Public Takings of Private Contracts

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This Article, part of a larger project analyzing how far public and private contracting arrangements should go in constraining democratic decision-making, examines whether the United States should be liable under the Takings Clause of the Fifth Amendment when its actions have the effect of destroying or impairing private contract rights. In the Omnia Commercial case, decided ninety years ago, the Supreme Court ruled that private contract rights represent "property" within the meaning of the Takings Clause, and that the courts should resolve the issue of whether such property has been "taken" by assessing whether the government has "appropriated" the contract interest (resulting in a taking), or merely "frustrated" it (not resulting in a taking). While Omnia Commercial reflects a sound intuition that private contract rights deserve special treatment under the Takings Clause, the appropriation versus frustration standard has no principled foundation and is irreconcilable with modern takings standards. In place of the Omnia Commercial standard, this Article suggests that the Supreme Court should adopt a two-part analysis. First, rather than treat all private contract rights as a form of "property," the Court should only treat the direct contractual commitments between the parties as property. Accordingly, only when the government has inserted itself into the parties' contractual relations, by taking over the contract benefits of one of the parties, or by transferring the benefits to some new party, should the government be regarded as having impinged on "property" in a fashion that could potentially support a taking claim. Second, the Court should conclude that a government action impinging on contract-based property generally results in a taking only when the action imposes a net economic burden on the contracting parties, considered together as a single unit. On the other hand, a taking claim should fail if the government action does not impose a net economic burden on the parties. This standard will avoid conferring a taxpayer-financed windfall on private contracting parties and preserve democratic prerogatives, while placing on the parties the responsibility to negotiate ex ante over how to allocate between themselves the risk of an

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unanticipated government action adversely affecting one party to the contract or the other.

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INTRODUCTION

Does the government take private property within the meaning of the Takings Clause when it destroys or otherwise impairs the value of a private contract right? To cite a few cases illustrating the diverse contexts in which this question can arise: Is the government liable for a taking if enforcement of the Endangered Species Act reduces the amount of water available to a water district under a water supply contract,1 or if a government agency assumes exclusive responsibility for conducting passenger screening at the nation’s airports and prevents a company from implementing its contract with the airlines to provide this service,2 or if the government establishes a National Wildlife Refuge around a remote island in the Pacific Ocean and blocks a fishing company from using it as a base of operations under a contract with the island’s owner?3 Despite a long and steady stream of cases involving this type of claim, the Supreme Court has failed to develop a coherent theory for addressing whether and/or how the Takings Clause should apply to alleged public takings of private contracts. Furthermore, while other scholars have

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2. See Huntleigh USA Corp. v. United States, 525 F.3d 1370, 1373 (Fed. Cir. 2008).
previously discussed this question, there has been no extended examination of the issue. Thus, claims of public takings of private contracts are ripe for an in-depth look.

Almost ninety years ago, in Omnia Commercial Co. v. United States, the Supreme Court set forth the standard ostensibly governing claims of alleged takings of private contract rights. The Omnia Commercial Company contracted with Allegheny Steel Company to purchase steel at a favorable price. Following the United States’ entry into World War I, the government requisitioned Allegheny’s production of steel for a period of one year, preventing Allegheny from fulfilling its contract with Omnia. Omnia brought suit against the United States, claiming a taking of its asserted property right to receive the steel it expected under the contract. The Supreme Court ruled that Omnia’s contract interest represented “property” within the meaning of the Takings Clause. But it concluded that Omnia had not suffered a “taking” of its property because the requisition order had not, in the Court’s words, “appropriated” Omnia’s contract expectancy, but merely “frustrated” it. The Supreme Court has never revisited this decision and the Omnia test continues, at least in theory, to govern claims of public takings of private contracts.

The Omnia takings test is badly flawed. To appreciate why, it is helpful to understand that the decision is a historical oddity. The Court decided Omnia only a few months after it handed down its far more famous decision in Pennsylvania Coal Co. v. Mahon.Mahon, of course, ultimately became the foundation for the Court’s modern regulatory takings jurisprudence. While takings ordinarily involve a direct appropriation or physical occupation of private property, the Mahon Court established that regulations and other government actions limiting the use of property may be so burdensome, or go “too far” in terms of economic impact, that they also can effect takings. The Mahon “too far” test sums up modern regulatory takings doctrine’s primary (though not necessarily exclusive) focus on the economic fairness of

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6. Id. at 507.
7. Id.
8. Id. at 507-08.
9. Id. at 508.
10. Id. at 511-12.
11. In particular, the U.S. Court of Appeals for the Federal Circuit, which has essentially exclusive jurisdiction over takings claims against the United States, routinely cites Omnia as the governing precedent for resolving claims of public takings of private contract. See, e.g., Palmyra Pac. Seafoods, LLC v. United States, 561 F.3d 1361, 1365 (Fed. Cir. 2009); Huntleigh USA Corp. v. United States, 525 F.3d 1370, 1376 (Fed. Cir. 2008).
government-mandated redistributions. A few months later, in the *Omnia* case, the Court cited the *Mahon* decision only in passing and ignored the newly formulated “too far” test. Instead, the Court resolved the alleged public taking of a private contract interest by announcing and applying the appropriation versus frustration test. Under this alternative test, the relative economic impact of the government action—the touchstone of the *Mahon* test—has little if any importance.

The *Omnia* decision reflects the appealing intuition that takings claims arising from government actions affecting private contract interests present different issues than other types of takings claims. But there is no obvious justification in the seminal *Mahon* decision—or in either the text or history of the Takings Clause or modern takings jurisprudence as a whole—for an entirely separate test for this particular type of taking claim. Moreover, the existence of a special takings test for alleged public takings of private contracts seems to undermine the overall normative coherence and doctrinal consistency of takings law. If the Court can adopt a special test for alleged takings of private contract interests, why not for property interests in water, or intellectual property, and so on? Because it represents an inexplicable outlier within takings doctrine as a whole, *Omnia*’s appropriation versus frustration test has been criticized by commentators and questioned by some courts. But it has not been overturned.

Application of the Takings Clause to alleged public takings of private contracts would stand on more solid footing if the Court acknowledged that such a claim is different, not because it should trigger a special takings analysis, but because it involves a distinctive type of property. An asserted property interest arising from a private contract is special in two senses that are relevant in takings cases. First, legal rights based on contract have an in personam character in that, as a general matter, they are binding on the parties to the contract, but not on others. This contrasts with legal rights based on ownership of land and other, more traditional property interests, which have an in rem character such that, as the saying goes, they are good against the world. Second, interests based on contract involve a bilateral relationship. When the

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13. The Supreme Court’s major decisions implementing the *Mahon* per se takings standard include *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1015 (1992) (holding that a regulation that makes private property valueless constitutes a per se taking), and *Penn Central Transportation Co. v. City of New York*, 438 U.S. 104, 124 (1978) (establishing a three-factor default test for regulatory takings claims, focusing on the economic impact of the government action, the degree of interference with investment-backed expectations, and the character of the government action).
15. See Kevin R. Garden, *Fifth Amendment Takings of Rights Arising from Agreements with the Federal Government*, 29 PUB. CONT. L.J. 187, 207 (2000) (“The difference between a frustration of rights and an appropriation or taking of rights may be nothing more than a matter of semantics.”); Goldberg et al., supra note 4, at 1136–37 (criticizing the reasoning in *Omnia*).
government impairs performance of an executory contract, it affects parties on both sides of the contract, one party expecting performance and the other expecting to perform. By contrast, when the government impairs an interest in real property, for example, only the single property owner typically feels the effect of the impairment. These two distinctive features of asserted property interests grounded in contract (assuming contract interests represent "property" at all, a topic addressed below) suggest that judicial analysis of alleged public takings of private contracts should produce distinct results.

First, the in personam nature of contract rights provides a basis for distinguishing, in the course of deciding a takings case, between government actions that affect the economic value or practical utility of a private contract right, and government actions that involve a taking over of the role of one of the parties to the contract. Because a contract basically establishes only in personam rights, a government action affecting the value or utility of a contract interest, like virtually any action by a stranger to a contract, does not intrude upon a legal interest protected by the contract. Therefore, such a governmental action should not be viewed as potentially giving rise to a takings claim. On the other hand, when the government inserts itself into the parties' contractual relationship, by taking over the contract benefits of one of the parties, or by transferring the contract benefits to some third party, the government does intrude upon a legal interest protected by the contract. In that circumstance, the government action should be viewed as potentially giving rise to a valid takings claim.

The bilateral nature of executory contracts points to another limitation on how the Takings Clause should apply to alleged takings of private contract interests. In some cases, government action affecting a contract right results in no net economic loss to the contracting parties when considered as a single unit. If the government prevents performance, one party might stand to gain (for example, because she can sell the goods that are the subject of the contract to a third party at a higher price) and the other party might stand to lose (because she is forced to buy replacement goods at a higher price). But the parties, considered together, suffer no net loss. In this circumstance, the parties could negotiate terms at the time of contract formation to ensure that, in the event of some government interference with their contract, neither party would suffer a loss. In this circumstance, the Takings Clause's traditional concern about "fairness and justice" does not support payment of compensation by the public to either of the parties, and the courts should reject any claim under the Takings Clause. On the other hand, when the government interference does produce a net loss to the contracting parties considered as a unit, which the parties could not have contracted around, concerns about fairness and justice generally will support payment of just compensation.

