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INTERGOVERNMENTAL TAKINGS AND JUST COMPENSATION: A QUESTION OF FEDERALISM

MICHAEL H. SCHILL†

Table of Contents

INTRODUCTION	830
I. EMINENT DOMAIN AND THE OBLIGATION TO COM- PENSATE UNDER CURRENT LAW	833
A. <i>The Power of Eminent Domain</i>	833
B. <i>Compensation For Intergovernmental Takings</i> ..	838
II. JUSTIFYING COMPENSATION FOR PUBLIC CON- DEMNESSES	841
A. <i>Preventing Unfair Distribution of Burdens of Government</i>	841
1. Preventing Unfair Burdens: History and Pre- cedent	842
2. Burdens and Benefits	844
3. Prevention of Unfair Burdens as a Rationale for Compensating Intergovernmental Con- demnees	847
B. <i>Minimizing Investment Risk</i>	851
1. Compensation, Risk Minimization, and the Private Condemnee	851
2. Risk Minimization and Intergovernmental Takings	857
C. <i>Avoiding Fiscal Illusion</i>	859
D. <i>Protection From Political Exploitation</i>	861
1. Private Takings, Just Compensation, and the Evils of Faction	862

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2. Intergovernmental Takings, Faction, and Federalism	865
a. <i>The Case For Federalism</i>	866
(i) Preservation of Individual Liberty	866
(ii) Promotion of Citizen Participation	868
(iii) "Laboratories For Experimentation"	870
(iv) Efficient Provision of Public Goods	871
b. <i>Federalism, the Courts, and the Political Process</i>	873
c. <i>Intergovernmental Takings and the Political Process</i>	880
III. COMPENSATING THE INTERGOVERNMENTAL CONDEMNEE	889
A. <i>Just Compensation For Private Condemnees</i>	890
B. <i>Just Compensation For Intergovernmental Condemnees</i>	892
C. <i>Measuring Compensation for Intergovernmental Condemnees</i>	897
CONCLUSION	901

INTRODUCTION

Since the late nineteenth century, the federal government has exercised the power of eminent domain¹ with respect to property owned by state and local governments.² The just compensation clause of the fifth amendment to the United States Constitution³ requires the federal gov-

¹ Eminent domain has been defined as "the right belonging to a sovereignty to take private property for its own public uses, and not for those of another." *Kohl v. United States*, 91 U.S. 367, 373-74 (1875); see also 1 NICHOLS ON EMINENT DOMAIN § 1.11 (J. Sackman 3d ed. 1985) (Eminent domain is "the power of the sovereign to take property for public use without the owner's consent." (footnote omitted)). For a discussion of the origins of the eminent domain power, see *infra* notes 10-18 and accompanying text.

² For the purpose of convenience, counties, cities, towns, villages, boroughs, and special districts will be collectively referred to in this article as "localities" or "local governments." For a discussion of the distinctions among different types of local governments, see 1 E. McQUILLIN, *THE LAW OF MUNICIPAL CORPORATIONS* §§ 2.01-2.52 (3d ed. 1987); O. REYNOLDS, *LOCAL GOVERNMENT LAW* §§ 6-13 (1982). Under current law, local governments are deemed to be subdivisions of the state in which they are located, deriving all of their power from the state. See *infra* note 40 and accompanying text. Federal exercise of the power of eminent domain with respect to property owned by states and localities will be referred to as "intergovernmental takings."

³ "No person shall . . . be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensa-

ernment to compensate private property owners when it condemns their property. Despite the absence of any reference to publicly owned property in the just compensation clause, federal courts have required the United States to compensate states and localities when it takes their property. In 1984, the United States Supreme Court first addressed the question of why compensation must be paid for intergovernmental takings, and how that compensation should be computed.⁴ In *United States v. 50 Acres of Land*,⁵ the Court unanimously held that public condemnees should receive the same compensation as private condemnees,⁶ because the loss to a public entity may be as severe as the loss to a private person or entity.⁷ In effect, the Court equated public entities with private entities, with respect to both the rationale for compensation, and the method for computing that compensation.

In this Article, I will demonstrate that the justifications for compensating private and public property owners whose property is condemned⁸ by the federal government are not congruent. Some of the

tion." U.S. CONST. amend. V.

⁴ The Court had previously held that states and localities were entitled to compensation for intergovernmental takings. See *United States v. Carmack*, 329 U.S. 230 (1946) (condemnation of local property for federal post office and customhouse). Nevertheless, in *Carmack* the Court failed to consider in any detail the justification for compensation, or how compensation should be computed.

⁵ 469 U.S. 24 (1984).

⁶ According to the Court, the appropriate measure of compensation is the condemned property's fair market value at the time of the taking. See *id.* at 33. For further discussion of the concept of just compensation and the *50 Acres of Land* case, see *infra* text accompanying notes 254-79.

⁷ As the Court stated:

When the United States condemns a local public facility the loss to the public entity, to the persons served by it, and to the local taxpayers may be no less acute than the loss in the taking of private property. Therefore, it is most reasonable to construe the reference to "private property" in the Takings Clause of the Fifth Amendment as encompassing the property of state and local governments when it is condemned by the United States.

50 Acres of Land, 469 U.S. at 31 (footnote omitted).

⁸ For the purposes of this Article, a "condemnation" will be treated as synonymous with an exercise by the federal government of its power of eminent domain. Unless specifically stated otherwise, all condemnations will be assumed to result from a conscious decision by the federal government to appropriate property for federal use or from physical damage to property caused by federal projects. See, e.g., *Carmack*, 329 U.S. 230 (1946) (condemnation of park, courthouse, city hall, and library for post office and customhouse); *Wayne County v. United States*, 53 Ct. Cl. 417 (1918) (destruction of public road by federal dam project), *aff'd* 252 U.S. 574 (1920). This Article does not explicitly consider instances in which a federal regulation diminishes the value of property so as to constitute an implicit or regulatory taking. See, e.g., *Andrus v. Allard*, 444 U.S. 51 (1979) (federal law prohibiting sale of objects containing eagle feathers is not a taking); *United States v. Central Eureka Mining Co.*, 357 U.S. 155 (government order temporarily closing gold mines not a taking), *reh'g denied*, 358 U.S. 858 (1958). Nevertheless, some of the present analysis would doubtless apply to regulatory takings.

functions served by compensating private condemnees have analogues to functions served by compensating public property owners. Nevertheless, by equating states and localities with private entities, the Court has failed to recognize that the most compelling justification for compensating intergovernmental condemnees derives from the structure of our constitutional system: A constitutional obligation to compensate intergovernmental condemnees protects the important role assigned to states in our federal system. Once the problem of intergovernmental takings is viewed in terms of the proper relationship between nation and state, it becomes clear that the mechanics of compensation should not be dictated, as the Court in *50 Acres of Land* indicates, by rules developed for private condemnees. To the contrary, an appropriate compensation rule must be one particularly suited to protecting states and localities from the disruption and exploitation made possible by the federal power of eminent domain.

In Part I of this Article, I describe how courts and commentators have justified the federal power to condemn property owned by private persons and public entities, and examine the judicial development of a compensation requirement for intergovernmental takings.

In Part II, I develop a justification for compensating state and local governments. I examine each of the rationales offered by courts and commentators for compensating private property owners and apply these rationales to states and localities. Two reasons often given for compensating private owners — preventing unfair and unequal economic burdens with respect to the costs of government, and minimizing investment risk — are much less compelling justifications for compensation when the condemnee is a public entity. Although these two rationales for compensation are ultimately unpersuasive, a close examination of how they apply to public entities enables one to understand better the nature of intergovernmental takings as well as their impact on states and localities. The third justification for compensation, prevention of allocative inefficiency caused by fiscal illusion, supports a compensation requirement, regardless of whether the condemnee is a public or private entity. The most important justification for compensating states and localities derives from the role that compensation serves in protecting the liberty of private citizens. Because states and localities play a vital role in the nation's political process, a constitutional compensation requirement is necessary to protect states, localities, and their citizens from exploitative and disruptive rent-seeking.

In Part III, I discuss how just compensation is computed for private and public condemnees, and conclude by proposing an alternative formula for compensating public entities. The "fair market value"

method of computing compensation for private condemnees, (which the Court in *50 Acres of Land* has also required for public condemnees) cannot be relied upon to protect states and localities from exploitation and disruption. I argue that, rather than relying on the inapt analogy between public and private condemnees, a more satisfactory method of computing just compensation for intergovernmental takings can be derived from the principle of full indemnification.

I. EMINENT DOMAIN AND THE OBLIGATION TO COMPENSATE UNDER CURRENT LAW

The fifth amendment to the United States Constitution provides that "private property [shall not] be taken for public use, without just compensation."⁹ In addition to omitting any reference to publicly owned property, the Framers of the Constitution failed specifically to empower the federal government to take property by eminent domain, regardless of whether the property is owned by private or public entities.

A. *The Power of Eminent Domain*

Despite the absence of any express delegation of power in the Constitution, the existence of a federal power of eminent domain has not been seriously questioned since the mid-nineteenth century.¹⁰ Although little is known about the deliberations leading to the inclusion of the just compensation clause in the Bill of Rights,¹¹ it is likely that the Framers were influenced by natural law theorists, most of whom assumed that the state had the power to expropriate property.¹² This

⁹ U.S. CONST. amend. V.

¹⁰ See, e.g., *United States v. Gettysburg Elec. Ry.*, 160 U.S. 668 (1896) (eminent domain used to condemn land owned by rail company in order to preserve Gettysburg battlefield); *Kohl v. United States*, 91 U.S. 367 (1875) (federal government may take private property without consent of state in which it is located). However, in 1845, the Supreme Court stated that "the United States have [sic] no constitutional capacity to exercise municipal jurisdiction, sovereignty, or eminent domain within the limits of a state or elsewhere, except in the cases in which it is expressly granted." *Pollard's Lessee v. Hagan*, 44 U.S. (3 How.) 212, 223 (1845).

¹¹ See F. BOSSELMAN, D. CALLIES, & J. BANTA, *THE TAKING ISSUE* 99-100 (1973) [hereinafter F. BOSSELMAN]; E. PAUL, *PROPERTY RIGHTS AND EMINENT DOMAIN* 74 (1987).

¹² See F. BOSSELMAN, *supra* note 11, at 100; E. PAUL, *supra* note 11, at 74-77; Stoebuck, *A General Theory of Eminent Domain*, 47 WASH. L. REV. 553, 559-60 (1972) [hereinafter Stoebuck, *A General Theory*]; Stoebuck, *Police Power, Takings, and Due Process*, 37 WASH. & LEE L. REV. 1057, 1076 (1980) [hereinafter Stoebuck, *Police Power*]. But see Note, *The Origins and Original Significance of the Just Compensation Clause of the Fifth Amendment*, 94 YALE L.J. 694, 710 & n.87 (1985) [hereinafter Note, *Origins & Significance*] (observing that while Madison was familiar

power typically was justified on the ground that those who consented to government implicitly agreed that private property must give way to public power when necessary to achieve a public purpose.¹³

In 1875, the Supreme Court held for the first time in *Kohl v. United States*,¹⁴ that the federal government had the power to condemn private property without the consent of the state in which the property was located.¹⁵ In finding that the United States government had the power of eminent domain, Justice Strong, echoing the natural law scholars of the sixteenth and seventeenth centuries, argued that the ability to take property was inseparable from the sovereignty of the federal government. If the national government could be blocked by state prohibitions or the unwillingness of property owners to sell their property, the "constitutional grants of power may be rendered nugatory, and the government is [sic] dependent for its practical existence upon the will of a State, or even upon that of a private citizen."¹⁶ The Court expanded upon *Kohl* in *United States v. Gettysburg Electric Railway Company*,¹⁷ observing that the power of eminent domain is implied because it is necessary and appropriate to the exercise of the

with writings of natural law scholars, he believed property rights were a creation of positive law). In addition to natural law, the Framers were likely influenced by English parliamentary and colonial practice. For examples of the exercise of eminent domain by the English parliament and American colonial governments, see Stoebe, *A General Theory*, *supra*, at 575-83.

¹³ As Grotius maintained:

[T]he property of subjects belongs to the state under the right of eminent domain; in consequence the state, or he who represents the state, can use the property of subjects, and even destroy or alienate it, not only in case of direct need . . . but also for the sake of public advantage; and to the public advantage those very persons who formed the body politic should be considered as desiring that private advantage should yield.

2 H. GROTIUS, *DE JURE BELLI AC PACIS* 807 (book III, ch. XX) (trans. 1925). Grotius and other natural law scholars who wrote on the power of eminent domain also argued that the owner whose property was taken should be entitled to compensation. See *infra* notes 46-47 and accompanying text.

¹⁴ 91 U.S. 367 (1875). In *Kohl*, private landowners challenged a federal condemnation of a parcel of land on which the government proposed to build a post office and other public facilities.

¹⁵ See *id.* at 374. Prior to the act challenged in *Kohl*, the federal government appropriated property in states by purchase, by instituting actions pursuant to state law, by requesting that the state condemn property and transfer it to the federal government, or by gaining the consent of the state in which the property was located. See 1 NICHOLS ON EMINENT DOMAIN, *supra* note 1, at § 1.24; E. PAUL, *supra* note 11, at 159 n.10.

¹⁶ *Kohl*, 91 U.S. at 371. The Court also argued that the existence of the power of eminent domain is implied by the just compensation clause. According to the Court, the just compensation clause limits the power of eminent domain, hence the power must exist in the first place. See *id.* at 372-73.

¹⁷ 160 U.S. 668 (1896).

federal government's delegated powers.¹⁸

In recent years, some commentators have questioned the wisdom of the premise underlying the *Kohl* and *Gettysburg Electric Railway* decisions.¹⁹ Condemnation of property entails a forced exchange of property for which a court seeks to determine the price that a willing seller would accept from a willing buyer.²⁰ Critics of eminent domain argue that the true value of property to a condemnee can be revealed only by a consensual transfer. Partly as a result of insufficient information and partly because of difficulties of computation, however, federal courts have developed rules of convenience that leave condemnees uncompensated for certain elements of the property that they might value.²¹

Because court-ordered compensation for a coerced sale is unlikely to equal that to which a willing seller would agree, eminent domain is considered economically inefficient.²² Critics argue that in many instances the inefficiencies created by condemnations could be avoided by requiring the government to purchase property through the private market.²³ Nevertheless, even those who criticize the power of eminent domain admit that it might be necessary in certain circumstances. For example, forced transfers may be required when a landowner has mo-

¹⁸ *Id.* at 679, 681.

¹⁹ See, e.g., R. COOTER & T. ULEN, *LAW AND ECONOMICS* 194 (1988) (when the government purchases from a small number of persons, it should not necessarily be allowed to compel a sale at fair market value); R. POSNER, *ECONOMIC ANALYSIS OF LAW* 49-50 (3d ed. 1986) (the government may not require the power of eminent domain when transaction costs are low).

²⁰ See *infra* note 247 and accompanying text.

²¹ For example, fair market value compensation typically does not include compensation for business losses, relocation expenses, or court costs. See *infra* notes 250-53.

²² The criterion of efficiency preferred by many economists is named after a nineteenth-century economist, Vilfredo Pareto. An allocation of resources is Pareto efficient if it is not possible to change the allocation to make someone better off, without making someone else worse off. The concept of Pareto efficiency, however, has limited utility since it is extremely difficult to conceive of any new policy that would not make someone worse off. A second measure of efficiency, Kaldor-Hicks efficiency, is more frequently utilized in cost-benefit analysis. A given allocation of resources is Kaldor-Hicks efficient if those made better off could compensate those made worse off. To meet the requirements of Kaldor-Hicks efficiency, actual compensation need not be paid. See G. DOWNS & P. LARKEY, *THE SEARCH FOR GOVERNMENT EFFICIENCY* 7 (1986). Court-ordered compensation is unlikely to be Pareto efficient because it may not equal the price the condemnee would voluntarily accept from a purchaser. The price differential indicates that the condemnee is worse off as a result of the condemnation. However, the condemnation may be Kaldor-Hicks efficient, because the government could, theoretically, redistribute the consumer surplus expropriated.

²³ See R. POSNER, *supra* note 19, at 49 (in settings with low transaction costs, the government should transact in the private market); Munch, *An Economic Analysis of Eminent Domain*, 84 J. POL. ECON. 473, 495 (1976) (eminent domain may not be more efficient than consolidation through the free market); see also Stoebe, *A General Theory*, *supra* note 12, at 560 (observing that it is "far from certain" that governments require the power of eminent domain).

monopoly power, or in situations where transaction costs are high, either as a result of strategic bargaining, or the existence of a large number of landowners.²⁴

The rationales that support a federal power of eminent domain with respect to private property also apply to federal takings of state and local property, albeit in a somewhat attenuated fashion. It is improbable that a state or local government would bargain strategically, seeking to appropriate the gains of a federal project for itself. Most federal projects that involve intergovernmental takings create significant benefits for states and localities, benefits which might be jeopardized by such bargaining.²⁵ Nevertheless, in exercising its constitutionally delegated powers, the federal government might require specific property with which a state or locality would not willingly part, either because of its value to the public entity, or because the state or locality wished to block a project that it viewed as undesirable. In these instances the federal power to condemn state and local property seems both necessary and justified to ensure that the United States government is able to exercise fully its constitutional authority.²⁶

Since the late nineteenth century, federal courts have upheld the authority of the federal government to condemn property owned by

²⁴ See R. POSNER, *supra* note 19, at 49-50. If the federal government did not have the power to condemn property, it would be forced to bargain with property owners. If only one particular parcel of property were appropriate for the government project, the owner of that parcel would have monopoly power with respect to the government. The owner would be able to extract from the government a price in excess of the opportunity cost for the property, thereby converting public surplus to private surplus. If the government and the property owner were each to bargain strategically (i.e., hold out for a price either higher or lower than the price they would otherwise accept), transaction costs would increase, potentially leading to inefficient results. For example, the parties might be unable to agree on a purchase price despite it being in the interests of both to consummate a sale. Alternatively, the transaction costs could be so high as to make an otherwise efficient project too expensive. Transaction costs would be multiplied for projects requiring property from many different owners. See Merrill, *The Economics of Public Use*, 72 CORNELL L. REV. 61, 74-75 (1986) [hereinafter Merrill, *Economics of Public Use*].

²⁵ See *infra* notes 70-81 and accompanying text. In many cases, not only does the state or locality submit to the federal eminent domain power without complaint, but frequently it contributes property to the federal project either for no money or for nominal reimbursement. Interview with Monroe Lesser, U.S. Army Corps of Engineers (Washington, D.C. June 13, 1988).

²⁶ A federal condemnation of public property against the wishes of the state or locality raises issues regarding the appropriate relationships among the federal government, states, and localities in our federal system. Under the conception of federalism set forth herein, federal power to coerce property transfers from states and localities is acceptable, provided that sufficient compensation is paid to the state or locality to enable it to replace the condemned property, if the state or locality can show that the facility taken provided a benefit that would not be as fully provided after the condemnation. See *infra* text accompanying notes 280-88.

states and localities. In 1887, in *Stockton v. Baltimore & N.Y.R. Co.*,²⁷ a federal appeals court upheld a federal law authorizing the condemnation of state property for construction of a railroad bridge. The court observed that the federal government had constitutionally delegated powers with respect to interstate commerce and that the exercise of these powers would frequently necessitate the acquisition of publicly owned property.²⁸ A requirement that the federal government obtain the state's consent to appropriate publicly owned property would permit states to stand in the way of the execution of these constitutionally vested powers.²⁹ The power of eminent domain with respect to state property, like the power to condemn private property, was necessary for the federal government to exercise its powers.³⁰ Later Supreme Court cases affirmed the principle that the national government must have the power³¹ to condemn state and local property.³²

²⁷ 32 F. 9 (1887).

²⁸ See *id.* at 20-21.

²⁹ See *id.* at 16-17.

³⁰ See *id.* at 17-19.

³¹ Some federal courts adopted rules of construction which had the effect of limiting the federal eminent domain power with respect to property which was already being used for public purposes. Under the test of "superior public use," when the federal government sought to condemn property already being used by a state or local government for public purposes, and the legislation authorizing the taking made no express provision for condemnation of public property, some courts required a showing that the proposed federal use was higher and superior to the public use of the state or locality. See, e.g., *United States v. City of Tiffin*, 190 F. 279, 282 (C.C.N.D. Ohio 1911) (requiring judicial determination of whether use of land for post office was more important than use of land for public alley); *In re Certain Land in Lawrence*, 119 F. 453, 456 (D. Mass. 1902) (suggesting, but not deciding, that use for post office was superior to use for public park).

Under the doctrine of "prior public use," some courts held that property already devoted to a public use could not be taken, absent legislation which authorized the taking in express words or by necessary implication. See, e.g., *United States v. 929.70 Acres of Land*, 205 F. Supp. 456, 457 (D.S.D. 1962) (Congress expressly or impliedly included property within authorization statute by specifically mentioning it in legislative reports); *United States v. Sixty Acres*, 28 F. Supp. 368, 372 (E.D. Ill. 1934) (finding that Congress implied condemnation of lands at issue, because they would be destroyed by federal dam project); *United States v. Certain Land In Town of New Castle*, 165 F. 783, 788-89 (C.C.D.N.H. 1908) (general federal authorization to purchase land not specific enough to permit condemnation of land devoted to prior public use). The doctrine of prior public use has been disapproved of or severely limited by subsequent cases. See, e.g., *United States v. Carmack*, 329 U.S. 230, 242-43 (1946) (upholding authority of government officials to choose specific sites owned by city for federal facilities based upon general congressional authorization); *United States v. Certain Parcels of Land in Town of Denton*, 30 F. Supp. 372, 379 (D. Md. 1939) (doctrine of prior public use not applicable when Congress delegates the power to select post office sites).

³² See *Carmack*, 329 U.S. 230 (1946) (condemnation of park, courthouse, city hall, and library for post office and customhouse); *United States v. Gettysburg Elec. Ry.*, 160 U.S. 668 (1896) (condemnation of land owned by rail company for preservation of Gettysburg battlefield); *Wayne County v. United States*, 53 Ct. Cl. 417 (1918)

B. *Compensation For Intergovernmental Takings*

Once federal courts decided that the federal power of eminent domain extended to state and local property, they were faced with the question of whether compensation should be paid to public condemnees. Although courts encountered no textual or doctrinal impediment to finding that states and localities should be treated as private individuals with respect to an implied power of eminent domain, the fifth amendment's express requirement of compensation for *private* property made extension of compensation to public entities problematic.³³ Neverthe-

(destruction of county road as result of dam project), *aff'd*, 252 U.S. 574 (1920); *United States v. Town of Nahant*, 153 F. 520 (1st Cir.) (1907) (condemnation of town sewer for fortifications and coast defenses). Nevertheless, some courts and commentators have indicated that the power of the national government to condemn state and local property might be limited by federalism concerns. *See, e.g.*, *United States v. 4,450.72 Acres of Land*, 27 F. Supp. 167, 175 (D. Minn. 1939) (lack of limits on eminent domain would give federal government power to "arbitrarily imperil the very functions of the state itself"), *aff'd*, 125 F.2d 636 (8th Cir. 1942); C. RANDOLPH, *THE LAW OF EMINENT DOMAIN* § 60 (1894) (maintaining that "in a controversy between the United States and a State the Supreme Court may [base its decision on relative state and federal interests] in order to fairly protect the agencies of the State"). *But see* *Oklahoma v. Guy F. Atkinson Co.*, 313 U.S. 508, 534 (1941) (tenth amendment is no bar to condemnation of state property for dam project); *St. Louis v. Western Union Tel. Co.*, 148 U.S. 92, 101 (1893) (implies in dicta that federal government could condemn statehouse if it paid compensation to state).

³³ Few clues exist to shed light on whether the just compensation clause was intended to mandate compensation for intergovernmental takings. Very little direct evidence exists regarding why the clause was included in the fifth amendment. *See infra* notes 46-54 and accompanying text. It is quite possible that despite the reference to private property, the just compensation clause was also intended to mandate compensation when the federal government appropriated property owned by states and localities. Historical evidence suggests that at least with respect to property owned by localities, the line distinguishing public and private property was blurred throughout the eighteenth century. Localities, even those that did not possess corporate charters, were treated by courts as corporations. *See* O. HANDLIN & M. HANDLIN, *COMMONWEALTH: A STUDY OF THE ROLE OF GOVERNMENT IN THE AMERICAN ECONOMY* 100 (1947); Frug, *The City as a Legal Concept*, 93 HARV. L. REV. 1057, 1098 (1980) [hereinafter Frug, *City as Legal Concept*]. Municipal corporations, such as New York City, were not characterized as "public" corporations because at the time no conceptual dichotomy existed to distinguish public from private corporations. *See* H. HARTOG, *PUBLIC PROPERTY AND PRIVATE POWER* 184-85 (1983); Frug, *supra*, at 1102; Frug, *Property and Power: Hartog on the Legal History of New York City* (Book Review), 1984 AM. B. FOUND. RES. J. 673, 673 [hereinafter Frug, *Property and Power*]. Instead, the eighteenth century American city was a corporation whose "property and governmental rights were blurred and mixed." H. HARTOG, *supra*, at 21. It was not until the nineteenth century that courts developed a uniform system of local government law along with the government/proprietary distinction to separate local government powers and private property into public and private spheres. *See* Frug, *Property and Power*, *supra*, at 676-77 (discussing the legal treatment of New York City); Williams, *The Development of the Public/Private Distinction in American Law* (Book Review), 64 TEX. L. REV. 225, 233 (1985) (discussing the public/private characterization of localities in Massachusetts and certain other New England states).

less, this interpretive difficulty was a matter of little concern to most federal courts. After the *Stockton*³⁴ case was decided, federal courts, without even discussing the omission of public property from the just compensation clause, held that states and localities were entitled to compensation when their property was taken by eminent domain.³⁵ Most courts that noted the seeming incongruity between compensating public condemnees and the text of the just compensation clause avoided the problem by conclusively equating private property with publicly owned property.³⁶

Some courts, however, did attempt to develop rationales for treating publicly owned property in the same manner as property owned by private individuals. For example, in *50 Acres of Land*, Justice Stevens implied that a taking of publicly owned land might harm the citizens who collectively comprise the public entity as much as a taking from each individual separately.³⁷ Because each citizen pays taxes to the public entity and those revenues are used to purchase and maintain its property, a taking by the federal government would burden each private citizen by expropriating his or her share of the collectively held asset.

A more thoughtful, if somewhat obscure, reason for treating state and local property as private property under the just compensation clause was suggested by the Court of Appeals for the First Circuit in

³⁴ *Stockton v. Baltimore & N.Y.R. Co.*, 32 F. 9 (1887).

