APPALACHIAN ELECTRIC REVISITED: THE RECAPTURE PROVISION OF THE FEDERAL POWER ACT AFTER *NOLLAN* AND *KAISER AETNA*

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In 1920, after heated debate,[1] Congress included a recapture provision in the Federal Power Act[2] that permits the United States to take over hydro-

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1. For a complete account of the debate on the Federal Water Power Act before its passage, see J. KERWIN, THE FEDERAL WATER POWER LEGISLATION (1926). *See also* H.R. 910, 66th Cong., 2d Sess. (1920); Chemehuevi Tribe v. FPC, 489 F.2d 1207, 1215-22 (D.C. Cir. 1973), *vacated on other grounds*, 420 U.S. 395 (1975); Fly, *The Role of the Federal Government in the Conservation and Utilization of Water Resources*, 86 U. PA. L. REV. 274 (1938); Pinchot, *The Long Struggle for Effective Federal Water Power Legislation*, 14 GEO. WASH. L. REV. 9 (1945); Shields, *The Federal Power Act*, 73 U. PA. L. REV. 142 (1924); Comment, *Federal Power Act—Jurisdiction and Functions of the Federal Power Commission*, 39 MICH. L. REV. 976 (1941).

2. Congress originally passed the Federal Water Power Act on June 10, 1920. Federal

electric facilities after the expiration of their owners' federal licenses, without paying just compensation.[3] In 1943, in *United States v. Appalachian Electric Power Co.*,[4] the Supreme Court upheld the recapture provision against a challenge that the provision violated the takings clause of the fifth amendment.[5] The validity of the provision is again being questioned because many hydroelectric licenses are nearing the end of their terms.[6]

This Article suggests the reasoning applied in *Appalachian Electric* has been undermined in two recent Supreme Court decisions: *United States v. Kaiser Aetna*[7] and *Nollan v. California Coastal Commission*.[8] Licensees may now want to revisit an argument raised unsuccessfully almost fifty years ago. The Article is divided into five parts. The first part describes the recapture provision and the general consensus that the provision is intended to permit the United States to take private property for less than the just compensation normally required under the fifth amendment. The second part explains the reasoning of the *Appalachian Electric* Court to uphold the recapture provision against constitutional challenge. The third part discusses the *Kaiser Aetna* and *Nollan* decisions and why they cast serious doubt on the continuing validity of *Appalachian Electric*. The fourth section discusses a possible argument of supporters of the recapture provision that, even if the reasoning of the Court in *Appalachian Electric* were no longer viable, the recapture provision would still provide the licensee with *greater* compensation than required under the takings clause. This argu-

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Water Power Act, ch. 285, § 30, 41 Stat. 1077 (1920). In 1935, Congress changed the name of the act to the Federal Power Act, and provided sections 1 to 29 of the Federal Water Power Act, as amended (sections 792, 793, former section 794, sections 795 to 797, 798 to 818, former section 819 and sections 820 to 823 of title 16 of the United States Code) would constitute subchapter I of the Act. Federal Power Act, ch. 689, § 212, 49 Stat. 847 (1935) (codified at 16 U.S.C. §§ 791a-828c (1988)).

3. 16 U.S.C. § 807 (1988). The recapture provision permits the federal government to pay "net investment value" as opposed to "just compensation," which effectively means the government need not compensate the licensee-property owner for any appreciation in the value of the property over the term of the license, which is typically fifty years. *See infra* text accompanying notes 17-26.

4. United States v. Appalachian Elec. Power Co., 311 U.S. 377 (1941).

5. *Id.* at 427-28. The takings clause of the United States Constitution provides: "[N]or shall private property be taken for public use, without just compensation." U.S. CONST. amend. V, cl. 4.

6. One hundred and eighty projects are scheduled for licensing or takeover in 1991 and 1992. 1988 FED. ENERGY REGULATORY COMM'N ANNUAL REP. at 20-32. The Commission notes "relicensing activities will constitute a large element of the Commission's future hydropower agenda." *Id.* at 15.

7. Kaiser Aetna v. United States, 444 U.S. 164 (1984).

8. Nollan v. California Coastal Comm'n, 483 U.S. 825 (1987).

ment is rejected in the fifth part because it is a mere repackaging of the discarded reasoning of *Appalachian Electric*.

I. FERC'S OPTIONS UNDER THE FEDERAL POWER ACT

A. *The Recapture Provision*

Under the Federal Power Act ("Act"), the Federal Energy Regulatory Commission ("FERC") and its predecessor, the Federal Power Commission ("FPC"),[9] issued and issues licenses to build, operate, and maintain hydroelectric project works.[10]

The term of these licenses cannot exceed fifty years, and, under section 799 of the Act, is conditioned on "acceptance by the licensee of all of the terms and conditions of this chapter and such further conditions, if any, as the Commission shall prescribe in conformity with this chapter, which said terms and conditions and the acceptance thereof shall be expressed in said license."[11]

FERC has three options when the fifty-year term expires: (a) reissue a license to the same licensee, (b) take over the project, or (c) issue a license to operate the project to a new licensee.[12] If FERC decides to exercise the second option, it takes possession of the licensee's property that is valuable and serviceable to the operation of the project, subject to the following condition contained in the recapture provision of the Act:

> [B]efore taking possession it [the United States] shall *pay the net investment of the licensee in the project or projects taken, not to exceed the fair value of the property taken*, plus such reasonable damages, if any, to property of the licensee valuable, serviceable, and dependent as above set

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9. In 1977, the FPC was terminated and its functions, personnel, property, and funds were transferred to the Secretary of Energy, except for the licensing and regulatory functions at issue here, which were transferred to FERC. *See* 42 U.S.C. §§ 7151, 7171(a), 7172(a), 7291, 7293 (1988).

10. 16 U.S.C. § 797(e) (1988). "Project works" is defined as "the physical structures of a project." *Id.* § 796(12). "Project" is defined as:

> complete unit of improvement or development, consisting of a power house, all water conduits, all dams and appurtenant works and structures (including navigation structures) which are a part of said unit, and all storage, diverting, or forebay reservoirs directly connected therewith, the primary line or lines transmitting power therefrom to the point of junction with the distribution system or with the interconnected primary transmission system, all miscellaneous structures used and useful in connection with said unit or any part thereof, and all water-rights, rights-of-way, ditches, dams, reservoirs, lands, or interest in lands the use and occupancy of which are necessary or appropriate in the maintenance and operation of such unit.

Id. § 796(11).

11. *Id.* § 799.

12. *Id.* §§ 807-808.

> forth but not taken, as may be caused by the severance therefrom of property taken, and shall assume all contracts entered into by the licensee with the approval of the Commission. The net investment of the licensee in the project or projects so taken and the amount of such severance damages, if any, shall be determined by the Commission after notice and opportunity for hearing. Such net investment shall not include or be affected by the value of any lands, rights-of-way, or other property of the United States licensed by the Commission under this chapter, by the license or by good will, going value, or prospective revenues; nor shall the values allowed for water rights, rights-of-way, lands or interest in lands be in excess of the actual reasonable cost thereof at the time of acquisition by the licensee: *Provided*, That the right of the United States or any State or municipality to take over, maintain, and operate any project licensed under this chapter at any time by condemnation proceedings upon payment of *just compensation* is expressly reserved.[13]

If FERC decides to license a new licensee, the new licensee takes possession of the initial licensee's project property "on the condition that the new licensee shall, before taking possession of such project or projects, pay such amount, and assume such contracts as the United States is required to do in the manner specified in [the recapture provision]."[14] Thus, under this third option, FERC may transfer ownership in a project from one private licensee to another provided the new licensee makes "the same payments to the original licensee that are required of the United States pursuant to [the recapture provision]."[15]

If the project is taken over by FERC, acceptance of the net investment formula of the recapture provision is a standard condition in the license itself under section 799.[16] Therefore, if FERC chooses to reissue a license, the licensee must often agree to accept compensation in the amount of its net investment with the adjustments provided in the recapture provision. Thus, all three options available to FERC at the end of a license term involve some aspect of the net investment formula.

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13. *Id.* § 807(a) (emphasis added). Additionally, after the first 20 years of operation of the project, earned surplus accumulated in excess of a specified reasonable rate of return on the net investment of the licensee is to be maintained in amortization reserves. *Id.* § 803(d). These reserves are, in the discretion of FERC, held until termination of the license or applied from time to time in reduction of the net investment. *Id.* The rate of return and proportion of surplus earnings to be held in the reserves are set forth in the license. *Id.*

14. *Id.* § 808(a).

15. Escondido Mutual Water Co. v. La Jolla Band of Mission Indians, 466 U.S. 765, 769 n.5 (1984).

16. *See* 16 U.S.C. § 803 (1988); United States v. Appalachian Elec. Power Co., 311 U.S. 377 (1941). The requirement of setting amortization reserves is also a standard provision of a FERC hydroelectric project license. 16 U.S.C. § 803 (1988).

