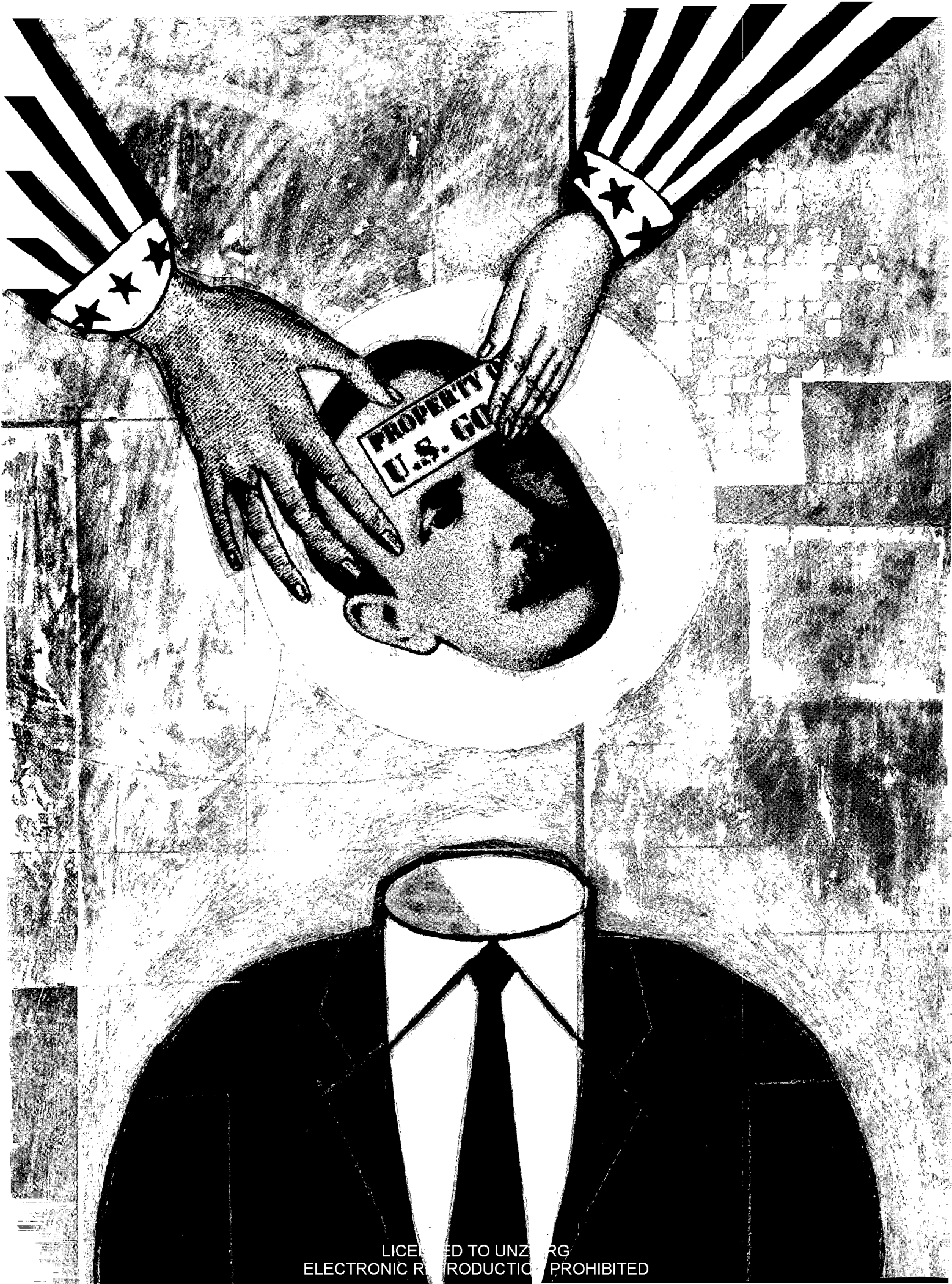

Taking Back the Fifth

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As government expands "takings" to intellectual property and other intangibles, will business start to care about property rights?

