Palazzolo v. Rhode Island: Recent Developments in Eminent Domain

by Lara Womack

INTRODUCTION

The inherent right of the U.S. government to take private property is acknowledged in the Fifth Amendment to the U.S. Constitution, which states that "private property [shall not] be taken for public use without just compensation." This is known as the eminent domain clause.

There are several bases upon which a property owner might challenge the government's authority under the eminent domain clause. The most likely challenge is that the compensation offered by the government is inadequate; it is not just. Another possible challenge is that the government's reason for having taken the property does not qualify as a public use. This challenge is difficult to maintain, however, because the standard used to determine the requirement of public use generally favors the government. Both of these challenges assume that a taking has in fact occurred, an occurrence that is itself frequently the subject of litigation.

The clearest cases of takings involve some physical intrusion upon land by the government, but a physical intrusion is not always necessary. The U.S. Supreme Court established in *Pennsylvania Coal Co. v. Mahon*[1] that government action which does not actually encroach upon or result in the physical occupation of property may constitute a taking, and thus trigger the requirement of just compensation, if those actions substantially affect and limit the use of the property. When there is no encroachment or physical occupation, there are two ways in which a landowner

ABOUT THE AUTHOR

Lara Womack *is an associate professor of business law at Middle Tennessee State University. She received her law degree from the University of Tennessee. She is a member of both the Honors College faculty and the Graduate College faculty.* [redacted] [redacted] [redacted])

can establish a taking. One alternative is to prove that they have been denied all economically beneficial or productive use of the land. The second alternative involves the application of three factors. These are the regulation's economic affect on the owner, the extent to which the regulation interferes with the owner's reasonable investment-backed expectations and the character of the government action. Collectively, these are known as the *Penn Central*[2] factors, a reference to the case in which they were established. When landowners allege that regulations have denied them the use of their property, or have interfered with their investment-backed expectations, the actions are commonly referred to as inverse condemnation cases.

Palazzolo v. Rhode Island[3] is such a case. The petitioner, Anthony Palazzolo, owned a parcel of real estate in Rhode Island, which was subject to that state's wetland regulations.[4] It had been purchased by a corporation, Shore Gardens, Inc. (SGI), in 1959. That corporation was formed by Palazzolo and some associates. SGI made several attempts to develop the property. Because most of the property was salt marsh and subject to tidal flooding, any development would have required filling of the land to some extent. Three different applications were made to state agencies for approval to fill substantial portions of the parcel. All three were eventually denied. At some point, Palazzolo bought out his associates and became the sole shareholder in SGI.

In 1971, Rhode Island created the Rhode Island Coastal Resources Management Council. The council, charged with protecting coastal properties, designated salt marshes as protected property and limited development on such property. In 1978, SGI's charter was revoked and, because he was the sole shareholder, Palazzolo became the owner of the property by operation of law. During the 1980s, Palazzolo again made efforts to develop the property, but the council rejected his applications on two occasions. At this point he filed suit in Rhode Island state court, claiming that the council's regulations constituted a taking of his property, entitling him to just compensation.

The state trial court ruled against Palazzolo and the Rhode Island Supreme Court affirmed that decision.[5] Mr. Palazzolo then appealed to the U.S. Supreme Court. The case raised three interrelated issues. The first was whether the petitioner's claim was ripe for review. The second was whether a property owner should be barred from asserting a takings claim when the regulations in question were already in effect at the time the property was acquired. The third was whether the property owner in this case had been denied of all economically beneficial use. Of these three issues, the one that has the greatest potential to impact the progress of environmental regulations is the second. Prior to *Palazzolo,* many lower courts had ruled that pre-acquisition notice was a bar to inverse condemnation proceedings. This case holds to the contrary, and so allows regulations of any type to be challenged for longer periods of time.

