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LITIGATION

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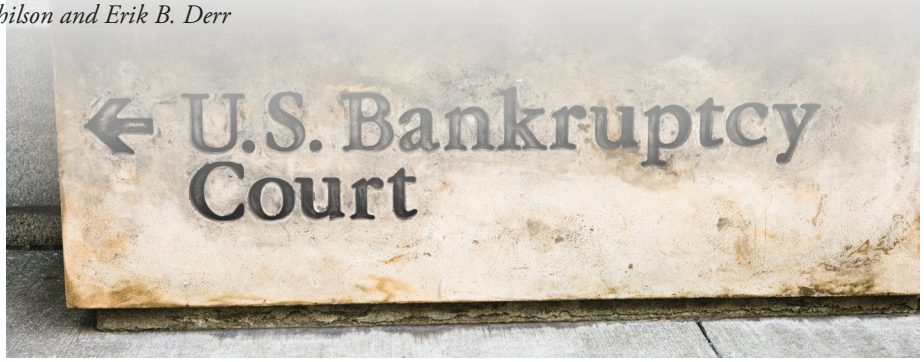
CAN BANKRUPTCY BE A TOOL TO COMBAT EMINENT DOMAIN? PROBABLY NOT

By Dana Windisch Chilson and Erik B. Derr



There are times when governments, attempting to revitalize a downtown area or conduct other operations, need to take private lands to further their purpose. To do so, they may invoke their eminent domain powers.

Conversely, property owners may attempt to protect their lands from government takings by filing for bankruptcy. Although the federal bankruptcy law provides many protections for those that utilize the law, one of the greatest assets is what is known as the automatic stay. The automatic stay, in essence, is a mandatory prohibition against creditors taking adverse actions against the debtor.

But how does a condemning entity's right to exercise eminent domain interact with a debtor's right to the automatic stay? Is bankruptcy a potential shield for debtors to protect themselves from eminent domain takings?

This issue presents a clash of federal protections granted to private debtors by Congress against the constitutional right of state governments (and certain private entities) to function effectively as independent units. Although there is no precedent in the Third Circuit, this question has been confronted in other federal jurisdictions.

Once debtors declare bankruptcy, all proceedings against them are stayed to allow time to reorganize assets and, in some instances, repay creditors. Bankruptcy courts across the country, however, have held that there are certain situations where actions against a debtor's property will not be stayed, including those initiated by the government. Under §362(b)(4) of the United States Code, the automatic stay can be lifted if the government is working to enforce its "police or regulatory power."

When will the government's eminent domain powers overcome the automatic stay of bankruptcy? Most federal courts follow the United States Supreme Court's precedent in holding that the government's eminent domain powers and police powers are coterminous and that either may be used to effectuate a taking. The minority position is that eminent domain and police powers are not the same, and thus government takings of a property owner in bankruptcy may only occur when

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the government entity is acting pursuant to "police and regulatory powers." Most courts, however, agree that if a government taking is framed within the scope of being a "police or regulatory power," it can overcome a private debtor's stay of actions against property.

Courts have devised two tests to determine whether the government is acting within its "police or regulatory powers:" the pecuniary interest test and the public policy test.

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The pecuniary interest test analyzes whether the government is acting for a pecuniary, or financial, interest, rather than in the interest of public health, safety, and welfare. If the government is acting purely in its financial interest, the stay will not be lifted. If it is acting for the public benefit, the stay will be lifted and the debtor's lands will be subject to condemnation. If the debtor can show that the government is not acting to advance the general welfare, health, or safety of the public, the presumption is that there is a pecuniary interest and the stay will not be lifted, thereby protecting the debtor's property.

The public policy test determines whether the government is acting to protect public or private rights. If the government is acting pursuant to its quasi-legislative or quasi-executive powers to enforce a public interest, the stay will be lifted. But if the government entity is acting in a quasi-judicious manner to resolve a private dispute, the stay will not be lifted.

So how are these tests applicable to eminent domain actions against private debtors? Debtors declaring bankruptcy will want to argue against having the automatic stay lifted by claiming that the government is acting with a pecuniary interest. If the reasons listed by the government for the taking do not cite public health, welfare, or safety, the taking is not likely to succeed and the stay will remain in effect, effectively thwarting the condemning entity's eminent domain power.

In practice, though, the umbrella of public health, safety, or welfare covers many broad government purposes. Historically, it has not been difficult for the government broadly to state its purposes in taking private property as an effort to protect the public health, safety, or welfare. Because the government has the ability to state its purpose broadly within these terms, seeking shelter from government action against private property under the shield of bankruptcy is not likely to be a successful strategy.