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In political discourse, *property rights* is the shorthand term for a constellation of legal, political, and moral issues surrounding the treatment of private property by governments. Those immersed in the topic think governments at all levels—local, state, federal, and international—have become cavalier about property rights, not just willing but eager to ignore both the letter and the spirit of the commandment in the Fifth Amendment to the U.S. Constitution that says "nor shall private property be taken for public use without just compensation." As a consequence, an institution that constitutes one of our most important civil liberties, essential to the economic efficiency of our society and to its moral ordering and legitimacy, is being undermined.

Property rights buffs usually focus on problems involving real estate. Examples are easy to find; regular newspaper reading quickly produces a large pile of clips about the use of government regulations to appropriate large chunks of property value. Often the owner is left with the husk of formal title (and the burden of real estate taxes) but stripped of ownership's benefits. Even if the goals are exemplary—stopping pollution, for example, or protecting rare animals—the means, which force a few landowners to pay for something that benefits the public as a whole, are not.

A press gang mentality is abroad in the land. During the Napoleonic Wars, England manned its ships through kidnapping. Anyone who "used the sea" was fair game to be pressed into the navy and sent off on voyages that might last for years. Contemporary environmentalism follows a similar principle: Anyone who uses the land can be pressed into the cause of environmental protection.

See, for example, the April 1 *Washington Times*, which describes the travails of John Taylor, a 79-year-old retired contractor who lives in the District of Columbia. Since his 74-year-old wife uses a wheelchair, Taylor wants to move out of their multistory house and into a single-story home he planned to build on an adjacent lot he owns. But a bald eagle has built a nest on nearby land, and the U.S. Fish & Wildlife Service has decreed a 750-foot no-build buffer around it, despite the fact that 10 houses already exist within the zone. The service is willing to let Taylor build the new home if he contributes $3,500 to a fish restoration program in the Potomac River aimed at increasing the food supply for eagles. The program has nothing to do with the nearby nest, but this is how things work under the Endangered Species Act. Taylor, exhibiting a punctilio of honor badly out of sync with contemporary Washington, refuses, saying: "I'm not going to bribe my government to let me build on my own land."

Other government actions, such as a recent effort to condemn land in Atlantic City so a casino could build a parking lot there, reallocate property rights among citizens. Or they exclude people from the public domain of the West—lands which, under a century-old bargain, the federal government is supposed to administer in a manner allowing reasonable access to citizens of every

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By James V. DeLong

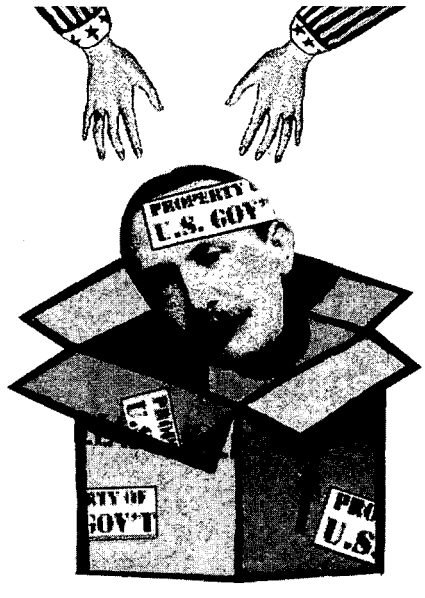
ILLUSTRATIONS: PETER BENNETT

stripe. The new policy is steadily shutting down productive uses of this national commons, eliminating logging, grazing, mining, and recreation.

In recent years, any property rights buff with a mania for piling up news clippings has been forced to add a couple of file cabinets. But the subject matter is changing. The property protected by the Constitution and enshrined in our political tradition encompasses more than real estate. It includes intellectual property such as patents and copyrights, information, business assets, franchises and contract rights, and personal possessions ranging from houses to cars to cash. It includes 401(k) plans, growing like weeds. These are the forms of property that provide the fodder for the latest batch of clips, and this time the involuntary donors include not a just few landowners but some of America's great corporations. As a result, businesses may be waking up to the importance of secure property rights, a shift that could invigorate a movement that so far has met with little success.

Consider some developments that may be prompting corporate America to take a second (or first) look at the Takings Clause:

■ A group of 19 state attorneys general has suggested that the federal and state antitrust action against Microsoft might be resolved by seizing the Windows operating system and making its basic computer code public. This would abruptly turn one of the most valuable chunks of intellectual property in the world into a public commons, as a penalty for actions whose nature and illegality remains unspecified. (See "The New Trustbusters," March.) Nor are the attorneys general alone in their casual attitude toward such property. A recent column in *PC* magazine said bluntly, "Let's nationalize Windows."



