OF WINDFALLS AND PROPERTY RIGHTS: *PALAZZOLO* AND THE REGULATORY TAKINGS NOTICE DEBATE

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Claims for government compensation due to regulatory takings usually hinge on the reasonable investment-backed expectations of the claimant. The 2001 U.S. Supreme Court decision Palazzolo v. Rhode Island *eliminated notice of existing regulations as a bar to such a takings claim. Left undecided was the extent to which notice affects the claimant's reasonable investment-backed expectations. In this Comment, Max Gibbons argues that notice should be irrelevant to a regulatory takings claim. Inclusion of this factor would impose a severe restraint on the alienation rights of regulated property owners. The Anglo-American common and statutory law has developed with a particular concern for unfettered alienation and none of the traditional justifications for limited alienation restrictions apply in the takings context. Yet an examination of the current Court indicates that the votes exist to set a precedent that would impose a new, unnecessary restriction on the alienation of real property. The author argues that eliminating notice from an assessment of reasonable investment-backed expectations would not only hold the government accountable for unconstitutional acts, but would allow both the current and previous owners to receive appropriate compensation for their property.*

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INTRODUCTION

Since the emergence of the regulatory takings doctrine, few legal issues have garnered more critical attention from judges and scholars alike. This interest stems primarily from the doctrine's ambiguous nature. While the government must adhere to the Fifth Amendment and pay just compensation for taking property through regulatory enactment, it is difficult to determine when a regulation actually effects a taking.

Regulatory takings emanate from the U.S. Constitution's protection of private property interests from governmental interference.[1] The Framers were wary of a government unrestrained in its ability to interfere with its citizens' property and the liberty that results from the ownership of land.[2] The U.S. Supreme Court initially recognized the existence of regulatory takings in a landmark decision in 1922.[3] Since that time American courts have struggled to assess when the effect of regulations on private property triggers the protection of the Fifth Amendment.

The law of regulatory takings has evolved considerably over time. It now consists of three per se rules used to dispose of a large number of disputes, and a complex test when the per se rules do not apply. The test balances three factors to reach an outcome that is fair and just.[4] The most important factor in this balancing test is the degree to which the regulation interferes with a property owner's reasonable investment-backed expectations.

Of particular controversy is the degree to which postregulation title transfer affects the reasonableness of the subsequent title holder's investment-backed expectations. An example will serve to illustrate the issue. Imagine Judith owns Greenacre, a parcel of land in her home state. The state legislature enacts a regulation that affects the development potential of Greenacre. Judith then sells Greenacre to Dave. Dave submits an application to the state regulatory authority requesting permission to build a house on Greenacre. The request is denied based on the existing regulations. Dave then files suit claiming that the state effected a regulatory taking requiring just compensation under the Fifth Amendment as extended to the state by the Due Process Clause of the Fourteenth Amendment. Because Dave took title to Greenacre after the regulation was enacted, will the court hold that he had no reasonable investment-backed expectations? The Supreme Court, while providing some guidance, has not ruled on whether title transfer should play a role in assessing

1. *See* U.S. CONST. amend. V.

2. *See, e.g.*, THE FEDERALIST NO. 10 at 78 (James Madison) (Clinton Rossiter ed., 1961) ("The protection of [property] is the first object of government.").

3. *See* Pennsylvania Coal Co. v. Mahon, 260 U.S. 393 (1922).

4. *See* Penn Cent. Transp. Co. v. New York City, 438 U.S. 104, 124 (1978).

reasonableness. In this Comment, I propose that this is a far more important question than it may appear, because of the eventual answer's effect on real property alienation. The Anglo-American common law evinces a prominent concern for the unfettered transfer of land. If the Supreme Court holds that a title transfer impairs a regulatory takings claim for just compensation, it would establish a rule of law that ignores the overwhelming justification for eliminating restrictions on real property alienation.

The Supreme Court's decision in *Palazzolo v. Rhode Island*[5] brings the question of postregulation title transfer and the reasonableness of investment-backed expectations to the fore. Part I of this Comment examines the American law of regulatory takings with an emphasis on reasonable investment-backed expectations. Part II considers how the Anglo-American common law has exhibited a bias against restrictions on the alienability of real property, and why this is so. Part III looks at the rare instances of permissible restrictions on real property alienation in contemporary law. It then explores the three limited justifications for these restrictions. Part IV analyzes *Palazzolo* and postregulation title transfer. It then argues that to include notice in an examination of the reasonableness of a property owner's investment-backed expectations would be contrary to the aims of the common law and an undesirable restriction on real property alienation.

I. REGULATORY TAKINGS LAW

The Fifth Amendment guarantees that "private property [shall not] be taken for public use, without just compensation."[6] This sweeping protection of private property is nonetheless, like most constitutional guarantees, qualified. The government can, under the auspices of the police power, severely regulate property in order to benefit the public.[7] But it is clear from the unambiguous phrasing of the Fifth Amendment that if the government takes property, it must provide compensation. The important question then, is what is a taking? Physical appropriation clearly qualifies, but beyond that the doctrine becomes murky.

The Supreme Court has recognized that government regulation can constitute a taking of private property. In *Pennsylvania Coal Co. v. Mahon*,[8] the Court held that a regulation that barred a property owner from mining coal effected a taking because it had "very nearly the same effect for constitutional

5. 533 U.S. 606 (2001).

6. U.S. CONST. amend V.

7. An illegitimate exercise of the police power, though rare, clearly constitutes a taking. *See* Agins v. City of Tiburon, 447 U.S. 255, 260 (1980).

8. 260 U.S. 393 (1922).

purposes as appropriating or destroying" the right to mine the coal.[9] Before *Pennsylvania Coal* it was generally thought that only a physical appropriation of property could constitute a taking.[10] But Justice Holmes, writing for the majority, explained that "while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking."[11] This statement begs the question, how far is "too far"? Although this question has never been satisfactorily answered, a number of tests have been conceived to dispose of regulatory takings disputes.[12]

A. Per Se Rules

If a fact pattern fits into the parameters of one of the judicially defined per se rules, the inquiry is far simpler than if not.

1. Nuisance Abatement

No matter how economically disabling a regulation is, if it is intended to abate activities that are nuisances at common law, the regulation does not constitute a taking.[13] After all, the bundle of rights that inheres in property ownership does not include the right to act unlawfully. The Supreme Court, in *Lucas v. South Carolina Coastal Council*,[14] declared that when the regulated use "was *always* unlawful . . . it was open to the State at any point to make the implication of those background principles of nuisance and property law explicit."[15]

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9. *Id.* at 414.

10. *See* Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1014 (1992) (tracing the history of regulatory takings jurisprudence).

11. *Pennsylvania Coal Co.*, 260 U.S. at 415. Justice Holmes opined that when the "seemingly absolute protection [of property by the Fifth Amendment] is found to be qualified by the police power, the natural tendency of human nature is to extend the qualification more and more until at last private property disappears." *Id.*

12. *See* Goldblatt v. Hempstead, 369 U.S. 590, 594 (1962) ("There is no set formula to determine where regulation ends and taking begins."); Penn Cent. Transp. Co. v. New York City, 438 U.S. 104, 124 (1978) (describing the cases as "essentially ad hoc, factual inquiries"); *see also* Richard A. Epstein, *Takings: Descent and Resurrection*, 1987 SUP. CT. REV. 1 (presenting an overview of the relevant tests).

13. *See* Mugler v. Kansas, 123 U.S. 623, 665, 671 (1887).

14. 505 U.S. at 1003.

15. *Id.* at 1030. The *Lucas* Court found fault with the traditional distinction between noxious uses of property, which harm others, and non-noxious uses, the elimination of which merely benefit the general public. *Id.* at 1024–26; *see, e.g.*, Miller v. Schoene, 276 U.S. 272, 278–81 (1928) (allowing the uncompensated destruction of red cedar trees because they contained a fungus that kills apple trees); Hadacheck v. Sebastian, 239 U.S. 394, 411–12 (1915) (upholding a zoning ordinance which forced a brickyard to shut down). The *Lucas* Court declared that "the distinction

2. Permanent Dispossession

When one of the next two per se rules apply, the property owner automatically receives compensation, unlike the first rule, which absolves the government without further inquiry. If the government regulation permanently dispossesses an owner of his property, the regulation effects a taking. The leading permanent dispossession case is *Loretto v. Teleprompter Manhattan CATV Corp.*,[16] in which the Supreme Court noted that "permanent physical occupation authorized by government is a taking without regard to the public interests that it may serve."[17]

3. Loss of All Economically Beneficial Use

Under *Lucas*, a regulation constitutes a per se taking if the owner loses all economically beneficial use of his property,[18] assuming the regulation does not reiterate a common law nuisance restriction or constitute a background principle of state law.[19] The Court explained that "regulations that leave the owner of land without economically beneficial or productive options for its use . . . carry with them a heightened risk that private property is being pressed into some form of public service under the guise of mitigating serious public harm."[20] At the core of this rule is an aversion to compelling private individuals

between 'harm-preventing' and 'benefit-conferring' regulation is often in the eye of the beholder." 505 U.S. at 1024.

16. 458 U.S. 419 (1982).

17. *Id.* at 426; *see* Kaiser Aetna v. United States, 444 U.S. 164, 180 (1979); United States v. Causby, 328 U.S. 256, 261 (1946).

18. This per se rule also applies when the owner is left with a mere "token interest." *See* Palazzolo v. Rhode Island, 533 U.S. 606, 631 (2001).

19. *See Lucas*, 505 U.S. at 1027. What constitutes a background principle is the subject of frequent debate. The disagreement is between those who think background principles evolve over time and those who think that they are static. *Compare* James S. Burling, *Private Property Rights and the Environment After* Palazzolo, 30 B.C. ENVTL. AFF. L. REV. 1, 13–14 (2002) *with* Timothy J. Dowling, *On History, Takings Jurisprudence, and* Palazzolo: *A Reply to James Burling*, 30 B.C. ENVTL. AFF. L. REV. 65, 75–77 (2002). The question is whether the *Lucas* Court meant to include only common law nuisance restrictions or also statutes, regulations, and non-nuisance rules in the concept of background principles. Other commentators argue that a background principles examination should include analysis of the public trust doctrine. *See, e.g.*, Patrick A. Parenteau, *Unreasonable Expectations: Why* Palazzolo *Has No Right to Turn a Silk Purse into a Sow's Ear*, 30 B.C. ENVTL. AFF. L. REV. 101, 110–12 (2002). The answer to this question determines to what extent the state can act to alter the background principles that inhere in the title under *Lucas*. If state property law can become part of the title, then the legislature can change the background principles by enacting new legislation; the courts too could conceivably change the principles through revised interpretation of existing laws and regulations.

20. *Lucas*, 505 U.S. at 1018.

to bear the entire burden of a public benefit.[21] When the property retains economic viability, the theory goes, the individual only has to bear the burden of partial economic loss or simple inconvenience; but, when the property loses all value, the uncompensated owner sacrifices too much for the common good.[22]

B. The *Penn Central* Balancing Test

Clearly some fact patterns do not fit conveniently into any of the per se rules. Consider an environmental regulation that forbids commercial development of certain types of land, but permits single-family residences. Commercial development is not outlawed at common law, and the owner has been neither permanently dispossessed of his land nor denied all economically beneficial use. In *Penn Central Transportation Co. v. New York City*,[23] the Supreme Court devised a balancing test to be used in resolving cases that cannot be decided by reference to the per se rules. Under *Penn Central*, courts must consider "[t]he economic impact of the regulation on the claimant";[24] "the extent to which the regulation has interfered with distinct investment-backed expectations";[25] and "the character of the governmental action."[26]

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

22. An interesting and spirited debate continues over the proper "denominator" in an analysis of whether a property has lost all economically viable use. For example, if a regulation renders five acres of a twenty acre parcel valueless, does this constitute a total taking of the five acres, which would require compensation, or a 25 percent taking of the twenty acres, which probably would not require compensation? *See* Marc R. Lisker, *Regulatory Takings and the Denominator Problem*, 27 RUTGERS L.J. 663, 664–70 (1996); Epstein, *supra* note 12, at 16–17; *see also Lucas*, 505 U.S. at 1016–17 n.7; Keystone Bituminous Coal Ass'n v. DeBenedictus, 480 U.S. 470, 497 (1987). The denominator question may have been settled by *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 535 U.S. 302 (2002). In it, the Supreme Court held that a development moratorium does not always constitute a total taking for the moratorium period. *See id.* at 1477–90. While the majority extended this holding on the temporal denominator to the question of the acreage denominator, it was dicta and the final answer remains to be given. See Anthony Saul Alperin, Palazzolo—*The Supreme Court's Decision Departs from Accepted Doctrine*, 34 URB. LAW. 297, 311–12 (2002) for a discussion of *Tahoe-Sierra Preservation Council's* impact on the denominator question. *See also* J. David Breemer, *Temporary Insanity: The Long Tale of* Tahoe-Sierra Preservation Council *and Its Quiet Ending in the United States Supreme Court*, 71 FORDHAM L. REV. 1, 23–52 (2002) (examining the holding from a critical perspective).

