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Friedenburg v. DEC: A Troubling Regulatory Takings Ruling

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A troubling case in point is *Friedenburg v. New York State Department of Environmental Conservation*,¹ decided by the Second Department of the Appellate Division on November 24, 2003. The court's decision upholds a trial court ruling that the Department of Environmental Conservation (DEC) effected a taking by denying a permit to fill and develop tidal wetlands on Shinnecock Bay in Long Island.

Unfortunately for the DEC, it probably would have prevailed if the court had addressed the actual arguments and record in the case, rather than an over-simplified version of the case that seemed predestined to support a finding of a taking.

II. AN OVERVIEW OF REGULATORY TAKINGS DOCTRINE

A brief review of regulatory takings doctrine may help the reader place this case in clearer context.

The takings clause of the Fifth Amendment to the U.S. Constitution states: "nor shall private property be taken for public use, without just compensation." Article I, Section 7 of New York Constitution contains identical language that apparently has the same meaning as the federal takings clause.

I. INTRODUCTION

After a decision is handed down, litigants sometimes have the discomfiting sense that the court decided the case it wished to decide rather than the case actually presented to the court. There are various explanations for why this occurs, ranging from an understandable human tendency to avoid having to decide difficult issues to, more disturbing, a possible judicial desire to reshape a case to advance a particular vision of the law.

A. Threshold Property Issue

The threshold issue in any regulatory takings case is whether the claimant can point to some property interest she held as of the date of the alleged taking that was affected by the challenged government action. In the case of land, the property may consist of a fee simple estate or some narrower interest. The threshold property inquiry also includes examination of whether the challenged regulation parallels relevant background principles

¹ 767 N.Y.S.2d 451 (App. Div. 2d Dept. 2003).

of state nuisance or property law, that is, whether the regulation impinges upon a property interest that the claimant can claim a protected right to exploit.

B. Physical Occupations vs. Use Restrictions

Assuming the threshold property issue has been resolved, alleged regulatory takings are divided into physical occupations and restrictions on the use of property. Physical occupations, which are “relatively rare” and “easily identified,”² involve government invasions of private property or government authorizations for third parties to invade private property. The most important doctrinal difference between physical occupations and use restrictions is that an alleged taking based on a use restriction must be evaluated using the “parcel as a whole” rule, whereas a physical occupation results in a taking “regardless of whether the interest that is taken constitutes an entire parcel or merely a part thereof.”³

C. *Lucas* and *Penn Central*

Alleged takings based on use restrictions are conventionally subdivided into “categorical” takings under *Lucas v. South Carolina Coastal Council*,⁴ and ad hoc takings under *Penn Central Transportation Co v. New York City*.⁵ A *Lucas*-type categorical taking occurs when regulation eliminates a property’s “economically viable use.” A finding of an ad hoc type taking under *Penn Central* depends on a case-specific analysis based on various factors, including (1) the economic impact of the regulation; (2) the reasonableness of the owner’s investment expectations; and (3) the character of the regulation.

Explaining precisely how the *Lucas* test differs from the *Penn Central* test has proven to be a considerable challenge. *Lucas* states that the categorical test applies “no matter how weighty the public purpose behind [the regulation],”⁶ implying that the purpose of the regulation is a relevant factor in evaluating a claim under *Penn Central*. But since any valid taking claim presumes that the government action serves a “public use,” i.e., a “legitimate” government purpose, it is difficult to see how government purpose can ever be a relevant consideration in

determining whether or not compensation is due under the takings clause.

Similarly, *Lucas* suggests that the investment expectations factor is a relevant consideration under *Penn Central*, but not in a *Lucas* case. However, as Justice Stephen Breyer observed in *Palazzolo v. Rhode Island*, allowing claims “to survive changes in land ownership could allow property owners to manufacture such claims by strategically transferring property until only a nonusable portion remains.”⁷ He pointedly added: “I do not see how a constitutional provision concerned with ‘fairness and justice’ could reward any such strategic behavior.”⁸

The Supreme Court in *Tahoe-Sierra Preservation Council v. Tahoe Regional Planning Agency*,⁹ may have resolved the problem of defining the difference between the *Lucas* and *Penn Central* tests by ruling that *Lucas* is limited to the rare (if not nonexistent) case where a regulation results in “the permanent obliteration of the value of a fee simple estate.”¹⁰ If a *Lucas* taking rarely if ever arises, it obviously becomes relatively unimportant to figure out how the *Lucas* test differs from the *Penn Central* test.

