-ranging sprawl.[24] Mediterranean-style houses, minimarts, and power centers are edging out crops and acreage along the San Joaquin Valley's 450 miles of Highway 99.[25] California currently converts about 2.5 acres of irrigated land each hour to non-agricultural uses in the San Joaquin Valley.[26] The San Joaquin Valley will be a fast-growing region for several decades; its population is projected to swell by about 130% to over 1.1 million by 2050.[27]

As a response to this growth, many San Joaquin Valley counties and cities are amending their general plans to reflect a preference for development on non-prime farmland and to establish greenbelts of conservation easements between cities.[28] For example, Merced County updated its general plan in 2000 and specified its preference for "productive" agricultural land.[29] "Productive" agricultural land, within the meaning of the Merced County General Plan, has good quality soil.[30] This is consistent with the intent of John Williamson and the original Act.[31]

These numbers do not mean the Act is not serving its purpose. Nonrenewals of Act contracts are being offset by the enrollment of five new counties into the Act for the first time since 2000.[32] Now, all but five California counties participate in the Act.[33] Despite development pressure, the Act as a whole has actually increased its enrollment from 15,812,511 acres in 1996-1997 to 16,560,132 acres in 2003-2004.[34] This is a strong indication the Act has enough importance to farmers to continue to be a piece of California's agricultural economy.

The primary reason for the conversion of farmland is the accommodation of new residents and commercial enterprises to support them. The U.S. Census Bureau lists California as the second fastest growing state in the nation from 2000 to 2007.[35] The California Building Industry Asso-

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[24] Kevin Frye, *Voices of the Valley*, FRESNO BEE, May 15, 2005, at 1.

[25] Mike Lee, *Growing Smaller*, SACRAMENTO BEE, Dec. 14, 2004, at 1.

[26] *Id.*

[27] *Id.*

[28] Merced County General Plan Ch. I Introduction, p. vii; Ch. VII Agriculture Element, p. VII-1; Fresno Local Agency Formation Commission (LAFCO) Executive Officer's Report October 10, 2007, p. 6.

[29] Merced County General Plan, *supra* note 28, at Ch. I Introduction, p. vii.

[30] Merced County General Plan, *supra* note 28, at Ch. VII Agriculture Element, p. VII-1.

[31] Interview of Geyer, *supra* note 14.

[32] Juliana Barbassa, *Update 1: Farmers Giving Up on Farmland Protection,* Associated Press, Jan. 18, 2006.

[33] *Id.*

[34] State of California Department of Conservation Williamson Act Program Reports and Statistics, *available at* http://www.conservation .ca.gov/dlrp/lca/stats_reports.

[35] Cumulative Estimates of Population Change for the United States, Regions, States, and Puerto Rico and Region and State Rankings April 1, 2000 to July 1, 2007, *available*

ciation ("CBIA") refers to land as "the basic raw material necessary for California's new home construction."[36] Between July 1, 2003 and July 1, 2006, over 431,087 new California residents created increased demand for housing, schools, social services, retail services, and business.[37] To accommodate these new residents, over the last sixteen years California has only produced an average of 135,000 new housing units per year when 240,000 were needed.[38] In the context of the last sixteen years, this under-production has led to higher demand and significant increases in housing prices. To make the situation worse, our regulatory environment is a myriad of land policies, environmental restrictions, and consumer sensitivity which creates complexity and increases cost for developers.[39] As a result, developers pass these costs on and California has become a relatively unaffordable place to live.[40] Only one in seven California families can afford to buy a home in most places.[41] Nearly all of the nation's top twenty-five least affordable cities are in California.[42] Housing--and the allowance of land upon which to build--is as much a legitimate interest for the residents of California as the preservation of farmland and food supply.

B. Intent of the Drafters

The basic Act Contract provides for a ten-year agreement not to improve the land in a manner unrelated to agriculture. The practical effect is not to permanently preserve agricultural land and put a castle-moat around agriculture as would a conservation easement. Rather, the Act slows down the conversion of agricultural land to improved uses and provides a subsidy for those using the land in an agricultural or open space manner.[43] Despite the Act's temporary nature and resulting criticism from those believing it lacks serious effect, it provides an important aid to farmers as well as a delay to developers seeking conversion to new

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at http://www.census.gov/popest/states/tables/NST-EST2005-02.xls California Population change estimates by county.xls.

[36] Policies and Procedures of CBIA, *supra* note 11, at 6.

[37] Cumulative Estimates of Population Change, *supra* note 35, at 3.

[38] *Id.*

[39] *Id.* at 4.

[40] *Id.* at 5.

[41] *Id.*

[42] *Id.*

[43] Assembly Committee on Natural Resources AB 1492 (Laird) May 13, 2003; "[t]he Williamson Act is one of several tools available *to slow the rate of farmland loss* in California; it currently restricts about 16 million acres." (italics added) Will, *supra* note 5, at 35.

uses. The question is: Does the societal benefit of temporarily conserving open space outweigh the societal burden of increased housing costs? The Department and, at times, participating public agencies claim that an Act Contract has Constitutional status.[44] Constitutional status ultimately means that Act Contracts are more difficult or impossible to cancel, rescind, or breach. This is not what the Act's drafters intended.

The drafters felt that the Act would work under the Constitutional framework existing at that time.[45] In 1965, many landowners held deeply under-assessed property and there was an effort underway to push county assessors to accurately reassess that land to generate more property tax revenue.[46] Once the Act was passed, a huge number of enrollments occurred to keep the lower tax status.[47] In response, many county assessors resisted the idea of using an assessment method other than the highest and best use method.[48] The assessors needed some legal authority to alleviate the pressure for reassessment and value the land by its actual use (an income valuation model based on farming income). Accordingly, the assessors were a driving force behind Article XVIII of the California Constitution, which was adopted in November, 1966.[49]

III. NATURE OF AN ACT CONTRACT AND CLAIMS OF CONSTITUTIONAL STATUS

A. The Phrase 'Enforceably Restricted' Does Not Vitiate Landowners' Rights

Despite its laudable reputation with farmers for providing them much-needed tax breaks in a struggling industry, the Act has received criticism in its forty-plus year existence for a perceived lack of effectiveness and enforcement.[50] The California Supreme Court and the Department have done their part in recent past to enforce the Act. The legal theory they cite is that an Act Contract is not subject to certain fundamental princi-

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[44] Faulk, *supra* note 4.

[45] Telephone Interview with Bill Geyer, Geyer and Associates Consulting, former Aide to State Assembly Member John Williamson (1964-1968), in Sacramento, Cal. (Feb. 15, 2008).

[46] *Id.*

[47] *Id.*

[48] *Id.*

[49] *Id.* CAL. CONST. art. XVIII, § 8 (Deering, LEXISNEXIS, 2007) Former Sections, note 1.