B. *Net Investment*

The term "net investment," as used in the recapture provision, is defined as "the actual legitimate[17] original cost" of the project, plus "similar costs of additions thereto and betterments thereof," minus certain deductions.[18] This formula is commonly understood to generate an amount less than one normally required as just compensation under the fifth amendment.[19]

The recapture provision provides for compensation consisting of "net investment . . . *not to exceed* fair value."[20] Thus, the amount of compensation generated by the net investment formula is normally assumed to be something less than "fair value." "Fair value," however, is the standard measure of just compensation under the takings clause.[21] Therefore, the

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17. "Legitimate" as used in this definition has been construed as meaning "reasonable." Alabama Power Co. v. McNinch, 94 F.2d 601, 606 n.3 (D.C. Cir. 1938).

18. 16 U.S.C. § 796(13) (1988). These deductions include the funds held in the project's amortization reserves. Section 796(13) provides in its entirety:

> "net investment" in a project means the actual legitimate original cost thereof as defined and interpreted in the "classification of investment in road and equipment of steam roads, issue of 1914, Interstate Commerce Commission", plus similar costs of additions thereto and betterments thereof, minus the sum of the following items properly allocated thereto, if and to the extent that such items have been accumulated during the period of the license from earnings in excess of a fair return on such investment: (a) Unappropriated surplus, (b) aggregate credit balances of current depreciation accounts, and (c) aggregate appropriations of surplus or income held in amortization, sinking fund, or similar reserves, or expended for additions or betterments or used for the purposes for which such reserves were created. The term "cost" shall include, insofar as applicable, the elements thereof prescribed in said classification, but shall not include expenditures from funds obtained through donations by States, municipalities, individuals, or others, and said classification of investment of the Interstate Commerce Commission shall insofar as applicable be published and promulgated as a part of the rules and regulations of the Commission.

Id.

19. *See, e.g.*, United States v. 5.96 Acres of Land, 593 F.2d 884, 889 (9th Cir. 1979) (noting the recapture provision permits potential United States acquisition of a project for "less than fair market value"—the normal measure of just compensation under the fifth amendment). *See infra* note 21. *See also* Nantahala Power & Light Co. v. FPC, 384 F.2d 200, 211 (4th Cir. 1967), *cert. denied*, 390 U.S. 945 (1968) (assuming net investment is less than "fair value" in the takings sense, thus equating "fair value" with just compensation).

20. 16 U.S.C. § 807(a) (1988) (emphasis added).

21. *See* United States v. 564.54 Acres of Land, 441 U.S. 506, 511 (1979) (fair market value measure is "working rule" in determining just compensation under the fifth amendment).

As explained in more detail, *infra* section II, the licensee-property owner in *Appalachian Electric* argued limiting compensation to net investment would be unconstitutional because the price for its property would be "fixed at less than a fair value, in the eminent domain sense, at the time of the taking." United States v. Appalachian Elec. Power Co., 311 U.S. 377, 427 (1941). In responding to this argument, the Court explained that even if the utility's conclusion were true as to "fair" or "true" value, the result would not constitute a taking. *Id.* at 427-28. Thus, both the licensee and the Court in *Appalachian Electric* assumed the term "fair value"

language of the recapture provision itself strongly suggests the net investment calculation used in the provision could result in less than the just compensation normally required by the fifth amendment.

Similarly, the last clause of the recapture provision provides if FERC decides to take over a project before expiration of a license, *then* the United States must provide "just compensation."[22] This clause suggests the net investment formula applied at the end of the license term differs from the just compensation standard applied before the end of the term.[23] The commentary and legislative history of the Federal Power Act also reflect the common understanding, that, should the United States decide to take over property at the end of a license term, less than just compensation would be provided.[24]

Finally, common sense also leads to the conclusion that the net investment formula provides for less than the just compensation required under the takings clause. A license term is typically fifty years. Under the net investment formula, a property owner does not receive compensation for any appreciation in the project property over the fifty-year term. Under the takings clause, however, the United States must normally pay the fair value of the appropriated property *at the time* it takes the property.[25] By ignoring the appreciated value of the property, the recapture provision fails to provide just compensation as normally calculated under the fifth amendment.[26]

II. *UNITED STATES V. APPALACHIAN ELECTRIC*[27]

Arising from the conclusion the recapture provision provides less than just compensation, is the obvious question of whether that provision violates the takings clause. The Supreme Court answered this question in the negative in *Appalachian Electric*.[28] In this case the United States sued to enjoin an owner of land bordering a river and the appurtenant riparian rights from building or maintaining a dam absent the acquisition of a FPC

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meant "true value," or the amount of compensation needed "in the eminent domain sense"—in other words, just compensation under the takings clause. *Id.*

22. 16 U.S.C. § 807(a) (1988).

23. *See* Nantahala Power & Light Co. v. FPC, 384 F.2d at 211 (the just compensation clause of the recapture provision provides "[s]upport for th[e] view" that the net investment computation for compensation is less than normally needed under the takings clause).

24. Elder, *The Use of Water Power in the Generation of Electricity*, 25 ILL. L. REV. 759, 773 (1931); LeBoeuf, *State or Federal Control of the Water Powers of Navigable Streams*, 15 GEO. L.J. 201, 228-29 (1927); Note, *The Federal Power Act*, 73 U. PA. L. REV. 142, 153 (1924); Comment, *Federal Power Act—Jurisdiction and Functions of the Federal Power Commission—Constitutional Limitations*, 39 MICH. L. REV. 976, 1000 (1941).

25. Monongahela Navigation Co. v. United States, 148 U.S. 312, 341 (1893).

26. Additionally, through use of the amortization reserves set up by the Act, FERC may not have to pay *anything* for appropriated project property. 16 U.S.C. § 807(a) (1988).

27. United States v. Appalachian Elec. Power Co., 311 U.S. 377 (1941).

28. *Id.* at 427.

license.[29] The primary defense of the defendant owner rested on the contention the stream was not navigable, and, therefore, not under the FPC's jurisdiction.[30] The FPC's standard form license also required the owner to accept the net investment compensation formula in the event the government should decide to take over the project after the expiration of the license term.[31] The owner objected to this condition, arguing an owner should not be compelled to accept a price that violated the takings clause.[32]

After focusing its discussion on the navigability question, the Supreme Court addressed the constitutionality of the recapture provision in a few paragraphs. It began its analysis by assuming, but not deciding, the application of the net investment formula could allow the United States to acquire the project property at less than the amount normally required under the takings clause.[33] Any loss under the recapture provision was viewed as "the price which (defendants) must pay to secure the right to maintain their dam."[34] Because the United States could build in the waters, the Court held it could lawfully acquire one already built.[35]

The Court arrived at this conclusion by first noting the United States' navigational servitude precluded the acquisition of a private property interest in the flow of a navigable stream.[36] Because no private property existed in the flow of navigable waters, the Court reasoned the flow had no assessable value to the riparian owner.[37] Therefore, "[i]f the Government were now to build the dam, it would have to pay the fair value, judicially determined, for the fast land; nothing for the water power."[38]

The Court then stated the federal government's navigational servitude would allow it to exclude riparian owners from the benefit of the stream flow without paying any compensation.[39] In other words, the government could simply prohibit every riparian owner or anyone else from building any project on a navigable stream. The Court reasoned that, because the federal government could deny a license, it followed the FPC could condi-

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29. *Id.* at 379.

30. *Id.* at 380. Under the Federal Power Act, FERC controls only the development of electric power on navigable waters (or public lands). 16 U.S.C. § 817(1) (1988).

31. United States v. Appalachian Elec. Power Co., 311 U.S. at 421 n.65.

32. *Id.* at 427.

33. *Id.* at 428.

34. *Id.* at 427-28.

35. *Id.* at 428.

36. *Id.* at 428-29. For a more detailed discussion, see *infra* section IV, subsection B. The nation's navigable waters have always been considered under the control of the federal government pursuant to the commerce clause. Gibbons v. Ogden, 22 U.S. (9 Wheat.) 1 (1824). This control is known as the government's navigational servitude, or the federal dominant servitude. It follows that the proper exercise of the servitude is not an invasion of any private property right. United States v. Rands, 389 U.S. 121, 123 (1967).

37. United States v. Appalachian Elec. Power Co., 311 U.S. 377, 427 (1941).

38. *Id.*

39. *Id.* at 424.

tion a license on takeover for less than "true value".[40] In the Court's view, "this 'is the price which [owners] must pay to secure the right to maintain their dam.'"[41]

In reaching this conclusion, the Court relied on an earlier decision in which it upheld the constitutionality of a Wisconsin law similar to the recapture provision in the Federal Power Act.[42] Under its own version of the recapture provision, the State imposed a permit condition similar to the net investment formula on a plaintiff who sought to build a dam for water power purposes.[43] The Supreme Court found in favor of the State, finding the conclusions of the Wisconsin Supreme Court to be determinative: (1) the riparian owner's right to use the water power in a navigable river was subordinate to the State's power to limit the use or obstruction of navigable waters; (2) the State could forbid all obstructions, such as dams; and (3) "[i]f the legislature may wholly refuse permission to erect a dam or other structure in the navigable waters of the state, it follows that it may grant such permission upon such terms as it shall determine will best protect the interests of the public."[44] In *Appalachian Electric*, the United States Supreme Court followed the rationale of the Wisconsin court—the government's superior power over the water flow permits it to refuse a license without any condition; therefore, the government can impose a condition that the property be subject to acquisition for less than just compensation.[45]

Since the Court's decision in *Appalachian Electric*, no court has found the net investment formula in the recapture provision violates the takings clause.[46] The Supreme Court's more recent decisions in *Kaiser Aetna* and *Nollan*, however, suggest the reasoning used in *Appalachian Electric* may no longer be sound.