D. Investment Expectations Factor

Under any understanding of takings law, the reasonableness of the claimant’s investment expectations is an important consideration in most if not all takings cases. In a trio of New York cases decided in 1997 — *Gazza v. New York State Dept. of Envtl. Conservation*,¹¹ *Anello v. Zoning Bd. of Appeals of the Village of Dobbs Ferry*,¹² and *Kim v. City of New York*¹³ — the Court of Appeals ruled that the existence of a regulatory requirement or policy at the time the property is purchased automatically bars a subsequent taking claim based on the regulation. In 2001, in *Palazzolo v. Rhode Island*,¹⁴ the Supreme Court modified the rule established by these decisions, concluding that advance notice of a regulatory constraint is a highly relevant factor, but not necessarily a dispositive consideration, in takings analysis.

² *Tahoe-Sierra Preservation Council v. Tahoe Regional Planning Agency*, 535 U.S. 302, 324, 122 S. Ct. 1465, 152 L. Ed. 2d 517 (2002).

³ *Id.* at 322.

⁴ 505 U.S. 1003, 112 S. Ct. 2886, 120 L. Ed. 2d 798 (1992).

⁵ 438 U.S. 104, 98 S. Ct. 2646, 57 L. Ed. 2d 631 (1978).

⁶ 505 U.S. at 1015.

⁷ 533 U.S. 606, 655, 121 S. Ct. 2448, 150 L. Ed. 2d 592 (2001). (dissenting opinion).

⁸ *Id.*

⁹ 535 U.S. 302, 324, 122 S. Ct. 1465, 152 L. Ed. 2d 517 (2002).

¹⁰ 535 U.S. at 330.

¹¹ 89 N.Y.2d 603, 657 N.Y.S.2d 555 (1997).

¹² 89 N.Y.2d 535, 656 N.Y.S.2d 184 (1997).

¹³ 90 N.Y.2d 1, 659 N.Y.S.2d 145 (1997).

¹⁴ 533 U.S. 606, 121 S. Ct. 2448, 150 L. Ed. 2d 592 (2001).

E. Exactions

The final piece of this quick overview of takings doctrine relates to exactions, which are mandates that landowners surrender some property interest as a condition of receiving a regulatory permit. The Supreme Court has ruled that exactions must meet the relatively demanding "essential nexus"¹⁵ and "rough proportionality"¹⁶ tests in order to avoid a finding of a taking. The Court also has made clear, however, that these tests are limited to the context of exactions.¹⁷

This in turn raises the question of what if any review of the reasonableness of government action applies under the takings clause outside the context of exactions. In *Bonnie Briar Syndicate, Inc. v. Town of Mamaroneck*,¹⁸ the New York Court of Appeals ruled that a challenge to a municipal rezoning under the takings clause was properly evaluated using a deferential standard akin to the due process rational basis test. The court did not address the more fundamental question, which has been debated by other state and federal courts,¹⁹ of whether a claim that a regulation fails to advance a legitimate public purpose states a claim under the takings clause at all, or instead raises an issue under the due process clause.

III. THE FRIEDENBURG CASE

A. Background

In 1962, Gwendolyn Londino purchased four adjacent building lots in the Village of Southampton as a speculative investment for \$122,000. Two lots front on Shinnecock Bay and the other lots, located across a village lane, front on the ocean. The bay and ocean lots are divided from each other by a 100-foot strip of government land. The land was purchased with one deed, and a single mortgage, covering all four lots, secured a loan of \$86,500 to finance the purchase.

The investment was a spectacular success, to say the least. Ms. Londino sold the two ocean lots, a few years after acquiring them, for \$165,000, allowing her to pay off the mortgage. About fifteen years later, she sold one of the bay lots to the state for \$660,000, yielding a total seven-fold return on the original investment, before even considering the fourth lot.

In 1987, following Ms. Londino's death, the executors of her estate filed an application with DEC for a tidal wetlands permit to construct a single family residence and a septic system on

the fourth lot. Pursuant to the Tidal Wetlands Act, in 1995 the DEC rejected the application, citing both the probable adverse effects of development on fragile wetlands and the likelihood that periodic flooding would cause releases of sewage effluent into Shinnecock Bay.

The executors filed suit in the Supreme Court, which found that the Department's action constituted a taking. The trial court, focusing exclusively on the lot that was the subject of the permit application, concluded that, absent the tidal wetlands regulation, the property would have a market value of \$665,000. The court also found that the property had a value of \$31,500 subject to the regulation, primarily based on its value for private recreation and as access to Shinnecock Bay. Based on this more than 95% reduction in value, the Supreme Court found a taking.

DEC appealed, principally arguing that the claim was barred under background principles of New York nuisance law and the public trust doctrine, and that the estimated reduction in value of the one lot failed to consider the substantial profit already earned on the rest of the property.