[50] McGurty, *supra* note 5, at 156.

ples of contract law because of its unique "constitutional nature."[51] Constitutional nature or status, as used by the Department, often has the loaded meaning that the Act Contract is subject to the principles and ideas that serve the Department and not to ordinary contract law. The position is generally grounded on article XIII, section 8 of the California Constitution, formerly article XVIII, which was added in 1966, shortly after the passage of the Act.[52] Article XVIII, section 8 provides:

> To promote the conservation, preservation and continued existence of open space lands, the Legislature may define open space land and shall provide that when this land is *enforceably restricted,* in a manner specified by the Legislature, to recreation, enjoyment of scenic beauty, use or conservation of natural resources, or production of food or fiber, it shall be valued for property tax purposes only on a basis that is consistent with its restrictions and uses. (italics added)[53]

In addition to the above constitutional language, a statement made by the majority of the California Supreme Court in *Sierra Club et al. v. City of Hayward, Y. Charles Soda, et al,* 28 Cal.3d 840 (1981) ("*Sierra Club*"), provides:

> If cancellation were a simple matter of showing that the restricted land is now more valuable for a developed use, we doubt whether Williamson Act Contracts could qualify as "enforceable restrictions" making the land eligible for taxation on use value rather than market value under the Constitution.[54]

After *Sierra Club*, the legislature amended the Williamson Act via the Robinson Act which was passed in direct response to *Sierra Club.*[55] It provided a window cancellation period within which a landowner could remove land from the Act. Subsequent challenges to the Constitutional validity of the window cancellation period were heard in the case of *Sherman Lewis et al. v. City of Hayward, Y. Charles Soda et al.* 177 Cal.App.3d 103 (1986) ("*Lewis*").[56] In *Lewis*, the First District Court of

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[51] Telephone Interviews with Kyle Nast, Staff Counsel, California Department of Conservation, Sacramento, Cal., (Oct. 5, 2005 and Dec. 16, 2005).

[52] *See supra* note 49.

[53] CAL. CONST. art. XIII, § 8 (Deering, LEXISNEXIS, 2007).

[54] Sierra Club et al. v. City of Hayward, Y. Charles Soda, *et al.,* 28 Cal.3d 840, 855 (1981) [hereinafter Sierra Club].

[55] Friends of East Willits Valley v. County of Mendocino, 101 Cal.App.4th 191, 204-205 (2002) [hereinafter Friends].

[56] "Our high court has held that a Williamson Act contract does not meet the constitutional standard if it can be cancelled solely upon a showing that the land is now more valuable for development." (Sierra Club, *supra,* note 54 at 855.) "The obvious reason for this conclusion is that a restriction to agricultural use, created to control urban development, would have little enforcement value if it could be cancelled whenever development drew near. Thus, even if section 8 allows the Legislature to define restrictions, it

Appeal found the window cancellation period invalid and reversed the trial court.[57] The *Lewis* court found the Legislature could not determine the definition of "enforceable restrictions" but only the manner in which land could be restricted.[58]

B. An Act Contract may be Enforceably Restricted and Still be Breached or Cancelled

Of course cancellation of an Act Contract is not a simple matter of showing that the restricted land is now more valuable for a developed use. Article XIII, section 8 provides that an appraiser, such as a county assessor, may not value land in a manner other than its highest and best use without some actual restriction on the land.[59] The actual restriction on the land is the agreement not to improve the property in a manner unrelated to agriculture. The enforceability of that restriction arises as a result of mutual obligations on each side in order to be consideration for each other.[60] An Act Contract is an enforceable bilateral contract. Like other contracts, the Act Contract is "enforceable" whether it is performed, cancelled, or breached.[61] The Legislature has specified procedures to address performance to term, cancellation, and breach within the Act.[62] Both landowner and state give obligations and receive benefits whether an Act Contract is performed, cancelled, or breached. To say a landowner always receives lower property taxes without returning some benefit to the state is incorrect. Some cases are documented where the landowner receives no tax savings at all.[63] In those situations, Act landowners have given the state the benefit of not improving their land for the ten-year term without receiving any resultant benefit.[64] Consider, for example, each of the three possible scenarios: performance; cancellation; and breach.

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does not permit a definition which renders such restrictions ineffective for land conservation purposes." Sherman Lewis et al. v. City of Hayward, Y. Charles Soda et al., 177 Cal.App.3d 103, 106 (1986) [hereinafter Lewis].

[57] Lewis, *supra* note 56, at 116.

[58] *Id.* at 113.

[59] *See supra* note 53.

[60] 1 Witkin Summary of Cal. Law Contracts § 225 Nature of Problem (10th ed. 2005).

[61] RESTATEMENT (SECOND) OF CONTRACTS § 8 (defining unenforceable contracts: "An unenforceable contract is one for the breach of which neither the remedy of damages nor the remedy of specific performance is available. . . .").

[62] CAL. GOV. CODE §§ 51245 (performance to term via nonrenewal), 51250 (liquidated damages for material breach); 51256 (rescission), and 51282 (cancellation criteria).

[63] Merced County General Plan, *supra* note 28, at Ch. VII Agriculture, p. VII-11-12.

[64] *Id.*

First, if the landowner performs under the contract, the landowner is obligated to refrain from developing the property in a manner unrelated to agriculture for a ten-year term and the state receives the benefit of that open space as well as the benefit of economic encouragement of a vital industry–food and fiber production.

Second, if the landowner applies for and receives cancellation, it is tantamount to a consensual termination because the landowner is obligated to pay a hefty 12.5% fee after demonstrating the land is no longer proper for open space preservation and by meeting cancellation criteria of the Act.[65] At cancellation, the state receives the benefit of the open space up to that point, the 12.5% fee, as well as contiguous planning and appropriate city growth.

Third, if the landowner opts to breach because the cancellation criteria cannot be met, the landowner is obligated to pay 25% of the land plus the improvement value as compensatory damages to the state, which would give the state the benefit of its bargain.[66]

The consequences of the view that an Act Contract has "constitutional status" that makes it more difficult or impossible to cancel or breach and thereby exempt from principles of contract law are disconcerting. Using the term "constitutional status" as a trump card to argue against cancellation or breach is tantamount to creating a duty to perform the Act Contract. Duties to perform lie in tort, not in contract.

When a landowner, who is probably unaware of these legal nuances and is almost assuredly not represented by legal counsel, signs an agreement which states "LAND CONSERVATION CONTRACT," that landowner should be assured that the ordinary rules of contract used in all other dealings apply to the Act Contract.[67] There is no notice to the landowner otherwise. If the legislature and judicial system intend to impose duties on the landowners' performance, the landowners have a due process right to notice that, unlike all other contracts which give parties the options of performance, breach, rescission, and cancellation, breach of this particular contract is actually a tort because the contract imposes a duty to behave in a certain way. If "constitutional status" means what the Department claims, it is a violation of due process and unconscionable to bury the legally loaded statement deep in the fine print of the Act Contract that it "constitutes an enforceable restriction under the provi-

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[65] CAL. GOV. CODE §§ 51282, 51283.

[66] CAL. GOV. CODE § 51250; Cal. Civ. Code § 3300.