Focusing on the nature of the underlying property interest leads to results that sometimes mirror the outcomes achieved by courts applying Omnia's frustration versus appropriation distinction. However, this new approach
provides a more satisfactory doctrinal foundation for the resolution of claims of alleged takings of private contract interests. The in personam and bilateral aspects of contract rights provide a logical explanation for how property rights based on contracts are different from other types of property, and therefore why private contract takings claims should be treated differently than other takings claims. Moreover, this approach, unlike the traditional Omnia test, eliminates the need for an ad hoc redefinition of what constitutes a "taking" to address this particular category of takings cases. At the same time, it must be acknowledged, this approach calls for a relatively unique definition of the relevant "parcel" to accommodate the bilateral nature of executory contracts, as explained below.

This Article proceeds as follows: Part I describes the universe of alleged public takings of private contracts, highlighting the occasional difficulty of locating the boundary between contract interests and more traditional property interests. Part II critiques three alternative approaches to analyzing alleged takings of private contract interests: (1) the longstanding Omnia appropriation versus frustration standard; (2) treating private contract interests as not constituting property within the meaning of the Takings Clause, precluding claims of public takings of private contracts; and (3) treating contract interests as indistinguishable from any other type of property interest, meaning that alleged public takings of private contracts should be analyzed in the same fashion as any other taking claim. Part II concludes that none of these alternatives is satisfactory in terms of providing a logical theory to govern alleged public takings of private contracts, or in terms of contributing to a coherent doctrine of takings law generally. Part III lays out a new theory of public takings of private contracts based on the distinctive character of property interests based on contacts. Under this theory, a relatively narrow doctrine of public takings of private contracts emerges, not because some special, narrow takings test applies (quite the contrary, in fact), but because of the special character of the property at stake. A brief conclusion offers some additional speculations based on the analysis presented in this Article.

I. TAKINGS CLAIMS BASED ON GOVERNMENT INTERFERENCE WITH PRIVATE CONTRACT RIGHTS

This Part defines a claim of a public taking of a private contract right and describes the characteristics of this species of taking claim. This discussion is designed to define the scope of the inquiry in this Article and to clear away potentially distracting analytic clutter. It provides the foundation for the critical analysis of the Omnia standard and other potential approaches to this type of taking claim.
A. Defining Private Contract Takings Claims

As a first approximation, an alleged taking of a private contract interest might be thought to encompass any government action that destroys or otherwise impairs the value or utility of a private contract interest, by making contract performance difficult or impossible, by making performance less valuable, or by transferring the expected benefit of the contract to some third party. Such a claim could logically arise from interference with a private contract by any department or level of government, including Congress or some federal agency, a State, or a unit of local government. While most of the case law examples in this Article involve alleged federal government interferences with contract rights, claims of this sort can be, and in practice are, asserted against state entities and units of local government.17

The term "private contract" as used in this Article encompasses not only contracts between private individuals and firms but also contracts between private parties and governments, or even potentially between two units of government. While this use of the term "private contract" may be slightly confusing, it appears to be justified conceptually. The linchpin of the definition is that it includes claims arising from all manner of contractual relations, including those involving government entities, but excludes takings claims against a government that itself is a party to the contract that created the rights assertedly taken. Thus, for example, a claim that the Bureau of Reclamation took some action that prevented it from carrying out its obligation to deliver water to one of its contractors does not involve a public taking of a private contract for present purposes. By contrast, the case of Tulare Lake Basin Water Storage District v. United States, which involved an alleged taking by the United States of a water district's right to receive water under a contract with the California Department of Water Resources,18 did involve, under the definition used here, an alleged public taking of a private contract. So long as the alleged government taker is not itself a party the contract, nothing in the analysis of the claim appears to depend on whether one or both of the parties to the affected contract is a public entity. Thus, the "private contract" label appropriately covers a large variety of contractual relations that might, in other contexts, be distinguishable from each other.

Cases in which the government allegedly interfered with a contract to which it is itself a party present different and relatively more complex questions. A claim in this type of case can be viewed as involving either a breach of contract by the government or a government taking of private property. Relevant decisions suggest, but do not definitively resolve, that when a claim can be framed as either a breach of contract by the government or as a

public taking of a public contract right by the government, the claimant is required to pursue his or her contract remedy rather than the parallel takings remedy. A claim of breach of contract against the government implicates the so-called sovereign acts defense, which protects the government from liability if performance of the contract has been made impossible as a result of some "public and general" government act; when the government has entered into a contract in its proprietary capacity, it cannot subsequently be held liable as contractor for sovereign acts that upend the contract. The theory underlying this defense is that the government should have the same rights as a private contractor in like circumstances; because a sovereign action is generally understood to create a condition of impossibility excusing a private party from performance, the government as contractor should be entitled to assert the same defense. The key point for present purposes, however, is that the complex questions surrounding alleged public takings of "public contracts" can be set aside for the purpose of this Article.

Finally, it is noteworthy that if a party sues a unit of state or local government for an alleged public taking of a private contract, the claim might potentially be framed in the alternative as a violation of the Contracts Clause, which provides, "No State shall . . . pass any . . . Law impairing the Obligation of Contracts." In the case of a suit against the United States, by contrast, a claim under the Contracts Clause is not an available alternative; the longstanding rule is that the Contracts Clause applies exclusively to state and local governments. While the potential alternative claim under the Contracts Clause is not the focus of this Article, the existence of the Contracts Clause logically informs the question of how the Takings Clause should be applied to private contracts, whether the government defendant is the federal government or a state or local government. In particular, as discussed in greater detail below, the explicit protection for contract interests in the Contracts Clause, coupled with the fact that the Contracts Clause does not apply at all to the federal government, suggests that it is problematic to assume that the term "property" in the Takings Clause can be read to implicitly encompass any and all contract interests.

19. See Hughes Commc'n Galaxy, Inc. v. United States, 271 F.3d 1060, 1070 (Fed Cir. 2001) ("[T]he concept of a taking as a compensable claim theory has limited application to the relative rights of party litigants when those rights have been voluntarily created by contract. In such instances, interference with such contractual rights generally gives rise to a breach claim not a taking claim." (quoting Sun Oil Co. v. United States, 572 F.2d 786, 818 (Ct. Cl. 1978))). But see Stockton E. Water Dist. v. United States, 583 F.3d 1344, 1368 (Fed. Cir. 2009) (arguing that Federal Circuit precedents merely establish a preference for resolving a claim on non-constitutional contracts claims rather than under the Takings Clause, but that a contract claim does not preclude a parallel takings claim).
B. The Bilateral Character of Executory Private Contracts

Another critical feature of alleged public takings of private contracts is that the government actions giving rise to the claims affect parties to a bilateral relationship rather than a single owner or set of owners. The ownership of the property interest at stake in a takings case is often the result of some prior, perhaps remote, contractual sales arrangement. But, for the purpose of analyzing a taking claim arising from government action affecting the property, the seller is long gone and has become legally irrelevant. In this sense, the current property owner stands alone with his claim against the government.\footnote{The seller of property is involved in a taking case only in the sense that a claimant’s investment-backed expectations, which are often shaped in part by the timing and nature of the contractual arrangement that led to the claimant’s ownership of the property, can be a critical factor in determining whether the claimant is entitled to recovery under the Takings Clause. See generally Palazzolo v. Rhode Island, 533 U.S. 606 (2001).}

By contrast, a government action impairing an executory contract affects two sides of a relationship, barring the obligor from performing and precluding the obligee from receiving the benefit of her bargain. A government action interfering with a private executory contract can, and often does, result in claims by either one party or the other against the government, and/or claims by one party against the other.

The bilateral nature of executory contracts has two important implications for the following analysis. First, the parties have the opportunity, in the course of their negotiations, to consider the risk of future government actions that might interfere with performance or impair the value of the contract, and to allocate the risk of such an event occurring between themselves. Thus, one party could obtain a contractual commitment protecting itself from the effects of some supervening government action while the other party could agree to bear the risk of the adverse effect of such an action. In the course of their negotiations, the parties might seek to identify which party could adapt to a governmental impairment of the contract most easily and at the lowest cost. With such information in hand, the parties could lower their mutual costs by assigning the responsibility for accommodating government action to the party who could do so at the lowest cost. Of course, a requirement to explicitly negotiate over such issues may impose at least marginally greater transaction costs on both parties.

