

# AGAINST AD HOCERY: A COMMENT ON MICHELMAN

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Frank Michelman believes that the Supreme Court is “moving noticeably towards a reformation of regulatory-takings doctrine.”<sup>1</sup> He criticizes this development, believing that the Court should instead engage in balancing. To him “balancing—or, better, the judicial practice of situated judgment or practical reason—is not law’s antithesis but a part of law’s essence.”<sup>2</sup> I argue in this Article that Michelman is wrong on both counts. Part I demonstrates that the Court does not appear to be articulating consistent formal principles in the takings area. Part II argues that it should try to do just that. Whatever the merits of ad hoc balancing in other areas of law, it has special difficulties in the takings area because of the important role of investment-backed expectations. Nonetheless, Michelman is correct in saying that the formal pattern he discerns is an undesirable one.<sup>3</sup> Thus, Part III suggests a way to think about the takings question that unifies physical and regulatory takings and provides a way to distinguish between government actions that require compensation and those that do not. Nevertheless, even a very imperfect, but clearly articulated, formal takings doctrine is likely to be superior to open-ended balancing.

## I. MICHELMAN AND THE STATE OF TAKINGS LAW

Michelman purports to discover a pattern by examining four regulatory takings cases decided in the 1987 Term.<sup>4</sup> At first glance, these cases seem an unlikely place to look for orderly doctrinal development. Contrary to the usual pattern in regulatory takings cases, the plaintiffs

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1. Michelman, *Takings*, 1987, 88 Colum. L. Rev. 1600, 1622 (1988).

2. *Id.* at 1629.

3. To Michelman, takings doctrine appears to be [resolving itself] into a series of categorical “either-ors”: *either* (a) the regulation is categorically a taking of property because (i) it works a permanent physical occupation (however practically trivial) of private property by the government . . . or (ii) it totally eliminates the property’s economic value or “viability” to its nominal owner, *or* (b) the regulation is categorically not a taking.

*Id.* at 1622 (footnotes omitted).

4. *Nollan v. California Coastal Comm’n*, 107 S. Ct. 3141 (1987); *First English Evangelical Lutheran Church v. County of Los Angeles*, 107 S. Ct. 2378 (1987); *Hodel v. Irving*, 107 S. Ct. 2076 (1987); *Keystone Bituminous Coal Ass’n v. DeBenedictis*, 107 S. Ct. 1232 (1987).

won in three of the four cases, and in the fourth, *Keystone Bituminous Coal Association v. DeBenedictis*,<sup>5</sup> the decision was five to four. Furthermore, *Keystone* involved a statute very similar to the one invalidated in *Pennsylvania Coal Co. v. Mahon*,<sup>6</sup> the one early case in which a regulatory taking was found. The four cases produced multiple opinions, and all but *Hodel v. Irving*<sup>7</sup> produced sharp dissents. Only Justice White was with the majority in all four cases although in *Hodel* he joined another Justice's concurrence. In short, the Court hardly seems to have united behind a single view of the takings clause.

This conclusion is confirmed by examining the one regulatory takings case decided in the 1988 term, *Pennell v. City of San Jose*.<sup>8</sup> The Court achieved a seven-Justice majority by refusing to rule on whether a taking had occurred in the absence of a concrete example of harm.<sup>9</sup> The two Justices writing in partial dissent would have reached the merits and found a taking.<sup>10</sup>

Michelman is able to discern a simple pattern emerging from recent takings cases because he is at pains to give a narrow interpretation to the two decisions that have the most potential for a broadened view of the takings clause. Thus, he argues that *Nollan v. California Coastal Commission*<sup>11</sup> should be understood "as a further manifestation, albeit in somewhat surprising form, of the talismanic force of 'permanent physical occupation' in takings adjudication."<sup>12</sup> Similarly, his reading of *First English Evangelical Lutheran Church v. County of Los Angeles*<sup>13</sup> is designed to give that opinion limited scope. Under his analysis, "all [that the Court] there decided, was that . . . the state must compensate the landowner in money for [the] interim of compelled compliance with [an] unconstitutional regulation."<sup>14</sup> For Michelman, the key to the finding of a time-limited taking in *First English* is "that the enactors of the offending regulation enacted it not as temporary but as indefinite."<sup>15</sup> Michelman may be correct in the sense that his reading of these cases was required to produce majority support for the finding of a taking in each case. That inference, however, is a far cry from Michelman's stronger claim that these decisions signal a reformalization of takings law. An alternative explanation, supported by the shifting makeup of the majorities in the recent cases, is that the future direction of takings law is very much in doubt. The Court has left itself free to move in any

5. 107 S. Ct. 1232.

6. 260 U.S. 393 (1922).

7. 107 S. Ct. 2076.

8. 108 S. Ct. 849 (1988).

9. *Id.* at 856-57.