■ The Federal Communications Commission has interpreted the Telecommunications Act of 1996 as requiring local telephone companies to make their facilities available to new entrants, at a price based on the hypothetical cost of new, highly efficient technologies. Actual costs do not matter. So an incumbent could wind up eating its investment for the benefit of a rival that has incurred no capital costs and run no risk. In a time of rapidly changing technology, this allows the new entrants to game the system, choosing to share winning investments and sloughing off any responsibility for losing bets. Faced with having their successful investments made into a commons, open to all, the incumbent firms are reluctant to invest, and efforts to promote competition in local service are stagnating.

■ The Pole Attachment Act of 1992 requires utility companies to allow communications firms to hitch lines to their poles. This is a defensible idea, given the monopoly problems intrinsic to rights of way, but it is also an appropriation of property, and it's doubtful that the payments mandated by the FCC represent fair compensation.

■ Under "must carry" rules, cable operators have to transmit without payment the signal of every television station in their catchment areas. Up to a third of channel capacity currently goes to meet these obligations, limiting viewer choice and raising cable prices. For Congress to appropriate one-third of someone's business certainly raises doubts about its respect for property.

■ In response to a lawsuit, the state of Florida argues that the constitutional doctrine of "sovereign immunity" protects it from being sued in federal court for patent infringement, despite an explicit federal law to the contrary. The implication of this position, which the Supreme Court is now considering, is that each state should be free to decide for itself how far, if at all, its government will recognize people's rights in their intellectual property. Florida is supported by 23 other states. Patents, and intellectual property in general, are the crown jewels of the modern business enterprise, so the idea that their integrity and protection could be subject to the fragmented whims of 50 different states makes businesses very nervous.

■ The U.S. Patent and Trademark Office recently stripped the Washington Redskins football team of its trademark protection for *Redskins*, on the ground that it's a pejorative term. The federal trademark statute, which defines the scope of protection given names, logos, and other brand identification assets, excludes names that are "disparaging," but until now this provision has been applied only to new applications. Experts say they have never before heard of an existing mark being canceled after 70 years because it had, over time, come to be viewed as disparaging by some people.

■ In Colorado, the state bar recently beat back a legislative proposal that lawyers be required to devote 10 percent of their time to pro bono work, for causes approved by the state. This may not look like a property rights case at first blush, but think about it. To a professional firm, time is *the* business asset, analogous to capital equipment in a factory or channel capacity in a cable TV system.

■ Electric utilities fear that deregulation of the industry will stick them with unrecoverable ancient costs—incurred, in their view, under government compulsion, in exchange for compensation that is less than "just." The appropriate treatment, legally and morally, of such "stranded costs" is a subject of hot debate.

■ Periodically, proposals surface to divert pension assets into "socially useful" channels—in other words, into channels that benefit politically favored groups. Bank and housing regulators

are already running a program that foreshadows what such a requirement would mean. They allege "discrimination" on the part of financial institutions and then bludgeon them into "community investment" as a form of reparations.

There are signs that businesses, reading such indicators, are beginning to recognize how important property rights are to their bottom lines. Pharmaceutical companies, shaken by federal willingness to trim the rights of patent holders according to the winds of political fashion, showed up on a panel at the last annual conference of the Washington, D.C., legal foundation Defenders of Property Rights. Another participant was Microsoft.

Such interest does not necessarily signify a principled commitment to property rights. Witness the inconsistent stance of the cable industry. A federal judge in Florida recently decided that the Pole Attachment Act, which mainly benefits cable companies, takes the property of utility companies, triggering the Fifth Amendment's requirement of just compensation. Meanwhile, the cable industry has been trying to convince the FCC that "must carry" rules take property without compensation. You might think it would welcome the Florida decision as a useful precedent, especially since pole attachment is a minor issue for the cable industry, while "must carry" really matters, largely because of its huge potential impact in the context of the shift to high-definition television. The industry is also under assault by Internet service providers, which are trying to ensure that any new investments in cable as a means of linking to the Internet are made available to all, not just to ISPs related to the cable companies—another reason to welcome a court's vindication of the Takings Clause. Yet the cable companies are asking an appeals court to reverse the Florida decision.

