Oil and Gas, Natural Resources, and Energy Journal

Volume 2 | Number 2

July 2016

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Recommended Citation

Daniel Franklin, *Voter Beware: Colorado's Ballot Initiatives and the Taking Of Private Property Under the U.S. Constitution*, 2 OIL & GAS, NAT. RESOURCES & ENERGY J. 89 (2016), https://digitalcommons.law.ou.edu/onej/vol2/iss2/3

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ONE J

Oil and Gas, Natural Resources, and Energy Journal

VOLUME 2 NUMBER 2

VOTER BEWARE: COLORADO'S BALLOT INITIATIVES AND THE TAKING OF PRIVATE PROPERTY UNDER THE U.S. CONSTITUTION

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Brief Introduction

In 2013, two municipalities in Colorado enacted moratoria on the use of hydraulic fracturing ("fracking")[1]—a technique that has been used for decades to stimulate oil and gas production from new and existing oil and gas wells. In addition to the fracking moratoria, various organizations and interest groups proposed a number of ballot initiatives relating to local regulation of oil and gas in 2014.

Colorado is one of a few states that allows its residents to amend the state constitution by popular vote. In Colorado, if enough signatures are collected in support of a ballot initiative, the initiative is placed on the ballot and submitted to a vote.[2] The oil and gas ballot initiatives proposed, among other things, gave local government regulatory authority over oil and gas operations in their jurisdictions and increased the statewide setback requirements for new wells. If approved, these initiatives would have

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1. *See Colorado Supreme Court Considers Legality of Fracking Bans*, Heartland Inst. (Feb. 18, 2016), http://news.heartland.org/newspaper-article/2016/02/18/colorado-supreme-court-considers-legality-fracking-bans.

2. *See Placing an Initiated Proposal on the Statewide Ballot*, Colo. Legislative Council, https://www.colorado.gov/pacific/cga-legislativecouncil/how-file (last visited June 28, 2016).

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amended the Colorado Constitution and seized regulatory authority from the Colorado Oil and Gas Conservation Commission.[3]

The minimum setback ballot initiatives required new wells to be drilled anywhere from 1,500 feet to 2,640 feet from occupied structures, representing a substantial increase from the current statewide 500-foot setback requirement.[4] The "local control" initiatives permitted local governments to enact more restrictive regulations on exploration and production of oil and gas than those currently enforced by the State and would likely result in outright bans on fracking. Both types of ballot initiatives would negatively affect the oil and gas sector in Colorado—and eliminating the use of fracking would eliminate virtually all economic oil and gas development in the state.

In November of 2014, Governor John Hickenlooper and United States Representative Jared Polis agreed to pull the ballot initiatives from the November ballot in an attempt to create legislative compromise.[5] Polis—who indicated the initiatives would resurface if he opposed the results of the compromise—pulled his support of the initiatives in exchange for an oil and gas task force.[6] The task force is responsible for minimizing the conflicts that occur between concerned citizens and oil and gas companies when oil and gas operations are in urban areas surrounding schools and homes.

These ballot initiatives resurfaced in January of 2016.[7] The new ballot initiatives provide for local regulation of oil and gas activity, an increase of mandatory statewide setbacks to 2500 feet, and an outright ban on fracking.[8] If these initiatives make the ballot and voters approve them, they will diminish the value of privately owned mineral rights and mineral leases held by oil and gas companies operating in the state. Voters should be aware that such measures could give rise to claims by mineral rights owners

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3. *See id.*

4. *See* Statement of Basis, Specific Statutory Authority, and Purpose New Rules and Amendments to Current Rules of the Colorado Oil and Gas Conservation Commission, 2 CCR 404-1, Cause No. 1R, Docket No. 1211-RM-04 Setbacks (Retrieved from https://cogcc.state.co.us/RR_HF2012/setbacks/FinalRules/Final_SetbackRules-StatementOfBasisAndPurpose.pdf).

5. *See* Mark Jaffe, *Hickenlooper Compromise Keeps Oil and Gas Measures off Colorado Ballot*, Denver Post (Aug. 4, 2014), http://www.denverpost.com/business/ci_26274685/hickenlooper-polis-float-colorado-oil-gas-local-control.