³⁵ See, e.g., *Carmack*, 329 U.S. at 242 (“[W]hen the Federal Government thus takes for a federal public use the independently held and controlled property of a state or a local subdivision, the Federal Government recognizes its obligation to pay just compensation for it and it is conceded in this case that the Federal Government must pay”); *United States v. Town of Nahant*, 153 F. 520, 521 (1st Cir. 1907) (“[B]ut having thus, under the strong arm of sovereignty, cut through private and municipal right, the rigor of the arm shall be relaxed, and the government itself will see that just compensation is awarded accordingly.”). One reason many courts did not distinguish between privately owned and publicly owned property may be that property owned by a municipality was frequently considered to be held in a “proprietary” capacity. See *Nahant*, 153 F. at 521 (characterizing the taking of a local sewer as a taking of “private or municipal property”); see also *supra* note 33 (line between public and private property blurred in eighteenth century). For a discussion of the public/private distinction with respect to takings of local property by states, see *infra* note 39.

³⁶ See, e.g., *United States v. Wheeler Township*, 66 F.2d 977, 982 (8th Cir. 1933) (“[T]he amendment reads that ‘private property cannot be taken for public use, without just compensation’ . . . yet ‘private,’ as thus used, includes property which is ordinarily regarded as public property. . . .” (emphasis in original)); *Wayne County v. United States*, 53 Ct. Cl. 417, 424 (1918) (“While such [county] property is within most of the definitions of public and not private property, we are of the opinion that for purposes of compensation as for a taking under the Constitution it is properly to be regarded as private property. . . .”), *aff’d*, 252 U.S. 574 (1920).

³⁷ See *50 Acres of Land*, 469 U.S. at 31.

Town of Bedford v. United States.³⁸ In *Bedford*, the United States condemned a portion of a town road for use in building a veterans hospital. The United States claimed that it had no obligation to pay compensation for the road because under Massachusetts law, no compensation would have been required if the property had been expropriated by the Commonwealth.³⁹ In rejecting this argument, the court reasoned that the relationship between the federal government and a state subdivision was qualitatively different from the relationship between a state and one of its own subdivisions. A municipality or town is considered to be a creation of the state and, as such, is subject to the unlimited power of its creator with respect to public property.⁴⁰ The United States, how-

³⁸ 23 F.2d 453 (1st Cir. 1927). The *Bedford* court also justified compensation by adopting a rationale similar to the one used by Justice Stevens in *50 Acres of Land*. See 23 F.2d at 454 (federal condemnations of public facilities increase financial burdens on taxpayers).

³⁹ *Id.* at 453. Because local governments are deemed creatures of the state under most states' laws, see *infra* note 40, states have considerable freedom to take local government property without compensation. Many states' laws make the compensation requirement depend on the government/proprietary distinction. If property is owned and used by a local government in its "public capacity," no compensation would be required in the event of a state condemnation. Property owned or used by local governments in their "private capacity," however, may not be taken without compensation. See *City of Worcester v. Commonwealth*, 345 Mass. 99, 100, 185 N.E.2d 633, 634 (1962); 1 NICHOLS ON EMINENT DOMAIN, *supra* note 1, at § 2.225[1]; see also Dau, *Problems in Condemnation of Property Devoted To Public Use*, 44 TEX. L. REV. 1517, 1527-30 (1966) (discussing when the government/proprietary distinction requires compensation, and when the distinction may be avoided by statutory construction); Payne, *Intergovernmental Condemnation as a Problem in Public Finance*, 61 TEX. L. REV. 949, 955 (1983) (noting that "the distinction requires compensation whenever the public property involved in the taking can be classified as 'proprietary,' while continuing to deny it for 'governmental' property"); Note, *The Sovereign's Duty to Compensate for the Appropriation of Public Property*, 67 COLUM. L. REV. 1083, 1092-98 (1967) (tracing the development and discussing the content of the government/proprietary distinction). Courts and commentators have criticized the government/proprietary distinction as empty. See *Campbell v. State*, 259 Ind. 55, 57-61, 284 N.E.2d 733, 735-36 (1972) (analyzing municipal liability); Frug, *City as Legal Concept*, *supra* note 33, at 1128-41 (public/private distinction has eroded).

⁴⁰ See *Bedford*, 23 F.2d at 456-57. The "creature of the state" characterization of localities is derived from the writings of Judge John F. Dillon. Under Dillon's Rule, local governments possess only those powers expressly given them by the state. Local government powers, therefore, are to be strictly construed. See 1 J. DILLON, *THE LAW OF MUNICIPAL CORPORATIONS* § 55, at 174, § 111, at 154-55 (2d ed. 1873); E. MCQUILLIN, *THE LAW OF MUNICIPAL CORPORATIONS* § 2.08a (3d ed. 1971); see also Williams, *The Constitutional Vulnerability of American Local Government: The Politics of City Status in American Law*, 1986 WIS. L. REV. 83, 88-89 (discussing Dillon's Rule); *Hunter v. City of Pittsburgh*, 207 U.S. 161, 178 (1907) ("Municipal corporations are political subdivisions of the State, created as convenient agencies for exercising such of the governmental powers of the State as may be entrusted to them."). For a critique of the conception of localities as instrumentalities of states, see Neuman, *Territorial Discrimination, Equal Protection, and Self-Determination*, 135 U. PA. L. REV. 261, 304-05 (1987). For a critique of the local powerlessness fostered by Dillon's Rule, see Frug, *City as Legal Concept*, *supra* note 33, at 1067-73, 1109-13.

ever, is a "stranger to the town"⁴¹ and therefore must treat municipal property as it would property owned by private individuals.⁴²

II. JUSTIFYING COMPENSATION FOR PUBLIC CONDEMNNEES

Before determining an appropriate method of compensating public condemnees, one must first consider whether a constitutional rule mandating compensation for intergovernmental takings is necessary. Only occasionally have courts attempted to explain why the federal government must compensate states and localities when it condemns their property, and those explanations have been sketchy at best. In this Part, I examine the most commonly offered rationales for compensating private individuals and entities, and consider whether or not these rationales apply to public condemnees. Two justifications for compensation, preventing an unfair distribution of the burdens of government and minimizing investment risk, do not support a compensation requirement for public condemnees. The remaining two rationales for compensating private condemnees, eliminating the problem of fiscal illusion and protecting liberty, do justify an interpretation of the just compensation clause that would require compensation for intergovernmental takings.

A. *Preventing Unfair Distribution of Burdens of Government*

Courts and commentators have frequently suggested that the just compensation clause was included in the Bill of Rights to prohibit unfair distribution of the costs of government among citizens.⁴³ Although few would argue that the burdens of government actions must be distributed in a precisely equal fashion among all citizens,⁴⁴ there is a

⁴¹ *Bedford*, 23 F.2d at 457.

⁴² Implicit in the "stranger to the town" metaphor are concerns about the proper relationship between the federal government, and states and localities in our federal system. The court's reasoning in *Bedford* may be a reflection of the contemporaneous conception of federal/state relations commonly referred to as dual federalism. Within their respective spheres, the federal government and the states were thought of as sovereign and independent. See *infra* note 176.

⁴³ See, e.g., L. TRIBE, *AMERICAN CONSTITUTIONAL LAW* § 9-6 (2d ed. 1988) (discussing the compensation requirement as an attempt to limit sacrifice by a minority of the population); Michelman, *Property, Utility, and Fairness: Comments On The Ethical Foundations of "Just Compensation" Law*, 80 HARV. L. REV. 1165, 1218-24 (1967) (discussing John Rawls' "justice as fairness" theory).

⁴⁴ Among modern commentators, Professor Epstein comes closest to this absolute view. See R. EPSTEIN, *TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN* 204-09 (1985) (discussing disproportionate impact test). Some commentators have suggested that one purpose of the just compensation clause was to prevent redistribution of wealth. See, e.g., Rose, *Mahon Reconstructed: Why The Takings Issue is*

consensus that the just compensation clause protects against the sacrifice of the few to the many.⁴⁵ In this section, I summarize the historical argument that the just compensation clause was included in the fifth amendment to prevent unfair burdens, and examine the extent to which federal courts have adopted this rationale. I argue that if the objective of the just compensation requirement is prevention of unfair burdens, a court computing compensation ideally should compensate only *actual* burdens, by reducing the amount paid to a condemnee by the amount she benefits from the project for which her property was condemned. Empirical evidence demonstrates that most intergovernmental takings generate significant benefits for the states and localities whose property is condemned. The existence of such benefits makes the case for compensating public entities much weaker than the case for compensating private property owners.

1. Preventing Unfair Burdens: History and Precedent

Although comparatively little is known regarding the origins of the just compensation clause, historical evidence supports the view that one of the purposes of the compensation requirement was to protect citizens from unequal treatment. The sixteenth and seventeenth century natural law theorists, whose views concerning eminent domain are thought to have influenced the Framers, wrote that when government exercises its power of eminent domain it should compensate the condemnee.⁴⁶ According to Pufendorf, compensation was appropriate because the property "seized and applied to public purposes . . . exceeds the proportion which he [the condemnee] was bound to contribute to the state."⁴⁷ At

Still a Muddle, 57 S. CAL. L. REV. 561, 583-87 (1984) (arguing that one purpose of just compensation clause was to avoid redistribution). Cf. C. BEARD, AN ECONOMIC INTERPRETATION OF THE CONSTITUTION OF THE UNITED STATES 176 (1913) ("None of the powers conferred by the Constitution on Congress permits a direct attack on property."). But see Sax, *Takings and the Police Power*, 74 YALE L.J. 36, 58-67 (1964) (purpose of just compensation clause was protection of liberty, not maintenance of wealth).

⁴⁵ See E. PAUL, *supra* note 11, at 75 (approving of an interpretation of the just compensation clause that would prohibit anyone from being compelled to pay more than his or her "fair share" of public improvements); L. TRIBE, *supra* note 43, at § 9-6, ("the just compensation requirement appears to express a limit on government's power to isolate particular individuals for sacrifice to the general good"). But cf. Merrill, *Rent Seeking and the Compensation Principle*, 80 NW. L. REV. 1561, 1579-80 (1986) (criticizing the equal sharing rationale) [hereinafter Merrill, *Rent Seeking*].

⁴⁶ See, e.g., H. GROTIUS, *supra* note 13, at 807 (bk. III, ch. XX) (when exercising the right of eminent domain "the state is bound to make good . . . the damage to those who lose their property"); 2 S. PUFENDORF, DE OFFICIO HOMINES ET CIVIS JUXTA LEGEM NATURALEM 136 (F. Moore trans. 1927) (expressing the same principle).

⁴⁷ S. PUFENDORF, *supra* note 46, at 136.

the time of the American Revolution, English statutes typically provided for compensation when the government expropriated land,⁴⁸ despite the absence of such a requirement in the Magna Carta.⁴⁹ Blackstone wrote that individuals were entitled to compensation: Parliament must not act "by absolutely stripping the subject of his property in an arbitrary manner; but by giving him a full indemnification and equivalent for the injury thereby sustained."⁵⁰

Prior to independence, colonial governments regularly paid compensation to citizens whose property was condemned.⁵¹ By the time the Constitution was ratified, two states had included compensation clauses in their constitutions.⁵² Nevertheless, no state requested inclusion of a takings provision in the Constitution or Bill of Rights.⁵³ Despite the apparent lack of interest among the states in a federal compensation requirement, James Madison included the just compensation clause in the fifth amendment. Madison's writings indicate that he was concerned with the prospect that the government might inflict unfair burdens upon individuals or groups of citizens.⁵⁴

⁴⁸ See E. PAUL, *supra* note 11, at 72 ("By tradition . . . land could be taken only by a parliamentary act accompanied by the payment of compensation."); Stoebuck, *A General Theory*, *supra* note 12, at 579 ("Throughout the seventeenth and eighteenth centuries compensation became a regular feature of English parliamentary acts.").

⁴⁹ The Magna Carta provides that "No free man shall be . . . disseised . . . except by the lawful judgement of his peers or by the law of the land." MAGNA CARTA art. 39.

⁵⁰ See 1 W. BLACKSTONE, COMMENTARIES *139. Blackstone's writings were very influential in the United States at the time the Constitution and Bill of Rights were adopted. See L. FRIEDMAN, A HISTORY OF AMERICAN LAW 112 (2d ed. 1985) (noting the "ubiquity of Blackstone"); G. WOOD, THE CREATION OF THE AMERICAN REPUBLIC 14 (1969) (same). Blackstone argued that while "the good of the individual ought to yield to that of the community . . . it would be dangerous to allow any private Man, or even any public tribunal, to be the judge of this common good, and to decide whether it be expedient or no." W. BLACKSTONE, *supra*, at *139. For a discussion of the dangers to liberty that might result from uncompensated takings, see *infra* notes 128-41 and accompanying text.

⁵¹ See F. BOSSELMAN, *supra* note 11, at 85 (colonial governments usually paid compensation for developed land); Stoebuck, *A General Theory*, *supra* note 12, at 579-83 (compensation paid for developed or enclosed land).

⁵² See F. BOSSELMAN, *supra* note 11, at 94-97 (discussing compensation clauses in the Vermont and Massachusetts constitutions); Grant, *The "Higher Law" Background of the Law of Eminent Domain*, 6 WIS. L. REV. 67, 70 (1931) (same).

⁵³ See F. BOSSELMAN, *supra* note 11, at 98; E. DUMBAULD, THE BILL OF RIGHTS AND WHAT IT MEANS TODAY 162, 173-205 (1st ed. 1957); McConnell, *Contract Rights and Property Rights: A Case Study in the Relationship Between Individual Liberties and Constitutional Structure*, 76 CALIF. L. REV. 267, 282-88 (1988).

⁵⁴ See *Property*, Nat'l Gazette, Mar. 27, 1792, in 14 J. MADISON, THE PAPERS OF JAMES MADISON 266, 267 (R. Rutland & T. Mason eds. 1983) (criticizing unequal taxation of property). Madison may have been primarily concerned with the potential inroads to personal liberty that absence of a compensation requirement would have made possible. See *id.* at 266-68; Note, *Origins and Significance*, *supra* note 12, at 708-13 (discussing Madison's liberalism as reflected in the fifth amendment). See also

Courts have applied the just compensation clause with the rhetoric, if not always the spirit,⁵⁵ of preventing unfair burdens. According to one commonly cited maxim, the just compensation requirement is designed to prevent "the public from loading upon one individual more than his just share of the burdens of government. . . ."⁵⁶ In practice, however, courts have been criticized for not requiring compensation in circumstances where government regulation imposes significant burdens, and for undercompensating condemnees in instances where a taking is found to have occurred.⁵⁷

2. Burdens and Benefits

Under current federal law, condemnees are entitled to receive as compensation the fair market value of the property condemned. Nevertheless, if the objective of the just compensation requirement is to prevent an unfair distribution of the burdens created by government action, particular attention should be given to *actual*, rather than nominal burdens borne by condemnees. If the federal project for which property is taken benefits the condemnee, the actual burden to the individual condemnee would be equal to the value of the property condemned, minus the benefits that accrue to the condemnee from the government action. In effect, such a compensation rule⁵⁸ would require

infra notes 134-37 and accompanying text (discussing the role of property in preserving individual liberty).

⁵⁵ In practice, federal courts permit property owners to bear significant losses resulting from government regulation without requiring compensation. *See, e.g., Penn Cent. Transp. Co. v. New York City*, 438 U.S. 104, 138 (local action prohibiting owner of historic structure from building a tower is not a compensable taking); *Hadacheck v. Sebastian*, 239 U.S. 394, 405, 413-14 (1928) (local law requiring abandonment of brick making which reduced value of property from \$800,000 to \$60,000 is not a compensable taking). For thoughtful analyses of current takings jurisprudence, see generally, B. ACKERMAN, *PRIVATE PROPERTY AND THE CONSTITUTION* (1977); R. EPSTEIN, *supra* note 44; Costonis, *Presumptive and Per Se Takings: A Decisional Model for the Taking Issue*, 58 N.Y.U. L. REV. 465 (1983); Michelman, *supra* note 43; Rose, *supra* note 44; Sax, *supra* note 44; Sax, *Takings, Private Property and Public Rights*, 81 YALE L. REV. 149 (1971).

⁵⁶ *Monongahela Navigation Co. v. United States*, 148 U.S. 312, 325 (1893). *See also Nollan v. California Coastal Comm'n*, 107 S. Ct. 3141, 3147 n. 4 (1987) ("One of the principal purposes of the Takings Clause is '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.'") (quoting *Armstrong v. United States*, 364 U.S. 40, 49 (1960) and citing *Penn Cent. Transp. Co.*, 438 U.S. at 123).

⁵⁷ *See supra* note 55 (regulatory takings), and *infra* notes 250-53 and accompanying text (condemnations).

⁵⁸ Obviously, requiring such a calculation on a case-by-case basis for private, as well as public condemnees, might be difficult, time-consuming and expensive. Because benefits to individual private condemnees from projects requiring takings are liable to be small in magnitude, *see infra* note 69 and accompanying text, and the transaction

courts to offset against the nominal value of the property taken, the "implicit in-kind benefits" received by the condemnee.⁵⁹

The proposition that compensation might not be necessary if the individual who suffers the burden of condemnation receives implicit in-kind benefits from the project or policy that created the loss, is not unprecedented in the law. In *Pennsylvania Coal Co. v. Mahon*,⁶⁰ the Supreme Court held that a state law that prohibited the mining of anthracite coal in such a way as to cause subsidence constituted a compensable taking of property under the just compensation clause.⁶¹ In his decision, Justice Holmes distinguished an earlier Supreme Court decision, *Plymouth Coal Co. v. Pennsylvania*,⁶² that had upheld a statute requiring mining companies to leave pillars of coal underground so as to protect miners in adjoining mines. Justice Holmes argued that the statute challenged in *Plymouth Coal* did not constitute a taking because it "secured an average reciprocity of advantage."⁶³ Although the statute at issue in *Plymouth Coal* created a burden for mine owners by requiring them to leave pillars of coal underground, compensation was not

costs of calculating in-kind benefits large, it might be more cost-effective for the condemnor to compensate nominal, rather than actual burdens. Therefore, practical considerations of convenience and efficiency may justify basing compensation for private condemnees on nominal, rather than actual burdens. Cf. Michelman, *supra* note 43, at 1215 (no compensation should be paid if settlement costs exceed the "demoralization costs" that would be created by an uncompensated taking). Nevertheless, if the purpose of the just compensation clause is to prevent disproportionate or unfair burdens, the "ideal" compensation rule (absent transaction and administrative costs) would be indemnification for actual burdens only.

⁵⁹ See R. EPSTEIN, *supra* note 44, at 195-215 (arguing that certain takings might not require compensation if implicit in-kind benefits are taken into account); cf. Hagman, *Windfalls for Wipeouts*, in *WINDFALLS FOR WIPEOUTS: LAND VALUE CAPTURE AND COMPENSATION* 20, 20-27 (D. Hagman & D. Mischynski, eds. 1978) (advocating recapture of windfalls created by government action and compensation for government-induced wipeouts).

⁶⁰ 260 U.S. 393 (1922).

⁶¹ *Pennsylvania Coal* was the first Supreme Court case to hold that a government regulation could constitute a taking of property under the just compensation clause. In *Pennsylvania Coal*, Justice Holmes set forth a test to determine when a regulation becomes a taking, a test which has puzzled generations of jurists, attorneys, and property owners: "The general rule, at least, is that while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking." 260 U.S. at 415. Scholars have expended much time and energy analyzing *Pennsylvania Coal* and its "general rule." See, e.g., B. ACKERMAN, *supra* note 55, at 156-167 (1977) (characterizing the opinion as "the most important and most mysterious writing in takings law"); Bender, *The Takings Clause: Principles or Politics?*, 34 *BUFFALO L. REV.* 735, 770-776 (1985) (there is "no justification [for the test] except [Justice Holmes'] overwhelming desire to shape the takings jurisprudence"); Rose, *supra* note 44, at 562 (identifying the "general rule" as the original source of the confusion in takings analysis).

⁶² 232 U.S. 531 (1914).

⁶³ 260 U.S. at 415.

required because those same owners would receive in-kind benefits from identical restrictions placed upon other mine owners. Apparently Justice Holmes felt compensation was required in *Pennsylvania Coal*, in part, because the mine owners did not receive similar in-kind benefits from the state law prohibiting subsidence.⁶⁴

Many non-compensable public regulations of land use have also been justified, at least in part, on the ground that they generate in-kind benefits. For example, in *Agins v. City of Tiburon*,⁶⁵ the Supreme Court considered the validity of a zoning ordinance that limited to five the maximum number of single family residences that could be built on a particular parcel of land. The Court stated in *dicta* that the zoning restriction did not constitute a taking,⁶⁶ noting that the ordinance benefited the restricted landowner, as well as the public, by promoting orderly development. According to the Court, "[a]ppellants therefore will share with other owners the benefits and burdens of the city's exercise of its police power. In assessing the fairness of zoning ordinances, these benefits must be considered along with any diminution in market value that the appellants might suffer."⁶⁷

Courts have not limited the practice of offsetting benefits or in-kind compensation to the burdens imposed by government regulation.

⁶⁴ See Rose, *supra* note 44, at 582.

⁶⁵ 447 U.S. 255 (1980).

⁶⁶ The Court's discussion of the zoning ordinance's applicability to *Agins*'s property was *dicta* because *Agins* had not, at the time of the litigation, submitted a plan to develop the property and therefore, no concrete controversy regarding application of the ordinance existed. See *id.* at 260.

⁶⁷ *Id.* at 262. See also *Keystone Bituminous Coal Ass'n v. DeBenedictis*, 480 U.S. 470, 491 (1987) (while each person is burdened by the restriction, they also benefit from the restriction); *Penn Cent. Transp. Co. v. New York*, 438 U.S. 104, 147-50 (1978) (Rehnquist, J., dissenting) (same). In *Penn Central*, the Supreme Court held that an historic preservation ordinance which limited the ability of owners of designated buildings to make structural alterations was not a taking. Both the majority and the dissenting opinions made use of the concept of offsetting benefits. Justice Brennan's majority opinion noted that although the New York City ordinance might prohibit the appellant from building a tower over Grand Central Station, the owner was not denied all use of its air rights. Under the law, the owner of a property designated as historic was permitted to transfer his or her "air rights" to nearby locations. The Court admitted that the transferable development rights might not constitute just compensation if a taking had occurred, but that they "undoubtedly mitigate whatever financial burdens the law has imposed on appellants and, for that reason, are to be taken into account in considering the impact of regulation." 438 U.S. at 137. In his dissent, Justice Rehnquist argued that what distinguishes historic preservation ordinances from other land use regulations, such as zoning, is that they fail to provide reciprocal benefits. With a zoning ordinance "any such abstract decrease in value will more than likely be at least partially offset by an increase in value which flows from similar restrictions as to use on neighboring properties . . ." 438 U.S. at 139-40 (Rehnquist, J., dissenting). For landmarked buildings, on the other hand, "a relatively few individual buildings, all separated from one another, are singled out and treated differently from surrounding buildings [so] no such reciprocity exists." *Id.*

When a portion of a tract of land is condemned by the federal government and the remaining land is increased in value as a result of the government action, courts will frequently require that the compensation paid to the landowner for the portion taken be decreased by the value of the benefit to the remainder.⁶⁸

3. Prevention of Unfair Burdens as a Rationale for Compensating Intergovernmental Condemnees

Historical evidence indicates that the just compensation clause was included in the fifth amendment, at least in part, to prevent individual property owners from bearing unfair burdens. To achieve this purpose, a property owner ideally should be compensated only for her *actual* burdens. Benefits generated by the project for which the owner's property was condemned should be offset against the value of the property taken. In this section, I argue that although compensation for private property owners is usually justified as necessary to prevent unfair burdens, the same rationale cannot be applied to public condemnees: Intergovernmental takings typically do not create actual burdens for state and local governments, unfair or otherwise.

When property is taken from a private individual for a public project, that individual suffers a concentrated loss, but is likely to be the recipient of only a small proportion of a widely dispersed benefit. The benefit, which might be considerable for the entire population of the locality or state, is unlikely to be large enough at the individual level to offset the burden created by the condemnation.⁶⁹ On the other hand, if a locality or a state is regarded as a surrogate for its residents, a taking of local or state property is likely to inflict a concentrated loss which is

⁶⁸ A court will not require benefits to be offset against the value of the property unless they are "special" rather than "general". See *Bauman v. Ross*, 167 U.S. 548, 574-75 (1897). The exact nature of a special benefit is somewhat unclear. One leading commentator on the question of whether benefits can be offset against compensation has noted that "[u]pon this subject there is a great diversity of opinion and more rules, different from and inconsistent with each other, have been laid down than upon any other point in the law of eminent domain." 3 NICHOLS ON EMINENT DOMAIN, *supra* note 1, at § 8.62. A special benefit is generally one that arises "from the peculiar relation of the land in question to the public improvement" whereas a general benefit arises "from the fulfillment of the public object which justified the taking." *Id.* at § 8.6203. If the benefit is one shared in common with the entire community it is likely that it will be classified as general rather than special and therefore its value will not be offset against the amount of compensation owed a condemnee.

⁶⁹ To quote Justice Holmes, at the individual level there does not exist for most condemnations an "average reciprocity of advantage" sufficient to make compensation unnecessary. *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922); see *supra* notes 60-64 and accompanying text.

offset by a corresponding concentrated benefit.⁷⁰ While the state or locality is presumably burdened by losing the use of its property, a large proportion of the benefits generated by the federal project are concentrated in the same state or locality. In effect, whereas the actual burden from uncompensated takings would usually be great for private individuals, it is likely to be non-existent or small for public entities.⁷¹

Empirical evidence supports the view that intergovernmental takings typically generate significant benefits for the locality or state which

⁷⁰ There might be instances in which the condemned public property benefitted one group of citizens whereas the federal project for which the condemnation occurred benefits a distinctly different segment of the population, thereby inflicting actual burdens on some residents. I contend, however, that it is inappropriate to assess the existence of actual burdens resulting from intergovernmental takings at the level of each resident. In most cases, individual residents of states and localities have no entitlement to benefits generated by particular parcels of publicly owned property. To the contrary, states and localities frequently change the use of public property, despite the fact that some segments of the population will benefit from the change at the expense of others. Because public property is held in trust for all residents, collective benefits and burdens are the appropriate indicator for determining whether an intergovernmental taking imposes actual burdens. Nevertheless, the fact that the federal government, rather than the state or local property owner, makes the allocative decision, raises questions regarding the appropriate relationship among the federal government and the states and localities in the American federal system. See *infra* text accompanying notes 202-38.