10. *Id.* at 859 (Scalia, J., concurring in part and dissenting in part).

11. 107 S. Ct. 3141 (1987).

12. Michelman, *supra* note 1, at 1608.

13. 107 S. Ct. 2378 (1987).

14. Michelman, *supra* note 1, at 1617.

15. *Id.* at 1619.

number of directions in the future without having explicitly to overrule any of these cases.

As a general matter, Michelman argues that, after *Pennsylvania Coal*<sup>16</sup> was decided in 1922, the Court moved "toward a highly nonformal, open-ended, multi-factor balancing method."<sup>17</sup> He claims that in recent years the Court has felt "unease about the lack of definition and rigor of its regulatory-takings doctrine."<sup>18</sup> While Michelman's view of the trend appears to be correct, I think he is wrong about the unease. Instead, the Court seems to be inordinately proud of the ad hoc nature of its takings opinions and has reiterated its support of case-by-case balancing in the current crop of opinions. Thus, Justice Stevens in *Keystone* cited with approval the statement in *Kaiser Aetna v. United States* that:

this court has generally "been unable to develop any 'set formula' for determining when 'justice and fairness' require that economic injuries caused by public action be compensated by the government, rather than remain disproportionately concentrated on a few persons." Rather, it has examined the "taking" question by engaging in essentially ad hoc, factual inquiries that have identified several factors—such as the economic impact of the regulation, its interference with reasonable investment backed expectations, and the character of the government action—that have particular significance.<sup>19</sup>

Chief Justice Rehnquist, dissenting in *Keystone*, found nothing to disagree with here: "Admittedly, questions arising under the Just Compensation Clause rest on ad hoc factual inquiries, and must be decided on the facts and circumstances in each case."<sup>20</sup> The only exception occurred in the partial dissent in *Pennell* written by Justice Scalia and joined by Justice O'Connor.<sup>21</sup>

In short, my view of the recent cases is the reverse of Professor

16. 260 U.S. 393 (1922).

17. Michelman, *supra* note 1, at 1621 (citation omitted).

18. *Id.* at 1622 (citation omitted).

19. *Kaiser Aetna v. United States*, 444 U.S. 164, 175 (1979), quoted in *Keystone Bituminous Coal Ass'n v. DeBenedictis*, 107 S. Ct. 1232, 1247 (1987) (citations omitted). Actually, Stevens is quoting from *Hodel v. Virginia Surface Mining and Reclamation Ass'n*, 452 U.S. 264, 295 (1981), which quoted *Kaiser Aetna*. The internal quotation in *Kaiser Aetna* is from *Penn Cent. Transp. Co. v. New York City*, 438 U.S. 104, 124 (1978). The Court repeated the "essentially ad hoc factual inquir[y]" language in *Pennell v. City of San Jose*, 108 S. Ct. 849, 856 (1988).

20. 107 S. Ct. at 1254. Similar language is found in Justice Brennan's majority opinion in *Andrus v. Allard*, 444 U.S. 51 (1979). "There is no abstract or fixed point at which judicial intervention under the Takings Clause becomes appropriate. Formulas and factors have been developed in a variety of settings. Resolution of each case, however, ultimately calls as much for the exercise of judgment as for the application of logic." *Id.* at 65 (citation omitted).

21. *Pennell*, 108 S. Ct. at 860–61 (Scalia, J., concurring in part and dissenting in part) (ad hoc factual inquiry inappropriate when challenge is to a law in all its applications).

Michelman's. The recent cases represent a continuation of the trend toward ad hoc balancing, but what takings law needs is a good dose of formalization.

## II. THE PERILS OF CASE-BY-CASE ANALYSIS

The Court's (and Michelman's) glorification of ad hoc balancing is impossible to reconcile with a belief in the importance of preserving "investment-backed expectation[s]." <sup>22</sup> Takings law should be predictable, on this view, so that private individuals confidently can commit resources to capital projects. <sup>23</sup> Nevertheless, as many economically oriented writers have argued, no taking can legitimately be claimed if the property owner correctly anticipated that an uncompensated state action was possible and if this belief affected the price paid for the asset. <sup>24</sup> If takings jurisprudence is both ad hoc and ex post, however, investors may have a very difficult time knowing whether a particular predictable state action will or will not be judged to be a taking. Therefore, even if the menu of possible state actions is known and probabilities can be assigned to each policy, investors will not be able to make informed choices because the Court has not provided clear standards to determine when compensation will be paid. <sup>25</sup> The shifting doctrines of takings law introduce an element of uncertainty into investors' choices that has nothing to do with the underlying economics of the situation. This uncertainty creates two problems. First, investors do not know whether or not damages will be paid. Second, in the event damages are not paid, investors will be left bearing the costs of an uninsurable risk. Thus, the Justices need to recognize that the investment-backed expectations they discuss are themselves affected by the nature of takings law. To the extent that investors are risk averse, the very incoherence of the doctrine produces inefficient choices. When legal rules affect behavior, clarity is a value in itself, independent of the actual content of the rule.