Second, the bilateral nature of the contract relationship, and the capacity of the parties to allocate the risk of a potential government impairment between themselves, suggests that the relevant unit for the purpose of analyzing the burden imposed by a government action should be the two contracting parties considered together as a unit, rather than either one party or the other. The *Omnia* case illustrates the point. From Omnia’s perspective, its contract to purchase the steel at a pre-war price was undoubtedly a valuable corporate asset. On the other hand, with the outbreak of World War I, Allegheny
presumably felt that it was saddled with an unfortunate commitment to sell steel at a, by then, below-market price. Thus, the government requisition imposed a burden on Omnia because it lost the benefit of its low-priced contract and presumably could not locate substitute steel at the lower price during wartime. But the requisition order apparently conferred a corresponding windfall on Allegheny because Allegheny received the higher wartime price for goods it originally expected to sell at a lower price. At the same time, the government’s interference presumably provided Allegheny a solid impossibility defense against any suit Omnia might bring against it for breach of contract, thereby shielding Allegheny from liability. Considering the effect of the requisition order on both parties as of the date of the impairment, the net effect was neutral when considering the parties as a unit. Since the parties could have negotiated ex ante over how to assign the risk of government intervention, the fact that the burden fell on Omnia was serendipitous.24 In the ensuing litigation, there was no good reason to impose an obligation on the public to indemnify Omnia for its loss, given that the government action that caused the loss simultaneously conferred a windfall on Allegheny, which at the time of contracting was within the control of the parties to avoid. In other words, awarding compensation in this case would have contradicted the so-called Armstrong principle animating the Takings Clause: government may not “forc[e] some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.”25

In other cases, however, the government interference might well have a net negative effect on the contracting parties considered together. The critical feature of the Omnia case is that the government interference was in the form of a requisition order accompanied by payment of the current market price for the steel—effectively an exercise of eminent domain supported by just compensation. But in other cases the government will not be offering payment that can serve to make the parties whole. Sometimes the government simply declares that continuation of a private contract arrangement is contrary to public policy, as when Congress determined post-9/11 that airport passenger screeners at the nation’s airports should be employed by a federal security agency rather than a private firm.26 In other instances, destruction of a private contract is the indirect consequence of some public initiative, as when the government’s efforts to protect Palmyra Island in the Pacific Ocean effectively destroyed the value of a company’s contract to use the island as the base for its fishing operation.27 Assuming a government action affecting a contract would

otherwise support a finding of a taking, an action that produces a net loss for the contracting parties arguably deserves different treatment than an action that has a neutral effect on the two parties when considered together.

C. The Frequent Obscurity of the Contract/Property Distinction

Finally, it is worth observing that it is sometimes difficult to discern whether a takings claim involves an asserted property interest based on a contract or a more traditional property interest, such as an interest in real property. The subtleness of this distinction (and the frequency with which courts obscure it) has added to the confusion surrounding alleged public takings of private contracts. Take the case of a lease. As all first-year law students learn, a lease can be characterized as either a contract or as an interest in real property.\(^{28}\) As a result, a leaseholder who can no longer enjoy her lease due to some intervening government action might conceivably claim either a taking of her property right in her contract, triggering analysis under *Omnia,* or a taking of her real property lease interest, triggering review under a traditional takings test. In an orderly legal universe, one might suppose it would be one or the other and not both. The same ambiguity implicitly infects the seminal *Mahon* case, which the Supreme Court described as arising from enforcement of a "statute [that] is admitted to destroy previously existing rights of property and contract."\(^{29}\) The Court's analysis essentially ignored the contractual basis of the plaintiff's interest in the coal, treating the case as involving a straightforward government interference with a traditional property interest.\(^{30}\) It is ironic that, when, a few months later, the Court actually confronted in *Omnia* an alleged taking of a contract interest, the Court applied an entirely new and different takings test.\(^{31}\)

In addition, contractual interests can mature over time into traditional property interests, and it may be difficult to know when the contract interest turns into a traditional property interest. In *Omnia,* for example, the steel would have unambiguously become the property of Omnia at some point in Allegheny's production and delivery process. Then, a requisition order affecting the steel owned by Omnia would have involved a taking of Omnia's property interest in the steel—not Allegheny's. Line-drawing problems of this type undoubtedly arise frequently.

Courts sometimes make outcome-determinative choices in describing the property at stake in a taking case as either a contract interest or as a more traditional property interest, without clearly explaining the choice. For example, in *Tulare Lake,* the U.S. Court of Federal Claims rejected the *Omnia* defense to the claim that the United States took the water district's alleged

\(^{28}\) Jesse Dukeminier et al., *Property* 374 (6th ed. 2006).

\(^{29}\) Pa. Coal Co. v. Mahon, 260 U.S. 393, 413 (1922) (emphasis added).

\(^{30}\) Id. at 413–16.

entitlement to water because the claim involved a taking of a right to the water itself rather than a mere contract right to the water.\textsuperscript{32} The Court reasoned that "\textit{Omnia}'s distinction between a contract that has been appropriated and one that has merely been frustrated is relevant only where the contract right that is claimed remains separate and distinct from the property that is the subject of the contract."\textsuperscript{33} In other words, \textit{Omnia} applies, the court said, when the plaintiff has only a bare contract right and "title to the property has not yet passed to the party seeking compensation."\textsuperscript{34} \textit{Omnia} did not control in \textit{Tulare Lake}, the court continued, because the water district did not merely have "a contract expectancy," but had "an identifiable interest in a stipulated volume of water."\textsuperscript{35} It is debatable whether the facts of the \textit{Tulare} case fairly supported the court's conclusion that the case involved a traditional property interest and not merely a contract expectancy. More specifically, it is difficult to see how the water district's expectation to receive a certain volume of water flowing down a canal was any more "identifiable" than \textit{Omnia}'s expectation to receive a certain volume of steel flowing out of the Allegheny steel plant. But the larger point illustrated by \textit{Tulare Lake} is that the Supreme Court's adoption of a special test for alleged takings of contract interests will require courts to determine, at least implicitly, whether a case involves an alleged taking of a contract right to the delivery of something or a taking of the thing itself.

The U.S. Court of Appeals for the Federal Circuit followed a similarly obscure approach in \textit{Cienega Gardens v. United States}, a case in which the court issued two notably different opinions at different stages of the litigation involving different sets of claimants. In the first opinion, the court characterized the takings claims brought by a set of developers of low-income housing as involving an alleged taking of contract interests,\textsuperscript{36} but in the subsequent opinion characterized similar claims by another set of developers as involving an alleged taking of real property interests.\textsuperscript{37} The federal legislation at issue in the case barred the plaintiffs from prepaying their mortgages in accordance with their mortgage agreements, forcing them to continue to rent units at below-market rates.\textsuperscript{38} In the first opinion, the panel focused on one set of plaintiffs' asserted property interests in their contractual right to prepay, and said a per se takings test applied.\textsuperscript{39} However, a subsequent panel, addressing the claims of a different group of developers, essentially ignored plaintiffs'
contract interests, focused instead on their interests in the buildings subject to the mortgages, and said a Penn Central analysis applied.40

With this review of the threshold issues in hand, it is appropriate to turn to a detailed analysis of the Omnia standard and alternative approaches for addressing alleged public takings of private contracts.

II. THREE ALTERNATIVE APPROACHES TO PRIVATE CONTRACT TAKINGS CLAIMS

This Part examines three different approaches to takings claims based on government actions affecting private contract interests. The first is the Omnia standard adopted by the Supreme Court almost ninety years ago and still widely followed today. The other two, which are based on academic commentary as well as judicial opinions, are potential alternatives to Omnia. The first is that contract interests should not be regarded as property within the meaning of Takings Clause at all, a position that precludes any claim of a public taking of a private contract. The second alternative goes in the opposite direction by jettisoning the limitations of the Omnia test and applying a standard takings analysis to alleged takings of contract interests.

This Part analyzes each of these approaches: starting with the first alternative to Omnia, which provides the least protection against government interference with contract interests; proceeding to the intermediate Omnia standard; and ending with the second alternative to Omnia, which provides the greatest protection to contract interests. No approach survives careful scrutiny.41

A. Does the Takings Clause Apply to Private Contracts at All?

The most radical, but surprisingly plausible, alternative is that the Takings Clause should not be read to protect contract interests at all. As discussed, the Omnia Court did not hesitate to characterize the contract interest in that case as

40. Cienega II, 503 F.3d at 1282.

41. In light of the doctrinal confusion surrounding private contract takings claims, it is hardly surprising that courts work hard to find alternative grounds for resolving these claims and strive to avoid applying Omnia. See, e.g., Acceptance Ins. Cos. v. United States, 583 F.3d 849, 855 n.4, 857 (Fed. Cir. 2009) (rejecting a taking claim based on the U.S. Department of Agriculture’s veto of the claimant’s planned sale of a portfolio of crop insurance policies, reasoning that the claimant relinquished its right to sell the policies free of government supervision when it entered into the heavily regulated and subsidized crop insurance business, thereby obviating the need to address the parties’ “arguments about whether the Court of Federal Claims correctly dismissed . . . [the claim] based on the Omnia Commercial line of cases”); Air Pegasus of D.C., Inc. v. United States, 424 F.3d 1206, 1219–20 (Fed. Cir. 2005) (rejecting a taking claim based on a government shut-down of a private helicopter operation in Washington D.C. following 9/11, concluding that the claimant could not assert a taking of its lease for the site of its helicopter operations because it lacked a protected property interest in using the navigable air space, again avoiding application of Omnia). These types of evasive maneuvers would become less attractive to the courts if there were a better theory governing alleged public takings or private contracts.
“property” for takings purposes, and subsequent Supreme Court decisions have embraced this premise. That contract rights are property rights is also an article of faith in the U.S. Court of Appeals for the Federal Circuit, which addresses many claims of public takings of private contracts. On the other hand, the contrary view is supported by no less a luminary than Professor Thomas Merrill, who, while acknowledging that contract interests should be regarded as “property” for the purpose of the Due Process Clause, argues that they should not be regarded as “property” for the purpose of the Takings Clause. As discussed below, the language and structure of the Constitution provide support for this dissenting view, while the long line of precedent ostensibly supporting the traditional view, upon examination, turns out to be rather thin.

