Rent Control in the New Lochner Era

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CONTENTS

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I.
INTRODUCTION

Housing is one of the necessities of life.[1] It also comprises a large share of most Americans' disposable income. Unlike other consumables, competition in supply and demand does not result in effective market restrictions on price. First, there is a limited supply of housing. The limit is both natural (there is a finite amount of land) and artificial (zoning restrictions limit housing supply). Second, consumers of rental housing do not have the same market power as do consumers of other goods. This is principally because substituting one product or brand for another, say at lease renewal time, exacts a high transaction cost — the considerable expense and inconvenience of relocating. Since rental housing is not fungible, each landlord is a demi-monopolist.[2] This is not meant as a pejorative, only to describe the owner's market power.

The absence of a free market in rental housing (at least in an idealized sense) often leads to exploitation by housing providers. This is especially true in times of economic stress, when the nation's resources are devoted to more pressing needs (*e.g.*, wartime), or during periods of high inflation and real estate speculation. It is during these times that government policy makers often consider restrictions on rent increases and other forms of tenant protection.[3]

Of course, there are other means to overcome market inefficiencies in housing. Tax and cash subsidies can encourage housing production or assist with rent payments. Zoning incentives can do likewise. But federal and state governments are not as concerned with housing as they once were; the issue is currently perceived as one of local concern. As a result, municipalities are left holding the bag, so to speak, with a dwindling arsenal of regulatory means available to them in addressing housing shortages. Rent control is one of those still-remaining means.

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1. *Block v. Hirsch*, 256 U.S. 135, 156 (1921).

2. *Id.* at 156 (rental housing is "necessarily monopolized in comparatively few hands"). Findings to this effect can be found in rent control laws. *See, e.g.*, Ventura Mobile Home Park Rent Stabilization Ordinance, noting a "virtual monopoly [exists] in the rental of mobile home park spaces" (quoted in *Ventura Mobilehome Commun. Owners Ass'n v. City of San Buenaventura*, 371 F.3d 1046, 1048 (9th Cir. 2004)). See also HOUSE AND HOME, Aug. 1960, at 126 (quoting Winston Churchill referring to landlords as "land monopolists").

3. For instance, nearly 100 California cities currently have rent control, many for mobilehome parks.

Rent controls were first enacted in the United States during World War I. Since then, the Supreme Court has considered the constitutionality of rent control at least a dozen times, upholding the challenged law on every occasion save one.[4] It is somewhat remarkable that even during periods of extraordinary judicial protection of property rights, rent control laws have nonetheless survived. This was true in the *Lochner* era,[5] as well as during the modern resurgence of property rights activism, at least at the Supreme Court.

Despite long-standing judicial acceptance of rent regulation, the attack on rent control has been unrelenting. For some reason, rent control triggers greater emotional and ideological opposition than do most other forms of economic regulation. Virtually every constitutional theory has been tried. Most challenges are based on the takings and due process clauses, but the contracts clause[6] and even the first[7] and thirteenth amendments[8] and equal protection[9] have made their way into the opinions. Creative statutory claims have also been mounted, such as the argument that rent control is an illegal form of price fixing.[10]

This article deals principally with takings clause challenges to rent control. There is some discussion of due process issues because they are often intertwined and sometimes confused with takings claims.[11] The sections that follow focus on substantive doctrine. Although equally important, procedural issues are omitted since they are covered elsewhere.

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4. *Chastleton Corp. v. Sinclair*, 264 U.S. 543 (1924) (lower court could consider whether emergency conditions, used as a predicate for the 1922 Rent Law, still existed).

5. *Lochner v. New York*, 198 U.S. 45 (1905).

6. *Edgar A. Levy Leasing Co. v. Siegel*, 258 U.S. 242 (1922).

7. *See Thomas v. Anchorage Equal Rights Commission*, 165 F.3d 692 (9th Cir. 1999) (enforcement of an anti-discrimination regulation imposed a substantial burden on owners' exercise of a central religious belief or practice).