[67] Tulare County Land Conservation Contract No. 7457 recorded as document number 8626 in the Tulare County Public Record, Feb. 28, 1972 (on file with the San Joaquin College of Law).

sions of section 421 et.seq. of the Revenue and Taxation code." The language "enforceably restricted" in the California Constitution may be necessary in order to provide a constitutional tax relief scheme to Act landowners. However, the land may be "enforceably restricted" while the Act Contract is breached or cancelled. In lieu of performance, the enforcement which gives the state the benefit of its bargain comes from the landowner's payment of: compensatory damages; liquidated damages; or rescission in the form of replacement agricultural land.

IV. CONSEQUENCES OF CONSTITUTIONAL STATUS

A. Modifying the Act Contract

Article I, Section 10 of the United States Constitution provides "No State shall . . . pass any . . . law impairing the Obligation of Contracts."[68] "Federal law controls whether an agreement constitutes a contract for purposes of Contract Clause analysis," which is invoked if subsequent legislation by the public agency prevents or materially limits the private party's ability to exercise contractual rights.[69]

> Though written in absolute terms, the Supreme Court narrowly construes the Contract Clause to ensure that local governments can effectively exercise their police powers. [citations] State governmental entities "must possess broad power to adopt general regulatory measures without being concerned that private contracts will be impaired, or even destroyed, as a result." [citations] *However, a "higher level of scrutiny is required" when the legislative interference involves a public rather than a private obligation.* [citations] (italics added)[70]

To violate the Contract Clause, the subsequent legislation must substantially impair the rights of the private party under the original contract.[71] Even if the subsequent legislation substantially impairs the rights of the private party, the ordinance will stand provided it was reasonable and necessary to fulfill an important public purpose.[72] If a public agency attempts to subsequently modify an existing contract with legislation, the modification is subject to high level scrutiny because "[a] governmental entity can always find a use for extra money, especially when taxes do not have to be raised. If a State could reduce its financial obligations

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[68] U.S. CONST. art. I, § 10.

[69] Southern Cal. Gas Co. v. City of Santa Ana (hereinafter "Southern Cal. Gas Co."), 336 F.3d 885, 889 (2003) and Univ. of Haw. Prof'l Assembly v. Cayetano, 183 F.3d 1096, 1102-1104 (9th Cir. 1999).

[70] Southern Cal. Gas Co., *supra* note 69, at 889-890.

[71] *Id.*

[72] *Id.*

whenever it wanted to spend money for what it regarded as an important public purpose, the Contract Clause would provide no protection at all."[73] Thus, cities and counties are "not free to consider substantial contractual impairments on a par with other policy alternatives."[74]

In *Southern California Gas Co. v. City of Santa Ana*, ("*Southern Cal. Gas Co.*"), 336 F.3d 885 (2003), the City of Santa Ana had adopted an ordinance in 1938 to grant Southern California Gas Company the right to construct and maintain pipes and appurtenances under city streets.[75] Other than a franchise fee, no fees were required of Southern California Gas Company under the 1938 ordinance.[76] In 2001, the City of Santa Ana adopted an ordinance that provided for fees prior to cutting a new trench.[77] The Ninth Circuit Court of Appeal held the trenching ordinance was a violation of the Contracts Clause of the United States Constitution because it substantially impaired the Gas Company's right to trench without fees under the 1938 ordinance.[78] The *Southern Cal. Gas Co.* court stated:

> Santa Ana has failed to explain, nor can we detect from the evidence submitted, why impairment is necessary in this case. If Santa Ana's recognition of higher costs alone sufficed, few if any contracts with government entities would be safe from impairment. . . . We cannot read the 1938 Franchise in a way that reserves to Santa Ana the power to unilaterally alter the terms of the agreement. Such an interpretation is "absurd;" section 8(a) "cannot be applied as broadly and retrospectively as its literal language may suggest." [citations] "When a State itself enters into a contract, it cannot simply walk away from its financial obligations." [citations][79]

Modifications of contracts generally must be supported by consideration from both parties to be binding.[80] To place this in the Act context, participating public agencies routinely pass ordinances that modify their Act implementation policy and the Legislature passes statutes that modify the Act itself. In the absence of mutual consideration, the parties may agree to the modification if it would be unfair in light of circumstances not anticipated by the parties when the contract was made, by statute, or by estoppel.[81] *Southern Cal. Gas Co.* shows us that even when operating

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[73] *Id.* at 894.
[74] *Id.*
[75] *Id.* at 887.
[76] *Id.* at 891.
[77] *Id.* at 888.
[78] *Id.* at 897.
[79] *Id.* at 893, 897
[80] RESTATEMENT (SECOND) OF CONTRACTS §§ 71, 73.
[81] RESTATEMENT (SECOND) OF CONTRACTS § 89.

under the exception of "by statute," the participating public agency must show a high level of benefit to society by making the modification.

For example, the late Arthur C. Tooby entered into an Act Contract with Humboldt County in 1977.[82] At that time the minimum parcel size for Act land was 160 acres.[83] In 1978, Humboldt County increased the minimum parcel size to 600 acres.[84] Some years later, a successor in interest named McKee owned the land and decided to sell 160 acre parcels.[85] Under ordinary contract law, the new minimum parcel size would be an unenforceable modification of the contract unless one of the above criteria applied. Humboldt County through its Board of Supervisors and impliedly, the state of California and the Department of Conservation, have recently disagreed with the assertion that Act Contracts are subject to ordinary contract law.[86] Their position is that Act Contracts have constitutional status; therefore, ordinary contract rules governing modifications of contracts do not apply.[87] Humboldt County and the Department may not have the solid legal footing for the constitutional status they claim. In November, 2005, Judge W. Bruce Watson ruled against Humboldt County by unequivocally rejecting the argument that the Act Contract is a lesser form of contract.[88]

> The judge found that the county could not use its police powers to amend contracts after they had been signed, at least not without proving that there was significant public benefit to be derived from such changes. The county did not meet that burden, the judge determined. David Blackwell, an attorney for McKee, said . . . 'The judge unequivocally rejected the Board of Supervisors' belief that the Williamson Act contract is a lesser contract and hopefully this will dissuade the board from continuing that erroneous interpretation with regard to its implementation of the Williamson Act,' . . . . The judge ruled that a Williamson Act contract is just like any other contract, and therefore governed by U.S. contract law. The county had been maintaining that there is a constitutional element to these contracts, that it's conditioned and controlled by statutory and constitutional overlays. A legal opinion by the state Department of Conservation backed up that position, although the judge apparently disagreed.[89]

In December, 2005, Judge Watson granted the County's motion to reconsider his decision that Act Contracts do not have a constitutional

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[82] John Driscoll, *McKee wins big in Tooby case*, THE TIMES-STANDARD, Nov. 3, 2006, at 1.

[83] *Id.*

[84] Faulk, *supra* note 4.

[85] Driscoll, *supra* note 82.

[86] Faulk, *supra* note 4.