The problem of judicially created uncertainty is exacerbated by the ex post nature of court decisions. Judges are reluctant to decide cases until someone has "actually" been harmed. Not only are they reluctant to articulate general principles of takings law, but judges are also unwilling to make general rulings on the status of state actions under individual statutes. Thus, in *Keystone*, Justice Stevens, in discussing

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22. This phrase comes from Michelman. See Michelman, *Property, Utility, and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law*, 80 *Harv. L. Rev.* 1165, 1233 (1967).

23. *Id.* at 1216-17.

24. See, e.g., Blume & Rubinfeld, *Compensation for Takings: An Economic Analysis*, 72 *Calif. L. Rev.* 569, 584-87 (1984). Michelman also recognizes this point. Michelman, *supra* note 22, at 1238.

25. See Epstein, *Takings: Descent and Resurrection*, 1987 *Sup. Ct. Rev.* 1, \*30 n.81. Epstein's own proposed reformulation of takings doctrine is, I believe, unsatisfactory. See *infra* note 66.

*Pennsylvania Coal Co. v. Mahon*, dismissed Justice Holmes's analysis of the general validity of the act as an uncharacteristic "advisory opinion."<sup>26</sup> Stevens then went on to argue that no taking had occurred under the similar Pennsylvania law at issue in *Keystone* because at the time of the lawsuit no company could demonstrate that it actually had been harmed. The companies were asking the Court to pass on the general legitimacy of the statute, and this the majority declined to do.<sup>27</sup> Similarly, in *Pennell* an association of landlords was given standing to challenge a portion of San Jose's rent control ordinance, but their claim that a taking had occurred was dismissed as "premature" because no landlord had actually suffered harm from the disputed provision.<sup>28</sup> Thus, in the field of regulatory takings, where the future direction of the law is unclear, economic actors cannot obtain a prospective ruling from a court on whether a particular law will effect a taking. They must wait until a concrete harm has occurred before the statute can be tested. In the face of this uncertainty, investors may forgo otherwise profitable activities, and thus, the current state of the law may produce an inefficiently low level of investment.

Investors are not the only ones adversely affected by the incoherence and unpredictability of takings law. Government officials may be affected as well since the vagueness of the doctrine may act as a force for conservatism among public officials. Risk averse officials facing the possibility of damage suits against their jurisdictions may restrict their activities simply because they dislike uncertainty.<sup>29</sup> As Justice Stevens noted in his dissent in *First English*:

It is no answer to say that "[a]fter all, if a policeman must know the Constitution, then why not a planner?" To begin with, the Court has repeatedly recognized that it itself cannot establish any objective rules to assess when a regulation becomes a taking. How then can it demand that land planners do any better?<sup>30</sup>

As the Court moves to reconsider the regulatory takings area, it appears to be developing a jurisprudence that is working against, what is to me, the fundamental goal of the takings clause. The clause is an

26. *Keystone Bituminous Coal Ass'n v. DeBenedictis*, 107 S. Ct. 1232, 1241 (1987) (citing *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 413-14 (1922)).

27. Rehnquist, in dissent, would have been willing to do this. He argued that in *Pennsylvania Coal* the general validity of the act "was properly drawn into question." 107 S. Ct. at 1254 (Rehnquist, C. J., dissenting).

28. *Pennell v. City of San Jose*, 108 S. Ct. 849, 854-56 (1988). The partial dissent, in contrast, would have reached the merits of the takings claim. *Id.* at 860-61 (Scalia, J., concurring in part and dissenting in part).

29. An expansive regulatory takings doctrine may also discourage government regulation. That result may or may not be desirable depending upon one's view of the costs imposed on property owners by regulations.

30. 107 S. Ct. at 2399 n.17 (Stevens, J., dissenting) (quoting *San Diego Gas & Elec. Co. v. City of San Diego*, 450 U.S. 621, 661 (1981) (Brennan, J., dissenting)) (citations omitted).

attempt to reconcile an unpredictable, democratically responsible polity with the existence of a capitalist economy based on private property and individual initiative.<sup>31</sup> The ad hoc nature of the law introduces an element of uncertainty into private investment decisions that could make the coexistence of democracy and private property more, rather than less, difficult.

### III. TOWARD A TAKINGS JURISPRUDENCE

Let us move now from criticism to prescription. If the courts did try to make sense of the takings issue as a general matter, what should they say? The answer has both an efficiency and an equity component. The efficiency analysis of the takings issue stresses its impact on both private and public investment and on the distribution of risk in society. Takings law also plays a role in enhancing political legitimacy and contributing to the fairness of the distribution of wealth.