23. 438 U.S. 104 (1978).

24. *Id.* at 124.

25. *Id.*

26. *Id.*

1. Economic Impact

After articulating the economic impact factor, the *Penn Central* Court quickly noted that "diminution in property value" by a regulation "reasonably related to the promotion of the general welfare" does not, by itself, constitute a taking.[27] The Court then cited two cases previously held to involve no taking, despite significant dips in property value.[28] The Court gave no useful guidance as to how this factor should be applied.[29] In *Penn Central*, the company's continued ability to use the land as a railroad terminal was enough to weigh against finding a compensable taking.[30]

2. Investment-Backed Expectations

Justice Brennan, writing for the majority in *Penn Central*, noted that "the extent to which the regulation has interfered with distinct investment-backed expectations"[31] is a factor in determining whether compensation is required. However, the Court quickly pointed out that "'[g]overnment hardly could go on if to some extent values incident to property could not be diminished without paying for every such change in the general law.'"[32] In fact, the *Penn Central* Court rejected the owner's claim for compensation after New York City's Landmarks Preservation Commission denied permission to construct an office building over Grand Central Terminal. The Court noted that the company's "primary expectation" for the property was its continued use as a railroad terminal, with which the regulation did not interfere.[33] Moreover, in rejecting the proposal for a large office building over the terminal the Commission did not pass judgment on whether a smaller structure would be permissible.[34] The challenged preservation regulation further provided for transferable development rights to parcels in the vicinity that, while not equal in value to the lost right to build on Grand Central, were of considerable

27. *Id.* at 131.

28. *See id.* The two cases are *Euclid v. Ambler Realty Co.*, 272 U.S. 365 (1926), and *Hadacheck v. Sebastian*, 239 U.S. 394 (1915). In *Euclid* the property at issue decreased in value by 75 percent, while in *Hadacheck* the decrease was 87.5 percent.

29. JOHN G. SPRANKLING, UNDERSTANDING PROPERTY LAW 666 (2000).

30. *Penn Central Transp. Co.*, 438 U.S. at 136.

31. *Id.* at 124. The concept of investment-backed expectations in regulatory takings law was originally proposed by Frank Michelman. *See* Frank I. Michelman, *Property, Utility, and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law*, 80 HARV. L. REV. 1165 (1967).

32. *Penn Central Transp. Co.*, 438 U.S. at 124 (quoting Pennsylvania Coal Co. v. Mahon, 260 U.S. 393, 413 (1922)).

33. *Id.* at 136.

34. *Id.* at 136–37.

value.[35] Therefore, the Court determined that the regulation did not interfere with the owner's investment-backed expectations enough to effect a regulatory taking requiring just compensation.[36]

3. The Character of Governmental Action

In *Penn Central* the Court pointed out that a physical invasion of property is more likely to qualify as a taking than when government "interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good."[37] The Court shied away from a distinction between harm-preventing and benefit-conferring regulations. Instead, it described earlier cases that seemed to turn on this distinction as upholding regulations "expected to produce a widespread public benefit and applicable to all similarly situated property."[38] The Court indicated that in cases in which the legislature has reasonably decided that health, safety, morals, or the general welfare is best protected by the regulation, there is no taking.[39]

C. Application of the *Penn Central* Balancing Test

1. The Bundle of Property Rights and Reasonableness

In *Andrus v. Allard*,[40] a 1979 decision, the Supreme Court validated a law that prohibited the sale of Native American artifacts, reasoning that "where an owner possesses a full 'bundle' of property rights, the destruction of one 'strand' of the bundle is not a taking, because the aggregate must be viewed in its entirety."[41] In *Allard*, there was no taking because the owners retained the right to possess, transport, donate, devise, and exhibit the artifacts.[42] In a decision from the same year, *Kaiser Aetna v. United States*,[43] the Court granted a takings claim based on the government's attempt to restrict the property owner's right to exclude others from its land.[44] In *Kaiser Aetna*

35. *Id.* at 137.
36. *Id.* at 137–38.
37. *Id.* at 124.
38. *Id.* at 133 n.30. *But see* SPRANKLING, *supra* note 29, at 666 ("In all probability, a nuisance-prevention regulation is less likely to be viewed as a taking than one that . . . is mainly oriented toward benefiting the public.").
39. SPRANKLING, *supra* note 29, at 665–66.
40. 444 U.S. 51 (1979).
41. *Id.* at 65–66.
42. *Id.* at 66.
43. 444 U.S. 164 (1979).
44. *Id.* at 393.

the U.S. Army Corps of Engineers sued to prevent a developer from altering a coastal pond and channel in an attempt to provide private access to the ocean.[45] The Court held that the government could not prevent the developer from excluding the public without providing compensation.[46] The decision was influenced by the Corps' failure to require a permit for the improvements that were subsequently the basis for the government's claim that the developer could not exclude the public.[47] Also notable was the slight shift by the Court from "distinct" to "reasonable" in its discussion of investment-backed expectations.[48] Taken together, *Allard* and *Kaiser Aetna* are confusing precedent to decipher. Investment-backed expectations only seem to be relevant regarding the entire spectrum of rights associated with property, but government action, or inaction, may disrupt the balance.[49] The *Kaiser Aetna* insertion of reasonableness into the test is of particular importance because subsequent decisions have evaluated the perceived validity of a property owner's expectations rather than examining the effect of the regulation on those expectations.[50]

2. Notice

In *Secesion Suarez v. Gelabert*[51] the Puerto Rican government imposed restrictions on the property owner's right to extract sand from the land. A federal district court rejected the property owner's taking claim because "[t]here was no reasonable expectation" that the owner could continue to use the property in the way it had previously been used "without there being some governmental restrictions and limitations."[52] This court included the expectation of possible future governmental regulation in its examination of the reasonableness of the property owner's investment-backed expectations. This notice element was broadened in *Ruckelshaus v. Monsanto Co.*[53] In *Monsanto*, the plaintiff chal-

45. *Id.* at 167–69.
46. *Id.* at 179–80.
47. *Id.*
48. *Id.* at 175. There is debate over whether this shift signified a change to an objective from a subjective test or an indication that balancing the public and private interests is important. *See* Daniel R. Mandelker, *Investment-Backed Expectations: Is There a Taking?*, 31 WASH. U. J. URB. & CONTEMP. L. 3, 14 (1987); Lynda J. Oswald, *Cornering the Quark: Investment-Backed Expectations and Economically Viable Uses in Takings Analysis*, 70 WASH. L. REV. 91, 115–16 (1995).
49. Daniel R. Mandelker, *Investment-Backed Expectations in Taking Law*, 27 URB. LAW. 215, 218 (1995).
50. R.S. Radford & J. David Breemer, *Great Expectations: Will* Palazzolo v. Rhode Island *Clarify the Murky Doctrine of Investment-Backed Expectations in Regulatory Takings Law?*, 9 N.Y.U. ENVTL. L.J. 449, 460–61 (2001).
51. 541 F. Supp. 1253 (D.P.R. 1982).
52. *Id.* at 1260.
53. 467 U.S. 986 (1984).

lenged a statute that authorized a federal agency to disclose data submitted by applicants seeking to register pesticides.[54] Because this would entail the disclosure of trade secrets, the plaintiff claimed a taking.[55] The Supreme Court held that the plaintiff did not have sufficient investment-backed expectations to justify compensation because it had constructive notice of the regulation.[56] In *Monsanto* the constructive notice took the form of a possibility that the government would extend regulation in what was already a heavily regulated industry. The Court also pointed out that, upon submission of the data, the plaintiff was aware of the conditions, and proceeded in the hope of an economic advantage.[57] However, *Monsanto* was a personal property case and three years later, in *Nollan v. California Coastal Commission*,[58] the Court rejected the constructive notice formulation in the realm of land-use restrictions.[59] Yet this line of cases illustrates the shift from a search for existing investment-backed expectations to an examination of the reasonableness of those expectations and provides the foundation for a possible examination of actual notice in real property takings cases.

3. Residual Value

In *Keystone Bituminous Coal Ass'n v. DeBenedictis*,[60] the Supreme Court found no taking when a statute prohibited a coal company from mining what amounted to two percent of its available coal. The Court held that there was "no showing that petitioners' reasonable 'investment-backed expectations' have been materially affected by the additional duty to retain the small percentage."[61]

In *Lucas* the Supreme Court articulated a difference between total takings cases and partial takings cases, in which the property retains some residual value.[62] It is only in the latter situation that the *Penn Central* reasonable

54. *Id.* at 998–99.

55. *Id.* at 1001.

56. *Id.* at 1006. Radford & Breemer, *supra* note 50, at 464, points out that the Court followed the *Monsanto* construction of reasonable investment-backed expectations in *Connolly v. Pension Benefit Guaranty Corp.*, 475 U.S. 211 (1986), and *Bowen v. Gilliard*, 483 U.S. 587 (1987).

57. *Id.* at 1006–07.

58. 483 U.S. 825 (1987).

59. *See* Mandelker, *supra* note 49, at 221–23. Daniel Mandelker points out that it was unclear whether Justice Scalia meant to remove constructive notice from takings considerations entirely or only to remove it as a bar to a takings claim. *Id.* at 220. Justice Scalia later made it clear that he believes it should be removed from the analysis. *See* Palazzolo v. Rhode Island, 533 U.S. 606, 636–37 (2001) (Scalia, J., concurring).

60. 480 U.S. 470 (1987).

61. *Id.* at 499.

62. Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1016–17 & n.7 (1992).

investment-backed expectations examination has a role.[63] When the property loses all value, a per se taking has occurred. Of course, the property retains value in the vast majority of cases.

Judicial application of the *Penn Central* balancing test has not followed a coherent pattern. Few absolutes have been recognized. Yet the basic framework has centered on an examination of the existence, or lack of, reasonable investment-backed expectations.[64]

D. What Are Reasonable Investment-Backed Expectations?

Reasonable investment-backed expectations have become an increasingly important issue in regulatory takings jurisprudence, while the other two *Penn Central* balancing test factors are now of questionable relevance.[65] Regulatory takings cases that are not decided by one of the per se rules usually turn on reasonable investment-backed expectations.[66] However, "Supreme Court decisions hardly have been coherent in their treatment of investment-backed expectations in taking cases."[67] The Court has not progressed much beyond the admonition that the expectation must be more than a "unilateral expectation or an abstract need"[68] and must be rooted in "justice and fairness."[69] This concept has been particularly troublesome for courts because of the traditional

63. See Radford & Breemer, *supra* note 50, at 480–82, for a discussion of how lower courts misinterpret the *Lucas* holding, conflating the idea of background principles of state law that inhere in the title and reasonable investment-backed expectations. Justice Kennedy added to this confusion in his *Lucas* concurrence when he wrote that reasonable investment-backed expectations have a role in determining whether the property has lost all of its value. *See Lucas*, 505 U.S. at 1034 (Kennedy, J., concurring). The majority held no such thing and this interpretation makes little sense because of the per se nature of the *Lucas* rule. Yet some courts have followed Justice Kennedy at the cost of further confusing regulatory takings law. *See, e.g.*, Good v. United States, 189 F.3d 1355, 1361 (Fed. Cir. 1999); Loveladies Harbor, Inc. v. United States, 28 F.3d 1171, 1179 (Fed. Cir. 1994).

64. For an argument that Justice Brennan did not intend to create a three-factor balancing test in *Penn Central*, but instead to subsume investment-backed expectations within the economic impact prong, see Zach Whitney, Comment, *Regulatory Takings: Distinguishing Between the Privilege of Use and Duty*, 86 MARQ. L. REV. 617, 632–35 (2002). This would explain at least some of the confusion courts have had interpreting the *Penn Central* test. More persuasive is that reasonable investment-backed expectations should be the focus of the balancing test because the other two prongs simply reiterate two of the per se rules. The economic impact prong is the *Lucas* total taking per se rule, while the character of the governmental action prong is the physical invasion per se rule. That leaves an examination of reasonable investment-backed expectations when the per se rules do not apply.

65. *See* Radford & Breemer, *supra* note 50, at 450 (noting that "recent years have seen a growing judicial tendency to rely on this poorly defined doctrine [of investment-backed expectations] to deny regulatory takings claims").

66. SPRANKLING, *supra* note 29, at 667.

67. Mandelker, *supra* note 49, at 225.

68. Ruckelshaus v. Monsanto Co., 467 U.S. 986, 1005 (1984) (quoting Webb's Famous Pharmacies, Inc. v. Beckwith, 449 U.S. 155, 161 (1980)).

