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Legal Briefs

Supreme Court Favors Property Owner Rights in Development Challenge

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In June, the U.S. Supreme Court issued a significant decision concerning inverse condemnation, or regulatory takings, in the case of *Palazzolo v. Rhode Island*. The ruling states that acquisition of property with notice of a prior regulation restricting its use does not, in and of itself, bar the purchaser from claiming that the regulation constitutes a taking. This ruling has potentially significant ramifications for landowners and developers who previously had been barred from developing their land due to government regulations.

Case Background

Anthony Palazzolo owns a waterfront parcel of approximately 20 acres in Westerly, R.I., most of which is salt marsh designated as coastal wetlands under Rhode Island law. He acquired the property in 1959 through Shore Gardens, or SGI, which he formed with associates whom he later bought out.

In the 1960s, SGI submitted several different development proposals for the property, and the Rhode Island Department of Natural Resources approved one proposal to build a private beach club. It later withdrew its approval, which SGI did not contest.

In 1971, the state established the Rhode Island Coastal Resources Management Council, an agency charged with protecting coastal properties. The council adopted the Coastal Resources Management Plan, a set of regulations that designated salt marshes as protected coastal wetlands on which development is limited.

Seven years later, Palazzolo became the titleholder of the

property after SGI's corporate charter was revoked. He renewed efforts to develop the property, first filing an application that contemplated filling in all of the land, which was rejected. In 1985, Palazzolo filed another application to fill more than half of the property and develop it as a beach club. The application was rejected, because the council's regulations require a special exception for filling protected coastal wetlands that can be obtained only for compelling public purposes. Palazzolo appealed the ruling to the state courts, which upheld the council's decision.

Palazzolo then filed an inverse condemnation action alleging that the wetlands regulations, as applied to his property, deprived him of use of the property without compensation, which is in violation of the takings clause of the Fifth Amendment to the U.S. Constitution.

The Fifth Amendment states that "nor shall private property be taken for public use, without just compensation." This clause normally applies to condemnation cases in which the government must pay property owners fair-market value to take title to their properties. Inverse condemnation means that a property has been so over-regulated that it no longer has any practical use; in effect, the government has taken the property without compensation. This act also is referred to as a regulatory taking.

The state court ruled against Palazzolo, and the Rhode Island Supreme Court affirmed denial of his claims. Palazzolo then appealed the case to the U.S. Supreme Court.

Facts of the Case

Palazzolo sought more than \$3.1 million in damages, claiming he would have received that amount in profit from his proposed development. He based his argument on the Fifth Amendment's takings clause and also on Article 1, Section 16, of the Rhode Island Constitution that states, "Private property shall not be taken for public uses, without just compensation."

In rebuttal, Rhode Island maintained that Palazzolo had no right to challenge the council regulations since his ownership of the property postdated their adoption. In effect, the state court held that any purchaser or succeeding titleholder is aware of any previously enacted restrictions affecting the property and is barred from challenging it as a taking.

Rhode Island also took the position that a regulation, once enacted, becomes a background principle of state property law that cannot be challenged by those acquiring affected property after its enactment.

Rhode Island also claimed that the Palazzolo case was not ripe, or ready for judicial review. For a court to make a decision on a takings case, it must be able to ascertain the extent of potential development on a property. Rhode Island maintained that Palazzolo had not exhausted all possible development plans; therefore, the case could not be reviewed by the Supreme Court.

Supreme Court Ruling

The U.S. Supreme Court ruled that Palazzolo had the right to challenge Rhode Island's refusal to allow him to develop his property, but it stopped short of awarding him compensation.

The Supreme Court strongly disagreed with Rhode Island's first contention, noting that such a rule would eliminate the state's obligation to defend any land use restriction it imposed once title had passed to a successor owner for the first time, regardless of how extreme or unreasonable the restriction might be. The Court stated that "future generations, too, have a right to challenge unreasonable limitations on the use and value of land."

The Supreme Court also disagreed with the state's second position, noting that a regulation does not become a background principle by mere passage of title, but must be part of a shared understanding applicable to all property owners before it becomes a background principle of law.

On the ripeness issue, the Supreme Court ruled that since it was evident that the council "interpreted its regulations to bar the petitioner from engaging in *any* filling or development activity on the wetlands," forcing Palazzolo to submit further development proposals was unnecessary.

The Supreme Court did not rule on the issue of compensation and returned the case to Rhode Island for an analysis of Palazzolo's right to recovery based upon reasonable investment-backed expectations, which is a standard established by the U.S. Supreme Court in another significant condemnation case, *Penn Central v. New York City*.

As a result of this case, it now is easier for property owners to challenge regulations that prohibit development on their land. However, the ruling does not make a definitive statement on compensation, leaving clarification of the meaning of “reasonable investment-backed expectations” to future cases.

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