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NAVIGATING THE TAKINGS MAZE:
THE USE OF TRANSFERS OF DEVELOPMENT
RIGHTS IN DEFENDING REGULATIONS AGAINST
TAKINGS CHALLENGES

Jennifer Scro *

I. INTRODUCTION:
JUSTICE SCALIA VERSUS *PENN CENTRAL*

Land use regulation, at whatever scale, typically generates passionate opposition from landowners whose private property has lost value, and their negative reactions often take the form of regulatory takings challenges based on the Fifth and Fourteenth Amendments. In anticipatory response, many communities have instituted Transfer of Development Rights (“TDR”) programs to assist in defending their land use regulations against such takings challenges.¹ TDRs allow regulated landowners to sell blocks of their development rights, unusable on the regulated sites under the terms of the challenged regulations, to purchasers who can use them to expand allowable development rights on designated off-site receiving parcels.² The sale of TDRs can thus generate significant revenues for regulated property owners because purchasers are often willing to pay large sums for the right to use the

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1. As of 2010, there are approximately 239 TDR programs currently in effect or proposed in the United States. ARTHUR C. NELSON ET AL., *THE TDR HANDBOOK: DESIGNING AND IMPLEMENTING TRANSFER OF DEVELOPMENT RIGHTS PROGRAMS*, xxiv (2012).

2. *See id.* at xix-xx, xxii.

TDR credits to build at much greater intensity than otherwise allowed under existing land use regulations.³

If TDRs are weighed as part of a court's constitutional takings balance under the *Penn Central* formulation,⁴ then many such challenged land use regulations will be upheld, and the utility and market value of TDR programs will remain secure. If, instead, the market value of TDRs is excluded from the regulatory validity balance, then many regulations would in all likelihood be struck down as excessively diminishing the regulated landowners' property values. Most courts follow the holding in *Penn Central*, written by Justice Brennan, and include TDRs as part of the landowner's retained post-regulation property value in constitutional takings balances.⁵ Conversely, Justice Scalia argues, in a strongly-worded concurring opinion, that TDRs should not be considered in determining the amount of property values lost by regulated landowners; rather, they should only be considered as part of a landowner's compensation package *after* the courts, disregarding the value of TDRs, have found the challenged regulations unconstitutional.⁶ The difference between the two conflicting roles of TDRs in courtroom challenges, and the dialogue between these two approaches, will determine the future viability of TDRs as an innovative land use tool in defining the public-private balances central to land regulation.

Penn Central Transportation Co. v. City of New York is the central Supreme Court holding in the area of regulatory takings. As in *Pennsylvania Coal Co. v. Mahon*,⁷ the Court's first decision scrutinizing regulatory takings, the Court's formulation in *Penn Central* took special notice of the degree of diminution of the regulated landowner's property value.⁸ In *Penn Central*, the majority held that TDRs represent valuable

3. For example, in 2011 in Brookhaven, New York, a single TDR credit sold for about \$88,000 on average. *Pine Barrens Credit Sales 1996 through 2012*, PINE BARRENS CREDIT PROGRAM (TRANSFERS OF DEVELOPMENT RIGHTS), http://pb.state.ny.us/pbc/pbc_credit_sales_1996_to_present.pdf (last updated Jan. 1, 2014). In 2011 in Brookhaven, over twenty-six TDR credits were sold for a total sales value of over two million. *Id.*

4. See *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124-25 (1978) (discussing *Penn Central*'s ad hoc test).

5. See ARDEB G, RATHKOPF ET AL., 3 RATHKOPF'S THE LAW OF ZONING AND PLANNING § 59:17 n.2 (4th ed.) and cases cited therein.

6. *Suitum v. Tahoe Reg'l Planning Agency*, 520 U.S. 725, 747-48 (1997) (Scalia, J., concurring).

7. 260 U.S. 393 (1922).

8. Compare *id.* at 415 ("The general rule at least is that while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking."), with *Penn Cent.*, 438 U.S. at 124 ("In engaging in these essentially ad hoc, factual

property rights retained by regulated landowners and, as such, are directly relevant to the question of whether an excessive, invalid regulatory taking has occurred.⁹ Justice Brennan wrote:

While these [TDR] rights may well not have constituted “just compensation” if a “taking” had occurred, the rights nevertheless undoubtedly mitigate whatever financial burdens the law has imposed on appellants and, for that reason, are to be taken into account in considering the impact of regulation [on the regulated landowner].¹⁰

For Justice Brennan, therefore, the value of TDRs is a factor in the initial judicial determination of whether a regulation has “gone too far,” leaving the landowner with no reasonable economic return.¹¹ If a regulation is indeed invalid, however, the TDR value may not be enough to constitute sufficient “just compensation” in the circumstances.¹² Justice Scalia attacked the *Penn Central* majority’s formulation of the role of TDRs in his separate concurring opinion in *Suitum v. Tahoe Regional Planning Agency*.¹³ He put a semantic turn on the definition of remaining value in

inquiries, the Court’s decisions have identified several factors that have particular significance. The economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations are, of course, relevant considerations. So, too, is the character of the governmental action.” (citation omitted)). Thus, regulatory takings challenges are subject to the famous *Penn Central* balancing test that weighs the (1) economic impact; (2) interference with investment-backed expectations; and (3) character of government action. *Penn Cent.*, 438 U.S. at 124. This *Penn Central* triad essentially weighs private diminution against government interests. *See id.* at 124-27 (describing various applications of the triad to specific cases). The third element, “character of governmental action,” has been to denote weighing the *public’s* interest against the private diminution. PLATER, ET AL., ENVIRONMENTAL LAW AND POLICY: NATURE, LAW, AND SOCIETY 155-56 (3rd ed. 2004); *see* Leigh E. Cummings III, *Finding the Third Penn Central Prong in the Palazzolo Remand: Weighing the Public Purposes of Wetlands Protection after Palazzolo and Tahoe*, in PLATER, ET AL., ENVIRONMENTAL LAW & POLICY, NATURE, LAW & SOCIETY 42, 42, 47-48 (Supp. 2007-2008), available at http://www.aspenlawschool.com/books/plater_environmentallaw/; *see also* Palazzolo v. Rhode Island, 533 U.S. 606, 634 (2001) (O’Connor, J., concurring) (“The purposes served, as well as the effects produced, by a particular regulation inform the takings analysis.”).