69. Kirby Forest Indus., Inc. v. United States, 467 U.S. 1, 14 (1984).

conception of an expectation as something less than a right.[70] Courts have looked at the reasonableness and investment-backed aspects of the concept separately in determining a property owner's reasonable investment-backed expectations.

1. Reasonableness

Courts usually focus on the reasonableness prong in deciding regulatory takings cases. Michael Berger has identified twelve factors that courts consider in determining the reasonableness of a property owner's expectations:

> (1) the severity and extensiveness of regulations at the time the property was purchased; (2) the past regulatory history of the specific property; (3) the degree of impairment of the uses of the property; (4) the uses available before enactment of the challenged regulation; (5) the novelty or expectedness of the governmental action; (6) whether specifically (and traditionally) recognizable "sticks" were removed from the owner's bundle of property rights; (7) whether any rights (like the transferable development rights in *Penn Central*) were substituted for those impaired; (8) whether existing uses were permitted to continue; (9) whether government representations were formal or informal; (10) the ability to sell the property to others at a fair price; (11) the general power of government to regulate; and (12) the harshness of the local regulatory and legal climate.[71]

Courts consider postregulation title transfer, the subject of this Comment, in evaluating the reasonableness of the new title holder's investment-backed expectations.[72] This is Berger's first reasonableness factor. The implication is that if an owner takes title to regulated land, then he has notice of the restrictions and cannot claim a taking. In other words, the restrictions on the land are part of the title that he has received. This Comment will examine the logic of this theory in Part IV. For now it suffices to say that courts have used this factor, and the others identified by Berger, to determine the reasonableness of a property owner's investment-backed expectations.

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70. Michael M. Berger, *Happy Birthday, Constitution: The Supreme Court Establishes New Ground Rules for Land-Use Planning*, 20 URB. LAW. 735, 767 (1988).

71. *Id.* at 765–67 (footnotes omitted). Berger also cites a number of cases illustrating how courts have applied these factors. *See id.* at 766–67 nn.156–67.

72. *See* Burling, *supra* note 19, at 40–46 (analyzing cases that insert title transfer into the assessment of reasonableness); Brent L. Slipka, Case Comment, *Constitutional Law—Inverse Condemnation: Supreme Court Gives Property Owners New Rights*, 78 N.D. L. REV. 177, 183–86 (2002) (considering whether postregulation acquisition eliminates standing to bring a claim).

2. Investment-Backed

The phrase "investment-backed expectations" is confusing on its face. It is unclear to what degree a property owner must be allowed to realize a return on his investment. Further, can a property owner who has made no financial investment in his property—for instance one who receives title through gift or inheritance—expect the same protections as a property owner who paid a substantial sum for his property?

Justice Brennan noted in *Penn Central* that the regulation allowed the property owner "not only to profit from the Terminal, but also to obtain a 'reasonable return' on its investment."[73] Courts have split on whether profitability should determine whether a taking has occurred.[74] The Supreme Court's decision in *Allard* has been a source of confusion on this topic. In *Allard*, a federal statute that prohibited the sale of bird parts and feathers was challenged as effecting a taking. The Court held that the mere reduction in value of the property did not constitute a taking and that the owner was not entitled to the most profitable use of his property.[75] This is not particularly surprising, but the Court went on to say that "loss of future profits . . . provides a slender reed upon which to rest a takings claim" and that courts are not competent to perform a profitability analysis.[76]

Another question is whether Justice Brennan, in using the phrase "'reasonable return' on its investment," meant to protect investment but not speculation.[77] Often courts have ignored this distinction and only applied the bias when it is clear that land speculation is the intent of the property owner.[78] Courts have also examined whether a title holder has followed through with planned development.[79]

The phrase "investment-backed expectations" implies that without financial investment the constitutional protections do not apply.[80] The Supreme

73. Penn Central Transp. Co. v. New York City, 438 U.S. 104, 136 (1978).

74. Berger, *supra* note 70, at 768. Berger cites a number of cases interpreting this factor in different ways. *See id.* at 768 nn.172–73.

75. Andrus v. Allard, 444 U.S. 51, 66 (1979).

76. *Id.*

77. Robert M. Washburn, *"Reasonable Investment-Backed Expectations" as a Factor in Defining Property Interest*, 49 WASH. U. J. URB. & CONTEMP. L. 63, 88 (1996). Robert Washburn defines land speculation as holding property to earn a profit on its capital appreciation when it is sold and investment as holding property to earn a profit on activities conducted on the land. *Id.*

78. *Id.* at 89.

79. *Id.* at 90.

80. At least to a certain degree this problem emanates from Michelman. He attempts to separate the speculator, who has no defined plan for what he will do with his land, from the owner, who is currently using the property in a defined way. *See* Michelman, *supra* note 31, at 1234.

Court indicated this in dicta in *Hodel v. Irving*.[81] This is an odd principle. It is hard to imagine why inherited property would be subject to less constitutional protection than purchased property and it seems unlikely that the Court would embrace this principle if it emerged as a central issue in a case.

Courts have focused primarily on the "reasonable" aspect of reasonable investment-backed expectations probably because of the uncertainty surrounding how "investment-backed" should be interpreted.[82] There has been no consensus on the meaning of "investment-backed" and the Supreme Court has never clearly addressed the issue.[83]

Just as the reasonable investment-backed expectations factor predominates over the other two *Penn Central* factors, the reasonableness prong of reasonable investment-backed expectations dominates most courts' analyses.

II. ALIENATION

John Locke wrote that property is the common gift of mankind.[84] But for much of history, property ownership was not attainable for common men. English and American property law history has witnessed a massive extension of land rights. One of the most important rights is the right to alienate property freely. Generally, the common law has acted to further this goal. The origins of the modern common law can be traced to twelfth and thirteenth century England and the rise of Parliament. Not surprisingly, considering the social structure of the time, property law was at the forefront of change.

A. The English Common Law

In feudal England, the king owned the land and granted parcels to ranking individuals, who then granted smaller parcels to others. This continued down the line until reaching those who actually worked the land.[85] This system created a complex hierarchy of individuals, in debt to one another and, ultimately, to the king. Property law in feudal times revolved around far different principles than those we honor today. The primary objective was to facilitate the seamless operation of service to lords and the king.[86] The ownership interest in land was complicated, and less concerned with the bundle of rights and

81. 481 U.S. 704, 715 (1987); *see* Oswald, *supra* note 48, at 116–17.

82. For a detailed discussion of courts' bifurcation of reasonable investment-backed expectations, see Berger, *supra* note 70 and Washburn, *supra* note 77.

83. *See* Washburn, *supra* note 77, at 91.

84. JOHN LOCKE, OF CIVIL GOVERNMENT 129 (Ernest Rhys ed., J.M. Dent & Son Ltd. 1943) (1690).

85. A. JAMES CASNER ET AL., CASES AND TEXT ON PROPERTY 253 (4th ed. 2000).

86. *Id.* at 254.

entitlements that inhere in modern ownership. Over time, however, land law evolved toward the recognition of entitlements, and at the core of this evolution was the freedom to alienate.

In feudal times landowners would often convey property to religious orders or the Church, thereby rendering large parcels of land inalienable.[87] This practice was forbidden by the Magna Carta in 1215 and the prohibition was confirmed by the Statute of Mortmain in 1279.[88] While this legislation kept the Church from receiving legal title to property, it could be circumvented by the passage of mere equitable title. This maneuver was banned in 1391.[89] Together, these laws reduced the amount of land owned by the Church. Because the Church was not a participant in the general stream of commerce, any land owned by the Church was effectively inalienable. Hence, this is an early example of legislation concerned primarily with keeping land free of alienation restrictions.

The Statute Quia Emptores, passed in 1290, is one of the early examples of government regulation of real property alienation.[90] The Statute restricted subinfeudation—the addition of individuals down the hierarchical line who owed services to the tenant—but not to the higher lord.[91] While the Statute performed a role in reducing the complexity of the feudal system,[92] and so arguably facilitated its downfall, it did not explicitly extend alienation rights. Yet the statute did grant affirmative property rights to a tenant: the right to substitute a different tenant in his place without permission from the lord and the right to subinfeudate by granting an estate less than a fee simple.[93] This affirmation of the rights of tenants was a major step toward the free alienation of property interests.

87. LEWIS M. SIMES & ALLAN F. SMITH, THE LAW OF FUTURE INTERESTS § 1114, at 7 (2d ed. 1956).

88. CASNER ET AL., *supra* note 85, at 266 n.21.

89. *Id.*

90. See *id.* at 259 for an edited, and helpful, excerpt of the statute:

> Forasmuch as purchasers of lands of the fees of great men and other lords have many times heretofore entered into their fees to be holden in fee of their feoffers and not of the chief lords of the fees, whereby the same chief lords have many times lost their escheats, marriages, and wardships, which thing seems very hard and extreme unto those lords and other great men, our lord the king, at the instance of the great men of the realm, ordained that it should be lawful for every freeman to sell at his own pleasure his lands so that the feoffee shall hold the same of the chief lord of the same fee, by such service and customs as his feoffer held before. [Here is a provision for division of the services due upon partial alienation.] This statute extendeth but only to lands holden in fee simple . . . .

Id.

91. See *id.* at 260 for an explanation of how the text of the statute did not make this prohibition clear, notwithstanding how it was interpreted.

92. *Id.*

93. *Id.*

The Rule in Shelley's Case and the Doctrine of Worthier Title similarly extended alienation rights even though that was not the intention of their advocates. The Rule in Shelley's Case converts a remainder in the heirs of the grantee into a vested remainder in the grantee, which merges with the grantee's life estate to create a present fee simple absolute.[94] The Doctrine of Worthier Title acts similarly, erasing a remainder to the heirs of the grantor.[95] Both the Rule in Shelley's Case and the Doctrine of Worthier Title stemmed from an aristocratic desire to perpetuate the payment of feudal incidents despite transfers of title.[96] Yet, while both rules are more complicated than described above, and could be avoided, the result was a more easily alienated estate in the grantee.

The gradual weakening of the fee tail is the most dramatic example of the common law trend toward unrestrained real property transfer. The fee tail estate was extremely popular in feudal England, but continued efforts by the courts to create disentailing devices eventually eliminated its prevalence. Prior to 1285 a conveyance "to A and the heirs of his body," which was intended to restrict the property to lineal descendants and, if the line ran out, to revert to the grantor, was instead interpreted by courts to grant a fee simple on the condition that A have heirs of the body.[97] Thus English courts interpreted the conveyance in a way that would free the property for transfer upon the satisfaction of one condition. This frustrated the intent of the grantor but released the property from a burdensome restriction. In response, Parliament passed the Statute De Donis Conditionalibus[98] in 1285, which created the fee tail estate. The statute and the resulting fee tail were direct attacks on the free

94. GRANT S. NELSON ET AL., CONTEMPORARY PROPERTY 274–76 (2d ed. 2002).

95. *Id.* at 276–77.

96. *Id.* at 274–77. The common law dictated that if the holder of a remainder received title to his property as a grantee from the original grantor, then the incidents of tenure payable to the lord would not arise. But if the remainder holder inherited property from the grantee of what was intended as a life estate, then the incidents did arise. So, by converting a deed that would create a life estate and remainder—both grants from the original property owner—into a grant of fee simple absolute to one individual who could then alienate his property freely, the feudal incidents were retained. *Id.*

97. *Id.* at 239–40.

98. 13 Edw. 1, c. 1 (1285) (Eng.). NELSON ET AL., *supra* note 94, at 240–41 translate into modern idiom an illustrative excerpt of the statute:

> Land is often given to a person and the heirs of his body with the condition expressed that if the same person dies without issue the land shall revert to the giver or his heir. Now it seems to the giver that his will being expressed it ought to be enforced, but it is not being enforced. The courts have held that as soon as the grantee has issue born he can alienate in fee simple and disinherit his issue. He can also cut off the reversion to the original grantor. Now, therefore, the King declares that from now on the will of the giver, according to the form of the gift, shall be observed. Specifically, the person to whom the land is given shall have no power to alien the land. Instead, the land will descend to the issue or, if issue fail, it shall revert to the giver.