Starting with the language of the Takings Clause, there are grounds for believing that “private property” does not encompass contract interests. At the most elementary level, there has been a longstanding understanding among legal practitioners and scholars, reflected in most U.S. law school curricula, that contracts and property represent distinct legal subjects. This pedagogical divide is obviously in tension with the idea that the term “property” can easily encompass contracts. More substantively, the presence of the Contracts Clause in the Constitution appears to support a reading of the Takings Clause that excludes contract interests. The drafters of the Bill of Rights (adopted in 1791) were undoubtedly well aware of the Contracts Clause in Article I of the Constitution (adopted in 1787). The use of the term “property” in the Takings Clause, rather than the term “contract,” initially suggests that the drafters intended the Takings Clause to apply to a different universe of interests than the Contracts Clause. In response, it could be argued the later-adopted Takings Clause was intended to refer to a more all-encompassing set of interests that includes contract interests as well as other interests that qualify as property, rather than refer to interests that are distinct from contracts. But this reading is problematic in light of the fact that the Contracts Clause, by its terms and according to longstanding precedent, applies only to the states.

44. See, e.g., Palmyra Pac. Seafoods, LLC v. United States, 561 F.3d 1361, 1365 (Fed. Cir. 2009) ("C)ontract rights can be the subject of a takings action."); Adams v. United States, 391 F.3d 1212, 1221 (Fed. Cir. 2004) ("When the Government and private parties contract, as in Lynch, the private party usually acquires an intangible property interest within the meaning of the Takings Clause in the contract."); Cienega I, 331 F.3d 1319, 1329 (Fed. Cir. 2003) ("[T]here is also ample precedent for acknowledging a property interest in contract rights under the Fifth Amendment.").
46. See U.S. CONST. art. I, § 10 ("No State shall ... pass any ... Law impairing the Obligations of Contracts ... ").
history, was understood to apply *exclusively* to the federal government.\textsuperscript{48} The Takings Clause and the Contracts Clause are not necessarily designed to constrain government action in exactly the same fashion.\textsuperscript{49} Nonetheless, it is implausible to suppose, following adoption of the Contracts Clause, which explicitly addressed contracts and was limited to the states, that the authors of the Bill of Rights suddenly reversed course in drafting the Takings Clause and—without explicitly saying so—established a broad restraint on federal government action affecting contract interests. Instead, it is more plausible to believe that the drafters, secure in the knowledge that the Contracts Clause barred state—and only state—impairments of contract rights, drafted a Takings Clause applicable to the federal government that addressed other types of interests, most notably interests in real property.\textsuperscript{50}

In light of the apparent force of this textual/historical argument, the confidence with which the Supreme Court has asserted that private contract interests constitute property for the purpose of the Takings Clause is striking. In *Omnia* the Court stated, without hesitation or qualification, that "[t]he contract in question was property within the meaning of the Fifth Amendment, and if taken for public use the government would be liable."\textsuperscript{51} A few years later, in *Lynch v. United States*,\textsuperscript{52} perhaps the mostly widely cited decision on the subject, the Court stated: "The Fifth Amendment commands that property be not taken without making just compensation. Valid contracts are property, whether the obligor be a private individual, a municipality, a state, or the United States."\textsuperscript{53} Modern decisions of the U.S. Court of Appeals for the Federal Circuit repeatedly cite the statement in *Lynch* quoted above as if it were an undeniable verity.\textsuperscript{54}

However, to support the conclusion that private contracts are "property" within the meaning of the Takings Clause, the *Omnia* Court principally relied upon *Long Island Water-Supply Co. v. Brooklyn*.\textsuperscript{55} The case arose from the City of Brooklyn's condemnation of a private water company's government-issued franchise to supply water to the public in a portion of this future New York City borough.\textsuperscript{56} The plaintiff's primary argument, which the Court

\begin{footnotes}
\item[48.] Chi., Burlington & Quincy R.R. Co. v. Chicago, 166 U.S. 226, 239 (1897) (ruling, for the first time, that the Takings Clause applies to the states via the Fourteenth Amendment).
\item[49.] See discussion, infra notes 64–66.
\item[50.] See William Michael Treanor, *The Original Understanding of the Takings Clause and the Political Process*, 95 COLUM. L. REV. 782, 818–835 (1995) (tracing the historical origins of the Federal Takings Clause to disputes over land, as well as concerns about the security of property rights in slaves).
\item[51.] *Omnia Commercial Co. v. United States*, 261 U.S. 502, 508 (1923) (citations omitted).
\item[52.] *Lynch v. United States*, 292 U.S. 571 (1934).
\item[53.] Id. at 579. *See also* Ruckelshaus v. Monsanto Co., 467 U.S. 986, 1003 (1984) (stating that *Lynch* establishes that valid contracts are property within the meaning of the Takings Clause).
\item[54.] See Palmyra Pac. Seafoods, LLC v. United States, 561 F.3d 1361, 1365 (Fed. Cir. 2009); *Cienega I*, 331 F.3d 1319, 1329–30 (Fed. Cir. 2003).
\item[55.] *Omnia*, 261 U.S. at 508 (citing Long Island Water Supply Co. v. Brooklyn, 166 U.S. 685, 690 (1897)).
\item[56.] *Long Island Water Supply*, 166 U.S. at 688–89.
\end{footnotes}
rejected, was that exercise of the eminent domain power with respect to the franchise violated the Contracts Clause. In the course of resolving that issue, however, the Court affirmed that the franchise was "property" subject to condemnation under the Takings Clause. To support this conclusion, the Court relied on Blackstone's categorization of a royal franchise as a form of property, specifically an "incorporeal hereditament." But it hardly follows from either Blackstone or Long Island Water-Supply Co. that every interest based on contract should be treated as property for the purpose of the Takings Clause. A government-issued franchise to provide utility service can plausibly be described as a type of property. Because it confers permission to engage in a particular activity in a specified geographic area, a utility franchise is closely analogous to a lease or an easement. But it is a considerable stretch from the narrow ruling in Long Island Water Supply Co. to the conclusion that all contract rights, including those based on simple contracts to purchase commercial goods, for example, should constitute property for takings purposes.

Professor Merrill has argued that, in light of the existence of the Contracts Clause, the term "property" in the Takings Clause "should not be construed in such a broad fashion that it automatically includes all contract rights." His reasoning is that the Takings Clause is "almost certainly more protective" than the Contracts Clause; therefore, if the Takings Clause is read as applying to contract interests, the Contracts Clause would become superfluous as a constraint on state and local government actions, and the distinction drawn by the Contracts Clause between federal and state impairments of contracts would be "erased." This analysis is debatable, at least today, in light of developments in takings jurisprudence that have occurred since Professor Merrill published this argument. The premise of his analysis was that a claim for compensation under the Takings Clause involves a relatively intrusive inquiry into whether the challenged government action advances a "substantial" public purpose. Subsequently, in the landmark Lingle case, the Supreme

57. Id. at 689–90.
58. Id. at 690.
59. Id. at 693 ("We are aware of nothing peculiar to a franchise which can class it higher, or render it more sacred, than other property. A franchise is property, and nothing more. It is incorporeal property, and is so defined by Justice Blackstone, when treating, in his second volume (chapter 3, p. 20), of the Rights of Things."). This ruling is consistent with the Court's earlier decision in West River Bridge Co. v. Dix, 47 U.S. 507, 534 (1848), which also relied on Blackstone.
60. Another decision cited by the Omnia Court, Cincinnati v. Louisville & Nashville Railway Co., 223 U.S. 390, 399–400 (1912), repeated the assertion that a contract interest can constitute property within the meaning of the Takings Clause, but the case actually involved a taking of an easement, a classic real property interest.
61. Merrill, supra note 45, at 990.
62. Id. at 990–91.
Court eschewed any Takings Clause inquiry into the legitimacy of government’s goals or the reasonableness of the means selected to achieve its goals, and also specifically repudiated the kind of intrusive judicial review apparently called for by the “substantially advance” test.\textsuperscript{64} Modern takings analysis, the Court explained, \textit{presupposes} the legitimacy of the government action, and focuses instead on the magnitude of the economic impact of the government actions.\textsuperscript{65} In contrast, while the burden of the government action is not entirely irrelevant in Contracts Clause cases, the primary emphasis is on the public significance and legitimacy of the government’s objectives and whether the government action is “appropriate” to achieve the objectives.\textsuperscript{66} In sum, the Takings Clause today is not properly viewed as “more protective” than the Contracts Clause, but rather as just different. As a result, excluding contracts interests from the scope of the term “property” in the Takings Clause cannot be justified as necessary to avoid making the Contracts Clause superfluous. Nonetheless, for the reasons explained above, even though subsequent development in Supreme Court takings jurisprudence has overtaken Professor Merrill’s specific reasoning, there are ample textual and historical reasons to doubt that the term “property” in the Takings Clause should encompass contracts.