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40. *Id.* at 427.

41. *Id.* at 427-28 (brackets in original) (citing Fox River Paper Co. v. Railroad Comm'n, 274 U.S. 651 (1927)).

42. *Id.* at 428. The Supreme Court stated *Fox River* "is decisive on the issue of confiscation." *Id.*

43. Fox River Paper Co. v. Railroad Comm'n, 274 U.S. at 653 (1927). The Wisconsin law provided that every applicant for a permit to build and operate a dam had to agree to allow the State to acquire its property at the end of thirty years for the reproduction cost of the structures and equipment at the time of the takeover, along with the value of the dam site and flowage rights prior to the time the permit was issued. *Id.* at 652-53. Thus, while the appreciation value of the real property and rights associated with that property were excluded, the appreciation value of the structures actually built by the permittee was not.

44. *Id.* at 654-55.

45. United States v. Appalachian Elec. Power Co., 311 U.S. 377, 427 (1941).

46. *See* United States v. Twin City Power Co., 350 U.S. 222, 225-27 (1956) (notes that Court's decisions allow government to use servitude to grant or withhold water rights as it chooses; exclusion of riparian owners from benefits of water power in navigable stream without compensation is "entirely within the Government's discretion"); Nantahala Power & Light Co. v. FPC, 384 F.2d 200, 211 (4th Cir. 1967) (given dominant federal servitude permitting government to prohibit all construction on navigable water, plaintiff conceded the government could grant right to build based on whatever terms it chose).

III. *KAISER AETNA V. UNITED STATES* AND *NOLLAN V. CALIFORNIA COASTAL COMMISSION*

Kaiser Aetna suggests the navigational servitude does not necessarily mean the United States' physical appropriation of property associated with the water subject to the servitude will not constitute a compensable taking.[47] *Nollan* indicates a government may constitutionally deny a license, but the government may not condition a license on the surrender of the licensee's property right without just compensation.[48] These cases seriously undermine the reasoning followed by the Court in *Appalachian Electric* in upholding the recapture provision.

A. Kaiser Aetna v. United States

In *Kaiser Aetna*, the defendants owned a Hawaiian fish pond.[49] The pond was not navigable, and the Army Corps of Engineers told the plaintiffs they did not need a permit to improve the pond.[50] The defendants then dredged and filled the pond, created a marina, and attached the marina to a bay.[51] By virtue of these improvements, the defendants made the pond a part of the navigable waters.[52] The Army Corps of Engineers then sought to compel the defendants to permit public access to the marina.[53] Because the water was now controlled by the government under its navigational servitude, the Army Corps argued it had the right to impose public access.[54]

The Supreme Court held the requirement to permit public access could not be enforced absent compensation for a taking of the defendants' property.[55] The navigational servitude, the Court stated, does not create a blanket exception to the takings clause whenever Congress exercises commerce clause authority to promote navigation.[56] The Army Corps could regulate the pond now that it was navigable due to the servitude, but it could not order the defendants to give up a fundamental property right.[57]

According to the Court in *Kaiser Aetna*, the existence of the navigational servitude simply means the court must consider the important public

47. Kaiser Aetna v. United States, 444 U.S. 164, 179-80 (1984).
48. Nollan v. California Coastal Comm'n, 483 U.S. 825, 841-42 (1987).
49. Kaiser Aetna v. United States, 444 U.S. at 167.
50. *Id.*
51. *Id.*
52. *Id.*
53. *Id.* at 168.
54. *Id.*
55. *Id.* at 180.
56. *Id.* at 172.
57. *Id.* at 172-73.

interest in the flow of interstate waters when deciding whether a taking has occurred.[58] Thus, for example, in an earlier case, the Court found running water in a great navigable stream is not capable of private ownership.[59]

The Court also conceded precedent had established the elements of compensation that the government must pay when condemning fast lands riparian to a navigable stream.[60] The Court further admitted "the strict logic" of the more recent cases regarding the liability of the government to compensate for loss of riparian access "if carried to its ultimate conclusion, might completely swallow up any private claim for 'just compensation' under the Fifth Amendment even in a situation as different from the riparian condemnation cases as this one."[61]

The Court, however, stated these fast land cases only show the government is not required to compensate landowners for certain elements of damage when it acquires fast lands "to improve navigation."[62] The Court rationalized the navigational servitude "gives rise to an authority in the Government to assure that such streams retain their capacity to serve as continuous highways for the purpose of navigation in interstate commerce."[63] Additionally, the Court noted precedent had never required the government to pay landowners for fast lands acquired by the government.[64]

The Court held the Army Corps' attempt to create a public right of access went beyond ordinary regulation or improvement for navigation.[65] Before the defendants improved the pond, it had not been a great navigable stream previously recognized as incapable of private ownership. Instead, the pond had been private property, similar to fast land. The Court reasoned the government could have refused permission to dredge the pond if the dredging impaired navigation, or could have conditioned permission to dredge on measures the government "deemed appropriate for the promotion of navigation."[66] It could not, however, take a fundamental property right—the right to exclude others—without paying just compensation.[67]

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58. *Id.* at 175.

59. *Id.* (citing United States v. Chandler-Dunbar Water Power Co., 229 U.S. 53 (1913) (party who built project on river under revocable permit had no compensable interest in water power after permit was revoked)).

60. *Id.* at 177 (stating the "shifting back and forth of the Court in this area until the most recent decisions bears the sound of 'old, unhappy, far-off things, and battles long ago'"). For a more detailed discussion of the Supreme Court's finding that the hydroelectric power value of fast lands need not be considered when computing the just compensation for the appropriation of such land, see *infra* section IV, subsection B.

61. Kaiser Aetna v. United States, 444 U.S. 164, 177 (1984).

62. *Id.*

63. *Id.*

64. *Id.*

65. *Id.* at 178.

66. *Id.*

67. *Id.* at 179-80.

The Court's reasoning in *Kaiser Aetna* suggests the government's navigational servitude in the water associated with a project does not negate the government's obligation to pay just compensation if it physically appropriates private property adjacent to or in the water. Equally important, the Court linked the obligation to pay just compensation with the government's purpose in exercising its navigational servitude. For example, complete denial of a permit to improve waters is sanctioned if the denial is "deemed appropriate for the promotion of navigation."[68] Similarly, the government need not pay for the value of fast land associated with access to navigable water if the government is acting "to improve navigation."[69] On the other hand, it follows the government would have to pay for the additional riparian value if its condemnation is *not* based on the promotion of navigation, but is simply an attempt to avoid the dictates of the takings clause. This view is supported in *Nollan*.[70]

B. Nollan v. California Coastal Commission

In *Nollan*, the plaintiff wanted to build a house on his beach lot.[71] The California Coastal Commission granted the plaintiff a building permit, conditioned on the surrender of a public access easement over his land.[72] The Supreme Court struck down this condition as an unconstitutional taking without just compensation.[73]

In support of the condition, the Coastal Commission argued it constituted a legitimate police power regulation, not a taking.[74] The Coastal Commission contended the easement protected visual access to the beach, lowered psychological barriers to such access, and helped offset the additional congestion on the beach that would be caused by the construction of the new house.[75]

The Court rejected this argument, stating a sufficient nexus between the easement condition and the purposes proffered for imposing the condition did not exist.[76] A regulation must substantially advance a legitimate governmental interest to avoid constituting a taking.[77] The Coastal Commission's easement condition did not meet this test.[78]

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68. *Id.* at 179.
69. *Id.* at 188.
70. Nollan v. California Coastal Comm'n, 483 U.S. 825, 831 (1987).
71. *Id.* at 828.
72. *Id.*
73. *Id.* at 842 (if the Commission "wants an easement across the Nollans' property, it must pay for it").
74. *Id.* at 836.
75. *Id.* at 835.
76. *Id.* at 837.
77. *Id.* at 834 (citing Agins v. Tiburon, 447 U.S. 255, 260 (1980)).
78. *Id.* at 836-37.

The Court stated that if the Coastal Commission had simply taken the easement rather than conditioning the permit on the grant of the easement then the action would have constituted a taking requiring just compensation.[79] The Coastal Commission asserted that the purposes for the easement condition could probably justify total denial of the permit.[80] The Court found the imposition of the easement condition on the plaintiff's permit was, however, unconstitutional because the condition had no nexus with the development of the property: "In short, unless the permit condition serves the same governmental purpose as the development ban, the building restriction is not a valid regulation of land use but 'an out-and-out plan of extortion.'"[81]

Thus, under *Nollan*, even if the government can deny development, it cannot condition the development of property on a restriction that fails to substantially advance a legitimate state interest, but rather subterfuges an attempted taking without compensation.

The potential application of the Supreme Court's reasoning in *Nollan* and *Kaiser Aetna* to the recapture provision is clear. An owner-licensee of a hydroelectric project could argue, based on these two decisions, the net investment compensation condition to its permit to develop a water project is not a legitimate regulation, rather it is an attempt to take property without just compensation. The purpose of the condition, the owner-licensee could argue, is not to further the legitimate state interest of promotion of navigation, but is out-and-out extortion.[82]

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79. *Id.* at 831.