[87] *Id.*

[88] *Id.*

[89] *Id.*

status.[90] However, despite Humboldt County's attempt to present new and additional legal argument, Judge Watson upheld his prior ruling because the county had not met its "heavy burden" to prove the "unilateral modifications" of the original landowner's 1977 contract with the 1978 guidelines were reasonable or necessary, as set forth in *Southern Cal. Gas Co.*[91]

The consequences of Judge Watson's ruling, should it withstand appeal, are presently undetermined. Humboldt County code enforcement claims that Judge Watson's ruling will make the Williamson Act unworkable throughout the state.[92] Landowners such as McKee, however, should not have contract modifications unilaterally imposed upon them by the contracting public agency absent a high level of public benefit. Like other parties to a contract, landowners deserve to know and approve the terms they have agreed to. If a contract is modified both parties must offer some new consideration to make the modification binding. Unless a landowner closely follows ordinances that may affect the local policies enforcing the Act, a public agency could unilaterally modify the terms of the Act Contract by subsequent legislation without the landowner ever knowing of the new terms, much less agreeing to them. Constitutional status is not a trump card that permits public agencies to unilaterally modify ordinances in their favor.

B. Cancellation and Rescission

In any contractual relationship, everything is simpler and easier when both parties to a contract perform their obligations. Performance to term and nonrenewal of an Act Contract under Government Code Section 51245 is no exception. The landowner performs by refraining from making improvements upon the land in a manner inconsistent with its agricultural use for a period of ten years. During that period the public agency assesses the land according to its use, resulting in lower assessed values and lower property taxes. Both parties have performed their obligations and received the benefit of their respective bargain.

Circumstances can change dramatically during a ten-year period. The parties may elect to exchange their performance obligations for other

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[90] Nathan Rushton, *Judge's ruling adds new to Tooby Ranch case*, EUREKA REPORTER, Dec. 16, 2005, at 1, *available at* http://www.eurekareporter.com/ArticleDisplay.aspx?ArticleID=6503.

[91] Nathan Rushton, *Superior Court judge's ruling clarifies factors in Tooby Ranch case*, EUREKA REPORTER, Feb. 9, 2006, at 1, *available at* http://eurekareporter.com/node/71789.

[92] Faulk, *supra* note 4.

remedies such as cancellation, rescission, or damages for breach. Outside the Act context, the term "cancellation" "is sometimes used interchangeably with 'rescission,' especially with respect to contracts." Effectively, there is no practical difference between rescinding and canceling a contract that has not been performed at all."[93] In the Act, however, cancellation and rescission are terms of art that have slightly different meanings.

If landowners have not performed the entire ten-year term of the Act Contract and would like to cancel, they are not allowed to simply agree to the cancellation and walk away. The public agency may be incentivized to change the use of the land to one that generates additional tax revenue and the landowner may be incentivized to sell the land to a developer for its fair market value. As a first-level protection against self-interested cancellations, the legislature requires the public agency to find that cancellation is either consistent with their general plan or in the public interest.[94]

Government Code Section 51282 provides that a county electing to cancel an Act Contract based upon consistency with the general plan ("Consistency Finding") must find: (1) a notice of non-renewal has been served; (2) cancellation is not likely to result in the removal of adjacent lands from agricultural use; (3) alternative uses of the land are consistent with the general plan; (4) cancellation will not result in discontiguous patterns of urban development; and (5) either (a) there is no proximate non-contracted land which is both available and suitable for the proposed alternative use, or (b) development of the contracted land would provide more contiguous patterns of urban development than development of proximate non-contracted land.[95]

A county electing to cancel an Act Contract based upon the public interest ("Public Interest Finding") must find: (1) other public concerns substantially outweigh the objectives of the Act; and (2) either (a) there is no proximate non-contracted land which is both available and suitable for the proposed alternative use, or (b) development of the contracted

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[93] Douglas Laycock, Modern American Remedies – Cases and Materials (3rd 2002) Aspen Publishers p. 552.

[94] CAL. GOV. CODE §51282.

[95] *Id.* One case that has interpreted the Consistency Finding is *Honey Springs Homeowners' Association, Inc. et al. v. Board of Supervisors of San Diego County; Presenting Jamul et al.* (hereinafter "*Honey Springs*"), 157 Cal.App.3d 1122, 1144 (1984), where the Court considered what "discontiguous patterns of urban development" meant.

land would provide more contiguous patterns of urban development than development of proximate non-contracted land.[96]

Among other things, the Robinson Act legislatively overruled that portion of *Sierra Club* which stated that "extraordinary circumstances" were required to cancel an Act Contract.[97] No additional findings of any kind, including extraordinary circumstances, are required to be shown in order to cancel an Act Contract.[98]

Once the County makes the Consistency Finding or Public Interest Finding, a statutory cancellation fee of 12.5% of the unrestricted fair market value of the land is assessed to the landowner.[99] Each County has its own Act implementation policies. These policies may provide for an additional fee payable to the County on cancellation. For example, Merced County requires an additional 12.5% fee on cancellation, for a total cancellation fee of 25%.[100] Property taxes in California are generally about 1.25% of the assessed property value.[101] One and one-quarter percent multiplied by ten, one for each year of an Act Contract, is 12.5%. Because property appreciates in value, when limited to a 2% increase in property tax each year under Proposition 13, it is worth noting the 12.5% cancellation fee will likely be more than the cumulative total the landowner has paid in property tax for the past ten years. This is true even though, on cancellation, the contract has already been partly performed and the landowner only receives a discount on property tax or no benefit at all.[102]

As an alternative to paying the cancellation fee, the landowner may replace the land under the Act Contract by dedicating an agricultural conservation easement on replacement land.[103] This is referred to as "voluntary rescission."[104] The exchange is not really for equal value be-

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[96] CAL. GOV. CODE §51282; Friends, *supra* note 55, which considered the availability and suitability of proximate non-contracted land and found a cancellation of 160 acres in order to construct homes on three and one-half acres was in the public interest.

[97] Friends, *supra* note 55, at 205.

[98] *Id.* CAL. GOV. CODE § 51282(f).

[99] CAL. GOV. CODE § 51283.

[100] County of Merced, Rules and Procedures to Implement the California Land Conservation Act of 1965 p. 7-8.

[101] Telephone Interview with Erica Whisenhunt, Staff Appraiser, Fresno County Assessor, Fresno, Cal., (Jan. 23, 2006).

[102] Merced County General Plan, *supra* note 28, at p. VII-11-12.

[103] CAL. GOV. CODE §51256.

[104] Cal. Department of Conservation Division of Land Resource Protection Williamson Act Easement Exchange Program Questions and Answers p. 1, *available at* www.conservation.ca.gov/dlrp/lca.

cause the Act Contract is temporary and the agricultural conservation easement is permanent.[105]

In any case, the restriction of the Act Contract is "enforced" through: (1) making the Consistency Finding or Public Interest Finding; (2) payment of the statutory cancellation fee of 12.5%; (3) payment of the local agency cancellation fee (up to an additional 12.5%); or (4) replacing the cancelled land acreage with permanently restricted land under conservation easement.