Ultimately, the fatal flaw with arguments for reading contracts out of the Takings Clause may be that it is simply too late in the day to embrace these arguments. In view of the very long line of Supreme Court decisions affirming that contract interests \textit{are} property, the principle of stare decisis arguably now precludes the opposite conclusion. At the same time, however pragmatically realistic this conclusion may be, it would be deeply dissatisfying as a matter of principle. Fortunately, it is unnecessary to rest on pragmatic realism alone. As discussed in Part IV, below, there is ample ground based on Supreme Court precedent interpreting the term “property” in the context of the Takings Clause, for concluding that private contracts can and should qualify as property, at least in a narrow and limited fashion and despite the contraindications discussed above.

\textsuperscript{65} Id. at 543.
\textsuperscript{66} See, e.g., U.S. Trust Co. of N.Y. v. New Jersey, 431 U.S. 1, 22 (1977) (“Legislation adjusting the rights and responsibilities of contracting parties must be upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption.”) (citing Home Bldg. & Loan Ass’n v. Blaisdell, 290 U.S. 398, 445–47 (1934)); Ass’n of Surrogates and Supreme Court Reporters Within N.Y. v. New York, 940 F.2d 766, 771 (2nd Cir. 1991) (“Generally, legislation which impairs the obligations of \textit{private} contracts is tested under the contract clause by reference to a rational-basis test; that is, whether the legislation is a ‘reasonable’ means to a ‘legitimate public purpose.’”) (quoting U.S. Trust Co. of N.Y. v. New Jersey, 431 U.S. 1, 22–23 (1977)).
B. The Omnia Test

The *Omnia* standard represents the second alternative approach to alleged public takings of private contracts requiring examination. As discussed, one of the most striking features of the *Omnia* decision is how quickly the Supreme Court brushed past the issue of whether a contract interest qualifies as "property" within the meaning of the Takings Clause. For the reasons already examined, there is substantial reason to doubt the correctness of the Court's premise that "property" was at stake in the case. Because this issue has been addressed above, and will be revisited in Part IV below, the focus in this Part will be on the appropriation versus frustration test announced in *Omnia*.

To explain why the taking claim failed on the assumption that the claimant did possess "property," the Court relied on two related lines of analysis. First, referring to government's broad power to advance the public welfare, the Court said that so long as the government is pursuing "a permitted purpose," the Takings Clause is not implicated even if the action "results in serious depreciation of property values." To support this reasoning the Court invoked the long line of nineteenth-century precedents, of which *Mugler v. Kansas* is the most famous, that barred takings claims arising from legitimate police power regulations. Despite the fact that the decision in *Omnia* followed the Court's decision in *Mahon* by only a few months, the Court offered no acknowledgment that *Mahon* had placed a limit on how far police power authority can go without triggering a duty to compensate under the Takings Clause. Ironically, the *Omnia* Court cited *Mahon* only once, as authority for the proposition that the government can destroy buildings in the path of a fire in order to abate its spread. To the extent *Omnia* suggested, following *Mahon*, that police power regulation can never result in a taking, this suggestion plainly was and is anachronistic.

Second, in the more frequently cited portion of *Omnia*, the Court justified rejection of the taking claim by stating that the government had not "appropriated" the contract—it had not acquired "the obligation or the right to enforce" it—but instead had merely "frustrated" performance of the contract. The Court further said the company's claim that it suffered a taking of its expectation of receiving steel under the contract improperly "confound[ed]" the subject matter of the contract (the steel) with the contract itself, which consisted of "the agreement and obligation to perform."

68. 123 U.S. 623 (1887).
69. See *Omnia*, 261 U.S. at 508 (citing *Mahon*, 260 U.S. 393, in passing).
70. *Id.* (also citing *Bowditch v. Boston*, 101 U.S. 16 (1879)).
73. *Id.*
The Supreme Court subsequently relied on Omnia in several cases, but did little to clarify the meaning of the frustration versus appropriation standard. In Brooks-Scanlon Corp. v. United States, a World War I requisition case involving facts very similar to Omnia, the Court ruled that the government had not merely frustrated a private contract to construct transport ships but actually appropriated the contract. The Court distinguished Omnia and said the government “put itself in the shoes of claimant and took from claimant and appropriated to the use of the United States all the rights and advantages that an assignee of the contract would have had.” Not surprisingly, given that the government appeared to effectively step into the shoes of the Omnia company in the same way that it stepped into the shoes of Brooks-Scanlon, several justices dissented, arguing that the claim should have been dismissed based on Omnia. In International Paper Co. v. United States, another case arising from World War I, the Court upheld a takings claim based on a U.S. government order that the Niagara Falls Power Company cease delivering water power pursuant to a contract with the International Paper Company. Instead, the government instructed the company to direct the power to another company deemed more important to the war effort. The Court concluded that the government “took the property” of International Paper. It purported to distinguish Omnia on the ground that that case involved a government action that made it “practically impossible” for a third party to carry out a “collateral contract,” rather than involving an appropriation. However, using this characterization, International Paper appears to also have involved a government order making it “practically impossible” for a company to carry out a collateral contract. Thus, it is difficult to understand why the Court believed Omnia did not govern resolution of International Paper. In more recent decades, the Supreme Court has cited Omnia only infrequently and in seemingly incidental fashion, raising at least a question about the continuing authority of this precedent.

The fundamental problem with the Omnia appropriation versus frustration standard is that the Supreme Court has never offered a convincing justification for this special test. If, as the Court posited, a contract right is property within the meaning of the Takings Clause, why should private contract takings claims be governed by a test that is different from the “too far” test that applies in other takings cases? Professor Richard Epstein, for example, has criticized the distinction between frustration and appropriation as “irrelevant” for the purpose

75. Id. at 120.
77. Id. at 408.
of takings analysis. In addition, a thoughtful opinion by a judge of the U.S. Court of Federal Claims, citing "certain curious features of the decision," questioned the validity of Omnia's distinction between frustration and appropriation:

If, as the Supreme Court declared in Omnia, contracts are property like any other form of property, it might now be questioned whether indeed the government could, by regulatory action or the exercise of its police power, so extensively "frustrate" the purposes of a contract (or a party's right to perform thereunder) as to go beyond regulation and become a taking.  A more recent decision issued by the U.S. Court of Appeals for the Federal Circuit reprised the same argument, referring to the contention "that the decision[] in Omnia . . . [is] contrary to more recent case authority," in particular Penn Central.

The distinction between appropriation and frustration arguably reflects the Supreme Court's pre-Mahon thinking that direct appropriations and physical invasions of private property can constitute takings whereas regulatory constraints of the use of property cannot. While the appropriation versus frustration test is unique to the contract takings context, these terms are arguably an echo of the more familiar, if outdated, nineteenth-century distinction between appropriation and regulation. Insofar as Mahon rejected the view that regulation (that is, frustration) can never constitute a taking, Omnia seems to contradict the spirit of Mahon in holding that frustration, as opposed to appropriation, can never constitute a taking. Consider the landmark Penn Central case. The city's regulation of development atop the historic Grand Central Terminal plainly could have been described as frustrating, rather than appropriating, the company's interest in developing the airspace above the terminal. But the Court in Penn Central did not suggest that any such distinction could justify rejection of the company's taking claim. So why should it continue to operate in takings cases involving private contract interests? In sum, Omnia's frustration versus appropriation standard appears to be an indefensible artifact of a bygone era in takings law.

Finally, the Omnia standard is subject to the further criticism that it functions as an ad hoc test for a particular situation and detracts from the overall coherence and consistency of takings doctrine. Current takings doctrine already draws a distinction between appropriations and physical occupations of private property, on the one hand, and regulatory restrictions on the use of

private property, on the other. It also draws a distinction between regulatory restrictions on property use that deny the owner all economically viable use and restrictions that merely reduce the value of the property. Do we really need or want one more test for resolving alleged public takings of private contract interests?

C. Applying Standard Takings Analysis

The third alternative, which naturally follows from the foregoing criticisms of *Omnia*, is to analyze a private contract takings claim in the same fashion that any other taking claim is analyzed. Under this approach, the appropriate takings analysis would be drawn from the array of takings tests already established by the Supreme Court. While the Court has articulated several different takings tests, the dominant framework of the *Penn Central* decision focuses on the economic impact of the government action, the degree of interference with investment-backed expectations, and the character of the government action. The analysis of this alternative proceeds, again, on the premise that a private contract interest represents property that is indistinguishable from any other property in a takings case.