⁷¹ *City of Van Buren v. United States*, 697 F.2d 1058 (Fed. Cir. 1983), is one case in which a court dealt with the issue of whether benefits to a state or locality should be offset against burdens in determining whether there exists a federal obligation to compensate for an intergovernmental taking. The federal government argued that damage to Van Buren's sewer lines caused by a federal dam project did not constitute a compensable taking because substantial benefits to the municipality generated by the dam "clearly outweigh[ed] the detriments . . ." *Id.* at 1061. The court rejected the government's argument on two grounds. First, the court argued that nothing in the record supported the government's contention that the damages sustained by the city were "de minimis" compared to the benefits generated by the federal project. See *id.* at 1062. Second, the court held that only special benefits could be offset against compensation otherwise due to a condemnee and the benefits generated by the dam project were general rather than special. See *id.*

The *Van Buren* court, like many courts considering intergovernmental taking cases, see *supra* notes 35-36, borrowed rules from private condemnation cases without considering whether those rules make sense in the context of a taking of public property. The reason most commonly given for refusing to offset general benefits (benefits that the entire community shares) against the value of property condemned is that "the owner whose land is taken is placed in a worse position than his neighbor whose estate lies outside the path of the improvement and who shares in the increased values without any pecuniary loss." 3 NICHOLS ON EMINENT DOMAIN, *supra* note 1, at § 8.6205. The argument that offsetting general benefits against compensation owed to private condemnees would be inequitable may have some merit. But see Haar & Hering, *The Determination of Benefits in Land Acquisition*, 51 CALIF. L. REV. 833, 874 (1963) (arguing that as long as a property owner receives full value for what she gives up she has no right to complain about better bargain of neighbor). However, this argument simply is not applicable to situations in which public land is condemned. Because the entire community bears the cost of the taking as well as enjoys the general benefits of the federal project (by definition), no inequity results from offsetting general as well as special benefits.

formerly owned the condemned property. Benefits attributable to federal programs may be categorized as "general," "local," or "group".⁷² A general benefit is a collective good that accrues to all citizens in relatively equal shares. Examples of general benefits include national security, and research and development. A local benefit is one that is primarily confined to a particular geographic area, whether it be a locality, state or region. Local benefits include increased employment of local residents, and the economic growth and prosperity generated by federal projects and public improvements.⁷³ A group benefit typically affects the interests of readily identifiable groups of citizens who, in many instances, may be dispersed throughout the United States.⁷⁴ Examples of group benefits include tax preferences for certain industries, and subsidies earmarked for particular demographic groups. A government program need not, and usually does not generate only one type of benefit.⁷⁵ Military projects, for example, usually create all three types of benefits. All citizens of the United States benefit from increased national security;⁷⁶ the economy of the locality or state in which the installation is located benefits from increased employment and economic stimulus;⁷⁷ and certain manufacturers of military technology and hard-

⁷² See Arnold, *The Local Roots of Domestic Policy*, in *THE NEW CONGRESS* 250, 253 (T. Mann & N. Ornstein eds. 1981).

⁷³ The distinction between general and local benefits is not an analogue of the government/proprietary distinction. Characterizing a program or policy as generating predominantly local benefits does not imply that the benefits are any less "public" than a program which generates mostly general benefits. The characterization of benefits as predominantly local merely means that they are concentrated on a group of citizens, most of whom reside in close proximity, rather than being proportionately dispersed throughout the nation. Most federal programs and policies will generate general, local, and group benefits. Although it may be difficult in some cases to determine whether the benefits generated by a particular program or policy are predominantly general or local, determining the incidence of benefits should be considerably easier and more meaningful than divining whether a particular government initiative generates private or public benefits.

⁷⁴ See Arnold, *supra* note 72, at 253.

⁷⁵ Cf. Frug, *Empowering Cities in a Federal System*, 19 *URB. LAW.* 553, 556 (1987) (virtually all public policy issues involve potential national, state, and city interests).

⁷⁶ This assumes, of course, that increased military spending yields some corresponding increase in the level of national security. See, e.g., A. GREGOR & M. CHANG, *THE IRON TRIANGLE* 116 (1984) (pointing out that the United States' investment in nuclear superiority did little to deter Soviet aggression in Africa, the Caribbean, and Asia).

⁷⁷ See R. ARNOLD, *CONGRESS AND THE BUREAUCRACY* 95 (1979) ("The principal military benefit sought by congressmen is assumed to be military employment. Such employment, even at a small installation, can pump millions of federal dollars into a local economy every year."). That military installations generate enormous local benefits can be seen from observing efforts by Congressmen to influence the Department of Defense to open facilities in their districts and to forestall efforts to close existing installations. See, e.g., *id.* at 114 (bureaucrats take into account committee members' prefer-

ware earn profits supplying necessary equipment.

An analysis of all federal condemnations since 1980⁷⁸ confirms the hypothesis that the projects for which public property has been condemned generate predominantly local benefits. Of 146 federal ventures which involved intergovernmental takings, the largest proportion by far, forty-five percent, were harbor, reservoir, and flood control projects. Federal water projects are generally considered to be the prototypical local benefit program.⁷⁹ Although some of these projects generate general benefits, most commentators suggest that their popularity stems from concentrated local benefits such as economic development and employment.⁸⁰ Most of the remaining intergovernmental takings during the 1980's involved undertakings which also generate substantial local benefits.⁸¹

Where there is a condemnation of public property for a federal project, it is possible that the ensuing benefits to the state or locality may not fully offset the burdens created by the takings.⁸² Nevertheless,

ences when deciding which military installations to close).

⁷⁸ The Land Acquisition Section of the United States Department of Justice is charged with the duty of coordinating the filing of condemnation actions for the United States government. The Land Acquisition Section maintains computerized records of all federal condemnations since 1980. A computer-generated list of all condemnations was examined on June 6, 1988. Information contained on the list for each condemned "tract" included the name of each condemnee, the federal district court in which each condemnation action was filed, and the name of the project for which the condemnation occurred. Because the amount of acreage contained in a "tract" varies from jurisdiction to jurisdiction, one cannot determine from this listing the amount of land condemned for each project. See Interview with William Kollins and Brenda Rossi, Land Acquisition Section, Department of Justice (Washington, D.C. March 11, 1988); see also Telephone interview with Brenda Rossi, Land Acquisition Section, Department of Justice (Washington, D.C. October 3, 1988) (same).

I classified a condemnation as intergovernmental if the condemnee was listed in the records of the Land Acquisition Section as a state or locality. Of 1,570 projects for which property was condemned since 1980, 146 projects, or 9% involved intergovernmental takings. See *id.*

⁷⁹ See Arnold, *supra* note 72, at 280.

⁸⁰ Each year, members of Congress propose and enact programs of questionable utility to straighten or elongate rivers, erect dams, and dredge waterways. See, e.g., J. FERREJOHN, PORK BARREL POLITICS 51-53 (1974) (analyzing the "pork barrel politics" that leads to enactment of river and harbor legislation).

⁸¹ Examination of the computerized records from the Land Acquisition Section, see *supra* note 78, reveals that 8 percent of federal condemnations of state and local properties provided land for federal facilities serving local communities such as post offices and hospitals; a similar proportion of condemnations amassed land for parks and wildlife preserves. A significant share of intergovernmental condemnations, 20 percent, were undertaken to appropriate land for military uses such as bases, proving grounds and storage depots. The remaining projects for which public property was condemned included roads, federal border facilities, air navigation monitoring posts, and the strategic petroleum reserve.

⁸² This result may occur as a result of intergovernmental takings that generate predominantly general benefits. See *supra* note 72 and accompanying text. In addition,

even in the instances where burdens are not completely offset by benefits, the actual burdens borne by intergovernmental condemnees are likely to be much less than those borne by private condemnees. Therefore, if the compensation requirement contained in the fifth amendment is justified on the ground of preventing unfair burdens, this justification, while possibly not irrelevant, is nonetheless much less persuasive in explaining why public condemnees should be entitled to compensation.⁸³

B. *Minimizing Investment Risk*

Paying compensation to condemnees has been justified on the ground that it contributes to economic efficiency by minimizing the risk of capital investment. Although this rationale may support a compensation requirement with respect to condemnations of private property, it does not apply with equal force to intergovernmental takings. Even if one were to assume that public entities invest efficiently in capital, states and localities have opportunities to minimize the risk created by uncompensated condemnations that are unavailable to most property owners in the private sector.

1. Compensation, Risk Minimization, and the Private Condemnee

If no compensation requirement existed, the possibility that the federal government might expropriate one's property would increase the risk⁸⁴ of capital investment. Risk and uncertainty are generally considered to be undesirable because they may lead to economic ineffi-

local benefits may not offset burdens if intergovernmental takings were utilized by groups of states to exploit other states. *See infra* notes 202-38 and accompanying text.

⁸³ In addition to preventing overcompensation, eliminating compensation for public condemnees might have the salutary effect of reducing the number of inefficient federal projects. Several commentators have noted the tendency of the federal government to sponsor "pork barrel" projects that generate substantial local benefits, but whose costs exceed total benefits. *See supra* notes 79-80; *cf. infra* note 212 and accompanying text. One of the major reasons for the existence of pork barrel projects is that members of Congress believe that sponsoring projects that generate significant localized benefits, but whose costs are dispersed throughout the nation, will assist them in maintaining and expanding their electoral support. With respect to projects that generate predominantly local benefits, eliminating compensation for takings of public property would raise the costs to the communities deriving concentrated benefits, perhaps inducing their representatives in Congress to demand a more efficient mix of public projects. *But see infra* text accompanying notes 114-19 (if compensation is not paid, fiscal illusion might lead to an inefficiently large number of projects).

⁸⁴ "Risk" may be defined as "the variation in the possible outcomes that exists in a given situation." C. WILLIAMS & R. HEINS, *RISK MANAGEMENT AND INSURANCE* 7 (3d ed. 1976). A person's conscious awareness of risk is sometimes called "uncertainty." *Id.* at 8.

ciency.⁸⁵ A profit-maximizing individual's investment decisions are likely to be efficient, provided that they are based upon an accurate perception of the investment's expected value.⁸⁶ If an individual were unaffected by the presence of risk, and had perfect information, her perception of the value of an investment should equal its expected value. Such a hypothetical person is said to be "risk neutral."⁸⁷ Most commentators, however, do not believe that the majority of people are indifferent to risk; rather, the majority are said to be "risk averse".⁸⁸ Therefore, risk, such as the possibility of an uncompensated taking by the federal government, may lead to economic inefficiency if risk averse investors avoid high risk activities with positive expected values, preferring safer, yet perhaps less productive investments.⁸⁹

Compensation can be justified as a method for reducing the risk of government action to an individual by spreading risk among all taxpayers. By reducing risk for the individual, compensation presumably promotes efficiency.⁹⁰ Thus, for example, an individual property owner,

⁸⁵ See *id.* at 15.

⁸⁶ To determine the expected value of an investment, one must multiply the possible yield from each aspect of the investment by the probability the yield will be received and then add the resulting products. See A. POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 27 (1983) ("the expected gain from a situation involving a 50 percent chance of winning \$10,000 is \$5,000.").

⁸⁷ A risk neutral person is indifferent to risk and cares only about the expected value of a particular venture. See *id.* ("A risk-neutral person would, by definition, be indifferent between [situations] with the same expected gain — such as a situation involving a 25 percent chance of winning \$20,000, or one involving certainty of winning \$5,000.").

⁸⁸ When faced with a choice between two investments which are expected to yield similar expected values, a risk averse individual will usually invest in the one with lower risk or alternatively, require a purchase price reduction to invest in the one with higher risk. See Blume & Rubinfeld, *Compensation For Takings: An Economic Analysis*, 72 CALIF. L. REV. 569, 585 (1984).

The proposition that most people are risk averse is illustrated by the fact that many people buy liability insurance, and that most investors demand a greater return on riskier investments. See Kaplow, *An Economic Analysis of Legal Transitions*, 99 HARV. L. REV. 511, 527 n.47 (1986). Such risk averse behavior can be explained as resulting from the decreasing marginal utility of income: the greater the yield, the less people value the extra income, whereas the greater the loss, the more value lost per decrease in income. See *id.*; see also C. WILLIAMS & R. HEINS, *supra* note 84, at 14 (providing a graphic illustration of this concept).

⁸⁹ See Blume and Rubinfeld, *supra* note 88, at 590; Fischel & Shapiro, *Takings, Insurance, and Michelman: Comments on Economic Interpretations of "Just Compensation" Law*, 17 J. LEGAL STUD. 269, 269 (1988); Kaplow, *supra* note 88, at 527-29; Knetsch & Borcharding, *Expropriation of Private Property and the Basis For Compensation*, 29 U. TORONTO L.J. 237, 243 (1979). As Knetsch and Borcharding suggest, "a failure to pay full compensation . . . may encourage risk-averse owners to hedge against what to them are fortuitous expropriation events by under-investing in improvements to their property." *Id.* Cf. Michelman, *supra* note 43, at 1214-15 (discussing demoralization costs that would occur from uncompensated taking).

⁹⁰ See Blume & Rubinfeld, *supra* note 88, at 590-592; Fischel & Shapiro, *supra*

guaranteed that her property interest will be compensated should the government require it for its own purposes, would not be dissuaded from investing in productive activities on account of the risk of government action.⁹¹

In recent years, several economists and lawyers have argued that the risk minimization rationale for compensation is overly simplistic and that compensating condemnees might not necessarily further the objective of efficiency. Their critique of compensation proceeds from the premise that an efficient level of investment occurs only when investors bear the costs of their decisions. The problem is that the government's assurance that it will compensate property owners when it takes land by eminent domain, eliminates, for the most part, the need for the investor to consider the risk of government action. Rather than leading to an efficient level of capital investment, the assurance of compensation may create an incentive for individuals to over-invest in property because they are not forced to internalize⁹² all of the expected costs of the venture.⁹³

note 89, at 269; Kaplow, *supra* note 88, at 528. Blume, Rubinfeld, and Shapiro discuss the argument that "[s]ince private insurance against the risk of a taking is not generally available, compensation in the case of taking can increase efficiency in a world of risk-averse investors." Blume, Rubinfeld & Shapiro, *The Taking Of Land: When Should Compensation Be Paid?* 99 Q.J. ECON. 71, 72 (1984). Nevertheless, each of the above-cited authors also critiques compensation for leading to other inefficiencies. See, e.g., *id.* at 90 (discussing inefficiencies that result when parties are not required to internalize all costs of a venture); Fischel & Shapiro, *supra*, at 271-77 (same); Kaplow, *supra*, at 529, 531 (same).

⁹¹ Madison's inclusion of the just compensation clause in the Bill of Rights may also reflect concerns of economic efficiency. Madison viewed protection of property rights as essential to productive investment. In an 1821 comment written on a draft of his speech before the Constitutional Convention of 1787, Madison argued that "[i]n civilized communities, property as well as liberty is an essential object of the laws, which encourage industry by securing the enjoyment of its fruits . . ." *Documentary History of the Constitution*, in DEPARTMENT OF STATE, BULLETIN OF THE BUREAU OF ROLLS AND LIBRARY, No. 11, pt. 2, at 440, 441 (1905); see also M. MEYERS, *THE MIND OF THE FOUNDER* 503 (1973) (quoting and analyzing Madison's 1821 comment concerning his address to the Constitutional Convention on August 7, 1787); see also Rose, *supra* note 44, at 586-87 (Madison believed that uncertainty created by redistributions of property would create turmoil for wealth-producing enterprise.).

⁹² An activity of one person which affects the welfare of another in a way that is outside the market is called an externality. See H. ROSEN, *PUBLIC FINANCE* 53 (2d ed. 1988). A person who is forced to take account of an externality is said to "internalize" the externality. See, e.g., Kaplow, *supra* note 88, at 540 ("the insurance premium internalizes this externality").

A basic principle of welfare economics is that markets may fail to allocate resources efficiently if individuals who create costs or benefits are not held accountable by the market for those costs or benefits. See H. ROSEN, *supra*, at 52 (discussing externalities as one of the standard causes of market failure). In the case of compensated takings, the risk from government action is external to the property owner and spread throughout the taxpaying public. See *supra* text accompanying note 90.

⁹³ See R. COOTER & T. ULEN, *supra* note 19, at 200; Blume, Rubinfeld and

In a recent article, Kaplow suggests that the optimal balance between risk and incentives might be reached by private market alternatives to government compensation, such as diversification and insurance.⁹⁴ Diversification typically involves investing in a number of unrelated assets, in effect reducing the magnitude of loss from an uncertain event.⁹⁵ If a person with a diversified portfolio of investments were to suffer a condemnation, only a small proportion of her total wealth would likely be affected. Unfortunately for most property owners, diversification is impractical because they lack sufficient wealth to invest in the number of assets required for proper risk reduction.⁹⁶

Insurance, on the other hand, is a widely used risk minimization strategy.⁹⁷ Kaplow argues that insurance can serve the same risk minimization function as government compensation.⁹⁸ Moreover, because the insurance premium includes a payment equal to the expected loss from condemnation, insurance would force property owners to internalize the costs associated with potential government condemnations,

Shapiro, *supra* note 90, at 90; Fischel & Shapiro, *supra* note 89, at 277; Kaplow, *supra* note 88, at 529, 531.

⁹⁴ See Kaplow, *supra* note 88, at 527-42.

⁹⁵ See J. VAN HORNE, FINANCIAL MANAGEMENT AND POLICY 50 (4th ed. 1977) (Risk exposure is reduced to the degree that assets exhibit less than a perfect positive correlation among their expected earnings.). To the extent that unrelated assets have a small probability of a perfect positive correlation, such a diversification reduces risk. See *id.* A property owner might diversify his or her risk of condemnation by investing in different types of property (e.g. tangible and intangible) or in similar types of properties that are geographically dispersed.

⁹⁶ See Blume & Rubinfeld, *supra* note 88, at 591-92 ("When a homeowner purchases a parcel of land, the investment in the land and structure often represents a substantial portion of that individual's net worth.").

⁹⁷ See Kaplow, *supra* note 88, at 527-28. Insurance is a device which entails pooling the risks of two or more persons. Each insured party contributes to a fund out of which losses are indemnified. See C. WILLIAMS & R. HEINS, *supra* note 84, at 200. In essence, the insured party exchanges the risk of loss in the future for a certain present cost, typically in the form of an insurance premium. R. POSNER, *supra* note 19, at 91. In most instances, an insurance premium will exceed the expected loss of the casualty. It will include charges to cover the insurer's expenses and profit. See C. WILLIAMS & R. HEINS, *supra*, at 492. In addition, it will usually be based upon the average probability of loss rather than individual probabilities. See R. POSNER, *supra*, at 91-92; Kaplow, *supra* note 88, at 543 (Insurance companies approximate individual premiums by "averaging risk factors over groups that cannot be more precisely differentiated without significant cost.").

⁹⁸ Compensation functions like insurance in many ways with respect to risk-bearing. The risk to the individual property owner of a condemnation is spread throughout the taxpaying public. See *supra* text accompanying note 90. A major difference between compensation and insurance is that for compensation, there is no necessary correlation between the amount of taxes paid by a citizen and the expected loss to that citizen from condemnation. With regard to insurance, however, the insured's premium includes a payment which is approximately equal to the expected loss from the event insured against.

thereby safeguarding against over-investment.⁹⁹

Although private sector alternatives to compensation may seem attractive on efficiency grounds, certain practical constraints may limit their utility. If the government were not required to pay compensation when it condemned property, it is not certain that the private sector would step into the void and provide insurance because of the problems posed by adverse selection and moral hazard.

The problem of adverse selection could be a major impediment to establishing a market in private condemnation insurance.¹⁰⁰ Condemnations are by their nature localized events, frequently made necessary by community or regional needs.¹⁰¹ In many instances, property owners may be in a better position to evaluate the probability that the government will require their property than employees of insurance companies, who are likely to have little familiarity with all of the localities in which their insurance companies operate.¹⁰² Because of the voluntary, self-selective character of insurance purchases, a disproportionate share of policies is likely to be issued to higher-risk individuals, resulting in a higher probability of insurance losses than the data concerning the likelihood of condemnation would predict. Eventually, excess losses and inadequate data could lead to the withdrawal of insurance companies

⁹⁹ See *supra* text accompanying notes 92-93.

¹⁰⁰ If the insured are better able to predict their probability of loss than the insurance provider, the premiums charged might not adequately cover the expected losses due to condemnation. See Blume & Rubinfeld, *supra* note 88, at 595-97; Fischel & Shapiro, *supra* note 89, at 286; Palmer, *Property, Compensation and Risk* (Book Review), 22 OSGOODE HALL L.J. 163, 169 (1984). But see Kaplow, *supra* note 88, at 545 (suggesting that mandatory insurance might solve this problem of adverse selection "by preventing low-risk individuals from dropping their coverage.").

¹⁰¹ See *supra* notes 78-81 and accompanying text for a discussion of the "local" nature of many federal projects requiring condemnations.

¹⁰² See Blume & Rubinfeld, *supra* note 88, at 595 ("insurers are not always as accurate as policyholders in assessing the probabilities of the event they are insuring"). But cf. *id.* at 597 n.84 ("these problems can be diminished to the extent that insurance companies can rely on specialists to develop expertise about local markets").

In addition, takings are typically the result of a political process that frequently involves lengthy discussion and debate. Cf. Kanner, *Condemnation Blight: Just How Just Is Just Compensation?*, 48 NOTRE DAME L. REV. 765, 767 & n. 11 (1973) (eminent domain consumes much time). It is quite possible that a property owner, being concerned with only a limited number of properties and having an intense interest in those properties, would have a greater incentive and ability to learn about how proposed government actions would affect her properties than would a provider of insurance. Some commentators have attributed the current absence of private insurance for costs typically uncompensated in eminent domain proceedings, such as goodwill and relocation expenses, to the problem of adverse selection. See Fischel & Shapiro, *supra* note 89, at 286 (discussing letter from Ellickson). In addition, no market exists to insure owners from the adverse effects of zoning decisions, even though the losses associated with rezoning can be large and are rarely compensated. See Blume & Rubinfeld, *supra* note 88, at 597 (a "market simply does not exist . . . for insurance against future land price changes resulting from government activity").

from the market.

Another impediment to development of a market for private condemnation insurance is the problem of moral hazard.¹⁰³ If a property owner does not bear any of the costs of the condemnation, she might not pressure the government to avoid a taking. Indeed, under certain circumstances property owners might actually encourage the government to condemn their property so as to collect insurance proceeds.¹⁰⁴ Adverse selection and moral hazard render effective private sector alternatives to compensation infeasible, and perhaps, undesirable.¹⁰⁵ Consequently, market alternatives to government compensation, such as condemnation insurance, are unlikely to lead to an efficient level of capital investment by risk averse individuals.

¹⁰³ A "moral hazard" is a situation in which an insured person or entity might take some action to actually cause a loss or fail to take some action within its power to avoid a loss. See Blume & Rubinfeld, *supra* note 88, at 593 ("Moral hazard occurs when the party to be insured can affect the probability . . . of the event that triggers payment.").

¹⁰⁴ See Blume & Rubinfeld, *supra* note 88, at 594 ("investors who believe that insurance payments will overcompensate them might lobby" for the event insured against). But see Kaplow, *supra* note 88, at 537-41 (arguing that co-insurance can alleviate the problem of moral hazard). Even if a market were to develop to provide insurance for condemnations, compensation might still be required for those who underestimate the risk of a condemnation. See Kaplow, *supra* note 88, at 548. Because a condemnation is an event that has a low probability of occurring, many property owners might not accurately perceive the risk of a taking and, therefore, fail to purchase insurance. As a result, the low probability of condemnations might result in insufficient risk spreading for some property owners. Furthermore, the absence of compensation might have negative distributional consequences since it is likely that compared to property owners who accurately estimate the risk of government condemnations, those who underestimate that risk are less sophisticated and have fewer resources to monitor public decision-making. See *id.* at 549. Because a property owner who underestimates the risk of condemnation is already likely to over-invest in property, compensation would be unlikely to distort further her investment choices and might remedy unfair distributional consequences. But cf. *id.* at 549-50 (arguing that compulsory insurance would be more desirable than compensation to deal with problem of underestimation of risk).

¹⁰⁵ Private insurance might be more costly to administer than the current system of compensation. Under the existing system, administrative costs are not expended until the government takes property. At that point, the property must be appraised and its value set either by consensual agreement or by litigation. Under a system of private insurance, however, all insured parties must transact with insurance companies regardless of whether their property is actually condemned. Properties must be appraised and risks must be evaluated by employees of the insurance companies. Typically, these administrative costs are passed along to the purchasers in the form of higher insurance premiums. If the transaction and administrative costs are large relative to the risk of loss due to condemnation, insurance may not be cost-effective. See generally Kaplow, *supra* note 88, at 545-548 (discussing the relative costs and benefits of insurance and compensation).

An additional cost of abandoning the compensation requirement would be increased inefficiencies in government decision making due to the problem of fiscal illusion. See *infra* notes 114-16 and accompanying text.

2. Risk Minimization and Intergovernmental Takings

Even if government compensation can enhance the efficiency of private capital investment (by spreading the risk of government takings to all taxpayers), the risk minimization justification is considerably less persuasive as a rationale for compensating public property owners such as localities and states. When the condemnee is a public, rather than a private entity, the assumptions underlying the risk minimization rationale for compensation become somewhat questionable.¹⁰⁶ First, there is considerable doubt as to whether states and localities behave in the same manner as the idealized, utility-maximizing individual. If, as the recent literature concerning political economy indicates, public entities do not maximize benefits and minimize costs,¹⁰⁷ their investment decisions — even disregarding the possible impact of uncompensated takings — are likely to be inefficient. Therefore, there is little reason to believe that minimizing the risk of government action will lead to efficient decision making.

Second, there is some literature that casts doubt on the assumption

¹⁰⁶ As discussed above, the risk minimization rationale for compensating private condemnees is based on the assumption that individuals are rational actors who seek to maximize the expected value of their investments. Because people are generally thought to be risk averse, the possibility of an uncompensated taking distorts the investors' perception of expected values, leading to allocative inefficiency. Compensation promotes efficient investments by spreading risk so that it is minimized for the individual investor. See *supra* text accompanying notes 84-91.

¹⁰⁷ Several commentators have suggested that elected officials and bureaucrats do not behave in an efficient fashion. These commentators suggest that rather than providing required public goods and services at least cost, legislators use allocative policy making to further their own reelection goals, and administrative officials seek to enlarge the size and importance of their bureaus. See generally R. ARNOLD, *supra* note 77, at 28-35 (arguing that representatives utilize allocation strategies designed to induce positive evaluations in their electoral districts); J. BUCHANAN & G. TULLOCK, *THE CALCULUS OF CONSENT* 119-262 (1962) (maintaining that government allocations of goods and services are not guided solely by maximizing benefits and minimizing costs); J. FEREJOHN, *supra* note 80, at 46 (offering a general indictment of the government's mishandling of public works projects, including overestimation of benefits and underestimation of costs); G. HOUSEMAN, *STATE AND LOCAL GOVERNMENT: THE NEW BATTLEGROUND* 102-08 (1986) (examining state government inefficiency); G. MILLER, *CITIES BY CONTRACT: THE POLITICS OF MUNICIPAL INCORPORATION* 72 (1980) (discussing incentives for city council members and city managers to support "particularistic services" and large budgets); W. NISKANEN, *BUREAUCRACY AND REPRESENTATIVE GOVERNMENT* 36-42 (1973) (stating that bureaucrats are people who are not entirely motivated to maximize the general welfare — they frequently allocate goods according to personal interest); M. SHEFTER, *POLITICAL CRISIS/FISCAL CRISIS: THE COLLAPSE AND REVIVAL OF NEW YORK CITY* 105-24 (1985) (discussing the political sources of New York City's fiscal crisis); Orzechowski, *Economic Models of Bureaucracy: Survey, Extensions and Evidence*, in *BUDGETS AND BUREAUCRATS: THE SOURCES OF GOVERNMENT GROWTH* 229, 230 (T. Borchering ed. 1977)("[B]ureaucrats maximize utility by producing outputs above minimum costs.").

that public officials are risk averse.¹⁰⁸ As we have seen, the objective in adopting a compensation rule for private condemnees is to minimize the inefficiencies introduced when investment decisions are made by risk-averse individuals. In keeping with the evidence that risk is not as salient for public decision-makers as for private investors, there is less reason to expect that minimizing the risk of intrusive federal action would promote economic efficiency.¹⁰⁹

Even if one were willing to extend the behavioral assumptions of utility maximization and risk aversion to public entities, the risk minimization justification remains a less compelling basis for compensating states and localities. Unlike most private persons,¹¹⁰ public entities typically own a considerable amount of property throughout the community or state,¹¹¹ and therefore, are in a better position to diversify against the risk of an uncompensated taking. Generally, states and localities are also better situated than private property owners to self-insure¹¹²

¹⁰⁸ See Arrow & Lind, *Uncertainty and the Evaluation of Public Investment Decisions*, 60 AM. ECON. REV. 364, 366 (1970) (maintaining that the total cost of risk-bearing is insignificant for public entities); Sikorsky, *Public Enterprise (PE): How Is It Different From the Private Sector*, 57 ANNALS PUB. & COOPERATIVE ECON. 477, 505 (1986) (noting that public enterprise may have more tolerance for risk). But cf. Rose-Ackerman, *Risk Taking and Reelection: Does Federalism Promote Innovation?* 9 J. LEGAL STUD. 593, 594 (1980) ("Although insecure incumbents may gain from sponsoring risky projects, secure incumbents are likely to behave as if they were 'risk averse' . . .").

