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FROM *PENN CENTRAL* TO *LINGLE*: THE LONG BACKWARDS ROAD

RICHARD A. EPSTEIN*

INTRODUCTION

My major task in this Symposium is to supply the golden mean between the two previous articles. Professor Dale Whitman has offered us a rigorous legal analysis of various precedents in this vexed area of land use law.¹ Thereafter, Professor Richard Green supplied an insightful economic analysis of all the land use material fits together.² My task is to blend some law with some economics in order to address the Supreme Court's recent decision in *Lingle v. Chevron USA, Inc.*³ I hope to examine the (negative) contribution that the Supreme Court's decision has made to a systematic understanding of the larger law governing the taking of private property. In order to do so I shall divide the analysis into five parts. The first analyzes the doomed test of a regulatory taking that the Supreme Court applies in *Agins v. City of Tiburon*.⁴ The second part analyzes the peculiar bit of economic protectionism that is found in Hawaii Act 257.⁵ The third part analyzes and applies the well-known tripartite test for takings articulated by Justice Brennan in *Penn Central Transportation Co. v. City of New York*.⁶ The fourth part critiques the *Penn Central* decision, and the fifth part defends the proposition that the current muddle in takings law is not an accident, but comes from the consistent unwillingness of the Supreme Court to apply the

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1. Dale A. Whitman, *Deconstructing Lingle: Implications for Takings Doctrine*, 40 J. MARSHALL L. REV. 581 (2007).

2. Richard Green, Oliver T. Carr Professor of Real Estate Finance at George Washington University, Address at The John Marshall Law School, Center for Real Estate Law, 2006 Kratovil Conference: The Takings Clause Clarified by the U.S. Supreme Court (Sept. 29, 2006).

3. 544 U.S. 528 (2005).

4. 447 U.S. 255 (1980).

5. HAW. REV. STAT. § 486H-10.4 (2006). For full text, see the appendix.

6. 438 U.S. 104 (1978).

systematic view of private property that has developed on the private law side into constitutional law.

I. THE DOOMED *AGINS* TEST

To set the stage, let me start by noting that *Lingle* put in the crosshairs the standard formula, first articulated in *Agins v. City of Tiburon*,⁷ that the United States Supreme Court has used on multiple occasions to analyze regulatory takings. That case announced that a government regulation of private property should be treated as though it “effects a taking if [that regulation] does not substantially advance legitimate state interests.”⁸ The clear negative implication is that if the regulation does advance a legitimate state interest, then it is impermissible to find a (compensable) taking, which in fact was the fate of the land owner in *Agins*. On its face, the formula does not appear to move the ball forward because it deflects the takings inquiry into the still more nebulous question of what counts as “legitimate state interests.” Yet the *Agins* decision offers no serious insight on that question. Rather, its studied use of conclusory language was consciously meant to signal that the scope of the government power was greater than that which is found under the traditional, and somewhat more descriptive, account of the police power that limited the appropriate justifications to the “health, safety, morals and general welfare” of the public at large.⁹

Historically, *Agins*'s shift in language signaled the Supreme Court's ratification of the proposition that the government could impose a broad range of regulations free of the obligation to compensate. In *Agins* that power was used to its best advantage, as the Court sustained a Tiburon ordinance that required a minimum lot size of five acres because it advanced the legitimate state purpose of preventing development that might well change the character of the neighborhood by increasing population density.¹⁰ It goes without saying, of course, that local governments could have a legitimate interest in concentrating development in particular areas as well. Indeed the range of legitimate purposes is in some sense so broad that the *Agins* test provides virtually no constitutional safeguards against the traditional forms of land use regulation. Put in a different sense, the legitimate state purpose language is very close to the “conceivable” public purpose language that has darkened the Court's discussion of the public use requirement of the takings clause.¹¹ But even if we assume that

7. 447 U.S. 255.

8. *Id.* at 260.

9. It is no surprise that this formula finds resonance in *Lochner v. New York*, 198 U.S. 45, 53 (1905).

10. *Agins*, 447 U.S. at 261-62.

