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Washington Legal Foundation v. Legal Foundation of Washington:

Much Ado About Nothing *

I. INTRODUCTION

“[N]or shall private property be taken for public use, without just compensation.”¹ This simple declaration has been severely convoluted in the United States Supreme Court’s struggle to develop a logical analysis of the ever-changing arena of property law. Illustrative of the Supreme Court’s latest constitutional property law debate is the controversy surrounding the Interest On Lawyer’s Trust Account (IOLTA) Programs. The American Bar Association (ABA) defines IOLTA as an “innovative funding source.”² It is a simple definition, but right on the money. More specifically, IOLTA is the brain child of federal banking regulations.³ In 1980, 12 U.S.C. § 1832 provided a legal basis for IOLTA programs. IOLTA programs fund legal services for the poor by authorizing attorneys to pool together modest interest accruals from client funds that are too nominal or in trust too briefly to earn net interest. Without IOLTA, interest accruals from these funds would remain with the bank, creating a windfall for the bank. Thus, IOLTA achieves the same objectives of the fabled hero Robin Hood because it takes money out of the hands of the bank and gives it to the poor. Better yet, it does so at no cost to the client. Without the program no net interest would accrue.

Despite IOLTA’s philanthropic purpose, plaintiffs in Washington are challenging as an unconstitutional taking the Washington IOLTA program in *Washington Legal Foundation v. Legal Foundation of Washington*, which will be decided by the United States Supreme Court in the upcoming term. IOLTA’s opponents contend the automatic transfer of interest to IOLTA is unconstitutional and should be terminated. The plaintiffs, represented by the

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* The Board of Editors of the Louisiana Law Review accepted this article for publication before the United States Supreme Court rendered its decision sustaining the IOLTA program. In light of the Court’s rationale, without economic damage there is no taking, the title of the piece, “Much Ado About Nothing,” is certainly prescient.

1. U.S. Const. amend. V.

2. American Bar Association network, *What is IOLTA?*, available at <http://www.abanet.org/legalservices/iolta/ioltback.html> (last visited Feb. 2, 2003).

3. 12 U.S.C. § 1832(a) (2002) (providing that “a depository institution is authorized to permit the owner of a deposit or account on which interest or dividends are paid to make withdrawals by negotiable or transferable instruments for the purpose of making transfers to third parties,” but only “with respect to deposits or accounts which consist solely of funds in which the entire beneficial interest is held by one or more individuals or by an organization which is operated primarily for religious, philanthropic, charitable, educational, political, or other similar purposes and which is not operated for profit . . .”).

Washington Legal Foundation,⁴ argue that though they realize no net interest, the interest is their property nonetheless. Though the validity of IOLTA was hotly debated in *Phillips v. Washington Legal Foundation*,⁵ the Supreme Court only held that the interest in IOLTA was property, refusing to decide whether the program effected an unconstitutional taking. Thus, the battle over IOLTA continues.

Washington Legal Foundation v. Legal Foundation of Washington requires the Court to answer the question it escaped in *Phillips* — whether IOLTA is an unconstitutional taking. To determine IOLTA's constitutionality, the court must first decide whether to apply a *per se* test, generally reserved for physical takings, or a multi-factor test, generally applied to regulatory takings. The Court has already cut a path for analyzing regulatory takings in *Penn Central Transportation Co. v. City of New York*⁶ by establishing a multi-factor test. As this paper will demonstrate, the Court must now apply the *Penn Central* test to pave the way toward a logical analysis of takings of intangible property (i.e., the interest at stake in IOLTA). *Washington Legal Foundation v. Legal Foundation of Washington* provides the Court with the perfect opportunity to establish, once and for all, the proper analysis for assessing takings of intangible property, such as the interest at issue in the constitutional challenge against IOLTA.

The Court's failure to clearly assert the proper standard for analyzing takings of intangible property such as interest or money, as opposed to real property such as land or a building, has unnecessarily clouded the controversy. IOLTA is not a regulatory taking, but it is not a physical taking either. Physical takings have generally been restricted to takings of real property, whereas regulatory takings have been restricted to takings of rights incidental to real property.⁷ The interest placed in IOLTA falls within neither category.

4. The reader is advised to be wary of the distinction between the Washington Legal Foundation and the Legal Foundation of Washington. The Washington Legal Foundation is a public interest group representing the plaintiffs, whereas the Legal Foundation of Washington is an entity the Washington Supreme Court established to implement the IOLTA program.

5. 524 U.S. 156, 118 S.Ct. 1925 (1998).

6. 438 U.S. 104, 98 S.Ct. 2646 (1978).

7. See *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 324-25, 122 S.Ct. 1465, 1479 (2002), wherein the Court stated:

This longstanding distinction between acquisitions of property for public use, on the one hand, and regulations prohibiting private uses, on the other, makes it inappropriate to treat cases involving physical takings as controlling precedents for the evaluation of a claim that there has been a "regulatory taking," and vice versa. For the same reason that we do not ask whether a physical appropriation advances a substantial government interest or whether it deprives the owner of all economically valuable use, we do not apply our precedent from the physical takings context to regulatory takings claims.

Nevertheless, as this paper will show, the fungible nature of interest requires an *ad hoc* consideration such as that which is normally applied to regulatory takings. All pertinent factors must be considered before a government program may be deemed to effect an unconstitutional taking. Interest should not be analyzed under the test used for physical takings, for such a test simply does not fit the fluid nature of interest. An *ad hoc* consideration of the facts reveals that IOLTA cannot be considered an unconstitutional taking. Efficiency and justice, the purposes of the Fifth Amendment's Takings Clause,⁸ cannot be achieved if government may not transfer meager amounts of interest to a program that benefits the public good without adversely affecting the client.⁹

Part II, Section A sets forth the facts of *Washington Legal Foundation v. Legal Foundation of Washington*. Part II, Section B analyzes the history and mechanics of the IOLTA program. Lastly, Part II, Section C summarizes the essence of the constitutional dilemma over IOLTA and the importance of *Washington Legal Foundation v. Legal Foundation of Washington*. Part III discusses scholarly interpretations of the Takings Clause by analyzing the theories of two nationally renowned constitutional law scholars, Frank Michelman and Richard Epstein, as well as the Supreme Court's interpretation of the Takings Clause as revealed by jurisprudence. Part IV, Section A addresses *Phillips v. Washington Legal Foundation*, wherein the Supreme Court first considered IOLTA and held the interest at issue was property. Finally, Part IV, Section B picks up where the *Phillips* Court left off and analyzes the constitutionality of IOLTA. This section argues that an *ad hoc* analysis, rather than a *per se* analysis, is the proper takings analysis for IOLTA. If the Court uses an *ad hoc* analysis, it should conclude that IOLTA does not effect a taking. However, even if the Court applies a *per se* analysis and concludes that IOLTA does effect a taking, it should ultimately decide that the proper compensation due is nil. Thus, regardless of the route it chooses to take, in deciding *Washington Legal Foundation v. Legal Foundation of Washington*, the Court should ultimately determine that IOLTA is a constitutional exercise of government power that does not require compensation.

8. See generally Michael A. Heller & James E. Krier, *Deterrence and Distribution in the Law of Takings*, 112 Harv. L. Rev. 997 (1999); Frank I. Michelman, *Property, Utility, and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law*, 80 Harv. L. Rev. 1165 (1967).