9. *See Penn Cent.*, 438 U.S. at 137.

10. *Id.*

11. *See infra* pp. 14-15 and notes 34-40.

12. *See Penn Cent.*, 438 U.S. at 137.

13. *See Suitum v. Tahoe Reg’l Planning Agency*, 520 U.S. 725, 747-50 (1997) (Scalia, J. concurring).

the regulatory takings analysis, arguing that TDRs have no place in the constitutionality balance.¹⁴ Justice Scalia wrote:

Just as a cash payment from the government would not relate to whether the regulation “goes too far” . . . but rather to whether there has been adequate compensation for the taking; and just as a chit or coupon from the government . . . would relate not to the question of taking but to the question of compensation; so also the marketable TDR, a peculiar type of chit . . . relates not to taking but to compensation.¹⁵

Justice Scalia was thus insisting that TDRs could only be part of the compensation package once a court declares a regulation unconstitutional.¹⁶ As such, TDRs become nothing more than a “peculiar type of chit” or “coupon” from the government, not representing relevant value to the regulated landowner.¹⁷

Justice Scalia’s formulation was seemingly rejected by Justice Brennan’s utilization of TDRs as an essential property right to be weighed in the takings regulatory balance. Justice Scalia attempted to align his view with *Penn Central’s* holding by teasing out a distinction on the *Penn Central* facts.¹⁸ In *Penn Central*, the affected corporate property owner happened to have been able to use the TDR air rights from a regulated historic train station to substantially expand development on other properties it owned.¹⁹ Justice Scalia thus acknowledged a narrow exception to his denial of including TDR values in a *Penn Central* balancing test if a landowner could make *personal* use

14. *See id.* at 747.

15. *Id.*

16. *See id.* at 750 (“I suggest only that the relevance of TDRs is limited to the compensation side of the takings analysis, and that taking them into account in determining whether a taking has occurred will render much of our regulatory takings jurisprudence a nullity . . .”).

17. *See id.* at 747. Justice Scalia envisions TDRs as complicated governmental cash vouchers for compensation for land regulation. *Id.* Except, as Scalia notes, the cash comes from third party purchasers, rather than the government, and the government in turn reimburses the purchasers for their “outlay” with a “variance from otherwise applicable land-use restrictions.” *Id.* at 748. One commentator describes the Scalian view of TDRs as believing that TDRs are “arbitrary administrative variances from land use restrictions.” Paul Merwin, *Caught Between Scalia and the Deep Blue Lake: The Takings Clause and Transferable Development Rights Programs*, 83 MINN. L. REV. 815, 816 (1999).

18. *See Suitum*, 520 U.S. at 748-49 (Scalia, J., concurring).

19. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 137 (1978).

of the TDRs.²⁰ By restricting *Penn Central's* holding to cases where development credits can be used by the regulated landowners themselves, Justice Scalia thereby separates TDRs from their status as “market value” rights and asserts that TDRs “have nothing to do with the use or development of the land to which they are (by regulatory decree) ‘attached.’”²¹

Justice Scalia was so disturbed by TDRs as a factor in the constitutional balance that he argued: “taking [TDRs] into account in determining whether a taking has occurred will render much of our regulatory takings jurisprudence a nullity.”²² He was perhaps building upon the not-unreasonable fear that to escape constitutional liability some governments might implement illusory TDR programs where the TDRs would, in reality, have minimal value.²³ TDR programs, however, cannot serve in the constitutional balance as an escape valve for government liability in regulatory takings challenges if the TDRs have little value.²⁴ All TDRs should be subjected to actual market value

20. *See Suitum*, 520 U.S. at 748-49 (Scalia, J., concurring). Justice Scalia reasoned that TDRs can be part of the constitutionality balance if transferred to a nearby lot owned by the same landowner, as had occurred in *Penn Central*. *Id.* He wrote:

This [*Penn Central*] analysis can be distinguished from the case before us on the ground that it was applied to landowners who owned at least eight nearby parcels, some immediately adjacent to the terminal, that could be benefited by the TDRs. The relevant land, it could be said, was the aggregation of the owners’ parcels subject to the regulation (or at least the contiguous parcels); and the use of that land, as a whole, had not been diminished. It is for that reason that the TDRs affected “the impact of the regulation.” *Id.* at 749 (citation omitted). For Scalia, therefore, TDRs represent an essential property right only when property owners are able to transfer credits to other parcels they own. Although Scalia typically refuses to look beyond the sending parcel for the takings analysis, *see id.* at 750, when regulated landowners can transfer TDRs to their own property, Scalia considers both the sending and receiving parcel.

However, by confining TDRs to compensation and carving out an exception for personal use, Scalia deprives TDRs of their usefulness and value. If TDRs do not represent real property rights with the potential to offset government liability in the regulatory validity analysis, then local governments have little incentive to implement TDR programs. Moreover, even if local governments create a TDR program there could be no TDR market because landowners could only transfer the credits to their own property. If a landowner does not own another parcel in the receiving area, the TDR is essentially worthless.

21. *See id.* at 747.

22. *Id.* at 750.

23. *See infra* pp. 30-32 and notes 62-67.

24. *See, e.g.,* *Fred. F. French Investing Co. v. City of New York*, 350 N.E.2d 381, 387-88 (N.Y. 1976) (finding the specific TDRs at issue worthless).

analysis,²⁵ and if their value is limited then their weight in constitutional balancing is accordingly minimized.

Ultimately, Justice Scalia's formulation in his separate *Suitum* opinion appears to be an attempt to increase the burden on governments defending regulations by deploying a combination of semantic distinctions. On one hand, as noted above,²⁶ he restricted the role of TDRs in the takings validity balance to situations of personal use by regulated landowners rather than acknowledging their marketability. As a corollary semantic distinction, he thus sought to define TDRs in takings challenges in terms of the regulated landowners' diminished property *use* rather than diminished *value*.²⁷ Unless the landowners themselves could "use" the TDRs, they would not be weighed. Their market *value* to the landowner would not be acknowledged under the Scalian formulation. The standard post-*Penn Central* constitutionality balance, however, does not turn on "use," but rather turns on the degree to which affected landowners retain property *value* post-regulation.²⁸ Because TDRs primarily serve to allow regulated landowners to recapture lost value by selling them in the marketplace, Justice Scalia's semantic redefinition provides no place for TDRs in the constitutionality balance.