6. *Id.*

7. *See Colorado 2016 Ballot Measures*, Ballotpedia, https://ballotpedia.org/Colorado_2016_ballot_measures (last visited June 28, 2016).

8. *Id.*

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and oil and gas operators under the "takings clause" of the Fifth Amendment of the U.S. Constitution. Such claims could result in cities, counties and the State being liable for billions of dollars in damages, and at the very least, years of costly litigation.

Overview of the Takings Clause

The last clause of the Fifth Amendment—which applies to state governments via the Due Process Clause of the Fourteenth Amendment[9]—says, "nor shall private property be taken for public use, without just compensation."[10] When either federal or state governments appropriate private property for the benefit of the public, the takings clause requires them to justly compensate property owners. There is no language in the takings clause that excludes the clause from applying to oil and gas mineral interest. On the contrary, "private property" is a broad concept and undoubtedly covers mineral interests and other property rights in realty.

The Supreme Court has repeatedly acknowledged that it has not provided clear-cut guidelines for determining when a taking occurs,[11] so determining whether government action amounts to a taking in violation of the Fifth Amendment is often an uncertain process. The most rudimentary form of taking occurs when the government physically intrudes upon or permanently occupies private property for the benefit of the public.[12] But, not all takings claims involve the physical seizing of private property.

Regulatory Takings: Total and Partial Economic Loss

Fracking bans and minimum setback requirements do not physically deprive mineral rights owners or oil and gas companies of property. Rather, the proposed ballot initiatives will severely limit the use of private property under the guise of a public benefit. These initiatives, therefore, fall into a second category of taking known as a "regulatory taking."

Regulatory takings can occur in two ways. A *Lucas* taking occurs when laws or regulations deny property owners of economically viable use of property—rather than a physical taking of property.[13] Jurisprudence

9. Webb's Fabulous Pharmacies, Inc. v. Beckwith, 449 U.S. 155, 160 (1980).

10. U.S. Const. amend. V.

11. *See, eg.,* Connolly v. PBGC, 475 U.S. 211, 224 (1986); Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419, 426 (1982); Penn Cent. Transp. Co. v. New York City, 438 U.S. 104, 124 (1978).

12. *See* Loretto, 458 U.S. at 427.

13. Lucas v. S.C. Coastal Council, 505 U.S. 1003, 1016 (1992). See also Keystone Bituminous Coal Ass'n v. DeBenedictis, 480 U.S. 470, 497 (1987).

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suggests that regulations are not takings unless there is a substantial—nearly complete—loss of economic value of the property.[14] Under *Penn Central*, if a regulation places economic limitations on property but does not eliminate all economically beneficial use, the regulation still may be a taking.[15] This depends on a variety of factors, such as the extent to which the regulation interferes with reasonable investment backed expectations.[16] If a court finds that regulatory interference *goes too far*, the property owner will be compensated.[17]

Obviously, not all laws that reduce property value give rise to a taking. The general rule is that property may be regulated to a certain extent, but if the regulation goes too far—based on a factual inquiry—it will amount to a taking.[18]

Lucas Taking: Total Economic Loss

In *Lucas v. South Carolina Coastal Council*, the Supreme Court considered whether a law that resulted in complete diminution of David Lucas's property value resulted in a taking under the Fifth Amendment. In the case, Lucas purchased two coastal lots in South Carolina.[19] Thereafter, the South Carolina legislature enacted the Beachfront Management Act, which prohibited Lucas from constructing any habitable structure on his property.[20]

Lucas filed suit in the South Carolina Court of Common Pleas against the South Carolina Coastal Council, the regulatory agency responsible for implementing South Carolina's coastal zoning laws.[21] Lucas claimed that the statute's application to him was a Fifth Amendment taking, and that he was therefore entitled to just compensation.[22] The trial court agreed with Lucas because the statute rendered Lucas's property interest "valueless" and ordered the state to pay Lucas a substantial judgment.[23] The South Carolina Supreme Court reversed the trial court, finding that the Beachfront