9. *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 413, 343 S.Ct. 158, 159 (1922) ("Government hardly could go on if to some extent values incident to property could not be diminished without paying for every such change in the general law.").

II. WASHINGTON LEGAL FOUNDATION V. LEGAL FOUNDATION OF WASHINGTON

A. Facts and Procedural History

In 1984, the Washington Supreme Court included an IOLTA program in its Rules of Professional Conduct.¹⁰ The Washington Supreme Court established the Legal Foundation of Washington in tandem with the IOLTA program to implement a grant application process by which IOLTA funds would be distributed.¹¹ Washington Rule of Professional Conduct 1.14 requires lawyers to place “client funds that are nominal in amount or expected to be held for a short period of time” in a pooled interest-bearing trust account if the attorney determines that the funds cannot be used to obtain a net return for the client.¹² The interest from this pooled account is paid to the Legal Foundation of Washington, a charitable organization dedicated to improving the availability and quality of legal representation for the poor. Under Washington’s program, the client’s attorney is given the sole discretion, unfettered by a need for client consent, to determine whether the client’s principal can be managed in a way that will earn the client a positive net return.¹³ In making this determination, the lawyer should consider the potential interest accrual of the funds for the anticipated length of deposit, the cost of maintaining the account including any attorney or tax reporting costs, and the ability of the financial institutions to both calculate and allocate the interest to individual clients.¹⁴

In this case, four individuals who claimed their interest had been “taken” by IOLTA along with the Washington Legal Foundation, a public interest advocacy group, filed suit to challenge the program as an unconstitutional taking. The district court granted summary judgment for the Legal Foundation of Washington, holding no property right was at stake. The Ninth Circuit Court of Appeals reversed and held the appellants owned the interest, reasoning that IOLTA effected a *per se* taking that required compensation.¹⁵ On rehearing *en banc* the Ninth Circuit reached a different conclusion and affirmed the district court ruling on the takings issue.¹⁶ The United States Supreme Court granted *certiorari*.¹⁷

10. See Wash. Rules of Prof'l Conduct R. 1.14 (2002).

11. Washington Legal Found. v. Legal Found. of Washington, 271 F.3d 835, 844 (9th Cir. Nov. 14, 2001).

12. Wash. Rules of Prof'l Conduct R 1.14 (c)(2), (c)(3) (2002).

13. Wash. Rules of Prof'l Conduct R. 1.14 (c)(3) (2002).

14. *Id.*

15. Washington Legal Found. v. Legal Found. of Washington, 236 F.3d 1097 (9th Cir. Jan. 10, 2001).

16. *Washington*, 271 F.3d 835.

17. *Brown v. Legal Found. of Washington*, 122 S.Ct. 2355 (2002).

B. *The IOLTA Program*

The Washington IOLTA program mirrors similar programs instituted in every other state. Washington's IOLTA program, like all others, transfers interest accruals, which would otherwise go to the bank, to programs that help provide legal assistance for indigents. These programs have essentially the same structure because they were developed as a result of the Consumer Checking Account Equity Act, passed in 1980.¹⁸ Prior to the Act's enactment, federal law prohibited federally insured banks from paying interest on checking accounts, which left attorneys with no other option but to place client monies in these accounts if they wanted to ensure availability of funds on demand.¹⁹ The Act, codified in 12 U.S.C. § 1832, authorized federally insured banks to pay interest on demand accounts, called Negotiable Order of Withdrawal (NOW) accounts, but only to a select few. Such accounts are only available for deposits consisting of funds "held by" charitable, philanthropic, educational or other non-profit organizations.²⁰ However, this requirement does not mean that only charitable organizations have access to NOW accounts. The Federal Reserve Board interprets § 1832(a) to allow corporate funds to be placed in NOW accounts if done pursuant to a program that entitles charitable organizations to all interest accruals.²¹ IOLTA programs fall within this class.

Congress's timing in passing the Consumer Checking Account Equity Act was perfect because it allowed states to capitalize on the soaring interest rates of the 70's by using interest from NOW accounts to meet their funding needs for programs providing legal aid to indigents.²² From 1974 to 1981, Legal Services Corporation, a federally funded corporation, had steadily been subsidizing local attorneys who provided legal services for the poor, but Congress drastically reduced the program's budget in 1981, leaving the states and their bar associations to look for funding elsewhere.²³ Thus, IOLTA was born.

18. *Washington*, 271 F.3d at 842.

19. *Id.*

20. 12 U.S.C. § 1832 (a)(2) (2002).

21. Letter from Federal Reserve Board General Counsel Michael Bradfield to Donald Middlebrooks (Oct. 15, 1981), reprinted in Donald M. Middlebrooks, *The Interest on Trust Accounts Program: Mechanics of its Operation*, 56 Fla. B.J. 115, 117 (Feb. 1982).

22. *Washington*, 271 F.3d at 843.

23. See James D. Anderson, *The Future of IOLTA: Solutions to Fifth Amendment Takings Challenges Against IOLTA Programs*, 1999 U. Ill. L. Rev. 717, 720.

Florida instituted the first IOLTA program in 1981.²⁴ Now there are IOLTA programs in all fifty states and the District of Columbia.²⁵ Common to all these states is the adoption of the classic canon of legal professionalism that attorneys are obligated to represent the poor.²⁶ In fact, Rule 6.1 of the Model Rules of Professional Responsibility encourages attorneys to render at least fifty hours of legal services without fee or expectation of fee to persons with limited means.²⁷ All attorneys are expected to fulfill this responsibility at some point in their career. IOLTA helps attorneys fulfill this ethical obligation without imposing additional costs on attorneys or their clients because, like Robin Hood, IOLTA confers this benefit on the poor by taking it from the bank.

Not all concede that IOLTA's goal is a noble one. This school of thought is embodied in plaintiffs who are waging wars against IOLTA across the United States.²⁸ IOLTA's opponents attack the program's merits and allege it gives money to attorneys instead of the poor by funding controversial causes such as support groups for attorneys with chemical dependancies.²⁹ While these are valid concerns, they are concerns best left to the individual states, not the United States Supreme Court.³⁰ Each state implements its own form of IOLTA and allocates the monies according to its needs. States, by design, serve as representatives of their citizens and, consequently, are the appropriate authority for complaints about the specifics.³¹

Despite the opposition, IOLTA is an effective program active in the fifty states and the District of Columbia.³² In 2002, IOLTA produced approximately one hundred forty-eight million dollars to help resolve everyday disputes such as spousal and child abuse, domestic relations, child support, and consumer and housing

24. *Phillips*, 524 U.S. at 161, 118 S.Ct. at 1929

25. *Phillips*, 524 U.S. at 159, 118 S.Ct. at 1927-28, n.1; Ind. Rules of Prof'l Conduct R. 1.15(d) (2000) (establishing an IOLTA program in Indiana after the Court decided *Phillips*).

26. Model Code of Prof'l Responsibility Canon 2 (2002) ("A lawyer should assist the legal profession in fulfilling its duty to make legal counsel available.").

27. Model Rules of Prof'l Responsibility R. 6.1 (2002) ("A lawyer should aspire to render at least (50) hours of pro bono publico legal services per year.").

28. *See generally Phillips*, 524 U.S. 156, 118 S.Ct. 1925; *Washington Legal Found. v. Massachusetts Bar Found.*, 993 F.2d 962 (1st Cir. 1993); *Cone v. State Bar of Florida*, 819 F.2d 1002 (11th Cir. 1987).