¹⁰⁹ Furthermore, even if one were to assume that government officials were risk averse, a compensation rule could hinder rather than promote efficiency. Several commentators have observed that public entities systematically underestimate the costs of their activities. See *infra* note 116. This tends to lead governments to overproduce goods and services. If public entities were risk averse, however, the risk of an uncompensated taking would result in less public output than would be justified by the expected loss attributable to the risk. Cf. *supra* text accompanying notes 85-89 (discussing the investment consequences of risk aversion in private actors). Therefore, it is possible that the absence of compensation would *increase* efficiency as the government's "natural" tendency to overproduce goods and services is offset by the tendency to underproduce attributable to the risk of condemnation.

¹¹⁰ According to a 1978 survey of landowners conducted by the United States Department of Agriculture, the typical landowner in the United States is a 50-year-old, white male with a high school education who lives on his own land; the average private landholding is forty acres. See G. GUSTAFSON, WHO OWNS THE LAND? A STATE AND REGIONAL SUMMARY OF LANDOWNERSHIP IN THE UNITED STATES iv (1982). Nine tenths of all private landowners are individuals whose landholdings "tend to be small compared with the holdings of others." *Id.* at 16.

¹¹¹ According to a 1982 inventory of land use in the United States, states and localities own approximately 155 million acres of land. See H. FREY & R. HEXEM, MAJOR USES OF LAND IN THE UNITED STATES: 1982 14 (1985). A recent census reveals that there are 82,340 state and local governmental units in the United States. See 1 BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, 1982 CENSUS OF GOVERNMENTS vi (1982).

¹¹² Self-insurance is a risk retention mechanism in which a private firm or government body plans to pay the losses it incurs from its own funds. See C. WILLIAMS &

against the risk of a condemnation. They typically have both greater assets and greater expertise in assessing risk. Many states and localities also have significant experience with self-insurance programs. Groups of localities or states frequently pool funds in an effort to obtain the benefits of both self-insurance and risk spreading.¹¹³

C. *Avoiding Fiscal Illusion*

In addition to making the decisions of potential condemnees more efficient by minimizing investment risk, compensation also has been justified as contributing to efficient decision-making by condemnors. If it were not required to pay for property it took by eminent domain, the federal government might substitute condemned property for other inputs that might be less valuable to society.¹¹⁴ This government utilization of more valuable resources in the place of less valuable ones is a form of "fiscal illusion."¹¹⁵ Because fiscal illusion interferes with resources finding their most valued use in the market, fiscal illusion creates allocative inefficiency. Hence, one function of a compensation requirement would be to eliminate the illusion, forcing the government to bear the real costs of its actions.¹¹⁶

R. HEINS, *supra* note 84, at 190. Self-insurance is typically used by firms or entities that: 1) are large enough to assume risk, 2) can reasonably predict future losses, and 3) can benefit from obtaining control over their losses by improving claim processing, and saving the loading charges that would be paid to an outside insurer. See Young, *Self-Insurance in RISK MANAGEMENT TODAY: A HOW-TO GUIDE FOR LOCAL GOVERNMENT* 59-61 (N. Wasserman & D. Phelus, eds. 1985).

¹¹³ During the early 1980's, many localities and states were unable to purchase insurance from private companies. See COUNTY AND MUNICIPAL GOVERNMENT STUDY COMMISSION, STATE OF NEW JERSEY, *LOCAL GOVERNMENT LIABILITY INSURANCE: A CRISIS* 9-13 (May 1986). Many public entities inaugurated or enhanced self-insurance programs and pooled funds. See Myers, *Managing Municipal Liability Risk*, GOVERNANCE 18 (Summer-Fall 1987).

¹¹⁴ See R. POSNER, *supra* note 19, at § 3.6.

¹¹⁵ "Fiscal illusion" traditionally refers to the methods utilized by governments to disguise the level of taxation in order to minimize taxpayer resistance. See R. BUCHANAN, *PUBLIC FINANCE IN DEMOCRATIC PROCESS* 131 (1967). In describing the writings of Amilcare Puviani, an Italian political scientist, Buchanan states that "[t]he ruling group attempts, to the extent that is possible, to create fiscal illusions, and these have the effect of making taxpayers think that the taxes to which they are subjected are less burdensome than they actually are." *Id.* Among the fiscal illusions suggested by Puviani are obscuring the real cost of public goods, timing the payment of taxes to coincide with favorable events, fragmenting the total tax burden among several taxes, and adopting taxes with uncertain incidence. According to Buchanan, certain modern taxes and tax practices exemplify elements of fiscal illusion, including tax withholding, social security taxes, and corporate income taxes. *Id.* at 139-41.

¹¹⁶ Justifying compensation as necessary to prevent fiscal illusion requires the acceptance of two assumptions: 1) Policy makers and bureaucrats fail to take into account social costs that are not translated into budgetary outflows, and 2) Government officials do not similarly discount the benefits generated by government programs. See Kaplow,

Prevention of fiscal illusion justifies compensation for public condemnees as well as private condemnees. Although a state is presumably better situated than a private individual to make the cost of a taking apparent to federal policy makers,¹¹⁷ there is no assurance that the government will properly take that cost into account unless it is forced to pay for the value of the property condemned.¹¹⁸ In addition, if only takings of private property were compensated, the problem posed by fiscal illusion would be magnified. For many projects, publicly owned property could be readily substituted for private property. If the federal

supra note 88, at 567-68. If government officials discounted benefits by the same amount that they discounted costs, no illusion would occur — the “net” benefit of the program would be the same as if no discounting took place. *See id.* at 568.

The available evidence supports the validity of these two assumptions. Notwithstanding political economists’ models of representative government indicating that small groups of intensely interested citizens can have a disproportionate influence on legislation, *see* M. OLSON, *THE LOGIC OF COLLECTIVE ACTION* 145-46 (1965) (explaining the surprising power of business lobbies), it would be extremely difficult for any one individual or entity to have sufficient power to force the government to account for the cost of condemned property. Moreover, given the isolated nature of condemnations, groups of condemnees would likely find the cost of organization to be prohibitive. In addition, several empirical studies indicate that governments overestimate benefits and underestimate costs generated by public programs. *See, e.g.*, J. FERREJOHN, *supra* note 80, at 20 (finding that the Army Corps of Engineers overestimates benefits and underestimates costs); G. DOWNS & P. LARKEY, *supra* note 22, at 125-127 (citing examples of cost underestimation and benefit overestimation); R. HAVEMAN, *THE ECONOMIC PERFORMANCE OF PUBLIC INVESTMENTS* 93-109 (1972) (concluding that the Army Corps of Engineers estimates have historically been lower than the realized costs of projects).

¹¹⁷ It is important to note that fiscal illusion can occur at two levels — in Congress, and in the federal bureaucracy. States are more likely than private individuals to be influential at both of these levels. Many states have hired professional staffs to lobby members of Congress. *See* D. HAIDER, *WHEN GOVERNMENTS COME TO WASHINGTON: GOVERNORS, MAYORS, AND INTERGOVERNMENTAL LOBBYING* 1-45 (1974) (describing national lobbying organizations of mayors and governors); Beer, *Federalism, Nationalism and Democracy in America*, 72 *AM. POL. SCI. REV.* 9, 18-19 (1978) (discussing intergovernmental lobby); Conlan, *Federalism and American Politics: New Relationships, a Changing System*, 11 *INTERGOVERNMENTAL PERSP.* 32, 43 (Winter 1985) (noting that individual states and cities have established lobbying organizations in Washington, D.C.).

Such lobbying can be doubly effective because legislators frequently have significant influence over administrative agencies by virtue of their committee assignments. *See generally*, R. ARNOLD, *supra* note 77, at 107-15 (discussing committee members’ influence over the actions of agencies). Even if an individual Member of Congress did not have direct influence over an agency threatening to condemn property in her district, she might be able to logroll with another who did. *See id.* at 49. If the object of the taking were to exploit or harm the state in which the condemned property was located, however, logrolling would likely be ineffective. *See infra* note 218 and accompanying text.

¹¹⁸ *But cf.* Blume & Rubinfeld, *supra* note 88, at 621 (observing that full indemnification may overcompensate condemnee if the government is subject only to partial fiscal illusion); Quinn & Trebilcock, *Compensation, Transition Costs And Regulatory Change*, 32 *U. TORONTO L.J.* 117, 135 (1982) (suggesting that compensation might not protect against allocative inefficiency due to manipulation of benefits).

government were required to compensate only private condemnees, officials might find it hard to resist taking state and local property, even if private property were better suited for the project.¹¹⁹

D. *Protection From Political Exploitation*

In addition to promoting fair distribution of the costs of government, minimizing investment risk, and preventing fiscal illusion, the just compensation clause serves a vital role in policing the political process. If the federal government were able to take private property without compensation, two types of abuse might occur. First, if groups of citizens, or factions, gained control of the legislative process, they might use uncompensated takings as an instrument for enriching themselves at the expense of other, less politically powerful citizens. Requiring the federal government to compensate property owners when it takes their property reduces the incentives for this type of "rent-seeking,"¹²⁰ by spreading the costs of such behavior to all citizens, including those in power. Second, if the federal government were not required to compensate condemnees, those in power could use the power of eminent domain to punish or coerce specific citizens, thereby depriving them of their liberty.¹²¹ The compensation requirement limits the ability of those in control of the federal government to use the power of eminent domain to deprive citizens of their liberty by indemnifying citizens, that is, requiring the government to ensure that the condemnees are in as good a position as they were prior to the government action.

This rationale for compensation also applies to intergovernmental takings, because states and localities, themselves, may be the objects of

¹¹⁹ Under some conditions, however, a compensation requirement for intergovernmental takings might hinder rather than promote economic efficiency. See *supra* note 109 (discussing the possible increase in efficiency that may result from states and local governments bearing some share of the cost of federal programs).

¹²⁰ In this context, "[r]ent-seeking refers to an attempt to obtain economic rents . . . through government intervention in the market." Macey, *Promoting Public-Regarding Legislation Through Statutory Interpretation: An Interest Group Model*, 86 COLUM. L. REV. 223, 224 n.6 (1986). Economic rents are payments for the use of an asset which are greater than what the asset would command in any alternative use. See J. BUCHANAN, R. TOLLISON & G. TULLOCK, *TOWARD A THEORY OF THE RENT-SEEKING SOCIETY* 3 (1980) [hereinafter RENT-SEEKING SOCIETY]; Merrill, *Rent Seeking*, *supra* note 45, at 1586.

¹²¹ See Reich, *The New Property*, 73 YALE L. J. 733, 771-74 (1964) (function of property is to create a zone of privacy and independence that promotes individual freedom). But see Baker, *Property and its Relation to Constitutionally Protected Liberty*, 134 U. PA. L. REV. 741, 775-82 (1986) (contrasting "formal" and "substantive" conceptions of liberty); Nedelsky, *American Constitutionalism and the Paradox of Private Property*, in CONSTITUTIONALISM AND DEMOCRACY 241, 241 (J. Elster & R. Slagstad eds. 1988) ("[P]rivate property no longer serves as a boundary between individual rights and governmental power.").

rent-seeking and factional abuse. Thus, compensation for intergovernmental takings can be justified as serving a political function analogous to compensation for private property owners. Requiring the federal government to pay for the property it expropriates raises the cost of rent-seeking behavior to the citizens of states in control of the legislative process, thereby limiting the disruption to the condemnee, and reducing the potential advantages to the rent-seeking states. Provided that intergovernmental condemnees receive full indemnification for their property, the ability of state factions to use the federal power of eminent domain for the purpose of disrupting or coercing other states would be limited. Like the preceding analyses of the other three justifications for compensation, I begin this section with a discussion of private condemnees and the way that compensation has been justified as a necessary protection against factional abuse. As an essential foundation for presenting the analogous rationale for intergovernmental takings, I present a normative argument to support the proposition that states and localities have an important, if at times problematic, role to play in the operation of our political system. On balance, the principles of federalism which preserve the integrity and independent decision-making authority of states are defensible on grounds of political theory and economic efficiency. Courts need not rely on strained analogies to private individuals in justifying compensation for intergovernmental condemnees. Instead, compensation for state and local condemnees may be justified as necessary to preserve the integrity and independence of states and localities in our federal system.

1. Private Takings, Just Compensation, and the Evils of Faction

Earlier in this Article, the just compensation requirement was shown to have been designed, in part, to prevent unfair burdens from falling on private property owners.¹²² Without a compensation requirement, some citizens might find themselves paying more than their fair share for public goods and services. In protecting against unfair burdens, the just compensation requirement, together with other constitutional provisions, serves a vital political function. Requiring the federal government to compensate citizens when it takes their property limits the opportunity for individuals to use the coercive power of the government for their own ends. Even the most cursory reading of historical sources reveals that the architects of our system of government were extremely concerned with the potential for one group of citizens to take

¹²² See *supra* text accompanying notes 46-54.

over the machinery of government and use it for their own advantage.¹²³ To guard against factional abuse,¹²⁴ the Framers constructed a system of government with structural safeguards against concentrations of power.¹²⁵

The Bill of Rights also contains a "shield of rights"¹²⁶ designed to protect citizens from incursions on liberty.¹²⁷ Among the elements of this shield of rights is the just compensation clause.¹²⁸ There can be no doubt that among the Framers' principal concerns was the protection of private property.¹²⁹ In addition to the contract¹³⁰ and due process¹³¹

¹²³ For example, Madison writes that an essential problem of governance is how to control the problems posed by factions, which he defines as "a number of citizens, whether amounting to a majority or minority of the whole, who are united and actuated by some common impulse of passion, or of interest, adverse to the rights of other citizens, or to the permanent and aggregate interests of the community." *THE FEDERALIST* No. 10, at 78 (J. Madison) (C. Rossiter ed. 1961); see also Sunstein, *Interest Groups in American Public Law*, 38 *STAN. L. REV.* 29, 38-40 (1985) [hereinafter Sunstein, *Interest Groups*] (noting that the federalists justified a federal system, in part, as suited to controlling factions).

¹²⁴ As Madison's statement of the problem indicates, see *supra* note 123, the Framers seem to have focused on the danger, or potential for abuse by groups of like-minded individuals. Contemporary scholars are divided as to the scope and seriousness of what is today called the "special interest group" problem. See Fitts, *The Vices of Virtue: A Political Party Perspective on Civic Virtue Reforms of the Legislative Process*, 136 *U. PA. L. REV.* 1567, 1582 n.36 (1988) (comparing divergent contemporary analyses of special interest groups).

¹²⁵ The Constitution sets up a system of government in which there are many checks and balances designed to prevent factions from gaining power. Under the doctrine of separation of powers, the three branches of the national government divide power horizontally. See L. FREEDMAN, *POWER AND POLITICS IN AMERICA* 9-10 (2d ed. 1974); Beer, *supra* note 117, at 12-13. "Vertical" checks and balances also exist between the states and the national government. See Sunstein, *Interest Groups*, *supra* note 123, at 44.

¹²⁶ See Sunstein, *Interest Groups*, *supra* note 123, at 33 (describing the shield as creating "spheres of individual autonomy into which the government may not enter").

¹²⁷ Some commentators have suggested that the system of government devised by the Framers also includes elements to promote civic virtue which would have the effect of countering tendencies toward faction. See *id.* at 32-33.

¹²⁸ See *id.* at 33 ("This shield of autonomy could protect . . . rights of traditional private property . . .").

¹²⁹ See, e.g., *THE FEDERALIST* No. 54, at 339 (J. Madison) (C. Rossiter ed. 1961) ("Government is instituted no less for the protection of property than of the persons of individuals."); *DOCUMENTS ILLUSTRATIVE OF THE FORMATION OF THE UNION OF THE AMERICAN STATES* (C. Tansill ed. 1927) 161-62 (quoting Madison's assertion that national government is necessary to provide security for property rights); Nedelsky, "Economic Liberties" and the Foundations of American Constitutionalism: *The Federalist Perspective*, in *TO SECURE THE BLESSINGS OF LIBERTY: FIRST PRINCIPLES OF THE CONSTITUTION* 221 (S. Thurow ed. 1988) (stating that protecting property was a central concern of Framers); Philbrick, *Changing Conceptions of Property in Law*, 86 *U. PA. L. REV.* 691, 713-14 (1938) (discussing the close relation between liberty and property for the Framers); Sunstein, *Interest Groups*, *supra* note 123, at 44 (protection of private property was a principal interest of Framers). Many adherents of republican thought recognized the importance of property in permitting citizens to avoid subordination to others and in permitting citizens to develop civic vir-

clauses, the just compensation clause is the principal protection of private property in the Constitution and Bill of Rights. The compensation requirement reduces the incentive for a faction to gain political power for the purpose of appropriating property for its own benefit.¹³² Perhaps even more important to the Framers, the just compensation clause also protects citizens from tyranny. Without a compensation requirement, factions that gained control of the federal government could deprive other citizens of their liberty by threatening to take their property if they did not submit to the will of those in power.¹³³

Madison's intention that the just compensation clause prevent factional abuse and protect individual liberty can be seen from contemporaneous history and Madison's own writings. In the years following the Revolutionary War, several states had passed laws that had the effect of benefiting debtors at the expense of creditors.¹³⁴ In addition, state legislatures enacted laws punishing citizens who had supported the crown by confiscating their property without compensation.¹³⁵ These actions, no doubt, influenced Madison, who wrote just after the ratification of the fifth amendment that a government which violated the rights of

tue. See Katz, *Thomas Jefferson and the Right To Property in Revolutionary America*, 19 J. LAW & ECON. 467, 474 (1976) (discussing Jefferson's belief that private property permits citizens to avoid subordination and cultivate inner strength).

¹³⁰ U.S. CONST. art. I, § 10.

¹³¹ U.S. CONST. amends. V, XIV § 1.

¹³² See Merrill, *Rent Seeking*, *supra* note 45, at 1577 (characterizing Epstein's view of the just compensation clause). Cf. Sunstein, *Interest Groups*, *supra* note 123, at 45 (constitutional safeguards against faction were designed principally to protect property rights). In addition to the compensation requirement, the public use requirement of the just compensation clause protects against exercises of eminent domain designed to benefit individual private interests. See R. EPSTEIN, *supra* note 44, at 169-70; Merrill, *Rent Seeking*, *supra* note 45, at 1578; Stoebuck, *A General Theory*, *supra* note 12, at 589; Sunstein, *Naked Preferences and the Constitution*, 84 COLUM. L. REV. 1689, 1724 (1984). But see *Hawaii Housing Authority v. Midkiff*, 467 U.S. 229, 240 (1984) (reducing the impact of public use test by holding that the power of eminent domain is coterminous with the police power).

¹³³ See Sax, *supra* note 44, at 57-60, 64-65 (1964) (arguing that the purpose of the just compensation clause is to protect citizens from arbitrary and oppressive government action, not merely to maintain property values). See also Tushnet, *Federalism and the Traditions of American Political Theory*, 19 GA. L. REV. 981, 985-86 (1985) (under liberalism, property contributes to liberty by preventing domination by others and promoting domestic tranquility).

¹³⁴ For example, several states enacted legislation suspending debts and took actions to devalue money. See A. KELLY, W. HARBISON & H. BELZ, *THE AMERICAN CONSTITUTION: ITS ORIGINS AND DEVELOPMENT* 88 (6th ed. 1983); A. NEVINS, *THE AMERICAN STATES DURING AND AFTER THE REVOLUTION* 569-72 (1924); G. WOOD, *supra* note 50, at 404-06; E. MORGAN, *THE BIRTH OF THE REPUBLIC 1763-1789* 127-28 (1956).

¹³⁵ All states with the exception of South Carolina passed laws confiscating loyalist estates without compensation. See A. NEVINS, *supra* note 134, at 507; Note, *Origins and Significance*, *supra* note 12, at 698.

property "is not a pattern for the United States."¹³⁶ Madison made the connection between the protection of property and the prevention of tyranny explicit in the same essay: "Where an excess of power prevails, property of no sort is duly respected. No man is safe in his opinions, his person, his faculties, or his possessions."¹³⁷

Courts and commentators have also espoused the view that the purpose of the just compensation clause goes beyond preventing unfair or unequal burdens to protecting the political system from factional abuse. In *Chicago, B. & Q. R.R. v. Chicago*,¹³⁸ the Supreme Court held that states were bound by the just compensation clause. In discussing why just compensation was an element of due process under the fourteenth amendment, Justice Harlan paraphrased language from *Loan Association v. Topeka*¹³⁹ stating that "a government by whatever name it was called, under which the property of citizens was at the absolute disposition and unlimited control of any depository of power, was, after all, but a despotism. . . ."¹⁴⁰ Similarly, in his *Commentaries on the Constitution*, Justice Story observes, "in a free government almost all other rights would become utterly worthless if the government possessed an uncontrollable power over the private fortune of every citizen."¹⁴¹

2. Intergovernmental Takings, Faction, and Federalism

Just as uncompensated takings would make private citizens vulnerable to abuse by factions that engaged in rent-seeking and curtailment of liberty, the absence of compensation for intergovernmental takings would make states and municipalities vulnerable to similar evils. Groups of states could band together in Congress to enact policies and programs that would benefit themselves by expropriating property belonging to other states. These expropriations could disrupt the ability of states to continue providing the services expected by their citizens. In

¹³⁶ See *Property*, *supra* note 54, at 267-68.

¹³⁷ *Id.* at 266.

¹³⁸ 166 U.S. 226, 235 (1897).

¹³⁹ 87 U.S. (20 Wall.) 655 (1874). In *Loan Association v. Topeka*, the Supreme Court invalidated a state statute which authorized towns to issue bonds in support of private industry. According to the Court, the use of the power of taxation to support interest payments on the debt was not a public purpose. *Id.* at 665.

¹⁴⁰ *Chicago, B. & Q. R.R.*, 166 U.S. at 237.

¹⁴¹ 2 J. STORY, COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES § 1790, at 570 (5th ed. 1891); see also, R. EPSTEIN, *supra* note 44, at 138 (noting that protection of private property fosters freedom of speech and the protection of liberty by preventing factions from seizing power); Philbrick, *supra* note 129, at 713 (discussing government's role as a protector of private property); Sax, *supra* note 44, at 54-60 (discussing the Framers' concern with tyrannical power).

addition, uncompensated takings could be used by groups of states to accomplish objectives more sinister than mere rent-seeking. Intergovernmental takings could be used systematically by those in control of the national government to disadvantage individual states, groups of states, or regions, by impoverishing them and disrupting their operations. Uncompensated intergovernmental takings, therefore, would constitute a threat to the values of federalism upon which the political system of the United States is based.

a. *The Case For Federalism*

A compensation requirement for intergovernmental takings predicated upon protecting federalism is compelling only if the values served by federalism are important, and are best promoted by a federal system. American federalism has been both controversial and enigmatic since its inception in the eighteenth century.¹⁴² Perhaps as good a definition of federalism as any is offered by William Riker: "The essential institutions of federalism are, of course, a government of the federation and a set of governments of the member units, in which both kinds of governments rule over the same territory and people and each kind has the authority to make some decisions independently of the other."¹⁴³ Four qualities are often identified as the essential virtues justifying a federal system: preserving individual liberty, promoting citizen participation, providing laboratories for political experimentation, and efficiently providing public goods.

(i) Preservation of Individual Liberty

Independent decision-making authority, the core of Riker's definition of federalism, is central to the oldest and most important justification for a federal system — the preservation of individual liberty. The existence of significant independent decision-making authority at the

¹⁴² In fact, it is somewhat ironic that Madison, Hamilton, and Jay came to be known as "Federalists." At the Constitutional Convention, Madison, along with the other members of his state's delegation, proposed the Virginia Plan, which gave Congress the power to "negative all laws passed by the several states, contravening in the opinion of the National Legislature the articles of the Union." Although the Virginia Plan was not adopted by the Convention, it illustrated Madison's sympathy for a strong national government, rather than a mere federation of states. See A. KELLY, W. HARBISON & H. BELZ, *supra* note 134, at 91-95; G. WOOD, *supra* note 50, at 525; Amar, *Of Sovereignty and Federalism*, 96 YALE L.J. 1425, 1426 n.9 (1987).

¹⁴³ W. RIKER, *FEDERALISM* 5 (1964). Even today, the definition is not a settled one. See Nathan, *The Role of the States in American Federalism*, in *POLITICS AND PUBLIC POLICY* 23-25 (G. Van Horne ed. forthcoming 1988 from Congressional Quarterly Publishers).

state level was designed to protect individual liberty. If the national government were to be captured by an authoritarian faction, the people could look to the states to rise up against the threat to liberty; in fact, the mere existence of independent state power would discourage despotism.¹⁴⁴

A second form of oppression would also be checked by independent state power — the ability of groups of states to coalesce and gain control of the machinery of government for the purpose of exploiting citizens from other states or regions. Although life under the Articles of Confederation had demonstrated that insufficient national power led states to engage in disastrous economic warfare,¹⁴⁵ many delegates to the Constitutional Convention of 1787, and the state ratifying conventions feared that too much national power might threaten citizens by

¹⁴⁴ According to Hamilton:

Power being almost always the rival of power, the general government will at all times stand ready to check the usurpations of the state governments, and these will have the same disposition towards the general government. The people by throwing themselves into either scale, will infallibly make it preponderate. If their rights are invaded by either, they can make use of the other as the instrument of redress.

THE FEDERALIST NO. 28, at 181 (A. Hamilton) (C. Rossiter ed. 1961); see also THE FEDERALIST NO. 51, at 323 (J. Madison) (C. Rossiter ed. 1961) (the national and state governments "will control each other"); Beer, *supra* note 117, at 14; Diamond, *The Federalist's View of Federalism*, in INSTITUTE FOR STUDIES IN FEDERALISM, ESSAYS IN FEDERALISM 21, 53-54 (1961) (noting the Federalists' view that in a system of rival governments, if either the national or state government begins to usurp power, the other will be able to rally the people against it); Nagel, *Federalism as a Fundamental Value: National League of Cities in Perspective*, 1981 SUP. CT. REV. 81, 100 (stating that the efficiency and responsiveness of state and local governments would enable them to act as a "counterpoise" to national authority).