11. *See* *Haw. Hous. Auth. v. Midkiff*, 467 U.S. 229, 241 (1984).

this account captures the sense of the words “public use”, it is sadly misplaced here. Public use allows for takings *with* compensation. The regulation question seeks to explain what justifications allow for regulation *without* compensation. It is hard to think that the same or similar words could serve these two disparate objectives simultaneously.

This analytical difficulty notwithstanding, *Agins* is a predictable outgrowth of the original Supreme Court zoning decision, *Euclid v Ambler Realty Co.*,¹² which allowed for extensive land use regulation without compensation, while paying lip service to the traditional definition of the police power — in that instance by expanding the notion of nuisance beyond its common law foundations. The legitimate state interest language pushes the process a step further by uncoupling the police power from its common law roots that were still noticeable in *Euclid*, all with the express agenda of enlarging state power. Think nuisance and *Agins* comes out for the landowner, for no one could contend seriously that any building on five acres or more is needed to prevent odors and filth from migrating between the properties of the rich and famous.

In one of those constant mysteries in the takings law, however, the parties in *Lingle* proceeded on the novel assumption that this broad *Agins* test places substantial limitations on the use of government power. *Lingle* arose in connection with a Hawaii statute that sought in a number of ways to limit the ability of large oil companies to deal with its lessee-dealers, those firms that leased their service stations.¹³ The particular provisions limited by complex formula the increases in rent that the oil companies could impose on their protected tenants. All increases were limited to fifteen percent of the profits on gasoline sales, plus fifteen percent of the gross sales that the dealers receive from the other products they sell, with a further adjustment to offset any increase in rent that the oil company is obligated to pay on its underlying ground lease. That provision blocked the introduction by Chevron of a new rental policy that would have required its lessee-dealers to pay rentals tied to an escalating percentage of rents. The statute also blocked the ability of the oil companies to remove the current tenants from the leased premises at the expiration of the lease, and it prevented the oil companies from setting up new stations in the immediate proximity of existing stations. It also explicitly guaranteed to the individual holders of service stations the right to sell their interests in the open market, free of any interference from the landlord. The combined impact of those provisions that dealt with leasehold extensions and rate limitations meant that

12. 272 U.S. 365 (1926).

13. HAW. REV. STAT. § 486H-10.4 (2006). For full text, see the appendix.

the lessors could not evict the tenant when the alternative use of the property was far more valuable. The entire purpose of the statute was to create a wealth transfer from the lessors to the protected dealer-lessees, which could be documented by making any assessment of the market value of their respective interests.

The decision of Justice O'Connor is notable for its near obsessive concern with textual detail. When she speaks of the relationship of *Agins* to *Lingle*, her sole concern is with parsing the language of *Agins* to explain why it does not accurately capture the rules on regulatory takings. The gist of her argument is that the test looks at only one portion of the means/ends test, which in her view is more appropriate to a due process test than to a takings challenge, even if the grounds for distinction are obscure, to say the least. In addition, she noted that test does not take into account the character of the regulation or its distributional impact on the various parties. It does not, in a word, read like the three-part test for takings that the Court articulated in its decision in *Penn Central v. City of New York*.¹⁴

Wholly absent from her conscientious dissection of *Agins* is the want of any substantive examination of the actual impact of the Act on the respective positions of the landlords who are subject to its provisions, or the lessees who benefit from the operation. As David Callies rightly noted in his introductory address for this symposium, the early death by legislative repeal of the statute is not to be lamented.¹⁵ But it hardly helps to analyze this statute under *Agins* without some substantive view of its underlying scheme. Nor is it helpful to say that the state has, here or anywhere else, a legitimate interest in responding with high prices. If that's a legitimate interest, then the state also has a legitimate interest in combating low prices. When these two interests are combined, then for any set of observed prices, the state has a legitimate interest in trying to either raise them or lower them. So, by the time this exercise is finished, under either *Penn Central* or *Agins* the law develops a perfectly vacuous test to determine which ordinances should survive, and which should be struck down. Litigators, of course, don't care whether the test is vacuous. What they care about is whether the test gives them a

14. 438 U.S. 104.