29. Cassandra C. Moore, *The IOLTA Program: The Invisible Hand*, *The CATO Review of Business & Government*, available at <http://www.cato.org/pubs/regulation/regv15n3/reg15n3-moore.html> (last visited Apr. 1, 2003).

30. *See generally* The Federalist No. 39 (James Madison).

31. *Id.*

32. *See supra* note 28.

problems.³³ This is a phenomenal amount, considering that had the interests not been pooled in IOLTA, nothing would have been generated except a windfall for the bank. Imagine the consequences of this beneficial program screeching to a halt at the hands of the Supreme Court with nothing to fill the void.

C. *The Essence of the Dilemma*

The constitutionality of IOLTA has lurched back and forth in courts across the country, resulting in a myriad of inconsistencies.³⁴ In *Washington Legal Foundation v. Texas Equal Access to Justice Foundation*,³⁵ the United States Fifth Circuit Court of Appeals contradicted every other circuit in the country³⁶ when it held that the interest earned on funds placed in IOLTA was property. The Supreme Court resolved the circuit split by affirming the Fifth Circuit's decision in *Phillips v. Washington Legal Foundation*,³⁷ but the Supreme Court's refusal to answer the takings issue created another split in the circuits on the issue of whether IOLTA effects an unconstitutional taking. The United States Fifth Circuit Court of Appeals, using a *per se* method of takings analysis, has held IOLTA to be an unconstitutional taking,³⁸ whereas the Ninth Circuit, applying an *ad hoc* analysis, has upheld IOLTA's constitutionality.³⁹ Thus, *Washington Legal Foundation v. Legal Foundation of Washington* provides the Supreme Court with the perfect opportunity to resolve this dispute among the circuits. The Court must, once again, wade

33. See *Washington*, 271 F.3d at 843.

34. See generally *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 873 F. Supp. 1 (W.D. Tex. 1995) (granting summary judgment to defendants), *aff'd in part, rev'd in part*, 94 F.3d 996 (5th Cir. 1996) (reversing summary judgment to defendants), *cert. granted sub nom; Phillips*, 521 U.S. 1117, 117 S.Ct. 2535 (1997), *and aff'd*, 524 U.S. 156, 118 S.Ct. 1925 (1998) (holding the client's interest was "property," but declining to answer whether IOLTA effected an unconstitutional taking); *Washington*, 236 F.3d 1097 (holding that IOLTA effected an unconstitutional taking), *rev'd en banc*, 271 F.3d 835 (holding IOLTA was not a Fifth Amendment taking, and even if it were, no just compensation was due); *Washington Legal Found. v. Massachusetts Bar Found.*, 993 F.2d 962 (holding IOLTA was not an unconstitutional taking).

35. 94 F.3d 996.

36. See generally *Washington Legal Found. v. Massachusetts Bar Found.*, 993 F.2d 962; *Cone v. State Bar of Florida*, 819 F.2d 1002; *Carroll v. State Bar of California*, 213 Cal.Rptr. 305 (Cal. Ct. App. 1985); *In re Lawyers' Trust Accounts*, 672 P.2d 406 (Utah 1983); *In re Minnesota State Bar Ass'n.*, 332 N.W.2d 151 (Minn. 1982).

37. 524 U.S. 156, 118 S.Ct. 1925.

38. See *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 270 F.3d 180 (5th Cir. 2001).

39. See *Washington*, 271 F.3d 835.

through the troubled waters of constitutional property law to determine the proper analysis for adjudging whether there is an unconstitutional taking of intangible property. IOLTA's future lies precariously in the hands of the Court.

III. RESOLVING THE CONFLICT BETWEEN IOLTA AND THE TAKINGS CLAUSE

A. The Enigma of Property Law and Takings Jurisprudence

Property has held an elevated position on the constitutional hierarchy since our Nation's inception. Unlike many other constitutional amendments, the Fifth Amendment was included in the United States Constitution virtually without debate.⁴⁰ Ironically, unanimity in 1798 has spawned much controversy in subsequent years as real life dilemmas demand that the scope of property be defined for purposes of the Fifth Amendment takings analysis. Thus, the Supreme Court is left with the responsibility of determining what the law is on constitutional property. Unfortunately, the Court has been unable to develop an absolute formula because the dimensions of property are constantly evolving.

1. Constitutional Scholars and the Takings Clause

There is much debate among the scholars regarding the proper theory to apply in a takings analysis; this paper will focus on two influential theories: the utilitarian approach of Professor Frank Michelman,⁴¹ associated with the *ad hoc* takings analysis, and the conceptual severance theory of Professor Richard Epstein,⁴² associated with the *per se* takings test. Michelman argues that before government can be required to compensate an individual for a taking, the court must determine whether fairness requires compensation.⁴³ Richard Epstein, on the other hand, insists that government must compensate an individual for the taking of any property right.⁴⁴ These differences in theory culminate into the consideration of what one considers to be the property interest at stake—the bundle of

40. David A. Dana & Thomas W. Merrill, *Property: Takings* 14 (Foundation Press 2002).

41. Constitutional law scholar and the Robert Walmsley Professor at Harvard Law School.

42. Constitutional law scholar and the James Parker Hall Distinguished Service Professor at the University of Chicago Law School.

43. See generally Michelman, *supra* note 8 at 1173.

44. Courtney C. Tedrowe, *Conceptual Severance and Takings in the Federal Circuit*, 85 Cornell L. Rev. 586, 593 (2000).

sticks taken as a whole, or each individual stick as a separate piece of property.

Ownership of property has long been associated with ownership of a “bundle of rights” or a “bundle of sticks.”⁴⁵ This metaphor stands for the proposition that property is what a layperson assumes is incident to ownership. Following this rationale, the sticks that make up the bundle are understood to be the rights of use, exclusion and disposition.⁴⁶ Though the metaphor of property as a bundle of sticks is helpful on a theoretical level, it provides little guidance in determining whether an unconstitutional taking has occurred. The metaphor fails in a takings analysis because it offers no assistance in determining whether one stick is constitutionally “heavier” than another, whether the removal of one stick is so destructive to the bundle that it should be considered a taking of the whole, or whether each stick should be considered separately for purposes of the Takings Clause. These considerations are reflected in two different theories — conceptual severance and utilitarianism.

Epstein furthers the theory of conceptual severance,⁴⁷ which essentially means that every incident of ownership, such as the right to use, enjoy or dispose of property, etc., may be severed from the bundle and considered a property right in itself.⁴⁸ He embraces the classic liberal conception of property, viewing the three predominant sticks in the bundle to be the exclusive rights to possession, use, and disposition.⁴⁹ Epstein contends that any government action that interferes with the three exclusive property rights is a prima facie taking that requires compensation.⁵⁰ Thus, for example, any government action that limits the right to freely dispose of property would be considered an unconstitutional taking of that property right (i.e. the right of disposition). To Epstein, the definition of property is limited to the specific portion or use of property of which the government deprives the owner.⁵¹ Thus, in essence, the property is defined by what the government has taken. Epstein’s view is extreme

45. John Lewis, *Law of Eminent Domain in the United States* § 55 at 43 (1888) (“The dullest individual among the people knows and understands that his property in anything is a bundle of rights.”).

46. *Id.* at 44.