The difference between Justice Brennan and Justice Scalia's views is not merely an interesting semantic or theoretical tension, but rather a major issue in attacks on regulatory programs that use TDRs as part of their fairness balances. If, as Justice Scalia argues, TDRs cannot be weighed toward the validity of regulatory programs, there is little practical governmental motivation to merely issue "coupons"²⁹ to compensate for unconstitutional takings.³⁰ Consequently, the usefulness and functionality of TDR programs would be lost. TDR programs are

25. TDRs are only valuable insofar as there is a viable market demand for them. If few or none of a specific TDR program's credits are being bought and sold, or are sold at a very low value, then the TDR's weight in the constitutionality balance is accordingly reduced. See e.g., *Fred F. French Investing Co., Inc. v. City of New York*, 350 N.E.2d at 388 (1976) (finding that TDRs had no effect on the validity given that the credits were worthless because there was no designated receiving area).

26. See *supra* note 20 and accompanying text.

27. Franklin G. Lee, *Transferrable Development Rights and the Deprivation of All Economically Beneficial Use: Can TDRs Salvage Regulations That Would Otherwise Constitute A Taking?*, 34 IDAHO L. REV. 679, 707-08 (1998).

28. See *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 350 (2002) ("[T]he categorical rule in *Lucas* was carved out for the extraordinary case in which a regulation permanently deprives property of all *value*.").

29. *Suitum*, 520 U.S. at 747 (Scalia, J., concurring).

30. NELSON, *supra* note 1 at 100 ("[T]he *Suitum* decision may spell the beginning of the end for TDRs as protection against takings challenges.").

only viable if the TDRs themselves are rightfully considered by courts to be both an essential property right and a fungible market asset.

Among the many local government land use initiatives at stake in the debate over the viability of TDR programs are programs like conservation, open space, floodplain management, historic preservation, agricultural, and other regulations where, under worsening economic conditions, municipalities lack the funds needed to acquire fee simple interest. TDRs, however, allow local governments to implement such regulations, which would otherwise be economically excessive, without purchasing the protected land outright. Yet, if TDRs are relegated to the status of conjectural government coupons, as Justice Scalia insists, then TDRs' potential to mitigate the property value impact of local government land use efforts is substantially undercut.³¹ This Article analyzes TDRs as part of a property owner's "bundle of sticks" and therefore argues that their market value should be a mitigating factor in a takings analysis. The second part of this Article notes the basic features of effective TDR programs. Part III then explores the nuances of Justice Scalia's arguments limiting the utility of TDRs in takings challenges. Part IV concludes that TDRs represent essential property rights and as such should be a functional factor in constitutionality balances as well as considerations of compensation should a court nevertheless find a regulation invalid.

II. TDR BASICS

Many communities implement TDR programs for their regulatory utility.³² In the classic zoning setting, transfers of development rights allow landowners to sever their rights to develop and sell those rights to another landowner to allow the receiving parcel to build at greater density than would otherwise be permitted under local zoning regulations.³³ "Sending parcels" are typically regulated for lower density or environmental or historical significance, where protective regulations can severely diminish allowed uses and thereby the market value of the regulated areas.³⁴ The following illustration from the Huron River

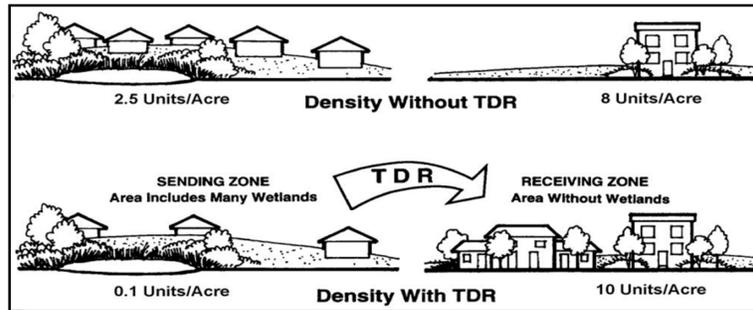
31. *Suitum*, 520 U.S. at 747 (Scalia, J., concurring).

32. See NELSON, *supra* note 1, at xix; Lee, *supra* note 27, at 679-80.

33. Lee, *supra* note 27, at 680.

34. Rick Pruetz and Erica Pruetz, *Transfer of Development Rights Turns 40*, 59 AM. PLANNING ASS'N, PLANNING AND ENVTL. LAW 1 (2006).

Watershed Council in Ann Arbor, Michigan depicts how density credit type TDRs can operate.³⁵



Illus. 1. Reprinted from Huron River Watershed Council, *Economic Approach to Watershed Protection*, <http://www.hrwc.org/publications/smart-growth-publications/transfer-of-development-rights/> (last visited Feb. 1, 2014).

TDRs help alleviate the economic burden of land use controls by allowing regulated landowners to recapture some lost economic benefit by selling TDRs. Consequently, the “receiving parcels” are often designated growth areas that attract developers with the ability to build beyond the constraints of zoning. Effectively implemented TDR programs, therefore, can preserve environmentally sensitive and historically significant areas while spurring local development.

TDRs have real economic value if well designed, which requires (1) clear sending and receiving parcels, and (2) a demand for the TDR rights in a functioning TDR market.³⁶ A sending district is the area where TDR credits originate. Thus, parcels in the sending district are typically protected by some regulation, and landowners are eligible for TDR credits. Alternatively, the receiving district is where the credits can be transferred. For example, the map pictured below illustrates a TDR program on Long Island, New York meant to preserve the Long Island Pine Barrens. This map makes clear the preserved parcels eligible for

35. Huron River Watershed Council, *Economic Approach to Watershed Protection*, <http://www.hrwc.org/publications/smart-growth-publications/transfer-of-development-rights/> (last visited Feb. 1, 2014).

36. NELSON, *supra* note 1 at 53; see Pruetz, *supra* note 34, at 4-5 (detailing TDR “success factors” and the actual detailed and complicated mechanics of a well-functioning TDR program); John J. Costonis, *Development Rights Transfer: An Exploratory Essay*, 83 YALE L.J. 75 (1973); see generally NELSON, *supra* note 1 (providing overview of the basic features of TDR programs, the economics behind TDRs, TDRs’ relationship with planning, and a model TDR ordinance).