15. David L. Callies, Benjamin A. Kudo Professor of Law at the William S. Richardson School of Law at the University of Hawaii at Manoa, Keynote Address at The John Marshall Law School, Center for Real Estate Law, 2006 Kratovil Conference: The Takings Clause Clarified by the U.S. Supreme Court (Sept. 29, 2006); see also 2006 HAW. SESS. LAWS 78 which was signed by the Governor May 5, 2006. That law indefinitely suspends the wholesale gas price controls that the state legislature had imposed in 2005, but it does not appear to affect § 486H-10.4. For a brief description of the recently passed law, see ABC News, Hawaii Gives Up On Gas Price Control, <http://abcnews.go.com/US/wireStory?id=1936960&CMP=OTC-RSSFeeds0312>.

plausible basis on which they can win a lawsuit. And so as we go through the particulars of this case, we should find at least some account of the Act that sets the rental provision in the larger context, thus making the nature of this wealth transfer wholly evident.

II. ECONOMIC PROTECTIONISM, HAWAII STYLE

To set the stage, it is important to understand that this Act is a classic piece of economic protectionism of the most ugly variety, benefiting independent dealers operating in the state of Hawaii. What the Court did was focus on the one provision that is sufficiently complicated to frustrate understanding — the rental provision — without revealing just how protectionist Act 257 is.¹⁶ The rate cap does allow for rents to increase with revenues in most cases, and with profits in the case of gasoline. But if the cap consistently was above the market or lease, then no one would choose to fight its existence. The law would be equivalent to setting the minimum wage at five dollars per hour when the market rate is at ten dollars. Similarly, even if we do not know the exact operation of this statute, we can be confident that it does not allow for a dollar-for-dollar offset by the simple device of raising gasoline prices. Presumably somewhere and somehow this cap has to bind, if not this year, then next. It counts as a fundamental theorem of sorts that ardent protectionists do not expend their political capital to pass idle acts.

That said, the anticompetitive aspects of other provisions in the Act are very clear. The territorial protections that the Act affords incumbents look like a straight-out division of markets that surely benefits the established dealers and only frustrates the efforts of out-of-state manufacturers to expand their market presence. The automatic renewal provision imitates the most obnoxious feature of all rent control laws. It takes a short term lease, and regards renewal as a free good for the benefit of tenants, which makes it impossible to remove incompetent dealers by waiting until the expiration of the lease. Now one has to buy them out, which hardly creates the desired incentives for excellent service. The tenant can of course throw off the lease if the value of the property goes down. But if it goes up then the option is worth exercising, which results in an implicit wealth transfer from landlord to tenant, equal to the capitalized value of the difference between the market and statutory rental rates. By allowing free assignability of the leasehold interest, Act 257 lets the present incumbent capture this differential by assigning the interest to a newcomer for a lump sum that is the best approximation of the

16. *Lingle*, 544 U.S. at 543-44.

discounted value of the future differential between market and contract rent.

The conclusion seems inescapable that Hawaii's Act 257 looks like an extremely easy case of expropriation. But Justice O'Connor was so focused on the verbal weaknesses of the *Agins* test that these economic matters were the last thing on her mind. In this regard, she was hardly helped by the focus of the expert testimony offered below. There the noted economic experts on both sides mainly discussed whether the reduced rents to the lessee-dealers would be passed onto consumers. The Ninth Circuit summarized the situation as follows:

The district court on remand heard testimony from Dr. John R. Umbeck, on behalf of Chevron, and Dr. Keith Leffler, on behalf of Hawaii. Based on their testimony, the court made the following relevant findings of fact: (1) oil companies will raise wholesale prices to offset any decrease in rent imposed by Act 257, thereby causing an *increase* in retail prices, (2) a preponderance of the evidence establishes that Act 257 will enable lessee-dealers to sell their leaseholds at a premium, (3) instead of decreasing retail gasoline prices by maintaining the presence of lessee-dealers in the market, Act 257 will *increase* gasoline prices by reducing the number of lessee-dealers. Based on these findings, the district court concluded that Act 257 does not substantially advance a legitimate state interest.¹⁷

The first of these findings seems odd, for if it were true then the dollar-for-dollar offset should imply that the statute has no effect on rents, at which point it is hard to explain why the Act would work an increase in retail prices, or why, as noted earlier, the lessee-dealers would work so hard for a provision that did not improve their economic position. The second finding is unquestionable, and offers conclusive evidence of the implicit wealth transfer. The third finding also looks correct since the territorial exclusions should on balance reduce the number of lessee-dealers. But all in all, the facial examination of Act 257 tells us all we need to know about who benefits and who loses. It is evident that the financial wealth of the oil companies did not help advance their political agenda when the local dealers had all the clout. The statute is a massive embarrassment, so the Court should have just struck it down.