The distinction between physical and regulatory takings is not meaningful in efficiency terms, and it also has little to recommend it under most ethical theories. Although this distinction retains a hold on the legal mind,<sup>32</sup> the takings jurisprudence outlined below does not begin with this dichotomy as a first principle. The analysis instead provides a general overview of the takings issue.

#### A. *Efficiency*

To begin, one must distinguish between efficient and inefficient compensated takings. The efficiency question has three prongs: (1) the possibility of over- or underinvestment by private individuals (the "private-investment" issue); (2) the problem of government-created uncertainty (the "insurance" issue); and (3) the impact of takings doctrine on the decisions of public officials (the "public-investment" issue).

The private-investment issue concentrates upon the use the government intends to make of the property. It distinguishes between improvements to property that the government will use and improvements that it will destroy. On this first efficiency ground, only the former should be completely compensated. Thus, a homeowner should be compensated both when the state takes his home to turn it into a tourist attraction and when the state passes a regulation requiring the homeowner to permit public access to her garden one month a year. Full compensation in other cases generally will be inefficient because it will produce overinvestment. If people expect to be fully compensated for a public policy that destroys their property, they will invest

31. Compare the similar position of the writers cited *infra* note 46.

32. See, e.g., *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 426 (1982). For a discussion of why this might be the case, see B. Ackerman, *Private Property and the Constitution* 112-67 (1974). Colum. L. Rev. 1702 1988

too much in the property.<sup>33</sup> Thus, a homeowner should not be fully compensated for the value of a house that is destroyed to make way for a highway.

Under such a compensation system, when the state destroys existing investments, homeowners will behave efficiently when compensation is set between zero and the level of investment that would be efficient in the absence of any compensation for the taking. Leaving aside the insurance issue, a level of compensation above zero would be required on efficiency grounds only if courts wished to force governments to take into account the opportunity costs of their actions.<sup>34</sup> In such cases, courts would need to judge the efficient level of homeowner investment *ex ante* given the possibility of future governmental use.

Notice that under this first theory, the compensation decision would depend only on the government's use of the property. This compensation policy is designed solely to produce optimal investment decisions by private owners. Both the economic status of the owner and the magnitude of the loss would be irrelevant. Therefore, owners should be compensated for any land-use regulation, such as an historical-preservation ordinance, when public benefits flow from past investment spending by individuals. Unfortunately, in practice, the probability of compensation is highest in just those areas in which overreliance is most likely. If the state destroys a "thing," it usually will be required to pay for it.<sup>35</sup> In contrast, if it merely uses assets without taking title to them, by, for example, requiring the owner to comply with historical-preservation standards, the state generally will not be required to compensate her.<sup>36</sup> This gives owners of buildings that might in the future be declared landmarks an incentive to tear them down quickly so that the issue will not arise.<sup>37</sup> Thus, legal doctrine in this area illustrates clearly the conflict between "scientific policymaking" and "ordinary observing" isolated in Bruce Ackerman's study of takings doctrine.<sup>38</sup> Economic analysis suggests a rule that is directly

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33. For fuller discussions of the issue of overinvestment, see Blume & Rubinfeld, *supra* note 24, at 618-20; Blume, Rubinfeld & Shapiro, *The Taking of Land: When Should Compensation Be Paid?*, 99 *Q.J. Econ.* 71 (1984). As Blume and Rubinfeld argue: "Whatever the exact determination of compensation, it is important that the measure be one that cannot be directly affected by the behavior of the individual investors, since any compensation measure which can be affected by private behavior will create the possibility of inefficiency due to moral hazard." Blume & Rubinfeld, *supra* note 24, at 618 n.144.

34. Cf. Fischel & Shapiro, *Takings, Insurance, and Michelman: Comments on Economic Interpretations of "Just Compensation" Law*, 17 *J. Legal Stud.* 269 (1988) (analyzing situations in which government actions produce demoralization costs).

35. See the critical analysis of this doctrine in B. Ackerman, *supra* note 32, at 130-36.

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

37. Cf. W. Fischel, *The Economics of Zoning Laws* 174 (1985) (giving an example).

38. B. Ackerman, *supra* note 32, at 108-16. *Colum. L. Rev.* 1703 1988

opposed to the idea that government should only pay for things that it physically appropriates.

A compensation rule designed to limit overreliance would have the hypothesized behavioral consequences, however, only if government actions are reasonably predictable so that investors can base their decisions on informed predictions about what the government will do in the future. Thus, the compensation rule proposed above should, in principle, be supplemented with a public policy of announcing public actions in advance and by stating at the same time that compensation will be paid only to those in possession of the property at the time of the announcement. Subsequent sales contracts would be required to include clauses explaining the future government action.