TDR credits in the darker sending district, and the area the TDRs can be transferred to in the lighter-shaded receiving district.³⁷ If a TDR program fails to designate a clear receiving district, then the TDRs will be worthless because the credits cannot be sold and used. Similarly, to be truly valuable, TDR credits must be an attractive purchase to create a functioning TDR market.³⁸ Often, TDR markets work best with a TDR “bank” to serve as an intermediary between the sellers and buyers.³⁹

Ultimately, TDR programs are tailored to the specific needs of each individual community. Accordingly, the relative value of TDRs varies greatly.⁴⁰ Towns can use TDRs to preserve a wide variety of areas including agricultural lands, historical monuments, and environmentally sensitive property.⁴¹ Due to the broad range of TDRs’ utility, the type of TDR will depend on the stated goals of the specific TDR program.

If TDR values are excluded from the regulatory validity balance, then in many cases, regulations will be economically excessive. TDRs can potentially mitigate government liability in takings because the value of the credits offsets the economic impact of the regulation. TDRs allow a landowner to recapture the diminished property value caused by the regulation. For example, assume that before regulation Parcel A was worth \$100,000 but after is worth \$50,000; if the regulated landowner also receives \$30,000 worth of TDR credits, then the owner can recover \$30,000 of the \$50,000 in lost value. However, if the owner of Parcel A receives credits that are essentially worthless, the landowner cannot recover any lost value. Accordingly, such TDRs should have little effect

37. NEW YORK STATE’S CENTRAL PINE BARRENS, *Long Island Pine Barrens Protection Areas*, http://pb.state.ny.us/maps_pdf/backup_Map-LIPB_core_cga_acres_map.pdf (last visited Feb. 1, 2014). Note that this map is meant to be illustrative. *Id.* The final receiving areas do not correspond exactly to the compatible growth areas. A map of the actual receiving areas in Riverhead, New York is available in *Proposed Final Central Pine Barrens Plan and Supplement Draft Generic Environmental Impact Statement*, Chapter 6 Pine Barrens Protection Program, 90-91 (1995). Although the actual receiving areas are more limited than the compatible growth areas depicted on the included map, the TDR program in the Long Island Pine Barrens has nonetheless been successful. For example, in 2013 in Riverhead, New York, the average value of one “Pine Barrens credit” was \$58,598.48. NEW YORK STATE’S CENTRAL PINE BARRENS, *Pine Barrens Credit Sales 1996 through 2013*, http://pb.state.ny.us/psc/psc_credit_sales_1996_to_present.pdf (last visited Mar. 8, 2014).

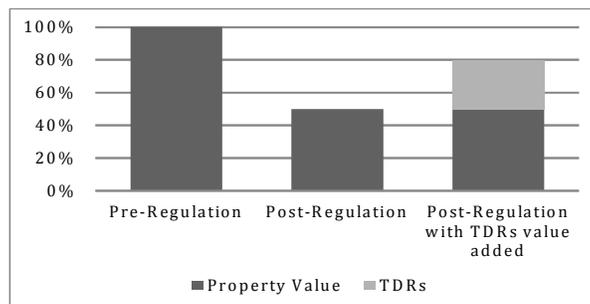
38. NELSON, *supra* note 1, at 53.

39. Sarah J. Stevenson, *Banking on TDRs: The Government's Role As Banker of Transferable Development Rights*, 73 N.Y.U. L. REV. 1329, 1341-43 (1998).

40. Merwin, *supra* note 17, at 833 (“The exact form of development rights varies with each specific TDR program.”).

41. *See id.*; Pruetz, *supra* note 34, at 1.

in reducing government liability. The graphic below depicts how TDRs allow regulated landowners to recover this lost value.



III. INTO THE MAZE:

DEBATING TDRs' ROLE IN THE TAKINGS VALIDITY BALANCE

Should TDRs be a factor in the courts' takings validity balance, or simply a form of compensation? Section A presents Justice Brennan's position in *Penn Central* that TDRs are a "mitigating" factor in the takings analysis. Section B explains Justice Scalia's position in *Suitum* that TDRs are governmental "coupons" that can only be used for compensation once a court finds a taking invalid. Finally, Section C argues that Justice Scalia's argument is an attempt to use TDRs to refocus the takings analysis on the lost property uses, rather than diminished economic value, thereby undercutting the validity of regulations.

A. The *Penn Central* View: TDRs as "Mitigating" Factor

In its landmark takings decision *Penn Central Transportation Co. v. City of New York*, the United States Supreme Court considered TDRs as part of the takings balance.⁴² The *Penn Central* Court held that the

42. See 438 U.S. 104, 137 (1978); NELSON, *supra* note 1, at 100. Some commentators suggest that *Penn Central* is contradictory on this point because later in the case the court refers to TDRs in its compensation analysis. Merwin, *supra* note 17, at 836; *Penn Cent.*, 438 U.S. at 122 ("whether the transferable development rights afforded appellants constitute 'just compensation' within the meaning of the Fifth Amendment."). This Article, however, asserts that this language is not contradictory. Rather, the *Penn Central* court rightly noted that TDRs could be considered for *both* the constitutionality of the taking and for compensation. The usefulness of TDRs to offset regulatory takings is not limited to either mitigation or compensation, but should be considered for both determinations.

constitutionality of a regulation depends on an ad hoc contextual balance of (1) the character of government action, (2) the regulation's economic impact, and (3) its interference with investment-backed expectations.⁴³ Regarding TDRs' place in this determination, Justice Brennan reasoned that the TDRs must be part of the constitutional balance.⁴⁴

Ultimately, the *Penn Central* balance is meant to weigh government interests against the diminution in property value caused by the regulation in question,⁴⁵ in a constitutional context of democratic fairness.⁴⁶ Thus, because TDRs offset the economic impact of the regulation upon the private landowner, Justice Brennan found that TDRs must be a factor in determining whether an unconstitutional taking has occurred.⁴⁷

Subsequently, other cases applied *Penn Central*'s balancing test to further define the modern regulatory takings framework.⁴⁸ In 1987, in *Keystone Bituminous*, the Supreme Court clarified that in determining the value that a landowner has lost with the imposition of the regulation, courts should look to the pre-regulation value of the landowner's entire "parcel-as-a-whole," rather than simply the regulated property portion or right.⁴⁹ Additionally, Justice O'Connor's concurrence in *Palazzolo* reasoned that in weighing the character of government action, courts should not only consider diminution in value, but also the public purpose of the regulation.⁵⁰ Finally, the *Tahoe-Sierra Preservation Council* court further highlighted that reasonable remaining value is the true measure of regulatory takings analysis, rather than the remaining uses available post-regulation.⁵¹ In sum, the modern regulatory takings analysis weighs the

43. *Penn. Cent.*, 438 U.S. at 124.