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ISSUE ONE: RIPENESS

The first issue addressed by the Court was whether the petitioner's claim was ripe for review. The ripeness doctrine is an extension of the general policy that courts in the U.S. do not function in an advisory capacity. They will hear cases only when presented with a present case or controversy. If a case is brought too early, it is not yet ripe for adjudication.[6] The ripeness doctrine prevents courts from engaging in premature adjudication and, where the legitimacy of an administrative agency regulation is at issue, also protects the agency from judicial interference while its decisions are still being formulated.[7]

In *Palazzolo,* the ripeness issue turned upon whether the government agency charged with implementing the regulations had reached a final decision on the application of those regulations to this particular parcel of property. The Rhode Island Supreme Court had ruled against Palazzolo on this issue. It acknowledged that at least four different applications to fill the land had been filed, either by Palazzolo personally or by SGI, and that all had been denied, but noted that these involved filling all or substantially all of the wetlands portion (18 acres) of the property. Further, none of these applications mentioned the particular development that Palazzolo

referenced in his claim for compensation, a plan to develop a 74-lot subdivision. Because Palazzolo had not been denied an application for that particular development, and because he had not pursued development options that were "less ambitious" than those requiring fill of so much of the wetlands area, the state Supreme Court ruled that his claim was not ripe.[8]

The U.S. Supreme Court disagreed with the Rhode Island Supreme Court on this issue. As to the determination that the particular development upon which Palazzolo had based his claim was not reflected in the applications, the Court stated that, under these circumstances, it was not necessary for an application of that type to have been filed. Palazzolo had been denied an application to fill the property. Since filling would have been a prerequisite to the 74-lot development, it was clear that the development itself would also have been prohibited.[9]

The Supreme Court focused more extensively on the state court's holding that the claim was not ripe because Palazzolo had not filed applications to develop a smaller portion of his property. The property did not consist entirely of wetlands. There was also a portion of upland property, the development of which would not have been subject to the same degree of restriction as the wetlands portion. The Court first addressed the need for additional applications to develop the wetlands portion. While Palazzolo's applications had involved the development of all, or substantially all, of this portion, it was not the size of the area covered which provided the basis of the denial. The applications were denied because they did not propose an activity that the state agency considered a compelling public purpose. There was no indication that the applications would have been accepted if the development proposed had occupied a smaller area. The agency had clearly communicated that it would allow no filling, and therefore no development, of the wetlands for any purpose, no matter how small or large the portion of the wetlands to be affected. The Court ruled that it was not necessary for additional applications covering smaller portions of the wetlands be filed in order to establish the ripeness of the claim.[10]

As to the uplands portion of Palazzolo's property, the Court explained that some doubt must exist as to the value of this portion of the property in order for the state to succeed on its argument that the takings claim was not ripe. The record reflected that all of the parties had accepted and subsequently cited uncontested testimony that the estimated value of this portion of the property was $200,000. Having accepted this estimate, the state could not later claim that the value was unknown. The Supreme Court ruled that Palazzolo's claim was ripe for adjudication.[11]

ISSUE TWO: PRE-ACQUISITION NOTICE

The pre-acquisition notice of the regulations as a bar to inverse condemnation proceedings was the second issue addressed by the Court. Because Palazzolo had become the owner of the property after the regulations in question became effective, the state courts had rejected his claim that he had been deprived of all beneficial use of the property. Those courts reasoned that, since the regulations pre-dated Palazzolo's acquisition of the property, he had never had the right to fill the property, and so it could not have been taken from him. Further, according to the state courts, the existence of the regulations defeated Palazzolo's claim that he had reasonable investment-backed expectations in the property. Since he had notice of the regulations, he could not reasonably have expected to fill and develop the property.[12]

The U.S. Supreme Court approached the pre-acquisition notice issue differently from the state courts. Rather than intertwining it with the issues of deprivation of all beneficial use and interference with reasonable investment-backed expectations, the Court viewed the notice issue as a preliminary one, much like that of ripeness. It also reduced the state courts' treatment of notice to one single rule: A purchaser or a successive title holder like petitioner is deemed to have notice of an earlier-enacted restriction and is barred from claiming that it effects a taking.[13]