When the case was before the Ninth Circuit, Hawaii abandoned the argument that Act 257 could lower consumer prices (by insulating dealers from competition, of course), but then shifted its position to make the last gasp argument that it was

17. *Chevron U.S.A., Inc. v. Bronster*, 363 F.3d 846, 855 (9th Cir. 2004) (emphasis added) (internal citations omitted), *affg* *Chevron USA, Inc. v. Cayetano*, 198 F. Supp. 2d 1182 (D. Haw. 2002). *Bronster* was reversed by *Lingle*, 544 U.S. 528 (2005).

proper to invoke the statute to protect lessee-dealers from the loss of their franchise.¹⁸ The entire expert dispute seems too obvious for words. Why would dealers work so hard to protect consumers at their own expense unless they received something from it? The issue of expropriation, moreover, should not turn on the question of whether the lessee-dealers had imbibed the spirit of Robin Hood, or whether they just sought to advance their own interests. Assume the former, and it is still not a defense against a taking from *A* to *B* show that *B* has given some portion of the spoils to *C*. As in so many cases, the only point that should occupy the attention of the Court is that the deliberate interference with ongoing contract relationships necessarily operates as a wealth transfer between the parties. At that point, the state could pay the oil companies for what it allows the lessee-dealers to take, or repeal the statute. And we know that once the implicit cost of the regulation is placed on the books, transparency will do its work, for no sane legislator would seek to tax his or her constituents for this parochial purpose.

This short exposition also tells us something about the unfortunate consequences that follow from some low-level rational basis review. Judges are often eager to say that the economics of a transaction is so complicated that we have to allow the legislatures to decide such question. But in truth, in this case the fingerprints of special interests are on every syllable of the statute, so that the net effect of the rational basis test is to force judges to turn somersaults to deny the obvious, in order to make the world safe for the kind of blatant political malfeasance embodied in Act 257.

III. *PENN CENTRAL* APPLIED

The irony, however, is that although Justice O'Connor's prolonged deliberation evaded the *Agins* test, she gave her endorsement to the standard *Penn Central* test for regulation with its tripartite formula that is no more responsive to the underlying substantive issues than is *Agins*. Recall by way of background that *Penn Central* gave a clear pass to the landmark preservation statute in New York City which allowed the city to prevent the use of the air rights over the Penn Central Terminal in order to preserve the distinctive view of that landmark. A simple direct analysis of that case notes that air rights are standard property rights in New York, which can be developed, mortgaged, leased, or sold. The only distinctive feature about them is that they necessarily require some support rights from below. But those details only go to the full delineation of the bundle of rights and its market value.

18. *Id.* at 855-57.

Any sound system of takings law recognizes that the government has the right to take by coercion even in circumstances where private parties can only acquire by voluntary purchase. But that analysis allows the state to condemn the air rights to preserve the public views, but only if it is prepared to pay the owner their market value. Justice Brennan, however, thought that it was better that New York be able to block the construction at no cost at all, so he refused to follow the state law characterization of property and developed, without argument, an alternative approach. His first move was to denature the relatively strong statement about property rights that was found in *Armstrong v. United States*: "The 'Fifth Amendment's guarantee . . . [is] 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."¹⁹ But Justice Brennan's basic move was to insist that the Court has been unable to develop any "set formula" to answer this question, so that "ad hoc" formulations are needed.²⁰ The upshot is his full version of the famous *Penn Central* test:

In engaging in these essentially ad hoc, factual inquiries, the Court's decisions have identified several factors that have particular significance. The economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations are, of course, relevant considerations. So, too, is the character of the governmental action. A "taking" may more readily be found when the interference with property can be characterized as a physical invasion by government, than when interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good.²¹