A requirement that governments announce their actions in advance, however, while fine in principle, misconceives the nature of most political processes. At any point in time a wide range of public policies is possible. Some may be enacted this year, some next year and others never. Thus, few policies will be wholly unexpected, and none will be completely certain. Nevertheless, takings law should require property owners to make informed guesses<sup>39</sup> and should encourage governments to be as specific as possible about their plans. A rule tying compensation to the date a project is announced would further this goal.

Given the uncertainty that is, I believe, an inherent feature of representative democratic government, the insurance branch of the efficiency analysis becomes of critical importance. The problem of risk spreading, unlike the issue of overinvestment, is tied to the situation of the private owner, independent of the government's use of the property. Because of its contrasting focus, this second efficiency concern produces results that will sometimes conflict with the first. Conflicts can be resolved by deciding whether government is best viewed as a well-organized process with known probabilities attached to possible future actions or as an essentially random and unpredictable enterprise, at least in its impact on particular persons. When the latter view is closest to being correct, compensation may be justified because it acts as a form of insurance. Even if the state is certain to carry out a particular policy, such as building a highway, no one may be able to predict who will be affected adversely, that is, which route will be chosen. If the *ex ante* probability of being harmed is distributed broadly across the population and if *no* compensation is paid, two different re-

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39. For example, in *Chang v. United States*, 13 Cl. Ct. 555 (1987), the Claims Court denied compensation to engineers whose employment contracts in Libya had been voided by an Executive Order issued by President Reagan. The court argued that "the risk that employment in Libya might be interrupted by tension in the relations between that government and the United States can hardly be said to have been outside the reasonable contemplation of plaintiffs at the time they entered into their employment contracts." *Id.* at 560. Furthermore, the engineers should have reasonably supposed that economic sanctions against Libya were possible.



sults are possible. On the one hand, if people are risk neutral, they will rationally cut back their investment just enough to compensate for the risk of expropriation. On the other hand, if people are risk averse, the uncertainty created by the threat of harm may lead them to underinvest and to hold their assets in a form that is unlikely to be affected by the public program.

Underinvestment would not occur if insurance were available, but the risks discussed here are generally uninsurable in the private market because of both the arbitrary incidence of harm and the problems of moral hazard and adverse selection. Moral hazard occurs when the existence of insurance leads the insured person to take actions that increase the probability or the magnitude of the loss. In this context, it occurs if property owners secretly lobby to have their property taken or at least do not actively oppose a policy that will produce that result. Although such lobbying is possible when the government pays compensation itself, the obvious budgetary consequences of such behavior will help to check abuses. Adverse selection occurs if insurance companies cannot adequately sort property owners into risk classes. In such a case high-risk and low-risk owners are charged the same rate so that very low-risk owners may decide to self-insure. The remaining pool of insured owners is thus riskier and premiums must rise. Now the remaining low-risk owners may opt out of the pool. If the insurance companies have less information about risks than property owners, profitable insurance contracts may be impossible to write.<sup>40</sup>

Therefore, when government creates risks for which private insurance is unavailable, efficient risk distribution provides an economically oriented reason for basing the compensation decision on the magnitude of the harm suffered. In considering the degree of harm, courts must decide which standard of comparison to use. For example, should they define the plaintiff's property as the coal that cannot be mined because of the regulatory statute, so that 100 percent of it has been taken, or as the firm's entire mining operation, so that only a small share has been lost?<sup>41</sup> A generally accepted rule of thumb is that individuals behave in a risk averse way when a major portion of their total wealth is threatened. Since owner-occupied housing represents a large proportion of most owners' personal wealth, government should compensate homeowners when it takes their houses either through physical confiscation or through a regulation that makes them uninhabitable.<sup>42</sup> Conversely, if it confiscates their toasters or passes an ordinance making them unusable, no compensation would need to be paid on risk-spreading grounds. In short, the standard of comparison should be the individual's total wealth, not just the property "affected" by the taking. In contrast, broadly held corporations should be viewed as risk neutral,

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40. Blume & Rubinfeld, *supra* note 24, at 584-99.

41. See *Keystone Bituminous Coal Ass'n v. DeBenedictis*, 107 S. Ct. 1232 (1987).

42. Blume & Rubinfeld, *supra* note 24, at 606-10. HeinOnline 28 Cal. Rev. 1705 1988

even toward large losses, because shareholders and other investors can insure by holding a diversified portfolio of investments. Compensation might, however, be provided to employees and owners of specialized assets if either group will suffer large declines in permanent income or wealth relative to their expectations in the absence of the public program. The courts should develop some simple rules of thumb that, although not perfectly adapted to all the individual situations that arise, will nevertheless provide insurance protection to most of those who would demand it.