The Court found fault with such a broad rule. It explained that if this rule were applied, transfers of property after the enactment of land-use regulations would absolve the government of its obligations under the eminent domain clause, without inquiry into how extreme or unreasonable those regulations were. If regulations are unreasonable, and constitute a taking, they do not become reasonable with the passage of time or the passage of title to the property affected.[14]

In rejecting the state courts' pre-acquisition rule, the Court noted the effect that it would have had on those who acquire title to property by some means other than an arm's length sale. The holding, however, does not appear to be based upon the manner in which title is acquired. The Court cited the

example of the individual whose property becomes subject to regulations, but who dies before an inverse condemnation claim can become ripe. Under the Rhode Island rule, the heir to that property would lose the right to claim compensation even if the claim did progress to the point of ripeness after the original owner's death. This, the Court concluded, would result in a windfall for the government. But the Court also specifically mentioned the effect that the Rhode Island rule would have on those owners who need to sell contrasted with those with sufficient resources to hold on to property.[15] Its rejection of the rule was not limited to those situations in which title passes by inheritance, or by operation of law, as in *Palazzolo*.

While seeming to make no distinction based upon the manner in which title is passed, the Court did make clear that its holding in this regard was not broad enough to apply to those cases involving a physical invasion of property. In such cases, the right to compensation is not passed to a subsequent owner. The difference, the Court explained, is based upon the manner in which the claim becomes ripe. When there is a physical invasion of property, the fact and extent of the taking are known at that time. When the impact on the property is regulatory in nature, it may not be known until a future point that a taking has occurred.[16] Thus, it is the party who owns the property at the time the claim becomes ripe who may bring the action, not necessarily the party who owned the property at the time the takings process began.

Many consider this issue to be the one with the greatest implications for both landowners and those advocating land-use regulations. The holding that notice is not an absolute bar to an inverse condemnation case will be of assistance to those who purchase property already subject to extensive regulations. Although those purchasers still have to carry the burden of proving that the regulations constitute a taking, they now have greater opportunity to initiate lawsuits. Most lower courts had refused to consider the merits of such cases, holding instead that purchasers who took with notice of the regulations were barred from making the claims at all. Knowing that litigation is more likely, governmental agencies may now weaken their regulations and allow more development, an outcome of particular concern to those who support the use of regulations for environmental reasons.[17]

This part of the ruling has already begun to affect other litigation. In *McQueen v. South Carolina Dept. of Health and Environmental Control*, a landowner had purchased property that had been affected by developmental regulation for over a century. The state Supreme Court ruled that the pre-existing regulations defeated the landowner's investment-backed expectations, and thus defeated his claim that a taking had occurred.[18] The day following its opinion in *Palazzolo*, the Court remanded this case to the South Carolina Supreme Court.[19]

Palazzolo leaves unanswered, or at least unclear, more questions than it clarifies. The one clear holding in the majority opinion is that pre-acquisition notice of land-use regulations does not bar a purchaser's inverse condemnation lawsuit. However, several questions remain open.

ISSUE THREE: THE MERITS

Having determined that Palazzolo's claim was ripe, and that it was not barred by his pre-acquisition notice of the regulations, the Court then gave some attention to the merits of his claim that the regulations had resulted in a taking of his property.

As noted above, there are two ways in which a landowner can succeed in the claim that land-use regulations have resulted in a taking of their property. One is to establish that they have been deprived of all economically beneficially use of the property. The other is to establish that a taking has occurred by application of the *Penn Central* factors. In *Palazzolo*, the state Supreme Court found against the landowner on both claims, but intertwined these issues with that of pre-acquisition notice. The Supreme Court took a different approach. After ruling that the landowner could proceed to the merits of his claim, it ruled that there had been no deprivation of the economic benefit, but that the *Penn Central* claim had not been adequately examined by the Court below.