C. Material Breach and Liquidated Damages

1. Definition of breach under Government Code 51250

Government Code 51250 became effective January 1, 2004, providing the participating public agency or the Department an additional and alternate remedy from the contract cancellation petition for a material breach of an Act Contract and extending the lot-line adjustment provisions to January 1, 2009.[106]

The material breach provisions of Government Code Section 51250 are designed to provide an "enhanced remedy for a material breach of contract" and provide:

> (b) . . . [A] breach is material if, on a parcel under contract, both of the following conditions are met: (1) A commercial, industrial, or residential building is constructed that is not allowed by this chapter or the contract, local uniform rules or ordinances consistent with the provisions of this chapter, and that is not related to an agricultural use or compatible use. (2) The total area of all of the building or buildings likely causing the breach exceeds 2,500 square feet . . . .[107]

2. Liquidated Damages Void as a Penalty

Where a landowner meets the above definition Government Code Section 51250 also provides a pre-defined penalty.

> (j) The monetary penalty shall be 25 percent of the unrestricted fair market value of the land rendered incompatible by the breach, plus 25 percent of the

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[105] *Id.*

[106] California Assembly Bill 1492 (Laird, 2005) adds § 51250 to the Government Code. *See* California Department of Conservation website www.conservation.ca.gov/dlrp/lca/lrcc/AB_1492.htm, Aug. 3, 2004. Cal. Gov. Code §§ 51281 et. seq contains cancellation provisions. California Assembly Bill 1492 (Laird, 2005) also amends § 51257 of the Government Code. *See* California Department of Conservation website www.conservation.ca.gov/dlrp/lca/lrcc/AB_1492.htm, Aug. 3, 2004.

[107] What AB 1492 Means to You, *available at* www.consrv.ca.gov/lca/lrcc/AB_1492.htm July 14, 2005; CAL. GOV. CODE § 51250.

> value of the incompatible building and any related improvements on the contracted land. . . .[108]

Where parties to a contract agree in advance to a pre-defined amount to be paid in the event of a material breach, the amount is considered to be "liquidated" damages. For liquidated damages provisions to be valid and enforceable: (1) damages must be difficult to calculate; and (2) the liquidated damages must be a reasonable estimate by the parties at the time of contracting.[109]

Certainly, the first condition is true of the material breach of an Act Contract. It is difficult to say what the value is of preserving a parcel of land as agricultural or open space for a ten-year period. However, we cannot say that the value would simply be the value of some other parcel of land to replace the Act land in violation. The United States Supreme Court has held that the just compensation to be paid a landfill owner on an action for eminent domain was the market value of the landfill taken, not the value of the replacement landfill the owner would have to purchase to retain the same function.[110] Another approach to calculating damages would be to compensate the state for the value of restricting development on the Act land. However, compensatory damages are impossible to calculate in the Act context, because there is no ascertainable market for development rights and such damages must be reasonably certain from which to fashion an equitable remedy.[111]

By enacting Government Code Section 51250, it appears the legislature has bought in to the idea of constitutional status for the Act Contract. No matter how damages are calculated, a penalty amounting to 25% of the land and improvements is not a reasonable estimate of damages by any measure. For example, if the Act land is worth a modest $500,000, then $75,000 will be the penalty for the land portion. Twenty-five percent of a residential house worth an additional $200,000 is $50,000. The penalty in this example would be $75,000 plus $50,000, for a total of $125,000. Twenty-five percent of a modest office building could easily reach $500,000. Twenty-five percent of a strip mall could easily reach $1,000,000. Damages of this magnitude are not reasonable in relationship to the modest tax savings that the landowner receives, which generally only amounts to a few hundred dollars per month. They are reasonable neither at the time the contract is entered, nor at the time of the breach. The 25% penalties should be void and unenforceable because

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[108] CAL. GOV. CODE § 51250(j).
[109] CAL. CIV. CODE § 1671(b).
[110] United States v. Fifty Acres of Land, 469 U.S. 24, 30 (1984).
[111] CAL. CIV. CODE § 3301.

the law does not allow parties to contract for punitive damages.[112] Constitutional status should not be an excuse to avoid the general rules of liquidated damages.

3. The 2,500 Square Foot Maximum is Overbroad

There are other problems with Government Code Section 51250. The 2,500 square foot limit on improvements sets a maximum size for improvements on the land whether it is related to agriculture or not. Farmers should not be limited to a 2,500 square foot home to take advantage of the Act. However, that is exactly what has happened since Government Code Section 51250 was added in 2004. Some public agencies have interpreted Government Code Section 51250 as limiting the size of the farmer's residence. While it may be desirable for the participating public agency to prevent commercial improvements on Act land, it is wholly unnecessary to limit the size of a farmer's primary residence to the arbitrarily selected size of 2,500 square feet.

A careful reading of the statute provides two alternative interpretations: either 2,500 square feet of improvement on Act land is per se violative of the Act regardless of its use; or the 2,500 square foot limit is not invoked as long as the use of the improvement is "related to" agriculture. The Calaveras County Board of Supervisors believes the former interpretation is correct and that farmers should be limited to the size home they build on Act land.[113] The Department agrees with this clearly unfair interpretation.[114] The California Farm Bureau Federation believes the second option is the proper interpretation and, given the ambiguity and unfairness to farmers, may propose legislation in the future to clarify the rule.[115] If an improvement greater than 2,500 square feet is, by definition, inconsistent with or unrelated to the agricultural use of the land, then farmers who wish to participate in the Act and simultaneously reside on their land are statutorily limited to a 2,500 square foot home. Even if the farmer's primary residence is automatically deemed related to agriculture, the current interpretation of 'related to agriculture' does not include a separate residence for an elder, a child, or even a farm manager who receives lodging as part of compensation.[116]

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[112] CAL. CIV. CODE § 1671.

[113] Dana M. Nichols, *Plan to build on protected land halted*, STOCKTON COUNTY RECORD, Dec. 13, 2005, *available at* http://www.recordnet.com/apps/pbcs.dll/article?AID=/20051213/NEWS01/512130319&SearchID=73232272299889.

[114] *See supra* note 59.

[115] *Id. See supra* note 16.

[116] *Id.*

The alternatives have serious consequences for landowners wishing to construct or make an addition to a residence on Act land. The request of Jon Giottonini, a co-owner of a 260 acre ranch in Calaveras County, to build a personal residence larger than 2,500 square feet was recently rejected by the Board of Supervisors.[117] Giottonini offered to remove the acreage on the proposed homesite and add acreage that was not in the Act, resulting in a 26 acre net gain of Act land.[118] The appropriate method of handling such situations, according to the Department, would be to file the entire 260 acres for nonrenewal under Government Code Section 51245 nine years in advance of the proposed construction, or obtain a lot line adjustment and nonrenew that portion of the land nine years in advance of the proposed construction.[119] That solution is clearly unworkable and grounded in the idea that performance of an Act Contract is not optional. The Act was not intended to limit the size of a farmer's primary residence. The 2,500 square foot material breach definition may have intended to target small-parcel, large-home landowners, but it has overreached and is now impacting the rights of farmers which are large-parcel, medium-sized home landowners.