44. *Id.* at 137.

45. PLATER, *supra* note 8, at 1146.

46. *Id.* at 1154 (Justice O'Connor's *Palazzolo* concurrence emphasizes public-private democratic fairness balance).

47. *Penn. Cent.*, 438 U.S. at 136.

48. See PLATER, *supra* note 8, at 1155.

49. The same could be said of *Penn Central* in that the court did not consider the loss of air rights separately from the potential economic profitability of the entire terminal. Thus, the *Penn Central* court also weighed the private diminution against the pre-regulation economic value of the entire parcel, rather than simply the loss of the regulated air rights.

50. *Palazzolo*, 533 U.S. at 634 (O'Connor, J., concurring); PLATER, *supra* note 8, at 1154.

51. See *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 331 (2002).

diminution of private property value of the parcel as a whole against the regulation's public purpose.⁵²

Accordingly, one reason that the *Penn Central* court may have included TDRs as a factor in the takings analysis is because the *Penn Central* TDRs were indeed valuable. In *Penn Central*, the Penn Central Transportation Co. claimed a taking after New York City's Landmark Preservation law prohibited the company from building an office building over Grand Central Terminal. The regulation effectively reduced the permissible zoning height over Grand Central, preventing Penn Central Co. from utilizing its air rights over the Terminal. New York City's TDR program, however, allowed the company to transfer development rights to other parcels to build higher than the maximum permissible zoning height requirements in place. Nevertheless, Penn Central Transportation Co. could only transfer the credits to a limited number of parcels, and the process for receiving a transfer permit was complex, among other problems.⁵³

In recognizing these imperfections, the majority noted that "[a]lthough appellants and others have argued that New York City's transferable development-rights program is far from ideal, the New York courts here supportably found, at least in the case of the Terminal, the rights afforded are valuable."⁵⁴ Here, the majority clearly regards the TDRs' value as the most important feature for the credits' stake in the takings analysis. A TDR credit can be limited and imperfect, but so long as it retains legitimate economic value, it can still be used to mitigate government liability in regulatory takings challenges.⁵⁵ Therefore, the amount that a TDR can mitigate the economic impact of the regulation will depend directly on the TDR's real market value.⁵⁶

Justice Brennan reasoned that TDRs should be a factor in the regulatory validity balance because they represent a valuable asset property right in the bundle of sticks.⁵⁷ By framing TDRs as a property right included in the constitutional balance, Justice Brennan drew from the arguments in the brief for the City of New York.⁵⁸ The City argued

52. PLATER, *supra* note 8, at 1155.

53. John J. Costonis, *The Chicago Plan: Incentive Zoning and the Preservation of Urban Landmarks*, 85 HARV. L. REV. 574, 585-89 (1972); *Penn Cent. Transp. Co. v. City of New York*, 366 N.E.2d 1271, 1277 (1977), *aff'd*, 438 U.S. 104 (1978).

54. *Penn. Cent.*, 438 U.S. at 137.

55. *See id.*

56. *See id.*

57. *See id.*

58. *See* Brief for Appellees at 20, *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104 (1978) (No. 77-444), 1978 WL 206883 at *11, *15.

explicitly that because the right to develop is a stick in the bundle of property rights, the Penn Central Transportation Co.'s TDRs represented a "valuable asset" that was fungible in the marketplace.⁵⁹ Consequently, the City reasoned that given that TDRs represented a valuable market asset, the development credits preserved the economic value of the air rights above the terminal.⁶⁰

*B. Justice Scalia Responds:
TDRs as Merely Relevant in Calculating Compensation*

In contrast to the *Penn Central* formulation, in his concurring opinion to *Suitum*, Justice Scalia argued that TDRs are not an essential property right that might mitigate takings liability, but rather a "coupon" from the government.⁶¹ For Scalia, TDRs merely represent an *in lieu* of cash "chit" that governments can use to pay affected landowners.⁶² As such, TDRs represent a form of compensation, relevant only after a court has declared a regulation invalid.⁶³ By removing TDRs from the initial validity review, moreover, Scalia's formulation would clearly substantially multiply the number of regulations struck down as invalid.

Justice Scalia defined the transfer of TDRs as the creation of a new unit rather than a valuable property right in itself, thereby erasing TDRs' applicability in the takings balance:

TDRs, of course, have nothing to do with the use or development of the land to which they are (by regulatory decree) "attached." The right to use and develop one's own land is quite distinct from the right to confer upon someone else an increased power to use and develop *his* land. The latter is valuable, to be sure, but it is a *new* right conferred upon the landowner in exchange for the taking, rather than a *reduction* of the taking.⁶⁴

Here, Justice Scalia appears to admit that TDRs can have potential value, but attributes that value not to the affected land, but to rather the artificial new credit purchasable by the person buying the credit.⁶⁵ By severing the value from the land affected by the regulation, Justice Scalia strips

59. *See id.*

60. *See id.* at 15.

61. *Suitum*, 520 U.S. at 747 (Scalia, J., concurring); NELSON *supra* note 1, at 100-01.

62. *Suitum*, 520 U.S. at 747-48.

63. *Id.*

64. *Id.* at 747.

65. Lee, *supra* note 27, at 700.

TDRs of their usefulness in defending the regulation.⁶⁶ TDRs can only mitigate government liability to the extent that their value offsets the economic impact of the regulation upon the landowner's property.⁶⁷ To mitigate liability, the value of the TDR must inherently be attributable to the affected landowner.⁶⁸ Under Justice Scalia's reasoning, however, any potential for TDRs to mitigate the economic impact on the regulated landowner becomes moot as it is not a "use" of the landowner's land, and the economic value is only to whomever buys the credits.⁶⁹ By severing TDRs' value from the affected landowner's property, Justice Scalia is able to justify his position that TDRs have no place in the constitutional balance.⁷⁰

Problematic elements and potential uncertainty in the particular Lake Tahoe TDR program in *Suitum* may have enhanced Justice Scalia's rejection of TDRs as a property right.⁷¹ Whereas *Penn Central's* TDRs had a restricted receiving area and a complex but financially tangible permit system, Lake Tahoe's TDR program was far more complex, unusual, and uncertain.⁷² Although the Court ultimately upheld the Lake Tahoe regulation, the value of the *Suitum* TDR credits was quite uncertain because landowners could only use some types of TDR credits if they also received an additional type of credit distributed through a lottery system.⁷³ Thus, the value of the plaintiff's TDRs was in doubt, considering that the one TDR credit she received had limited

66. See NELSON, *supra* note 1, at 100.

67. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 137 (1978).