On the issue of whether he had been deprived of all economically beneficial use, the very fact that had worked in favor of Mr. Palazzolo during the Court's analysis of the ripeness issue, worked against him. The Court determined that he had not been deprived of all economically beneficial use because the uplands portion of the property had an established value of $200,000. This value, the Court concluded, was more than a token interest and did not leave the parcel economically idle. On this point, the U.S.

Supreme Court found itself in agreement with the state Supreme Court.[20]

The state Supreme Court, however, had not evaluated the merits of the landowner's claim under the *Penn Central* factors. Although the majority opinion gives no guidance in how those factors ought to be applied in this case, its ultimate conclusion was the case should be remanded for that purpose.[21]

UNANSWERED QUESTIONS

There are two important questions left unanswered by the majority opinion in *Palazzolo*. One is only identified in the opinion, and the other is explored in more than one of the separate opinions, both concurring and dissenting. In addition, the patchwork of separate opinions in the case suggests that the entire subject of regulatory takings is far from settled.

The first unanswered question is presented in the majority opinion. In arguing that he had been denied all economically beneficial use of his property, Palazzolo attempted to segregate the uplands portion of his property, which had an established value of $200,000, from the wetlands portion, which was much more heavily regulated. This would have allowed him to more effectively argue that the wetlands portion had been taken, even though the upland portion retained some value. The Court would not allow him to pursue this argument, however, because he had not pursued it in the state courts.[22]

Although it rejected his attempt to segregate the property, the Court recognized that this argument, when presented in the correct manner, might be meritorious. Some previous cases have indicated that the extent of deprivation caused by a regulation must be measured against the value of the whole property, but other cases have questioned the logic of that rule. Acknowledging all of this, the Court still refused to consider the argument, leaving the issue open for debate in subsequent cases.[23] This issue was not further discussed in any of the five other opinions that were written.

Another important issue is raised by the majority opinion, but then left to be resolved by the lower courts. That is the extent to which the property owner's pre-acquisition notice of the regulations affects their reasonable investment-backed expectations. The majority opinion clearly states that pre-acquisition notice is not a bar to an inverse condemnation case, but give no further guidance on the issue.

Three of the justices offered further comment on this matter. In her concurring opinion, Justice O'Connor stated that the timing of the regulations to the acquisition of the property should not be considered immaterial; it should help to shape the reasonableness of the property owner's expectations. Justice Breyer, writing separately, agreed. Scalia also discussed this issue in his concurring opinion, but reached a different conclusion from O'Connor's. Scalia stated that restrictions in existence at the time title was acquired should have no bearing on the determination of whether a taking has occurred.

There were a total of six opinions written in *Palazzolo*. These reflect an array of views on the two primary issues involved in the case—ripeness and pre-acquisition notice as a bar. A bare majority of five justices agreed that the case was ripe and that notice was not a bar to an inverse condemnation action. Those five were Kennedy, Rehnquist, O'Connor, Scalia, and Thomas. Another justice, Stevens, joined with that group on the ripeness issue, but wrote a separate opinion in which he dissented on the notice issue. O'Connor and Scalia both wrote separate opinions to expand upon the impact that notice might have on a property owner's reasonable investment-backed expectations. Ginsberg wrote a dissenting opinion, in which she was joined by Souter and Breyer. They concluded that the case was not ripe for review, but Breyer also wrote a separate dissent in which he agreed with O'Connor on the notice issue. This fragmented approach should raise concern with both those who promote the use of regulations for environmental purposes, and those who favor unrestricted development.

CONCLUSION

Palazzolo leaves unanswered, or at least unclear, more questions than it clarifies. The one clear holding in the majority opinion is that pre-acquisition notice of land-use regulations does not bar a purchaser's inverse condemnation lawsuit. Several questions remain open. These include:

- To what extent must a landowner pursue development possibilities, and be denied, before the takings claim becomes ripe? A total of six of the justices ruled that this particular case was ripe. This indicates that it is not necessary to pursue and be denied development possibilities to the extent previously believed, but the case gives little or no guidance for future petitioners to determine whether they will be deemed to have satisfied the ripeness standard.