Similarly, attorneys may object when a state tries to steal their time for pro bono work, but they are happy to help it steal other people's money. Many states require lawyers to deposit client funds entrusted to them in special accounts. The interest, by law, goes not to the clients but to finance state- and bar-approved pro bono enterprises. The rationale is that the amounts are so small that divvying them up is not worth the transaction costs, but this is patently false. A homeowner putting up half a million for a real estate deal loses $82 per day when interest rates are at 6 percent, a sum worth tracking in this era of cheap computing. Last year, in *Phillips v. Washington Legal Foundation*, the U.S. Supreme Court ruled that such interest is indeed property, sending the case back to a district court in Texas to determine whether the state's use of the money amounts to a taking.

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A psychological barrier keeps business executives, and their lawyers especially, from joining the property rights movement. Since the 1930s, legal education has imbued students with contempt for the Supreme Court justices of the early 20th century, who are depicted as mossbacks resisting the progress represented by New Deal.

Not many businesses grasp the connection between government appropriation of property in the name of environmental goals and government appropriation in the name of optimal market structure or for the benefit of campaign contributors or other favored groups. They have not realized that a Congress that does not think twice about the property rights implications of reallocating cable TV channels learned its bad habits from dealing with rural landowners.

Because the connection has not yet been made, property rights issues still have little political traction with the white-collar masses of suburbia or with the business PACs capable of forcing issues to the attention of politicians hungry for campaign cash. Business employees generally have applauded as the right to property was undermined in the name of environmentalism. When Microsoft employees object to the assault on the company's intellectual property, it is fair to ask where they stood when Spotted Owl protection was devastating timbering communities and landowners in the Northwest.

There is also a tendency among business executives to assume that the source of their troubles is some sort of mistake or misunderstanding. Last year, as the Microsoft litigation began to heat up, Bill Gates met with a group of Washington think tank representatives, mostly libertarian in orientation and steeped in the "public choice" view of government as driven by the interests of the people who run it and the groups that reward them. Afterward, Fred Smith, president of the Competitive Enterprise Institute, observed: "Gates still thinks government is basically efficient and effective, but that in this one case it is making a mistake. Once that is pointed out, government will change its policies. He does not realize that to politicians Microsoft is merely a vulnerable and wealthy target, ripe for the picking."

Another psychological barrier keeps business executives, and their lawyers especially, from joining the property rights movement. Since the 1930s, legal education has imbued students with contempt for the Supreme Court justices of the early 20th century, who are depicted as mossbacks resisting the progress represented by New Deal legislation. The political, social, and legal story of that era is much more nuanced then this, of course, but victors write history, and the New Dealers won. The result, after half a century, is that most business lawyers feel uncom-

fortable supporting the right to property. It is like being seen by your neighbor in the X-rated section of the video store.

This discomfort is reinforced by the lawyers' corporate clients, who have been told for 20 years that defending the right to property makes one "anti-environment." Nancy Marzulla runs Defenders of Property Rights and, like anyone in such a position, is always looking for potential supporters. She reports that corporate representatives keep calling, but it is awfully hard to convince them that this is the side they should be on because it's the right side and because it's in their interest.

But the prospect of losing his firm's core assets tends to focus the mind of a corporate executive. So consciousness is indeed being raised, as business realizes there is something new and ominous in the current tide of regulatory proposals. In the past, regulation mostly involved control at the margins. It could be a nuisance, it could raise costs, it could be pointless, but it was an irritant rather than a threat to the essence of the enterprise. Now business as a class is realizing that legislators and regulators are losing their inhibitions, that governments are become more boldly appropriative, not just adding costs but asserting dominion over key assets. As recently as a decade ago, a proposal such as the one put forward by the state attorneys general for Microsoft would have been dismissed as nonsense. Today, industry had better take it seriously. Gates' next meeting with the think tanks may have a different tone.

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While business executives were looking the other way, thinking it was not their problem, historic protections were being diluted. According to the Supreme Court, regulation does not constitute a "taking" unless it deprives the owner of virtually all use of the property, which means 90 percent of the value can disappear with no redress.

This spillover of property rights issues into the boardrooms of corporate America is creating an interesting political situation. To date, the property rights movement has not been doing very well. It is the ragged relation of conservatism, invited to dinner on major holidays but relegated to the children's table, where its advocates can be patted on the head occasionally while not interfering with the serious conversation.