The final element in an efficiency analysis concerns the impact of takings law on the calculations of public officials. The compensation requirement can be understood as a way to force public policymakers to consider the opportunity costs of their proposed actions. Policies that "take" private property would then have concrete budgetary impacts that would be immediately reflected in tax bills or borrowing capacity. The efficiency consequences of a comprehensive compensation requirement depend upon one's view of the way government policy is made. If cost-benefit tests are used, actual compensation is not required since the analyst can be expected to take into account all costs and benefits, not just those that show up in the budget. Efficient takings rules can depend entirely upon the impact of compensation on the behavior of private individuals. Conversely, if decision makers are imperfect agents of the public, compensation requirements may have little impact on their choices because the required payments come from taxpayers, not from the decision makers' own pockets. Once again, but for very different reasons, takings rules can depend upon their impact on private individuals. Finally, if public choices are the result of the competition of various groups for political benefits, powerful groups will not need a constitutionally mandated takings doctrine in order to preserve their interests. They will be able to insist that the overall legislative package be beneficial to them. Left out of this account, however, are politically ineffective individuals severely harmed by some public policy. Efficiency requires that their costs be taken into account; yet the operation of the political process may not incorporate these costs. Under this view of the political system, compensation should be paid for these losses to force politicians to recognize their existence.

Since government policymaking can at least sometimes be characterized as a struggle between organized groups,<sup>43</sup> takings law should consider whether the affected individuals suffer special difficulties in having their interests taken seriously by the political process. The takings clause, however, is unlikely to be an effective means of equalizing the power of various population groups. It can be most effective as a

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43. See, e.g., K. Schlozman & J. Tierney, *Organized Interests and American Democracy* (1986); Peltzman, *Toward a More General Theory of Regulation*, 19 *J.L. & Econ.* 211 (1976); Stigler, *The Theory of Economic Regulation*, 2 *Bell J. Econ. & Mgmt. Sci.* 3 (1971).

way to protect the property interests of unorganized individuals with nothing in common except that they would otherwise bear the costs of some public policy.<sup>44</sup>

Thus, an efficient takings doctrine should not be concerned primarily with the impact of the doctrine on the calculations of public officials. Instead, except for special claims advanced by the politically weak, the emphasis should be on encouraging efficient actions by private property owners. This perspective produces the following rough guide to deciding cases. Always compensate for property that the government will use in the form in which it is provided by the owner. In other cases, compensate when the asset represents a major proportion of the owner's wealth so that a hypothesis of risk aversion is plausible. Employ a presumption in favor of risk aversion for individuals and risk neutrality for publicly held corporations. In addition, compensate even risk-neutral individuals whose loss represents a large proportion of their wealth if these individuals are politically ineffective.

To counteract the moral hazard created by compensation, courts should develop a notion close to mitigation of damages in contract law.<sup>45</sup> When government appropriation becomes likely, owners should be reimbursed only for new investments that either can be used by the government or would be rational if no compensation were to be paid. To minimize the private burden of this last provision, courts should employ a presumption in favor of the private property owner with the burden of proof on the government to show both that it has given notice and that the investment was excessive.

### B. *Political Legitimacy and Fairness*

Efficiency is not the whole story in analyzing takings doctrine. When public policies are uncertain and have unpredictable impacts on small groups in the population, the legitimacy of the state may depend upon the payment of compensation to mitigate the arbitrary distributive consequences of many public policies.<sup>46</sup> Citizens whose assets have been taken are unlikely to be satisfied with the argument that the system is fair *ex ante*. Compensation is then a substitute for imposing severe restrictions on the substance of public policies or the degree of consent required. Thus, the Court has interpreted the fifth amendment as designed to prevent

the public from loading upon one individual more than his just share of the burdens of government, and [it] says that

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44. See *infra* Section IIIB.

45. See *Merced Irrigation Dist. v. Woolstenhulme*, 4 Cal. 3d 478, 496, 483 P. 2d 1, 12, 93 Cal. Rptr. 833, 844 (1971) (landowner not entitled to compensation for "project enhancement" accruing after it was probable land would be taken).

46. B. Ackerman, *supra* note 32, 52-53, 68, 79-80; J. Ely, *Democracy and Distrust* 97-98 (1980); L. Tribe, *American Constitutional Law* 605-07 (2d ed. 1988); Michelman, *supra* note 22; Sax, *Takings and the Police Power*, 74 *Yale L.J.* 308, 364-65, 75-76 (1964).

when he surrenders to the public something more and different from that which is exacted from other members of the public, a full and just equivalent shall be returned to him.<sup>47</sup>

Similarly, Justice Scalia, in finding that a taking had occurred in *Nollan*, argued that even if the California Coastal Commission's policy is sound, it does not follow that coastal residents "can be compelled to contribute to its realization. . . . [I]f [the Commission] wants an easement across [their] property, it must pay for it."<sup>48</sup>

However, the United States Constitution, in permitting policies to be adopted by majority votes in representative assemblies and approved by the President, did not contemplate that all statutes would meet with unanimous approval. Some people would suffer losses while others benefited. The status quo is not given the deeply privileged position that it would have under an unanimity rule. Therefore, since some losses can be imposed constitutionally, the problem for takings jurisprudence is to decide when an individual has borne more than his or her "just share of the burdens of government."<sup>49</sup> This is not a question that can be answered in this short Article, but it is one that should be taken up in a self-conscious way by the Court.<sup>50</sup> While a full-fledged theory of the takings clause cannot be developed here, I can, nevertheless, isolate three situations in which compensation should *not* be paid.