- To what extent will the pre-acquisition notice defeat the purchaser's claim that the regulations interfered with their reasonable investment-backed expectations? O'Connor's opinion suggests that such notice should have some bearing on the outcome, while Scalia's suggests that it should not.

- Will future inverse condemnation petitioners be allowed to segregate land and successfully claim that regulations have resulted in a taking of one portion, even though the other portion retains some economically beneficial use? This question was clearly identified in the majority opinion, but no possible answers were offered.

What is abundantly clear is that there will be more inverse condemnation litigation after *Palazzolo*. By removing the pre-acquisition bar and lowering the standard for establishing that a claim is ripe, the Court has insured that it will have the opportunity to address those issues identified herein, as well as others in the eminent domain area.[24] REI

NOTES

1. 260 U.S. 393; 67 L.Ed. 322, 43 S.Ct. 158 (1922).
2. *Penn Central Transp. Co. v. New York City*, 438 U.S. 104, 57 L.Ed.2d 631, 98 S.Ct. 2646 (1978).
3. 121 S.Ct. 2448; 150 L.Ed. 2d 592; 2001 U.S. LEXIS 4910 (2001). Hereinafter *Palazzolo*.
4. Although the eminent domain clause applies to the federal government as written, it has been applied to state governments through the fourteenth amendment.
5. *Palazzolo v. State of Rhode Island*, 746 A.2d 707; 2000 R.I. LEXIS 50; (2000).
6. *See*, Ronald D. Rotunda and John E. Nowak, Treatise on Constitutional Law, 3rd Ed., West Group, 1999 at section 2.13(d).
7. *See, Abbott Laboratories v. Gardner*, 387 U.S. 136, 87 S.Ct. 1507; 18 L.Ed.2d 681; 1967 U.S. LEXIS 2974 (1967).
8. Palazzolo, 746 A.2d at 714.
9. Palazzolo, 121 S. Ct. at 2461.
10. *Id.* at 2459.
11. *Id.* at 2460.
12. Palazzolo, 746 A.2d at 715–717. Justice Stevens took a similar approach in his separate opinion. He stated that "it is the person who owned the property at the time of the taking that is entitled to the recovery," but also stated that the taking occurred at the time the regulations were adopted. *See, Palazzolo v. Rhode Island*, 121 S.Ct. 2448; 150 L.Ed. 2d 592; 2001 U.S. LEXIS 4910 (2001) (Stevens, J., concurring in part and dissenting in part).
13. Palazzola, 121 S.Ct. at 2462.
14. *Id.* at 2462-2463.
15. *Id.* at 2463.
16. *Id.*
17. Marcia Coyle, "Landowners win right to attack rules." *The National Law Journal*, July 16, 2001, p.A1.
18. *McQueen v. South Carolina Dept. of Health and Environmental Control*, 340 S.C. 65, 530 S.E.2d 628, 2000 S.C. LEXIS 88 (2000).
19. *McQueen v. South Carolina Dept. of Health and Environmental Control*, 121 S.Ct. 2581, 150 L.Ed 2d 742, 2001 U.S. LEXIS 4949, (2001).
20. Palazzolo, 121 S.Ct. at 2465.
21. In September of 2001, the Rhode Island Supreme Court remanded the case to the Superior Court for the Penn Central analysis. *Palazzolo v. Rhode Island*, 785 A.2d 561, 2001 R.I. LEXIS 210 (2001).
22. Palazzolo, 121 S.Ct. at 2465.
23. *Id.*
24. *See*, Mark J. Zimmermann, "Decision of Note: Supreme Court Clarifies Takings Clause." *Environmental Compliance and Litigation Strategy*, July 2001, p.4.