No. 09-766

IN THE

Supreme Court of the United States

PALMYRA PACIFIC SEAFOODS, L.L.C.;
PALMYRA PACIFIC ENTERPRISES, L.L.C.,
PPE LIMITED PARTNERSHIP;
AND FRANK SORBA

Petitioners,

v.

UNITED STATES

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

PETITIONERS' REPLY BRIEF IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI

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RULE 29.6 STATEMENT

Petitioners respectfully make reference to the Rule 29.6 Statement included in our December 29, 2009 Petition for a Writ of Certiorari. That statement remains accurate and current in all respects.

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INTRODUCTION

The arguments in the Government's Opposition Brief — and reasoning of the Federal Circuit decision the Government seeks to keep this Court from reviewing — treat contracts as a lesser form of property, to which the full protection of the Fifth Amendment's Takings Clause does not apply.

Principally, the Government argues that the Court need not concern itself with this case because, in the Government's view, the Government affected PPS's contract indirectly rather than directly. Even if that were true (and it is not), this Court's regulatory-takings decisions establish that the Takings Clause protects other forms of property against the indirect effects of Government action. Thus, unless a special takings doctrine applies to property that happens to be in the form of a contract, the Government's position conflicts with precedent.

The basic issue presented in this case, therefore, is whether contracts are entitled to the same, modern Takings Clause protection — including protection against the sort of non-appropriative regulatory takings that the Government worked on PPS's contract — as other forms of property. That issue underpins both of the Questions Presented set forth in our Petition. Those questions are timely and of great national importance, and this Court should grant the Petition so that it can resolve them.

I. THIS CASE PRESENTS AN EXCELLENT VEHICLE FOR THE EXPOSITION OF REGULATORY TAKINGS DOCTRINE AS IT APPLIES TO CONTRACTS

The Government asserts that "[t]his case would present a poor vehicle" "to determine "whether regulatory-takings principles apply to contracts." Opp. Br. 14. As support, the Government claims that regulatory takings doctrine — indeed, *all* takings doctrine — is inapplicable here because the Government frustrated PPS's contract rights without acting against them "directly." *Id*. *See also id*. at 9, 10, 15.

The Government's premise that it acted only indirectly against PPS's contract is incorrect. PPS showed — without the benefit of any discovery — that the Government acted directly. Government agents, "upset" that PPS held the contractual right to establish a commercial fishing base on Palmyra, sought to "beat up" on PPS. Pet. App. 40a. In short order, the same department of the Government propounded regulations that made it impossible for PPS to exercise its contractual rights meaningfully. *See id*. at 4a. The Government acted with the purpose of negating PPS's contract, and the Government's acts had precisely the intended effect. That is about as "direct" as Government action can get.

Regardless, even if we credit the Government's argument that it acted only indirectly against PPS's contract, the Government's conclusion that no takings liability can attach does not follow.

A. The Government is Not Automatically Immune From Takings Liability Where Its Actions Cause Harm Indirectly

This Court has repeatedly held that where the property interest underlying a takings claim is land, indirect effects of Government action can so severely impair the owner's use of the property as to effect a compensable taking.

For example, in *United States v. Kansas City Life Ins. Co.*, 339 U.S. 799 (1950), the Government dammed the Mississippi River, which flowed at its closest point more than a mile from plaintiff's property. The dam had the direct effect of raising the level of the Mississippi to its ordinary high-water mark and continuously maintaining it there. Raising the river level had the indirect effect of raising the level of a tributary, Dardenne Creek, that abutted plaintiffs' farmland. In turn, raising the level of the creek had the second-order indirect effect of "rais[ing] the water table and soak[ing] [plaintiff's] land sufficiently to destroy its agricultural value," *without* submerging the surface. *Id.* at 810 & n.5. While acknowledging that "[t]he plaintiff still owns its land," *id.* at 804 n.4, the Court held that "the resulting destruction of the agricultural value of the land affected, without actually overflowing it, is a taking of private property within the meaning of the Fifth Amendment." *Id.* at 801.