4. The 2,500 Square Foot Maximum is Arbitrary

The selection of 2,500 square feet has no basis in law. A common misconception is that the 2,500 square foot number was derived or imported from the Subdivision Map Act.[120] This is not the case. Its selection was merely the random result of a compromise of California State Assembly Member John Laird, the sponsor of Assembly Bill 1492 (2004), who wanted 4,000 square feet, and the Department, who wanted a mere 1,000 square feet.[121] The 2,500 square foot maximum provides a bright line test: less is "consistent" and more is "inconsistent" with the agricultural use. The problem with bright line standards is that there are always situations where the rule is not valid.

For example, consider the term of the Act Contract. If a farmer were to breach an Act Contract by expanding his existing primary residence beyond 2,500 square feet, the farmer would be forced out of the Act and penalized 25% of the value of the land plus another 25% of the value of the offending structure. This is an unnecessary and unfair restriction. By anyone's common sense definition, a farmer's residence for his or her

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[117] *See supra* note 113.
[118] *Id.*
[119] *See supra* note 55.
[120] *Id.*
[121] *Id. See supra* note 16.

family is consistent with the agricultural use of the land, regardless of size. Farms require farmers and farmers require residences. The size of the improvement does not change the use of the property. The land remains in use as a farm for the purpose of agriculture regardless of the size of the farmer's residence. The fact that some farmers can afford to build homes larger than 2,500 square feet is not inconsistent with the Act. This penalty could be assessed even though the farmer had performed under the Act Contract for nine years out of ten. Even though the farmer substantially complied with more than ninety percent of the Act Contract's term the expansion is a material breach because the statute, somewhat unimaginatively, does not contemplate any other manner of measuring breach.[122] Neither the term of the Act Contract nor other factors are considered therefore the legislation is poised for inequitable and undesirable results.

Under the ordinary principles of contract law, courts seek to enforce contracts where there is substantial compliance under the terms of the agreement because the law abhors a forfeiture.[123] Whether a breach is material or not is determined by the following factors: loss of benefits expected (i.e. did the non-breaching party get substantially what it bargained for); forfeiture of failing party (what rights would the breaching party give up under the contract); compensation for those lost benefits; if trivial breach, can the plaintiff get damages to make up for the loss; failing party's likelihood they will cure the failure; more or less certain that they will ultimately fully perform; and the good faith of failing party.[124] Under an Act Contract that is partly or substantially performed by the landowner, and the land is not improved for nine years out of ten, the state has received substantially what it bargained for because the land has remained open or agricultural in nature for the majority of the agreed upon ten-year term. Under Government Code Section 51250, the trivially breaching farmer forfeits far more money than ever could have possibly been received as a property tax discount for the entire term of the Act Contract. Assuming the farmer will ultimately fully perform and continue the agricultural use of the land, it is a grossly disproportionate forfeiture of the landowner to be forced to pay 25% of the land value and 25% of the value of the improvement as a penalty.

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[122] Nine years and one month out of ten years is actually 90.8% (109 months / 120 months).

[123] *UNUM Life Insurance Company of America v. John R. Ward*, 526 U.S. 358, 370 (1999).

[124] RESTATEMENT (SECOND) OF CONTRACTS § 241.

Courts have sometimes characterized such provisions as the excuse of conditions subsequent in lieu of material breach to avoid disproportionate forfeiture.[125] "In determining whether the forfeiture is "disproportionate," a court must weigh the extent of the forfeiture by the [landowner] against the importance to the [public agency] of the risk from which he sought to be protected and the degree to which that protection will be lost if the non-occurrence of the condition is excused to the extent required to prevent forfeiture."[126] The extent of the forfeiture by the landowner is the payment of 25% of the value of the land and 25% of the value of the property--a vast sum compared to the potential tax savings the farmer bargained for originally. The state has sought to be protected from the risk of unmitigated improvement of agricultural and open space land. The degree to which that protection would be lost is very small in this scenario, only one year out of ten and one square foot over 2,500. This simple example reveals the inequitable and undesirable results of Government Code Section 51250, and another undesirable consequence of treating the Act Contract as having constitutional status.

D. The Impetus of Government Code Section 51250

After numerous questions and concerns regarding the effects of Government Code Section 51250, the Department of Conservation Division of Land Resource Protection website published some background information.[127] The intent of Government Code Section 51250 is to address the most egregious violations of the Williamson Act by penalizing those who engage in contract violations.[128] "Egregious" means "surpassing; extraordinary; distinguished (in a bad sense)."[129] The legislative history is illuminating. In the Senate Local Government Committee meeting, July 2, 2003, one of the comments made in support of Assembly Bill 1492 (2004) which enacted Government Code Section 51250 was:

> Imagine their surprise when state officials hear that developers have built houses and department stores on Williamson Act contracted land. Imagine

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[125] RESTATEMENT (SECOND) OF CONTRACTS § 229.

[126] *Id.*

[127] What AB 1492 Means to You, July 14, 2005, *available at* www.consrv.ca.gov/lca/lrcc/AB_1492.htm.

[128] *Id.*

[129] "Egregious. . . Extremely or remarkably bad, flagrant. . . ." BLACK'S LAW DICTIONARY 421 (7th ed. 2000).

> the current landowners' surprise when state officials say that their property falls under decades-old enforceably restrictive contracts.[130]

The Department also claims that landowners and local governing bodies have permitted uses, such as malls and subdivisions, on Contract lands.[131] Both the Senate Rules Committee and the Department claim that these violations are due to poor record keeping and statutory misinterpretations.[132] Consider two of the Department's examples: the West Tracy Mall and City of Porterville.

1. West Tracy Mall was not an 'Egregious' Violation

The West Tracy Mall development was not an "egregious" violation of an Act Contract because the state received substantially what it had bargained for and the developer relied on the City of Tracy's writings and conduct that indicated compliance with the Act. General Growth Management ("General") developed ninety-seven acres of land near the city of Tracy, in San Joaquin County.[133] The mall included about thirty-two acres of land subject to an Act Contract.[134] The previous owner filed a notice of nonrewal, received by the county assessor on November 28, 1986, and recorded on February 5, 1987.[135] In San Joaquin County, the renewal date for an Act Contract is March 1.[136] Thus, March 1, 1987, began the first year of the ten-year waiting period on nonrenewal, so the Contract did not expire until March 1, 1996.[137] However, General proceeded to develop the mall during 1995, the year before the Contract's expiration.[138]

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[130] Bill Analysis, Senate Local Government Committee, Assembly Bill 1492 (Laird, 2005) July 2, 2003.

[131] *See supra* note 128.

[132] *See supra* notes 128, 130.

[133] Andrew F. Hamm, *Mall Owners To Pay Fine On Farmland*, SAN JOAQUIN COUNTY PRESS, Dec. 6, 1995 at 1.