14. *See, e.g.*, Jafay v. Bd. Of Cnty. Comm'rs, 848 P.2d 892, 901 (Colo. 1993)(en banc).
15. Penn Cent. Transp. Co., 438 U.S. at 124-25.
16. *Id.* at 124.
17. Pa. Coal Co. v. Mahon, 260 U.S. 393, 415 (1922).
18. *Id.*
19. Lucas, 505 U.S. at 1006.
20. *Id.* at 1007.
21. *Id.* at 1009.
22. *Id.*
23. *Id.*

Management Act's objective of preventing public harm as a result of beach erosion was within the nuisance exception to takings clause liability.[24]

The Supreme Court expressly rejected the nuisance theory used by the Supreme Court of South Carolina, stating that "it becomes self-evident noxious-use logic cannot serve as a touchstone to distinguish regulatory 'takings'—which require compensation—from regulatory deprivations that do not require compensation."[25] The Court further stated that "the legislature's recitation of a noxious-use justification cannot be the basis for departing from our categorical rule that total regulatory takings must be compensated."[26] The court ultimately solidified a rule requiring payment for regulations that deny property owners all economically beneficial use of their property for the benefit of the public[27] and remanded the case to the South Carolina Supreme Court to determine whether the Beachfront Management Act constituted a taking of Lucas's property by completely extinguishing Lucas' ability to realize any beneficial economic use from the property.[28]

Colorado may be exposed to a *Lucas* claim if the public enacts the ballot initiatives. The Supreme Court's *Lucas* decision requires compensation when a regulation deprives a property owner of *all* economically beneficial use of his or her property.[29] If sued, the state would likely argue that no *Lucas* taking has occurred since fracking bans do not impede a company's ability to drill conventional vertical wells on their leasehold. Any diminution in value, therefore, is not a loss of *all* economically beneficial use of the property as required by *Lucas*. Landowners, however, will argue that outright fracking bans destroy *all* economic value of their mineral rights because fracking is the only available method to recover oil and gas in economic quantities. Oil and gas companies—who can only derive economic gain from the production of oil and gas—might also argue that fracking bans create a total loss of the economic value of their leases because conventional drilling cannot produce hydrocarbons in paying quantities. If these points prove true, a ban on fracking likely constitutes a taking and it is a violation of the Fifth Amendment to disproportionately burden a few private citizens—instead of the public as a whole—with the cost of governmental action intended to benefit the public.

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24. *Id.* at 1009-10.
25. Lucas, 505 U.S. at 1026.
26. *Id.*
27. *Id.* at 1015-17.
28. *Id.* at 1031-32.
29. *Id.* at 1016.

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The State will likely counter this argument with the parcel-as-a-whole rule. When evaluating the merits of a takings claim, courts generally do not divide a parcel of land into separate distinct property rights to determine if a property owner has been deprived of economical use of a particular piece or segment of ownership.[30] Rather, when determining whether a government action is a taking, courts focus on the extent of the interference with rights in the *parcel as a whole* instead of viewing the individual property right being limited.[31] A regulation that eliminates one "strand" in an entire bundle of property rights may not be a taking if the owner can still put the land to other economically beneficial uses.

For example, a mineral rights owner would face an obstacle in a takings claim against a municipality that bans fracking. The city could argue that the ban only affects one piece of the entire bundle of property rights—the subsurface mineral rights. The surface owner retains its economically viable use for housing or agriculture.

On the other hand, the Supreme Court has expressed concern with the logic of the parcel-as-a-whole rule.[32] Moreover, several courts have held that mineral rights are distinct parcels for takings purposes if the mineral owner acquired those rights separately from other property interests.[33] This is usually the case in Colorado, where mineral rights in oil and gas are typically "severed" and acquired separately from surface ownership.