The first situation involves the specification of the property entitlement itself. Compensation should not be paid when the complainant cannot legitimately claim to be entitled to the benefits that are lost when the government acts. For example, courts have found that individuals do not have the right to create a nuisance. Thus, if the state imposes regulations or confiscates a nuisance, the owner has no right to claim compensation. Nothing has been taken that the individual had a right to claim as his own. The classic statement is in *Mugler v. Kansas*:<sup>51</sup> "[A]ll property in this country is held under the implied obligation that the owner's use of it shall not be injurious to the community."<sup>52</sup> Citing *Mugler* with approval, Justice Stevens in *Keystone* stated that the Court hesitates "to find a taking when the state merely restrains uses of property that are tantamount to public nuisances."<sup>53</sup>

47. *Monongahela Navigation Co. v. United States*, 148 U.S. 312, 325 (1893), quoted in *Keystone Bituminous Coal Ass'n v. DeBenedictis*, 107 S. Ct. 1232, 1256 (1987) (Rehnquist, C.J., dissenting).

48. *Nollan v. California Coastal Comm'n*, 107 S. Ct. 3141, 3150 (1987).

49. Richard Epstein takes a contrary position, reading the takings clause as imposing severe restrictions on the ability of the government to redistribute wealth. See R. Epstein, *Takings: Private Property and the Power of Eminent Domain* (1985). But see Grey, *The Malthusian Constitution*, 41 U. Miami L. Rev. 21 (1986) (criticizing Epstein's position).

50. Cf. L. Tribe, *supra* note 46, at 607-13 (discussing the problematic nature of property in Supreme Court jurisprudence).

51. 123 U.S. 623 (1887).

52. *Id.* at 665.

53. *Keystone Bituminous Coal Ass'n v. DeBenedictis*, 107 S. Ct. 1232, 1245 (1987);

The difficulty with this doctrine is twofold. First, Ronald Coase has shown that in a two-sided controversy it is not straightforward to decide who "caused" the harm.<sup>54</sup> Second, this doctrine may tie the regulatory state too closely to doctrines of the common law that may be obsolete in particular regulatory situations. This compensation rule makes some types of regulatory programs much more expensive than others. In practice, however, courts do not seem to have limited themselves to common-law nuisances. The *Mugler* case itself dealt with brewery property made valueless by a Kansas constitutional amendment prohibiting the manufacture and sale of intoxicating liquors, and the opinion's language is quite broad:

The power which the States have of prohibiting such use by individuals of their property as will be prejudicial to the health, the morals, or the safety of the public is not—and, consistently with the existence and safety of organized society cannot be—burdened with the condition that the State must compensate such individual owners for pecuniary losses they may sustain, by reason of their not being permitted, by a noxious use of their property, to inflict injury upon the community.<sup>55</sup>

Justice Stevens quoted this statement both in his opinion in *Keystone*<sup>56</sup> and in his dissent in *First English*.<sup>57</sup> Chief Justice Rehnquist, however, would read the nuisance exception quite narrowly to accord more closely with common-law doctrine. He has argued that the "nuisance exception to the taking guarantee is not coterminous with the police power itself."<sup>58</sup> It is instead a "narrow exception allowing the government to prevent 'a misuse or illegal use.'"<sup>59</sup> A similar contrast in views is evident in *Nollan*. Justice Scalia argued that the state has taken an "essential stick in the bundle of rights"<sup>60</sup> while Justice Brennan found that the owners had no legitimate entitlement for the state to take.<sup>61</sup> These different views of the content of legitimate property entitlements imply that prior to any resolution of the takings issue the Court must

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see also *id.* at 1246 n.22 (citing cases holding that compensation is not required when the public action abates a public nuisance or stops illegal activity).

54. Coase, *The Problem of Social Cost*, 3 *J.L. & Econ.* 1 (1960); see also L. Tribe, *supra* note 46, at 594 ("Increasingly, deciding who had harmed whom seemed to open a choice to provide any determinate solution to the question of compensation.") (citation omitted).

55. *Mugler*, 123 U.S. at 669.

56. *Keystone*, 107 S. Ct. at 1244.

57. *First English Evangelical Lutheran Church v. County of Los Angeles*, 107 S. Ct. 2378, 2392 (1987) (Stevens, J., dissenting).