Theoretically, state and local officials would gain the allegiance of their constituents by appealing to local sentiments. Moreover, they would have had the opportunity to develop competence and demonstrate their abilities at governance while serving their states and localities. See Benson, *Values of Decentralized Government*, in ESSAYS IN FEDERALISM, *supra*, at 1, 10; Macmahon, *The Problems of Federalism: A Survey*, in FEDERALISM: MATURE AND EMERGENT 11 (A. Macmahon ed. 1955). Furthermore, states and localities are particularly well suited to organize popular resistance to a tyrannical national government by virtue of their independent authority to require citizens to contribute to the opposition. See, e.g., Rapaczynski, *From Sovereignty to Process: The Jurisprudence of Federalism After Garcia*, 1985 SUP. CT. REV. 341, 388-89 (states can break national government's monopoly on coercion).

History, however, has shown that the existence of a federal form of government may be insufficient to prevent national tyranny. See A. BRECHT, *FEDERALISM AND REGIONALISM IN GERMANY* 7, 21-22, 118-19 (1945) (opposition of Prussia insufficient to prevent Nazi takeover of German government and abolition of state authority). States may also be more likely than the national government to deprive citizens, especially minorities, of their rights. See W. RIKER, *supra* note 143, at 142-45; Rapaczynski, *supra*, at 385-86 (homogeneity and cohesiveness of state populations increase likelihood of state oppression of minorities).

¹⁴⁵ See A. KELLY, W. HARBISON & H. BELZ, *supra* note 134, at 87.

establishing a vehicle for regional domination.¹⁴⁶ Creating a strong national government, yet at the same time permitting states to remain as independent political units with substantive power, helped to resolve this dilemma.¹⁴⁷

(ii) Promotion of Citizen Participation

In addition to protecting citizens from national oppression, a significant role for states enhances the legitimacy of government institutions and may promote their effectiveness. A representative democracy such as the United States depends upon the participation of well-informed citizens. Many political commentators believe that meaningful participation is fostered by decentralized, rather than centralized, governments.¹⁴⁸ Compared to centralized political systems, decentralized

¹⁴⁶ One of the major arguments against the Constitution was that centralized power would permit particular states or sections to gain control and drain wealth from citizens of other states by discriminatory taxation and commercial legislation. See P. ONUF, *THE ORIGINS OF THE FEDERAL REPUBLIC: JURISDICTIONAL CONTROVERSIES IN THE UNITED STATES 1775-1787*, at 186-94 (1983) (discussing Antifederalist objections to the Constitution); see also 3 *THE DEBATES IN THE SEVERAL STATE CONVENTIONS ON THE ADOPTION OF THE FEDERAL CONSTITUTION* 615 (J. Elliot ed. 1901) (Report of a speech by Rep. Grayson at Virginia Convention: "[t]he little states gain in proportion as we lose . . ."); 1 *THE RECORD OF THE FEDERAL CONVENTION OF 1787*, at 341 (M. Farrand rev. ed. 1937) [hereinafter M. FARRAND] (Madison, summarizing a speech by Delegate Luther Martin (Maryland): The American people formed the federal government "to defend the lesser States agst. [sic] the ambition of the larger . . ."); *id.* at 167 (Madison summarizing speech by Delegate Gunning Bedford, Jr. (Delaware): The "large states [will] crush the small ones whenever they stand in the way of their ambitions or interested views.").

Concerns about large states, primarily in the South, dominating smaller states, primarily in the North, eventually produced what later became known as the "Great Compromise." Membership in the House of Representatives is based upon population, whereas membership in the Senate is apportioned equally among the states. See generally A. KELLY, W. HARBISON & H. BELZ, *supra* note 134, at 97-100. For further analysis of how regional conflict, both real and potential, shaped public debate and policy in the early years of the republic, see J. DAVIS, *SECTIONALISM IN AMERICAN POLITICS 1774-1787* (1977); H. HENDERSON, *PARTY POLITICS IN THE CONTINENTAL CONGRESS* (1974); McCoy, *James Madison and Visions of American Nationality in the Confederation Period: A Regional Perspective*, in *BEYOND CONFEDERATION* 226-58 (R. Beeman, S. Botein & E. Carter eds. 1987).

¹⁴⁷ The Constitution contains several safeguards against unequal treatment of states by the national government. See *infra* text accompanying notes 219-31.

¹⁴⁸ See R. DAHL & E. TUFT, *SIZE AND DEMOCRACY* 53-65 (1973) (discussing surveys indicating that citizens feel participation at the local level is more effective than at the national level); J. NAGEL, *PARTICIPATION* 84-87 (1987) (opportunity for direct democracy declines as size of polity increases and homogeneity decreases); Anton, *Models of American Intergovernmental Relations* 3 (paper prepared for Workshop on Ocean Resources and Intergovernmental Relations in the 1980's, September 12-13, 1985) (describing participatory bias of federal political system). But see R. DAHL, *DEMOCRACY IN THE UNITED STATES: PROMISE AND PERFORMANCE* 175-86 (4th ed. 1981) (citizens are less active and competition between political parties is less intense in state and local elections than in national elections); Fitts, *supra* note 124, at 1641 n.259

government offers citizens a broader array of opportunities to become personally involved in civic affairs,¹⁴⁹ greater influence over elected officials,¹⁵⁰ and an increased ability to monitor public affairs and hold government officials accountable for their actions.¹⁵¹

In addition, as the recent literature on the "republican revival"¹⁵² makes clear, participation in public affairs can serve a less instrumental function, quite distinct from merely promoting an accurate aggregation of citizen preferences. Under this view, participation itself is beneficial, infusing citizens with a sense of purpose and control over their lives.¹⁵³ Participation in public affairs and the deliberative process engaged in by citizens as part of this participation serves an educative and developmental function, permitting citizens to select values and develop a sense of "empathy, virtue and feelings of community."¹⁵⁴

("the possibility exists, contrary to the classic civic virtue view, . . . that dispersion of authority to *increase* points of access will *decrease* general popular participation." (emphasis in original)).

¹⁴⁹ Approximately 500,000 elected officials and 13,000,000 appointed officials perform governmental functions for states and localities in the United States. See Anton, *supra* note 148, at 4.

¹⁵⁰ See McConnell, *Federalism: Evaluating The Founder's Design* (Book Review), 54 U. CHI. L. REV. 1484, 1509-10 (1987) (endorsing the position that constituents' influence on state legislators is proportionately greater than their influence on members of Congress).

¹⁵¹ See Kaden, *Politics, Money, and State Sovereignty: The Judicial Role*, 79 COLUM. L. REV. 847, 853-54 (1979) (local government increases access and accountability).

¹⁵² See Sunstein, *Beyond the Republican Revival*, 90 YALE L.J. 1539 (1988).

¹⁵³ See Frug, *City as Legal Concept*, *supra* note 33, at 1068-69 (contrasting "public" with "individual" freedom and characterizing a critique of Western society as the limited ability of citizens to control their own lives); Rapaczynski, *supra* note 144, at 400 (political activity viewed as a good in itself, linked to human freedom).

¹⁵⁴ See Sunstein, *supra* note 152, at 1556. See also J. NAGEL, *supra* note 148, at 13-15 (discussing developmental effects of participation); Frug, *City as Legal Concept*, *supra* note 33, at 1069 (popular involvement in the decision-making process is possible only at the local level); McConnell, *supra* note 150, at 1510 (accepting that civic virtue could be cultivated only in small republics because the spirit of benevolence becomes weaker as the distance between individual and object of benevolence increases); Rapaczynski, *supra* note 144, at 402 (if non-instrumental participation is possible, it can realistically exist only at local level).

However, claims that widespread participation at the local level contributes to the public good may be overrated. Experience with efforts to decentralize urban power frequently demonstrates that, contrary to producing altruism and civic virtue, citizen participation and decentralized decision-making authority may lead to corruption and the pursuit of parochial interests. See D. YATES, *NEIGHBORHOOD DEMOCRACY* 160 (1973) ("[T]o the extent that neighborhood institutions articulate and act on their parochial interests, there is a clear tension between neighborhood democracy and the public interest."); Barbanel, *Koch Proposals to Convert 2 Buildings to Shelters are Rejected*, N.Y. Times, March 12, 1988, at A36, col. 1 (New York City Board of Estimate rejects conversion of vacant commercial buildings into homeless shelters in face of neighborhood opposition); Blumenthal & Verhovek, *Of Patronage and Profit: Tale of School Board 12*, at A1, col. 1, (corruption within decentralized community school board);

(iii) "Laboratories For Experimentation"

One of the most frequent justifications for federalism is reflected by Justice Brandeis's famous observation that the nation benefits from a system in which "a single courageous state may, if its citizens choose, serve as a laboratory, and try social and economic experiments without risk to the rest of the country."¹⁵⁵ Advocates of the "laboratory" justification of federalism point to numerous examples of state initiatives such as unemployment compensation, health and safety regulations, and public financing for political campaigns, which were later emulated by a presumably more cautious national government.¹⁵⁶

Other commentators have argued, however, that the experiments taking place in states and localities are somewhat less impressive than the proponents of federalism admit. Competition between states, sometimes cited by these advocates as increasing the likelihood of innovation, might have the opposite effect. Rather than risk losing capital and jobs to neighboring jurisdictions as a result of a failed experiment, states and localities might be overly cautious in trying new approaches to deal with social problems or service delivery.¹⁵⁷ In addition, some have ar-

Buder, *Decentralization of Schools Provided Painful Lessons*, N.Y. Times, Dec. 11, 1988, at E6, col 1 ("decentralization [of schools] not only failed to fulfill many of the early hopes but also spawned a range of abuses and excesses."); Polsky, *Shelter Sites Draw Community Ire*, Newsday, Aug. 13, 1987, at 19, col. 1 (community opposition to seventeen proposed shelters for the homeless).

¹⁵⁵ *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J. dissenting). Multiplying the number of independent legislative arenas creates manifold opportunities for the development of unique solutions to problems which can be imitated by other states. See Macmahon, *supra* note 144, at 10 (multiplication of legislative arenas increases the scope of experimentation); McConnell, *supra* note 150, at 1498-1500 (same). The existence of independent centers of government may also make possible the expression of political viewpoints that do not share the support of the entire nation. See, e.g., R. NATHAN & F. DOOLITTLE, *REAGAN AND THE STATES* 7 (1987) (states adopt programs associated with political liberalism when national government is dominated by conservatives).

¹⁵⁶ See Benson, *supra* note 144, at 13-14; Kmiec & Diamond, *New Federalism Is Not Enough: The Privatization of Non-Public Goods*, 7 HARV. J.L. & PUB. POL'Y 321, 342 (1984). "[S]tates may help Congress out by tackling novel policy issues and by continuing to handle many familiar problems that Congress either chooses to ignore or . . . fails to find a national solution for." Derthick, *Preserving Federalism: Congress, the States, and the Supreme Court*, 4 BROOKINGS REV. 32, 35 (Winter/Spring 1986). States' experimentation may also serve as a model for change in other states. See Scheiber, *American Federalism and the Diffusion of Power: Historical and Contemporary Perspectives*, 9 U. TOL. L. REV. 619, 636 (1984) [hereinafter Scheiber, *American Federalism*].

¹⁵⁷ See G. BENSON, *THE NEW CENTRALIZATION* 23-24 (1941); Rose-Ackerman, *supra* note 108, at 594. One of the reasons why competition in the public sector may be less effective in promoting innovation than competition in the private sector is that payoffs from successful innovation may be less immediate and visible. But see Walker, *The Diffusion of Innovations Among The American States*, 63 AM. POL. SCI. REV. 880, 890 (1969) (interstate competition can promote diffusion of innovation). Interstate

gued that states and localities lack the capacity for efficient innovation.¹⁵⁸

(iv) Efficient Provision of Public Goods

A significant benefit of a political system that decentralizes decision-making authority is its ability to provide goods and services that are responsive to the needs and desires of its citizens. If all public goods and services were provided by the national government, it is likely that they would be relatively uniform throughout the United States, even though needs and desires might vary from region to region.¹⁵⁹ To the extent that decisions are made by smaller units of government, there is likely to be a greater correspondence between citizen demand and government production of public goods.¹⁶⁰ The increased likelihood that

competition for economic benefits may even promote a destructive "race to the bottom" in state regulation of economic enterprises. Some commentators have argued that states have an incentive to pass laws advantageous to corporate managers, but harmful to shareholders. See Carey, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663, 668 (1974). But see Romano, *Law as a Product: Some Pieces of the Incorporation Puzzle*, 1 J.L. ECON. & ORG. 225, 279-81 (1985) (empirical evidence shows that reincorporations in Delaware are not related to negative shareholder returns); Winter, *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251, 251-52 (1977) (state regulation will lead to laws favorable to stockholders).

¹⁵⁸ See G. BENSON, *supra* note 157, at 40-42 (states are administratively inefficient and fail to conduct adequate research); COMMITTEE FOR ECONOMIC DEVELOPMENT, *MODERNIZING STATE GOVERNMENT* 10-11 (1967) (noting that states have failed to come to grips with economic and social issues). But see R. NATHAN & F. DOOLITTLE, *supra* note 155, at 9, 362 (in the past two decades states have enhanced their standing and capability); Beam & Benton, *Intergovernmental Relations and Public Policy: Down the Road*, in INTERGOVERNMENTAL RELATIONS AND PUBLIC POLICY 205-06 (J. Benton & D. Morgan eds. 1986) (discussing the resurgence of states and localities); Reeves, *Look Again at State Capacity: The Old Gray Mare Ain't What She Used To Be*, in AMERICAN INTERGOVERNMENTAL RELATIONS TODAY: PERSPECTIVES AND CONTROVERSIES 143 (R. Dilger ed. 1986) (cataloging recent improvements in state administration).

¹⁵⁹ See W. OATES, *FISCAL FEDERALISM* 11 (1972); Anton, *supra* note 148, at 24-25. One reason why nationally provided goods and services would tend to be uniform is the desire to promote horizontal equity. A second, more practical, explanation is that the national government may lack detailed information regarding the tastes and preferences of citizens residing in different parts of the country. See Benson, *supra* note 144, at 11-13 (centralized bureaucracy may have insufficient information). The informational problem could be solved, however, by administrative, rather than political decentralization.

¹⁶⁰ The correspondence between demand and supply of public goods is, of course, limited to "effective demand." Despite the significant need of their residents, many central cities are unable to afford adequate social services due to severely limited tax bases. See generally D. JUDD, *THE POLITICS OF AMERICAN CITIES: PRIVATE POWER AND PUBLIC POLICY* 198-253 (3d ed. 1988) (noting the restrictions on public budgets from smaller tax bases, inflation, and various other social and economic pressures); J. TEAFORD, *THE TWENTIETH-CENTURY AMERICAN CITY: PROBLEM, PROMISE, AND REALITY* 127-50 (1986) (detailing reasons for fiscal crises underlying the economies of

demand and supply will correspond in smaller juridical units indicates that provision of many public goods by states and local governments, rather than by the national government, furthers economic efficiency.¹⁶¹

The interaction between decentralized decision-making authority and citizen mobility also contributes to economic efficiency. According to an economic model developed by Tiebout,¹⁶² the ability of people to move to different jurisdictions creates a market for public goods. Based upon a set of "heroic"¹⁶³ assumptions, including perfect information, costless mobility, and the absence of external effects,¹⁶⁴ Tiebout argues

central cities); W. WILSON, *THE TRULY DISADVANTAGED: THE INNER CITY, THE UNDERCLASS, AND PUBLIC POLICY* (1987) (examining the decline of American cities and the changing class structure of American ghettos); Clark, *Fiscal Strain: How Different are Snow Belt Cities?* in *THE NEW URBAN REALITY* 253, 253-80 (P. Peterson ed. 1985); Netzer, *Financing Urban Government*, in *THE URBAN ECONOMY* 41, 41-56 (H. Hochman ed. 1976) (assessing the fiscal impact of changing demographics in urban areas); Peterson, *Finance*, in *THE URBAN PREDICAMENT* 35, 35-118 (W. Gorham & N. Glazer eds. 1976) (noting the problem of diminishing tax bases in cities with growing public needs); Rose-Ackerman, *Beyond Tiebout: Modeling the Political Economy of Local Government*, in *LOCAL PROVISION OF PUBLIC SERVICES: THE TIEBOUT MODEL AFTER TWENTY-FIVE YEARS* 55, 73 (G. Zodrow ed. 1983) ("[T]he fragmentation of metropolitan government systems has frequently been criticized because it permits wealthy people to cluster together and avoid paying taxes that provide benefits to low income people."); R. Nathan & C. Adams, *Four Perspectives on Urban Hardship* (Oct. 1988) (unpublished manuscript available from the authors).

¹⁶¹ See Benson, *supra* note 144, at 11. Cf. H. ROSEN, *supra* note 92, at 509 ("It is often argued that under a decentralized system . . . communities will provide the types and quantities of public goods desired by their inhabitants."). The argument that state and local decision-making authority encourages efficient provision of public goods does not necessarily require that this authority be constitutionally guaranteed. See W. OATES, *supra* note 159, at 17. At a minimum, to reap the benefits of decentralized service provision, states and localities must have the ability to raise revenue from their citizens and the power to decide how that revenue is spent. If efficient and responsive provision of public goods by decentralized government is a value to be protected from potential encroachment by the central government, a federal system that accords independent authority to sub-national governments is desirable. See Posner, *The Constitution As An Economic Document*, 56 GEO. WASH. L. REV. 4, 28 (1987) ("the Constitution guarantees a limited sovereignty to the states and thereby increases the likelihood that governmental services. . . will be provided efficiently."); cf. Macey, *Competing Economic Views of the Constitution*, 56 GEO. WASH. L. REV. 50, 65-67 (1987) (one difference between constitutional and ordinary legal rules is the former's durability); Tollison, *Public Choice and Legislation*, 74 VA. L. REV. 339, 346 (1988) (constitutional provisions are more durable than legislation). To the extent that local power is not subject to revocation, because it is constitutionally protected, citizens are more likely to support the level of taxation necessary to achieve an optimal level of public spending.

¹⁶² See Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416, 418 (1956).

¹⁶³ See Oates, *An Economist's Perspective on Fiscal Federalism*, in *THE POLITICAL ECONOMY OF FISCAL FEDERALISM* 7 (W. Oates ed. 1977).

¹⁶⁴ See Tiebout, *supra* note 162, at 419. The model also assumes: that consumers could choose to live in a large number of different communities; that their mobility is unhindered by employment considerations; and that communities below the optimum size will seek to attract new residents through mechanisms such as advertisement, whereas communities above or at optimum size will seek to discourage new residents by

that citizens are consumers who choose to reside in communities that provide their desired mix of public goods.¹⁶⁵ In effect, the existence of decentralized decision-making at the sub-national level permits individuals to "vote with their feet," selecting a package of taxes and services that is more likely to reflect their preferences than any probable combination offered by the national government.¹⁶⁶

b. *Federalism, the Courts, and the Political Process*

Discerning the appropriate relationship between states and the federal government has engendered substantial, persistent, and perhaps, inevitable conflict. Since the Constitution was ratified in 1787, courts have repeatedly been called upon to referee states' claims that the national government has overstepped its constitutional authority and interfered in matters of state authority.¹⁶⁷ Nevertheless, in the ensuing years the Supreme Court has been unable to develop a doctrine to define the nature of state powers, and the extent to which these powers are insulated from federal encroachment.¹⁶⁸

using techniques such as exclusionary zoning. *See id.* at 419-20.

¹⁶⁵ *See id.* at 418.

¹⁶⁶ *See id.* at 418, 420. Although Tiebout's model provides support for the existence of decentralized decision-making authority, not all of its implications are salutary. One outcome of such a system is that localities are likely to be economically homogeneous, utilizing public regulations such as exclusionary zoning to keep out low income households that would increase demand for public services, yet be unable to pay their full share of the cost. *See Oates, supra* note 163, at 7-9 (Tiebout solution implies a tendency toward segregation by income and use of exclusionary zoning).

Actions of states and localities have external effects, both negative and positive which may be difficult to internalize due to ill-defined property rights, high transaction costs and strategic bargaining. In these instances, a national government may be required to impose an efficient solution. *See W. OATES, supra* note 159, at 10-11; *see also* Inman & Rubinfeld, *A Federalist Constitution For An Imperfect World: Lessons From the United States* 23-24 (Jan. 1988) (unpublished manuscript available from the Institute for Law and Economics, Univ. of Pa.) (an expanded role for national government is justified when localities are unable to bargain effectively).

Finally, citizen mobility, so essential to efficient outcomes under the Tiebout model, may doom efforts by states and localities to redistribute income. *See W. OATES, supra* note 159, at 6-8 (redistribution at local level will cause influx of low income households and exodus of high income households); H. ROSEN, *supra* note 92, at 508 (same); Peterson & Rom, *The Case For A National Welfare Standard*, 6 BROOKINGS REV. 24, 29 (Winter 1988) (empirical evidence from the 1970's and 1980's shows that increased welfare benefits in states are correlated with higher poverty rates); Rose-Ackerman, *Cooperative Federalism and Co-optation*, 92 YALE L.J. 1344, 1345 (1983) ("[S]tate and local governments are poor instruments of redistributive policy.").

¹⁶⁷ Conversely, the federal government has also challenged state actions as interfering with federal authority. *See, e.g., McCulloch v. Maryland*, 17 U.S. (4 Wheat) 316 (1819) (state may not tax national bank).

¹⁶⁸ In recent years the Court has stopped trying to develop a set of rules to protect states from federal encroachment. Instead, the Court has adopted the view that the states must look to the political process, rather than judicial review, for protection. For

The source of this dilemma is the text of the Constitution. There can be no doubt that the Constitution presumes that the states will continue to exist and function as governing bodies.¹⁶⁹ However, the nature of the states' role in the federal system is, for the most part, undefined.¹⁷⁰ The powers to be exercised by the states are barely mentioned in the Constitution.¹⁷¹ The tenth amendment to the Constitution merely makes explicit what is implicit in the text of the Constitution: All powers not delegated to the national government are reserved for the states and the people.¹⁷² In contrast to the undefined nature of the states' role under the Constitution, the national government is the recipient of broad grants of power.¹⁷³

Despite the absence of explicit textual references to state powers, the rather meager protections against national encroachment and broad

a discussion of current Supreme Court doctrine on federalism, see *infra* text accompanying notes 186-201.

¹⁶⁹ See, e.g., U.S. CONST. art. I, § 2, cl. 1 (members of the House of Representatives shall be chosen by the people of the several states); art. I, § 2, cl. 3 (census shall be taken by state and Representatives apportioned by census); art. I, § 3, cl. 1 (Senate composed of two members from each state); art. II, § 1, cl. 2 (each state entitled to number of Electors to choose President equal to number of Representatives and Senators); art. III, § 2, cl. 2 (state may invoke original jurisdiction of Supreme Court); art. IV, § 4 (each state guaranteed a republican form of government, protection against invasion and, upon application, protection against domestic violence).

¹⁷⁰ The fact that the Constitution does not define state powers is unsurprising. At the time the Constitution was ratified, states and their colonial forebears had been functioning as governmental bodies for many years. Undoubtedly, the Framers expected state governments to continue providing public goods and services as they had under the Articles of Confederation, except in those cases in which the Constitution forbade state action, or gave powers exclusively to the national government. See *infra* note 174.

¹⁷¹ See, e.g., U.S. CONST. art. I, § 3, cl. 1 (states shall choose Senators) (later modified by 17th Amendment); art. II, § 1, cl. 2 (states shall appoint electors); art. V (states' role in ratifying constitutional amendments).

¹⁷² See U.S. CONST. amend X. The Constitution is more explicit in detailing certain actions that states may not take. For example, states may not enter into treaties or alliances, coin money, pass bills of attainder or ex post facto laws, impair the obligations of contract, grant titles of nobility, lay imposts or duties (except in limited circumstances), keep troops or ships of war in peacetime, engage in war unless invaded or in imminent danger, or enter into interstate or foreign compacts. See *id.* art. I, § 10.

¹⁷³ Among the enumerated powers are the power to regulate commerce, to tax, to borrow money, and to wage war. See U.S. CONST. art. I, § 8. The national government also is given the power "[t]o make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution." *Id.* at art. I, § 8, cl. 18. Moreover, pursuant to article VI, federal law is supreme, notwithstanding any state law to the contrary. See *id.*, at art. VI. The Constitution places some express limits on federal power over the states, most of which are designed to protect the states' territorial integrity and political representation in the national government. See, e.g., *id.* at art. I, § 8, cl. 16 (states may appoint and train officers of a militia that Congress may organize); *id.* at art. I, § 8, cl. 5 (states cannot be taxed on exports); *id.* at art. I, § 9, cl. 6 (Congress may not discriminate among state ports); *id.* at art. IV, § 3 cl. 1 (Congress may not join or divide states without their consent); *id.* at art. V (states shall not be denied equal suffrage in the Senate).

language regarding national powers, it is inconceivable that the Framers intended the role of the states to be defined solely according to the whims of the national government.¹⁷⁴ But as the nation grew, both economically and geographically, the activities of the national government likewise expanded, assisted by broad judicial interpretations of the powers specified in the Constitution.¹⁷⁵ It is perhaps not surprising that as the national government grew, the sphere of authority once thought to be reserved to the states, diminished. American intergovernmental relations, once characterized by the term "dual federalism,"¹⁷⁶ came to be more accurately described as "cooperative federalism."¹⁷⁷ Congress's power to regulate interstate commerce became the major judicial battle-

¹⁷⁴ See Scheiber, *American Federalism*, *supra* note 156, at 627. At the Constitutional Convention, the Virginia Plan, which would have made state legislation subject to national veto, failed to gain approval. See *supra* note 142.

In their writings advocating ratification of the Constitution, Madison and Hamilton argued that the national government would have limited powers, leaving to the states "inviolable sovereignty" over all other matters. See THE FEDERALIST NO. 39, at 245 (J. Madison) (C. Rossiter ed. 1961). See also THE FEDERALIST NO. 9, *supra*, at 76 (J. Hamilton) (writing that proposed Constitution leaves exclusive sovereign powers to states); THE FEDERALIST NO. 45, *supra*, at 292 (J. Madison) ("The powers delegated by the proposed Constitution to the Federal Government are few and defined. Those which are to remain in the State Governments are numerous and indefinite."); R. BERGER, *FEDERALISM: THE FOUNDERS' DESIGN* 59-61 (1987) (discussing Madison and Hamilton's writings as envisioning dual federalism). But see Soifer, *Truisms That Never Will Be True: The Tenth Amendment And the Spending Power*, 57 U. COLO. L. REV. 793, 808 (1986) (asserting that THE FEDERALIST was "obviously and purposefully ambiguous on basic issues of federalism").

¹⁷⁵ See, e.g., *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 194 (1824) (commerce clause); *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 324-25 (1819) (necessary and proper clause).