Similarly, in *United States v. Causby*, 328 U.S. 256 (1946), the Court held that frequent, low-altitude military flights within the federal air

servitude above plaintiff's farm so deleteriously affected the land as to effect a compensable taking. There, as here, the Government argued that any effect was incidental, consequential, and indirect, and therefore not cognizable as a taking: "The United States concludes that when flights are made within the navigable airspace without any physical invasion of the property of the landowners, there has been no taking of property. It says that at most there was merely incidental damage occurring as a consequence of authorized air navigation." *Id*. at 260. The Court rejected that position and held that a compensable taking had occurred. *Id*. at 267. *See also Portsmouth Harbor Land & Hotel Co. v. United States*, 260 U.S. 327 (1922) (Government firing artillery rounds over but not onto plaintiff's land could constitute a taking).

To the extent it might be argued that *Causby* and *Portsmouth Harbor* involved direct rather than indirect effects because the planes and shells at issue passed directly above the plaintiffs' land, the lower courts have not adopted such a narrow interpretation. Indeed, none other than the Federal Circuit has held that "nothing in *Causby* or the intervening precedent limits a takings claim" involving military aircraft noise and vibration to flights passing directly over the subject land. *Argent v. United States*, 124 F.3d 1277, 1282 (Fed. Cir. 1997). In that case, the Government again asserted the direct/indirect distinction, but was rebuffed:

> [T]he Argents allege[d] that the rearward blast of the jets as the Navy planes corner destroys their enjoyment

> of their property *even when the aircraft do not fly directly over their land*. According to the Government, however, the Argent's cannot base their claim on all the United States' flights around [the relevant base], but must base their claim *solely on those flights passing directly overhead*.

Id. (emphasis added). The Court of Appeals rejected the Government's argument. "The Government ascribes to takings jurisprudence an inflexibility that does not exist. The United States may take private property not only by physical occupancy, but also by imposing such burdens upon the use of the property as to deprive the owner of the enjoyment of the land." *Id*. at 1283 (citation omitted).

Thus, where the underlying property is land, the Government can effect a taking indirectly. Moreover, this Court has also held that Government action that indirectly affects property *other than land* can support a takings claim.

For example, in *Armstrong v. United States*, 364 U.S. 40 (1960), the Court held that the Government effected a compensable taking of certain liens attached to partially built ships the Government had commissioned. The liens could be considered intangible property or they could be considered interests in personalty (the ships and some unused supplies), but they could not be considered interests in land.[1] The Government's direct action in taking

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[1] *See In re Jones*, 768 F.2d 923, 928 (7th Cir. 1985) (Posner, J.) ("While a lien is property, it is not real estate even if it is a lien on real estate. Rather, a lien is intangible personalty.").

possession of the ships had the indirect effect of rendering the liens worthless because sovereign immunity would preclude any action to enforce them.

The Court nevertheless held that the Government's action effected a compensable taking of the liens. As the Court explained:

> The total destruction by the Government of all value of these liens, which constitute compensable property, has every possible element of a Fifth Amendment 'taking' and is not a mere 'consequential incidence' of a valid regulatory measure. Before the liens were destroyed, the lienholders admittedly had compensable property. Immediately afterwards, they had none. This was not because their property vanished into thin air. It was because the Government for its own advantage destroyed the value of the liens, something the Government could do because its property was not subject to suit, but which no private [party] could have done.

Id. at 48.

Thus, the Court has held that the indirect effects of Government action can so severely affect an owner's use of land and personalty — property other than contracts — as to effect a compensable taking.

Accordingly, the Government's argument here — that the purportedly indirect nature of the effects of Government's action on PPS's contract bars PPS's

claim — depends on the application of a special takings doctrine that would apply to contracts but not other forms of property.

B. The Government Also Is Not Automatically Immune from Takings Liability Where It Exercises Sovereign Power

In a slight variation on its indirect-effects theme, the Government also argues that PPS's claim is unworthy of the Court's attention because the Government's regulation addressed a subject over which the Government has sovereign authority, *i.e.*, activity in the waters of the United States. *See* Opp. Br. 9, 10.

It is true that the Government established the Palmyra National Wildlife Refuge in the ocean, not on land. And it is true that the Government has sovereign authority over the part of the sea in which the Refuge was established.