In *Whitney Benefits, Inc. v. United States*, Whitney Benefits and Peter Kiewit Sons' Co. ("Whitney Benefits") owned coal-bearing property in Sheridan County, Wyoming.[34] In 1977, Congress enacted the Surface Mining Control and Reclamation Act ("SMCRA"), which Whitney Benefits claimed amounted to a taking of their property[35] because the SMCRA prohibited surface coal mining on their property.[36]

In the case, Whitney Benefits applied for a strip mining application with the Wyoming Department of Environmental Quality,[37] which was

30. *See* Keystone, 480 U.S. at 497; *See also,* Penn Cent. Transp. Co., 438 U.S. at 130-31.

31. *Id.*

32. *See* Lucas, 505 U.S. at 1016-17, (Footnote 7).

33. State ex rel. Shelly Materials Inc., v. Clark Cnty. Bd. Of Commr's., 115 Ohio St.3d 337, 344 (2007); *See also* Cane Tenn., Inc. v. United States, 54 Fed. Cl. 100, 108 (Fed. Cl. 2002) (distinguishing severed coal rights from unsevered coal rights when performing a regulatory takings analysis).

34. 752 F.2d 1554, 1555 (Fed. Cir. 1985)

35. *Id.*

36. *Id.*

37. *Id.*

subsequently denied.[38] Whitney Benefits promptly filed suit in the United States District Court for the District of Wyoming.[39] The principal issue in the case was whether the Claims Court correctly concluded that SMCRA's "prohibition of surface mining of alluvial valley floors was a taking of the Whitney Benefits coal property."[40]

After several years of costly litigation, the United States Court of Appeals for the Federal Circuit affirmed the lower court's award of sixty million dollars to the plaintiffs.[41] The court of appeals held that the prohibition of mining in a particular tract of land—where the only property interest the plaintiff owned in the tract was the right to surface mining—was a total taking because the regulation wholly destroyed the economic value of the plaintiff's property without just compensation.[42]

The aforementioned cases support "total takings" claims by mineral rights owners and oil and gas companies if the proposed ballot initiatives result in fracking bans or moratoria. Total takings claims based on increased setback requirements may be more difficult. If setbacks are increased it will still be possible to drill in some cases, even though the number of wells on the mineral leasehold may be significantly reduced. Because it may still be possible to drill, the increased setback may not effectuate a total taking of the economic value of a mineral interest or oil and gas lease. Additionally, because of the parcel-as-a-whole rule, it may be an uphill fight for landowners to prevail under the total takings analysis if they own the entire parcel, including the un-severed mineral rights, because increased setbacks would not affect their ability to utilize the parcel for other economic ventures. But, in light of the Supreme Court's contempt for the parcel-as-a-whole rule and cases like *Whitney Benefits* that require just compensation for regulations that destroy the economic value of mineral estates, landowners and oil and gas operators have strong arguments for *Lucas* claims.

Partial Regulatory Takings

If a claim is unsuccessful as a total taking under *Lucas*, mineral rights owners and oil and gas companies may still have "partial" takings claims if the regulation "goes too far." Whether a partial taking has occurred depends mostly on specific circumstances in a particular case. After *Penn Central*

38. *Id.*
39. *Id.* at 1156.
40. Whitney Benefits, Inc. v. United States, 926 F.2d 1169, 1170 (Fed. Cir. 1991).
41. *See id.* at 1178.
42. *Id.* at 1177.

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Transportation Company v. City of New York, courts generally balance the economic impact of the regulation, the regulation's interference with investment-backed expectation, and the character of the governmental action.[43]

In *Penn Central*, the Court noted that Grand Central Terminal "is one of New York City's most famous buildings. Opened in 1913, it is regarded not only as providing an ingenious engineering solution to the problems presented by urban railroad stations, but also as a magnificent example of the French beaux-arts style."[44] In 1967, the New York City Landmarks Preservation Commission, after a public hearing on the issue, designated the terminal as a landmark.[45] This meant that any alterations to the building's exterior or architectural features would require Commission approval.[46]

In 1968, in an effort to generate supplemental income, Penn Central entered into a fifty-year lease and sub-lease agreement for the construction of either a fifty-five-story office building above the terminal or a fifty-three-story office building that would require some alterations to the terminal.[47] Both parties agreed that the building would meet all zoning and safety requirements not connected with historic preservation.[48] Despite this fact, the Commission elected to preserve the terminal and its landmark status and rejected Penn Central's application on the grounds that both plans were an "aesthetic joke."[49]