The Supreme Court has arguably suggested that the *Penn Central* framework can properly apply to private contract takings claims, but it has done so in an ambiguous and confused fashion that ultimately leaves the question up in the air. In two companion cases decided several years apart, *Concrete Pipe & Products of California, Inc. v. Construction Laborers Pension Trust for Southern California*, and *Connolly v. Pension Benefit Guaranty Corp.*, the Court addressed takings claims arising from federal legislation that increased employers' pension liabilities and abrogated the employers' agreements with their employees to cap contributions to employee pension funds. While the Court plainly viewed the contractual agreements as relevant to the takings analysis, the opinions are opaque on whether the property allegedly taken was the additional money the companies were required to deposit in the pension funds or the employers' contract right to limit their pension contributions, or possibly both. In any event, the Court's analysis of the takings claims is instructive for present purposes.

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84. See Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1014–20 & n.8 (1992) (distinguishing between the per se test applicable to regulations that deny the owner all economically viable use of the property and the more nuanced *Penn Central* analysis applicable to regulations that result in less than "total takings").
In *Connolly*, to uphold rejection of the takings claim, the Court offered up a smorgasbord of arguments. On the one hand, the Court said that the taking claim failed because “the United States has taken nothing for its own use, and only has nullified a contractual provision limiting liability by imposing an additional obligation that is otherwise within the power of Congress to impose.” While not expressed in the familiar appropriation versus frustration terminology, this ruling appears to follow the logic of *Omnia*; in substance, the Court said there was no taking because the government frustrated the contract (by “nullifying” it) but did not appropriate it (by devoting it to the government’s own “use”). After making this ruling, which the Court might well have treated as sufficient to dispose of the case, the Court went on to say, expressing itself in a convoluted double negative, that its reasoning was “not inconsistent” with the Court’s prior precedents, in particular the *Penn Central* decision. It then proceeded to perform a separate, comprehensive analysis of the taking claim based on the *Penn Central* three-factor framework. The Court concluded all of the factors weighed against the taking claim, observing that the legislation involved a traditional government effort to “adjust[] the benefits and burdens of economic life to promote the common good,” that “a significant number of provisions” in the legislation “moderate[d] and mitigate[d]” the impact of the legislation, and that “prudent employers” in the position of the plaintiff should have known that withdrawal from the pension “might trigger additional financial obligations.” In sum, the Court concluded that the claim failed under *Penn Central*, but without actually resolving whether the *Penn Central* framework was sufficient to resolve this type of claim. The Court in *Concrete Pipe*, a few years later, applied the same ambiguous analysis.

The Court’s discussion in *Connolly* about the employers’ asserted contractual rights reveals the Court’s uncertainty about how to address this type of claim. Justice Byron White, writing for the Court, began by asserting that the taking claim “gains nothing” from the company’s contractual agreement with its employees. “Contracts, however express,” he said, “cannot fetter the constitutional authority of Congress.” In the same vein, he also said that when “contracts deal with a subject matter which lies within the control of Congress, they have a congenital infirmity.” Taken together, the foregoing statements suggest that government interference with a private contract, by

88. *Id.* at 224.
89. *Id.*
90. *Id.* at 224–27.
91. *Id.* at 225.
92. *Id.*
93. *Id.* at 227.
94. *Id.* at 223.
96. *Id.* at 223–24 (quoting *Norman*, 294 U.S. at 307–38).
itself, can never give rise to a valid taking claim. On the other hand, he also said that contracts "may create rights of property," and then, restating the point in obverse fashion, declared, "This is not to say that contractual rights are never property rights or that the Government may always take them for its own benefit without compensation." 97 Finally, in summing up, and specifically citing Omnia, Justice White wrote that "the fact that legislation disregards or destroys existing contractual rights does not always transform the regulation into an illegal taking." 98 The only possible reading of Justice White's opinion is that, while wishing to dispose of the takings claim in this case in favor of the government, the Court (or at least Justice White) wished to place as few limits on the Court's future options as possible!

As Justice White's opinion demonstrates, there is no particular obstacle, in a mechanical sense, to applying the Penn Central factors to evaluate a claim of a taking of a contract interest (assuming such an interest constitutes property). But the larger question, with which neither Connolly nor Concrete Pipe grapples, is whether alleged takings of private contract interests should be evaluated in the same fashion as any other contract claim. Treating contract interests as being the same as any other property, and analyzing private contract takings claims under the same standards as any other taking claim, would have the virtue of promoting consistency and doctrinal coherence. But the longstanding appropriation versus frustration standard limits the scope of the Takings Clauses as applied to contract interests relative to the way the Takings Clause applies to other types of property. Thus, applying the modern Penn Central analysis to contract interests would expand the scope of current takings doctrine. Given the large number and wide variety of private contract expectancies that can potentially be affected by government action, the magnitude of the expansion would be considerable. Whether or not such a dramatic change in the scope of takings doctrine would be desirable depends upon one's normative assessment of the takings project in general. Those who believe takings law is not sufficiently protective of private property rights would undoubtedly welcome as positive steps the elimination of the appropriation versus frustration standard and the assimilation of this claim into the main body of takings law. On the other hand, those who are concerned about the potential for takings liabilities to undermine representative democracy would tend to be reluctant to endorse this change, the advantages of consistency and coherence notwithstanding. 99 Furthermore, accepting for the sake of argument that potential takings liability can sometimes serve as a useful

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97. Id. at 224 (emphases added).
98. Id. (emphasis added).
99. Cf. Omnia Commercial Co. v. United States, 261 U.S. 502, 513 (1923) ("The government took over during the war railroads, steel mills, shipyards, telephone and telegraph lines, the capacity output of factories and other producing activities. If appellant's contention is sound the government thereby took and became liable to pay for an appalling number of existing contracts for future services or delivery, the performance of which its action made impossible.").
restraint against government overreaching, it is debatable whether this logic applies, or at least applies with the same force, in the contracts context, given the varied and private character of many contracts and the consequent unpredictability of the effects of government action on contract interests and contracting parties.

Finally, and perhaps most importantly, applying a traditional takings analysis to alleged public takings of private contract rights overlooks the distinctive character of property rights based on private contracts, the focus of the next Part. It might be contended that the specific nature of the property interest created by contract should not matter because, regardless of whether a claim is rooted in contract or ownership of a parcel of real property, for example, the fundamental issue remains the same: have the claimant's expectations been unreasonably frustrated to advance some public purpose? But takings law does not protect expectancies—it protects property interests. Only if a claimed interest independently has the force of law behind it, and only so far as the force of law goes, can a taking claim proceed.

III. TOWARD A NEW TAKINGS JURISPRUDENCE FOR PRIVATE CONTRACTS

The proposed method of applying the Takings Clause to private contract interests discards the idea that "taking" analysis should be tailored to meet this particular category of cases, and instead focuses on the nature of the asserted "property" at stake. According to this proposal, claims of takings of private contract interests deserve special treatment because contract interests represent a special, more limited form of property than more traditional property interests. Once the special character of the property involved is recognized, there is no reason to depart from traditional takings analysis to resolve such a claim.

A. Defining Property Within the Meaning of the Takings Clause

The first step in any takings case is to determine whether the plaintiff possesses "property" and, if so, the nature and scope of the asserted property interest.100 If the challenged government action does not affect a protected property interest, the court need not address whether there might have been a taking if the government action had affected some property interest. Despite the fundamental importance of the threshold property issue in takings litigation, the Supreme Court has given remarkably little attention to this step in a takings case, especially in comparison with its voluminous examinations of what constitutes a "taking."

The Court has asserted that property interests are "not created by the Constitution," but "are created and their dimensions are defined by existing rules or understandings that stem from an independent source such as state law." Read literally, this statement could suggest that the Takings Clause completely delegates the job of defining (and redefining) property interests to state law and state law-making institutions. But the statement cannot be taken at face value, because such a reading would effectively eviscerate the Takings Clause as a federal constitutional safeguard. If the Takings Clause is entirely dependent on how state law defines property, state legislatures could achieve their goals free from any claims under the Takings Clause simply by redefining "property" directly rather than adopting controls on property use. Not surprisingly, the Supreme Court has cut off this alternative by holding that state legislative redefinitions of property, like measures restricting the exercise of recognized property rights, can constitute takings.

The Supreme Court has indicated, if somewhat obliquely, that the Takings Clause must be read to impose certain sideboards on what kinds of state-created interests constitute "property" and how such interests should be characterized for the purpose of takings analysis. First, the Court has said that an asserted property interest must be "specific and identifiable" to qualify as property under the Takings Clause. As a result of this limitation, government actions imposing an undifferentiated financial liability on a firm or individual, or adversely affecting the level of revenues or profitability, do not affect "property" within the meaning of the Takings Clause. Second, while the Court has been more obscure on the point, commentators generally agree that property ownership within the meaning of the Takings Clause must include the authority to exclude others from accessing or using it. This limitation arguably follows from the fact that, in the broadest sense, property law addresses relations among people regarding the control and disposition of things. The constitutional definition of property in the Takings Clause

102. See id. at 164 (ruling that the Florida legislature effected a taking by defining as public property interest earned on private funds held in interpleader account). But cf. Stop the Beach Renourishment, Inc. v. Fla. Dept. of Envtl. Prot., 130 S. Ct. 2592 (2010) (leaving unresolved whether a judicial change in state property rules can constitute a taking of private property).
103. See E. Enters. v. Apfel, 524 U.S. 498, 541–45 (Kennedy, J., concurring in the judgment and dissenting in part); id. at 554–56 (Breyer, J., dissenting).
104. Id.
105. The Supreme Court has repeatedly stated that "the right to exclude" is "one of the most essential" rights of property. See, e.g., Dolan v. City of Tigard, 512 U.S. 374, 384 (1994) (quoting Kaiser Aetna v. United States, 444 U.S. 164, 176 (1979). But it has never gone so far as to say that the right to exclude is an essential element of an interest in order for it to be recognized as "property" within the meaning of the Takings Clause.
106. See Merrill, supra note 45, at 970–71 (advancing this view and quoting other academics who share the same view).
therefore must incorporate some principle for defining the owner—as opposed to a non-owner—of a thing. Finally, the Supreme Court has adopted a principle of agglomeration, the so-called “parcel as a whole” rule, which requires courts to assess the impact of a government action, not in terms of the specific portion of a claimant’s property affected by the action, but in relation to the totality of the property.  