Justice O'Connor shows fealty to this decision when she writes: "The *Penn Central* factors . . . have served as the principal guidelines for resolving regulatory takings that do not fall within the physical takings or *Lucas* rules."²² It should be apparent, however how little this list of factors advances the inquiry into the constitutionality of Act 257. The economic impact of that regulation is negative on the oil companies and positive to the dealer-lessees, but in proportions that are difficult to determine. The inquiry is even more difficult than might appear because it seems proper to take all the provisions of the limitation into account together, and not isolate the price limitation for separate consideration. That comprehensive evaluation tilts the case in

19. *Penn Central Transp. Co. v. New York City*, 438 U.S. 104, 123 (1978) (quoting *Armstrong v. United States*, 364 U.S. 40, 49 (1960)).

20. *Id.* at 124.

21. *Id.*

22. *Lingle*, 544 U.S. at 539 (citing *Penn Central*, 438 U.S. at 124).

favor of invalidation, but cannot, given the squishy nature of the tripartite test, conclude the inquiry.

The interference with “investment-backed expectations” is also difficult to assess. Act 257 honored those expectations, after a fashion, by allowing a dollar-for-dollar pass through of any increases in the ground lease, which counts as a plus for the Act. But at the same time, it clearly blocked the rent flexibility that the oil companies thought that they had for good commercial reasons built into their leases. It is hard to sort these elements out in the context of *Penn Central*, for Justice Brennan wrote only about changes in land use, and held that new uses were not protected so long as existing uses covered costs.²³ My guess is that he would think that this factor therefore cut in favor of the state because it did not force the oil companies to go out of pocket, but only removed opportunities for future gain. Stated otherwise, he would show a lot of tolerance for government actions that were directed only to money, not towards use, as was the case with traditional rent control legislation, which has long been judged by that sort of relaxed standard.²⁴ Finally, on the physical/regulatory line, it seems clear in principle that the inability to recover possession at the termination of a lease amounts to a physical taking. But the entire history of the rent control laws rejects that characterization, and Justice O’Connor herself badly misfired on this issue when she held that so long as the tenant is allowed in for a year, then it should be treated as though he were allowed in to the property in perpetuity.²⁵ Only in the topsy-turvy world of constitutional accounting is the length of leasehold provision a side element in the bargain. My guess therefore is that this case would in the end be treated as a garden variety rent control statute under *Penn Central*, from which there is no relief.

IV. *PENN CENTRAL* CRITIQUED

The overall analysis takes a very different turn if we start with a critique of the *Penn Central* decision on which Justice O’Connor places such confidence.²⁶ Justice O’Connor did not fill any conceptual gap by offering some reasoned defense of the test. Rather, her only stab in that direction was the unilluminating statement that the major impetus of the Court’s jurisprudence is to identify forms of regulation that “are functionally equivalent to

23. *Penn Central*, 438 U.S. at 136.

24. See, e.g., *Birkenfeld v. City of Berkeley*, 550 P.2d 1001 (Cal. 1976) (invalidating a five year rollback in rents with no provision for increases of any sort).

25. See *Yee v. Vill. of Escondido*, 503 U.S. 519 (1992).

26. For my longer critique of the decision, see Richard A. Epstein, *The Ebbs and Flows in Takings Law: Reflections on the Lake Tahoe Case*, 1 CATO SUP. CT. REV. 5 (2002).

the classic taking,²⁷ without considering that all of them are. Most critically she did not explain why the constitutional test should differ from the private law approach, which places two propositions front and center: first, no owner is entitled to compensation for the negative economic impact from competition, and, second, any landowner may block the efforts of any neighbor to impose unilaterally a restrictive covenant on land use. That difference is, however, wholly obscured in the *Penn Central* formulation, which treats legal restrictions and competitive impact as indistinguishable from each other by rightly rejecting the proposition that “diminution in property value, standing alone, can establish a ‘taking’” — only to misapply it in the same breath by assuming that the imposition of a state restrictive covenant through a zoning ordinance counts as a simple diminution in value, without more.²⁸

In principle, however, the difference between zoning restrictions and economic competition as the source of value reduction is critical. Recall that competition advances social welfare in the way in which the simple expropriation of a partial interest in land does not. Nor is the *Penn Central* test saved by the observation that large damages are compensable, but smaller ones are not. That position makes no more sense than saying that a landowner can recover nothing if the property taken is worth a thousand dollars but recover everything if it is worth a million dollars. The usual and proper rule is that the extent of damages governs nothing more than the extent of compensation. It never functions as an on/off switch to see whether compensation is owing at all.