But it is *not* true that those facts doom PPS's claim. This Court's takings decisions demonstrate that the Government is not immune from takings liability merely because it acts in an area where it has sovereign authority.

For example, writing for the Court in *Kaiser Aetna v. United States*, 444 U.S. 164 (1979), Justice Rehnquist noted that "this Court has never held that the navigational servitude creates a blanket exception to the Takings Clause whenever Congress exercises its Commerce Clause authority to promote navigation." *Id*. at 172. Similarly, the Court noted in *Causby* that "the United States has complete and

exclusive national sovereignty in the airspace over this country," but held that the way the Government exercised its sovereignty in the air above plaintiffs property effected a taking. *Causby*, 328 U.S. at 260 (internal quotation marks and citation omitted). And in *Kansas City Life Ins.*, the Court acknowledged "the Government's paramount power over the bed of navigable streams," but held the Government liable for a taking that resulted from the Government's placement of a dam within the bed of just such a waterway. *Kansas City Life Ins.*, 339 U.S. at 807.

C. The Character of the Government's Action Against PPS Warrants this Court's Attention

There is no dispute that the Government did not appropriate PPS's contract. Thus, as we explained in our Petition, the tripartite regulatory-takings paradigm this Court established in *Penn Central* provides the proper framework for resolving this case. *See Penn Central Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

Of the three *Penn Central* factors, the most important here is "the character of the government['s] action." *Id.* That factor is most relevant in this instance because the character of the actions the Government took against PPS — at least so far as we could determine based on the limited, pre-discovery record — was, frankly, sinister.

Admittedly "upset" about PPS's contractual right to establish a commercial fishing operation on a remote atoll where a powerful and politically favored

interest wished to establish a glitzy "ecotourism camp," the Government set out to "beat up" on PPS. Pet. App. 40a. The Government settled on a scheme that would negate PPS's contract, but without appropriating it or even so much as acknowledging it in the relevance regulations.

By the Government's lights, though, the character of the Government's action — its choice to "beat up" on PPS — is irrelevant here: No matter how devious the character of Government action that affects a private contract, an injured party like PPS has no recourse under the Takings Clause unless the Government appropriates or "directly" regulates the contract.

In our view, by contrast, the Court's takings jurisprudence is meant to promote "fairness and justice," *see Armstrong*, 364 U.S. at 49, through "essentially ad hoc, factual inquiries," applied flexibly to each case, *see Penn Central*, 438 U.S. at 124. Under such an approach, the character of the Government's actions toward PPS's contract must be considered, not ignored.

* * *

The Government's Opposition asks this Court to countenance different treatment of contracts from other property protected by the Takings Clause. Moreover, the Government's position that direct action can support a takings claim but indirect action cannot would preclude courts from considering the character of the Government's action where that action is most devious.

Those are the circumstances in which a takings remedy is most necessary. This case is a perfect vehicle for determining the extent to which the Takings Clause, and regulatory takings doctrine established thereunder, provides for one when the property at issue is a contract.

II. WE DID NOT WAIVE THE ARGUMENT THAT GOVERNMENT FRUSTRATION OF A PRIVATE CONTRACT CAN EFFECT A COMPENSABLE REGULATORY TAKING

The Government asserts that in the court of appeals, we "did not distinguish between appropriations and regulatory takings, and [we] did not ask the court to conduct a *Penn Central* analysis." Opp Br. 15.

In our Federal Circuit briefing, we cited to *Penn Central*, and implored the court to remand the case so that the trial court could conduct the "case-specific, fact-intensive inquiry" *Penn Central* mandates. *See* PPS Appeal Br. 16 & n.53. Our appellate briefing stressed the same issue presented in our Petition — whether the decision in *Omnia Commercial Co. v. United States*, 261 U.S. 502 (1923), precludes a takings claim where the character of the Government's action is to nullify a particular private contract by frustration. *See id*. at 26-41; PPS Appeal Reply Br. 13-19.