If, for example, a claimant owns a one-hundred-acre parcel of land, and is claiming a taking based on a restriction barring development of one acre of wetlands, the impact of the regulation is measured in relation to the one-hundred acres, not the one restricted acre. The Court has never provided a thorough explanation of the parcel rule. But it is useful, if not indispensable, to support the Court’s longstanding understanding that regulatory takings doctrine should be reserved for “extreme circumstances.” This understanding is supported in turn by the considerable historical evidence that the drafters of the Bill of Rights did not envision that the Takings Clause would apply to regulations at all, and by the fact that the Supreme Court only developed the regulatory takings doctrine early in the twentieth century to address regulations that were so economically burdensome that they were “tantamount” to true takings involving direct appropriations or physical invasions. By contrast, when a government action amounts to an actual appropriation or physical invasion, the parcel as a whole rule does not apply at all.

Applying this guidance, private contract interests appear to qualify, at least in some sense, as “property” within the meaning of the Takings Clause. Private contract interests represent private entitlements that have an obviously different character and origin than other types of property, such as interests in real property. But private contract interests are “specific and identifiable” in much the same way that individual interests in real or personal property are specific and identifiable. Although contract interests do not have the in rem character of interests in land, that does not make them any less specific and identifiable. Similarly, private contracts establish, at least in a limited way, a right to exclude in the sense that only the parties to a contract can exercise the rights and responsibilities created by the contract. A contract right holder perhaps does not have as strong or explicit a right to exclude as the owner of real estate vis-à-vis trespassers. But there is no reason in principle, and

111. See Treanor, supra note 50, at 792–93.
112. Tahoe-Sierra Preservation Council, 535 U.S. at 322 n.17.
114. But cf. Merrill, supra note 45, at 992–94 (arguing that contracts should not regarded as property for the purpose of the Takings Clause).
certainly nothing in Supreme Court precedent, to suggest that a contract right holder does not have sufficiently exclusive rights with respect to the contract to qualify as a property owner for the purpose of the Takings Clause. Whether or not the whole parcel rule affects the treatment of contract interests under the Takings Clause depends upon whether alleged takings of a contract interests should be treated as a kind of regulatory taking or as a direct taking triggering per se analysis. This last issue is addressed below.

If private contract interests can qualify as property for the purpose of the Takings Clause, the next question is the nature and scope of the property interest created by a contract interest. In accord with the understanding that the “dimensions” of property interests are not defined by the Constitution itself, the answer has to be found in state law—specifically, the general common law of contracts.

B. The In Personam Nature of Contract Rights

The most distinctive feature of contracts for present purposes is that they constitute in personam rights. In other words, private contracts establish rights and responsibilities that are generally binding only on the parties, and not on society as a whole. Thus, a valid contract for the sale of goods between company A and company B creates binding legal obligations between the two companies, but not between the companies and the larger world. This is in marked contrast to ownership interests in land, for example, which constitute in rem rights. A sale of Blackacre by company A to company B not only grants rights in the land to B that are enforceable against A, but also establishes rights in B against the world at large, in particular against potential trespassers. The in personam feature of contract law is part of the “background principles” of the common law of contracts that shapes the nature and scope of asserted property rights based on contract.115

The in personam nature of contract interests does not mean that private contracts create no legal rights and responsibilities vis-à-vis third parties. The doctrine of tortious interference with contractual relations proscribes certain kinds of third-party actions affecting private contract interests: “One who intentionally and improperly interferes with the performance of a contract . . . between another and a third person by inducing or otherwise causing the third person not to perform the contract, is subject to liability to the other for the pecuniary loss resulting to the other from the failure of the third person to perform the contract.”116 While this doctrine provides significant protection against third-party interference, it is limited in the sense that it only applies to “intentional” and “improper” interfering acts. By contrast, owners of real property generally have a nearly absolute and unqualified right to exclude third

parties, and trespass law protects owners from virtually any unwanted invasion of their land. While the differences between contract interests and more traditional property interests cannot be expressed in black and white terms, there are sufficient differences between them to support the conclusion that the differences should affect the outcome of takings cases. Because in personam contract interests are more limited than in rem property interests, the protection the Takings Clause provides to the former is necessarily narrower in scope than the protection it provides to the latter.

The more limited nature of property rights based on contract provides a logical basis for distinguishing between how the Takings Clause applies to traditional property interests and how it applies to property interests based on contract. Under the Supreme Court's takings jurisprudence, any government action that directly appropriates or physically invades real property—any action that is akin to a trespass—constitutes a taking. Similarly, by analogy, any economically burdensome regulation of property that is "tantamount" to a classic physical taking will also constitute a taking. This result is consistent with the fact that in rem property interests are generally good against the world, including governmental actors. By contrast, a government action that adversely affects the value or utility of an interest based on contract, without directly interfering with the contractual relationship itself, does not affect an interest encompassed by the contract that creates only in personam rights. Therefore, this kind of effect on a contract right should not support a taking claim. By contrast, when the government, acting in a fashion akin to a tortious interferer with contract, steps into the shoes of one of the contracting parties, and takes over the rights of one of the parties or mandates the transfer of the rights to some third party, the government has interfered with in personam rights established by the contract. In such a circumstance, it is appropriate to treat the interference as the potential basis for a takings claim.

As discussed in greater detail below, this proposed approach will produce results that frequently parallel those produced under the Omnia standard. A government action can be reasonably characterized as merely "frustrating" a contract interest when it adversely affects the value or utility of the interest. On the other hand, a government action can reasonably be characterized as "appropriating" a contract interest when the government directly inserts itself into the parties' contractual relations by assuming the benefits of the contract or transferring them to some third party. It is therefore possible to interpret Omnia's frustration versus appropriation distinction as implicitly resting on the nature of the property interest created by a contract, rather than on the nature of the government action allegedly producing the taking. But the Court has certainly never articulated the distinction in this way. The advantage of explicitly focusing on the nature of the underlying property interest is that it provides a basis for distinguishing private contract takings claims from other

117. See Singer, supra note 107, at 27–28.
types of takings claims that is rooted in the actual nature of the property interests at stake in each type of case. On the other hand, this approach avoids the vague and unmoored distinction between frustration and appropriation in takings analysis. Finally, it promotes a more coherent and consistent takings doctrine generally, by eliminating the need for a special ad hoc takings test for resolving private contract takings claims.

C. The Bilateral Nature of Contract Rights

The second feature of contract interests pertinent to the analysis of public takings of private contracts is the bilateral nature of the contractual relationship. As discussed above, a government action impairing an executory contract will affect the parties on both sides of the contract. It may adversely affect one party, while having a positive impact on the other party. The question created by the bilateral nature of the contractual relationship is whether the courts should focus exclusively on the party to the contract who has come into court asserting economic injury, or whether the courts should also consider the effect of the government action on the other non-injured party. Under this proposal, the courts should take the broader view.

The Supreme Court has repeatedly affirmed that the basic purpose of the Takings Clause is to prevent "government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." In order to apply this principle effectively in the context of an interference with an executory contract, the courts need to analyze the impact of the government action in relation to the contracting parties as a single unit. If a government action has conferred a windfall on one party and imposed a harm on the other party, the net effect on the contracting parties as a unit may well be neutral. It would be unfair to the public to require the government to compensate one party when the other party has received a windfall from the government. The government would be required, in effect, to pay compensation twice. It also would not be necessary or appropriate to provide compensation in this circumstance in order to achieve fairness. The parties, in the course of their negotiations, could have agreed in advance that neither party would suffer any economic harm if some intervening government action ruptured the contract and had a net neutral (or better) effect on the parties considered together. Accordingly, when the net effect of a government action on the contracting parties as a unit is neutral (or better), any takings claim should be rejected.

This proposed rule presupposes that the parties could and would negotiate over this issue ex ante, in advance of the government action impairing the contract and giving rise to the taking claim. Imposing this type of duty on contracting parties is both fair and practical. It is fair because it is within the power of the parties to ensure that neither party is economically injured, and

any harm to either party flowing from the parties' lack of foresight should not be imposed upon the public. It is practical because this type of contract term is analogous to the kind of risks of future events, such as potential government exercises of the eminent domain power or destructive acts of God, that contracting parties routinely address in contract documents. Once it is established that parties can and should anticipate possible government disruption of their contractual relationships, contract terms addressing this issue will likely become a routine matter in commercial negotiations, helping to avoid an *Omnia* situation.