¹⁷⁶ Dual federalism included constitutional doctrines based on the principles that: 1) the national government is one of enumerated powers only, 2) within their respective spheres, states and the national government are sovereign and co-equal, and 3) the relationship between states and the national government is one of tension, rather than collaboration. See Corwin, *The Passing of Dual Federalism*, 36 VA. L. REV. 1, 3-4 (1950); Scheiber, *American Federalism*, *supra* note 156, at 628; Sundquist, *American Federalism: Evolution, Status and Prospects*, 19 URB. LAW. 701, 715 (1987). For examples of Supreme Court decisions applying concepts of dual federalism, see *Ableman v. Booth*, 62 U.S. (21 How.) 506, 516 (1858); *McCulloch*, 17 U.S. (4 Wheat.) at 410. Commentators frequently have used the metaphor of a layer cake to describe dual federalism — the powers of each level of government being separate and distinct. See, e.g., Scheiber, *Federalism and Legal Process: Historical and Contemporary Analysis of the American System*, 14 L. & SOC'Y REV. 663, 670-71 (1980) (discussing the descriptive validity of the "layer-cake" metaphor for American federalism).

¹⁷⁷ Cooperative federalism depicts a system in which the nation and the states collaborate with each other and share resources to achieve public objectives. Public functions are not carried out by only one government, as is typically implied by the concept of dual federalism. See Elazar, *The Shaping of Intergovernmental Relations In The Twentieth Century*, in THE POLITICS OF AMERICAN FEDERALISM 20 (D. Elazar ed. 1969). In contrast to the layer cake metaphor associated with dual federalism, cooperative federalism makes use of a different confectionery metaphor — the marble cake. See Grodzins, *The Sharing of Functions*, in THE POLITICS OF AMERICAN

ground¹⁷⁸ between the states and the national government.¹⁷⁹

Prior to 1937, private litigants had met with some success in overturning federal regulatory legislation on the ground that it interfered in areas over which the states had exclusive authority. Supreme Court decisions rejected federal attempts to prevent monopolization of manufacturing¹⁸⁰, to ban the products of child labor,¹⁸¹ and to regulate the wages and hours of workers,¹⁸² on the ground that these activities were not part of interstate commerce. Nevertheless, after tremendous controversy, including the furor surrounding President Roosevelt's court-packing plan,¹⁸³ the continued dislocation and unrest created by the Great Depression, and a change in court personnel, the Supreme Court eventually upheld federal legislation regulating wages and working

FEDERALISM, *supra* at 12 ("As colors are mixed in the marble cake, so functions are mixed in the American federal system.").

¹⁷⁸ The relationship between the states and the nation also changed dramatically as a result of the Civil War. Not only did the Union's victory over the Confederacy eliminate nullification and secession as viable legal doctrines, *see* E. POWELL, NULLIFICATION AND SECESSION IN THE UNITED STATES, 375-76 (1897) (asserting that the Civil War established the dissolubility of the Union, except by revolution), but the post-war constitutional amendments set the framework for national legislation to protect individual rights. *See, e.g.*, Voting Rights Act of 1965, 42 U.S.C. §§ 1971-1974 (1982 & Supp. III 1985); Civil Rights Act, 42 U.S.C. §§ 1981-2000h-6 (1982 & Supp. III 1985). In addition, most of the rights contained in the first eight amendments to the Constitution have been made applicable against the states by incorporation into the fourteenth amendment. *See, e.g.*, *Klopper v. North Carolina*, 386 U.S. 213 (1967) (speedy trial); *Malloy v. Hogan*, 378 U.S. 1 (1964) (freedom from self-incrimination); *Gideon v. Wainwright*, 372 U.S. 335 (1963) (right to counsel); *Mapp v. Ohio*, 367 U.S. 643, 660 (1961) (freedom from unreasonable searches and seizures); *Everson v. Board of Educ.*, 330 U.S. 1, 5-8 (1947) (establishment clause); *Cantwell v. Connecticut*, 310 U.S. 296, 306-07 (1940) (free exercise clause); *Gitlow v. New York*, 268 U.S. 652, 670-72 (1925) (freedom of speech and press); *Chicago B. & Q. R.R. v. Chicago*, 166 U.S. 226, 228 (1897) (just compensation for takings).

¹⁷⁹ Conflicts over the nature of the relationship between states and the federal government also have involved issues of sovereign immunity and judicial abstention. *See, e.g.*, *Edelman v. Jordan*, 415 U.S. 651 (1974) (eleventh amendment sovereign immunity); *Younger v. Harris*, 401 U.S. 37, 41, 44 (1971) (federal abstention based upon principles of "Our Federalism").

¹⁸⁰ *United States v. E.C. Knight Co.*, 156 U.S. 1 (1895).

¹⁸¹ *Hammer v. Dagenhart*, 247 U.S. 251 (1918), *overruled*, *United States v. Darby*, 312 U.S. 100 (1941).

¹⁸² *Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935).

¹⁸³ After several elements of President Roosevelt's New Deal legislation had been struck down by the Supreme Court on the ground that they exceeded federal power, *see* *Carter v. Carter Coal Co.*, 298 U.S. 238 (1936) (Bituminous Coal Conservation Act of 1935); *United States v. Butler*, 297 U.S. 1 (1936) (Agricultural Adjustment Act); *Schechter Poultry*, 295 U.S. at 495 (National Industrial Recovery Act), Roosevelt submitted a plan to Congress to "reform" the court system. He alleged the court system was inefficient, partly due to "aged or infirm judges." W. LEUCHTENBURG, FRANKLIN D. ROOSEVELT AND THE NEW DEAL 233 (1963). Under the proposed program the President would have been empowered to appoint as many as six new judges to the Supreme Court and forty-four new judges to the lower federal courts. The proposed legislation failed to pass Congress. *See id.* at 232-38.

conditions. In *United States v. Darby Lumber Co.*¹⁸⁴ the Court greatly expanded the authority of the federal government, holding that Congress could regulate intrastate activities which affected interstate commerce.¹⁸⁵

The Court again considered the appropriate relationship between states and the federal government in 1985. In *Garcia v. San Antonio Metropolitan Transit Authority*,¹⁸⁶ the Court held that Congress could, pursuant to the commerce clause, extend the minimum wage and maximum hour provisions of the Fair Labor Standards Act to employees of a public transit authority, despite the transit authority's legal status as a local public body.¹⁸⁷ The Court observed that the "principal means chosen by the Framers to ensure the role of the States in the federal system lies in the structure of the Federal Government itself."¹⁸⁸ Citing

¹⁸⁴ 312 U.S. 100 (1941).

¹⁸⁵ The Court noted that the tenth amendment did not constitute an independent limitation of federal power: "Our conclusion is unaffected by the Tenth Amendment. . . . The amendment states but a truism that all is retained which has not been surrendered." *Id.* at 123-24.

Since *Darby* was decided in 1941, the Supreme Court has struck down federal legislation on the ground that it exceeded the federal power to regulate interstate commerce only once. In *National League of Cities v. Usery*, 426 U.S. 833 (1976), *overruled*, *Garcia v. San Antonio Metro. Transit Auth.*, 469 U.S. 528 (1985), the Court held that the 1974 amendments to the Fair Labor Standards Act ("FLSA") violated the Constitution. Under the FLSA amendments, local governments were required to observe federally prescribed minimum wage and maximum hour guidelines. Although the Court recognized that the type of regulation contained in the FLSA was within the commerce power, it drew a distinction between regulating private citizens and the "States as States." *National League of Cities*, 426 U.S. at 845. According to the Court, "there are attributes of sovereignty attaching to every state government which may not be impaired by Congress . . . because the Constitution prohibits it from exercising the authority in that manner." *Id.* Under the *National League of Cities* regime, the Court developed a three-prong test to determine whether federal regulation was valid. *See Hodel v. Virginia Surface Mining & Reclamation Ass'n*, 452 U.S. 264, 287-88 (1981). To be invalidated the statute must: 1) regulate the "States as States," 2) address matters that are indisputably attributes of state sovereignty, and 3) it must be apparent that compliance by the states would directly impair their ability to "structure integral operations in areas of traditional governmental functions." *See id.* at 288 (quoting *National League of Cities*, 426 U.S. at 852).

Nine years after *National League of Cities* was decided, the Supreme Court overturned the decision. In *Garcia*, the Court concluded that making state immunity from federal regulation turn on judicial appraisal of whether a particular governmental function is "integral" or "traditional" was "unsound in principle and unworkable in practice." *Garcia*, 469 U.S. at 546-47.

¹⁸⁶ 469 U.S. 528 (1985).

¹⁸⁷ The minimum wage and maximum hour provisions of the FLSA challenged in *Garcia* were similar to those struck down in *National League of Cities*. *See supra* note 185.

¹⁸⁸ *Garcia*, 469 U.S. at 550. The Court cited portions of THE FEDERALIST to support its contention that states would be protected by the structure of the United States government. *See id.* at 551-52 (citing Madison's statement that the equal representation of states in the Senate was "at once a constitutional recognition of the portion

scholarly works by Choper¹⁸⁹ and Wechsler,¹⁹⁰ the Court catalogued several ways in which the structure of the federal government protected the states from overreaching by the national government, including the states' control over electoral qualifications, their role in the Electoral College, and their equal representation in the United States Senate.¹⁹¹

After establishing that the Constitution builds protections for states into the federal system, the Court concluded that "the fundamental limitation that the constitutional scheme imposes on the commerce clause to protect the 'States as States' is one of process rather than one of result."¹⁹² In effect, the Court held in *Garcia* that the states may not look to the judicial branch to protect their constitutional status, but must instead rely upon the structure of the federal system.¹⁹³ Nevertheless, the Court stopped short of holding that all issues of federalism are non-justiciable. The Court noted that "[a]ny substantive restraint on the exercise of commerce clause powers must find its justification in the procedural nature of this basic limitation, and must be tailored to compensate for possible failings in the national political process. . . ."¹⁹⁴ The Court also implied that some affirmative limits on federal action affecting states under the commerce clause might exist,¹⁹⁵ but explicitly

of sovereignty remaining in the individual States, and an instrument for preserving that residuary sovereignty." THE FEDERALIST NO. 62, at 378 (J. Madison) (C. Rossiter ed. 1961)).

¹⁸⁹ See *Garcia*, 469 U.S. at 551 n.11 (citing J. CHOPER, JUDICIAL REVIEW AND THE NATIONAL POLITICAL PROCESS 175-84 (1980)) [hereinafter J. CHOPER, JUDICIAL REVIEW].

¹⁹⁰ See *Garcia*, 469 U.S. at 551 n.11 (citing Wechsler, *The Political Safeguards of Federalism: The Role of the States in the Composition and Selection of the National Government*, 54 COLUM. L. REV. 543 (1954)).

¹⁹¹ *Garcia*, 469 U.S. at 551. In addition to those safeguards listed by the Supreme Court in *Garcia*, Choper included the following among his list of structural protections: 1) each state has at least one representative in the House of Representatives, 2) state legislatures draw district lines, 3) state delegations to Congress typically work together and assist each other in getting advantageous committee assignments, 4) members of Congress typically serve in state or local government prior to running for national office, and therefore, are sensitive to state concerns, 5) the President typically is obligated to some degree to state and local parties for their help in the presidential election campaign, and 6) states and local governments have organized effective lobbying organizations. See J. CHOPER, JUDICIAL REVIEW, *supra* note 189, at 176-81.

¹⁹² *Garcia*, 469 U.S. at 554.

¹⁹³ In *Garcia*, the Court adopted much of the reasoning of Choper and Wechsler regarding the role of the courts in determining questions of federalism. See J. CHOPER, JUDICIAL REVIEW, *supra* note 189, at 175 ("[T]he constitutional issue of whether federal action is beyond the authority of the central government and thus violates 'states' rights' should be treated as nonjusticiable"); Wechsler, *supra* note 190, at 559 ("[T]he Court is on weakest ground when it opposes its interpretation of the Constitution to that of Congress in the interest of the states. . . .").

¹⁹⁴ *Garcia*, 469 U.S. at 554.

¹⁹⁵ See *id.* at 556. The Court cited *Coyle v. Oklahoma*, 221 U.S. 559 (1911), in support of its statement that affirmative limits on federal action might exist. See *Gar-*

refrained from identifying those limits.¹⁹⁶

In a 1988 decision, *South Carolina v. Baker*,¹⁹⁷ the Court elaborated on the types of failings of the national political process that might justify judicial intervention to protect states from federal encroachment. In rejecting South Carolina's tenth amendment challenge to a federal tax law that subjected the interest earned on certain state and local bonds to taxation,¹⁹⁸ the Court reiterated its holding in *Garcia* that

cia, 469 U.S. at 556. In *Coyle*, the Court examined whether Congress could, in admitting a state into the Union, require that its capital be located in a particular city for a temporary period of time. The Court held that a state at the time of admission could not be treated unequally with respect to existing states. Since an existing state could not be forced by Congress to locate its capital in a city not of its choosing, *see Coyle*, 221 U.S. at 565, neither could a newly admitted state. *See id.* at 579. The Court noted that the United States "was and is a union of States, equal in power, dignity and authority, each competent to exert that residuum of sovereignty not delegated to the United States by the Constitution itself." *Id.* at 567.

¹⁹⁶ The majority decision in *Garcia* elicited sharp criticism from four dissenting Justices. Justice Powell wrote that "[t]he Court's action reflects a serious misunderstanding, if not an outright rejection, of the history of our country and the intention of the Framers of the Constitution." 469 U.S. at 577 (Powell, J., dissenting). Justice Powell argued that in limiting judicial review of federalism issues the majority violated the principle set forth in *Marbury v. Madison*, 5 U.S. (1 Cranch) 137 (1803), that it is "the settled province of the federal judiciary 'to say what the law is' with respect to the constitutionality of Acts of Congress." *Garcia*, 469 U.S. at 567 (quoting *Marbury*). In addition, Powell cast doubt on the majority's contention that the structure of the federal government would provide sufficient protection for the states. He wrote that changes which have taken place in the twentieth century, including the adoption of the seventeenth amendment providing for the direct election of Senators, "have made Congress increasingly less representative of state and local interests, and more likely to be responsive to the demands of various national constituencies." *Id.* at 565 n. 9. For additional examples of changes that have weakened the influence of states on Congress, *see* Howard, *Garcia and the Values of Federalism: On the Need for a Recurrence to Fundamental Principles*, 19 GA. L. REV. 789, 793 (1985); Kaden, *supra* note 151, at 860-68. For scholarly critiques of the *Garcia* decision, *see* generally Howard, *Garcia: Of Federalism and Constitutional Values*, 16 PUBLIUS: THE JOURNAL OF FEDERALISM 17, 31 (Summer 1986) ("[N]o branch of government should be the ultimate and unfettered judge of its own powers."); Redish and Drizin, *Constitutional Federalism and Judicial Review: The Role of Textual Analysis*, 62 N.Y.U. L. REV. 1, 14 (1987) (the Constitution "inescapably reveals the assumption that the states required at least a certain degree of counter-majoritarian constitutional protection"); Van Alstyne, *The Second Death of Federalism*, 83 MICH. L. REV. 1709, 1732 (1985) (*Garcia* treats the Constitution as "not a Constitution as Law, but a constitution of more ordinary politics"). *But see* Choper, *Law Before and After Garcia*, in PERSPECTIVES ON FEDERALISM: PAPERS FROM THE FIRST BERKELEY SEMINAR ON FEDERALISM 23, 23 (H. Scheiber ed. 1987) (*Garcia* decision was a "welcome surprise"); Field, *Garcia v. San Antonio Metropolitan Transit Authority: The Demise of A Misguided Doctrine*, 99 HARV. L. REV. 84, 103-06 (1985) (approving the overruling of *National League of Cities*).

¹⁹⁷ 108 S. Ct. 1355, *reh'g denied*, 108 S. Ct. 2837 (1988).

¹⁹⁸ In *South Carolina v. Baker*, the Court upheld federal legislation that removes the federal income tax exemption for interest earned on publicly offered long-term bonds issued by states and localities, unless those bonds are issued in registered form. *See id.* at 1368-69. Interest earned on debt obligations of states and local governments

states must find their protection from federal regulation through the political process.¹⁹⁹ The Court further stated that "some extraordinary defects in the national political process" might render regulation invalid under the tenth amendment.²⁰⁰ Nevertheless, the Court noted that "South Carolina has not even alleged that it was deprived of any right to participate in the national political process or that it was *singled out in a way that left it politically isolated and powerless*."²⁰¹ By implication, the Court indicated that states could challenge federal incursions on their authority in federal court if they could show that they had somehow been excluded or politically isolated in the deliberation and enactment process.

c. *Intergovernmental Takings and the Political Process*

The strongest justification for a constitutional rule requiring compensation for intergovernmental takings derives from the principles of federalism. States and localities serve important, if controversial, functions in our political system. The existence of independent state decision-making power protects citizens from a potentially oppressive national government, provides numerous forums for citizen participation in governance, increases the number of opportunities for innovative policy making, and promotes efficient and responsive delivery of some, though not all, public goods. Uncompensated intergovernmental takings could disrupt the ability of states and localities to function as governmental bodies and interfere with their ability to provide public goods and services. In addition, the absence of a constitutionally mandated compensation requirement would enable factions to gain control of the national government and utilize the power of eminent domain to exploit the wealth of certain states. In a particularly bleak scenario,²⁰²

is typically not taxable to the recipient. For a further discussion of *South Carolina v. Baker* and the doctrine of intergovernmental tax immunity, see *infra* note 231.

For purposes of deciding the state's tenth amendment claim, the Court treated the federal legislation as directly regulating states by prohibiting the issuance of bearer bonds. See *Baker*, 108 S. Ct. at 1360. A "bearer bond" is an unregistered debt obligation which entitles the holder to principal and interest payments. See *id.* at 1358.

¹⁹⁹ See *id.* at 1360.

²⁰⁰ *Id.*

²⁰¹ *Id.* at 1361 (emphasis added).

²⁰² Throughout this section the scenario of regional conflict and exploitation will be used to justify a rule requiring compensation for all intergovernmental takings. I am mindful of Justice Frankfurter's observation in *New York v. United States*, 326 U.S. 572, 583 (1946), that "[t]he process of Constitutional adjudication does not thrive on conjuring up horrible possibilities that never happen in the real world and devising doctrines sufficiently comprehensive in detail to cover the remotest contingency." American interregional conflict and prejudice, unfortunately, is not merely a fanciful hypothetical devised by a law school professor to illustrate an abstruse point. To the con-

groups of states or regions could coalesce and utilize this ability to disrupt state and local governments to oppress citizens from other states and regions.

One inherent characteristic of intergovernmental takings — their particularity — makes their intrusiveness especially problematic. Unlike most types of federal regulation,²⁰³ intergovernmental takings rarely, if ever, apply to large numbers of states; instead, takings single out one state at a time. Thus, even if one were to accept the precepts of *Garcia*, a judicial rule of compensation would be justified. Due to the particularized nature of intergovernmental takings, states and localities could not rely upon the political process to protect themselves from oppression by other states.²⁰⁴ This potential failure of the political process could largely be remedied by an appropriate constitutional compensation requirement.

Even if compensation were not already required by federal courts, it is unlikely that the adoption of such a rule would disrupt the federal government. To the contrary, with respect to condemnations undertaken for *benign* motives, it is likely that Congress, itself, would adopt a practice of universal compensation. In recent years, political economists have developed models to explain legislative behavior regarding distributive policy in majority rule institutions.²⁰⁵ Typically these mod-

trary, this nation has repeatedly experienced regional conflict since its founding. See *supra* text accompanying notes 145-47. For a discussion of the recent resurgence of regionalism, see *infra* notes 235-37 and accompanying text.

Furthermore, in *New York v. United States*, Justice Frankfurter, himself, proposed a rule that, by necessity, was overinclusive in application. In order to prevent possible federal incursions into state activities, Frankfurter argued that any direct tax on states could not discriminate against states, but must fall on private individuals as well. 326 U.S. at 582. Like a compensation requirement for intergovernmental takings, prohibiting discriminatory taxation stops or impedes the national government from taking certain actions, even though its motives in any particular action might be innocent, and the effect on the states, benign. To protect against possible, if not likely, abuses, an overinclusive prophylactic rule is required. Cf. Blasi, *The Pathological Perspective and the First Amendment*, 85 COLUM. L. REV. 449, 450 & n.1 (1985) (arguing that the federalism system should be informed by the "pathological perspective"). For further discussion of the nondiscrimination principle set forth in *New York v. United States*, see *infra* note 231.

²⁰³ But see *South Carolina v. Katzenbach*, 383 U.S. 301 (1966) (upholding the Voting Rights Act against a claim that certain provisions were targeted against a small number of states); Neuman, *supra* note 40, at 344 (1987) (observing that frequently "federal law varies from state to state").

²⁰⁴ Cf. Choper, *Law Before and After Garcia*, *supra* note 196, at 20 (admitting that the desires of certain regions will periodically be "submerged" in Congress); Redish & Drizin, *supra* note 196, at 38-39 (political process may be insufficient to protect a minority of states).

²⁰⁵ A distributive policy is one that confers benefits unequally to discrete portions of the country. Examples of distributive programs include public works programs and military installations. See Weingast, *A Rational Choice Perspective On Congressional*

els assume that: 1) legislators represent discrete geographic districts, 2) their primary motive is to win reelection, 3) they believe that programs which benefit their district will improve their chance for reelection, and 4) the cost of federal programs will be paid for by general taxation.²⁰⁶ Early models of legislative behavior typically indicated that legislators would maximize their districts' benefits and minimize the cost to their constituents by forming coalitions with a bare majority to pass public works programs.²⁰⁷ Forming "minimum winning coalitions"²⁰⁸ enabled the smallest number of districts to maximize their benefits from federal programs, while spreading the costs to losers as well as winners.²⁰⁹ Minimum winning coalitions were expected to be unstable over time, with new ones periodically forming.²¹⁰

Empirical studies have consistently shown that the model of minimum winning coalitions does not accurately portray how Congress operates. To the contrary, most studies show that congressional distributive programs are broadly inclusionary — containing benefits for the districts of many more members of Congress than would be necessary to secure passage of the legislation.²¹¹ The tendency to include benefits for all congressional districts in legislation is referred to as "universalism."²¹² Explanations of universalism center around the concept of un-

Norms, 23 AM. J. POL. SCI. 245, 246 (1979).

²⁰⁶ See J. BUCHANAN & G. TULLOCK, *supra* note 107, at 18 ("[T]he economic assumption is simply that the representative or the average individual . . . will choose 'more' rather than 'less.'"); Fiorina, *Universalism, Reciprocity, and Distributive Policymaking in Majority Rule Institutions*, in 1 RESEARCH IN PUB. POLICY ANALYSIS & MGMT. 197, 204 (J. Crene ed. 1981) (the district's tax share is exogenous to project approval; legislators are primarily interested in reelection, and chances for reelection increase with district benefits).

²⁰⁷ See J. BUCHANAN & G. TULLOCK, *supra* note 107, at 139; W. RIKER, *THE THEORY OF POLITICAL COALITIONS* 247-78 (1962). But see B. BARRY, *POLITICAL ARGUMENT* 253-56 (1965) (participants in political process will reach a "reasonable solution" to ensure victory rather than rely on stable minimum winning coalitions).

²⁰⁸ W. RIKER, *supra* note 207, at 270.

²⁰⁹ In effect, states or districts not included in a particular minimum winning coalition were exploited since they were excluded from receiving federal benefits, but nonetheless were forced to pay for them.

²¹⁰ See J. BUCHANAN & G. TULLOCK, *supra* note 107, at 152 ("[A]ny single winning coalition will be relatively unstable and impermanent."). As Shepsle and Weingast note, unstable minimum winning coalitions create "a kind of over-time universalism in which legislators take turns as members of the victorious MWC [minimum winning coalition]" Shepsle & Weingast, *Political Preferences For The Pork Barrel: A Generalization*, 25 AM. J. POL. SCI. 96, 97 (1981). For a discussion of "universalism," see sources cited in *infra* note 212.

²¹¹ See, e.g., J. FERREJOHN, *supra* note 80, at 247 ("[M]ore than a bare majority of congressional districts . . . and states received benefits from [water] projects in a given year."); D. MAYHEW, *CONGRESS: THE ELECTORAL CONNECTION* 88 (1974) (members of Congress follow policy of universalism).

²¹² See Fiorina, *supra* note 206, at 198; Weingast, *supra* note 205, at 249. See generally, Cox & Tuttle, *Universalism and Allocative Decision Making in the Los An-*

certainty. Each legislator is uncertain whether she will be included in a particular minimum winning coalition. Rather than be faced with the prospect of going back to her constituents with no benefits and a bill for programs benefiting other districts, a legislator will tend to vote for certain benefits for all, as well as certain costs.²¹³ Inclusion can be seen as a form of insurance.²¹⁴

Although the model of universalism was developed to explain legislative behavior with respect to the distribution of benefits, its central insight is likely to be applicable to the distribution of concentrated costs,²¹⁵ such as intergovernmental takings. A legislator is likely to be

geles County Board of Supervisors, 46 J. POL. 548 (1984) (discussing universalism in Los Angeles county); Niou & Ordeshook, *Universalism in Congress*, 29 AM. J. POL. SCI. 246 (1985) (discussing universalism as an optimal model for individual legislators); Shepsle & Weingast, *supra* note 210 (extending universalism to pork-barrel politics).

²¹³ See Cox & Tutt, *supra* note 212, at 551-54 (legislators will tend to vote for benefits in an inclusionary fashion to insure against being in the minority and receiving no benefits); Fiorina, *supra* note 206, at 209-11 (arguing that universalism is in the long-term self-interest of the legislators); Niou & Ordeshook, *supra* note 212, at 256 (according to game theory, a strategy based on universalism will become the "preferred legislative norm given each legislator's goal of reelection"); Shepsle & Weingast, *supra* note 210, at 107-10 (universalism is a hedge against the uncertainty of not being in a MWC); Weingast, *supra* note 205, at 249-52 (demonstrating mathematically that the legislator's expected benefits of following a universalist approach exceed the expected payoffs from a minimum winning coalition approach).

²¹⁴ Cf. Shepsle & Weingast, *supra* note 210, at 109 (universalism is "insurance-like").

²¹⁵ Recent legislation enacted to deal with the problem of disposing of high level nuclear waste illustrates the likelihood that Congress would adopt a universal approach in distributing geographically concentrated burdens. For many years, federal policy makers have grappled with the need to locate disposal sites for highly radioactive waste generated by nuclear power plants, scientific research, and national defense activities. For obvious reasons, past proposals to locate disposal sites in particular states have been greeted by intense controversy, litigation, and political pressure. See J. SELEY, *THE POLITICS OF PUBLIC-FACILITY PLANNING* 87-112 (1983); Kneese, *Typical Cases Involving Natural Resources*, in *REGIONAL CONFLICT AND NATIONAL POLICY* 76-84 (K. Price ed. 1982). In 1983, Congress enacted the Nuclear Waste Policy Act of 1982, which established a framework for selecting disposal sites and provided for state consultation and cooperation. See Pub. L. No. 97-425, 96 Stat. 2201 (codified as amended at 42 U.S.C. §§ 10101 to 10226 (1982 & West Supp. 1988)). The legislation also provided that an affected state could veto site selection subject to congressional override. Despite these procedures for safeguarding state interests, the program continued to engender controversy. See Montange, *Federal Nuclear Waste Disposal Policy*, 27 NAT. RESOURCES J. 309, 376-405 (1987) (criticizing federal regulatory efforts to contain the hazards of spent nuclear fuel).