Nor does Justice O'Connor offer the slightest explanation of why Justice Brennan was correct to use the tendentious phrase “investment backed expectations” to determine the scope of the takings clause. That term appears nowhere in the Constitution,

27. “Although our regulatory takings jurisprudence cannot be characterized as unified, these three inquiries (reflected in *Loretto*, *Lucas*, and *Penn Central*), share a common touchstone. Each aims to identify regulatory actions that are functionally equivalent to the classic taking . . .” *Lingle*, 544 U.S. at 542.

28. *Penn Central*, 438 U.S. at 131:

Appellants concede that the decisions sustaining other land-use regulations, which, like the New York City law, are reasonably related to the promotion of the general welfare, uniformly reject the proposition that diminution in property value, standing alone, can establish a “taking,” see *Euclid v. Ambler Realty Co.*, 272 U.S. 365 (1926) (75% diminution in value caused by zoning law) . . .

Note that Justice Brennan is writing in the *Euclid* tradition, which makes it hard to defend the landowner's position in *Penn Central*. Justice Rehnquist's dissent stresses the “spot zoning” aspect of the case, i.e., the singling out of *Penn Central*'s property for special treatment creates an impermissible burden on the single owner. See *Penn Central*, 438 U.S. at 138-39.

and it evokes no clearly defined meaning. It surely cannot refer to the notion that property is unprotected if it is acquired by gift. Nor could it mean that the only property rights that are protected are those that have already been utilized. To the contrary, the function of property is to create security of title so that people do not have to build foolishly today in order to perfect their rights to develop the property tomorrow, which is what this unfortunate phrase seems to suggest. In the end, therefore, the *Penn Central* test was meant to convey the view that if the landowner could make effective use of his existing ground interest, then he had no right to use the air rights as well, because he could cover his costs of operation without being able to exploit the common law development rights.

Unfortunately, this position makes no more sense than allowing the state to take the north end of the land for free because the south end has been fully developed so that it covers the cost of acquisition for the whole. Justice Brennan's position has created immense difficulties in deciding what should be done when the air rights, as it were, went right down to the ground, so that no development could take place at all.²⁹ At this point, the landowner has no current viable use of property that covers initial costs, so that it is not possible to adopt without adjustment the *Penn Central* strategy of allowing current uses to continue while prohibiting new ones from taking place. In responding to this difficulty Justice O'Connor is happy to repeat the familiar bromide that "the owner's right to exclude others from entering and using her property [is] perhaps the most fundamental of all property interests."³⁰ Justice O'Connor seems aware that the "most fundamental" interest cannot be the only one,³¹ for if it were, then the state could respect the landowner's right to exclude others on the one hand while excluding the landowner himself. Clearly any impoverished *definition* of private property that literally only encompassed the right to exclude should — an indeed does — flunk constitutional scrutiny. The takings protection is reduced to a hollow shell if the interests in entry, occupation, use, development and disposition are allowed unceremoniously to fall to the cutting room floor because somehow they do not rate as fundamental. Yet once these other rights are admitted back into the bundle, it is an utter mystery why they should be regarded as second-tier for constitutional purposes when they have equal dignity with the right to exclude as a matter of the private law.

Nor does the *Penn Central* test do better on its third element. The character of the government action refers to the undefended

29. See, e.g., *Lucas v. S.C. Coastal Council*, 505 U.S. 1003 (1992).

30. *Lingle*, 544 U.S. at 539.