Id.

alienability of real property. The fee tail was popular in aristocratic England because it made the destruction of the country's land wealth lineage nearly impossible.[99] However, "the search for free alienability of land remained a powerful force."[100] Soon English courts introduced common recovery, a device that facilitated avoidance of the fee tail restrictions.[101] Common recovery is a conveyance by means of a collusive lawsuit, which originally allowed the holder of the fee tail to merely cut off the interest of his heirs, but was eventually extended by courts to allow the holder to cut off the reversionary right of the grantor as well.[102] Courts wanted desperately to foil the Statute De Donis Conditionalibus and the fee tail conveyance. Currently, while the fee tail can still theoretically exist, legislation in England and the United States make it generally obsolete.[103]

In 1536 the Statute of Uses was passed in England, the major effect of which was to convert equitable estates (uses) into legal estates by operation of law.[104] The Statute of Uses also permitted transfer of real property with a mere document, thus eliminating the traditional feoffment requirement.[105] As a result, the competing claims and attendant obstacles that complicated the transfer of property were eased. While this was not the expressed goal of the Statute of Uses, it was an effect that must have been recognized at the time. In 1677 the Statute of Frauds went a step further, requiring a written instrument for a valid transfer, thereby rendering the feoffment useless and providing for a reasonable system of title security.[106] In contrast to earlier property law legislation, the very purpose of the Statute of Frauds was "to make ordinary people more secure in their property holdings and in their contracts and to protect them against trumped-up claims."[107] By dictating a mandatory method of transfer, the Statute of Frauds not only secured property rights, it also freed land for uncontroversial transfer. The Statute of Frauds, at its basest level, was aimed at

99. *See id.* at 241 ("The fee tail estate was one of the devices for perpetuating and preserving English landed estates.").

100. *Id.*

101. The decision that first introduced common recovery was *Taltarum's Case*, Y.B. 12 Edw. 4, 19 (1472). A. JAMES CASNER & W. BARTON LEACH, CASES AND TEXT ON PROPERTY 216 (3d ed. 1984), describes the decision as "an all-time high in legalistic hocus-pocus."

102. *Id.* at 216.

103. *See* NELSON ET AL., *supra* note 94, at 241–43.

104. The Statute was the brainchild of King Henry VIII, who was running out of money and needed to concoct a system whereby landowners were unable to escape the feudal incidents owed to the Crown. CASNER ET AL., *supra* note 85, at 265–66.

105. CASNER & LEACH, *supra* note 101, at 693. For a further explanation of the reasons for, and effects of, the Statute of Uses, see *id.* at 317–35. Feoffment consisted of a ceremony in which the transferor gave the transferee a physical symbol of the property transfer, such as a twig, and announced the estate that he was transferring. *See* NELSON ET AL., *supra* note 94, at 205.

106. *Id.* at 693.

107. *Id.* at 695.

releasing property from encumbrances and promoting safe and reliable alienation.

The Rule against Perpetuities was first articulated in the Duke of Norfolk's Case.[108] Courts employed this rule primarily because of a concern with releasing land for unfettered alienation.[109] The problem of the fee tail had already been addressed by the judicially created process of disentailing and contingent remainders were destroyed when the preceding vested or possessory estate expired.[110] But the Rule against Perpetuities attacks a different problem: the potential for executory interests to indefinitely restrict property alienation. The Rule, though more complicated, can be stated simply as such: "No interest is good unless it must vest, if at all, not later than twenty-one years after some life in being at the creation of the interest."[111] Joel Dobris sums up the reasons for the Rule:

> The standard list of charges against the perpetuity, the arrangement that lasts longer than the reasonable period allowed by the Rule, includes the following: perpetuities tie up the management of property and prevent property from reaching its highest and best use; perpetual trusts concentrate wealth to the detriment of society; all trusts unwholesomely interfere with the character, laboring, and investment productivity of the beneficiaries; and perpetuities lead to intergenerational inequities.[112]

All of Dobris' concerns relate to the free alienation of land. The lack of efficient use of property when it is tied up for years is a standard argument against restrictions on alienation.[113] The concentration of wealth in the hands of a select few is another concern; if the land is unencumbered by alienation restrictions, there will be shifts amongst those who own land, and the wealth they accrue thereby, and amongst those who do not own land. Perpetuities artificially restrain this natural market dynamic and provide a disincentive to use land productively. Finally, perpetuities create intergenerational inequities because alienation is controlled by those who are no longer living.

B. Property Rights in America

Stanley Katz argues that the English law of inheritance, based on primogeniture, was scorned by the American Revolutionaries because it reinforced

108. 22 Eng. Rep. 931 (Ch. 1682).
109. CHARLES DONAHUE, JR. ET AL., CASES AND MATERIALS ON PROPERTY 550 (3d ed. 1993).
110. *See id.* at 529–32.
111. JOHN CHIPMAN GRAY, THE RULE AGAINST PERPETUITIES 191 (4th ed. 1942).
112. Joel C. Dobris, *The Death of the Rule Against Perpetuities, or the RAP Has no Friends—An Essay*, 35 REAL PROP. PROB. & TR. J. 601, 614 (2000).
113. *See infra* text accompanying notes 126–129.

the aristocratic aspects of English rule.[114] They reacted by reforming the law to rid it of primogeniture and entail.[115] The reform was part and parcel of a guiding ideology promoting egalitarian ends.[116] Thomas Jefferson in particular was bothered by the concentration of land wealth in the hands of an elite class and wanted to redistribute land, both for efficiency ends and egalitarian ideals.[117] While Jefferson's views were extreme, his concern about encumbered and inefficiently used property was addressed by eviscerating English restrictions on property alienation. Thus, colonial America witnessed another episode in the progression of the law toward free alienation of real property.

Adverse possession, the common law device whereby a claimant gains title to property by holding adversely to the true owner for a certain number of years without the owner asserting his right, can be viewed as yet another common law bias in favor of free alienation of property. Judge Richard Posner presents an economic explanation for adverse possession, first espoused by Justice Oliver Wendell Holmes:

> Over time, a person becomes attached to property that he regards as his own, and . . . the restoration of the property would cause only moderate pleasure. This is a point about diminishing marginal utility of income. The adverse possessor would experience the deprivation of the property as a diminution in his wealth; the original owner would experience the restoration of the property as an increase in *his* wealth. If they have the same wealth, then probably their combined utility will be greater if the adverse possessor is allowed to keep the property.[118]

The point is that it would be better for society as a whole to vest the property in the hands of the individual who values it most. At the crux of this

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114. Stanley N. Katz, *Republicanism and the Law of Inheritance in the American Revolutionary Era*, 76 MICH. L. REV. 1 (1977).

115. *Id.* at 11.

116. *Id.* at 14–15. Stanley Katz quotes from North Carolina's 1784 revision of the law of inheritance, 1 The Public Acts of the General Assembly of North Carolina, ch. 22 (J. Iredell ed., F.X. Martin rev. 1804):

> Whereas it will tend to promote that equality of property which is of the spirit and principle of a genuine republic, that the real estates of persons dying intestate should undergo a more general and equal distribution than has hitherto prevailed in this state . . . .
>
> And whereas it is almost peculiar to the law of Great-Britain, and founded in principles of the feudal system, which no longer apply in that government, and can never apply in this state, that the halfblood should be excluded from the inheritance . . . .
>
> And whereas entails of estates tend only to raise the wealth and importance of particular families and individuals, giving them an unequal and undue influence in a republic, and prove in manifold instances the source of great contention and injustice . . . .

Id.

117. Katz, *supra* note 114, at 15–18.

118. RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 89–90 (5th ed. 1998) (footnote omitted).

is the idea that the potential owner who values the property more, does so because he will use it more efficiently. So adverse possession forces a transfer of the land. In order to have one's land taken through adverse possession, the land owner must be detached enough from his property to have no knowledge of the trespass.[119] In such an instance, the property not only is going to waste from an economic standpoint, but is unlikely to be transferred to an owner who will make better use of it. The property has been taken out of the stream of commerce and, effectively, is encumbered by a restriction on alienation. The law effects a forced transfer so a new owner will make use of the property and, if he so chooses, alienate the land.

It is not just property law that evinces this concern for unrestricted alienation. In the United States, long-term capital gains are taxed at a significantly lower rate than ordinary income.[120] Real property is one of the major types of capital assets that receive this special treatment.[121] One of the reasons, and the most persuasive, for this disparity is Congress' reluctance to inhibit the transfer of real property for tax reasons.[122] Gains are not taxed until realized and sale or transfer is an indisputable realization event. Thus, property owners who do not wish to be taxed at high rates on the appreciation of real estate are tempted to hold on to their property to avoid the tax consequences. Congress taxes capital gains at lower rates to avoid undesirable stagnation of invested capital.

Similarly, the potential taxpayer can avoid federal recognition of his realized gains on the sale or transfer of real property by immediately reinvesting in real estate.[123] While there are restrictions on this provision,[124] it reveals the same concern that real property owners will resist transfer for tax reasons. Such concern illustrates the continued importance placed on the unfettered alienation of real property.

C. Why Does the Common Law Show a Preference for Unrestricted Alienation?

Having examined ways in which the common law prefers unrestricted alienation of real property, we must ask why this is so. "[P]rivate volition with respect to the transfer of property is an essential element in the way our society

119. Granted, the majority of adverse possession cases are matters of minor encroachments, such as steps protruding over a boundary line. But the theory behind the doctrine remains the same.

120. *See* MARVIN A. CHIRELSTEIN, FEDERAL INCOME TAXATION 347 (9th ed. 2002).

121. *Id.*

122. *Id.* at 351.

123. *See id.* at 335–39.

124. For example, the real estate must be business or investment related, and must be domestic. *Id.*

uses the market mechanism to effect an efficient allocation of resources."[125] But efficiency is by no means the sole justification for the common law's distinct preference for free alienation. Efficiency and other reasons are explained below.

1. Efficiency

Land should be easily alienable primarily to promote efficiency. The evolution of the law reflects this concern.[126] It is inefficient to tie up property for long periods of time with no way of shifting title to those who will use the property to greater value. A device such as the fee tail, which potentially restricts the transfer of a parcel of land far into the future, frustrates the efficiency realized by shifting property to those who value it most and will use it to its highest social value.[127] For instance, consider a tract of land used by the present owner for growing corn. The land could also be used for mining coal, a far more profitable endeavor. But the owner is not interested in the hassle associated with coal mining and is perfectly content to make his living selling corn. If a potential buyer comes along, interested in mining the coal, he will inevitably offer more for the property than the land is worth to the owner because of the difference in the value of corn and coal. In this situation it would be inefficient for greater society if the title were restricted such that the property could not be sold to the aspiring coal miner.[128] There is a reason why coal is worth more than corn: The demand is higher and the supply scarcer. Thus it clearly would be for the greater good to allow the sale, as the land could be used to mine coal. The current owner would receive the value he deems equal or greater to the future value of his farming activity on the property; the buyer would receive the land at a price he believes would be worth it to him once he profits from coal mining; and the desire of the greater populace for coal over corn would be satisfied. Land taken out of the general stream of commerce has no insurance against underproductivity, which reduces the national wealth.[129]

125. DONAHUE, JR. ET AL., *supra* note 109, at 449.

126. *See* POSNER, *supra* note 118, at 86 ("The history of English land law is largely a history of efforts to make land more readily transferable, and hence to make the market in land more efficient.").

127. *But see id.* (positing that perhaps laws which frustrate the intent of the grantor are "paternalistic and hence questionable from an efficiency standpoint").

128. *See, e.g., id.* at 37 ("Efficency requires a mechanism by which the farmer can be induced to transfer the property to someone who can work it more productively. A transferable property right is such a mechanism.").

129. *See* SIMES & SMITH, *supra* note 87, at 10; *see also* THOMAS JARMAN, A TREATISE ON WILLS 219 (2d ed. 1843) *quoted in* SIMES & SMITH, *supra* note 87, at 11:

> The necessity of imposing some restraint on the power of protracting the acquisition of the absolute interest in, or dominion over property, will be obvious, if we consider, for a moment, what would be the state of a community in which a considerable portion of the land and capital was locked up. That free and active circulation of property, which is one of the springs

2. Bias Against Restricting Land Wealth to Historically Privileged Families

It is not in the public interest to allow a wealthy aristocracy to persist because of restraints on the alienation of real property.[130] Allowing certain people to remain artificially wealthy without regard to recent productivity is not only undesirable from an efficiency standpoint, but also from a general policy perspective. A preferable system permits those who do well to accumulate wealth, while leaving those who cannot or will not do well, to attain less.[131]

3. Fair Balance Between the Right to Control Property and the Avoidance of Dead Hand Control

Title holders generally desire the ability to convey property however they choose. But certain conveyances frustrate that same desire in subsequent title holders. Thus, a balance should be struck that comes close to giving everyone what they want. A regime of free alienation absent dead hand control does exactly that. Title holders can convey their title in any form as long as it does not unreasonably burden a subsequent title holder. While there are some restrictions that a conveyor can place on the title, generally those that make conveyance impossible are forbidden.

III. JUSTIFICATIONS FOR THE LIMITED RESTRICTIONS ON THE ALIENATION OF REAL PROPERTY

This Comment has examined the overwhelming bias in the Anglo-American common and statutory law in favor of unrestricted alienation. Restrictions nevertheless exist.