[134] The City Council of the City of Tracy Resolution Tentatively Approving the Williamson Act Cancellation Application of General Growth and Authorizing the Certificate and Recordation of a Certificate of Tentative Cancellation Application Number 1-95-WA, Resolution No. 95-372, Dec. 5, 1995 (on file with the San Joaquin College of Law).

[135] Notice of Nonrenewal of Williamson Act Contract 76-C1-168 (copy on file at San Joaquin College of Law).

[136] Letter from Kenneth E. Trott, Manager, Land Conservation Unit, Department of Conservation to Fred Diaz, City Manager, City of Tracy (Oct. 18, 1995) (on file with San Joaquin College of Law).

[137] *Id.*

[138] Agreement for Payment of Williamson Act Cancellation Fee between the State of California, by and through the Resources Agency, Department of Conservation and General Growth Management of California, Inc., 1-2.

Controversy erupted when the San Joaquin County Assessor's Office notified the City of Tracy that part of the West Tracy mall remained under Act Contract.[139] The Department of Conservation argued there was no excuse for the violation because the notice of nonrenewal for the land had been on record since 1987 and a failure to enforce would create indifference on the part of other Act Contract holders.[140] The City of Tracy, by and through their City Council, adopted the I-205 Corridor Specific Plan on August 21, 1990, and certified the I-205 Environmental Impact Report ("I-205 EIR"), which erroneously indicated the Act Contract for the mall would expire in March of 1995.[141] Further, in June of 1995, the City of Tracy issued building permits for the mall and commenced construction on approximately five acres of Act land that General deeded back to the City for roads.[142]

Negotiations commenced between the Department of Conservation and counsel for General. General, under protest, filed for cancellation, which would subject General to a fee amounting to 12.5% of the value of the land, whereas a successful nonrenewal has no cost at all.[143] Pursuant to California Government Code section 51283, the San Joaquin County Assessor derived a cancellation value of $4,500,000.[144] The City of Tracy held a public hearing on the issue on December 5, 1995, in which the cancellation of the contract was ratified.[145] General disputed the need for cancellation because it had detrimentally relied on the City of Tracy's own I-205 EIR in the I-205 Specific Plan, which indicated the contract would expire in 1995.[146] General ultimately paid $562,500 as a cancellation fee as part of a settlement agreement with the Department.[147]

West Tracy Mall is a good example of a non-egregious violation of an Act Contract. West Tracy Mall was destined for development due to its location. The land was located at the corner of I-205 and Grant Line

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[139] *Id.*

[140] *See supra* note 137; Grant Deed of 4.83 acres from Tracy Mall Partners, L.P. to City of Tracy, recorded in the San Joaquin County Public Record Nov. 21, 1994, #94125887.

[141] *See supra* note 139.

[142] Letter from Orval F. Papon, Vice President-Development, General Growth Management of California, Inc. to Barry Hand, Community Development Director and Robert M. Conant, Jr., Senior Planner, City of Tracy, Re: Application for Williamson Act Cancellation (Sep. 21, 1995) (on file with San Joaquin College of Law).

[143] *Id.*

[144] Letter from Les Flemmer, Supervising Appraiser, San Joaquin County Assessor to Mr. Robert M. Conant Jr., Senior Planner, City of Tracy Community Development Department (Oct. 23, 1995) (on file with San Joaquin College of Law).

[145] *See supra* note 134.

[146] *See supra* note 142.

[147] *See supra* note 138.

Road.[148] The City of Tracy had: annexed the land; approved the I-205 Specific Plan for the development of the area, approved building permits; and had completed infrastructure improvements of its own.[149] Nonrenewal had been filed more than nine years prior to improvement.[150] General, and its predecessor in interest, had substantially complied with the terms of the contract by waiting more than nine of the ten years. While the actual date nonrenewal commenced was public record, the date nonrenewal was to be complete had to be computed. The I-205 Specific Plan stated the nonrenewal completion date as 1995 and General relied on that information.[151] Yet, sponsors of the legislation and the Department saw the West Tracy Mall breach as an 'egregious violation' worthy of creating Government Code Section 51250 which raised the penalty for breach by approximately 400%.

2. Residential and Commercial Improvements in the City of Porterville were not 'Egregious' Violations

Residential and commercial improvements in the City of Porterville were not "egregious" violations because the City of Porterville had protested the formation of Act Contracts between Tulare County and landowners near the edges of the City of Porterville in order to have the right to void those Contracts on annexation. Prior to 1991, a city formally protesting the formation of an Act Contract on land within one mile of its borders could later annex that parcel without succeeding to the terms of the Act Contract. In 1990, Assembly Bill 2764 amended Government Code section 51243.5, which ended a city's ability to protest new contracts.[152] Today, a city may annex land without succeeding to the Act Contracts on that land if that Act Contract was protested prior to 1991 and within one mile of city limits at the time of the protest.[153] In 1970, Porterville resolved to "generally" (meaning it was not directed at any particular contract or parcel) protest any future Act Contract within one mile of its borders.[154]

Ennis Development ("Ennis") purchased 120 acres near the city of Porterville, in Tulare County around 1988, which were subject to Act

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[148] *See supra* note 134.

[149] *See supra* notes 142, 138.

[150] *Id.*

[151] *See supra* note 142.

[152] California Assembly Bill 2764 (1990) ch. 841 § 6.

[153] CAL. Gov. CODE § 51243.5.

[154] Judgment Pursuant to Stipulation at Exhibit E at 4, People of the State of California v. Ennis Development Corporation, Super. Ct. of the State of Cal., County of Sacramento (No. 98AS01208).

Contract #7457 within County Agricultural Preserve #689.[155] Contract #7457 was entered into on February 25, 1972, after the general protest.[156] Since Contract #7457 covered land on parcels whose borders were not a perfect one-mile mirror of the city limits, portions of the 120 acres extended beyond one mile. At the appropriate time, Porterville requested a finding from Tulare County Local Agency Formation Commission ("LAFCO"), a public agency made up of representatives from City and County, that the annexation of the 120 acres would cancel the Act restrictions.[157] The Tulare County LAFCO found the annexation and subsequent cancellation of the contracts on the annexed parcels valid provided the parcel was within one mile of the city limits at the time the contract was entered into.[158] Ennis constructed commercial and residential improvements on the annexed parcels both within and beyond the one mile range.[159] During a routine audit in January, 1997, the Department discovered the improvements and notified Ennis of the alleged violation.[160] In March, 1998, a settlement was entered into between the Department, Tulare County LAFCO, the city of Porterville, Tulare County, First American Title Insurance Company, and Ennis Development.[161] In the settlement, Tulare County, the City of Porterville, and Tulare County LAFCO disputed the Department's conclusion that Contract #7457 violated the Act restrictions.[162] The parties agreed: that land beyond one mile from city limits was still under Contract #7457, not to allow 'general' protests for cancellation in the future, and Ennis paid a $100,000 fine.[163]

Ennis built on land that was annexed by the City of Porterville with the approval of LAFCO. Annexation by a City necessarily includes the entire parcel, not just that portion of the parcel which was within one mile of the previous city limit boundary. It is wholly impractical, if not impossible, in this situation for a City to require a developer to split parcels along an irregular one-mile boundary parallel to city limits in order to develop only that portion of the land which was cancelled on annexation.