47. Professor Radin, professor of law at the University of Southern California Law Center, coined the term “conceptual severance” after reading Epstein’s book, *Takings: Private Property and the Power of Eminent Domain*. See Tedrowe, *supra* note 44.

48. Richard A. Epstein, *Takings: Private Property and the Power of Eminent Domain* 57-62, 57-58 (1985).

49. *Id.* at 59.

50. *Id.* at 57.

51. Margaret Jane Radin, *The Liberal Conception of Property: Cross Currents in the Jurisprudence of Takings*, 88 *Colum. L. Rev.* 1667, 1669 (1988).

and impractical. Under his theory, all forms of taxation, welfare contributions and zoning restrictions would be considered unconstitutional takings.⁵² Epstein urges that compensation by the government to all who are adversely affected maximizes efficiency.⁵³ However, Epstein's logic is difficult to follow. Efficiency is abandoned if government may not reallocate resources to maximize value without paying every step of the way.⁵⁴ Conceptual severance, at best, thwarts efficiency in the name of an extremely conservative pro-property rationale.

Michelman's view of property, on the other hand, is associated with utilitarianism. For utilitarians, the ultimate goal is the maximization of utility for society as a whole, rather than for individuals.⁵⁵ According to Michelman, the proper inquiry is whether it is fair to reallocate an individual's resources in the name of government action aimed at benefitting society as a whole without granting a claim to compensation for the private loss inflicted.⁵⁶ Michelman notes that the common denominator among all Takings Clause cases is a four factor inquiry: 1) whether the public or its agents have physically occupied the claimant's property; 2) the degree of the harm or extent to which the property has been devalued; 3) whether the loss is outweighed by the public's gain; and 4) any other loss sustained by the claimant other than the ability to participate in an unlawful or otherwise harmful activity.⁵⁷ Although these factors are instrumental in determining whether compensation is needed, Michelman concedes that the dynamic nature of property precludes one factor from being dispositive.⁵⁸ Thus, the overarching theme of Michelman's view is clear: each factor must be carefully considered before deeming a taking unconstitutional.

B. Supreme Court Application

The Supreme Court has never fully accepted the Epstein view in its constitutional analysis of takings under the Fifth Amendment.⁵⁹ Instead, Michelman's theory has had greater influence over the Court, and this is illustrated by the prevailing use of a multi-factor balancing

52. *Id.*

53. Tedrowe, *supra* note 44.

54. *See supra* text accompanying note 9.

55. D. Benjamin Barros, *Defining "Property" in the Just Compensation Clause*, 63 Fordham L. Rev. 1853, 1859 (1995).

56. Michelman, *supra* note 8, at 1171-72.

57. *Id.* at 1184.

58. *Id.*

59. *See* Radin, *supra* note 51, at 1671.

test as seen in *Penn Central*.⁶⁰ However, there are decisions that indicate the conceptual severance theory still looms in the shadows.⁶¹ The following cases shed light on the Court's development of regulatory takings through the years. Though IOLTA is not a regulatory taking, regulatory takings cases are relevant. In fact, the Court relied on regulatory takings cases in its first confrontation with IOLTA in *Phillips*.⁶² A thorough examination of the cases reveals that the only logical solution to analyzing intangible property takings cases is to consider *all* the pertinent facts of a particular situation by applying the *Penn Central* balancing test.

*Penn Central Transportation Co. v. City of New York*⁶³ provides the prevailing standards for a constitutional regulatory takings analysis. *Penn Central* assigns a practical application to the analysis first stated in *Pennsylvania Coal Co. v. Mahon*,⁶⁴ where the Supreme Court, led by Justice Holmes, stated that a regulation that goes too far will be considered a taking.⁶⁵ *Penn Central* provides what *Pennsylvania Coal* was lacking: the mechanism for determining how far is too far.

At issue in *Penn Central* was the constitutionality of New York City's Landmarks Preservation Law, which prohibited Penn Central Transportation Co., owners of the Grand Central Terminal ("Terminal"), from building a multi-story office building above the Terminal in the name of preserving a historical landmark.⁶⁶ Penn Central Transportation Company argued that the regulation effected a taking, and thus required compensation. Before refuting these claims, the Supreme Court noted its inability to settle on a simple formula and stressed the importance of relying on the particular circumstances of the case.⁶⁷ The Court set forth the relevant factors to be considered in a takings analysis, otherwise known as the *Penn Central* multi-factor balancing test. These considerations are: "[t]he economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations"⁶⁸ With the aid of these factors, the Court held that the

60. 438 U.S. 104, 98 S.Ct. 2646 (1978).

61. See generally *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 112 S.Ct. 2886 (1992).

62. 524 U.S. 156, 118 S.Ct. 1925.

63. 438 U.S. 104, 98 S.Ct. 2646.

64. 260 U.S. 393, 43 S.Ct. 158 (1922) (deeming unconstitutional a Pennsylvania statute that forbade the Pennsylvania Coal Co. from mining coal beneath homes).

65. *Id.* at 414-15.

66. *Penn Cent.*, 438 U.S. at 117-18, 98 S.Ct. at 2655-56.

67. *Id.* at 124, 98 S.Ct. at 2659 (citing *United States v. Cent. Eureka Mining Co.*, 357 U.S. 155, 168, 78 S.Ct. 1097, 1104 (1958)).

68. *Id.*

Landmarks Law did not effect a taking because the regulation not only promoted the general welfare, but also afforded appellants alternatives for enhancing the Terminal site and surrounding properties.⁶⁹ Finally, the Court explicitly disavowed any support for a conceptual severance argument in stating that the property should be considered as a whole, and not as inconspicuous pieces.⁷⁰ Thus, whether there was a regulatory taking depended on the character and extent of the interference with respect to the entire city block because the entire block was considered the "landmark site."⁷¹

In *Lucas v. South Carolina Coastal Council*,⁷² Justice Scalia broke new ground and introduced a *per se* rule for regulatory takings similar to the rule applied to physical takings.⁷³ In *Lucas*, the Court held that South Carolina's Beachfront Management Act, which prohibited the plaintiff, Lucas, from building homes on his residential lots, was an unconstitutional taking under this *per se* analysis. According to Scalia, this *per se* category would require compensation for any government action resulting in a complete deprivation of all feasible use of a claimant's property, thus making it analogous to a physical appropriation.⁷⁴ This decision was expansive in that it seemingly placed regulatory takings on equal footing with physical invasions of property, the latter of which having long been considered especially egregious.⁷⁵ However, Scalia limited his reasoning to situations where there is a complete taking of *all* economically beneficial uses of the property.⁷⁶ In *Lucas*, Scalia asserted that Lucas had been deprived of all economic value of his property because Lucas purchased the lots for the sole reason of building homes thereon, a use prohibited by the

69. *Id.* at 138, 98 S.Ct. at 2666.

70. *Id.*, 438 U.S. at 130-31, 98 S.Ct. at 2662 ("'Taking' jurisprudence does not divide a single parcel into discrete segments and attempt to determine whether rights in a particular segment have been entirely abrogated. In deciding whether a particular governmental action has effected a taking, this Court focuses rather both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole — here, the city tax block designated as the 'landmark site.'").

71. *Id.*

72. 505 U.S. 1003, 112 S.Ct. 2886.

73. *Id.* at 1019, 112 S.Ct. at 2895 (Scalia reasoned, "[T]here are good reasons for our frequently expressed belief that when the owner of real property has been called upon to sacrifice *all* economically beneficial uses in the name of the common good, that is, to leave his property economically idle, he has suffered a taking.").

