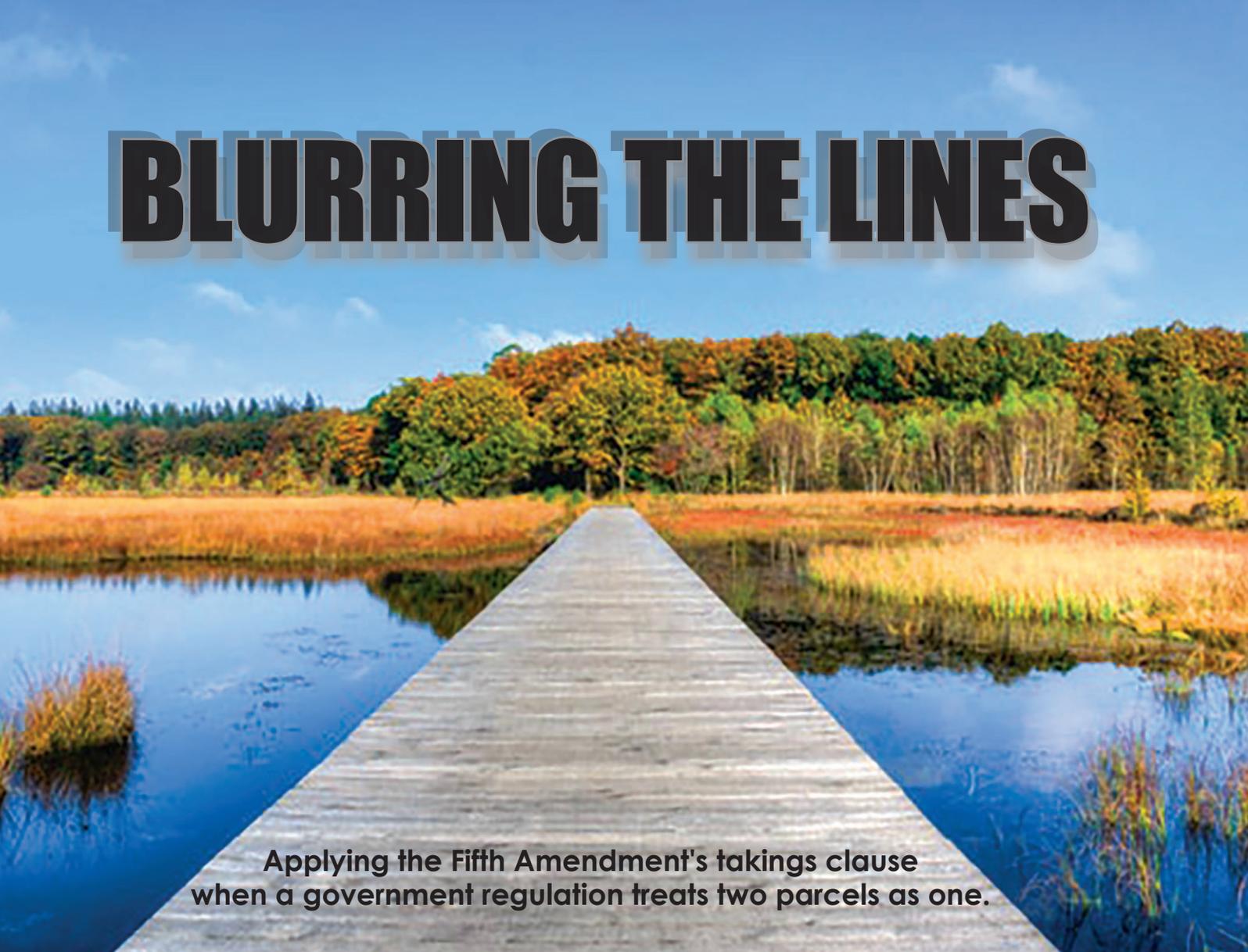


BLURRING THE LINES



Applying the Fifth Amendment's takings clause when a government regulation treats two parcels as one.

This scenic property along the St. Croix River became the focus of a lawsuit when the government barred the property owner from selling one of their two lots.

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As government regulations become increasingly pervasive, private property rights are often threatened. Depending upon the extent of the regulation, property owners may have no alternative but to seek compensation for the resulting damages.

For nearly 100 years, the U.S. Supreme Court has recognized that laws often go too far in regulating the use of private property, thereby violating the Fifth Amendment's takings clause. Since then, the Court has addressed a number of cases that involve what lawyers call "regulatory taking" claims.

The Threshold Issue

On June 23, 2017, the Supreme Court ruled on a case where private property owners were barred from selling their two river front lots separately. The plaintiffs argued that regulations set forth in state and local law, that precluded them from selling or developing one of their two lots separate from the other, constituted a "taking" of the one lot they wished to sell.

In certain situations, a threshold issue in determining whether a regulatory taking has occurred is the delineation

or definition of the “property” allegedly impacted. Sometimes a particular regulation will prohibit development of a portion of a large parcel of land or will preclude a property owner from utilizing certain aspects of the “bundle of rights” that comprise ownership of real property. When that happens, the property owner may allege that the regulation effectuates a “taking” of the impacted portion of their property. The Supreme Court has historically rejected such claims, stating that the U.S. Constitution’s Fifth Amendment protections only adhere to an entire parcel of property, not to each and every possible unit into which it may be subdivided.