While it is clear that improvements were made on portions of parcels that were outside the one mile boundary, it is also clear that cancellation

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[155] *Id.* at 3.
[156] *Id.*
[157] *Id.* at 4.
[158] *Id.*
[159] *Id.*
[160] *Id.* at 5.
[161] *See supra* note 154, at Exhibit A, 1.
[162] *Id.* at 2.
[163] *Id.* at 2, 6.

took place on a portion of each of those parcels. The City of Porterville requested and received a finding from Tulare County LAFCO that the annexation and cancellation was valid.[164] Ennis' breach is, at worst, a technical one, based on statutory misinterpretations and impractical guidelines. In the settlement agreement, the parties even "conclude that the facts surrounding the Ennis development in Tulare County are unique."[165] Certainly these facts do not rise to the level of an "egregious" violation and should not be used as justification for a 400% increase in material breach penalties or for treating the Act Contract as having constitutional status.

V. CONCLUSION

A. Society Should not Discourage Efficient Breach

One theory behind contract law is built on the premise that no agreement would be entered into if there were not some bargained-for exchange that made at least one of the parties better off than before entering into the agreement.[166] Known as the Pareto Principle or Social Utility Theory, this holds that one allocation of resources is superior to another and if everyone consents to the reallocation, it must be better for them all.[167] Ultimately, Social Utility holds to the premise that the efficient society is wealthier than the inefficient.[168]

As discussed above, the entire purpose of the Act is to value land based on agricultural use and not as highest and best use because, for whatever reason, the landowner wants to continue farming and does not want to sell the land for its highest value. [169] On formation of the Act Contract, the landowner and the participating public agency agree to a reallocation of resources in order to restrict the land from development in exchange for modest property tax reductions. If at some point in the

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[164] *Id.* at 3.

[165] *Id.*

[166] "Pareto superiority - the principle that one allocation of resources is superior to another if at least one person is better off under the first than under the second and no one is worse off - was thought, by Pareto himself, to solve the traditional problem of practical utilitarianism - that of measuring happiness across persons to determine a policy's effect on total utility." J. RICHARD POSNER, THE ECONOMICS OF JUSTICE 88-90 (1983) (*citing* Jules L. Coleman, *Efficiency, Exchange, and Auction: Philosophic Aspects of the Economic Approach to Law*, 68 CALIF. L. REV. 221 (1980)).

[167] *Id.*

[168] *Id.*

[169] The general rule is that "[w]hether land is improved or vacant, its value is economically a function of its highest and best use." RICHARD M. BETTS, SILAS J. ELY, DENNIS MCKENZIE, BASIC REAL ESTATE APPRAISAL 105 (5th ed. 2001).

future, circumstances change where the landowner or the public agency find an even more profitable allocation of resources, they should be able to pursue it.

The essence of the Act is a simple contract between state and landowner.[170] Consider the fundamental difference between tort and contract. If you commit a tort, you are liable to pay a compensatory sum. "If you commit a contract, you are liable to pay a compensatory sum unless the promised event comes to pass, and that is all the difference."[171] Similarly, if a landowner enters into an Act Contract, he or she is liable to pay a compensatory sum (cancellation fee, rescission acreage, or liquidated damages for breach) unless the promised event comes to pass (nonrenewal and no development inconsistent with agricultural use for ten years). Justice Holmes' theory, that a contracting party has the option to perform or to pay damages, has been revived and expanded by economists who speak of "efficient breaches." Judge Richard A. Posner, writing for the Fifth Circuit, states:

> Even if the breach is deliberate, it is not necessarily blameworthy. The promisor may simply have discovered that his performance is worth more to someone else. If so, efficiency is promoted by allowing him to break his promise, provided he makes good the promisee's actual losses. If he is forced to pay more than that, an efficient breach may be deterred and the law doesn't want to bring about such a result.[172]

Efficiency theorists would argue that a landowner who has discovered his farmland is no longer worth $15,000 per acre but is now worth $300,000 per acre should sell for the higher price because it makes society as a whole wealthier.[173] However, as discussed above, some landowners do not want to stop farming their land and find it a better allocation of resources to enter into Act Contracts. At some point the land may increase in value so much over a short period of time that the landowner could actually cancel, rescind, or breach the Act Contract, pay the cancellation fee, replace the land, or pay liquidated damages and still make a profit. Ordinary contract law permits this, and efficiency theorists encourage it because the infusion of wealth into the economy makes society wealthier as a whole.

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[170] Faulk, *supra* note 4.

[171] 2-7 CORBIN ON CONTRACTS §7.12, IS A CONTRACTUAL DUTY ALWAYS ALTERNATIVE?

[172] *Id.*

[173] Posner, *supra* note 166 (in regards to making society wealthier); Barbassa, *supra*, note 32 (in regards to land value).

B. Constitutional Status

The Department and certain public agencies would have farmers believe the language "enforceably restricted" means that an Act Contract is not subject to the ordinary rules of contract law and, consequently, that a cancellation or breach of the Act Contract is either impossible or subject to a showing of extraordinary circumstances. This is simply not the case.

The enforcement of the restriction is found in either: performance and nonrenewal under Government Code Section 51243; partial performance and cancellation by meeting the criteria of Government Code Section 51282 and paying the cancellation fee; partial performance and rescission by dedicating replacement land to an agricultural conservation easement under Government Code Section 51256; or material breach and payment of liquidated damages under Government Code Section 51250. If landowners have a duty to perform an Act Contract such that they are not free to be cancelled, rescinded, or breached, then the Act Contract is really not a contract at all.

Modifications of Act Contracts by local ordinance should not be made unilaterally by the participating public agency absent a high showing of public necessity.

The 2,500 square foot definition of breach is overbroad and arbitrary. Farmers should have the ability to build primary and secondary residences on Act land without being penalized in an amount which is grossly disproportionate to their tax savings. The 2,500 square foot maximum should either be removed so that determinations of material breach would be made on a case-by-case basis or it should be amended in such a way as to narrow the scope of the definition to avoid undesirable application.

Those unfortunate landowners who elect to cancel or breach are deterred by fees that are grossly disproportionate to any possible benefit they could have received. The 25% penalty for material breach is excessive and ill-founded. Such a provision in an ordinary contract would be void as against public policy because it does not represent a reasonable estimate of the damages.[174]

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[174] "[T]he parties to a contract are not free to provide a penalty for its breach. The central objective behind the system of contract remedies is compensatory, not punitive. Punishment of a promisor for having broken his promise has no justification on either economic or other grounds and a term providing such a penalty is unenforceable on grounds of public policy." RESTATEMENT, (SECOND) OF CONTRACTS § 356.