74. *Id.* at 1030, 112 S.Ct. at 2901.

75. *Penn Cent.*, 438 U.S. at 124, 98 S.Ct. at 2659 ("A 'taking' may more readily be found when the interference with property can be characterized as a physical invasion by government, than when the interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good.") (citations omitted).

76. *Lucas*, 505 U.S. at 1030, 112 S.Ct. at 2901.

Beachfront Management Act.⁷⁷ Thus, the Court held that compensation was required.

Though it was never actually termed as such, the theory of conceptual severance was looming in the shadows of *Lucas* because, in order to find that the regulation effected a total taking, Scalia had to sever the use right the Act prohibited (i.e., development of the beachfront property) from the rest of the property.⁷⁸ As Justices Kennedy and Blackmun pointed out in their concurring and dissenting opinions, there are other economic uses available to owners of beachfront property.⁷⁹ By ignoring these other economic uses available to Lucas, Scalia, in effect, limited the property at issue to the incident of property that was affected by the regulation, rather than considering the property as a whole. This argument is indeed conceptual severance.

Lucas has not been overturned, but subsequent Supreme Court decisions have either ignored or distinguished *Lucas*, revealing the Court's disfavor with applying Scalia's *per se* theory.⁸⁰ *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*,⁸¹ decided in 2002, is the latest Supreme Court holding on regulatory takings. *Tahoe* does not overrule *Lucas*, but it clearly illustrates the Court's disavowal of a *per se* analysis for regulatory takings in favor of *Penn Central ad hoc* factual inquiries.⁸² The facts of *Tahoe* are similar to those in *Lucas*. The Tahoe Regional Planning Agency (TRPA) imposed two moratoria prohibiting development of the land surrounding Lake Tahoe.⁸³ A group of real estate owners challenged the constitutionality of the regulation, alleging it effected a taking of

77. *Id.* at 1018, 112 S.Ct. at 2895.

78. *See Tahoe*, 535 U.S. at 331, 122 S.Ct. at 1483 (alluding to the conceptual severance argument in *Lucas* in stating, "Petitioners' 'conceptual severance' argument is unavailing because it ignores *Penn Central's* admonition that in regulatory takings cases we must focus on 'the parcel as a whole.'").

79. *Lucas*, 505 U.S. at 1044, 112 S.Ct. at 2908 (Blackmun, J., dissenting) ("State courts frequently have recognized that land has economic value where the only residual economic uses are recreation or camping.").

80. *See Tahoe*, 535 U.S. at 332, 122 S.Ct. at 1484 ("[T]he categorical rule in *Lucas* was carved out for the 'extraordinary case' in which a regulation permanently deprives property of all value; the default rule remains that, in the regulatory taking context, we require a more fact specific inquiry."); *Palazzolo v. Rhode Island*, 533 U.S. 606, 636, 121 S.Ct. 2448, 2467 (2001) (O'Connor, J., concurring) (resisting "[t]he temptation to adopt what amount to *per se* rules in either direction.").

81. 535 U.S. 302, 122 S.Ct. 1465.

82. *Id.* at 321, 122 S.Ct. at 1478 ("[O]ur cases do not support [the petitioners] proposed categorical rule — indeed, fairly read, they implicitly reject it. [T]he answer to the abstract question whether a temporary moratorium effects a taking is neither 'yes, always' nor 'no, never'; the answer depends upon the particular circumstances of the case.").

83. *Id.* at 306, 122 S.Ct. at 1470.

private property without compensation.⁸⁴ The Court rejected the petitioners' contention that, under *Lucas per se* rule, they were entitled to compensation because they were deprived of all economically viable use of their property.⁸⁵ Justice Stevens, speaking for the Court, asserted that when confronted with regulatory takings cases, the Supreme Court had abrogated the use of a categorical rule in favor of an analysis assessing all pertinent facts.⁸⁶ The Court reconciled its decision with *Lucas* by arguing that, unlike in *Lucas* where the regulation precluded all economically feasible use of the property, the regulation at issue only placed a temporary halt on such use.⁸⁷ Thus, according to the Court, anything less than a complete or total loss of all economic use would require a *Penn Central* multi-factor analysis.⁸⁸

Chief Justice Rehnquist and Justices Scalia and Thomas dissented and suggested support for the theory of conceptual severance. They treated the property owners' economic interests as separate and apart from all other ownership interests in the land surrounding Lake Tahoe. Rehnquist held fast to *Lucas*, arguing that the regulation deprived the property owner of all economically beneficial use of his land so as to constitute a taking.⁸⁹ Thomas and Scalia dissented separately and expressed their disapproval of considering the property as a whole. They argued that a regulation depriving the owner of even a "temporal slice" of the use of his property is a taking for which the owner must be compensated unless state property law would have precluded this use anyway.⁹⁰ Though they only comprise a minority of the Court, Rehnquist, Scalia and Thomas will likely continue to apply conceptual severance to require compensation for interference with any property right incident to ownership.⁹¹ Thus, conceptual severance lives on, and could again rear its ugly head in the upcoming constitutional challenge against IOLTA in *Washington Legal Foundation v. Legal Foundation of Washington*.

IV. THE UPCOMING DECISION OF LEGAL FOUNDATION V. LEGAL FOUNDATION OF WASHINGTON

A. *Is the Interest Property?*

1. *Phillips v. Washington Legal Foundation*

Washington Legal Foundation, a Texas attorney and a Texas citizen brought an action against the justices of the Texas Supreme

84. *Id.*

85. *Id.* at 330-31, 122 S.Ct. at 1483.

86. *Tahoe*, 535 U.S. at 321, 122 S.Ct. at 1478.

87. *Id.* at 332, 122 S.Ct. at 1484.

88. *Id.* at 330, 122 S.Ct. at 1483.

89. *Id.* at 346, 122 S.Ct. at 1491-92.

90. *Id.* at 355, 122 S.Ct. at 1496 (citations omitted).

91. See discussion *supra* Part III, § A(1).

Court, the Texas Equal Access to Justice Foundation, and the Foundation's chairman, arguing that the Texas IOLTA program was an unconstitutional taking of private property. The United States District Court for the Western District of Texas granted summary judgment for the defendants and held that the interest in IOLTA was not "property."⁹² The United States Fifth Circuit Court of Appeals reversed.⁹³ The United States Supreme Court granted *certiorari* and held the interest income generated by funds held in IOLTA was the private property of the owner of the principal for purposes of the Takings Clause.⁹⁴ The *Phillips* holding was limited to the property question, and did not address whether the IOLTA program effected an unconstitutional taking of private property without just compensation.

In determining that the interest earned on a client's principal (i.e. the initial sum placed in trust) is his property, the Court followed the same property law principles as it had in *Board of Regents of State Colleges v. Roth*.⁹⁵ In *Roth*, the Court stated that the Constitution does not create property rights.⁹⁶ Instead, the dimensions of property interest are defined by existing rules from independent sources such as state law.⁹⁷ Thus, in deciding how to classify the interest accruals from principal amounts placed in trust accounts pursuant to IOLTA, the *Phillips* Court deferred to the age old common law principle that "interest follows principal."⁹⁸ The court was unconcerned that affected clients would realize no net interest, reasoning that property does not cease to be property because it lacks a positive economic value.⁹⁹

92. *Washington Legal Found. v. Texas Equal Access to Justice*, 873 F. Supp. 1.