In 1987, the Nuclear Waste Policy Amendments Act of 1987, Pub. L. No. 100-203, §§ 5001-5604, 101 Stat. 1330-227 to 255 (1987) (codified at 42 U.S.C. §§ 10101 to 10222 (West Supp. 1988)), designated a site in the Yucca Mountains of Nevada as the first disposal site. The legislation also added a new provision designed to cushion the impact of selecting the Nevada site and future disposal sites. Each Indian tribe on whose reservation a site is located or state in which a site is located will be entitled to substantial "benefits" ranging from five to twenty million dollars each year the disposal facility is operated. See Pub. L. No. 100-203, at § 5031, 101 Stat. 1330-238. The

uncertain whether public property in her district or state will be required by the federal government. Rather than take the chance of being forced to explain to her constituents why she could not forestall the harm, a rational²¹⁶ legislator might prefer to adopt a universal rule of compensation for intergovernmental takings.²¹⁷ Each legislator would support marginally increased taxes, in return for insurance against the risk of uncompensated takings of public property in her district.

While the political process might be sufficient to protect states from random or benign takings, it is highly unlikely to protect states or localities from *exploitative* intergovernmental takings. A universal practice of compensation would almost certainly not be extended to takings designed to exploit individual states or groups of states. Providing compensation to such states would raise the cost of exploitative behavior to states in control of the legislative process, and lessen the disruption to the states in which condemnations occurred. Provided that the coalition of states in power could assure themselves against defections,²¹⁸ a compensation rule would be self-defeating.

The proposition that states require constitutional, rather than merely legislative, protection from the threat of regionalism is implicit in the Constitution. Among the constitutional provisions designed to protect states from discriminatory treatment at the hands of the national political process, the tax uniformity clause²¹⁹ is most relevant to

benefits authorized by the Nuclear Waste Policy Amendments Act are consistent with an extension of the norm of universalism to geographically concentrated burdens as well as benefits. Members of Congress, uncertain as to where a facility might be located in the future, agree *ex ante* to compensate each other's constituents for a burden they might each have to bear.

²¹⁶ A legislator who is risk averse would be even more likely to support a universal compensation rule than would a risk neutral legislator. *Cf.* Weingast, *supra* note 205, at 252 ("Risk averse legislators . . . favor reductions in their risk of defeat.").

²¹⁷ The precise mechanics of a universal practice of compensation for intergovernmental takings may depend upon which branch of government makes the ultimate selection of the specific parcels of property to be condemned. For condemnations specifically authorized by legislation, *see, e.g.,* *United States v. 929.70 Acres of Land*, 205 F. Supp. 456, 457 (D.S.D. 1962) (Congress expressly or impliedly included property within authorization statute by specifically mentioning it in legislative reports.), Members of Congress would likely develop an informal norm of logrolling, including in each statute compensation for state or local condemnees. Because Members of Congress would frequently delegate the choice of particular parcels of property to administrative agencies, *see, e.g.,* *United States v. Carmack*, 329 U.S. 230, 242-43 (1946) (choice of specific parcel to be condemned left to the discretion of administrative agency), it is also likely that legislation would be enacted to provide for uniform compensation for all state or local property so selected.

²¹⁸ One can imagine numerous situations in which legislators could not be persuaded or "bribed" to cease exploiting other states or regions. Animosities between regions over economic development and racial or ethnic populations could make legislators resistant to defection.

²¹⁹ U.S. CONST. art. I, § 8, cl. 1.

the problem of intergovernmental takings.²²⁰ A taking is, in many ways, analogous to a tax — both require the owner of wealth or property to donate a portion of her assets to the government for public use.²²¹ In addition, both the tax uniformity clause and a compensation requirement for intergovernmental takings are designed to protect entities and individuals from being invidiously singled out for discriminatory treatment by the national political process.

The tax uniformity clause requires that "all Duties, Imposts and Excises shall be uniform throughout the United States."²²² The Court has interpreted the clause to apply to indirect taxes, including most sources of federal revenue other than the income tax.²²³ According to a recent Supreme Court case, the clause was included in the Constitution to prohibit Congress from discriminating against particular states:

Some States [at the Constitutional Convention] . . . remained apprehensive that the regionalism that had marked the Confederation would persist. There was concern that the National Government would use its power over commerce to the disadvantage of particular States. The Uniformity Clause was proposed as one of several measures designed to limit the exercise of that power.²²⁴

²²⁰ Among the other constitutional provisions preventing federal discrimination among states are the bankruptcy and naturalization uniformity clause, U.S. CONST. art. I, § 8, cl. 4, and the port preference clause, art. I, § 9, cl. 6. *See also* Coyle v. Smith, 221 U.S. 559, 565-68 (1911) (equal footing doctrine with respect to admission of new states under art. IV, § 3, cl. 1).

²²¹ *Cf.* R. EPSTEIN, *supra* note 44, at 283-305 (various forms of taxation are takings).

²²² U.S. CONST. art. I, § 8, cl. 1.

²²³ The Constitution requires that direct taxes be apportioned among the states. U.S. CONST. art. I, § 2, cl. 3; art. I, § 9, cl. 4. Prior to 1895, the Supreme Court interpreted direct taxes to include only capitation taxes and taxes on real estate. *See, e.g.,* Springer v. United States, 102 U.S. 586 (1880) (Civil War income tax is not a direct tax); *Veazie Bank v. Fenno*, 75 U.S. (8 Wall.) 533 (1869) (duty on state bank notes is indirect tax). Nevertheless, in *Pollock v. Farmers' Loan & Trust*, 158 U.S. 429 (1895), the Court held that a tax on income was a direct tax and thereby unconstitutional because it was not apportioned. 158 U.S. at 634-35. In 1913, the Sixteenth Amendment effectively reversed *Pollock* by empowering the United States to tax incomes without apportionment. *See* 1 R. ROTUNDA, J. NOWAK & J. YOUNG, *TREATISE ON CONSTITUTIONAL LAW: SUBSTANCE AND PROCEDURE* § 5.3 (1986) (historical background and current status of direct versus indirect taxes); Annotation, *Supreme Court's View as to Constitutionality of Federal Tax Legislation Under Uniformity Clause of Article I, § 8, Clause 1 of Federal Constitution*, 76 L. Ed. 2d 868 (1985) (analyzing the cases in which the Supreme Court has construed the uniformity clause).

²²⁴ *United States v. Ptasynski*, 462 U.S. 74, 81 (1983) (citation omitted). The Court continued its discussion of the purpose of the tax uniformity clause by quoting from Justice Story:

[The purpose of the clause] was to cut off all undue preferences of one State over another in the regulation of subjects affecting their common

In *United States v. Ptasynski*,²²⁵ the Court stressed the importance of preventing discrimination against individual states. The respondent in *Ptasynski* had challenged the Crude Oil Windfall Profit Tax Act of 1980²²⁶ on the ground that it exempted certain oil produced in particular geographic areas, primarily in Alaska. The Court stated that "a 'tax is uniform when it operates with the same force and effect in every place where the subject of it is found.'"²²⁷ Congress may define the subject of a tax in geographic terms, but its choice will be examined "closely [by the Court] to see if there is actual geographic discrimination."²²⁸ The Court upheld the exemption, noting that it was supported by valid policy objectives,²²⁹ and that it was not coterminous with state political boundaries.²³⁰ Thus, in the *Ptasynski* decision, the Supreme Court reiterated the importance of constitutional doctrine protecting states from being discriminated against by the national government.²³¹

interests. Unless duties, imposts, and excises were uniform, the grossest and most oppressive inequalities, vitally affecting the pursuits and enjoyments of the people of different States, might exist. The agriculture, commerce, or manufactures of one State might be built up on the ruins of those of another; and a combination of a few States in Congress might secure a monopoly of certain branches of trade and business to themselves, to the injury, if not to the destruction, of their less favored neighbors." 1 J. Story, *Commentaries on the Constitution of The United States* § 957 (T. Cooley ed. 1873).

462 U.S. at 81.

²²⁵ 462 U.S. 74 (1983).

²²⁶ 26 U.S.C. §§ 4986-4998 (1982 & Supp. IV 1986).

²²⁷ 462 U.S. at 82 (quoting *Head Money Cases*, 112 U.S. 580, 594 (1884)).

²²⁸ *Id.* at 85.

²²⁹ Among the rationales cited by the Court for the exemption were the higher cost of oil production in arctic and sub-arctic regions caused by severe weather, remoteness, and geological and environmental conditions. *See id.* at 78, 85.

²³⁰ *See id.* at 85-86.

²³¹ In another recent decision, *South Carolina v. Baker*, 108 S. Ct. 1355 (1988), the Supreme Court again recognized that the political process, alone, may be insufficient to protect states from discriminatory treatment. In the *South Carolina* decision, the Supreme Court upheld a federal tax on interest income earned on certain debt obligations issued by state and local governments. The Court overturned much of what remained of the doctrine of intergovernmental tax immunity which had prohibited federal taxation of private individuals and entities employed by or doing business with states. *See, e.g.,* *Pollock v. Farmer's Loan & Trust*, 158 U.S. 601 (1895) (interest from municipal bonds not subject to federal taxation), *overruled*, *Baker*, 108 S. Ct. at 1355; *Collector v. Day*, 78 U.S. (11 Wall.) 113 (1871) (income of county judge immune from federal taxation), *overruled*, *Graves v. New York*, 306 U.S. 466 (1939). Nevertheless, with respect to direct taxation of states and localities, the Court implicitly approved and retained the nondiscrimination principle set forth by Justice Frankfurter in *New York v. United States*, 326 U.S. 572 (1946). *See supra* note 202. In responding to the dissent's position that lifting intergovernmental tax immunity would leave states at the mercy of Congress, the majority opinion argued that the nondiscrimination principle provides sufficient protection. If the federal government tried to destroy a state by ruinous taxation, a requirement that the tax be applied to private, as well as public entities would ensure that public pressure would be brought to bear against the tax in Con-

Implicit in the Constitution and the *Ėtasynski* decision is the proposition that the "political safeguards of federalism" are insufficient to protect states and their citizens from regional exploitation. Conflict among regions has played a central role in the history of the nation. Fears of interstate rivalry and exploitation took on great importance at the Constitutional Convention of 1787 and the ensuing ratification process.²³² Repeated conflicts among states and regions in the succeeding two hundred years, one erupting into a bloody war, have justified these concerns.²³³

During much of the twentieth century, however, regionalism seemed to be on the decline. In fact, during the 1950's and 1960's some political scientists questioned whether increased regional interdependence and mobility would lead to the demise of American sectionalism.²³⁴ However, a sharp increase in conflict between states and regions in recent years has undercut those who prophesied the death of regionalism. The energy crisis of the 1970's and the exodus of manufacturing from the northeast to the south and southwest are only two of the causes of renewed regional tension and conflict pitting the "frostbelt" against the "sunbelt."

Interregional hostility has frequently taken the form of groups of states using the national political process to advantage themselves, by disadvantaging other regions. Conflicts have erupted over the distribution of federal intergovernmental assistance, with each region forming organizations to lobby for a greater share of federal largess.²³⁵ In addi-

gress. 108 S. Ct. at 1367 n.14.

²³² See *supra* note 146.

²³³ Although most sectional conflicts pitted North against South, a number polarized East and West. See J. TURNER, PARTY AND CONSTITUENCY: PRESSURES ON CONGRESS 191-209 (E. Schneier, Jr. rev. ed. 1970). As Frederick Jackson Turner noted in the 1920's, "sectionalism was the dominant influence in shaping our political history." F. TURNER, THE SIGNIFICANCE OF SECTIONS IN AMERICAN HISTORY 323 (1932); see also R. BENSEL, SECTIONALISM AND AMERICAN POLITICAL DEVELOPMENT 1880-1980, at 5 (1984) ("The existence of sectionally based political conflict constitutes the most massive and complex fact in American politics and history."). Turner, after assessing the historical importance of sectionalism, predicted that regional self-consciousness and differences would become magnified as the nation matured and "crystallized sections feel the full influence of their geographic peculiarities, their special interests, and their developed ideals." F. TURNER, *supra*, at 45.

²³⁴ See, e.g., V. KEY, POLITICS, PARTIES AND PRESSURE GROUPS 245-48 (1964) (inevitable sectional differences would decline in importance as north and south become increasingly interwoven); J. TURNER, *supra* note 233, at 189 (recent decline in southern solidarity will likely lead to decline in interregional conflict); Key, *The Erosion of Sectionalism*, 31 VA. Q. REV. 161 (1955) (sectional differences would decline in importance); MacMahon, *supra* note 144, at 18-19 (observing that "[m]uch of the petty, protective protectionism of the depression period has been overcome.").

²³⁵ See generally, R. DILGER, THE SUNBELT/SNOWBELT CONTROVERSY: THE WAR OVER FEDERAL FUNDS (1982). Cf. Evans, *Sunbelt versus Frostbelt: The Evolu-*

tion, federal environmental legislation has been utilized to favor eastern and midwestern commercial interests at the expense of those located in the west.²³⁶ States and regions have also aggressively sought to disadvantage commercial interests from other sections of the country by enacting "exploitative" legislation such as restraints on imports, natural resource severance taxes, and taxes on the incomes of interstate businesses that are already subject to taxation elsewhere.²³⁷

In light of recent history, concerns that uncompensated intergovernmental takings could be used to exploit individual states and regions do not seem far-fetched. An interpretation of the fifth amendment requiring the United States to compensate states and localities when it condemns their property need not be grounded on the similarity of public and private entities. To the contrary, a compensation requirement may be justified as necessary to protect states from exploitation and rent-seeking.²³⁸

tion of Regional Conflict Over Federal Aid To Cities in the House of Representatives, 67 SOC. SCI. Q. 108, 108 (1986) (disparity between sunbelt and frostbelt support for urban aid is increasing).

²³⁶ See B. ACKERMAN & W. HASSLER, *CLEAN COAL/DIRTY AIR* 46-47 (1981) (discussing how an amendment to the Clean Air Act supported by eastern commercial interests and environmentalists passed Congress despite opposition from western commercial interests); R. CRANDALL, *CONTROLLING INDUSTRIAL POLLUTION: THE ECONOMICS AND POLITICS OF CLEAN AIR* 110-130 (1983) (Representatives from the northeast supported Clean Air Act amendments for the purpose of limiting growth in the South and West); Crandall, *Clean Air and Regional Protectionism*, 2 BROOKINGS REV. 17, 18 (1983) ("It seems quite clear that members of Congress from the Frost Belt are the strongest supporters of a set of policies that deliberately discourage the construction of new plants in those regions of the country where new facilities are most likely to be built — the South and West."); Landsberg, *Energy "Haves" and "Have-Nots"*, in *REGIONAL CONFLICT AND NATIONAL POLICY*, *supra* note 215, at 36-38 (Clean Air Act amendments were designed to assist eastern commercial interests).

²³⁷ See Kneese, *supra* note 215, at 67-75; Levmore, *Interstate Exploitation and Judicial Intervention*, 69 VA. L. REV. 563, 570-75 (1983). Additional issues which divide regions and threaten to provoke conflict include acid rain, toxic waste disposal, and protectionism. See, e.g., R. BENSEL, *supra* note 233, at 408 (protectionism); Crandall, *supra* note 236, at 20 (acid rain); Kneese, *supra* note 215, at 75-84 (nuclear waste disposal).

²³⁸ Interpreting the just compensation clause to require compensation for states and localities as a protection against regionalism is, of course, both over- and under-inclusive. To protect against the possibility of regional exploitation, compensation will be required for all takings, even those motivated by purely benign objectives. In addition, requiring compensation for intergovernmental takings will not leave Congress without other means to discriminate against individual states and regions. See, e.g., *South Carolina v. Katzenbach*, 383 U.S. 301 (1966) (discussed *supra* note 203); 12 U.S.C. § 1713(c)(2) (1982) (mortgages on housing in Alaska not subject to certain limitations that apply to other states); 42 U.S.C. § 418(d)(6)(G) (1982) (seven specific states allowed separate retirement systems). See generally Neuman, *supra* note 40, at 344-59 (discussing federal burdens on particular states and the District of Columbia). Nevertheless, the existence of gaps in constitutional protections against interstate discrimination and exploitation does not justify removing all other protections.

III. COMPENSATING THE INTERGOVERNMENTAL CONDEMNEE

In *United States v. 50 Acres of Land*,²³⁹ the Supreme Court held that when the federal government condemns property owned by a state or locality, it must treat the public condemnee in the same manner as it would a private individual.²⁴⁰ Because the federal government pays private individuals the fair market value of their property, state and local governments are entitled to no more. Underlying the Court's decision that public and private condemnees should be treated equally is the premise that compensation serves the same function for both.

As I have demonstrated in Part II, the premise underlying *50 Acres of Land* is inaccurate. The justifications for compensating public entities are not identical to the rationales typically offered for compensating private property owners. The role that compensation plays in preventing unfair burdens and minimizing investment risks for private citizens is much less important when the condemnee is a public entity. Instead, other functions served by compensation — the prevention of fiscal illusion and the protection of states and localities from exploitation — justify compensation for intergovernmental takings.

By failing to analyze carefully *why* compensation is necessary for intergovernmental takings, the Supreme Court prescribed a method of computation that fails to achieve these objectives. Although compensation based upon the fair market value of the property taken may force federal policy makers to take the costs of their actions into account, it does not sufficiently protect the integrity of states and localities. Intergovernmental condemnees should receive compensation over and above the fair market value of the property taken, when they can demonstrate that there is a need to replace the condemned property and that the replacement cost exceeds its market value.

In Part III, I briefly describe how compensation is computed for federal condemnations of private property, and then trace the development of rules governing compensation for intergovernmental takings, culminating in the *50 Acres of Land* decision. Finally, I conclude that a method of compensation similar to the one repudiated by the Supreme Court in *50 Acres of Land* is more appropriate than the current fair market value standard, if states and localities are to be protected from disruption and exploitation. If states and localities can demonstrate that the public facility taken by the federal government provided a benefit that would not be as fully provided after the condemnation, they should be entitled to a compensation award in excess of the prop-

²³⁹ 469 U.S. 24 (1984).

²⁴⁰ See *id.* at 31.

erty's fair market value. To protect states and localities from disruption and exploitation, as well as to promote economic efficiency, intergovernmental condemnees should be entitled to the cost of replacing the condemned facility less the amount by which the condemned property had depreciated.

A. *Just Compensation For Private Condemnees*

Although the Supreme Court has consistently stated that the purpose of the just compensation clause is to protect private individuals from bearing unfair burdens,²⁴¹ it has been less consistent in formulating rationales for how that compensation should be computed. In most eminent domain cases, the Court states that the objective of compensation is to indemnify the condemnee; the person whose property is taken by the federal government is "entitled to be put in as good a position pecuniarily as if his property had not been taken."²⁴² An indemnification objective necessarily focuses on the value of the property to the owner; otherwise one could not be sure that the condemnee was "made whole" following the condemnation. At the same time, however, the Court has stressed that compensation is not for the owner, but for the property.²⁴³ Indeed, the Court seems to have disregarded the owner's measure of value in stating that "[t]he value compensable under the Fifth Amendment . . . is only that value which is capable of transfer from owner to owner. . . ."²⁴⁴ In contrast to an indemnity approach, compensating only transferrable values seems to shift attention from what the condemnee has lost, to what the condemnor gains.²⁴⁵

Although the Court continues to restate the indemnification princi-

²⁴¹ See *supra* notes 55-57 and accompanying text.

²⁴² *Olson v. United States*, 292 U.S. 246, 255 (1934). See also *Almota Farmers Elevator & Warehouse Co. v. United States*, 409 U.S. 470, 473-78 (1973) (deciding that a lessee with no right of renewal is entitled to compensation equal to the fair market value of its leasehold improvements, taking into account the possibility that the lease might or might not be renewed); *United States v. Reynolds*, 397 U.S. 14, 16 (1970) (discussing how to account for the effects of the condemnation itself on the fair market value); *United States v. Miller*, 317 U.S. 369, 373 (1943) (just compensation means receiving the "full and perfect" monetary equivalent of the property taken).

²⁴³ See *Monongahela Navigation Co. v. United States*, 148 U.S. 312, 326 (1893) ("just compensation, it will be noticed, is for the property, and not to the owner").

²⁴⁴ *Kimball Laundry Co. v. United States*, 338 U.S. 1, 5 (1949); see *United States v. 564.54 Acres of Land*, 441 U.S. 506, 514 (1979) ("nontransferable values arising from the owner's unique need for the property are not compensable").

²⁴⁵ See Kanner, *supra* note 102, at 781 (discussing clash between the value the taker acquires and the indemnification of owner); Comment, *Eminent Domain Valuations in an Age of Redevelopment: Incidental Losses*, 67 YALE L.J. 61, 67 (1957) (limiting compensation to tangible property rights effectively means government must pay for what it gains rather than what condemnee loses).

ple, recent decisions make it clear that compensation should be based upon transferrable value only.²⁴⁶ In computing compensation courts are instructed to determine the fair market value of the property taken. One leading commentator defines fair market value as "the amount of money which a purchaser willing but not obliged to buy the property would pay to an owner willing but not obliged to sell it, taking into consideration all uses for which the land was suited and might in reason be applied."²⁴⁷ For reasons of simplicity²⁴⁸ and economy,²⁴⁹ owners are not indemnified for economic losses attributable to business disrup-

²⁴⁶ See *supra* note 244. The Court has acknowledged that its rules of compensation fail to give the principle of indemnification "its full and literal force." 564.54 *Acres of Land*, 441 U.S. at 511; see also *Kirby Forest Indus. Inc. v. United States*, 467 U.S. 1, 10 n.15 (1984) ("We have acknowledged that, in some cases, this standard [fair market value] fails to indemnify the owner for his loss.").

²⁴⁷ 4 NICHOLS ON EMINENT DOMAIN, *supra* note 1, at § 12.2[1]. Courts usually utilize one of three methods to determine a property's fair market value: comparable sales, income capitalization, or reproduction cost minus depreciation. See *United States v. Certain Property In Borough of Manhattan*, 403 F.2d 800, 802 (2d Cir. 1968). See generally J. GELIN & D. MILLER, *THE FEDERAL LAW OF EMINENT DOMAIN* §§ 4.1-4.3 (1982); 4 NICHOLS ON EMINENT DOMAIN, *supra* note 1, at §§ 12.1-12.51; 1 ORGEL ON VALUATION UNDER EMINENT DOMAIN (2d ed. 1953).

If the property is of a type that is frequently bought and sold, a court will determine its value by referring to comparable sales (i.e. sales similar in time, quantity, and quality). Courts view the comparable sales method as giving the most accurate estimate of a property's fair market value. See *United States v. Miller*, 317 U.S. 369, 374-75 (1943) (if condemned property or similar property has not been recently sold then estimate of its fair market value will be an informed guess); *United States v. Whitehurst*, 337 F.2d 765, 775 (4th Cir. 1964) (comparable sales are the best evidence of market value).

If sufficient comparable sales for an income-producing property do not exist, a court may determine its value by analyzing what amount an investor would pay for the stream of income generated by the building — the income capitalization method. Finally, for special purpose properties such as churches and institutional buildings which are seldom sold and do not generate income, courts will estimate the amount it would cost to reproduce the condemned property. Because the condemned property is typically not new, the court usually estimates how much it has depreciated and deducts that amount from the reproduction cost. Because many courts are skeptical about the degree of correspondence between reproduction cost and a property's fair market value, the reproduction-cost-minus-depreciation method of valuation is typically used only in exceptional cases. See, e.g., *United States v. 1132.50 Acres of Land*, 441 F.2d 356, 358 (2d Cir. 1971) (criticizing reproduction cost method), *cert. denied*, 404 U.S. 850 (1971); *United States v. 55.22 Acres of Land*, 411 F.2d 432, 435 (9th Cir. 1969) ("Generally speaking, reproduction cost is not considered the best evidence of fair market value . . ."); 4 NICHOLS ON EMINENT DOMAIN, *supra* note 1, at § 12.313, ("evidence of reproduction cost is admissible only in exceptional cases.").

²⁴⁸ See 564.54 *Acres of Land*, 441 U.S. at 511 (because of "serious practical difficulties" in determining the worth of individual properties, the Court requires an objective working rule).

²⁴⁹ See *United States v. Commodities Trading Corp.*, 339 U.S. 121, 123 (1950) (The dominant consideration is: "What compensation is 'just' to both an owner whose property is taken and to the public that must pay the bill?").

tion,²⁵⁰ lost goodwill,²⁵¹ relocation costs,²⁵² or litigation expenses.²⁵³

B. *Just Compensation For Intergovernmental Condemnees*

Prior to 1984, most courts computed compensation for intergovernmental takings based upon the substitute facilities doctrine, rather than the fair market value standard. Under the substitute facilities measure, states and localities were entitled to the cost of constructing a "functionally equivalent substitute"²⁵⁴ when the federal government condemned public property. Most courts required compensation for substitute facilities only if it were necessary for the state or locality to replace the facility taken.²⁵⁵ Although some courts required that the state or locality be legally compelled to replace the facility,²⁵⁶ most

²⁵⁰ See *United States v. General Motors Corp.*, 323 U.S. 365, 383 (1945) (injury to business is not to be included in compensation award); *United States ex rel. Tennessee Valley Auth. v. Powelson*, 319 U.S. 266, 281 (1943) (frustrated business plans are not compensable); *Mitchell v. United States*, 267 U.S. 341, 345 (1925) (destruction of agricultural business not compensable). But see *Kimball Laundry Co. v. United States*, 338 U.S. 1, 14-15 (1949) (condemnee might be entitled to lost business profits during period of temporary taking, due to the impracticability of relocating).

Several commentators have criticized federal condemnation practices on the ground that they fail to compensate for incidental and consequential losses. See, e.g., Bigham, "Fair Market Value," "Just Compensation," and the Constitution: A Critical View, 24 VAND. L. REV. 63, 65-66 (1970) (objecting to the government's failure to make the condemnee whole); Durham, *Efficient Just Compensation as a Limit on Eminent Domain*, 69 MINN. L. REV. 1277, 1278-79 (1985) (noting that market value does not always reflect all of the costs borne by the condemnee); Francis, *Eminent Domain Compensation in Western States: A Critique of the Fair Market Value Model*, 1984 UTAH L. REV. 429, 430-41 (noting examples of disparities between market value and the value derived by the owner from the property); Comment, *supra* note 245, at 61 (noting costs borne unfairly by owners and lessees of property).

²⁵¹ See *General Motors*, 323 U.S. at 383 (lost goodwill is noncompensable); R. EPSTEIN, *supra* note 44, at 80-86 (criticizing the failure of courts to compensate for lost goodwill); Aloï & Goldberg, *A Reexamination of Value, Good Will, and Business Losses In Eminent Domain*, 53 CORNELL L. REV. 604, 635 (1968) (courts fail to compensate for "going business" value).