68. *Id.*

69. See *Suitum*, 520 U.S. at 747 (Scalia, J., concurring).

70. See *id.*; see also Lee, *supra* note 27, at 700; NELSON, *supra* note 1, at 100.

71. R.S. Radford, *Takings and Transferable Development Rights in the Supreme Court: The Constitutional Status of TDRs in the Aftermath of Suitum*, 28 STETSON L. REV. 685, 691 (1999) (ultimately, because plaintiff never applied for the TDR program, the value of her TDR credits was unknown. Consequently, the Supreme Court held that case was not ripe for adjudication).

72. See *id.*

73. Tahoe Regional Planning's TDR program allowed landowners to receive three types of TDRs: (1) Residential Development Right (RDR); (2) Land Coverage Rights (LCR); and (3) Residential Allocations, which were awarded by lottery system. To build using these credits a landowner needed both a RDR and RA. Because plaintiff's parcel was located in the received area, it automatically had an RDR credit with the possibility of receiving three bonus TDR credits. RA credits, however, were only distributed by lottery. At least one commentator defended TRPA's lottery system as possibly "the most fair and equitable way to spread the burden of TRPA's development restrictions over similarly situated landowners." Lee, *supra* note 27, at 706. Still, RA credits were the most valuable TDRs, and the plaintiff had only a one in five chance of receiving it by lottery. See Radford, *supra* note 71, at 691.

independent fungibility.⁷⁴ In contrast, the *Penn Central* TDR program, however imperfect, was far more typical of TDRs in that all of the *Penn Central* credits were independently useful and valuable (on the regulated owner's other properties or any other properties within the designated receiving area).⁷⁵ The vagueness of the Lake Tahoe TDR program is perhaps one reason that Justice Scalia used it as an opportunity to portray TDRs as only a form of compensation, and a very minimal compensation, rather than a valuable property right in the constitutionality balance.⁷⁶

Despite Justice Scalia's contrary arguments, many courts have followed the *Penn Central* holding by weighing TDRs in the takings validity balance in determining the economic impact of the regulation and its interference with investment-backed expectations.⁷⁷ For example, in *Gardner v. New Jersey Pineland Commission*, the New Jersey Supreme Court directly considered TDRs as a significant factor in the takings balance.⁷⁸ In *Gardner*, a farm owner challenged the state's Pineland protection regulations that severely limited residential development and restricted all undeveloped land to agricultural use as an invalid uncompensated taking.⁷⁹ The regulations created a TDR program for landowners in the Pineland protection area who incorporated the regulation's restrictions into their deeds. Once in conformity with the regulations, the New Jersey Pineland Commission awarded these landowners with Pineland Development Credits (PDCs) that enabled landowners to sell their development rights in "designated Regional Growth Areas."⁸⁰ Although many PDCs sold "privately at market prices," at least one county's PDC bank reported payments of \$10,000 per credit.⁸¹ In upholding the constitutionality of the regulations, the *Gardner* court adopted Brennan's view that TDRs should be incorporated into the takings balance: "Penn Central could offset its loss by transferring valuable property rights to other properties, even if such transfers did not fully compensate it. Plaintiff possesses the similar right to offsetting benefits; it may receive Pinelands Development Credits in return for recording the deed restrictions."⁸² Thus, the potential

74. See Radford, *supra* note 71, at 691.

75. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 137 (1978).

76. See Radford, *supra* note 71, at 691.

77. See RATHKOPF, *supra* note 5, § 59:17 n.2 (4th ed.) and cases cited therein.

78. *Gardner v. New Jersey Pinelands Comm'n*, 593 A.2d 251, 261 (1991).

79. *Id.* at 253.

80. *Id.* at 256.

81. *Id.*

82. *Id.* at 261.

economic value of the PDCs factored into the *Gardner* court's application of the *Penn Central* constitutionality balance.

Likewise, in *Aptos Seascape Corp. v. County of Santa Cruz*, the California Supreme Court rejected a facial takings challenge to a zoning ordinance that designated property open space because the ordinance also permitted the plaintiff to receive compensating density credits on adjoining parcels.⁸³ Aptos Seascape Corporation (Seascape) had purchased 110 acres on the California coast.⁸⁴ Subsequently, the county adopted a comprehensive plan⁸⁵ that designated seventy of these acres "[o]pen reserve park playground."⁸⁶ The zoning ordinance, however, also permitted the company to receive transferrable density credits.⁸⁷ These credits allowed Seascape to build at a greater intensity than normally permitted under zoning regulations on its remaining forty acres that were not designated as open space.⁸⁸ In upholding the validity of the ordinance, the court reasoned that because Seascape could receive and utilize the density credits, it was "free to pursue [its] reasonable investment expectations."⁸⁹ The *Aptos Seascape* court, therefore, weighted the potential value and utility of the transferrable density credits in determining the regulation's constitutionality.⁹⁰

Still, TDRs cannot entirely shield government from takings liability. A taking can still be unconstitutional despite the presence of a TDR program if the TDRs are insufficiently valuable. In *Fred French F. Investing Co., v. City of New York*, the New York Court of Appeals rejected a zoning amendment as unconstitutional, despite the amendment's TDR program, because the city did not designate any receiving parcels for the credits.⁹¹ Without available receiving parcels,

83. *Aptos Seascape Corp. v. County of Santa Cruz*, 188 Cal. Rptr. 191, 199-200 (Cal. Ct. App. 1982).

84. *Id.* at 193.