31. See *supra* note 27.

categorical distinction between physical and regulatory takings, where the former are said to be governed by a near *per se* rule for compensation and the latter is subject to the very weak standards of rational basis review.³² Justice O'Connor is of course right that physical dispossession by government should be strongly discouraged, but does not explain why that principle does not reach the air rights that were placed off limits in *Penn Central* or the lease renewal provisions in *Lingle*, which of course keep the landlord out of possession when the lease expires, and thus denies him the right to exclude in the future. And even if these various forms of occupation are not at issue, Justice O'Connor never explains why the restrictive covenant that the state unilaterally imposes is not a taking of the development or use rights inherent in land.

In the end, Justice O'Connor's merciless dissection of the incomplete *Agins* formula leads her to jump from the frying pan into the fire. At the conceptual level, under *Penn Central*, no one quite knows the definition of the parcel of rights that are protected by the Takings Clause. No one knows how much diminution in value is required before a landowner is entitled to compensation, and no one knows what kind of public justifications cut off the right to reparations. Dale Whitman confesses that he does not understand how this test works twenty-eight years after this formulation.³³ No one else who litigates these matters does either.

V. PRIVATE PROPERTY VERSUS "CONSTITUTIONAL" PRIVATE PROPERTY

The impasse over Act 257 is neither unique nor ephemeral, for it exposes the enduring disjunction between the massive sophistication that private lawyers use to wring every ounce of value out of private property and the primitive tools that constitutional lawyers use to drain private property of its value and utility by removing from it the key attributes of use, development, and distribution.

The key to the success of the private law in this area is that lawyers know that unlocking the value from property often depends on the ability to break down the property rights in land (or indeed any other asset) into its constituent elements. Hence the initial owner who acquires private property by occupation has the undivided fee simple, which he is free to divide by time, by leases, by concurrent interests, through tenancies in common, by credit instruments, through mortgages, by physical divisions, as

32. See, e.g., *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982) (affirming that permanent occupation by the government of physical property constitutes a taking).

33. Whitman, *supra* note 1, at 589.

through air and mineral rights, and through covenants and easements between neighbors. Those owners all follow the simple proposition that they will enter into any complex transaction of property rights if the gain from the subdivision of rights exceeds the transaction costs needed to bring those gains about. As those costs are reduced by more sophisticated contracting and registration, the state of a title assumes an ever more complex state in which the sum of the rights remains constant while the value of the rights in separate hands increases. A sensible constitutional law would track the private law so as to allow each of these elements to be created. To the private lawyer, all property rights have equal dignity no matter how defined, so long as they derived from a single grant from the original owners. But our constitutional law holds exactly the opposite, such that fragmented interests, such as air rights or restrictive covenants, are subject to confiscation when separated from the original fee simple interest.

We can see this massive difference by looking at how private law treats restrictive covenants, which restrict the use of land owned by others, and easements, which allow entrance over land owned by others. The private law has worked long and hard to unify these two branches of law so that both easements and servitudes have become part of the larger law of servitudes.³⁴ Yet one look at Justice Scalia's decision in *Nollan v. California Coastal Commission*³⁵ shows just how far astray from this basic conception the Supreme Court has gone, even for Justices with some inclination for protecting property rights. There the Court ingeniously applied some version of the doctrine of unconstitutional conditions by holding that the state could not extract a lateral easement over the front of Nollan's land by threatening to withhold the permit to build.³⁶ It only had to reach that position because it was caught in the intellectual vice of *Euclid*, which had led all members of the present Supreme Court to take the position that easements are property because they're possessory, but restrictive covenants are not (really) property because they are only rights that restrict the use that others make of their own land. Once these restrictive covenants in the form of zoning laws are taken out from underneath the entire protection of

34. See RESTATEMENT (THIRD) OF PROPERTY: SERVITUDES § 1.1 (2000) (classifying easements as servitudes); Susan F. French, *Toward a Modern Law of Servitudes: Reweaving the Ancient Strands*, 55 S. CAL. L. REV. 1261 (1982) (grouping easements, real covenants, and equitable servitudes into one category collectively called "servitudes"). My earlier writings on this point are Richard A. Epstein, *Covenants and Constitutions*, 73 CORNELL L. REV. 906 (1988), and Richard A. Epstein, *Notice and Freedom of Contract in the Law of Servitudes*, 55 S. CAL. L. REV. 1353 (1982).