²⁵² See *United States v. Westinghouse Elec. & Mfg. Co.*, 339 U.S. 261, 264 (1950) (when entire property interest of condemnee is taken, removal costs are not compensable); *United States v. Petty Motor Co.*, 327 U.S. 372, 378 (1946) (cost of relocating business not compensable when government takes leasehold interest even though lease contains renewal option); *General Motors*, 323 U.S. at 383 (removal damages may not be compensated as independent items of damage though they may be taken into consideration in determining market value of temporary occupancy).

²⁵³ See *United States v. Bodcaw Co.*, 440 U.S. 202, 204 (1979) (attorneys' fees and litigation expenses not included in compensation award).

²⁵⁴ *United States v. Certain Property In Borough of Manhattan*, 403 F.2d 800, 803-04 (2d Cir. 1968). Some courts deducted an amount representing the depreciation of the condemned facility from the cost of reconstruction. See *id.* at 804 n.11.

²⁵⁵ See *City of Fort Worth v. United States*, 188 F.2d 217, 221 (5th Cir. 1951) (city entitled to an award sufficient to restore necessary roads).

²⁵⁶ See, e.g., *United States v. Wheeler Township*, 66 F.2d 977, 985 (8th Cir. 1933) (township is entitled to compensation when it is the "legally compellable duty of

courts held that if replacement was reasonably necessary to meet the needs and desires of their citizens, compensation should be paid.²⁵⁷ In instances where substitute facilities were not necessary, some courts awarded no compensation or nominal compensation,²⁵⁸ while others required the federal government to pay states and localities the fair market value of the property taken.²⁵⁹

Courts gave two reasons for deviating from fair market value to invoke the substitute facilities doctrine. Many courts reasoned that the concept of fair market value had little relevance to takings of publicly owned property. Roads, parks, and public buildings and facilities are seldom sold, and judges found it both difficult and artificial to determine their market value.²⁶⁰ Secondly, courts seemed to recognize that states and localities typically hold property for different purposes than private individuals.²⁶¹ While fair market value may be adequate to compensate condemnees who own property primarily for economic or commercial advantages,²⁶² it may not be sufficient to prevent serious

the township to maintain" the function provided by the condemned property); *United States v. Alderson*, 53 F. Supp. 528, 530-31 (S.D. W. Va. 1944) (if state road is damaged and state is legally compelled to replace road, substitute facility is appropriate compensation).

²⁵⁷ See *Certain Property In Borough of Manhattan*, 403 F.2d at 803-04; *County of Sarpy v. United States*, 386 F.2d 453, 457-58 (Ct.Cl. 1967).

²⁵⁸ See, e.g., *United States v. Streets, Alleys and Public Ways In Stoutsville*, 531 F.2d 882, 886 (8th Cir. 1976) (no compensation is due if there is no reasonable necessity to replace roads condemned by federal government); *United States v. Certain Lands Located in Raritan and Woodbridge*, 246 F.2d 823, 824 (3d Cir. 1957) (if substitute highway is not necessary, no compensation is due); *Woodville v. United States*, 152 F.2d 735, 737 (10th Cir.) (if substitute street is not necessary, city is not entitled to substantial damages), *cert. denied*, 328 U.S. 842 (1946).

²⁵⁹ See, e.g., *United States v. 3,727.91 Acres of Land*, 563 F.2d 357, 360-61 (8th Cir. 1977) (drainage district entitled to fair market value of land condemned even though it would not replace levees and ditches); *California v. United States*, 395 F.2d 261, 266-68 (9th Cir. 1968) (state entitled to monetary value of condemned underwater parcels despite lack of necessity for replacement); *United States v. Certain Land in Borough of Brooklyn*, 346 F.2d 690, 695-96 (2d Cir. 1965) (if new playground is not necessary the city is entitled to value of property taken by federal government); *United States v. Jacksonville*, 257 F.2d 330, 333-34 (8th Cir. 1958) (city entitled to scrap or salvage value of condemned sewage system even though replacement not necessary).

²⁶⁰ See *Certain Property In Borough of Manhattan*, 403 F.2d at 802-04 (market value test is often unworkable because public facilities are not commonly bought and sold on the open market).

²⁶¹ See *Jefferson County v. Tennessee Valley Auth.*, 146 F.2d 564, 565 (6th Cir.) (highway easements are "totally unlike" property held by private entities), *cert. denied*, 324 U.S. 871 (1945).

²⁶² Current methods of computing compensation based upon fair market value, however, may fail to indemnify adequately even those who own property solely for its commercial or economic value. Most courts exclude from condemnation awards compensation for business losses, lost goodwill, relocation expenses, litigation costs, and other consequential and incidental losses. See *supra* notes 250-53. Perhaps even more importantly, many people own property for reasons other than economic or instrumen-

disruptions to states and localities which are required to maintain provision of public goods and services.²⁶³

The demise of the substitute facilities doctrine began with a 1979 Supreme Court decision, *United States v. 564.54 Acres of Land*.²⁶⁴ The respondent, a private, nonprofit religious group, operated three summer camps which were condemned for a federal recreational project. The three camps had been exempted from expensive regulation under a grandfather provision. Respondent contended that it was entitled to the cost of developing functionally equivalent facilities on a new site; an award based on the fair market value of the property would not enable it to do so because new property for rebuilding the camps would not enjoy the former exemption from government regulation.²⁶⁵

At trial,²⁶⁶ the district court judge instructed the jury that it could award compensation based upon the substitute facilities doctrine if it

tal advantage. For example, property may be intimately bound up with a person's identity and be necessary for that person to flourish. See Baker, *supra* note 121, at 761-64; Radin, *Property and Personhood*, 34 STAN. L. REV. 957 (1982). Compensation based upon fair market value standards fails to include a component for a person's subjective valuation of his or her property. Therefore, for "personal property," such as a home, fair market value — or perhaps any monetary compensation — will often be insufficient to make a person whole after a condemnation. See Radin, *supra*, at 1002-08; cf. Ellickson, *Alternatives To Zoning: Covenants, Nuisance Rules, and Fines as Land Use Controls*, 40 U. CHI. L. REV. 681, 736-37 (1973) (providing a bonus over fair market value may be a desirable system to compensate lost consumer surplus attributable to condemnation of nonfungible property).

Much of the present critique of current methods of computing compensation for intergovernmental takings applies with equal force to compensation for takings of private property. Compensation based upon the fair market value of condemned property may be inadequate to ensure that the functions served by the just compensation clause are fulfilled. Although a discussion of the appropriate method for compensating private condemnees is beyond the scope of this article, some aspects of the compensation rule proposed for public condemnees would also be applicable to their private counterparts. However, it is also likely that an appropriate compensation rule for private property owners would differ in several respects from the rule advocated herein. See *infra* note 281 (illustrating how fair market value method of compensation might be appropriate for private condemnee, but not public condemnee). For example, compensation for subjective losses is considerably less relevant for public condemnees than for individual citizens. Moreover, a compensation rule for "fungible property" would likely include elements for consequential and incidental damages that would be unnecessary for either owners of personal or public property. Cf. Radin, *supra*, at 986 (distinguishing personal property from fungible property).

²⁶³ See *Certain Land In Borough Of Brooklyn*, 346 F.2d at 695 (loss of public property may put a "serious strain on other public facilities").

²⁶⁴ 441 U.S. 506 (1979).

²⁶⁵ See *id.* at 508.

²⁶⁶ The Third Circuit had earlier reversed the District Court's ruling that respondent was only entitled to the fair market value of the property. See *United States v. 564.54 Acres of Land*, 506 F.2d 796, 800-02 (3d Cir. 1974) (nonprofit organizations

found that the property “‘fulfill[ed] a community need or purpose.’”²⁶⁷ The Court of Appeals for the Third Circuit reversed the jury’s verdict in favor of the government on the ground that the district court had defined “reasonable necessity” too stringently. According to the court, for a facility to be reasonably necessary, “it must provide a benefit to the community that will not be as fully provided after the facility is taken.”²⁶⁸

The Supreme Court reversed, finding that compensation based on the fair market value of the property was feasible because a market, albeit a thin market, existed for the sale of campgrounds.²⁶⁹ In addition, the Court found that even though the respondent might not be fully indemnified by an award based upon the fair market value of the campgrounds, such an award was consistent with past rulings holding that nontransferable values arising from an owner’s unique need for condemned property are not compensable.²⁷⁰ Furthermore, the Court observed that as a private entity, the respondent would not be required to use the compensation to rebuild the facilities and, therefore, compensation based upon the substitute facilities doctrine might constitute a windfall.²⁷¹

In a footnote to *564.54 Acres of Land*, the Court also cast doubt upon the propriety of compensating states and local governments according to the substitute facilities doctrine.²⁷² Although the Court expressed no formal opinion on that issue, it distinguished and limited an earlier Supreme Court decision that many had interpreted as placing the Court’s imprimatur on the substitute facilities doctrine.²⁷³ Five

are entitled to substitute facilities compensation if no ready market exists for property and if facilities are reasonably necessary to the public welfare).

²⁶⁷ 441 U.S. at 509 (quoting *564.54 Acres of Land*, 576 F.2d 983, 995 n.16 (3d Cir. 1978)). The district court also instructed the jury that to award substitute facilities compensation, it must find that “‘the fair market value of the condemned property [was] substantially less than the cost of constructing functionally equivalent substitute facilities.’” *Id.* (quoting *564.54 Acres of Land*, 576 F.2d at 992 n.9 (3d Cir. 1978)).

²⁶⁸ *564.54 Acres of Land*, 576 F.2d at 995.

²⁶⁹ See 441 U.S. at 513 (evidence was submitted showing the sale of eleven comparable facilities in the vicinity).

²⁷⁰ See *id.* at 514. Interestingly, the Court did not consider whether the grandfathering provisions ran with the land and would have benefitted subsequent purchasers. Under the Court’s analysis, if the benefits of the exemption were transferrable, presumably they would be compensable.

²⁷¹ *Id.* at 515-16.

²⁷² *Id.* at 509 n.3.

²⁷³ In *Brown v. United States*, 263 U.S. 78 (1923), the federal government condemned three-quarters of a town for a reservoir project. As compensation, the federal government condemned additional private property and proposed to relocate the town to that new site. The owners of the substitute property challenged the power of the federal government to take property for purposes of substituting it for other condemned property. The Court upheld the government’s action stating that “[a] method of com-

years later, in *50 Acres of Land*, the Court addressed the issue raised by its footnote, holding that the substitute facilities method of computing compensation was inappropriate for public as well as private condemnees.²⁷⁴ The Supreme Court held that when the fair market value of property could be ascertained,²⁷⁵ the federal government should pay a public condemnee the same amount as it would pay a private property owner.²⁷⁶ The Court justified the fair market value standard by citing prior decisions holding that just compensation should exclude subjective values and instead should compensate property owners solely for those elements of value that are transferrable.²⁷⁷ According to the Court, the advantage of excluding subjective values is to reduce the "risk of error and prejudice."²⁷⁸

What is most problematic about the Court's decision in *50 Acres of Land*, is that in discussing the appropriate measure of compensation for public entities, the Court failed to consider the differences between public and private condemnees and the special role states and localities play in our federal political system. Although the Court seemed to ad-

pensation by substitution would seem to be the best means of making the parties whole." *Id.* at 83.

Many lower federal courts had cited this language in holding that compensation for state and local governments should be measured by the substitute facilities doctrine. See, e.g., *Certain Property In Borough of Manhattan*, 403 F.2d 800, 803 (2d Cir. 1968) ("When the public condemnee proves there is a duty to replace . . . it is entitled to the cost of constructing a functionally equivalent substitute . . ."); *United States v. Certain Parcels of Land, Town of Clarksville*, 104 F. Supp. 369, 373 (E.D. Va. 1952) (the value of public property must be "measured by the cost of a substitute"). Nevertheless, the Court in *564.54 Acres of Land* noted that *Brown* addressed the "scope of the Government's condemnation power, not the compensation requisite under the Fifth Amendment." 441 U.S. at 509 n.3; see also *United States v. 50 Acres of Land*, 469 U.S. 24, 33 (1984) ("*Brown* merely indicates that it would [be] constitutionally permissible for the Federal Government to provide the city with a substitute [facility] instead of . . . cash.>").

²⁷⁴ See *50 Acres of Land*, 469 U.S. at 33-36. The federal government had condemned a sanitary landfill belonging to the City of Duncanville. To replace the landfill, the city had purchased a parcel of land twice the size of the condemned property. The court of appeals reversed the district court's decision awarding Duncanville the fair market value of the site condemned. Instead, the court required the federal government to pay the city the amount reasonably spent to create a functionally equivalent facility. See *50 Acres of Land* 706 F.2d 1356, 1360 (5th Cir. 1983) ("[T]he reasonable cost of a functionally equivalent facility is the just measure of compensation when a public entity is obligated to replace the condemned property."). On retrial the court also required the jury to discount the cost of the substitute facility to account for its increased capacity and superior quality. See *id.* at 1362-63 (noting that even though "Duncanville . . . gained noticeably from the replacement" the trial court nevertheless failed to "take into account the need to deduct for the benefits which Duncanville gained").

²⁷⁵ Somewhat surprisingly, the Court found that there was a "fairly robust market for sanitary landfill properties." *50 Acres of Land*, 469 U.S. at 30.

²⁷⁶ See *supra* notes 5-7 and accompanying text.

²⁷⁷ *50 Acres of Land*, 469 U.S. at 35-36.

²⁷⁸ *Id.* at 36.

mit that the lack of full indemnity inherent in fair market value compensation might disrupt states and localities,²⁷⁹ it failed to examine the consequences of such disruptions.

C. *Measuring Compensation for Intergovernmental Condemnees*

As demonstrated in Part II, intergovernmental takings can disrupt states and local governments, threatening the core of independent decision-making power central to our federal political system. Any measure of compensation which fails to alleviate these disruptions could place individual states or regions at the mercy of a potentially hostile federal government. Although the Supreme Court's ruling in *50 Acres of Land* may set an appropriate floor on compensation,²⁸⁰ it fails to ensure that states and localities will be able to provide the same level of public goods and services after a condemnation as they had prior to the taking. Therefore, compensation based upon the fair market value of the property taken fails to protect states and localities from disruption and exploitative rent-seeking.²⁸¹

²⁷⁹ See *id.* at 34 ("The city's legal obligation to maintain public services that are interrupted by a federal condemnation does not justify a distinction between public and private condemnees for the purpose of measuring 'just compensation.'") (footnote omitted). In a concurring opinion, Justice O'Connor, joined by Justice Powell, characteristically showed more solicitude for state and local governments:

When a local governmental entity can prove that the market value of its property deviates significantly from the make-whole remedy intended by the Just Compensation Clause and that a substitute facility must be acquired to continue to provide an essential service, limiting compensation to the fair market value in my view would be manifestly unjust.

Id. at 37 (O'Connor, J., concurring).

²⁸⁰ Even in instances in which the state or locality no longer requires a substitute property after the condemnation, fair market value compensation might still be necessary to avoid economic inefficiency due to fiscal illusion. Although the property no longer has a "public value" to the state or locality, it nevertheless has an economic value as fungible property. See *supra* notes 114-19 and accompanying text.

²⁸¹ The inadequacy of fair market value compensation for certain intergovernmental takings is well-illustrated by federal condemnation of an office building owned by a locality or state. Public office buildings are frequently located in inner city neighborhoods, many of which have experienced declining property values in recent years. If the office building were condemned and the court awarded compensation based upon the property's fair market value, it is likely that it would base the award on sales prices of other office buildings in the area. The court would adjust the award upward or downward to reflect differences between the condemned building and comparable properties. See *United States v. 0.161 Acres of Land*, 837 F.2d 1036, 1044 (11th Cir. 1988) (employing the comparable sales method for downtown property); *Hickey v. United States*, 208 F.2d 269, 273 (3d Cir. 1953) (approving comparable sales method for downtown office building), *cert. denied*, 347 U.S. 919 (1954); *United States v. 49,375 Square Feet of Land*, 92 F. Supp. 384, 393-94 (S.D.N.Y. 1950) (comparable sales method for office building better than capitalization of income method), *aff'd sub nom. United States v. Tishman Realty & Const. Co.*, 193 F.2d 180 (2d Cir.), *cert. denied*, 343 U.S.

To protect their important role in our political system, states and localities should be compensated according to a method analogous to the substitute facilities doctrine. When state or local property is condemned by the federal government, the condemnee should be entitled to receive, at a minimum, the fair market value of the condemned property. This minimum award serves the basic requirement of preventing fiscal illusion.²⁸² When the state or local government can show that the facility taken provided a benefit that would not be as fully provided after the condemnation,²⁸³ it should be entitled to compensation based upon the amount it would cost to replace²⁸⁴ the condemned property.²⁸⁵

928 (1952). If, as is likely, the state or locality were unable to purchase an equivalent building suited to its needs, and found it necessary to construct a new facility, "comparable sales" compensation (based on the depressed property values in the surrounding community) would be inadequate to cover the cost of building a new facility. Thus, while compensation based upon comparable sales may adequately compensate private investors who view their property as fungible, such a measure of compensation could well be inadequate for public entities which must construct alternative facilities in order to continue providing public services.

²⁸² See *supra* notes 114-19 and accompanying text.

²⁸³ In determining whether states and cities should be awarded an amount to replace the property condemned, the "reasonable necessity" standard of the substitute facilities doctrine, see *supra* note 257 and accompanying text, is difficult to reconcile with a recognition of the value of state and local decision-making authority. In applying the reasonable necessity standard, federal judges must substitute their own views regarding the need for public services in place of decisions made by duly elected state and local legislators. See Note, *Just Compensation and the Public Condemnee*, 75 YALE L.J. 1053, 1055 (1966) (issue of necessity of public projects is inappropriate for judicial determination). Nevertheless, merely requiring that the substitute facility serve a rational governmental purpose, see *id.*, seems to be an open invitation for tenuous rationalizations geared to obtaining as much money from the federal fisc as possible. A more objective standard based upon whether the community has been harmed as a result of the taking is more desirable. This was the test adopted by the Third Circuit in *564.54 Acres Of Land*, 576 F.2d at 995, (discussed *supra* text accompanying note 268).

²⁸⁴ It is possible that the federal government may occasionally condemn state or local property which is not replaceable. For example, certain public facilities such as harbors and parks may be tied to specific geographic locations. If the public entity can show that the facility taken provides a benefit which would not be provided as fully after condemnation, a dilemma would be presented. On the one hand, the federal government should be able to acquire the property to exercise fully its constitutional powers. Nevertheless, because replacement is impossible, states and localities would be subject to disruption and potential exploitation as a result of the condemnation. In these unusual circumstances, courts may be required to step in to ensure that the taking is necessary to achieve a legitimate governmental objective. Cf. *United States v. Ptasynski*, 462 U.S. 74, 85 (1983) ("where Congress does choose to frame a tax in geographic terms, we will examine the classification closely to see if there is actual geographic discrimination [in violation of the tax uniformity clause].") Courts applying this type of "close" scrutiny should be especially sensitive to possible motives of interstate discrimination and exploitation; they should invalidate condemnations of non-substitutable property that are unnecessary and disruptive.

²⁸⁵ Public condemnees should be awarded compensation for replacement only in instances where the cost of replacement exceeds the condemned property's fair market value. If replacement cost is less than fair market value, fair market value is the appro-

In instances where the condemned property includes improvements such as structures or equipment, however, an award based upon full replacement cost might be inappropriate. If the condemned facility's remaining useful life is less than that of the replacement facility, an award based upon full replacement cost might place the public condemnee in a better economic position after the taking than it had enjoyed prior to condemnation. This potential windfall to state and local condemnees could promote government inefficiency by creating an additional incentive for federal legislators to support federal projects whose overall costs exceed benefits, but which nonetheless generate significant local benefits.²⁸⁶

priate measure of compensation so as to eliminate the possibility of fiscal illusion.

Compensation based upon replacement cost should not, with due respect to the Court in *50 Acres of Land*, be exceedingly more complex and subjective than computing the fair market value of property. As recent hearings before Congress indicate, appraisal standards are notoriously complex and manipulable, providing numerous opportunities for interested parties to ensure that their desired valuation and the one produced by the appraiser coincide. See HOUSE COMM. ON GOV'T OPERATIONS, IMPACT OF APPRAISAL PROBLEMS ON REAL ESTATE LENDING, MORTGAGE INSURANCE, AND INVESTMENT IN THE SECONDARY MARKET, H.R. REP. NO. 891, 99th Cong., 2d Sess. 42-43 (1986); *Impact of Faulty and Fraudulent Real Estate Appraisals on Federally Insured Financial Institutions and Related Agencies of the Federal Government: Hearings Before the Subcomm. on Commerce, Consumer, and Monetary Affairs of the House Comm. on Gov't Operations*, 99th Cong., 1st Sess. 1421-44 (1985); Barnett, A Proposal for Regulating Real Estate Appraisals: Structuring Deterrents in a Permissive System, 11, 14 (Feb. 8, 1988) (unpublished student paper, Yale School of Law).

Experience in eminent domain proceedings also supports the proposition that estimation of the fair market value of property is less than an exact science. See *United States v. Miller*, 317 U.S. 369, 374-75 (1943) (appraisal unlikely to reflect market value "with nicety"; where property in vicinity has not been sold recently and in significant amounts the application of the fair market value standard "involves, at best, a guess by informed persons."); 4 NICHOLS ON EMINENT DOMAIN, *supra* note 1, at § 12.31 [2] (stating that the "market value of a piece of real estate is not ordinarily the subject of ready computation"). In the absence of impropriety by state and local officials, the value of replacement property could be accurately measured by the price paid. Although some difficult adjustments might need to be made to accommodate the purchase of properties that go beyond mere replacement, or to take into account financing arrangements, it is by no means clear that the method of computation is either more complex or more subjective than computing fair market value. See Durham, *supra* note 250, at 1292 (valuation of substitute facility unlikely to be more difficult than valuing condemned property); Note, *Restoration Costs As An Alternative Measure of Severance Damages In Eminent Domain Proceedings*, 20 HASTINGS L.J. 800, 806 (1969) (noting that the "cost of restoration standard is probably more objective than the fair market value standard"). Furthermore, similar methods of compensation based on "equivalent reinstatement" have frequently been used in Canada and England to compensate persons whose property was appropriated by the national government. See Cullingworth, *Compulsory Acquisition of Land in Canada*, 7 URB. L. & POL'Y 385, 392-93 (1985); Denyer-Green, *Eminent Domain: A Comparative Discussion on the Assessment of Compensation in the United States and England*, 50 APPRAISAL J. 212, 216-17 (April 1982).

²⁸⁶ See *infra* notes 211-14 and accompanying text, for a discussion of the tendency of Members of Congress to engage in porkbarrel politics.

Compensation for intergovernmental condemnees should promote efficient government action as well as limit the potential for interstate exploitation. While intergovernmental condemnees should be entitled to an award that will enable them to continue providing the same public goods and services as they had prior to the condemnation, they should not be overcompensated. Thus, while the compensation award should be based upon replacement cost, an amount representing the actual economic depreciation²⁸⁷ of the condemned property should be deducted from the compensation award. Although compensation based upon replacement cost minus economic depreciation may be less than the full cost of acquiring an equivalent, substitute facility, or rebuilding the condemned property, in most cases the public condemnee should be able to finance the shortfall through its capital budget.²⁸⁸ Therefore, this method of calculating compensation awards should achieve the twin objectives of promoting efficient government action and limiting the ability of the federal government to disrupt states and localities.

²⁸⁷ See C. SIRMANS, *REAL ESTATE FINANCE* 166 (1985) (distinguishing between real, economic depreciation, and accounting or tax depreciation).

²⁸⁸ States and localities regularly finance capital projects by issuing bonds. See generally M. GELFAND, *STATE & LOCAL GOVERNMENT DEBT FINANCING* § 1:04 (1987); W. OATES, *supra* note 159, at 153-61; Durning, *The New Capital Market Heavyweights*, 61 J. STATE GOV'T 124, 125-26 (1988). The ability of a public condemnee to finance the portion of the cost of the substitute facility that has been deducted as depreciation ensures that the condemnee receives full, but no more than full, indemnification. For example, assume that a particular type of facility has a useful life of 50 years, depreciates in value in equal increments each year, and costs \$10,000,000 to reconstruct in current dollars. Further assume that the federal government condemns the facility after it has been in service 10 years. If the government were to compensate the condemnee based upon the method advocated herein, the state or locality would receive an award of \$8,000,000 [$\$10,000,000 - 10/50 (\$10,000,000)$]. The state or locality could then issue bonds to make up the additional \$2,000,000 of the cost to rebuild or replace the condemned facility. This method of compensation not only serves to prevent disruption of the state or locality, it also puts the state in a position economically equivalent to the one it had been in prior to the condemnation with an asset worth \$10,000,000, and a corresponding liability of \$2,000,000.

States and localities may, however, be vulnerable to disruption and exploitation if they are unable to borrow in the capital markets either because of poor credit ratings, see M. SHEFTER, *supra* note 107, at 127-48 (describing New York City's experience), or because of state limitations on debt, see, e.g., IOWA CONST. art XI, § 3 (limits annual aggregate indebtedness to five percent of taxable property in locality); M. GELFAND, *supra*, at § 9 (discussing state constitutional and statutory debt ceilings). Such instances present a tradeoff between protecting states and localities from disruption, and promoting economic efficiency. Although the choice between these objectives is by no means clear, based upon my belief in the importance of protecting states from disruption and exploitation, I am inclined toward a compensation rule which does not deduct depreciation from awards to intergovernmental condemnees when the public entity can demonstrate: 1) that the public facility taken provided a benefit that would not be as fully provided after the condemnation, see *supra* note 283, 2) that it has insufficient funds to cover the difference between the cost to replace and the property's depreciated value, and 3) that it cannot borrow those funds in the capital market. See *supra*.

CONCLUSION

The specter of interstate exploitation, central to this article's critique of current condemnation jurisprudence, is admittedly less prominent today than it was at the framing of the Constitution. It is perhaps a tribute to the system created by the Framers that in a nation of such magnitude and diversity as the United States, regional tension has erupted so infrequently. Nevertheless, the principle that the integrity of states must be preserved is implicit in the Constitution; the means to single out and harm individual states or regions must be kept from the national government.

Perhaps the greatest achievement of these constitutional protections goes beyond the fact that they have, to a large extent, worked as intended. These same constitutional principles have also had an educative effect, making open and intense regional warfare less a possibility in the minds of American citizens. Nevertheless, as recent events have demonstrated, regionalism is not a concern that can be relegated to the past. Interstate rivalry, especially over economic issues, is as strong today as it has been in decades. Gaps in our constitutional protections against interstate conflict must be filled, rather than papered over. Recent jurisprudence regarding federal condemnations of state and local property has failed to acknowledge that compensation is of a piece with other constitutional protections of federalism. Restoring full indemnification for intergovernmental takings is necessary, not only to promote economic efficiency, and preserve the integrity of our federal system, but also to reinforce the constitutional barrier against regional conflict.