85. A "comprehensive plan" outlines the city or town's goals and reasoning for its local land use regulations for a period of time. California is known as a "plan state," meaning that local governments are required by state statute to implement such plans. See DANIEL R. MANDELKER, *LAND USE LAW* § 3.16 (5th ed. 2003); Daniel J. Curtin, Jr. & Jonathan D. Witten, *Windfalls, Wipeouts, Givings, and Takings in Dramatic Redevelopment Projects: Bargaining for Better Zoning on Density, Views, and Public Access*, 32 B.C. ENVTL. AFF. L. REV. 325, 332 (2005).

86. *Aptos Seascape Corp.*, 188 Cal. Rptr. at 193.

87. *Id.* at 200.

88. *See id.*

89. *Id.*

90. *See id.*

91. *Fred F. French Investing Co., v. City of New York*, 350 N.E.2d 381, 388-89 (N.Y. 1976).

the TDRs were only “disembodied abstractions of man’s ingenuity, float[ing] in . . . limbo,” and, therefore, essentially worthless.⁹² The court, however, made clear that *valuable* TDRs would still be considered in determining a regulation’s validity:

[T]he development rights are an essential component of the value of the underlying property because they constitute some of the economic uses to which the property may be put. As such, they are a potentially valuable and even a transferable commodity and may not be disregarded in determining whether the ordinance has destroyed the economic value of the underlying property.⁹³

Given that TDRs’ weight in the validity balance is contingent on their economic value, if the TDRs are worthless, as in *French*, they will have no impact on the balance.⁹⁴

92. *Id.* at 388.

93. *Id.* at 387.

94. Despite the fact that TDRs do not automatically circumvent takings liability under the *Penn Central* takings balance, Scalia feared that local governments could use TDR programs to circumvent liability under what would otherwise constitute an unconstitutional taking under his holding in *Lucas*. See Merwin, *supra* note 17, at 841-43. Writing for the majority in *Lucas*, Justice Scalia held that a regulation that deprives a landowner of all economic value is a categorical taking. *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1015 (1992). Unlike *Penn Central*, the *Lucas* analysis did not balance or consider the weight of government interests at all. See *id.* If, however, a TDR regulation grants regulated landowners viable and valuable credits, the landowners retain some economic value and, therefore, do not fall under *Lucas*’s *per se* taking rule. Merwin, *supra* note 17, at 842-43. Regulations that fall short of *Lucas*’s complete economic deprivation standard—as virtually all do—are analyzed under the *Penn Central* balancing test. *Tahoe-Sierra Pres. Council v. Tahoe Reg’l Planning Agency*, 535 U.S. 302, 303 (2002) (“*Lucas* was carved out for the “extraordinary case” in which a regulation permanently deprives property of all use; the default rule remains that a fact specific inquiry is required in the regulatory taking context.”). Moreover, if, as in *French*, the TDRs are worthless, the credits will not relieve the government of liability under either *Lucas* or *Penn Central*. Nevertheless, it could well have been the potential of TDRs to “sidestep” *Lucas* that prompted Scalia to argue that allowing TDRs as mitigation in the takings analysis would “render much of our regulatory takings jurisprudence a nullity.” *Suitum v. Tahoe Reg’l Planning Agency*, 520 U.S. 725, 749 (1997) (Scalia, J. concurring); Merwin, *supra* note 17, at 840-41.

*C. Justice Scalia's Use of TDRs to Reorient the
Focus of the Takings Analysis on Diminished Property Use*

Justice Scalia's framing of the takings review role of TDRs focuses on the degree of actual *use* rights in regulated land before and after regulation, rather than the *value* of the land to the regulated landowner.⁹⁵ Framed this way, because TDRs do nothing to mitigate the diminished use of a regulated parcel they are irrelevant to a Scalian takings test and regulations will more easily be struck down.

Even if TDRs allowed an affected landowner to re-capture *the entire value lost* due to regulation, Justice Scalia's emphasis on regulated use rather than value would mean that the regulation could nevertheless still be void as an excessive regulatory burden on the landowner.

Justice Scalia's stratagem, reframing TDRs to undercut regulations' validity, echoes similar previous attempts where he focused on properties' active *use* rather than owners' remaining property *values*. In *Lucas v. South Carolina Coastal Council*, he asserted that regulation is categorically unconstitutional when it "denies an owner economically viable *use* of his land."⁹⁶ Although in *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, the Supreme Court clarified that diminished *value* is the true focus of the taking analysis,⁹⁷ Scalia strongly disagreed by joining the Thomas dissent, which stressed the importance of deprived use over diminished value: "[n]o one seriously doubts that the land-use regulations at issue rendered petitioners' land unsusceptible of *any* economically beneficial use. . . . These individuals and families were deprived of the *opportunity to build* single-family homes . . . on land upon which such construction was authorized when purchased."⁹⁸

Thus, Scalia regards the takings analysis as protecting landowners' *physical uses* of their property. Inherently suspicious of government regulation, Scalia's "use" formulation would create an even lower threshold for regulatory invalidity because lost use definitions tend to

95. See Lee, *supra* note 27, at 708-09.

96. *Lucas*, 505 U.S. at 1016 (emphasis added) (quoting *Agins v. City of Tiburon*, 447 U.S. 255, 260 (1980)).

97. *Tahoe-Sierra*, 535 U.S. at 331; see also PLATER, *supra* note 8, at 1160-61.

98. *Tahoe-Sierra*, 535 U.S. at 355 (Thomas, J., dissenting) (emphasis added). Scalia's opinions evince a marked antagonism to regulation of private property, even referring to government as a "thief" in his *Palazzolo* concurrence. *Palazzolo v. Rhode Island*, 533 U.S. 606, 637 (2001) (Scalia, J., concurring). Thus, for Scalia, one way to protect landowners from this governmental "thief" is to relegate TDRs to a government "coupon" and confine their viability merely to post-verdict compensation.

incorporate the landowner's optimistic individual plans.⁹⁹ In contrast, an analysis based on appraisals of market value is substantially more objective.¹⁰⁰ Accordingly, because TDRs restore ascertainable lost value to regulated landowners, they deserve a place in the constitutionality balance.