93. *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 94 F.3d 996.

94. *Phillips*, 524 U.S. 156, 118 S.Ct. 1925.

95. 408 U.S. 564, 577, 92 S.Ct. 2701, 2709 (1972).

96. *Id.* ("Property interests . . . are not created by the Constitution. [T]hey are created and their dimensions are defined by existing rules or understandings that stem from an independent source such as state law . . .").

97. *Id.*

98. *Phillips*, 524 U.S. at 165, 118 S.Ct. at 1930 (citing *Beckford v. Tobin*, 1 Ves.Sen. 308, 310, 27 Eng.Rep. 1049, 1051 (Ch. 1749)) ("[I]nterest shall follow the principal, as the shadow the body."). The Court also noted that Texas law supports the interest follows principal rationale. See *Sellers v. Harris County*, 483 S.W.2d 242, 243 (Tex. 1972).

99. *Phillips*, 524 U.S. at 169-70, 118 S.Ct. at 1933 (citing *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 102 S.Ct. 6164 (1982); *States v. General Motors Corp.*, 323 U.S. 373, 378, 65 S.Ct. 357, 359 (1945)) ("We have never held that a physical item is not 'property' simply because it lacks a positive economic or market value. [P]roperty is more than economic value . . . ; it also consists of 'the group of rights which the so-called owner exercises in his dominion

The Court analogized *Phillips to Webb's Fabulous Pharmacies, Inc. v. Beckwith*.¹⁰⁰ There, the Supreme Court addressed the constitutionality of a Florida statute that deemed all interest generated from funds deposited in the court registry to be income of the clerk of court's office.¹⁰¹ In *Webb's*, the appellant placed nearly two million dollars into the court's registry for an interpleader action.¹⁰² The controversy arose when the clerk of court deducted over nine thousand dollars from the fund as a fee for services, in addition to retaining over one hundred thousand dollars in interest that had accrued from the appellant's principal.¹⁰³ In *Webb's*, the Court relied on the "interest follows principal" theory and held that the Florida statute violated the Fifth Amendment Takings Clause, noting that the owners had a reasonable and substantial expectation that the principal would earn net interest.¹⁰⁴

The petitioners in *Phillips* urged that *Webb's* was not definitive, citing circumstances in Texas where the interest does not always follow the principal.¹⁰⁵ Alternatively, the United States as *amicus curiae* noted that but for legislation authorizing NOW accounts, no interest would accrue for the client, and that, therefore, the interest was not the client's property but rather a gratuitously conferred benefit.¹⁰⁶ Lastly, the petitioners argued there could be no property interest because, with or without IOLTA, the clients had no expectation of income from the principal.¹⁰⁷ The Court quickly dismissed these arguments, noting that the common law exceptions to the "interest follows principal" rule did not apply.¹⁰⁸ The Court did recognize that a state may not simply circumvent through legislation the traditional rule that interest follows principal.¹⁰⁹ The earnings of the principal are property, just as the principal is

of the physical thing,' such 'as the right to possess, use and dispose of it.'").

100. 449 U.S. 155, 101 S.Ct. 446 (1980).

101. *Id.*, 449 U.S. at 156, 101 S.Ct. at 448 n.1.

102. *Id.* at 156, 101 S.Ct. at 448.

103. *Id.* at 158, 101 S.Ct. at 449.

104. *Id.* at 161, 101 S.Ct. at 451.

105. Brief for Petitioners at 22, *Phillips*, 524 U.S. 156, 118 S.Ct. 1925 (No. 96-1578) (citing situations in which the interest does not follow the principal in Texas, such as "income-only" trusts where one beneficiary receives the principal and another receives the interest, as well as community property law that requires the interest earned on the principal to be owned jointly by the spouses rather than solely by the depositor).

106. Brief for United States as *Amicus Curiae* at 20, *Phillips*, 524 U.S. 156, 118 S.Ct. 1925 (No. 96-1578).

107. Brief for Petitioners at 27-8, *Phillips*, 524 U.S. 156, 118 S.Ct. 1925 (No. 96-1578).

108. *Phillips*, 524 U.S. at 168, 118 S.Ct. at 1932.

109. *Id.* at 167, 118 S.Ct. at 1931 (citing *Webb's*, 449 U.S. at 164, 101 S.Ct. at 452).

property. Thus, the court deemed the interest earned on monies placed in IOLTA to be property.¹¹⁰

2. *Phillips: A Decision, but not an Answer*

The major flaw of *Phillips* is that the Court considered the property question without also considering the interconnected taking and compensation issues. Thus, although the Supreme Court rendered a decision in *Phillips*, it resolved little because the constitutionality of IOLTA stills hangs in the balance. *Phillips* left us with nothing but a wasted trip to Capitol Hill and a stack of unfinished business that *Washington Legal Foundation v. Legal Foundation of Washington* must now resolve. Perhaps the Court was just biding its time until it was ready to make the right decision. Fortunately, the *Phillips* Court resolved the property issue when it recognized a property interest in the monies placed in NOW accounts. Thus, the only remaining issue for the Court to address in *Washington Legal Foundation v. Legal Foundation of Washington* will be whether the property has been taken without just compensation.

B. *The interest is property, but is IOLTA an unconstitutional taking?*

Regulatory takings have traditionally involved governmental regulations that place limitations upon property rights incidental to the property, e.g., disposition rights, use rights, exclusionary rights, etc.¹¹¹ IOLTA, however, is not a regulatory taking because, rather than placing limitations on incidental property rights, IOLTA actually appropriates the property itself. Though this would appear to be a physical taking, the Supreme Court has noted that, due to its fungible nature, money cannot be physically appropriated as can real or personal property.¹¹² The Supreme Court has already analyzed IOLTA in the context of a regulatory takings analysis, which suggests that the Court will likely look to a regulatory takings analysis in deciding *Washington Legal Foundation*.¹¹³

The nature of the property interest involved in *Washington Legal Foundation* makes it unreasonable to analogize it to real property. The transfer of interest to IOLTA does not affect the property owner in the same way that a physical invasion of one's property would. This

110. *Phillips*, 524 U.S. at 172, 118 S.Ct. at 1934.

111. See generally *Dolan v. City of Tigard*, 512 U.S. 374, 114 S.Ct. 2309 (1994); *Nollan v. California Coastal Comm'n*, 483 U.S. 825, 107 S.Ct. 3141 (1987); *Penn Cent.*, 438 U.S. 104, 98 S.Ct. 2646.

112. See *United States v. Sperry*, 493 U.S. 52, 62 n. 9, 110 S.Ct. 387 (1989); but see *Washington*, 271 F.3d 835, 866 (J., Kozinski, dissenting).

113. 524 U.S. 156, 118 S.Ct. 1925.

becomes clear when the nature of interest in IOLTA is contrasted with the nature of real property. Interest payments are highly regulated as a matter of course, and thus create an expectation of regulation by the government or financial institution.¹¹⁴ On the other hand, one would not expect the government to take physical property, like a portion of one's home or driveway, without paying for it. Thus, although IOLTA is not a regulatory taking, due to the nature of the property at stake, a regulatory takings analysis is entirely appropriate.

