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Takings Watch

CRC's Monthly Update on Regulatory Takings

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QUOTE OF THE MONTH

"[T]houghts of compensation are * * * simply out of place in most instances, if not quite all, of regulatory restrictions of land use. American constitutional democracy's disposition from the beginning has been to treat the bulk of these events as belonging to the normal give and take of a progressive, dynamic, democratic society. Regulation stands, in our public law, as an ordinary part of the background of risk and opportunity, against which we all take our chances in our roles as investors in property."

Frank I. Michelman, The Common Law Baseline and Restitution for the Lost Commons: A Reply to Professor Epstein, 64 U. Chi. L. Rev. 57, 69 (1997).

FEATURE CASE

Federal Appeals Court Rejects Takings Challenge to Tobacco Disclosure Law

State and local officials interested in curbing the adverse health effects of smoking should take note of the October 16, 2001 ruling in *Philip Morris, Inc. v. Reilly*, No. 00-2425, 2001 WL 1215365 (1st Cir. 2001). The ruling rejects a takings challenge to a Massachusetts statute that requires tobacco companies to disclose the ingredients in their products on a brand-by-brand basis, information that the companies claim to be trade secrets.

More than 700 additives are used in tobacco products. The challenged statute is designed to allow health professionals to study the synergistic effects of certain ingredients in particular brands. The tobacco companies allege that disclosure would allow competitors to "reverse engineer" the popular brands.

The ruling comes as a surprise because the appeals court had previously affirmed a preliminary injunction that prohibited enforcement of the statute based on the court's conclusion that the companies were likely to prevail on the takings claim. In rejecting the claim on the merits, however, the appeals court stressed that it had reconsidered the issue "with the benefit of additional briefing, argument, study, and reflection." It relied on a 1919 U.S. Supreme Court case, *Corn Products Refining Co. v. Eddy*, which states that "the right of a manufacturer to maintain secrecy as to his compounds and processes must be held subject to the right of the State, in the exercise of its police power and in promotion of fair dealing, to require that the nature of the product be fairly set forth." The appeals court also invoked a 1984 Supreme Court ruling in *Ruckelshaus v. Monsanto Co.* that the federal government could condition the right to sell pesticides on the voluntary submission of confidential trade secrets, as well as the use of that information by others. The *Monsanto* Court held that no taking occurs so long as the manufacturer is aware of the conditions under which the trade secrets are submitted and the conditions are rationally related to the public interest. The First Circuit concluded that *Monsanto* controlled the case before it and required rejection of the tobacco companies' takings claim.

OUTRAGE OF THE MONTH

Some say ignorance is bliss, but certain developer lawyers are turning ignorance into an art form. Consider a contribution to a land-use listserve moderated by the American Bar Association. In response to a request for information on treatises that discuss sprawl and smart-growth initiatives, one Louisville, Kentucky real-estate lawyer responded by denying that sprawl is a serious problem. He then stated: "I do not recommend reading a whole lot of books on the subject. * * * The only reason to read the books is to learn the language of Smart Growth so that you can use it to help your developer-clients more easily provide people with their dreams." We're all entitled to our respective opinions, but regardless of where you stand on sprawl and smart growth, it takes a special kind of head-in-the-sand arrogance for a lawyer to discourage other lawyers from educating themselves about an important social policy issue. If we're ever going to resolve the question of how to balance community rights with individual rights in the debate over sprawl, all stakeholders need to stay informed. Let's hope this remark represents a decidedly minority view among ABA members who represent developers.

EYE ON WASHINGTON

D.C. Firm Brings $1 Billion Takings Suit Against Feds

In our August issue of *Takings Watch*, we reported on the deeply disturbing nomination to the Court of Federal Claims (CFC) of Larry Block, a Senate staffer who has been a driving force behind radical takings bills for many years. Anyone who doubts the importance of the CFC should think again. Drawing comfort from the awful decision of the CFC in *Tulare Lake v. U.S.* (See May *Takings Watch*), the Washington, D.C. "property-rights" law firm of Marzulla & Marzulla recently filed a one billion dollar regulatory takings lawsuit against the United States in the CFC, challenging restrictions on irrigation water from Klamath Lake in Oregon needed to protect coho salmon and other endangered fish. The suit should fail, both because the water rights are different than those at issue in *Tulare Lake* and because *Tulare Lake* should be reversed on appeal, but the $1 billion price tag certainly illustrates the stakes at issue in the takings debate. Nancie Marzulla is the President of Defenders of Property Rights, and her husband, Roger, is the former head of the Justice Department's Environment and Natural Resources Division, which will now defend against the suit. The water withdrawal at issue marks the first time since the Klamath Project irrigation system opened in 1907 that the U.S. has acted in the interest of commercial fishers and Indian Tribes, who have suffered for years due to declining salmon runs.

ON THE HORIZON — IOLTA Redux in the U.S. Supreme Court?

Because the U.S. Supreme Court grants only a tiny percentage of the thousands of requests for review filed each year, it would be folly to guarantee that the Court will hear any particular case. But we're tempted to throw caution to the wind regarding the October 15, 2001, ruling by the U.S. Court of Appeals for the Fifth Circuit in *Washington Legal Foundation v. Texas Equal Access to Justice Foundation*, No. 00-50139. The ruling's implications are so great, its legal reasoning so shallow, and its result so starkly in tension with rulings from other federal appeals courts and state supreme courts that a grant of certiorari seems likely. Toss in the fact that the case proved worthy of Supreme Court review once before in 1998, and a return trip to the Court starts to appear highly probable.

The appeal court's ruling enjoins operation of Texas's "Interest on Lawyers Trust Accounts" (IOLTA) Program. Under this and similar programs adopted in all 50 states, the interest on funds deposited by clients with their lawyers is used to fund legal services, public legal education, indigent defense, and other programs that promote the administration of justice. IOLTA programs across the country generate tens of millions of dollars for legal service programs for the poor. Because IOLTA programs are a critical source of funding, the state and local government community filed an amicus brief in support of the government defendants when the case previously went to the Supreme Court.

When considering the takings implications of the Texas IOLTA program, the key fact to keep in mind is that the clients suffer no economic harm. No client funds qualify for the program unless they are so small and held for such a short duration that they could not generate net interest (interest minus bank fees) for the client on their own. Under the IOLTA program, however, the funds are pooled and thus generate interest. The clients do not lose a penny because without the IOLTA program, no interest would be generated at all.

In 1998, the Supreme Court ruled that the interest is a property right of the client cognizable under the Takings Clause, but it left open the issues of whether the IOLTA program works a taking and, if so, what compensation is due. On remand, the Fifth Circuit held that the IOLTA program works a *per se* taking akin to a permanent physical occupation under *Loretto*. More disturbingly, it held that the plaintiffs are entitled to injunctive relief -- a prohibition on the operation of the IOLTA program -- even though they suffered no economic loss. As noted by the dissent, just compensation for any taking would be zero, and thus there has been no violation of the constitutional prohibition against taking property without just compensation. The Fifth Circuit's holding conflicts with rulings from the First and Eleventh Circuits and the highest appellate courts of seven states, all of which have rejected takings challenges to IOLTA programs.

The lead plaintiff in the case is Washington Legal Foundation, a non-profit "property rights" group with little to gain except the satisfaction of depriving poor people of needed legal services. The dissent compared the plaintiffs to Aesop's fable about the dog who refused to allow the cow into the manger to feed on the hay, even though the hay was of no use to the dog. Let's hope the U.S. Supreme Court gives this story a happy, and just, ending.

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