As to Justice Scalia's narrowly acknowledged exception—allowing TDRs to weigh in the constitutional balance only when the regulated landowners themselves could “use” them themselves on *their own adjacent lands*—a number of courts have expressly rejected that view and instead incorporated *Penn Central*'s formulation that TDRs are a mitigating factor when TDR transfers are to third parties.¹⁰¹ In *Good v. United States*, the Federal Claims Court upheld the U.S. Army Corps of Engineers' denial of a permit to drain and fill protected wetlands against a takings challenge by considering the value of \$110,000 worth of TDR credits to the plaintiff.¹⁰² The *Good* court expressly rejected Justice Scalia's *Suitum* argument:

While the concurring Justices in *Suitum* clearly indicate opposition to this proposition [that TDRs are relevant to determining takings liability], their opinion underscores the Court's reaffirmance of the *Penn Central* holding that the value of TDRs is to be considered to answer the threshold question of whether a taking has occurred.¹⁰³

99. See Brian Crossman, *The Use-Value Distinction in Regulatory Takings Law: Which Property Interest is Protected by the Constitution*, in ENVIRONMENTAL LAW & POLICY, NATURE, LAW AND SOCIETY 96, 100 (Supp. 2004-2005), available at http://www.aspenlawschool.com/books/plater_environmentallaw/updates/21_Crossman_Takings_Use_Value_Article.pdf. For example, in *Palazzolo* the plaintiff's diminution arguments used Mr. Palazzolo's hopes to build seventy-four single-family homes in an eighteen-acre marsh as the basis of their loss of use calculation. *Palazzolo*, 533 U.S. at 616.

100. Crossman, *supra* note 99, at 103.

101. Some jurisdictions do not allow TDRs to serve as any form of compensation because state constitutions require payment for takings to be in cash. For example, the Arizona appeals court found a zoning ordinance unconstitutional but refused to consider TDRs as part of the landowner's compensation package because the “state constitution requires compensation for a taking to be made by payment of money in an amount that has been judicially determined.” *Corrigan v. City of Scottsdale*, 720 P.2d 528, 540 (Ct. App. 1985) *aff'd in part, vacated in part*, 720 P.2d 513 (Ariz. 1986). Because TDRs represent a fungible market asset rather than straight cash, TDRs could never constitute adequate compensation under state constitutions. Consequently, whatever small utility TDRs retain under Scalia's personal use exception would disappear at the state level.

102. 39 Fed. Cl. 81, 84, 107, 114 (Fed. Cl. 1997) *aff'd*, 189 F.3d 1355 (Fed. Cir. 1999).

103. *Id.* at 108.

Although Scalia attempts to evade *Penn Central* with his personal use exception, the *Good* court reveals the contradiction. The *Penn Central* Court's calculation that TDRs are part of the constitutionality inquiry applies to all TDR programs, not simply credits transferred between the same landowner.

IV. INCLUDING TDRS IN THE TAKINGS CONSTITUTIONAL BALANCE

If courts followed Justice Scalia's lead in truncating the nature and role of TDRs in takings balances, the functionality of economically viable TDR programs would be severely undercut. With TDRs stripped of their practicality, local governments would have little incentive to use TDR programs and would be further discouraged from enacting regulations that might be vulnerable without them. In the event that TDRs are relegated to government coupons, bereft of regulatory force, local governments would not implement them and property owners would not buy them.

Therefore, to maintain TDRs' continuing viability, courts should consider TDRs as a mitigating property right both in the takings analysis itself and for potential post-verdict compensation. By including TDRs in both analyses, courts can preserve TDRs' status as essential property rights and market assets, and ensure that diminished value is the proper measure of the takings analysis.

Accordingly, to accomplish these functions transparently, courts appropriately proceed with a three-step approach.¹⁰⁴ First, a court considers the economic effect of the regulation on the property value in order to establish the degree to which the challenged regulation has depleted the market value of the regulated property.¹⁰⁵ Using accepted courtroom appraisal methods, financial impact is determined objectively by comparing the property's economic value before and after the regulation.¹⁰⁶ The constitutional balancing test effectively determines how much the regulation has diminished the property's economic value and the extent to which TDRs allow landowners to recapture some of that lost value.¹⁰⁷

104. See, e.g., *Gardner*, 593 A.2d at 261; *Glisson v. Alachua County*, 558 So.2d 1030, 1036 (Fla. 1st. Dist. Ct. App. 1990); *Deltona Corp. v. United States*, 657 F.2d 1184, 1192 n.14 (Ct. Cl. 1981); RATHKOPF, *supra* note 5 (collecting cases).

105. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

106. *Gardner*, 593 A.2d at 205.

107. *Id.*

Second, a court weighs the value of such TDR credits.¹⁰⁸ If the TDR credits are valuable, then the constitutional balance will tip in favor of regulatory validity because the credits will reduce the economic diminution caused by the regulation. In contrast, if the TDR credits have only slight value, then the constitutional balance will remain unchanged. Moreover, Justice Scalia's fear that TDRs will circumvent takings liability is unfounded because if a TDR program produces credits of inadequate value, then the program will have little to no impact on mitigating government liability in takings. Finally, if a court finds an unconstitutional taking—the regulation is unconstitutionally excessive, notwithstanding the TDRs' value—then TDRs will also appropriately be considered in determining compensation.¹⁰⁹

Justice Brennan in his majority decision in the classic *Penn Central* case and Justice Scalia in his separate *Suitum* opinion set out starkly conflicting notions of TDRs' role in regulatory takings. Justice Brennan asserted that TDRs are a significant factor to be weighed in the constitutionality balance, in determining whether a regulation has *gone too far* in imposing economic burdens on regulated landowners. Justice Scalia instead argued that TDRs must be excluded from the takings balance and only considered as partial compensation when regulations are struck down, as many would be, if balanced without TDRs. Justice Scalia attempts to focus the takings analysis on loss of actual physical *use* of land, rather than the more normal focus on the extent of a property owner's diminished *value*. Viewed in context, Justice Scalia's semantic formulations fundamentally multiply a regulation's negative effect on a regulated landowner, excluding the very real retained private values attributable to transferable credits in well-designed TDR programs. Instead, to support TDRs' continuing utility, courts rightfully consider TDRs based on their actual ascertained market value in navigating the complex mazes presented by constitutional takings cases.

108. *See id.* at 124-28.

109. *Id.* at 130. Although TDRs alone might not fully constitute "just" compensation, they should still be included in the final compensation package. For example, if "just compensation" is \$100,000 and a regulated landowner has \$30,000 in TDR credits, then the TDRs should be included as compensation to force the government to pay the difference—\$70,000. The amount that TDRs contribute toward the regulated landowner's compensation, like the constitutionality balance, will depend on their value.