Based on this analysis, it is easy to reach the outcome in *Omnia*, although it was decided on other, incorrect grounds. Assuming the government requisition order constituted the type of governmental interference with a contract that would support a finding of taking, the net economic effect of the order on the two parties was neutral. *Omnia* was unquestionably harmed by the government's requisition order, but the order simultaneously conferred a windfall on Allegheny. *Omnia* and Allegheny could have guarded against the risk of financial loss to either party due to government interference with their contract by requiring Allegheny to transfer any windfall to *Omnia*.1

There was no justification based on "fairness and justice" to award takings compensation to *Omnia*.

**D. Defining the Appropriate Takings Analysis**

Under the foregoing analysis, a private contract takings claim will lie when: (1) the government has directly inserted itself into the parties' contractual relationship, by assuming the contract benefits of one of the parties, or by transferring them to some new party; and (2) when the government action imposes a net burden on the contracting parties considered as a unit. The only remaining issue to be addressed is which takings test to apply to a private contracts takings claim.

A preliminary question is whether, assuming a contract interest would otherwise constitute protected property for takings purposes, other background principles of state (or possibly federal) law might bar the claimant from asserting a property interest based on the contract. One type of contract for which this type of threshold analysis might matter would be contracts designed to serve an illegal purpose, which are generally unenforceable by the parties as a matter of law.2 Because no contract right holder can claim a protected right to enforcement of an illegal contract, a party to an illegal contract should be barred from claiming a taking of such a right.

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The more consequential question is what takings test should apply when the government allegedly takes a private contract interest in accordance with the limitations of the claim outlined above. The answer is that the taking claim should be analyzed as a per se taking. In other words, if the government action directly intrudes upon the contractual relationship itself, imposes a net economic burden on the contracting parties, and no relevant background principle applies, the government should always be liable for compensation under the Takings Clause. Under this proposal, a viable taking claim can only arise when the government takes over the contract rights of one of the contracting rights, or transfers the rights to a third party. This type of government action should be viewed as a kind of appropriation of private property warranting per se treatment. On the other hand, the standard Penn Central analysis does not apply to this type of action because it does not involve the kind of constraint on the use of property that triggers a regulatory takings analysis. This proposal is not, in the end, an argument for highly forgiving review under the Takings Clause. It is a proposal for demanding review within a narrow sphere.

It remains to be determined precisely how to define the “taking over” of a contract right. One option is to reserve the “taking over” concept for a situation where the government mandates a literal assignment to itself of all the outstanding rights under an executory contract, or the assignment of such rights to a third party. A second, more practical approach would be to disregard the precise terms of the original contractual arrangement and instead focus on whether the government has seized the functional equivalent of the right to receive the substance of the performance promised. Focusing on substance rather than form, it appears more sensible to ask whether the government has taken over the benefits of the contract, regardless of whether all the original contract terms apply. Thus, for example, in Omnia the Court should have regarded the government as having substituted itself for Omnia in its contractual relationship with Allegheny, even though the United States did not demand a formal assignment of the prior contract. Of course, for the reasons just described, the taking claim in Omnia nonetheless should have failed, but on other grounds.

E. Applying the Proposed Test

Reexamining cases decided under the Omnia standard using this proposed method yields the conclusion that some prior cases were correctly decided for the wrong reasons, and some were incorrectly decided.

As discussed, under the proposed analysis, the Supreme Court correctly rejected the taking claim in Omnia but for the wrong reasons. The United States in effect took over Omnia’s contract rights by appropriating its right to receive

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the steel under its contract with Allegheny. Nonetheless, the takings claim was properly rejected because, under the second part of the proposed test, the requisition order did not impose a net loss on the contracting parties as a unit.

Applying the proposed analysis to the facts of *Palmyra Pacific Seafoods, LLC v. United States*,\(^{122}\) suggests that the U.S. Court of Appeals for the Federal Circuit properly rejected this takings claim. The Court ruled that the Department of Interior did not effect a taking of a private contract interest when it established a National Wildlife Refuge around a remote island in the Pacific Ocean.\(^ {123}\) The Department’s action undoubtedly adversely affected the value of the claimant’s contractual right to use the island as the base for a commercial fishing operation by banning fishing around the island. But the Court correctly rejected the claim because the government action did not interfere with the claimant’s contract rights by taking them over or transferring them to a third party. Instead, the government merely made a decision that adversely affected the value or utility of the contract rights. The opinion does not reveal the terms of the contract between the claimant and island owner and, therefore, it is impossible to determine whether the contracting parties, considered together as a single unit, suffered a net harm as a result of the government’s action. Thus it cannot be determined whether there might have been an alternative basis for rejecting the claim.

On the other hand, applying the proposed method, the U.S. Supreme Court probably erred in upholding the takings claim in *International Paper Co. v. United States*.\(^ {124}\) The Court ruled that the United States was liable for a taking when it directed a power company to cease delivering hydropower to the International Paper company, which had a contract right to the power, and ordered the power company to instead deliver the power to another company. The United States directly inserted itself into the parties’ contractual relationship by, in effect, transferring International Paper’s contractual right to performance to a third party. However, based on the facts recited in the Court’s opinion, it appears that the government requisition order probably did not have an adverse economic effect on the parties when considered as a single unit. Thus, the claim should have been rejected.

Finally, applying the proposed analysis, the U.S. Court of Appeals for the Federal Circuit probably erred in *Huntleigh USA Corp. v. United States*\(^ {125}\) by rejecting a meritorious taking claim. Congress effected a taking by abrogating the claimant’s contractual agreement with airline companies to provide passenger screening at the nation’s airports by transferring this responsibility to the newly created Transportation Security Agency. The federal legislation authorizing the government takeover acknowledged as much by explicitly

\(^{122}\) Palmyra Pac. Seafoods, LLC v. United States, 561 F.3d 1361, 1363 (Fed. Cir. 2009).

\(^{123}\) Id. at 1363–64, 1370.

\(^{124}\) See Int’l Paper Co. v. United States, 282 U.S. 399, 408 (1931).

\(^{125}\) Huntleigh USA Corp. v. United States, 525 F.3d 1370, 1373 (Fed. Cir. 2008).
authorizing the TSA to choose between either literally taking over the existing contracts (and paying just compensation for the taking), or simply declaring that it would take over the screening function in fact (without paying compensation). By allowing the agency to chose the latter option, the Federal Circuit elevated form over substance; under both options, the government was substituting itself for the company in performing the contracted for services. Furthermore, there is no indication in the Court’s opinion that the economic effect on the contracting parties was neutral. The government should have been liable for a public taking of a private contract interest.

CONCLUSION

This Article offers a specific doctrinal solution to a frequently recurring question in takings litigation: how to analyze an alleged taking of an asserted property interest grounded in a contract expectancy. The case for rejecting the nearly one-hundred-year-old appropriation versus frustration standard rests on the fact that it is anachronistic throwback to an outmoded reading of the Takings Clause, lacks any logical or coherent foundation, and represents a strange legal outlier that mars the newly emerging coherence of takings doctrine. The case for this new test, in contrast to the existing test, is that it is logically rooted in the special features of this particular takings claim and supports greater doctrinal coherence. Eventually, the Supreme Court will need to reexamine its Omnia precedent. This Article hopefully provides a place to start.

The analysis in this Article also raises larger issues about takings doctrine. First, a key theme has been that judicial analysis of private contract takings claims has focused too much on how the alleged “taking” should be analyzed instead of on the nature of the asserted property interest. A similar focus on the underlying property interest might be productive in addressing other types of takings claims. Examination of a takings claim typically begins by asking whether the claimant can point to a protected property interest, and the issue is often answered in blunt yes/no fashion. As illustrated by this Article’s examination of private contractual interests, however, the claimant may be able to point to property, but it may have a limited or nuanced character. Perhaps a similarly qualified approach could be deployed in other types of takings cases.

For example, a recurring debate in takings law is whether the categorical takings rule announced in Lucas v. South Carolina Coastal Council only applies to full fee interests in land, of the kind at issue in that case, or whether the logic of the opinion extends to the destruction of any stick in the bundle of

126. Id. at 1374–75
property interests, no matter how narrow the stick. Most of the analysis of this question has considered whether the so-called Lucas per se takings rule can and should be broadly applied. But the question might more profitably be addressed from the other direction, by asking whether the distinctive scope and character of less than fee interests call for a different outcome.

The analysis in this Article also may offer some useful guidance on how the courts might address takings claims based on alleged government impairments of contracts to which the government itself is a party. As discussed, a key difference between public-private contracts and private-private contracts is that government impairments of the former raise the possibility of a takings claim in lieu of or perhaps alongside a breach of contract claim. Setting aside this important complexity, which raises a host of difficult issues, there is no obvious reason why an alleged taking of a property interest based on a public-private contract should be analyzed any differently than an alleged taking of a property interest based on a private-private contract. In particular, if the in personam character of a contract right is the key factor defining the potential scope of a taking claim in the latter type of litigation, why not in the former type as well?


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