B. The Issues

The issues the Appellate Division expressly decided in its recent opinion are relatively non-controversial. First, the court ruled that despite the greater than 95% reduction in value, the case did not constitute a taking under *Lucas*. The court read *Tahoe-Sierra* as having "narrowed" the scope of the *Lucas* test, limiting it to the situation where a regulation works a "complete elimination of value" or a "total loss." This appears to be an accurate reading of *Tahoe-Sierra*, one which other courts have embraced as well.²⁰

Second, the court ruled that, under the circumstances of the case, a greater than 95% reduction in value was sufficient to establish a taking under *Penn Central*. In particular, the court emphasized that Ms. Londino purchased the property before the tidal wetlands law was in place, and on that basis distinguished the case from *Gazza* and the other decisions in which a claimant's advance notice of a regulatory constraint defeated a taking claim.

The court can be faulted for not using another, arguably more useful measure of the economic impact of a regulation, the difference between the original purchase price of the property and the current value of the property in its regulated state.²¹ This measure usually provides a more reliable estimate of the

¹⁵ *Nollan v. California Coastal Comm'n*, 483 U.S. 825, 837, 107 S. Ct. 3141, 97 L. Ed. 2d 677 (1987).

¹⁶ *Dolan v. City of Tigard*, 512 U.S. 374, 391, 114 S. Ct. 2309, 129 L. Ed. 2d 304 (1994).

¹⁷ See *City of Monterey v. Del Monte Dunes at Monterey Ltd.*, 526 U.S. 687, 703, 119 S. Ct. 1624, 143 L. Ed. 2d 882 (1999).

¹⁸ 94 N.Y.2d 96, 699 N.Y.S.2d 721 (1999).

¹⁹ Compare *Richardson v. City and County of Honolulu*, 124 F.3d 1550 (9th Cir. 1997), *cert. denied*, 525 U.S. 871 (1998) (alleged failure of regulation to "substantially advance a legitimate state interest" states a claim under the takings clause) with *Simi Investment Co., Inc. v. Harris County*, 256 F.3d 323 (5th Cir.), *cert. denied*, 534 U.S. 1022 (2001) (claims of "illegitimate and arbitrary governmental abuse" properly rest on the due process clause, not the takings clause).

²⁰ See, e.g., *Boise Cascade Corp. v. United States*, 296 F.3d 1339, 1350 n. 8 (Fed. Cir. 2002), *cert. denied*, 123 S. Ct. 1484 (2003) ("[A] per se regulatory taking occurs when a regulation permanently destroys all economic value in the property.")

²¹ See *Walcek v. U.S.*, 303 F.3d 1349 (Fed. Cir. 2002) (holding that economic impact of regulation on property is properly assessed by comparing current market value with the unadjusted purchase price).

effect of a regulation on property value than the Appellate Division's approach of comparing the property's current market value to its hypothetical unregulated value. Given the pervasiveness of constraints on tidal wetlands development, and the consequent increase in the value of shore properties, the hypothetical unregulated value represents an inflated estimate that mostly reflects the positive effect of the regulations themselves on land values. Having said this, however, it must be acknowledged that the court's finding of a taking based on the estimated 95% reduction in value is consistent with the approach followed by some other courts.

The more remarkable part of the court's opinion is not merely its rejection of, but its complete failure to address, DEC's strongest arguments. First, DEC's defenses based on nuisance principles and the public trust doctrine appear to provide persuasive grounds for rejecting this taking claim. Certainly the release of human sewage into public waters has been repeatedly recognized as a nuisance, and the likelihood of such releases was established in this case by the explicit findings of the DEC Commissioner in the order denying the permit. Other courts around the country have repeatedly relied upon the public trust doctrine to reject takings claims based on denials of permission to fill public trust lands. The court simply ignored this aspect of the state's case.

Second, the court focused myopically on the fourth lot and ignored the fact that the original investment included three other lots and Ms. Londino had received an impressive return on her original investment. Under the parcel as a whole rule, the court was required to evaluate the claim in relation to all four lots, not the single lot subject to regulation under the tidal wetlands act. The narrow physical divisions between the lots provided no basis for disregarding the other lots, given that Ms. Londino acquired and managed all of the lots as a single unit. Again, the court simply ignored DEC's argument based on the parcel as a whole rule.

IV. CONCLUSION: AMBIGUOUS CANDIDATE FOR APPEAL

DEC faces a somewhat unusual problem in deciding whether or not to appeal this decision to the Court of Appeals. On its face, the court's decision is hardly outrageous — at least given the court's stated version of the record and the issues raised. But the Appellate Division arguably conferred an unjustified windfall on an undeserving claimant by failing to acknowledge, much less resolve, the Department's strongest arguments. In any event, the Appellate Division decision is unlikely to be the last word on the several important issues raised by this case.

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