LOCKE LORD® QUICK Study
Eminent Domain Practice
June 29, 2017

SCOTUS Establishes a New Three-Part Test To Determine the "Whole Parcel" in Regulatory Takings Cases

By: Jeff Mead and Clint Schumacher

Property owners who allege a regulatory taking will now need to analyze their holdings against a new, fact-specific, three-factor standard announced by the U.S. Supreme Court to determine what constitutes the owners' "whole parcel." This analysis will be required in order to evaluate the extent to which the regulation denies an owner the use of her land, which may then entitle the owner to just compensation. An owner of multiple parcels of real property, for example, will need to consider: (1) how state and local law treat all the owner's real property, including adjacent (or possibly non-contiguous) tracts; (2) the physical characteristics of the parcel; and (3) the prospective value of the regulated land as against any benefit attributable to the remaining land.

The U.S. Supreme Court announced the new standard in *Murr v. Wisconsin*, No. 15-214, 2017 WL 2694699 (U.S. June 23, 2017). A discussion of the case, including an in-depth look at the new standard, follows.

Factual background

Murr involves two adjacent lots—Lot E and Lot F—along the St. Croix river. *Murr*, 2017 WL 2694699, at *4–6. In the early 1960s, a couple purchased Lot F, titled the lot in their family plumbing company's name, and built a small recreational cabin on it. *Id.* at *5. In 1963, the couple bought the adjacent Lot E, which they titled in their own names. *Id.*

In the 1970s, the portion of the St. Croix river abutting the two lots became subject to federal, state, and local regulations passed to protect the "wild, scenic, and recreational qualities of the river for present and future generations." *Id.* at *4. One such regulation barred the sale or development of any lot with less than an acre of developable land. Neither Lot E nor Lot F had an acre of developable land, meaning they were substandard lots. *Id.* at *5. Two other provisions are relevant here. First, a grandfather clause permitted sale or development of substandard lots so long as the lots were separately owned as of January 1, 1976. *Id.* Second, a merger provision barred the sale or development of substandard, adjacent lots under common ownership. *Id.*

So as of the mid-1970s, the two separately owned, substandard, adjacent lots could have been sold or developed by virtue of the grandfather clause, and the merger clause had, at that time, no effect on the lots.

In the mid-1990s, the couple transferred ownership of both lots to their children, the petitioners in *Murr*. *Id.*

In the mid-2000s, the petitioners decided they wanted to relocate the cabin within Lot F, and wanted to sell Lot E to finance the relocation. *Id.* at *6. But the local—and later, state—government denied the petitioners' request for a variance. *Id.* The governments' argument, adopted by the courts, was that the merger provision in the 1970s regulation was triggered when the parents conveyed the lots to the petitioners ten years earlier, meaning the petitioners could not sell or develop either Lot E or Lot F individually. *Id.*

The petitioners sued, claiming a regulatory taking. *Id.* The trial court granted summary judgment to the State of Wisconsin, the Wisconsin Court of Appeals affirmed, and the Wisconsin Supreme Court denied review. *Id.* at *6–7.

Murr: Introduction

The U.S. Supreme Court affirmed in a 5-3 decision. Justice Kennedy, writing for the majority, began by discussing the two historical types of regulatory takings. First, a regulation that "denies all economically beneficial or productive use of land" constitutes a taking (a *Lucas* taking). *Id.* at *8. Second, a regulation that does not rise to the level of a *Lucas* taking can be a taking if a "complex of factors" is met, including: "(1) the economic impact of the regulation on the claimant; (2) the extent to which the regulation has interfered with distinct investment-backed expectations; and (3) the character of the governmental action" (a *Penn Central* taking). *Id.*

The crux of the problem in these cases, though, is determining "the proper unit of property against which to assess the effect of the challenged governmental action," or, in other words, "[b]ecause our test for regulatory taking requires us to compare the value that has been taken from the property with the value that remains in the property, one of the critical questions is determining how to define the unit of property 'whose value is to furnish the denominator of the fraction.'" *Id.* at *9.

This is the so-called "denominator problem." In trying to determine what the denominator should be, the Court in *Murr* rejected the bright-line rules proposed by the owners (who argued that the denominator should be Lot E alone, because it is a separate parcel under state law), *id.* at *13, and by the State (which argued that the denominator should be Lot E *and* Lot F combined by virtue of the merger provision), *id.* at *12.