80. *Id.* at 835-36.

81. *Id.* at 837 (citing J.E.D. Assocs., Inc. v. Atkinson, 121 N.H. 581, 584, 432 A.2d 12, 14-15 (1981)). In *J.E.D. Associates*, the New Hampshire Supreme Court struck down a zoning regulation requiring a developer to deed seven and one-half percent of the total land area of its subdivision to the town. *Id.* at 15. The court stated, "This appears to us to be an out-and-out plan of extortion whereby developers are required to pay for the privilege of using their land for valid and reasonable purposes even though it satisfied all other requirements of the town's zoning and subdivision regulations." J.E.D. Assocs., Inc. v. Atkinson, 121 N.H. at ___, 432 A.2d at 14.

In support of its holding in *Nollan* the Court also cited *Loretto v. Teleprompter Manhattan CATV Corp.* Nollan v. California Coastal Comm'n, 483 U.S. 825, 831 (1987). In *Loretto* the Court noted "a landlord's ability to rent his property may not be conditioned on his forfeiting the right to compensation for a physical occupation." Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419, 439 n.17 (1982).

82. A recent district court case illustrates the impact of *Kaiser Aetna* and *Nollan*. *See* Boone v. United States, 725 F. Supp. 1509 (D. Haw. 1989). In *Boone*, as in *Kaiser Aetna*, the Army Corps of Engineers attempted to compel the owner of a man-made lagoon to permit public access to the lagoon. *Id.* at 1510-11; Kaiser Aetna v. United States, 444 U.S. 164, 170 (1984). As in *Kaiser Aetna*, the court rejected the Army Corps' claim. Boone v. United States, 725 F. Supp. at 1522; Kaiser Aetna v. United States, 444 U.S. at 172-73.

The government tried to distinguish *Kaiser Aetna* from the situation presented in *Boone* based on the fact the body of water improved by the landowner was navigable before the im-

IV. IN DEFENSE OF *APPALACHIAN ELECTRIC*

The Supreme Court's decisions in *Kaiser Aetna* and *Nollan* strongly suggest the constitutionality of the net investment compensation formula of the recapture provision is open to question, despite the ruling in *Appalachian Electric*. It is not certain, however, the recapture provision will ultimately be struck down. On the contrary, various arguments can be raised to uphold the provision.

A. *The Checkered History of the Doctrine of Unconstitutional Conditions*

One troubling sign for licensees interested in challenging the recapture provision is that the reasoning in *Nollan* for striking down the Coastal Commission's easement condition is not new to constitutional jurisprudence.[83] The doctrine proposed a government cannot grant a privilege on the condition the beneficiary surrender a constitutional right, even if the government may otherwise withhold that privilege altogether.[84] Commentators differ as to when the Supreme Court recognized this "unconstitutional conditions" doctrine.[85] But without doubt, the doctrine

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provements, and because the Army Corps required a permit to build before allowing the owner to make the improvement. Boone v. United States, 725 F. Supp. at 1522.

The district court found these factors nondeterminative. First, the court noted that in *Kaiser Aetna* the Supreme Court had stated the Army Corps could condition approval of a dredging permit on an agreement to comply with measures the Army Corps deems appropriate *for the promotion of navigation*. *Id.* at 1523. *Nollan*, the district court explained, puts an increased burden on the Corps to justify the conditions in its permits. *Id.* The government's burden of proving substantial advancement of a legitimate state interest is especially pertinent, the district court commented, when the condition requires the actual conveyance of property, because such a condition presents a greater risk that the true purpose of the condition is to avoid just compensation, rather than fulfillment of a proper governmental objective. *Id.* (citing Nollan v. California Coastal Comm'n, 483 U.S. at 841). Putting all these factors together, the district court concluded that even if the interest allegedly advanced by the Corps' condition was the improvement of navigation, the public access condition did not substantially advance that interest. *Id.*

83. *See generally* Comment, *supra* note 1, at 1000-01 (noting the Court in *Appalachian Electric* "ignored" the doctrine of unconstitutional conditions). The *Appalachian Electric* Court was obviously well aware of the doctrine, even using the term "unconstitutional conditions" when determining whether the challenge to the recapture condition was ripe. United States v. Appalachian Elec. Power Co., 311 U.S. 377, 421 (1941). *See also infra* notes 85-86 (noting the well-established nature of the unconstitutional condition doctrine prior to 1943).

84. *See* Sullivan, *Unconstitutional Conditions*, 102 HARV. L. REV. 1413, 1415 (1989).

85. Richard Epstein traces the doctrine back to the Court's decisions in Lafayette Insurance Co. v. French, 59 U.S. (18 How.) 404, 407 (1856) (conditions may be imposed "provided they are not repugnant to the Constitution or laws of the United States") and Doyle v. Continental Insurance Co., 94 U.S. 535, 543 (1877) (Bradley, J., dissenting) ("Though a State may have the power, if it sees fit to subject its citizens to the inconvenience, of prohibiting all foreign corporations from transacting business within its jurisdiction, it has no power to im-

was firmly entrenched by the time the Court issued its opinion in *Appalachian Electric*.[86]

So why did the Court in *Appalachian Electric* ignore this doctrine?[87] FERC could argue the Court's failure to discuss the doctrine explicitly should be viewed as an implied finding that the recapture provision withstands analysis under the doctrine. In other words, the recapture provision does "'substantially advance' the legitimate state interest."[88]

The net investment formula was the product of a compromise between legislators who wanted *no* private ownership of water projects and other legislators who argued private ownership was needed because private interests had the financial resources to develop projects and would not do so if projects could be taken at will.[89] Arguably the compromise between these two views, reflected in the net investment formula, reflects a substantial advancement of a state interest. The conditioning of the privilege of developing a water project on a less than full value compensation for the project promotes the development of cost-effective water power.

Based on the language of the recapture provision itself, however, the interest being furthered under the investment formula is not the development of cost-effective water power. On the contrary, inclusion of the net investment formula undermines private development of water power by threatening the potential developer with a less than fair market return on its investment.

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pose unconstitutional conditions upon their doing so."). Epstein, *Unconstitutional Conditions, State Power and the Limits of Consent*, 102 HARV. L. REV. 4, 6-7 n.7 (1988). Kathleen Sullivan suggests the Supreme Court fashioned the doctrine in the *Lochner* era. Sullivan, *supra* note 84, at 1416. For a discussion by the Court of the doctrine's early history, see Fidelity & Deposit Co. v. Tafoya, 270 U.S. 426 (1926). Traced to its conceptual roots, the doctrine stems from the principle that the government may not, "under the pretext of executing its powers, pass laws for the accomplishment of objects not entrusted to the government"—a concept recognized in 1819. McCulloch v. Maryland, 17 U.S. (4 Wheat.) 315, 422 (1819).

86. The Supreme Court's seminal recognition of this doctrine is found in Frost & Frost Trucking Co. v. Railroad Commission, 271 U.S. 583, 594 (1926). *See* Van Alstyne, *The Demise of the Right-Privilege Distinction in Constitutional Law*, 81 HARV. L. REV. 1439, 1445 (1968); Note, *Unconstitutional Conditions*, 73 HARV. L. REV. 1595, 1596 (1960). Pre-*Appalachian Electric* decisions by the Court invoking the doctrine explicitly or implicitly include Helvering v. Independent Life Insurance Co., 292 U.S. 371 (1934); Coombes v. Getz, 285 U.S. 434 (1932); and National Life Insurance Co. v. United States, 277 U.S. 508 (1928). *See* United States v. Chicago, M., St. P. & Pac. R.R., 282 U.S. 311 (1931) (finding doctrine "settled").

87. *See supra* note 83. The Supreme Court's application of the doctrine has always been checkered. *See* Western S. Life Ins. Co. v. State Bd. of Equalization, 451 U.S. 648, 657-58 (1981) (noting prior cases seem "inconsistent or illogical"); Sullivan, *supra* note 84, at 1416 (remarking the doctrine is "riven with inconsistencies").

88. Nollan v. California Coastal Comm'n, 483 U.S. 825, 834 (1987).

89. Clark-Cowlitz Joint Operating Agency v. FERC, 775 F.2d 366, 377 (D.C. Cir. 1985), *vacated & reh. granted*, 787 F.2d 674 (D.C. Cir. 1986), *rev'd on other grounds*, 826 F.2d 1074 (D.C. Cir. 1987), *cert. denied*, 485 U.S. 913 (1988). See authorities cited *supra* note 1.

The application of the net investment formula must be premised on the federal government's ability to exact a fee for the use of navigable waters. As *Appalachian Electric* emphasizes, the government, not any private property owner, controls the flow of navigable streams.[90] It is not unconstitutional to charge a fee to a private entity for the privilege of using the government-owned property.[91] If navigable waters are viewed as property "owned" by the federal government by virtue of navigational servitude, then the recapture provision should withstand constitutional scrutiny.[92]

B. *The Navigational Servitude*

Some authority exists for the proposition that the federal government's interest in navigable waters is proprietary.[93] The majority view, however,

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90. United States v. Appalachian Elec. Power Co., 311 U.S. 377, 424 (1940).

91. The United States has the rights of an ordinary property owner with respect to the land it owns. Camfield v. United States, 167 U.S. 518, 524 (1897). The government can fix whatever terms it wishes for the use of its property. Light v. United States, 220 U.S. 523, 536 (1911).