58. *Penn Cent. Transp. Co. v. New York City*, 438 U.S. 104, 145 (1978) (Rehnquist, J., dissenting).

59. *Keystone*, 107 S. Ct. at 1256 (Rehnquist, C.J., dissenting) (quoting *Curtin v. Benson*, 222 U.S. 78, 86 (1911)).

60. *Nollan v. California Coastal Comm'n*, 107 S. Ct. 3141, 3145 (1987).

61. *Id.* at 3158-59 (Brennan, J., dissenting).

resolve fundamental questions concerning the nature of property. These questions should be resolved without giving a canonical status to common-law jurisprudence.

The second situation involves the state's authority to appropriate excess profits or economic rents. This principle, implicit in antitrust law,<sup>62</sup> provides a justification for the Supreme Court's refusal to find a taking in *Keystone*. The Court found that all mines would continue to operate and that the losses would not be severe.<sup>63</sup> This finding, if correct, implies that the companies were earning excess profits that could be used to pay for the regulation without causing anyone to go out of business. This standard also supports Brennan's dissent in *Nollan*. He argued that the Nollans "can make no tenable claim that either their enjoyment of their property or its value is diminished by the public's ability merely to pass and re-pass a few feet closer to the seawall beyond which appellants' house is located."<sup>64</sup> Thus, the appellants' claim could be viewed as an attempt to extract rents from their exclusive control of a piece of beach needed for convenient access between two public beaches. Under this view, they do not deserve compensation because they have no right to these economic rents. Finally, in *Pennell*, the Court reiterated previous decisions finding that the monopoly power of private business provides a justification for public action that lowers excess returns.<sup>65</sup>

In the third situation, compensation should not be paid if the government action is analogous to a private action that is seen as one of the risks of economic life. For example, if the government competes with a private business, this should not produce a takings claim because competitive losses do not give rise to damage claims in the private sector. These losses, labeled pecuniary externalities by economists, do not

62. The Sherman Act and the Clayton Act both seek to penalize firms that monopolize industries. Instead of compensation, violators may be subject to fines and triple damages. See F.M. Scherer, *Industrial Market Structure and Economic Performance* 494-95 (2d ed. 1980). For another application of this principle, see Rose-Ackerman, *Unfair Competition and Corporate Income Taxation*, 34 *Stan. L. Rev.* 1017, 1036 (1982).

63. "We do know, however, that petitioners have never claimed that their mining operations, or even any specific mines, have been unprofitable since the Subsidence Act was passed. Nor is there evidence that mining in any specific location . . . has been unprofitable." *Keystone*, 107 S. Ct. at 1248.

64. *Nollan v. California Coastal Comm'n*, 107 S. Ct. 3141, 3157 (1987) (Brennan, J., dissenting).

65. *Pennell v. City of San Jose*, 108 S. Ct. 849, 857-58 (1988). The partial dissent is even clearer on this point:

When excessive rents are forbidden . . . landlords as a class become poorer and tenants as a class (or at least incumbent tenants as a class) become richer. Singling out landlords to be the transferors may be within our traditional constitutional notions of fairness, because they can plausibly be regarded as the source or the beneficiary of the high-rent problem.

Id. at 863 (Scalia, J., concurring in part and dissenting in part)

have the adverse efficiency consequences of externalities that arise when individuals use scarce resources for which they do not pay. The distributive consequences produced by market pressures are a cost of maintaining the incentives needed to make markets work efficiently. Thus, if the government sells surplus military supplies, it should not compensate private firms selling competing products. Similarly, the Tennessee Valley Authority should not have to compensate competing power companies for lost business. Finally, a regulation that is cheaper for one firm to comply with than another should not give rise to a compensation claim from the disadvantaged firm.

#### CONCLUSION

In this brief Article, I have not tried to develop a comprehensive answer to the takings question. My main message, however, is that such an effort is sorely needed. While the Court should try for a principled resolution, this is one legal area in which almost any consistent, publicly articulated approach is better than none. Clear statement, even if not backed by clear thinking, will do much to preserve the investment-backed expectations the Court talks so much about. Clear thinking would be even better, and here I have provided only a rough guide. The suggestions based on efficiency, equity and political legitimacy outlined above must be supplemented with an understanding of just what it is that people can be said to own.<sup>66</sup> In attempting to answer that question, historically generated expectations may need to be preserved for the sake of fairness, but they should not straitjacket our thinking about the future.

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66. Epstein claims to present just this kind of clear rule, but he has begged many of the most important questions. He does this by taking as relatively unproblematic the issue of how private property should be defined and using a definition that does not permit concerns with distributive justice to help determine the outlines of property claims. See R. Epstein, *supra* note 49, especially ch. 19 at 306-29 and the conclusion at 331-50; Epstein, *supra* note 25, at 40-41, 44-45.