> as well as the consequences of commerce, would be obstructed; the improvement of land checked; its acquisition rendered difficult; the capital of the country gradually withdrawn from trade; and the incentives to exertion in every branch of industry diminished. Indeed, such a state of things would be utterly inconsistent with national prosperity . . . .

Id.

130. *See, e.g.*, Edgerly v. Barker, 31 A. 900, 906 (N.H. 1891) ("Perpetuities, as applied to real estates, were conducive to the power and grandeur of ancient families, and gratifying to the pride of the aristocracy; but they were extremely disrelished by the nation at large, as being inconsistent with the free and unfettered enjoyment of property."); *see also* W. Barton Leach, *Perpetuities in Perspective: Ending the Rule's Reign of Terror*, 65 HARV. L. REV. 721, 727 (1952) (pointing out that the Rule against Perpetuities was thought to have protected the "threat to the public welfare from family dynasties built either on great landed estates or on great capital wealth").

131. RESTATEMENT OF PROPERTY § 2132 (1944). But see SIMES & SMITH, *supra* note 87, at 13, for an argument that succession and estate tax laws are more effective at preventing the undeserved accumulation of familial wealth. Further, society today is more interested in protecting those who are economically unsuccessful, not ensuring their continual struggle. *Id.*

Direct restraints on alienation come in three forms: (1) disabling restraints, which simply prohibit alienation, (2) forfeiture restraints, which cause the property to revert to the grantor or a third party upon an attempt at alienation, and (3) promissory restraints, which make the owner liable for a breach of a covenant upon an attempt to transfer.[132] Generally, all of these limitations on fees are invalid.[133] Indirect restraints on alienation, which merely discourage transfer, are similarly frowned upon. Yet both direct and indirect restrictions do exist.

There are three justifications for restricting real property alienation: to protect the interests of third parties, to realize distributional goals, and to grant additional property entitlements to the current title holder.

A. Externalities

Guido Calabresi and Douglas Melamed aptly describe a classic situation that calls for restrictions on the sale of real property:

> [I]f Taney were allowed to sell his land to Chase, a polluter, he would injure his neighbor Marshall by lowering the value of Marshall's land. Conceivably, Marshall could pay Taney not to sell his land; but, because there are many injured Marshalls, freeloader and information costs make such transactions practically impossible. The state could protect the Marshalls and yet facilitate the sale of the land by giving the Marshalls an entitlement to prevent Taney's sale to Chase but only protecting the entitlement by a liability rule. It might, for instance, charge an excise tax on all sales of land to polluters equal to the estimate of the external cost to the Marshalls of the sale. But where there are so many injured Marshalls that the price required under the liability rule is likely to be high enough so that no one would be willing to pay it, then setting up the machinery for collective valuation will be wasteful. Barring the sale to polluters will be the most efficient result because it is clear that avoiding pollution is cheaper than paying its costs—including its costs to the Marshalls.[134]

The action that would lead to the greatest possible good, and therefore the most efficient result, is to restrict the sale of the land. In this hypothetical the externalities (costs to third parties) are great, and will not be absorbed in the evaluations of the transaction costs by those privy to the transaction. The market acts inefficiently because major interests are not realized by the primary

132. JOHN P. DWYER & PETER S. MENELL, PROPERTY LAW AND POLICY: A COMPARATIVE INSTITUTIONAL PERSPECTIVE 185 (1998).

133. *Id.*

134. Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089, 1111 (1972).

parties, and are thus neglected, resulting in greater costs to society than are justified by the uninhibited sale of the land.

B. Distributional Goals

Occasionally restrictions on the transfer of real property are justified by a policy of allocating resources to certain classes of people.[135] For instance, the Homesteading Acts[136] were passed to facilitate the development of the western United States. The Acts were predicated on the theory that available land should not go to those already financially successful, but instead to those who lacked wealth.[137] The Acts included restrictions on the transfer of land in order to insure that the land would be developed by nonwealthy farmers and ranchers.[138] The land transfer restrictions served to keep wealthy land speculators from gathering up the property after the government gave title to the homesteaders.[139] In this situation, the government had two major goals: the development of western lands and the concentration of the available property in the hands of a certain class of people. Without restrictions on alienation these goals likely would have been frustrated.

Various sections of the U.S. Code recognize restrictions on alienation applicable to certain Native American lands.[140] The distributive goal is that the U.S. government, having seized land in North America over a long period, has subsequently given some of the land back to Native Americans with the express goal of having it remain in their possession. Free transfer of this land would undoubtedly frustrate this goal over time, as the land made its way into the general real estate market.

Distributional goals that are implemented through restrictions on the alienation of real property clearly have costs associated with them.[141] In order for a distributional goal to warrant an alienation restriction, the value of the goal should outweigh the cost of the restriction. Because free alienation of property is efficient most of the time, it is difficult to outweigh the costs of restriction.

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135. *See id.* at 1114.

136. *See, e.g.*, Act of May 20, 1862, ch. 75, 12 Stat. 392 (repealed 1976).

137. *See* Susan Rose-Ackerman, *Inalienability and the Theory of Property Rights*, 85 COLUM. L. REV. 931, 960 (1985).

138. *Id.*

139. *Id.* at 940.

140. *See, e.g.*, 25 U.S.C. §§ 391–416j (2000).

141. See POSNER, *supra* note 118, at 92–94, for a discussion of the distributive effects of property rights assignments.

C. Granting of Additional Property Rights

There are instances when potential restrictions on alienation are beneficial to the current property holders and the law affords these individuals the opportunity to take advantage of that potential entitlement. Leasehold estates may contain extensive restrictions on alienation.[142] Thus, even though the tenant has the right of possession, he may not have the right of alienation. Precisely because they inhibit alienation, lease provisions that prohibit assignment and sublease are strictly constructed, but are generally valid.[143] This is an acknowledgement of an overriding property right possessed by the landlord to determine who uses his land. This property right outweighs the bias in favor of unrestricted alienation. Restrictions are "justified as reasonable protection of the interests of the lessor as to who shall possess and manage property in which he has a reversionary interest and from which he is deriving income."[144] In order to ensure the continued viability of his property interest, the law grants the lessor this entitlement.

Similarly, the gradual demise of the Rule against Perpetuities is due to the desire to allow title holders to restrict the subsequent alienation of their property. Historically, the argument in favor of the Rule was that property should not be tied up for long periods of time. Now, however, the law is allowing an increasing number of perpetuities.[145] While it appears unlikely that a majority of states will repeal the Rule,[146] there is a general lack of concern about its future existence.[147] Dobris points out that the perceived harm of perpetuities is fading.[148] Placing restrictions on one's own assets has always been popular and society now tends to look more favorably on large pools of capital and attempts to perpetuate one's wealth.[149] Moreover, trusts are increasingly popular, and not just among those who create them.[150] Trustees now have a high degree of investing freedom, so society is hardly worried that the assets will be inefficiently used.[151] People want to restrict the alienation of their property to

142. NELSON ET AL., *supra* note 94, at 539.

143. *Id.* Some courts have held that leasehold alienation restrictions must be "reasonable" to be valid, but that is a clear minority position. *See, e.g.*, Kendall v. Ernest Pestana, Inc., 709 P.2d 837, 841 (Cal. 1985).

144. ROBERT S. SCHOSHINSKI, AMERICAN LAW OF LANDLORD AND TENANT § 8:15, at 579 (1980).

145. Dobris, *supra* note 112, at 606–10.

146. *Id.* at 663.

147. *Id.* at 655.

148. *See id.* at 613.

149. *Id.* at 623–26.

150. *Id.* at 627.

151. *Id.* Joel Dobris gives an extensive list of reasons why trusts may no longer be detrimental, and why the general public views them favorably. *See id.* at 627–32.

ensure a continuing benefit to their heirs. Whether or not this is a positive development is questionable; but the trend in the direction of relaxing the Rule against Perpetuities is the result of a policy permitting property owners to realize an additional entitlement tied to their assets. If a title holder chooses to restrict the future movement of his property, the law is more likely now to look on this desire favorably.

The demise of the Rule against Perpetuities and the unusual right to restrict alienation granted to lessors are fundamentally different than other types of restrictions on alienation. Leaving aside the question of whether they are warranted, they are clearly concessions to the present title holder that enable him to have a hand in who will benefit from the property in the future. They are not blanket restrictions on alienation and are very narrow.

IV. *PALAZZOLO V. RHODE ISLAND*

Westerly is a small village on the southern tip of Rhode Island. It is a beach town whose population of 23,000 doubles during the summer months, as tourists arrive to enjoy the pleasant weather and beautiful waterfront.[152] Westerly is also home to Anthony Palazzolo and his parcel of beachfront wetlands and uplands, which became the most recent battleground in the regulatory takings debate.[153]

A. Facts and Background

In 1959, Anthony Palazzolo and his associates formed Shore Gardens, Inc. (SGI) to purchase three undeveloped adjoining parcels, encompassing about eighteen acres along Winnapaug Pond, an intertidal pond with an outlet to the Atlantic Ocean.[154] Palazzolo then bought out his associates to become the sole shareholder of SGI.[155] Over the next decade SGI divided the parcel into various lots and applied to the Rhode Island Division of Harbors and Rivers to fill the entire property in order to make it suitable for construction.[156] The application was denied.[157] SGI then filed a similar application and while that one

152. Marcia Coyle, *'I Will Do No Harm,'* NAT'L L.J., Mar. 26, 2001, at A17.

153. The Supreme Court decision in *Palazzolo* was highly anticipated by advocates on both sides of the regulatory takings divide. *See generally* Dwight H. Merriam, *The* Palazzolo *Palaestra*, 23 ZONING & PLAN. L. REP. 93 (2000). Numerous interest groups and government entities filed amicus briefs. Dwight H. Merriam & Bryan W. Wenter, Palazzolo *Promotes Property Rights*, 24 ZONING & PLAN. L. REP. 45, 49 (2001). For a sample of advocates' reaction to the decision, see *id.* at 51–53.

154. Palazzolo v. Rhode Island, 533 U.S. 606, 613 (2001); Coyle, *supra* note 152.

155. *Palazzolo*, 533 U.S. at 613.

156. *Id.* at 613–14.

157. *Id.* at 614.

was pending, filed a third proposing more limited filling and the development of a private beach club.[158] The second two applications were passed to the Rhode Island Department of Natural Resources, which originally approved, but then reversed based on adverse environmental impacts.[159] There was no further attempt to develop the property until 1983, by which time state legislation had created the Rhode Island Coastal Resources Management Council (Council) to oversee the protection of the state's coastal areas.[160] Also, in 1978, SGI's corporate charter was revoked and title to the Winnapaug Pond property passed to Palazzolo, the company's sole shareholder.[161] In 1983, Palazzolo applied to the Council to allow him to fill the property.[162] The application was rejected, citing detrimental environmental impacts and perceived insufficiencies in the application.[163]

In 1985, Palazzolo again submitted an application to the Council requesting permission to construct a private beach club.[164] Once more the Council rejected Palazzolo's request, ruling that to justify filling the salt marsh the proposal must serve "a compelling public purpose which provides benefits to the public as a whole as opposed to individual or private interests."[165] Palazzolo appealed this decision to the Rhode Island state courts, where the Council's decision was affirmed.[166]

B. History in the State Courts

Palazzolo then filed a separate action in the Rhode Island courts, claiming that the State's wetlands regulations effected a taking of his property and that the state's failure to compensate him violated the Fifth Amendment of the U.S. Constitution, as extended to Rhode Island by the Due Process Clause of the Fourteenth Amendment.[167] Palazzolo claimed that under *Lucas* he was entitled to compensation, as the State had deprived him of "all economically beneficial use" of his property.[168] The Superior Court rejected Palazzolo's claim.[169]

158. *Id.*
159. *Id.*
160. *Id.*
161. *Id.*
162. *Id.*
163. *Id.* at 614–15.
164. *Id.* at 615.
165. *Id.* (citing Rhode Island Coastal Resources Management Program § 130A(1) (as amended, June 28, 1983)).
166. *Palazzolo*, 533 U.S. at 615.
167. *Id.*
168. *Id.* at 615–16.
169. *Id.* at 616.