92. FERC's defense of its net investment formula must be grounded as a fee for use of the navigable waters as opposed to the submerged land surrounding that water, because that land belongs to the states, not the federal government. *See* Phillips Petroleum Co. v. Mississippi, 484 U.S. 469, 474 (1988); Utah Div. of State Lands v. United States, 482 U.S. 193, 196 (1987); Shively v. Bowlby, 152 U.S. 1, 57-58 (1894); Pollard v. Hagan, 44 U.S. (3 How.) 212, 229 (1845).

Indeed, the Supreme Court has often stated the state's ownership extends to the navigable waters themselves. *See, e.g.*, Port of Seattle v. Oregon & Wash. R.R., 255 U.S. 56, 63 (1920) ("The right of the United States in the navigable waters within the several states is limited to the control thereof for purposes of navigation. Subject to that right [the State of] Washington became, upon its organization as a State, the owner of the navigable waters within its boundaries and of the land under the same."); St. Anthony Falls Water Power Co. v. St. Paul Water Comm'rs, 168 U.S. 349, 359 (1897) (state has "title and jurisdiction . . . over the navigable waters within her boundaries"); Weber v. Board of Harbor Comm'rs, 85 U.S. (18 Wall.) 57, 65 (1873) (under the common law, "title to . . . the arms of the sea . . . is . . . in this country, in the State"); Pollard v. Hagan, 44 U.S. (3 How.) at 229 ("Then to Alabama belong the navigable waters, and soils under them.").

The states, in turn, establish laws regarding riparian rights to which any FERC licensee must adhere. Before the licensee can build its project, it must obtain all necessary local water rights. *Cf.* Shively v. Bowlby, 152 U.S. at 26 ("each State has dealt with the lands under the tide waters . . . according to its own views of justice and policy").

These pronouncements by the Supreme Court declaring the states own navigable waters undermine arguments the federal government's navigational servitude incorporates proprietary characteristics. *See infra* notes 93-96 and accompanying text.

93. For example, in 1865 the Court stated: "Commerce includes navigation.... For this purpose [navigable waters] *are the public property of the nation.*" Gilman v. Philadelphia, 70 U.S. (3 Wall.) 713, 724-25 (1866) (emphasis added). *See also* A. TARLOCK, LAW OF WATER RIGHTS AND RESOURCES § 3.02[1] (1990) (water rights law changed from passive concept of negative community to "active ownership" of water in trust for the public). For an analysis of the navigational servitude that reaches the conclusion the government's interest pursuant to the servitude is proprietary, see Bartke, *The Navigation Servitude and Just Compensation—Struggle for a Doctrine*, 48 OR. L. REV. 1 (1968).

is navigable waters belong either to everyone (*res commun*)[94] or to no one (*res nullius*)[95]—neither the private riparian owner nor the government has a proprietary right in the corpus of the waters.[96]

Based on this proprietary limbo, when the federal government appropriates fast land adjacent to navigable waters, it need not pay for the water value of that land, including its value as a part of a hydroelectric project.[97] The Court begins with the general proposition that, under the takings clause, compensation must be paid for what the private property owner loses rather than for what the government gains.[98] Because the private property owner does not own the navigable waters, it need not be compensated for the value of the flow of the stream itself or for the value of the fast land associated with the riparian location.[99] For example, in 1913, the federal government condemned land adjacent to a canal to improve navigation on the river.[100] In so doing, it revoked the owner's permits, licenses, and authority to build dams and develop water power.[101] The owner sought to include, as a

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94. The Institutes of Justinian provides that running water is common to all by natural law: "Thus, the following things are . . . common to all—the air, *running water*, the sea, and consequently the seashore." J. INST. 2.1.1 (emphasis added). *See* Johnson, *Water Pollution and the Public Trust Doctrine*, 19 ENVTL. L. 485, 491 n.26 (1989); Note, Phillips Petroleum Co. v. Mississippi *and the Public Trust Doctrine: Strengthening Sovereign Interest in Tidal Property*, 38 CATH. U.L. REV. 571, 574 n.31 (1989).

95. *See* J. KERWIN, *supra* note 1, at 76 (corpus of running water belongs to neither state nor citizen).

96. *But see* cases cited *supra* note 92 (decisions regarding state ownership). If any sovereign holds ownership interests in navigable waters within the United States, it appears that body is the state, not the federal government. *See also* United States v. Fuller, 409 U.S. 488, 492 (1973) (Court contrasted land "owned outright" by the federal government with navigable waters merely subject to the navigational servitude). Even the Supreme Court cases cited as support for the proprietary view do not blanketly profess the federal government "owns" navigable waters. For example, in *Gilman* the Court stated: "Commerce includes navigation. ... *For this purpose* [navigable waters] are the public property of the nation." Gilman v. Philadelphia, 70 U.S. (3 Wall.) at 724-25 (emphasis added).

97. Indeed, one technical definition for the navigational servitude is "the privilege to appropriate without compensation which attaches to the exercise of the 'power of the government to control and regulate navigable waters in the interest of commerce.'" United States v. Virginia Elec. & Power Co., 365 U.S. 624, 627-28 (1961) (citing United States v. Commodore Park, 324 U.S. 386, 390 (1945)).

98. United States *ex rel.* Tenn. Valley Auth. v. Powelson, 319 U.S. 266, 281 (1943); United States v. Miller, 317 U.S. 369, 375 (1943); United States v. Chandler-Dunbar Water Power Co., 229 U.S. 53, 76 (1913); Boston Chamber of Commerce v. City of Boston, 217 U.S. 189, 195 (1910); *cf.* United States v. Fuller, 409 U.S. 488 (1973); United States v. Cors, 337 U.S. 325, 334 (1949) (government need not compensate for value it creates).

99. United States v. Chandler-Dunbar Water Power Co., 229 U.S. at 76. The Court relied on *Chandler-Dunbar* when it upheld the recapture provision in *Appalachian Electric*. United States v. Appalachian Elec. Power Co., 311 U.S. 377, 424 (1940). *See also* A. TARLOCK, *supra* note 93, § 9.04[2][a] ("The fifth and fourteenth amendments guarantee of just compensation do not apply because no property rights in navigable waters exist.").

100. United States v. Chandler-Dunbar Water Power Co., 229 U.S. at 66-67.

101. *Id.* at 68-69.

part of its compensation for the takeover of its property, the value of the power of the river in excess of the supposed requirements of navigation.[102] The Court rejected this argument, finding the owner was only entitled to compensation for the fast land.[103] It reasoned the owner had not been deprived of any private property right in water power.[104]

Forty years later, Congress condemned land adjoining the Savannah River for flood control and other purposes.[105] The landowners, utilities which had purchased the property for its power project potential, sought the value of the land as a prospective site for hydroelectric operations.[106] In a five to four decision, the Supreme Court rejected this argument, relying on the Court's earlier decision in 1913.[107]

Many other decisions could be cited for the proposition that water value is excluded when calculating the appropriate compensation for a federal taking of fast land adjacent to navigable waters.[108] The owner is entitled to nothing for water power itself, and the compensated value of its fast land excludes the value associated with that water power.[109]

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102. *Id.* at 61.

103. *Id.* at 72.

104. *Id.* The fact the federal government could then profit by using the surplus water power incidentally produced by its construction of dams and locks in aid of navigation was irrelevant: "If the primary purpose is legitimate, we can see no sound objection to leasing any excess of power over the needs of the Government." *Id.* at 73 (citing Kaukauna Water Power Co. v. Green Bay & Miss. Canal Co., 142 U.S. 254, 273 (1891) (holding is similar with respect to the State of Wisconsin's ability to profit from the sale of water power produced as an incident of its right to construct a navigational improvement)).

Technically, the Supreme Court has continued to base the federal government's ability to control and exploit the water power of navigable waters on the fiction that such water power is being created as an incident to improving navigation on the waters. Even the Tennessee Valley Authority was upheld on this basis (combined with the federal government's war powers). Ashwander v. Tennessee Valley Auth., 297 U.S. 288, 328-30 (1936).

105. United States v. Twin City Power Co., 350 U.S. 222, 223 (1956). Like the Tennessee Valley Authority, the purposes of the federal project were ostensibly multiple, including flood control and navigation, but also included a major hydroelectric project based on the power to be produced "incident" to these other purposes. *See id.* at 224.

106. *Id.* at 225.

107. *Id.* at 226-28. The Court, in an opinion written by Justice Douglas, stated the owners sought a value in the flow of the stream which "inheres" in the federal government's servitude, and which the government "can grant or withhold as it chooses." *Id.* at 225. The four dissenting Justices distinguished *Chandler-Dunbar* on the fact the owner was seeking compensation for the loss of the use of the navigable waters that was purely speculative; unlike in *Twin City*, the owner in *Chandler-Dunbar* was not seeking the value of its fast land due to its "favorable riparian location . . . for assured uses." *Id.* at 245 (Burton, J., dissenting).

108. *See, e.g.*, United States v. Rands, 389 U.S. 121, 123-24 (1967); United States v. Virginia Elec. & Power Co., 365 U.S. 624, 629 (1961); United States v. Twin City Power Co., 350 U.S. at 222.