Murr: The Three-Factor Test

Instead, the Court announced a three-factor test to be used to determine the denominator:

> These include [1] the treatment of the land under state and local law; [2] the physical characteristics of the land; and [3] the prospective value of the regulated land. The endeavor should determine whether reasonable expectations about property ownership would lead a landowner to anticipate that his holdings would be treated as one parcel, or, instead, as separate tracts. The inquiry is objective, and the reasonable expectations at issue derive from background customs and the whole of our legal tradition.

Id. at *11.

The first factor—how state and local law treat the property—should be given "substantial weight." *Id.* A purchaser of land "must acknowledge legitimate restrictions affecting his or her subsequent use and dispensation of the property," which does not mean that a pre-existing law would necessarily defeat a takings claim, just that a pre-existing restriction "can be one of the objective factors that most landowners would reasonably consider in forming fair expectations about their property." *Id.* For the same reason, "a use restriction which is triggered only after, or because of, a change in ownership should also guide a court's assessment of reasonable private expectations." *Id.* In *Murr*, this factor weighed in favor of treating the lots as combined because of two facts: (1) the merger provision, which the Court found to be legitimate, effected a merger of Lots E and F; and (2) the parents, armed with knowledge of the merger provision, nevertheless united ownership of Lots E and F by conveying them to the petitioners. *Id.* at *14.

The second factor—physical characteristics of the property—include "the physical relationship of any distinguishable tracts, the parcel's topography, and the surrounding human and ecological environment." *Id.* at *11. Importantly, "it may be relevant that the property is located in an area that is subject to, or likely to become subject to, environmental or other regulation." *Id.* at *11. In *Murr*, this factor also weighed in favor of treating the lots as combined. *Id.* at *14. First, the lots were bisected by a steep bluff, meaning the owners should have reasonably expected a limited ability to use the lots. *Id.* Second, the lots were located along a scenic and frequently visited river, which would lead a reasonable

person to conclude that the riverside property could be subject to regulation. *Id.* Third, the river was, in fact, subject to such regulation predating the petitioners' acquisition of the lots. *Id.*

The third factor—the prospective value of the regulated land—should include "special attention to the effect of burdened land on the value of other holdings." *Id.* at *12. The Court described this as an inquiry into whether there was a "special relationship" between the holdings: although "a use restriction may decrease the market value of the property, the effect may be tempered if the regulated land adds value to the remaining property, such as by increasing privacy, expanding recreational space, or preserving surrounding natural beauty." *Id.* The existence of such a special relationship would point to treating all the property as the denominator; the absence would point to treating only the regulated land as the denominator. *See id.* In *Murr*, this factor also supported the combined-lot denominator conclusion. *Id.* at * 15. Each lot, the Court held, benefitted from the other in "allowing increased privacy and recreational space, plus the optimal location of any improvements." *Id.* The Court also found it significant for this "special relationship" factor that Lot E was valued, subject to the restriction, at $40,000, and Lot F at $373,000, but that the value of Lot E and F combined was valued at nearly $700,000. *Id.*

The Court thus affirmed the state-court conclusion to treat the parcels as combined for purposes of establishing the denominator. *Id.* at *16.

Armed with the denominator (both lots combined), the Court then took the analysis a step further and held that a taking had not occurred under either *Lucas* or *Penn Central*. *Id.* There was no *Lucas* taking, the Court held, because the owners had not been deprived of all economically beneficial use of their property. *Id.* The owners could still use the property (i.e. both lots combined) for residential purposes, and the value of the land (i.e. both lots combined) had decreased by less than 10 percent. *Id.* And there was no *Penn Central* taking because the owners could not reasonably say they expected to sell or develop Lot E, given the pre-existence of the reasonable merger provision. *Id.*

Murr: Two Dissents

Justice Roberts, joined by Justice Thomas and Justice Alito, dissented, arguing that the Court went too far in creating a new, three-factor standard. *Id.* at *16–17 (Roberts, C.J., dissenting). Instead, Justice Roberts would have looked simply at state law for step one (determining the property at issue), which defines the boundaries of parcels of land. Then, in step two of his analysis (determining whether a taking of that property had occurred), any adjacent property under common ownership could factor into whether a taking had occurred. *Id.* at *17 (Roberts, C.J., dissenting).

Justice Thomas also dissented, claiming "it would be desirable for us to take a fresh look at our regulatory takings jurisprudence" to determine whether the Fifth Amendment even protects against regulatory takings. *Id.* at *25 (Thomas, J., dissenting).

For more information on the matters discussed in this *Locke Lord QuickStudy*, please contact the authors.

Jeff Mead | 214-740-8678 | jmead@lockelord.com
Clint Schumacher | 214-740-8587 | jschumacher@lockelord.com