Palazzolo appealed to the Rhode Island Supreme Court, which also rejected his claim.[170] This court held that the claim was not ripe, as Palazzolo had not exhausted all possible channels in seeking development approval; that he had not lost all economically beneficial use of his property because the uplands portion of the tract still had development value; and that Palazzolo could not challenge regulations enacted before he gained title to the property from SGI.[171]

C. Supreme Court Majority

In *Palazzolo v. Rhode Island* the U.S. Supreme Court addressed all three grounds relied on by the Rhode Island Supreme Court in rejecting Palazzolo's claim, upholding one, but reversing the other two.[172]

1. Ripeness

While the Rhode Island Supreme Court indicated that Palazzolo's claim was not ripe because the Council rejected his extensive development plan but did not rule on a less intrusive proposal, the U.S. Supreme Court majority pointed out that this argument was contradicted by "the unequivocal nature of the wetland regulations at issue and by the Council's application of the regulations to the subject property."[173] Clearly Palazzolo was not going to be allowed to fill the wetlands. Moreover, the Court held, the fact that the development potential of the uplands parcel was not entirely clear did not make the claim unripe.[174] The Court also dismissed other contentions by Rhode Island that Palazzolo had not done enough to determine what uses of the property the State might approve, and that he had been less than forthcoming in the present action about his plans for development.[175] The ripeness argument was a threshold issue that, if the Court had ruled in favor of Rhode Island, would have cut off Palazzolo's claim. Because the claim was ripe, the *Lucas* and *Penn Central* tests could then be applied to the facts.[176]

170. Palazzolo v. State *ex rel.* Tavares, 746 A.2d 707, 717 (R.I. 2000).

171. *Id.* at 714, 716–17.

172. Not surprisingly, the decision left Anthony Palazzolo with little additional insight as to whether he would eventually receive compensation from the state of Rhode Island. *See* Anthony Flint, *Landlocked on the Coast for 40 years, Anthony Palazzolo Has Battled R.I. over Property Rights, All the Way to the Supreme Court*, BOSTON GLOBE, Nov. 3, 2002, at B1.

173. *Palazzolo*, 533 U.S. at 619.

174. *Id.* at 621–22.

175. *Id.* at 624–26.

176. Various commentators have examined the impact of the *Palazzolo* ripeness holding. *See, e.g.*, Burling, *supra* note 19, at 19–27 (arguing that *Palazzolo* shifts the burden to the government to indicate other uses for the property once a permit application has been rejected); Dowling, *supra* note 19, at 81–87 (claiming that the *Palazzolo* ripeness holding will have little effect on government action);

2. The *Lucas* Test

The Court acknowledged the considerable debate concerning the denominator that should be used to determine whether a regulation deprives the owner of all economically beneficial use.[177] Because Palazzolo argued that his property should be conceptually divided so that the uplands portion, which retained value, was distinct from the wetlands portion, which he could not develop, this question would determine whether *Lucas* applied. But the Court sidestepped the issue by noting that Palazzolo did not make the denominator claim in state court, or in his petition for certiorari, so it could not be raised at a later juncture.[178] Accordingly, the premise before the Supreme Court was that the entire property was the denominator in Palazzolo's claim. As it clearly retained value, the claim failed the *Lucas* test.

3. Notice

Palazzolo's notice claim is of primary interest to this Comment. When title transferred to Palazzolo from SGI, the wetlands regulations already were in force. The Rhode Island Supreme Court held that this fact negated a *Lucas* claim—as the regulations were then background principles of state law—and a *Penn Central* claim, as Palazzolo had no reasonable investment-backed expectations upon taking title to the land.[179] The court deemed that a title holder such as Palazzolo took title with notice, whether constructive or actual, of the restrictions on land use.[180] The U.S. Supreme Court found this to be unpersuasive. Justice Kennedy, writing for the majority, expressed concern with the implication that the Takings Clause would, by the logic of the Rhode Island court, have an "expiration date."[181] Moreover, Justice Kennedy pointed out that, as evidenced by this case, ripening of a claim can take years, during which time a transfer of title would extinguish the claim, thereby allowing the state to "secure a windfall for itself."[182] This would put title holders with varying characteristics in different positions with respect to the Takings Clause; for example, an older owner would be in a worse position than a similarly situated

Sheldon Whitehouse & Michael Rubin, *The Supreme Court's* Palazzolo *Decision—Its Bark Is Worse than Its Bite*, 30 B.C. ENVTL. AFF. L. REV. 155, 156–57 (2002) (arguing that *Palazzolo* added almost nothing new to the regulatory takings ripeness doctrine).

177. *Palazzolo*, 533 U.S. at 631; *see also supra* note 22.

178. *See Palazzolo*, 533 U.S. at 631–32. See Dowling, *supra* note 19, at 95–99, for a discussion of the *Palazzolo* denominator question dicta and the subsequent decision in *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 535 U.S. 302 (2002). *See also supra* note 22.

179. Palazzolo v. State *ex rel.* Tavares, 746 A.2d 707, 716–17 (R.I. 2000).

180. *Id.*

181. *Palazzolo*, 533 U.S. at 627.

182. *Id.*

younger owner.[183] In examining Rhode Island's claim that the regulations were background principles of state law under *Lucas*, the Court held that "a regulation that would otherwise be unconstitutional absent compensation is not transformed into a background principle of the State's law by mere virtue of the passage of title."[184] If it were, the regulation would be a background principle of state law for some title holders, but not for others.[185] The Court held that notice is not a bar to a compensation claim under either a *Lucas* or a *Penn Central* test.[186]

D. What Does It Mean?

A transfer of title does not extinguish the potential for government compensation based on application of a *Lucas* test showing loss of all economically beneficial use. In Palazzolo's case, the Court rejected the *Lucas* claim regardless, because the uplands portion of his property clearly retained substantial value. In the future it should be clear that transfer of title is irrelevant to a *Lucas* claim. A *Lucas* claim is based on a showing of loss of all economically beneficial use of the property, followed by possible defenses by the government, including demonstrating that the regulation in dispute is a background principle of state law or abates a common law nuisance. The Supreme Court's holding in *Palazzolo* eliminates any place for an examination of title transfer in such an analysis.[187] However, it does not do the same for a *Penn*

183. *See id.*

184. *Id.* at 629–30.

185. *Id.* at 630.

186. See Michael A. Culpepper, Comment, *The Strategic Alternative: How State Takings Statutes May Resolve the Unanswered Questions of* Palazzolo, 36 U. RICH. L. REV. 509 (2002), for an examination of post-*Palazzolo* takings issues and how state property rights statutes inform an analysis of them.

187. There is by no means consensus on this point. *See, e.g.*, Michael C. Blumm, Palazzolo *and the Decline of Justice Scalia's Categorical Takings Doctrine*, 30 B.C. ENVTL. AFF. L. REV. 137, 145–46 (2002); John D. Echeverria, *A Preliminary Assessment of* Palazzolo v. Rhode Island, 31 ENVTL. L. REP. 11112, 11118–21 (2001). These commentators cite Justice Kennedy's *Lucas* concurrence, in which he argued that reasonable investment-backed expectations are relevant to the *Lucas* per se test as well as to the *Penn Central* balancing test, as support for their premise that title transfer is still relevant to a *Lucas* claim. *See* Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1034 (1992) (Kennedy, J., concurring). Moreover, Justice Kennedy cited his *Lucas* concurrence in his *Palazzolo* majority opinion. *See* Palazzolo v. Rhode Island, 533 U.S. 606, 617 (2001). However, Justice Kennedy's *Lucas* concurrence is not the law and was not joined by a single additional justice. It is also clearly in conflict with Justice Scalia's binding majority opinion in *Lucas*. *See Lucas*, 505 U.S. at 1014–32. The apparent concern of these commentators is a potential manufactured taking. If a property owner's land consisted of 2 percent wetlands rendered undevelopable by government regulation, the owner could conceivably sell only that portion to an individual who could then press a *Lucas* total taking action for compensation. The worry is that if notice were irrelevant to a *Lucas* claim, then the government would lose a crucial, and justifiable, defense to this action. This would admittedly be an undesirable application of the Takings Clause, but the proposed notice rule is ill suited to combat it. Rather, the property examined in the takings claim should be the parcel as it existed when the government passed the regulation. This is logical, as the government was acting with respect to a defined parcel,

Central claim.[188] A *Penn Central* analysis is aimed at the balancing of three factors, of which the reasonable investment-backed expectations prong has become the most important.[189] While the Court's holding in *Palazzolo* makes clear that title transfer should not be dispositive in rejecting a *Penn Central* claim, it does not eliminate the possibility that the transfer will be used as part of a balancing of factors comprising the reasonableness of the title holder's investment-backed expectations. This is debated in the *Palazzolo* concurrences and dissents.

1. O'Connor Concurrence

Justice O'Connor made one primary point in her concurrence: Pre-acquisition regulation enactment should be a factor in a *Penn Central* analysis of reasonable investment-backed expectations. Justice O'Connor submitted that "it would be just as much error to expunge this consideration from the takings inquiry as it would be to accord it exclusive significance."[190] In Justice O'Connor's opinion, the regulations in place when an owner takes title should inform the reasonableness of the owner's investment-backed expectations, although they should not be the only factors in such an analysis.[191] Justice O'Connor's concern in pressing this point is that "if existing regulations do nothing to inform the analysis, then some property owners may reap windfalls and an important indicium of fairness is lost."[192]

2. Scalia Concurrence

Justice Scalia took the opposite view in his concurrence. He described the situation that Justice O'Connor seemed to be worried about as such:

> [A] sharp real estate developer, realizing (or indeed, simply gambling on) the unconstitutional excessiveness of a development restriction

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not potential future parcels. This rule is consistent with expunging notice from takings claims. Just as courts should not allow an unconstitutional governmental act (taking property without paying just compensation) to become constitutional merely because title is passed, neither should courts allow a constitutional governmental act (regulating land under the legitimate authority of the police power) to become unconstitutional merely because of parcel division.

188. In *Nollan v. California Coastal Commission*, 483 U.S. 825, 833 n.2 (1987), the Court implied that notice is irrelevant to any takings claim. *See supra* text accompanying notes 51–60. In *Palazzolo*, Justice Kennedy referred to *Nollan* as "controlling precedent." *Palazzolo*, 533 U.S. at 629. Yet the *Palazzolo* majority expressly limited the holding to eliminating notice as a bar to a takings claim and did not reaffirm the categorical rule implied by *Nollan*. *See id.* at 629–30; *see also* Echeverria, *supra* note 187, at 11117–18 (proposing that *Nollan* can be reconciled with *Palazzolo* because the former involved a physical taking while the latter involved a regulatory restriction).

189. *See supra* text accompanying notes 23–63.

190. *Palazzolo*, 533 U.S. at 633 (O'Connor, J., concurring).

191. *Id.* at 634–36.

192. *Id.* at 635.

> that a naïve landowner assumes to be valid, purchases property at what it would be worth subject to the restriction, and then develops it to its full value (or resells it at its full value) after getting the unconstitutional restriction invalidated.[193]

Justice Scalia acknowledged that this might be a windfall, but a windfall like those we see every day in other transactions.[194] Moreover, while something can be said in the name of fairness for returning some of the windfall to the original owner, nothing can be said for returning it to the government.[195] In Justice Scalia's opinion, it is the government that caused the problem by acting unconstitutionally. To let the action stand because of a title transfer would be to give "the malefactor the benefit of its malefaction."[196]

3. Ginsburg, Breyer, and Stevens Dissents

Justice Ginsburg, joined by Justice Breyer and Souter, dissented from the majority because she believed that Palazzolo's claim was unripe and that he

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193. *Id.* at 636 (Scalia, J., concurring).

194. *Id.*

195. *Id.* at 636–37.

196. *Id.* at 637. Justice Scalia likened the government's actions to those of a thief who sells property with false title at a bargain rate. *Id.* Justice O'Connor responded to this with the following footnote:

> Justice Scalia's inapt "government-as-thief" simile is symptomatic of the larger failing of his opinion, which is that he appears to conflate two questions. The first question is whether the enactment or application of a regulation constitutes a valid exercise of the police power. The second question is whether the State must compensate a property owner for a diminution in value effected by the State's exercise of its police power. We have held that "[t]he 'public use' requirement [of the Takings Clause] is . . . coterminous with the scope of a sovereign's police powers." The relative timing of regulatory enactment and title acquisition, of course, does not affect the analysis of whether a State has acted within the scope of these powers in the first place. That issue appears to be the one on which Justice Scalia focuses, but it is not the matter at hand. The relevant question instead is the second question described above. It is to this inquiry that "investment-backed expectations" and the state of regulatory affairs upon acquisition of title are relevant under *Penn Central*. Justice Scalia's approach therefore would seem to require a revision of the *Penn Central* analysis that this Court has not undertaken.