109. *See, e.g.*, United States v. Fuller, 409 U.S. 488, 491 (1973) (stating a long line of cases regarding the navigational servitude "evidences a continuing refusal to include, as an element of value in compensating for fast lands that are taken, any benefits conferred by access to such benefits as a potential portsite or a potential hydro-electric site."); United States v.

Based on this well-established rule, FERC could argue the net investment formula effectively awards a licensee *greater* compensation than constitutionally required under the takings clause. While some equipment, such as an electric turbine and a transmission line, has value outside its application in a hydroelectric project, the bulk of useful property in a project, such as a dam, has little value outside its application to the flow of water. This value, even including fifty years of appreciation, could easily amount to less than the licensee's initial costs in purchasing and constructing the property. Under this reasoning, a licensee should be pleased to receive its net investment at the end of its license term, and should fight to preserve inclusion of the formula in the Federal Power Act.

C. *Reasonable Investment-Backed Expectations*

As additional support for the constitutionality of a compensation formula less than or equal to net investment, FERC could point to the licensee's lack of expectation in receiving any greater amount. One important question generally considered in determining just compensation concerns the property owner's reasonable investment-backed expectations: Did the owner have any reason to believe it would be compensated for its loss?[110] FERC could argue a FERC licensee could have no such reasonable belief beyond recouping its net investment.

The Supreme Court has long recognized just-compensation rules applicable in other situations cannot always be transposed directly to appropriations involving the navigational servitude.[111] Therefore, a riparian owner is put on notice from the beginning that the general rules for compensation may not apply. Although the fair market value measure is the general rule, the Court has also indicated this measure is neither exclusive nor absolute; instead, the Court's ultimate criterion has always been basic fairness.[112]

Rands, 389 U.S. at 124-25 (1967) (government appropriated land along Columbia River for lock and dam project to develop navigation on the river; proper to exclude value of fast land as a port site in computing landowner's compensation).

110. *See, e.g.*, Penn Cent. Transp. Co. v. New York City, 438 U.S. 104, 124-25 (1978). In citing this factor as one weighed in determining whether property has been taken, the *Penn Central* Court referred to *Chandler-Dunbar* and United States v. Willow River Power Co., 324 U.S. 499 (1945). In *Willow River*, the Court held a riparian owner had no property interest in the maintenance of high-water level of a river because the government's navigational servitude allowed it to alter that level. *Id.* at 509.

111. *See* United States v. Cherokee Nation, 480 U.S. 700, 704 (1987) ("there can be no doubt that '[t]he Commerce Clause confers a unique position upon the Government in connection with navigable waters'") (quoting United States v. Rands, 389 U.S. at 122).

112. United States v. Fuller, 409 U.S. at 490; United States v. Virginia Elec. & Power Co., 365 U.S. at 631 (1961).

Given the longstanding precedent excluding water power value from compensation, the seventy-year existence of the recapture provision, and the almost fifty years during which *Appalachian Electric* has stood unchallenged, FERC could claim no licensee has any reasonable expectation in compensation beyond the net investment measure; therefore, it is fair to limit compensation to that measure.[113] This conclusion is also supported by the fact FERC licensees are often public utilities. FERC could argue these utilities have no reasonable expectation in obtaining anything beyond a just return on their investments.[114] After fifty years of licensed operations, utility shareholders will have obtained fifty years of fair return. Because the shareholders are entitled to no more under this reasoning, *no* additional compensation award is constitutionally required.[115] Thus, licensees should be grateful the government goes beyond the Constitution's minimum requirements by awarding net investment compensation.

D. *Section 15 of the Federal Water Power Act*

Section 15 of the Federal Water Power Act imposes the same net investment formula for takeover as does the recapture provision; however, it does so in the context of transfer of the project property to a new licensee, not

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113. *See* United States v. Kansas City Life Ins. Co., 339 U.S. 799, 808 (1950) ("ample notice" has been given to riparian property owners that their property is "subject to a dominant public interest"); A. TARLOCK, *supra* note 93, § 9.04[2][a] ("The best explanation for the special no compensation rule of the navigation servitude is that the long history of the recognition and protection of public rights of navigation, even against the sovereign, has put all riparians on notice that private claims inconsistent with the exercise of the servitude will not be recognized.") (citation omitted); *see also* Michelman, *Property, Utility, and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law*, 80 HARV. L. REV. 1165, 1240-41 n.128 (1967).

This Article does not discuss the difficult question whether a licensee who was subjected to a condition in its license accepting the net investment formula for its compensation on takeover is estopped from complaining at the end of the term of the license if that condition is exercised.

114. *See* Duquesne Light Co. v. Barasch, 488 U.S. 299, 314-15 (1989); FPC v. Hope Natural Gas Co., 320 U.S. 591, 602 (1944). Under *Duquesne* and *Hope*, to avoid constituting confiscation, "the total effect of a rate order cannot be ... unjust and unreasonable." FPC v. Hope Natural Gas Co., 320 U.S. at 602. Under this test, the investor's return "should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital." *Id.* at 603 (citing Missouri *ex rel.* S.W. Bell Tel. Co. v. Public Serv. Comm'n, 262 U.S. 276, 291 (Brandeis, J., concurring)). Typically, the investor base on which the ratesetter determines an appropriate return is either the property used and useful in providing power, or the amount prudently invested in the utility. *See* Note, *Takings Clause Analysis of Utility Ratemaking Decisions: Measuring* Hope's *Investor Interest Factor*, 58 FORDHAM L. REV. 427, 438 (1989).

115. Indeed, the amortization reserves set up under 16 U.S.C. § 803(d) (1988) are designed to ensure that FERC does not have to pay anything at the time of takeover. *See supra* notes 13, 25.

to the government.[116] FERC could argue that whether it retains appropriated project property or transfers ownership of the property to a new licensee, the analysis of the constitutionality of the net investment formula should remain the same.

The takings clause requires the power of eminent domain be exercised for a "public use."[117] If that power is not exercised for such a use, then the property cannot be appropriated, with or without compensation.[118] The "use" of the property transferred under section 15 is as a water project. Such a use is public and legitimate.[119] Under the takings clause, the term "public use" refers to the purpose to which the property is put, not the identity of the operator.[120] Therefore, it is irrelevant to the takings clause analysis whether, in advancing the goal of water development in the public interest, the government itself owns and operates the project or transfers the project property to another private entity to own and operate the project.[121]

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116. 16 U.S.C. § 808 (1988); *see supra* text accompanying note 14.

117. U.S. CONST. amend. V, cl. 4.

118. *See* Hawaii Hous. Auth. v. Midkiff, 467 U.S. 229, 239-43 (1984); Berman v. Parker, 348 U.S. 26, 32-33 (1954).

119. Mount Vernon-Woodberry Cotton Duck Co. v. Alabama Interstate Power Co., 240 U.S. 30, 32 (1916) (condemnation of land to manufacture, supply, and sell to the public power produced by water is a public purpose). Additionally, under 16 U.S.C. § 797(e) (1988), FERC must determine whether a license is in the public interest. To make this determination, FERC looks at factors such as future power demand and supply, alternate sources of power, and wilderness preservation. *See* Udall v. FPC, 387 U.S. 428 (1967); United States *ex rel.* Chapman v. FPC, 345 U.S. 153 (1953). If the project initially met this standard, as it had to before it was licensed, then the public interest is presumably advanced whoever happens to be operating the project. United States *ex rel.* Chapman v. FPC, 345 U.S. at 168-73.

120. Lac Courte Oreilles Band of Lake Superior Chippewa Indians v. FPC, 510 F.2d 198, 207 n.36 (1975).

121. Even if FERC's decision to transfer a license were not based on the conclusion that the new licensee would be better able to meet the needs of the public, but were rather based on a desire to redistribute control over hydroelectric facilities, that purpose would probably also withstand scrutiny under the "public use" requirement of the takings clause. *See, e.g.*, Hawaii Hous. Auth. v. Midkiff, 467 U.S. at 240 (upholding Hawaii Land Reform Act, which transferred private land from one group of private owners to another group of private owners, with goal to redistribute the land from a small group of wealthy owners to a larger group of citizens; judicial review of what constitutes a public use under the takings clause is "extremely narrow") (citing Berman v. Parker, 348 U.S. 26, 32 (1954) (upholding exercise of eminent domain to redevelop slum areas and sell or lease property to private interests)).

Thus, while the Court has repeatedly stated one person's property may not be taken for the benefit of another private person without a justifying public purpose (even if compensation is paid), see Thompson v. Consolidated Gas Corp., 300 U.S. 55, 80 (1937), the Supreme Court rarely finds a purpose not public. The fact the property is transferred to a private interest is not determinative: "[W]hat in its immediate aspect [is] only a private transaction may . . . be raised by its class or character to a public affair." Hawaii Hous. Auth. v. Midkiff, 467 U.S. at 244 (citing Block v. Hirsh, 256 U.S. 135, 155 (1921) (upholding rent control)). *But see* Kaukauna Water Power v. Green Bay & Miss. Canal Co., 142 U.S. 254, 273 (1891) ("it is probably true that it is beyond the competency of the State to appropriate to itself the property of individuals for the sole purpose of creating a water power to be leased for manufacturing purposes" because such con-

V. RESPONSE TO DEFENSE

Each of the arguments set forth above in defense of the recapture provision's net investment formula can be refuted.