Penn Central filed suit in the Supreme Court of New York arguing that the Landmarks Preservation Law as applied to them appropriated their property without "just compensation in violation of the Fifth and Fourteenth Amendments."[50] The New York Supreme Court agreed and granted declaratory and injunctive relief to Penn Central.[51] On appeal, the New York Supreme Court, Appellate Division, reversed.[52] The United States Supreme Court granted certiorari and considered three factors when determining whether the governmental action constituted a taking: (1) the economic impact of the regulation; (2) the regulation's interference with

43. *Penn Cent. Transp. Co.*, 438 U.S. at 124.
44. *Id.* at 115.
45. *Id.* at 115.
46. *See id.* at 117.
47. *Id.* at 116-17.
48. *Id.* at 115-18.
49. Penn Cent. Transp. Co., 438 U.S. a*t 117-18.*
50. *Id.* at 119.
51. *Id.*
52. *Id.*

investment-backed expectation; (3) and the character of the governmental action.[53] The Court ultimately concluded that the application of New York City's Landmark Preservation Laws had not effectuated a taking of private property because in equipoise, the character of the governmental action—promotion of the general welfare and promoting reasonable beneficial use of the landmark—outweighed the interference with investment-backed expectation and the economic impact of the law.[54]

The *Penn Central* factors are vague and often lead to an ad hoc factual inquiry. It is clear, however, that a decrease in property value, by itself, generally is not enough to amount to a taking.[55] But, oil and gas operators and mineral rights owners can make strong arguments that the initiatives constitute takings.

Mineral rights owners can claim that bans and moratoria on fracking and radical increases in statewide setbacks destroy the investment expectations in their property. Oil and gas operators—who have spent billions purchasing mineral leases and building infrastructure expecting to earn a return on their investment—would find that the number of wells they can drill is greatly reduced. When courts consider the loss of investment expectation in conjunction with the decrease in value of the mineral estates as a result of the increased setbacks, it seems clear that the proposed regulation constitutes a taking.

Conclusion

When a court decides that government action amounts to a taking, the court declares that the general public, rather than a single citizen or small group of citizens, should bear the burden of an exercise of governmental power intended to benefit the public. No set formula exists for weighing these private and public interests. If Colorado voters approve the proposed ballot initiatives on fracking or increased setbacks, mineral rights owners and oil and gas companies operating in the State will have legitimate federal constitutional claims requiring compensation for the taking of their property. Voters should be aware that if those claims are successful, the resulting billions of dollars in damages could bankrupt local governments and the State.

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53. *Id.* at 124.
54. *See id.* at 138.
55. Animas Valley Sand & Gravel v. Bd. of Cnty. Comm'rs., 38 P.3d 59, 65 (Colo. 2001).

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But, in addition to the cost of the lawsuit and the potential liability for state and local governments, voters should consider the economic impact and budgetary problems that these initiatives may cause.

> A statewide fracking ban would prove damaging to the Colorado economy, setting the state back an average of 68,000 jobs in the first five years and $8 billion in GDP. Over the long term (2015-2040), the impact of a ban would result in average 93,000 fewer jobs and $12 billion in lower GDP when compared to a baseline scenario.[56]

The resulting reduction in GDP and taxable income will likely exacerbate Colorado's burgeoning budgetary deficit.

The anti-fracking and increased setback initiatives offer little (*if any*) benefit to Coloradans and are fiscally irresponsible. When voters set aside the political factors surrounding these ballot initiatives, it is clear that these initiatives will fiscally harm Colorado if passed—even if state and local governments were to escape takings liability. The only way for state and local governments to win this zero sum game is to not play. Voter beware.

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56. Richard Wobbekind & Brian Lewandowski, *Hydraulic Fracturing Ban: The Economic Impact of a Statewide Fracking Ban in Colorado*, at 17 (Cindy DiPersio ed., 2014).

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