Id. at 635 n.* (O'Connor, J., concurring) (citation omitted). Justice Scalia responded with a footnote of his own: "Contrary to Justice O'Connor's assertion, my contention of governmental wrongdoing does not assume that the government exceeded its police powers by ignoring the 'public use' requirement of the Takings Clause. It is wrong for the government to take property, *even* for public use, without tendering just compensation." *Id.* at 637 n.* (Scalia, J., concurring) (citations omitted). It does seem that Justice O'Connor misunderstands the crux of Justice Scalia's argument. Justice Scalia does not say that the government has no right to regulate Palazzolo's property. If he did, he would be saying that the State exceeded its police powers. Instead, he is saying that even when the State acts within the scope of its police powers, if that action constitutes a taking under the Fifth Amendment, the State violates the Constitution when it does not compensate the property owner.

failed to properly present his argument, relying on a *Lucas* claim and only adding a *Penn Central* theory upon appeal to the U.S. Supreme Court.[197] Yet she weighed in on the notice issue, opining that a title transfer can impair a *Penn Central* regulatory taking claim, but offering no further explanation.[198] Justice Breyer agreed with Justice Ginsburg that Palazzolo's claim was unripe, and also took the side of Justice O'Connor in her debate with Justice Scalia. While Justice Breyer stressed that a title transfer should not be dispositive,[199] he argued that a *Penn Central* inquiry, concerned as it is with "fairness and justice," is equipped to analyze this factor and include it if appropriate.[200]

Justice Stevens focused his dissent on the notice issue. He wrote that a taking is a discrete event that occurs at a certain moment in time and, therefore, a succeeding property owner should not receive compensation for an interest taken from a previous owner.[201] According to Justice Stevens, this must be so because the value of the interest taken is the value of the property at the time of the taking. The interest on the award accrues from that same time, so the recipient of the award should be the owner at that time.[202] Justice Stevens argued that the subsequent owner can seek to enjoin the enforcement of the regulations, but has no standing to sue for compensation.[203] After all, if the regulations were already in place when he acquired title, then he only received the reduced value of the property, and never lost anything to the government.[204]

197. *Id.* at 645–54 (Ginsburg, J., dissenting).

198. *See id.* at 654 n.3.

199. *Id.* at 654–55 (Breyer, J., dissenting).

200. *Id.* at 655.

201. *Id.* at 638–39 (Stevens, J., concurring in part and dissenting in part). Justice Stevens' opinion evinces general skepticism regarding the validity of regulatory takings claims in any context. Justice Stevens described the notion of regulations going so far as to merit compensation a "somewhat dubious proposition." *Id.* at 639 n.2. The entire opinion attempts to limit regulatory takings to the point that it is highly questionable whether one ever would occur under a Justice Stevens regime.

202. *Id.* at 639.

203. *Id.* at 642.

204. Justice Stevens wrote that his concern is with the possibility of a "one-time transfer of wealth from society at large to those individuals who happen to hold title to large tracts of land at the moment this legal question is permanently resolved." *Id.* at 645. This seems like an unfortunate thing to worry about, as resolution of the legal question certainly will not make even one regulation require compensation—it will simply expand the pool of individuals who stand to benefit from regulations that do effect takings, and hold the government accountable for such action. Moreover, a worry about who will benefit if the mandate of the Constitution is followed hardly seems an appropriate concern for someone whose sole task is to interpret the Constitution.

4. Summary

The *Palazzolo* majority ruled out notice as a disqualifier for a Fifth Amendment claim for compensation, notwithstanding Justice Stevens' protestations. However, the majority gave little guidance on whether courts should include this fact in an analysis of whether the claimant's investment-backed expectations were reasonable. Justice Scalia thinks it should have no role, while Justices O'Connor, Ginsburg, Souter, and Breyer think it should. This is no small matter. The inclusion of notice into the examination would present a major hurdle for any claimant who takes title after the enactment of the challenged regulations. Given Supreme Court authority that postregulation acquisition is relevant to an owner's investment-backed expectations, courts would probably assume that this title transfer eliminated such expectations. It would seem to be a nearly insurmountable obstacle in all but the rarest of title transfer cases.[205]

E. Notice and the Reasonableness of Investment-Backed Expectations

Justices O'Connor, Ginsburg, Souter, and Breyer believe that notice should be included in an examination of the reasonableness of a property owner's investment-backed expectations. Thus, a property owner who takes title when the land is already subject to regulation would have a harder time proving that his expectations were reasonable than an owner who took title before the contested regulation was passed. Justice Stevens thinks that the owner who takes title to property subject to preexisting regulations has no standing to make a claim for compensation. The majority, including Justice O'Connor, has ruled against him on this point. Presumably, given his loss on the first issue, Justice Stevens would sign on with Justices O'Connor, Ginsburg, Souter, and Breyer on the question of whether a title transfer should affect the reasonableness of investment-backed expectations. With five justices apparently taking this position, the Court is dangerously close to creating a new restriction on the alienation of real property that is entirely inconsistent with the aims of the common law.

1. The Common Law Preference and the *Palazzolo* Scenario

This Comment has examined the many instances in which the common law exhibits a bias in favor of the free alienability of real property. The situation in *Palazzolo* is comparable. Were the Court to adopt a rule that a title

205. *See* Echeverria, *supra* note 187, at 11118 (stating that pre-acquisition notice will bar most takings claims after *Palazzolo*).

transfer could impair a regulatory taking claim for compensation, the property in question would be effectively rendered inalienable. Imagine the following scenario. A state passes a regulation that restricts development of Paul's property. Paul is not sure, and cannot be sure, to what extent his developmental rights are impaired. In order to figure this out, he must submit applications to the proper state authority to determine what he can still do with his land. This can be a very long process. Until completed, any regulatory takings claim for compensation Paul might make would be unripe. Yet, under Justice O'Connor's system, a transfer of title from Paul to Sally would damage this claim for Sally. Paul would be left with a piece of property that is not only severely regulated by the government, but has also become virtually inalienable. Sally is interested in buying the property from Paul, and either developing the land after approval from the state authority, or challenging the regulation as an uncompensated regulatory taking. But the Court appears close to frustrating this desire.

Title can be transferred through will, intestate succession, and, in Anthony Palazzolo's case, through operation of law after a corporate dissolution. This is why Justice Stevens' position seems so bizarre. If a property owner dies, leaving a tract of regulated land to his daughter, Justice Stevens apparently would hold that the daughter has no standing to sue for compensation from the government. Assuming the government had effected a regulatory taking without providing compensation, the death of the father would allow the government to act unconstitutionally and reap a windfall out of fortuitous timing. Elderly people, unlikely to survive until the claim becomes ripe, would find themselves without any recourse against the government. Justice O'Connor's position, while more reasonable, threatens to reach the same result. Courts would have the discretion to ignore a transfer of title under such extreme circumstances. But they would also have the opportunity to rule for the government and reject claims for compensation based on the title transfer.[206] The common law protects the rights of property owners to alienate property and to feel secure in those transactions. Justice O'Connor's proposal would run contrary to this goal.

Justice O'Connor's proposal interferes with the efficiency goals that form the strongest justification for common law rules against restrictions on alienation. If Lucy owns a heavily regulated parcel of land, and has no interest in going through the process of ripening her claim for compensation from the government, it would certainly be in her best interest if she could sell. George wants the property to build a condominium complex. But in its

206. Radford & Breemer, *supra* note 50, at 478–95, demonstrates how courts often go out of their way to rule against property owners in regulatory takings cases.

regulated condition it is unclear whether George's proposal would be approved by the state regulatory authority. Under a Justice O'Connor regime, George would be unwilling to buy the property because if the authority rejected his development proposal, the transfer of title would be held against him in an action for compensation. It is hard to imagine that under this scenario a court would not hold that the transfer made George's investment-backed expectations unreasonable. So George will not buy the property, Lucy will not attempt development, and the property will remain idle. That may be the goal of the regulation, but it is either an inefficient use of property or an unconstitutional result. Perhaps the state authority would accept some development. George would find that out, but Lucy may not. If the regulations permit no development, then it is likely that this is an uncompensated taking in violation of the Fifth Amendment. In the first case, Justice O'Connor's system creates an inefficient use of property. In the second, it allows an unconstitutional governmental action to stand unchallenged.

If Justice Scalia's suggestion is heeded, a dramatically different outcome is realized. Without the prospect of eliminating a claim for compensation, the property can be freely alienated and will end up in the hands of the owner who values it most. George would be willing to purchase the property from Lucy because even if the state rejects his development proposal, he can proceed with a Fifth Amendment claim for just compensation from the government. Under Justice Scalia's regime, the property will make its way into the hands of an owner who will determine whether the property can be developed and, if not, whether the government has acted unconstitutionally. In direct contrast to Justice O'Connor's system, this scenario results in an efficient determination of the potential uses of the property and a challenge to unconstitutional government action. It is hard to argue against a regime that promotes efficient resource use and judicial scrutiny of unconstitutional acts, especially if the alternative results in idle land and unchallenged acts in contravention of the Constitution.

This situation is analogous to clouded title scenarios. An investor can purchase clouded title to land, attempt to clear the cloud, and if successful, have good title.[207] Not only is this practice condoned, it is encouraged. Clouded title is inefficient because it is hard to know who owns the land, and difficult for anyone to feel secure enough to invest in it. Severely regulated property is similar to property with a title cloud. Perhaps the regulation can be voided, perhaps it requires compensation, and perhaps it is simply a valid regulation that does not require compensation. But it is efficient to have the property in the hands of an owner who is interested in determining what can be done with the

207. 65 AM. JUR. 2D *Quieting Title* § 1 (2001).

land, just as it is efficient to have clouded title in the hands of someone who is interested in clearing the cloud. If a subsequent owner were not permitted to clear the cloud, this efficiency would go unrealized. By the same token, if a subsequent owner is not allowed to make a claim for just compensation from the government, then a similar efficiency will be ignored.[208]

2. O'Connor's Proposed Alienation Restriction

Clearly there is a strong efficiency argument for Justice Scalia's proposal. Moreover, in the absence of a compelling argument in favor of alienation restrictions, surely the common law trend toward free alienation should be followed. But Justice O'Connor made a proposal that would severely restrict alienation. Her proposal, however, suffers from a number of shortcomings.

a. The Windfall Concern

Justice O'Connor is concerned with property owners reaping windfalls by challenging regulations that were already in place when they purchased the property.[209] Apparently, in this Justice's view, such compensation rightfully belongs to the owner of the property at the time the regulation was enacted. Yet her solution would not permit either property owner to collect.[210] As Justice Scalia pointed out, this would avoid the windfall for the second owner, but provide a windfall for the government.[211] This generates a strange result, because the government is the one party that has acted unconstitutionally.[212]

Imagine the state passes a regulation that appears to affect the development potential of Blackacre, an undeveloped parcel of beachfront land owned by Susan. In order to develop the land Susan would have to submit applications to the state regulatory authority, wait for a response, and perhaps repeat until it is clear what is permitted under the regulation. Susan does not have the time or the interest required to complete this process. But her friend Adam is a real estate developer who has been hoping to build a beachfront resort for some

208. Two additional arguments against eliminating reasonable investment-backed expectations if on notice are that regulators can interpret old laws in new ways, thereby changing what the property owner was on notice of, and that permit requirements only provide notice to a prospective owner that he may need a permit, not he will be unable to develop. Burling, *supra* note 19, at 27–28; H. David Gold, Note, *Relaxing the Rules: The Supreme Court's Quest for Balance in* Palazzolo v. Rhode Island, 29 ECOLOGY L.Q. 137, 143–44 (2002).

209. *See Palazzolo*, 533 U.S. at 635 (O'Connor, J., concurring).

210. Justice O'Connor has not proposed, as Justice Stevens has, giving standing to the previous property owner in a suit against the government. She has merely impaired the claim of the current title holder.

211. *Palazzolo*, 533 U.S. at 636–37 (Scalia, J., concurring).

212. *Id.*

time. As we saw earlier, under Justice O'Connor's system, Adam would never purchase Blackacre. Under Justice Scalia's system, however, Adam could purchase from Susan both the title and an uninhibited potential claim against the government. Adam, unlike Susan, is in the business of negotiating with regulatory bodies to determine what can be done with regulated land. If he completes the process and feels that his property has been taken by the state in violation of the Fifth Amendment, he can then sue for just compensation.

But does Susan get shortchanged in this transaction? Not if the law were settled in favor of Justice Scalia's interpretation. Susan would sell her property knowing full well that Adam's title has value, whether through development rights or a claim against the government. This value would significantly raise the price of the regulated real estate. So Susan can sell her property, as she desires, thus losing just compensation from the government, but knowing that the transferability of her potential compensation claim will fetch her a fair price. Adam thinks that the value of the compensation claim or the development rights is higher than the selling price, while Susan thinks that the selling price is worth more to her than the uncertainty surrounding the property. This is exactly the type of free market transaction that the law should encourage. In fact, Susan is placed in a far better position under Justice Scalia's system than under Justice O'Connor's system. There are numerous personal and economic reasons why Susan would want, or need, to sell her property. Yet under a Justice O'Connor regime, she would not find a buyer willing to pay a fair price because of the uncertainty surrounding the property and the possibility that the transfer would eliminate a compensation claim by the purchaser. Under Justice Scalia's system she would receive a fair price. Perhaps Adam will get more from the government in compensation than he paid for the property, perhaps he will get less. Even if he gets more, he will have spent considerable time and money pursuing his claim. Susan and Adam might place different values on their time and have different levels of financial risk aversion. That is a question that courts are particularly incompetent to determine. It is just as likely that Adam will go through the application process and determine that the land does have some development value. Maybe that value will be worth substantially more than the price he paid to Susan. Should we worry about that? No; those are the risks and rewards of real estate transactions. Individuals determine what is of more value to them and sometimes it works out well and sometimes it does not.