A. *The Navigational Servitude Does Not Permit FERC to Exclude the Water Power Value of Project Property in Calculating Just Compensation*

The primary theme of the arguments set forth in section IV is no compensation beyond net investment is constitutionally required because long-settled precedent establishes that navigational servitude precludes a licensee from reasonably anticipating it will obtain the water power value of appropriated property. The assumptions on which this defense is based, however, can be challenged.

First, the case law on the effect of the navigational servitude on just compensation is not a model of unswerving clarity.[122] For example, in 1893, the Supreme Court held the United States' condemnation of a utility's lock and dam entitled the utility to the "whole" value of its property.[123] Whole value was measured "necessarily" by the income it obtained for exacting tolls for passage through the lock.[124] The Court expressly rejected a measure of compensation limited by the owner's investment costs.[125] This case has never been expressly overruled; instead, the Court has attempted, unconvincingly, to distinguish the holding.[126] Similarly, in 1913, the

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duct would be the appropriation of private property for the benefit of another private person, and not a constitutional exercise of eminent domain).

122. *See supra* note 60; *see also* A. TARLOCK, *supra* note 93, § 9.04[2][a] (historical basis for exclusion of water power value "not overwhelming").

123. Monongahela Navigation Co. v. United States, 148 U.S. 312, 329 (1893).

124. *Id.*

125. *Id.* at 328 ("The value, therefore, is not determined by the mere cost of construction, but more by what the completed structure brings in the way of earnings to its owner"). To measure compensation by the mere cost of building project equipment, the Court stated, would deprive the owner of the value of its franchise to operate the project, without compensating for that loss. *Id.* at 329.

126. For example, in distinguishing *Monongahela* the Court has stated the decision rests primarily on estoppel (Congress had impliedly invited the owner to build the lock and dam). *See, e.g.*, Omnia Commercial Co. v. United States, 261 U.S. 502, 513-14 (1923); United States v. Rands, 389 U.S. 121, 126 (1967). This concept, however, is reflected in *Monongahela* in one paragraph of a twenty-one page opinion. Monongahela Navigation Co. v. United States, 148 U.S. at 334-35.

In United States *ex rel.* Tenn. Valley Auth. v. Powelson, 319 U.S. 266, 282 n.12 (1943), aside from estoppel, the Court noted two other distinguishing factors: (1) the State had granted the property owner a franchise; and (2) the United States in *Monongahela* had appropriated the use of the lock and dam (versus precluding the owner from developing unexploited water power). Here, of course, when the recapture provision is used, the United States *is* appropriating the use of privately built property, and the licensee is very often a franchisee. Ironically,

Supreme Court awarded an owner of a lock and canal the value of that property because of its strategic location.[127] The Court's later attempts to distinguish its ruling have been less than satisfactory.[128]

Other cases confirm inconsistency is the norm in the computation of just compensation for property affected by the navigational servitude.[129] Even after *Appalachian Electric*, the Court continues to struggle with the adoption of consistent compensation rules when navigational servitude is implicated.[130]

The Court cannot agree on a general rule governing the effect of the navigational servitude on compensation for the same reason FERC cannot rely on the navigational servitude as a remedy to its compensation obligations. The underlying reason is that a policy for reducing compensation based on the servitude is neither logical nor compelling.[131] A sensible reason to treat property interests in navigable waters differently from land

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the Court cited *Monongahela* with approval in *Appalachian Electric*. United States v. Appalachian Elec. Power Co., 311 U.S. 377, 427 n.89 (1940) (It is the Court, not Congress, which determines what compensation is just).

127. United States v. Chandler-Dunbar Water Power Co., 229 U.S. 53, 77-78 (1913). But the Court also held the owner was not entitled to compensation for the loss of water power per se. *Id.* at 76. In the words of one commentator, the case created "an ambiguity which has not been resolved completely even today." Bartke, *supra* note 93, at 12.

128. In United States v. Twin City Power Co., 350 U.S. 222, 226 (1956), the Court speculated it may have been influenced in *Chandler-Dunbar* by the fact the lock and dam at issue in *Chandler-Dunbar* had been wholly consistent with the navigational servitude, and, in fact, aided navigation. In *United States v. Rands* the Court stated that part of the holding in *Chandler-Dunbar* awarding compensation for the lock and dam was confined to its "special facts," and, if inconsistent with *Twin City*, did not survive the latter decision. United States v. Rands, 319 U.S. 121, 127 (1967).

129. For example, in United States v. River Rouge Improvement Co., 269 U.S. 411 (1926), the Court was confronted with the flipside of the situation found in *Chandler-Dunbar*. In *River Rouge*, the government condemned fast lands to build a navigational improvement and requested a jury instruction reducing the surrounding owners' compensation for the appropriated land based on the increased value their remaining land would have due to its proximity to the improvement. *Id.* at 414-15. The district court rejected this argument, based on the government's absolute control over the navigational servitude—the government could remove the benefit whenever it chose. *Id.* at 417. The Supreme Court reversed, approving the instruction, citing Port of Seattle v. Oregon & Wash. R.R., 255 U.S. 56 (1921) for the proposition that the servitude is limited to control over navigable waters for the purposes of navigation. *Id.* at 419, 422.

Read together, *Chandler-Dunbar* and *River Rouge* paradoxically stand for the proposition that water power value is not taken into account when calculating a private property owner's loss, but is considered when calculating its gain to offset its loss.

130. For example, in United States v. Virginia Elec. & Power Co., 365 U.S. 624 (1961), the Supreme Court awarded compensation to a property owner who only owned a flowage easement over land being appropriated by the United States. *Id.* at 631. Logically, under the rule excluding compensation for water power, the owner should have received nothing. *See* Michelman, *supra* note 113, at 1230.

131. *See* Dunham, Griggs v. Allegheny County *in Perspective: Thirty Years of Supreme Court Expropriation Law*, 1962 SUP. CT. REV. 63, 104-05.

interests does not exist.[132] Even if there were good reason, the navigational servitude is what its name suggests—the power to preclude others from behaving in a certain manner. It is, as *Kaiser Aetna* shows, not a *carte blanche* for appropriating private property.[133] The servitude is "narrower in scope" than the government's broad, affirmative powers under the commerce clause.[134] By definition, servitude does not allow its owner to "do" anything.[135] Servitude may permit the government to destroy a liberty a private property owner may otherwise possess, and even help define the type of public use for which property may be appropriated. It does not, however, simultaneously transfer any private property right to the government or excuse the United States from its constitutional duty to provide just compensation for the property.

These inherent weaknesses in the rationale for having the servitude and using it to reduce compensation, have led the Court to at least apply that rationale narrowly. *Kaiser Aetna* was not the first case to suggest the case law reducing compensation for fast land based on the navigational servitude could not be extended outside that limited context, even if it were logical to do so.[136] In a 1973 case, the Court repeated the view that water power value may be excluded when the government condemns fast land, based on the navigational servitude.[137] Nevertheless, the Court stated, this did not mean the principle could be carried to its "logical extreme."[138] The Court contrasted the interest at issue in the case before it, a revocable permit to use land owned "outright" by the government, with "the value added to property by a completed public works project, *for which the Government must pay.*"[139] Language in other decisions hints less strongly that the distinction between unexploited water power and constructed project property could influence the Court's determination of whether full compensation must be awarded.[140]

Following this caveat, the navigational servitude seems a highly untenable rationale for the net investment formula of the recapture provision.

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132. *See* Sax, *Takings and the Police Power*, 74 YALE L.J. 36, 52-53 (1964) ("Why it is more inconceivable [that one should obtain a proprietary interest in navigable waters] than that one should obtain a proprietary interest in land, good as against a subsequent state or federal road building plan, or more inconceivable than that one should obtain a proprietary interest in petroleum, or any other precious resource, has not been explained to the satisfaction of this observer.").

133. *See also* United States v. Kansas City Life Ins. Co., 339 U.S. 799, 808 (1950) (when the government exercises its navigational servitude it "is exercising its paramount power in the interests of navigation, rather than taking the private property of anyone").

134. *Id.*

135. *Id.*; *see* Michelman, *supra* note 113, at 1186-87 n.45 (distinguishing affirmative easements from negative servitudes).

136. *See supra* note 60 and accompanying text.

137. United States v. Fuller, 409 U.S. 488 (1973).

138. *Id.* at 493.

139. *Id.* (emphasis added).

140. *See, e.g.*, *supra* notes 126, 128.

The government's right to use the servitude as a basis for diminishing compensation must, due to the scope of the servitude, relate to regulation of the uses of navigable waters. The recapture provision, however, is predicated on the mere transfer of ownership. It is triggered by a change in the user, not the use. Because the subsequent use of the appropriated property is not altered, the servitude should not have any affect on decisions made pursuant to the provision. In short, it is not self-evident the navigational servitude cases, on which FERC would have to rely to support its denial of the water-associated value of project equipment under the recapture provision, apply, either by virtue of the language of the cases or the logic behind them.

Other factors also undermine an argument based on the licensee's reasonable expectations. Generally, the "reasonable investment-backed expectations" to which the Court refers when considering takings issues include the expectation a property owner will be permitted to continue to use the property.[141] One could argue the limited term of a FERC license strips the licensee of any reasonable expectancy of a continuation of that license, but it does not follow the licensee should expect its property to be taken for less than the constitutionally required measure after the expiration of that license.