To be sure, our briefing in the Court of Appeals focused on the applicability of takings doctrine generally rather than on regulatory takings doctrine

specifically. But regulatory takings doctrine is obviously a lesser included element of takings doctrine, and our briefing unquestionably addressed a key element of regulatory takings analysis — the character of the Government's action against PPS's contract rights. We emphasized the importance of the "motivation" and "purpose" animating the Government, *see*, *e.g.*, Appeal Br. 18-25, and we argued that the "nature of the government's action here is crucial and dispositive." Appeal Reply Br. 14. Thus, we have raised no new issue in our Petition to this Court by noting that the Federal Circuit failed to apply *Penn Central* properly.

III. THE CIRCUIT SPLITS WE IDENTIFIED ARE REAL

The Government claims that the circuit splits we identified in our petition are illusory. Not so.

A. The Circuits Are Split on the Degree of Takings Protection to Be Afforded Contracts

The Government first claims that "there is [no] disagreement among the circuits on th[e] question" whether contracts are or are not property protected by the Takings Clause. Opp. Br. 11-12.

In describing the Seventh Circuit's decision in *Pro-Eco, Inc. v. Board of Comm'rs*, 57 F.3d 505 (7th Cir. 1995), though, the Government makes our point for us. As the Government notes, the Court of Appeals "concluded that, because 'options to buy real estate do not create property rights *in real estate*' under Indiana law, the plaintiffs' option to purchase

land in Indiana was 'not a property interest protected by the Takings Clause.'" Opp. Br. 13 (*citing Pro-Eco*, 57 F.3d at 509-11) (our emphasis). The Seventh Circuit's holding, therefore, is that a contract — the plaintiff's option to purchase land — is "not a property interest protected by the Takings Clause" because it is not an interest in "real estate." *See Pro-Eco*, 57 F.3d at 509-11. The Seventh Circuit could not have been more clear — interests in land are protected property, whereas purely contractual interests are not. As we noted in our Petition, this holding conflicts with that of other Courts of Appeals. Pet. 6-8.

The Government also asserts that "there is no dispute" between the parties here as to whether contracts are property protected by the Takings Clause. Opp. Br. 12. But as we have explained, the Government's arguments depend on treating contracts differently from other property for takings purposes. We disagree. Hence, despite the Government's protest, the issue is in dispute.

B. The Circuits Are Split on the Applicability of Regulatory Takings Doctrine to Contracts

The Government claims that no circuit split exists concerning the application of regulatory takings doctrine to contracts because "the Federal Circuit *has* applied regulatory-takings analysis to contract rights." Opp Br. 16 (Government's emphasis). To support that claim, the Government directs the Court to *Cienega Gardens v. United States*, 331 F.3d 1319 (Fed. Cir. 2003).

Evidently, the Government and the Federal Circuit understand that decision differently. In its opinion here, the Federal Circuit distinguished *Cienega Gardens* because "[t]he 'distinct property interest' that was taken in *Cienega Gardens* was the developers' '*real property rights* to sole and exclusive possession after twenty years and to convey or encumber their properties after twenty years,'" *i.e.*, (at least in the court's eyes) *not* a contractual interest. Pet. App. 14a (emphasis added).

CONCLUSION

The Federal Circuit and the Government would excuse the Government from paying just compensation when it takes property in the form of contracts, so long as the Government cloaks its actions as negating contracts indirectly — *i.e.*, by frustration — rather than by appropriating the contracts or regulating them "directly."

With the benefit of such a rule, the Government would have every incentive to frustrate private contracts it deems undesirable out of existence. And as we demonstrated in our petition, the Government has recently given every indication that it finds many types of common private contracts undesirable.

In many — probably most — instances where Government action frustrates a private contract, the public and general "character of the government['s] action" will not support a takings claim. We accept that "Government hardly could go on if to some extent values incident to property could not be diminished without paying for every such change in

the general law." *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 413 (1922).

But in other, especially troubling, cases — like here, where "upset" Government agents schemed to "beat up" on PPS, then did so by frustrating PPS's valuable contract rights — the character of the Government's conduct is so specific and so sinister as to require a remedy.

Accordingly, we respectfully urge the Court to grant the Petition so that it can decide whether one is available.

Respectfully submitted,

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April 12, 2010