For example, in the recent Bankruptcy Court decision from Alabama *In re Bevelle*, a debtor owned property that the local county government sought to condemn for purposes of constructing a new courthouse. The landowner argued that because he declared bankruptcy, he was protected by the automatic stay and the county could not use its eminent domain powers to take the property. The court conducted a two step analysis. First, following United States Supreme Court precedent, it held that eminent domain fell under the "police and regulatory powers" exception. Second, the court found that the new facility would advance the public health, safety, and welfare because the old courthouse was unable to conform to modern safety standards. The stay was therefore lifted.

The eminent domain process can be riddled with issues such as the ones presented to the Court in *In re Bevelle*. The attorneys at McNees Wallace & Nurick can assist both landowners and condemning entities in navigating these tricky areas. ■

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FINDING THE FACTS BEFORE THE LAWSUIT BEGINS: PRE-COMPLAINT DISCOVERY IN PENNSYLVANIA

By James J. Franklin and Erik B. Derr

You find yourself either facing the prospect of litigation or already embroiled in litigation. You want to discover information about the opposing party, the issues involved in the litigation, or your odds of success in litigation. Under what circumstances and through what procedures may you discover such additional information before you advance further into litigation?

When a party suspects that it is about to become involved in litigation, or when it has recently become involved in litigation, it is common for that party to want to obtain and learn additional information as soon as possible. Courts, however, have very specific and varying rules governing when and to what extent a party may engage in this discovery. Accordingly, whether pre-complaint discovery will be available will depend on several factors.

The answer first depends on whether litigation has already commenced, and, if so, how it was commenced. If litigation has not yet commenced, then usually a party will not be able to use the power of the courts to discover information about a potential adverse party or a potential litigation issue. This especially is true in Pennsylvania's state courts. Of course, the party always may resort to searching publicly-available information, or approaching the adverse party to voluntarily provide or exchange information. The former approach, however, may not provide the information that the party seeks, while the latter will be a business and strategic decision, as doing so may tip the party's hand as to its potential claims.

A potential exception, exists in both federal courts and Pennsylvania state courts; but the potential exception is narrow. Where the prospective claim could be brought in federal court, Federal Rule of Civil Procedure No. 27(a) provides the circumstances and procedures under which a party may pursue discovery against another party before filing any legal action. The party, however, must first provide specific information to the court, provide notice to all interested parties, and obtain the court's approval. Normally, the court will only approve the request for discovery prior to filing a complaint where there is a substantial danger of evidence being lost or destroyed; this is a high burden to overcome. Even if the burden is overcome, the rule may limit the pre-complaint discovery to a deposition. Pennsylvania Rule of Civil Procedure No. 1532 provides for a similar procedure.

If a lawsuit has commenced, the answer then depends on how the plaintiff commenced the lawsuit. If the plaintiff filed a complaint, then, generally speaking, either party may serve discovery requests, including but not limited to interrogatories, requests for production of documents, and requests for admission, on a wide range of topics. The procedure will be similar in both federal courts and Pennsylvania state courts. In Pennsylvania state courts, however, a plaintiff may also start a lawsuit by filing a writ of summons, which simply notifies the opposing party of the lawsuit and contains little factual information other than the name of the parties and the court.

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Upon the proper filing of a writ of summons, Pennsylvania Rule of Civil Procedure No. 4003.8 permits a plaintiff to serve discovery before filing a complaint; much like pre-complaint discovery in federal court. However, the permitted discovery is narrow in scope. In other words, a plaintiff will not have free reign to seek any and all information that they desire before filing a complaint. Instead, Rule 4003.8 limits the plaintiff to information that is necessary to file a complaint. Pennsylvania state courts usually interpret this limitation to mean identifying information, such as the name of a party, company, or key witness. Therefore, a plaintiff likely will be unable to gather other, potentially useful, information before filing a complaint, e.g. information as to insurance coverage, liens, defenses to potential claims, etc. Lastly, even if the pre-complaint discovery requests only include identifying information, the adverse party may object to the discovery requests and seek the court's protection. In that case, the requesting party would have to convince the court that the requests seek only necessary information and that the requests would not cause substantial burden, annoyance, oppression, or embarrassment to the opposing party.

Overall, once a plaintiff has filed a complaint, all parties to that litigation will have a broad range of tools at their disposal to discover a wide range of information about the other parties and the issues involved in litigation. Without a complaint, whether in federal or Pennsylvania state court, a party may still conduct discovery through the legal system to learn useful information, but the courts and rules will strictly control and limit the timing, scope, and method of such discovery. As a result, while pre-complaint discovery can be beneficial, there are many detailed procedures and restrictions on it, and a party may ultimately find itself unable to obtain all of the information that it desires without first filing a complaint. If you find yourself contemplating pre-complaint discovery, then it is essential that you follow the pertinent federal, state, and local rules. The litigators at McNees Wallace & Nurick are available to counsel parties with potential claims on how to find critical information necessary to determine whether and how to pursue litigation. ■

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