The reasons for this situation can be understood by considering the economic interests at stake. Because the property rights issue is associated primarily with real estate, the core of the movement is landowners, mostly rural, allied with some natural resource companies, trying to defend against a complex array of regulatory innovations concerning wetlands, endangered species, land use, coastal zones, public lands, rails to trails, heritage rivers, and other causes.

Once upon a time in America, the combination of natural resource companies and rural landowners could make the political system quake. But the technological revolutions of the 20th century have shifted the nation's economic center of gravity, and what counts now is money, machinery, information technology, and brain power. Even agriculture and natural resource industries are as automated as manufacturing plants, no longer relying on the huge base of skilled workers that leads to political power.

In any event, the natural resource companies' interest in property rights is a bit academic. They get burned occasionally on site-specific issues, but they have learned to cut deals, giving up some of their property in exchange for the right to exploit the rest. The payoff demand spurned by John Taylor, the D.C. retiree trying to build a new house, would be a routine transaction to any large company. Besides, if a company cannot operate in the United States, well, it's a big world. As long as Americans need the fruits of the earth to support their consumption, a timber, mining, or oil company can find more welcoming climes and ship its products home.

Even real estate developers, who cannot move offshore, are not vitally concerned with property rights. They have learned not to inventory land. They buy options, get all the permits nailed down, and only then take title. The nation wants homes, workplaces, and malls, so the developers will be allowed to build somewhere, and the exact site matters little to them. In fact, the tighter the restrictions, the higher the rewards to those who can navigate the environmental and permitting maze, and the higher the roadblocks against less savvy or well-wired competitors.

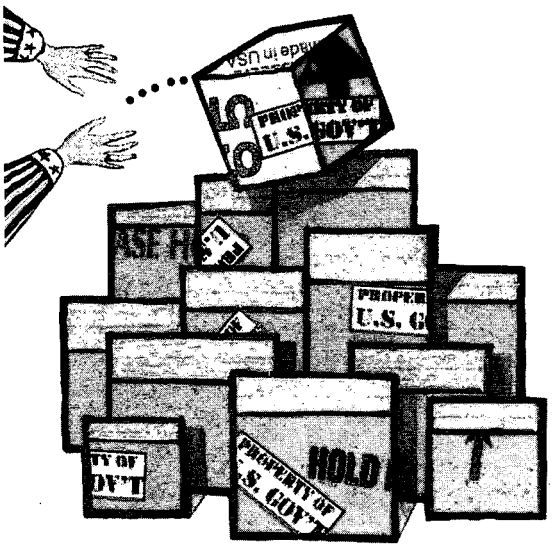
The outcry from the general public is muted as well. Most people use land to live or recreate on, not to make a living. The offending rules are not directed at the homeowners of suburbia, for whom property is a consumption item. Restrictions do affect some members of this class, and the files of the advocacy groups are full of dire tales from individual homeowners like John Taylor. Restrictions may also raise housing prices and impose other indirect costs, such as longer commutes and more unattractive sprawl, but these are pretty well hidden. Governments are not assaulting suburbanites as a class in an obvious way, and any nascent resistance has been mild.

The West, in particular, is split on property rights. It is the most urbanized part of the country, judged by the percentage of the populace in metropolitan areas. Urban Westerners are inclined to applaud restrictions on rural land use, by reason of both

environmentalist ideology and perceived self-interest. The less that grazers, loggers, miners, or farmers get to use land, they think, the more will be available for the urbanites. They are not always right in their judgment of self-interest. Obliterating the old logging roads in the national forests, for example, as the Clinton administration is trying to do, turns these into de facto wilderness—accessible only to hardy backpackers, as remote as the moon from the married-with-children set or the geriatric brigade—but that truth has not yet come home to the residents of Denver and Portland.

For the property rights movement, the upshot of these factors is political weakness. Legislation gets introduced in Congress, but it never goes anywhere. States have passed some property protection laws, but these are for the most part Band-Aids. Now that government has expanded its assault on property rights beyond land-based interests to include the bastions of contemporary economic power, the property rights movement may be on the verge of a revival.