What if Adam gets lucky? Susan is unsophisticated, unaware of the law, and sells the property for less than it is worth, not knowing that Adam can proceed with her claim against the state.[213] Does Adam then get a windfall that

213. See Gold, *supra* note 185, at 154–55, for an indictment of land speculators.

we should be concerned about? No more so than when someone makes a bad deal in the stock market. Susan's lack of knowledge, economic or legal, is not protected by Justice O'Connor's system.[214] Rather, Adam's savvy is punished.[215]

If Adam buys the land for below value and then obtains compensation from the government, should the purchase price factor into a determination of Adam's compensation?[216] Again, this would be an attempt to eliminate a supposed windfall for Adam. It is the government that has taken property for the public welfare. The value of that which has been taken is not affected by Adam's purchase price. If Adam made a wise investment, there is no compelling argument to allow courts to take that from him, while rewarding the government for an unconstitutional act.

b. The Proposed Restriction Is Inconsistent with the Traditional Reasons for Restricting Property Alienation

Even if the windfall concern was convincing, it would be an inappropriate reason for ignoring the strong preference in favor of the free alienability of real property. Earlier, this Comment discussed the justifications in the rare instances of restrictions on real property alienation. Those justifications do not apply in this case.

(1) Externalities Revisited

There are no externality arguments against Justice Scalia's proposal. There are no third party injuries that are ignored by his system. The government, theoretically acting for the greater societal good, has determined that a certain type of property is of greater value undeveloped than it would be developed. In order to keep this evaluation honest, the Constitution mandates

214. Susan would still receive a low price under Justice O'Connor's system. The only difference would be that Adam likely could not receive just compensation from the government.

215. Michelman also worries about this supposed windfall. *See* Michelman, *supra* note 31, at 1238 (hypothesizing a scenario in which an investor buys a parcel of land along a scenic highway for a discount while there has been public discussion of forbidding all development on such land). The fallacy of this concern is that it is created by the regime that those with the worry support. If the government regulates land in a draconian fashion, then surely the government owes just compensation. So why would someone sell the land for a price so low that the new owner would reap a windfall upon receiving just compensation? Clearly he would not, unless he really had to sell the land, and the claim against the government was not transferable. Under that scheme, the new owner would not get a windfall, the old owner would not get his just compensation and would get a low selling price, and the government would get the windfall. However, if the claim against the government was transferable, the selling price would go up to reflect that and the purchaser's windfall would be eliminated. Immediately, Professor Michelman's worry is eradicated, demonstrating the circularity of his concern. In trying to solve the problem, the problem is created.

216. Radford & Breemer, *supra* note 50, at 529–30, suggests that this might be appropriate.

that the costs of such an action are spread evenly among the beneficiaries, rather than landing on one individual. The government stands in the shoes of all third parties in this transaction. No one has an unprotected economic interest. It is a concern for unrepresented third parties that occasionally validates a restriction on alienation, but no party is unrepresented in this transaction.

(2) Distributional Goals Revisited

Distributional goals similarly do not justify Justice O'Connor's proposal. If Susan owns the property and decides she wants to sell it to Adam, there is no policy justification for keeping the property in Susan's hands. Unlike the Homesteading Acts or the provisions for Native American lands, there is no societal advantage to keeping the property in the hands of Susan's class of property owners.[217]

(3) Additional Property Entitlements Revisited

Occasionally, alienation restrictions are allowed because the current property owner desires them, and courts view this entitlement as important enough to outweigh the arguments in favor of free alienation. This justification does not apply here. Susan wants to sell her property and no previous owner had any objection to this. Restricting her right to sell in this case would constitute taking a property entitlement away, not granting a new one.

3. Government Regulation and the Supreme Court

Not only is Justice O'Connor's proposal inconsistent with the general aim of the common law to eliminate restrictions on the alienation of real property, it is inconsistent with doctrine in analogous situations. Consider Whiteacre, a parcel of real estate subject to a restrictive covenant confining use of the property to single family residences. Cindy, a speculator, purchases the property. She wants to convert the residence into a group home for mentally retarded adults. Cindy thinks this will make Whiteacre more valuable than the purchase price reflects, and plans to challenge the restrictive covenant as contrary to public policy. Clearly she will have standing to make this argument in court.[218] Cindy may win, or she may lose. But standing to challenge the restrictive covenant, of which she had notice when she took title, is passed with the underlying title. It is hard to imagine why this public policy claim is transferable, but a takings claim might not be. The former passes with the title

217. *See supra* text accompanying notes 136–140.
218. *See, e.g.*, Westwood Homeowners Ass'n v. Tenhoff, 745 P.2d 976 (Ariz. Ct. App. 1988).

because a clause that is contrary to public policy should not be left to stand simply through passage of time. Similarly, an unconstitutional act should not be allowed to stand without condemnation because of the passage of time.

Another similar situation is the transfer of property subject to physical invasion by the government. What if an eminent domain action has already been initiated? The claim could clearly be transferred, although such a transfer exemplifies Justice Stevens' concern about compensating someone other than the owner at the time of the taking. But what if the government had not indicated that it would voluntarily pay for the invasion, and then title was transferred? The new owner would have standing to sue for compensation. The Supreme Court is loath to allow the government to physically invade property without providing just compensation.[219]

The transfer of a regulatory takings claim for compensation is different than the two scenarios just described. Unlike in the case of an invalidation of a restrictive covenant, the government has to pay money when a court orders compensation for taken property. Unlike physical invasions, the Supreme Court is hesitant to extend the right to receive compensation based on a regulatory taking.[220] The two differences are intertwined. The existence of a regulatory takings doctrine means that the government will have to pay for its regulations, at least in some instances. Until the decision in *Pennsylvania Coal Co. v. Mahon*[221] there was no judicial recognition of regulatory takings. Once the Court recognized that regulations can go so far as to warrant compensation in order to avoid burdening one individual with the costs of the public welfare, the government had to absorb more of the costs of its regulations. Regulatory takings are controversial because they threaten to cost the government a lot of money. The opinions of Justice O'Connor and Justice Stevens evince a far greater concern for the financial welfare of the government than the financial welfare of the individual property owner. That, however, is not an accurate reflection of the concerns of the Constitution.

By limiting the ways in which property owners can receive compensation for regulatory takings, these justices are protecting the government till. They express no concern for the property owner who would receive a low price for his property because his claim against the government is not transferable. Rather, they express concern that the subsequent owner will get a windfall from a takings claim, and that the government will suffer. Justice O'Connor's solution does not adequately protect the interests of either property owner.

219. *See, e.g.*, Nollan v. Cal. Coastal Comm'n, 483 U.S. 825, 833 n.2 (1987).

220. Justice Stevens's *Palazzolo* dissent is a prime example of this reluctance. *See* Palazzolo v. Rhode Island, 533 U.S. 606, 639 n.2 (2001) (Stevens, J., concurring in part and dissenting in part).

221. 260 U.S. 393 (1922).

The only party her proposal protects is the government, which could avoid paying just compensation, and thus act unconstitutionally, with the help of a title transfer.

Why does the prospect of compensating regulatory takings worry the defenders of government regulation? If the cost of property regulations was spread among the benefactors, the general public, through the payment of just compensation and accordingly higher taxes, the broad enthusiasm for heavy regulation would likely quell. By imposing the costs on a small group of property owners, the general public is kept unaware of the costs of such regulation. While the small group suffers from an immense financial burden, the public approval of regulation continues.

Members of the Court have stepped in to propose a backhanded way to avoid the Fifth Amendment and the requirement of just compensation. The Constitution was written to protect the citizen from the government; the interpreters of that document should not strive to protect the government from the Constitution.

CONCLUSION

Of primary concern to many of those inclined to the government side of the regulatory takings debate is the protection of the natural environment. To many of them, any policy that increases the aggregate number of potential takings is anathema. Regulatory takings no doubt threaten legislative protection of environmental treasures. The government would likely respond to increased liability for regulatory takings not with an open checkbook, but rather with a rollback of regulation. That is a worrisome prospect to many people, including the author of this Comment. To many of us, paying increased taxes to fund the government's legitimate exercise of the police power is a small price to pay for the enduring benefit to our surroundings and to future generations.

Yet a proper, and permanent, solution to this problem is not to circumvent the Constitution by burdening individuals with the substantial cost of the public welfare. The solution does not lie in ignoring the foundational principles of real property law, such as the right to freely alienate. A lasting solution must consist of convincing the general public of the need for increased and meaningful legislative protection of the environment. Working within the confines of constitutional safeguards will establish a regulatory scheme that reflects the true value of the natural world to its many inhabitants without the public backlash against regulations that unfairly burden a small group of property owners.

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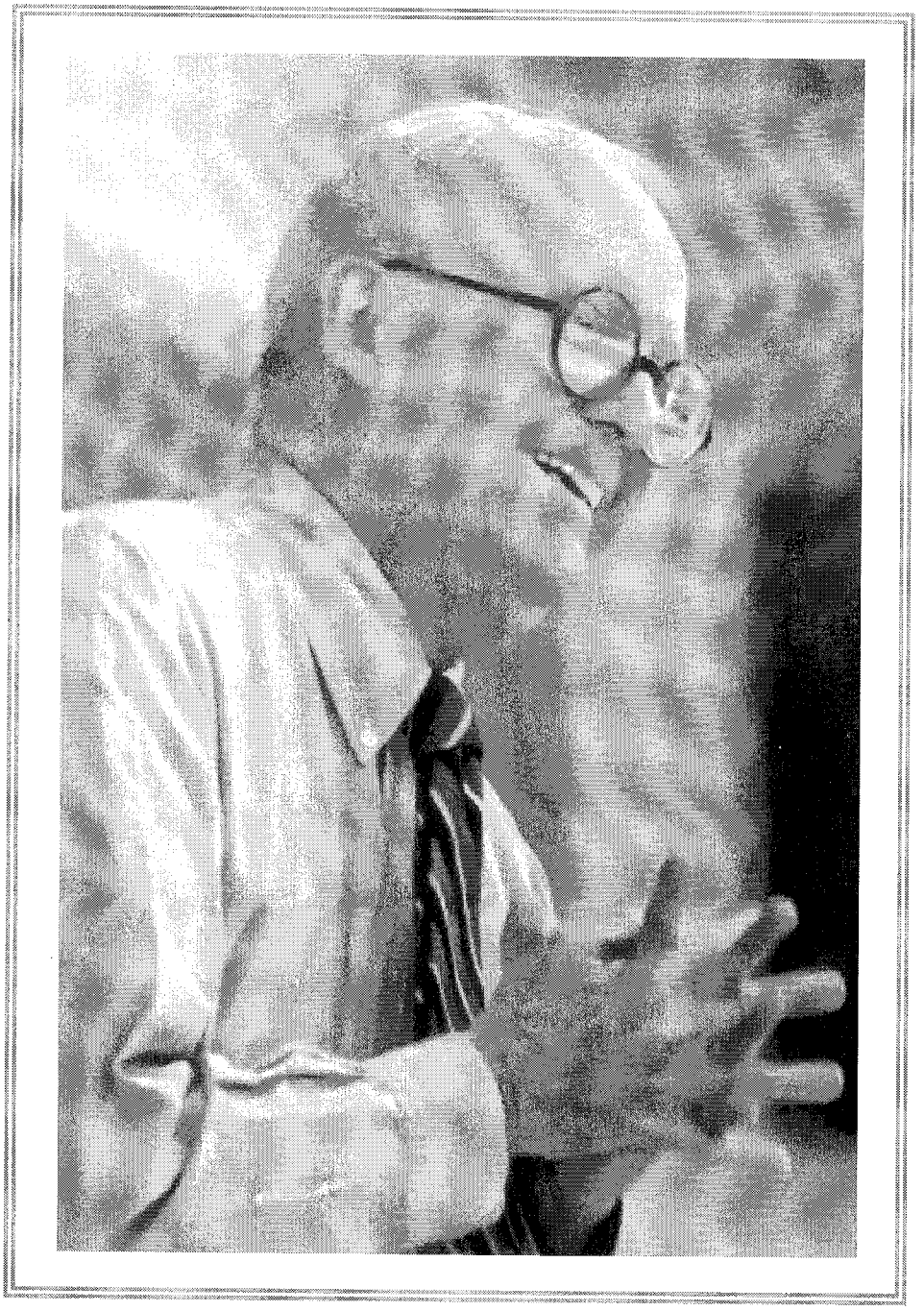

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