35. 483 U.S. 825 (1987).

36. *Id.* at 837.

property, the question of whether they live or die in any individual cases is subject to huge and pointless political struggles.

Thus with easements, the Supreme Court follows the rules that on matters of valuation, which holds "the more you take, the more you pay." Given that basic direction, the law of takings is *never* concerned with how much of the original bundle of rights remains after the government has taken its sticks. It only asks what sticks were taken. So if you have 100 acres and the government takes 60, it pays you for the 60 and you get to keep the 40. The fine points come into play because in different settings the 40 acres that remain could be worth either more or less than 40% of value. But once the discussion turns to covenants, then this rule is junked. No longer does the government face a legal regime that requires it to pay more when it takes more. That approach is too simple. Instead the Supreme Court tries to establish some permissible *ratio* between what is taken and what is left over. Of course it does not tell us what number tips that balance. All we know is that some major restrictions may be imposed with impunity, so that the dominant incentive on local governments is to stop just short of that imaginary line in the sand when it restricts land use. Accordingly, the law raises this huge discontinuity. Let local government put a little restriction on land, and it pays nothing; restrict a little more, and it still pays nothing. Perhaps the same technique applies several times. Then the local government reaches that magic point, and once it gets up there, Bingo! It pays for everything. Well, every single land use lawyer knows this drill, and none of them like to lose at Bingo. So what they do is put in place as much regulation as they can, so long as their pay out obligation is zero. But occasionally they overreach, which is why this game often ends in high stakes litigation.

CONCLUSION

The moral is clear. The right results depend on the right starting point. Until the Justices of the Supreme Court recognize that private law conceptions of private property ought to inform the constitutional analysis, they will never get the analysis right. Justice Brennan's magic system of property rights in *Penn Central* was just the wrong place to begin. Occasionally there's a glimmer of recognition, as in the *Nollan* case, which sought to place some limitations on the state's ability to impose hard choices on landowners. But in general, the decision of the Supreme Court to embrace "ad hoc" determinations of takings law has a predictable result: it makes a mess out of an area of law that is amenable to great precision. It is surely time to start over. The Supreme Court made a small step forward when it rejected the *Agins* test which asked whether regulations substantially advanced a

legitimate state interest. But it took a giant backwards when it reaffirmed the confused and mischievous *Penn Central* standard.

APPENDIX

§ 486H-10.4. Restrictions on manufacturers or jobbers in operating service stations; lease rent controls; definitions.

(a) Beginning August 1, 1997, no manufacturer or jobber shall convert an existing dealer retail station to a company retail station; provided that nothing in this section shall limit a manufacturer or jobber from:

(1) Continuing to operate any company operated retail service stations legally in existence on July 31, 1997;

(2) Constructing and operating any new retail service stations as company retail stations constructed after August 1, 1997, subject to subsection (b); or

(3) Operating a former dealer retail station for up to twenty-four months until a replacement dealer can be found if the former dealer vacates the service station, cancels the franchise, or is properly terminated or not renewed.

(b) No new company retail station shall be located within one-eighth mile of a dealer retail station in an urban area, and within one-quarter mile in other areas.

(c) All leases as part of a franchise as defined in section 486H-1, existing on August 1, 1997, or entered into thereafter, shall be construed in conformity with the following:

(1) Such renewal shall not be scheduled more frequently than once every three years; and

(2) Upon renewal, the lease rent payable shall not exceed fifteen per cent of the gross sales, except for gasoline, which shall not exceed fifteen per cent of the gross profit of product, excluding all related taxes by the dealer operated retail service station as defined in section 486H-1 and 486H-10.4 plus, in the case of a retail service station at a location where the manufacturer or jobber is the lessee and not the owner of the ground lease, a percentage increase equal to any increase which the manufacturer or jobber is required to pay the lessor under the ground lease for the service station. For the purposes of this subsection, "gross amount" means all monetary earnings of the dealer from a dealer operated retail service station after all applicable taxes, excluding income taxes, are paid.

The provisions of this subsection shall not apply to any existing contracts that may be in conflict with its provisions.

(d) Nothing in this section shall prohibit a dealer from selling a retail service station in any manner.