When business executives actually examine the body of Fifth Amendment doctrine, they are going to be surprised. While they were looking the other way, thinking it was not their problem, historic protections were being diluted. According to the Supreme Court, regulation (as distinguished from a physical occupation) does not constitute a "taking" unless it deprives the owner of virtually all use of the property, which means 90 percent of the value can disappear with no redress. Nor is there any limitation on the use to which the government puts appropriated property. A "public use" is anything the executive branch says it is, and it can include taking property from one citizen and giving to another. Under existing law, the Taylors have no legal protection from the Fish & Wildlife Service, which can turn their lot into a wildlife refuge even though no wildlife actually live on it. Meanwhile, the Supreme Court has for the most part let stand a host of procedural obstacles designed to block the few claims that are valid under the precedents.



The legal situation is not uniformly bleak, however. Several of the cases won by landowners in recent years erect principles upon which judges can build. Under *Dolan v. City of Tigard* (1994), for example, a locality does not have boundless authority to condition a construction permit on a landowner's willingness to dedicate part of his property to public use. Any requirement must bear a reasonable relationship to problems created by the construction. And under *Lucas v. South Carolina Coastal Council* (1991), a state may not summarily define as a "nuisance" a particular use of land—such as erecting a house on a beachfront lot amid existing beach houses—and then prohibit it. The definition of *nuisance* has to be grounded in the state's established property law.

Furthermore, two recent Supreme Court decisions may be signs of growing judicial uneasiness over the rising tide of legislative and regulatory threats to property rights in the business context. Last year, in *Eastern Enterprises v. Apfel*, the Supreme Court found that Congress had violated the Takings Clause with a law that funds health benefits for former coal miners by imposing a retroactive tax on almost all firms that have ever been in the coal business.

And in the 1996 case *United States v. Winstar*, the Court upheld the contract rights of savings and loan investors who had been promised regulatory relief by the Federal Deposit Insurance Corporation. The gist of the matter was that the FDIC induced sound institutions to ride to the rescue of failing S&Ls by promising that some dubious "goodwill" could be claimed as an asset for purposes of meeting capital requirements. The deal was a bad one for the public, motivated mostly by the government's desire to cover up the magnitude of the S&L disaster by avoiding closure of busted S&Ls, but it was a deal, and the rescuers relied on it. Then Congress outlawed this accounting method, which put the rescuers in violation of capital requirements, and the FDIC closed them down, imposing severe losses on their shareholders. The Court ruled that government could not enter a contract as a party, then turn around, put on a regulatory hat, and repudiate it. It could not rely on its status as a sovereign to summarily snuff out a contract right it had created without paying for the harm caused by the repudiation.

In addition to the possibilities opened up by such rulings, protective legislation, long stalled in Congress, may be viable if political support for property rights spreads beyond the current limited circle. So if corporate officers and directors start carrying around copies of the Constitution and proclaiming, "They can't do that to me," it could turn out that in fact they can't. It would be nice if businesses started doing this as a matter of principle, but principle is not really necessary. It is more important that companies realize this is where their long-term interest lies. Business cannot thrive if its energies are diverted from the economic market into the political market, into continual jockeying for favoritism in a war of all against all. What is really needed for the security of property is intelligent selfishness. ◆

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Required Reading

Why is the Bureau of National Affairs Washington's biggest media organization? Because for more than 70 years, it's covered the government's every move.

By Michael W. Lynch

Ask most Americans which news organization is the most ubiquitous and influential in Washington, and they'll probably name *The Washington Post* or perhaps split the ticket with CNN. They'd be surprised to know that the news organization with the most reporters covering the daily machinations of the federal government is not the mighty *Post*, the hometown's dominant daily. Nor is it *The New York Times*, America's paper of record, which claims to gather all the news that's fit to print.

Washington's most omnipresent media organization is something called the Bureau of National Affairs. Unless you buy one of its products—which means you're most likely a lobbyist, health care executive, bureaucrat, human resource officer, labor lawyer, government affairs manager for a major corporation, or environmental compliance officer—you've probably never heard of BNA. But each day, this unsung company sends about 220 reporters into the halls of Congress and executive agencies, compared with about 60 each for the *Post* and *Times*. These BNA journalists, part of a worldwide staff of 1,657, fill some 200 high-priced publications with thousands of pages of "just the facts" copy, all chronicling, in great detail, what federal, state, and international bureaucracies are up to.

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