The trend toward conducting the *ad hoc* factual inquiries of *Penn Central* to analyze regulatory takings is apparent in the Supreme Court's Takings Clause jurisprudence. After analyzing years of constitutional takings cases it is apparent that it is the most appropriate method for regulatory takings cases. Granted, Justice Scalia persuaded a majority of the Court, in *Lucas*, to equate a regulatory taking to a physical taking when government action results in a complete loss of all property value.¹¹⁵ However, the Court has shied away from applying the *Lucas* rule. The Court has exercised this restraint because regulatory takings are simply not as egregious as physical takings of real property, a fact even the *Lucas* Court conceded.¹¹⁶ Thus, as became clear in *Tahoe*, although the Court has not overruled *Lucas*, it has explicitly disavowed any regulatory takings analysis other than *Penn Central ad hoc* analysis.¹¹⁷

An *ad hoc* analysis, in the case of IOLTA, would allow for a consideration of *all* the relevant facts, thereby assuring that not one factor or stick, if you will, is dispositive in determining whether compensation is required. Applying the *Lucas* categorical rule would be illogical and arbitrary because it would improperly augment the client's rights at the expense of the government. In other words, applying the *per se* rule would create too much property.¹¹⁸ Perhaps it is for this reason that the Court has been reluctant to apply a *per se* analysis to any government actions but actual physical takings of real property.¹¹⁹

Choosing the *ad hoc* analysis over the *per se* analysis might appear to some members of the Court to be an arbitrary decision, but Justice

114. *Andrus v. Allard*, 444 U.S. 51, 66, 100 S.Ct. 318, 327 (1979) (“[T]he interest in anticipated gains has traditionally been viewed as less compelling than other property related interests.”).

115. *Lucas*, 505 U.S. 1003, 112 S.Ct. 2886.

116. *Lucas*, 505 U.S. at 1028, 112 S.Ct. at 2900 (“Where ‘permanent physical occupation’ of land is concerned we have refused to allow the government to decree it anew (without compensation), no matter how weighty the asserted ‘public interests’ involved. . . .”) (citing *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 426, 102 S.Ct. 3164, 3171); see *supra* text accompanying note 87.

117. See *supra* text accompanying note 85.

118. *Id.* at 1479 (“Treating them all as *per se* takings would transform government regulation into a luxury few governments could afford.”).

119. *Tahoe*, 535 U.S. at 326-27, 122 S.Ct. at 1481.

Kennedy, for one, would likely agree that such a choice would be no more arbitrary than the one the Court made in *Lucas*. Justice Kennedy expressed these sentiments most accurately in voicing disapproval of the categorical rule in *Lucas*: “The Court seems to treat history as a grab bag of principles, to be adopted where they support the Court’s theory, and ignored where they do not.”¹²⁰ Kennedy’s disapproval must be taken with a grain of salt, however, because even if the Court resurrects the conceptual severance theory of *Lucas*, it would not have much bite in the case of *Washington Legal Foundation*. IOLTA does not deprive the owner of all economic use of the property (i.e. the interest plus the principal). The client does not lose any ability to use, enjoy, or dispose of the principal. Nevertheless, however proper the result might be were the Court to take such an approach, the proper test to apply to IOLTA is the *Penn Central ad hoc* analysis.

Conceptual severance is a slippery slope, even more dangerous than the Court’s analysis in *Lucas*, which the Court has continued to distinguish away.¹²¹ Since *Lucas*, the Court has backed away from applying the *per se* analysis to regulatory takings, presumably because it was just too expansive. The Court just is not ready to subject regulatory takings to the level of scrutiny applied to physical takings.¹²² Thus, the Court has whittled the holding of *Lucas* to practically nothing. *Lucas* only applies in the most extreme cases (i.e. where the regulation strips the property of all of its beneficial uses).¹²³ Similarly, conceptual severance would require the government to pay for every interference with any stick in the bundle of rights, not only affecting IOLTA, but also countless other government programs, incentives, and/or regulations. According to Epstein, even taxation is an unconstitutional taking.¹²⁴ Conceptual severance would reflect a sweeping and disconcerting change in the Court’s view of the Fifth Amendment and its purposes of efficiency and justice.

Undoubtedly, Justices Rehnquist, Scalia, and Thomas will urge the conceptual severance argument upon the Court. However, even though conceptual severance is easy to visualize, this does not make it logical. One can only find solace in the prospect that at least five justices will recognize the dangerously expansive nature of conceptual severance, and the far-reaching repercussions it promises for IOLTA and all other such government programs in disavowing its application in *Washington Legal Foundation v. Legal Foundation of Washington*.

Washington Legal Foundation v. Legal Foundation of Washington places before the Court a program that requires interest from the

120. *Lucas*, 505 U.S. at 1060, 112 S.Ct. at 2917.

121. See *supra* note 80.

122. See *supra* text accompanying note 75.

123. See *supra* note 80.

124. See discussion *supra* Part III, § A(1).

client's principal to be transferred to a program that helps provide legal services to the poor. The Court must follow the guidelines set forth by Michelman as well as those set forth by the Court in *Penn Central*. These guidelines suggest a number of factors should be considered: the size of the claimant's harm or the degree to which the property has been devalued, the action's effects on the owner's distinct economic expectations,¹²⁵ and whether the claimant's loss is outweighed by the public gain.¹²⁶ Considering each of these factors, and taking the property as whole,¹²⁷ IOLTA programs simply cannot be deemed a taking that requires compensation.

First, the client suffers absolutely no economic loss under IOLTA. By definition, the only monies allowed to be deposited in IOLTA are those the attorney determines would not even earn a net interest. IOLTA is essentially appropriating interest from the bank, because the client would never realize any net interest. In essence, this is property the client would *never* see. All IOLTA does is pool this interest into a trust account where it can actually produce an economic benefit for society as a whole, rather than a windfall for the bank. Furthermore, the only reason the principal may accrue interest at all is due to the establishment of NOW accounts. NOW accounts allow interest to be earned on demand deposits only if the interest accruals are transferred to charitable institutions.¹²⁸ Thus, with or without IOLTA, the client would not receive a net interest payment and, therefore, the factor concerning the size of the harm weighs heavily in favor of IOLTA because the harm is absolutely nonexistent.

Second, IOLTA in no way affects the investment-backed expectations of the client because it does not decrease the value of the principal value in any way. The interest is a mere portion of the whole — namely the interest plus the principal. The interest is affected, but it does not disadvantage the client because IOLTA takes something the client would never be able to use, enjoy, or dispose of in the first place. One cannot reasonably have investment-backed expectations in interest payments to which he was never entitled. If the client is clearly not due an interest payment in any event, it is inconceivable that the client could have any legitimate expectations of entitlement to the property. The client's expectation of earning a net interest is nothing more than an abstract need, the denial of which cannot justify compensation.¹²⁹ Further, the principal amount placed in trust by the

125. *Penn Cent.*, 438 U.S. at 124, 98 S.Ct. at 2659.

126. Michelman, *supra* note 8 at 1173.

127. Considering the property as a whole is what the United States Supreme Court has explicitly stated we should do in past cases. See *Penn Cent.*, 438 U.S. 104, 98 S.Ct. 2646; *Tahoe*, 535 U.S. 302, 122 S.Ct. 1465.

128. See *supra* text accompanying note 3.

129. *Webb's*, 449 U.S. at 160, 101 S.Ct. at 451.

client is unaffected, thus allowing any investment-backed expectations in the principal to be fulfilled. Because IOLTA does not adversely affect the client's legitimate investment-backed expectations, this factor, too, must fail.