While that rule may be applicable to most circumstances, there are situations where the parcel or the unit of property allegedly damaged is the subject of disagreement. Such a disagreement formed the issue presented to the Court this year in *Murr v. Wisconsin*.

The issue stems from the fact that in the 1970s, after the parents of the plaintiffs in Murr had purchased the subject property, the State of Wisconsin adopted a new law that restricted development on properties located along the St. Croix River and Lake St. Croix. The new law was designed to guarantee the protection of the wild, scenic and recreational qualities of the river for present and future generations.

Historical Background

In the 1960s, the Murr family purchased two adjacent lots—about a year apart. They built a cabin on one property (Lot F) and held the other property (Lot E) for investment purposes. For about 30 years, the Murrs held title to Lot F in the name of a family-owned business. However, they kept the title to Lot E in their own name. Each lot was deeded and taxed separately.

In 1994, the family business conveyed title to Lot F to the parents’ adult children. A year later, the parents conveyed title to Lot E to the same children. Thus, by the mid-1990s, record title to both lots was in the names of the children. About 10 years after acquiring

ownership, the children decided to make improvements to Lot F. To finance those improvements, they sought to sell Lot E. However, they quickly learned that because the 1976 law had imposed new restrictions on the lots, Lot E was unmarketable as a standalone parcel because it was no longer developable.

The Regulations

Speaking generally, the regulations precluded new development on any parcel of property that did not have at least one acre of buildable land within its boundaries. Due to its topography, Lot E, although encompassing 1.25 acres in land area, did not contain one acre of buildable area.

However, while under separate ownership, Lot E had the benefit of a “grandfather clause” that was included in the 1976 regulations. The grandfather clause meant that, despite the fact that Lot E did not include one acre of buildable land, as long as it remained in separate ownership, it could be developed regardless of the general prohibition. But if title to Lot E merged with title to an adjacent lot, Lot E would lose its grandfathered status. That merger unfortunately happened in the 1990s when title to the two lots was conveyed to the Murr children.

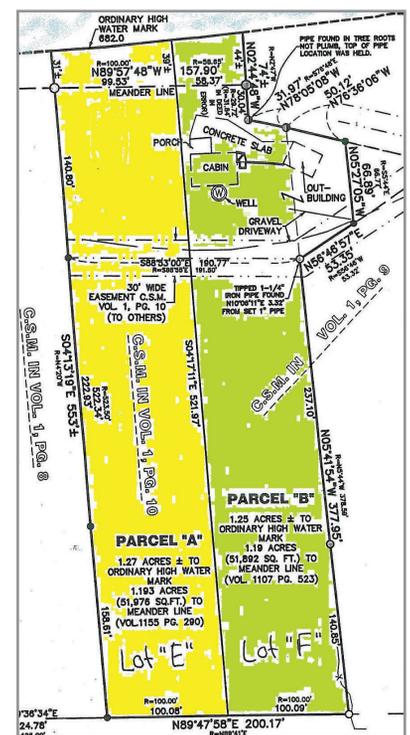
State Court Lawsuit

In 2004, when the Murr family sought to sell the investment lot, the law prohibited them from doing so unless they sold the other lot and cabin with it. So they filed a lawsuit in Wisconsin state court alleging that the 1976 law effected a regulatory taking of Lot E because it deprived them of “all, or practically all, of the use of Lot E because it could not be sold or developed as a separate lot.” They sued under the Fifth Amendment’s Takings Clause, which prohibits the government from taking private property for public use without just compensation. In effect, the 1976 law had taken their right to sell one of their two lots, a basic right of property ownership.

In examining the plaintiffs’ claim, the Wisconsin trial court first determined that Lots E and F should be considered as a single property because they were adjacent parcels that were held in common ownership and available for the same or similar uses. Under that assumption, there was no taking because—when treated as a whole—the property could and was being used for recreational housing purposes. The Wisconsin Court of Appeals affirmed for similar reasons. But in 2015, the U.S. Supreme Court granted certiorari, an order by which the higher court reviews a decision of a lower court.

Supreme Court Precedent

To decide the Murrs case, the Court first looked at its precedents. In particular, the Court turned to a 1978 decision, *Penn Central v. New York*, which introduced a three-part balancing test to determine whether a regulatory taking has occurred. Under it, a court must weigh a



1976 changes in state law barred the property owners from selling Lot E and Lot F separately.

regulation's economic impact on the property, its interference with investment-backed expectations of the owners and the character of the government action. And the crucial point is that those factors must be applied to "the parcel as a whole."

Another case the Court applied was a 1992 decision, *Lucas v. South Carolina Coastal Council*, where the Court held that an ordinance prohibiting the plaintiff from virtually all rightful uses of his property constituted a taking because it wiped out all of the property's value.