Even the property of a regulated utility is still property. A utility can expect the profits it obtains through dedication of that property to a public use will be regulated, but no case law supports the general proposition that utilities are entitled to less compensation for seized property than are other types of owners. The identity of a property owner should not affect the compensation it receives when its property is appropriated.

Finally, even if a licensee anticipates it is only entitled to its net investment once FERC took its property, it does not follow that such anticipation should end the constitutional inquiry. Unconstitutional conduct does not become constitutional through mere duration. Indeed, the deliberateness of conduct effecting a taking can support the need for compensation for that conduct.[142]

B. *Appropriation of Project Property Requires Full and Just Compensation*

Stripped of reliance on the navigational servitude, the reduction in compensation permitted under the recapture provision is devoid of support. Government takeover of project property physically appropriates that prop-

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141. *See, e.g.*, Penn Cent. Transp. Co. v. New York City, 438 U.S. 104, 136, 138 n.36 (1978) ("primary expectation" of property owner is continuation of a "present ability to use the [property] for its intended purposes and in a gainful fashion").

142. *See* Michelman, *supra* note 113, at 1216.

erty and is, without question, a taking.[143] Moreover, the purpose of the takeover is not to stop a detrimental use, but is simply intended to change the owner of the property. Thus, FERC cannot rely on a "nuisance" exception or a harm/benefit distinction for denying full compensation.[144]

Phrased differently, the purpose of the net investment formula is not to preserve a natural resource. FERC's takeover of project property does not reduce exploitation of a resource. It merely changes the identity of the possessor of the property useful for exploitation. Therefore, a determination as to whether navigable waters are subject to a "public trust" has no impact on the question of whether the government should pay less compensation if it takes over private property designed to perpetuate the use to which the private party was dedicating that property.[145]

To summarize, if FERC decided it wanted to clear the waters on which a project was located for navigational purposes, then FERC could decline to renew a license and order the licensee to remove its project equipment from the waters without paying any compensation at all.[146] Such a decision would fall precisely within the proper application of the federal navigational servitude.[147] When the United States is not attempting to clear a project from navigable waters as an obstruction, but seeks to purchase the project equipment, then it should pay for the equipment at the market price, including the water power value of that equipment.

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143. *See* Keystone Bituminous Coal Ass'n v. DeBenedictis, 480 U.S. 470, 488 n.18 (1987) ("the Court has almost invariably found the permanent physical occupation of property constitutes a taking"); Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419, 435 (1982) (when the government permanently physically occupies property, "our cases uniformly have found a taking").

While this bright-line physical occupation rule is typically applied to determine whether a taking has occurred, as opposed to how much compensation must be paid, the Court's rationale in applying the rule suggests no reason to discount compensation for particular types of physical occupations.

144. *See* Connors, *Back to the Future: The "Nuisance Exception" to the Just Compensation Clause*, 19 CAP. U.L. REV. 139 (1990).

145. The theory behind the public trust doctrine is that the general public should have a legal right to participate in governmental decisions relating to the management of natural resources so contemporary environmental concerns can be taken into account when determining the appropriate uses of those resources. *See* Sax, *The Public Trust Doctrine in Natural Resource Law: Effective Judicial Intervention*, 68 MICH. L. REV. 473, 474 (1970). Thus, the application of the doctrine could influence the government's decision whether navigable waters should be dammed at all to exploit their water power. The doctrine should not, however, affect the calculation of compensation for effectively purchasing the equipment to exploit that power.

146. Louisville Bridge Co. v. United States, 242 U.S. 409, 421 (1917); Hannibal Bridge Co. v. United States, 221 U.S. 194, 205 (1911); Union Bridge Co. v. United States, 204 U.S. 364, 385 (1907); United States v. Bellingham Bay Boom Co., 176 U.S. 211, 215 (1900); United States v. Rio Grande Dam & Irrigation Co., 174 U.S. 690, 709 (1899).

147. *See* Gibbons v. Ogden, 22 U.S. (9 Wheat.) 1, 189-90 (1824) (assuming it makes sense to have a navigational servitude at all).

A 1917 Supreme Court obstruction case recognized this distinction when distinguishing an earlier decision in which the Court had required payment for appropriation of a lock and dam.[148] The Court distinguished its earlier decision by stating it:

> was not a case of removing a structure from the river on the ground that it interfered with navigation, but a taking over of a structure and employing it in the public use . . . . In short, there was a clear taking of the property of the company for public use as property, and an attempt at the same time to exclude from consideration an essential element of its value when ascertaining the compensation to be paid.[149]

This language applies today as it did seventy years ago.

C. *Any New Licensee Should Also Be Required to Pay Full Compensation*

The arguments supporting full and just compensation for property and water power value when FERC appropriates a project itself apply equally when FERC transfers project equipment to a new licensee. The new licensee should pay the full market value under section 15 when it, in effect, purchases the former licensee's project equipment. Although the arguments noted above at section IV, subsection D, suggest the converse—if the Court does uphold the net investment formula for FERC takeovers, there are no additional reasons why section 15 would not pass constitutional muster[150]—the inequities that result under current law provide an additional basis for challenging application of the net investment formula when new licensees take the former licensee's project equipment.[151]

When a former or new licensee condemns property for a project by any means other than section 15, it must pay for the power site value of the

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148. Louisville Bridge Co. v. United States, 242 U.S. at 422-23 (distinguishing United States v. Chandler-Dunbar Water Power Co., 229 U.S. 53 (1913)).

149. *Id.* The element of value the government was trying to exclude was the value of the lock and dam owner's franchise to operate. *Id.* at 411. The Supreme Court has since come to distinguish this holding on very different grounds. *See supra* text accompanying notes 123-26.

150. *But see* Johnson, *supra* note 94, at 504 (in a case in which the state takes a water right from prior appropriator A and gives it to B, "a potential takings question arises").

151. A new licensee could argue on its own behalf that any transfer of the license by FERC is supported by equity principles, because the transfer would be based on FERC's finding that the new licensee will better serve the public interest. For example, FERC could decide the former licensee is not complying with the terms of its license, or that, for any reason, the new licensee is better capable of exploiting the navigable waters' power efficiently and with a minimum of environmental harm. This argument, however, does not support selling the former licensee's property for less than full market value. Just because party X, for example, can run a grocery store more efficiently than party Y, it does not follow that X should be permitted to take Y's grocery store property for less than a fair price.

property it condemns.[152] No reason exists why section 15 should insulate a new licensee from the rules of compensation normally applied to it.[153] A licensee of the federal government possesses no navigational servitude.[154] Therefore, any merits of permitting a reduction in compensation based on the navigational servitude when the federal government condemns property do not apply to new licensees.

VI. CONCLUSION

Pursuant to the navigational servitude and the broader authority of the commerce clause, the federal government possesses considerable powers to regulate the use of navigable waters. The Supreme Court, in *Appalachian Electric*, relied on these powers when it upheld the recapture provision of the Federal Power Act.

Together, however, *Nollan* and *Kaiser Aetna* make clear the federal government's legitimate powers to regulate cannot be abused in an effort to take property by subterfuge. When FERC, relying on the recapture provision, conditions a hydroelectric project license on the licensee's surrender of its constitutional right to just compensation, the government is not substantially advancing any legitimate governmental interest. Instead, the condition is designed simply to avoid paying the licensee what is mandated by the takings clause. Such an application of the recapture provision of the Federal Power Act is unconstitutional; therefore, the provision should be struck down and *Appalachian Electric* should be reversed.

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152. Section 21 of the Federal Power Act, 16 U.S.C. § 814 (1988), provides FERC licensees may acquire property needed for a project "by the exercise of the right of eminent domain . . . . The practice and procedure in any action of proceeding for that purpose . . . shall conform as nearly as may be with the practice and procedure in similar action or proceeding in the courts of the State where the property is situated." In Public Util. Dist. No. 1 v. City of Seattle, 382 F.2d 666 (9th Cir. 1967), *cert. denied*, 396 U.S. 803 (1969), the court held a FERC licensee exercising its right of eminent domain under section 21 cannot rely on the navigational servitude as an excuse for not paying full compensation for property, including power site value. *See also* Grand River Dam Auth. v. Grand-Hydro, 335 U.S. 359, 372 (1948) (licensee in state condemnation action must pay power site value); Boom Co. v. Patterson, 98 U.S. 403, 410 (1878) (approved compensation award from private condemnor taking into account special adaptability of three islands in the Mississippi River for construction of a boom).

153. Effectively, however, such a result was permitted in United States v. Rands, 389 U.S. 121 (1967). In *Rands*, the State of Oregon optioned land along the Columbia River owned by the defendant. *Id.* at 122. The State planned to build an industrial park and port, but let the option lapse. *Id.* At that point, the United States condemned the land, which it then sold to the State for less than the original option price. *Id.* The federal government's insulating condemnation of the property enabled the State to purchase the property for less than the price it would have paid if the United States had not acted as a conduit.

154. Public Util. Dist. No. 1 v. City of Seattle, 382 F.2d at 672 ("Seattle as licensee of FPC may not assert the Government's dominant navigational servitude").