Finally, IOLTA is a program that generates over one hundred million dollars each year to fund socially beneficial services necessary to uphold "equal justice under law"¹³⁰ and the American democracy we laud. Most significantly, it funds these services from interest amounts the client would never see anyway. The beauty of IOLTA is best appreciated after considering the alternatives. Should the Court shut down IOLTA in *Washington Legal Foundation*, over one hundred million dollars in funding will be lost. Due to the importance the legal profession places on providing legal services to the underprivileged, someone or something will be forced to pick up the slack. Voluntary contributions were attempted as a funding source, and quickly proven ineffective.¹³¹ In fact, the failure to sustain an adequate funding source prompted the establishment of IOLTA in the first place. For non-lawyers, a particularly enticing alternative is assessing attorneys with the costs of providing legal services to indigents since attorneys insist upon providing the service. But this result places clients in an even worse position than IOLTA would. If attorneys' costs increase, so will the cost of acquiring legal services in general. However, this time the funding will be pulled directly from the client's pocket, not the bank's. No matter what the alternative, the client pays. But, with IOLTA, the client pays with monies he would never receive. Ultimately, the financial institution is the loser, not the client. Unquestionably, the benefits of a program that provides millions of dollars for socially beneficial programs without adversely affecting the client must outweigh the losses.

All of Michelman and *Penn Central's* factors weigh in favor of IOLTA. The client's degree of harm is minimal, if not nonexistent, because the interest transferred is interest the client would never receive. The client cannot have legitimate investment-backed expectations in interest payments to which he is not entitled. Lastly, the benefits of IOLTA outweigh the losses because IOLTA raises millions of dollars for programs that benefit the public good by making an efficient use of otherwise dormant property. Unless

130. In the first day of Constitutional Law II at the Paul M. Hebert Law Center on the campus of Louisiana State University, my professor and advisor on this case note, Paul R. Baier, began our class by stating these immortal words, informing the class that these words are etched into the Supreme Court building. This phrase served as a jumping off point for the Summer Term of 2002, and has inspired me in my journey toward an understanding of constitutional law.

131. See *supra* note 2.

conceptual severance is foolishly resurrected, IOLTA cannot be deemed an unconstitutional taking.

However, the Court may decide to use a conceptual severance analysis to conclude that IOLTA effects a taking. According to Epstein's theory of conceptual severance, the interest can be severed from the principal and considered as a property interest in and of itself.¹³² To him, the property interest at stake would be the interest alone, and any interference with that property right demands compensation.¹³³ Consequently, under a conceptual severance analysis, the appropriation of interest to IOLTA would result in a taking of all the property's beneficial uses because the property is the interest itself. Thus, if conceptual severance is applied, *Washington Legal Foundation v. Legal Foundation of Washington* would come close to falling within the realm of *Lucas* because IOLTA appropriates all of the interests' value. Because interest is calculated separately from the principal, it is easy to conceptually sever the two.

Should the Court follow the reasoning of Rehnquist and Scalia and apply a conceptual severance theory to find that there is a taking requiring just compensation, no compensation is due. A taking due no just compensation simply cannot be unconstitutional. The Fifth Amendment does not prohibit all takings, just takings without just compensation. With or without IOLTA, the client remains in the same position he was prior to the transfer because, by definition, no funds are placed into IOLTA unless they cannot earn net interest. Though the Court has deemed the interest to be property, it does not change the fact that it is property that would never be reduced to the client's possession. Further, the purpose of just compensation is to place the property owner in the same position he was in prior to the government interference.¹³⁴ Repayment for the interest appropriated to IOLTA, would place the client in a better position; thus no payment is due. Just compensation is zero, and if just compensation equates to no compensation, then there is no unconstitutional taking. To hold otherwise is a mere inconsequential abstraction.¹³⁵

Paying the client the value of his interest would put the client in a better position than he was in before the alleged taking. Requiring the government to pay the client the face value of each interest accrual would not further the compensation requirement of the Takings Clause. To pay the client the value of the interest would not only be

132. See discussion *supra* Part III, § A(1).

133. See discussion *supra* Part III, § A(1).

134. *Suitum v. Tahoe Reg'l Planning Agency*, 520 U.S. 725, 748, 117 S.Ct. 1659, 1671 (1997) (citing *U.S. v. 564.54 Acres of Monroe and Pike County Land*, 441 U.S. 506, 510, 99 S.Ct. 1854, 1856 (1979)) (stating the owner must be put "in as good a position pecuniarily as if his property had not been taken").

135. *Phillips*, 524 U.S. at 174-75, 118 S.Ct. at 1935 (Souter, J., dissenting).

costly in terms of allocation, but would also undermine the very premise upon which IOLTA stands. IOLTA makes beneficial use of otherwise dormant property, thus increasing its efficiency. Should IOLTA be required to pay for its use of the interest, the use is no longer efficient. As Justice Holmes stated in *Pennsylvania Coal*, "Government hardly could go on if to some extent values incident to property could not be diminished without paying for every such change in the general law."¹³⁶

V. CONCLUSION

The *per se* categorical approach is inappropriate for analyzing IOLTA's constitutionality. Instead, all of the pertinent factors must be considered. After an *ad hoc* consideration of all the facts, IOLTA must be upheld. A public program that utilizes otherwise dormant interest amounts to benefit the poor at no detriment to the client cannot be considered an unconstitutional taking. When just compensation is absolutely zero, there is no unconstitutional taking.

Washington Legal Foundation v. Legal Foundation of Washington is a weighty decision. The answer lies in the Supreme Court's view of constitutional property law. Justices Rehnquist, Scalia and Thomas will likely urge conceptual severance to strike down the Washington IOLTA program, and ultimately IOLTA programs everywhere. Justices Souter, Stevens, Ginsburg, and Breyer, who dissented in *Phillips* and argued that IOLTA would not effect an unconstitutional taking, will likely declare IOLTA constitutional in *Washington Legal Foundation v. Legal Foundation of Washington*. Thus, the deciding votes may lie in the hands of Justices O'Connor and Kennedy, who have shown a preference for *ad hoc* considerations and considering the property interest as a whole.

Overwhelming United States Supreme Court jurisprudence reveals an unwillingness to apply the categorical rule established in *Lucas*, culminating most recently in *Tahoe*. This preference for *ad hoc* factual inquiries, and the seeming positions of the justices on the issue bodes well for IOLTA. The Court is willing to compensate practically any physical taking no matter how minimal the intrusion, but it just is not ready to assign the same presumption in favor of intangible property takings, particularly when the transfer of interest into IOLTA does not rise to the level of a physical invasion due to the nature of the property itself. Applying the factors set forth in *Penn Central*, IOLTA simply cannot be considered an

136. *Pennsylvania Coal*, 260 U.S. 393, 413, 43 S.Ct. 158, 159.

unconstitutional taking. Whether the Court will follow these suggestions is anyone's guess. But, if efficiency and justice prevail, IOLTA will live to fight another day.

*Tara E. Montgomery***

** The author dedicates this casenote to the late Senator A. Harold Montgomery, who would have beamed at the sight of his granddaughter's name in print. Also, the author extends her thanks to Professor Paul M. Baier for not only suggesting the topic, but also for advising the author during the writing process. Finally, the author thanks her family and friends for their constant encouragement and support throughout her law school career.