In the Murrs' case, if the lots are treated separately, as the separate deeds and property taxes have long implied, then all value in the investment lot has been wiped out by the 1976 law and, under *Lucas*, the Murrs are entitled to compensation for the taking. But with the two lots combined as one, value remains in "the parcel as a whole," under *Penn Central*. So under the *Penn Central* analysis, the state could escape paying the Murrs any compensation.

An Unexpected Affirmation

In a 5-3 decision, U.S. Supreme Court Justice Kennedy delivered the majority opinion affirming the judgment of the Wisconsin Court of Appeals. In his words, the threshold issue in the case was this: "What is the proper unit of property against which to assess the effect of the challenged governmental action?" If the unit of property is deemed to be the combined Lots E and F, the impact of the subject regulation would likely be much less severe than if the unit of property is Lot E alone.

Justice Kennedy identified a number of factors that courts must consider in order to determine what constitutes the "property" for purposes of a Fifth Amendment regulatory taking claim. Those include: 1) Treatment of the land, in particular how it is bounded or divided, under state and local law; 2) Physical characteristics like topography, surrounding development and environmental attributes; and 3) Value of the property under the challenged regulation, with special attention to the effect of the burdened land on the value of other holdings.

Applying those factors, the majority concluded that, "for purposes of determining whether a regulatory taking has occurred here, petitioners' property should be evaluated as a single parcel consisting of Lots E and F together." As its basis, the Court cited the voluntary conduct of the petitioners and their parents in transferring title to both parcels to the children after enactment of the regulation at issue, thereby effectuating what the Court called a "merger of the lots under state law." Next, the Court opined that the physical characteristics of Lots E and F, including their shape, topography and location along the river, should have indicated to the petitioners that, "public regulation might affect their enjoyment of their property..."

Finally, relying on appraisal evidence in the record, the Court explained that the value of the combined lots at \$698,300 greatly exceeded the value of Lot F alone, which was \$373,000, including the cabin. Therefore, Lot E added considerable value to Lot F, and the regulation that mandated the merger did not result in an uncompensated taking of petitioners' property interests.



Addressing the media in March 2017 was Donna Murr (center) and Pacific Legal Foundation's General Counsel John Groen (right).



The property owner simply wanted to sell their vacant lot to upgrade the 1960s cabin on the adjacent property.

“...the ordinance had taken their right to sell one of their two lots, a basic right of property ownership.”

The Facts v. Majority's Conclusion

In this case, Wisconsin law defined Lots E and F as two separate parcels for all purposes except for the 1970's regulations. Therefore, it seems unjust to use the regulations in dispute as the basis for concluding that there had been a merger of the two lots. Lots E and F have two distinct legal descriptions—they are depicted as two parcels on an approved plat and are separately assessed for property tax purposes. In essence, state and local law confirms that they were two separate parcels of property when the County sought to impose its development restriction regulations.

Dissent Respects State Property Law

Chief Justice Roberts, joined by Justices Thomas and Alito, dissented. The Chief Justice's principal objection was succinctly summarized in the opening section of his dissent: "I would stick with our traditional approach: State law defines the boundaries of distinct parcels of land, and those boundaries should determine the 'private property' at issue in regulatory takings cases."

In addition, Chief Justice Roberts noted that the majority's approach gives the government an unfair advantage in the overall regulatory takings analysis. Under the test set forth in Justice Kennedy's opinion, the government is permitted to apply the regulation to the threshold determination as to the proper unit of property. Then, after the unit of property is determined, the government may apply the regulation again to the process whereby a court makes the determination of whether the regulation effectuates a taking. "The result," according to the Chief Justice, "is that the government's goals shape the playing field before the contest over whether the challenged regulation goes 'too far' even gets underway."

The Preferable Approach

For a number of reasons, I believe that the dissent's approach is preferable. First, property rights should not be lost merely because an intra-family transfer resulted in a unification of title with regard to two subdivided lots. When the lots were originally acquired in the 1960s, they were distinct, independently developable and marketable parcels of property. The fact that the parents decided to convey the titles to their children should not deprive them of pursuing the individual development potential of either one unless the family is compensated for the deprivation.

Second, if preserving the wild and scenic qualities of such areas is of significant societal importance, the public should compensate the owners of the impacted properties. After all, that area was already subdivided, improved with roadway access and developed with housing before the regulations were enacted. Under circumstances in place when the owners had purchased the land—before the imposed development restrictions—the rights of those prior owners should be protected.

Third, property law is historically the responsibility of state and local jurisdictions. If the Supreme Court deems it appropriate to become involved in matters involving application of state regulatory law to state property law, the Court should apply the state laws without consideration of the allegedly offensive regulation. The regulation

itself should not dictate the unit of property involved in the regulatory taking analysis. Rather, it should only become significant after the unit of property has been determined.

And finally, as one of our Founding Fathers, Alexander Hamilton, observed: "the security of property is one of the great objects of government." That object can only be fulfilled if the law protects investment-backed expectations with regard to private property. By using the regulation as a consideration in its determination of the subject unit of property, the majority opinion in this case fails to achieve that fundamental objective. 🌟

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