8. *See Nash v. City of Santa Monica,* 37 Cal. 3d 97, 688 P.2d 894 (Cal. 1984) (rent control and eviction law did not force landlord to remain in the apartment rental business thereby creating an involuntary servitude).

9. *See Santa Monica Beach v. Santa Monica Rent Control Bd.*, 968 P.2d 993, 1045 (19 Cal. 1999) 4th at 1031 (Brown, J., dissenting) (rent control was likely unconstitutional because of "*distributive inequality*." A small (apparently politically powerless) segment of society — property owners — has been singled out to bear public burdens) (original emphasis).

10. *See Fisher v. Berkeley*, 475 U.S. 260250 (1986) (rent control does not violate the Sherman Act).

11. For a good discussion of the difference between due process and takings doctrines in the context of rent control, *see Kavanau v. Santa Monica Rent Control Bd.*, 941 P.2d 85116 Cal. 4th 761 (1997).

II.
RECENT DEVELOPMENTS

The Supreme Court has upheld every rent control law it has faced since 1922. Yet, takings doctrine has undergone major changes in recent years. While these developments typically occur in land use cases, lower courts are often asked to apply them to rent control. While evolving doctrine must be applied, lower courts often reach wrong results. One can speculate why that is so, and why Supreme Court review is often needed to correct misunderstandings of takings law. Perhaps it is the shifting ideology of federal judges, or their views on the balance of power between the judicial and legislative branches. Whatever the reason, what was once thought to be a settled issue, has moved back onto the front burner of judicial activism.

Two takings issues have emerged in recent years that deserve special attention in the context of rent control. They are briefly described in this overview section, and receive detailed attention below. First, is the notion of fractional or partial takings – if an owner's property interest can be conceptually divided into component parts, and her interest in any of those parts is found to have been completely extinguished, then a partial taking has occurred. Thus, if the difference between regulated and market rents (the consumer's saving due to price regulation) is a distinct property right, then rent control fully takes that component. This notion gained currency in a series of Federal Circuit takings cases, and applied to rent control in *Hall v. Santa Barbara*.[12] But, it was firmly rejected by the Supreme Court in *Tahoe-Sierra Pres. Council v. Tahoe Reg'l Planning Agency*.[13]

The second recent development in takings doctrine is the standard of review a court should use when examining the constitutionality of property regulation. Until recently, the Supreme Court had articulated two significantly different standards similar to those used in due process cases – strict scrutiny and rational basis. The former applied to possessory takings (*e.g.*, government occupation of land) and categorical takings (regulations that deprived all viable use). In these cases, no degree of justification can exempt the state from paying just compensation for taking all meaningful value from the owner. The deferential standard was used in all other takings cases, since it was not ordi-

12. 833 F.2d 1270 (9th Cir. 1987).
13. 535 U.S. 302, 331 (2002).

narily a judicial function to second-guess the reasonableness of a legislature's economic judgments and adjustments.

A third category of takings cases emerged starting in the late 1980s. These involved the granting of conditional land-use permits, where government required concessions from owners (such as easements) in exchange for discretionary permits. In *Nollan v. Calif. Coastal Comm'n*[14] and *Dolan v. Tigard*,[15] the Supreme Court held that the use of conditional permits carried a risk that government could withhold discretionary permissions as a way of exacting unrelated property rights from owners. Hence, the standard of review was elevated in this category, to require that regulation "substantially advance" underlying state interests. This heightened scrutiny, in conditional permit cases, is consistent with the "unconstitutional conditions" doctrine, which prevents the state from using its largesse (discretionary benefits and permits) to force people to relinquish constitutional rights.[16]

As originally developed by the Supreme Court, the "substantially advance" requirement was to be applied to a narrow category of takings cases – those involving ad hoc conditions on discretionary permits. However, some lower courts began to broaden this use of heightened scrutiny, and apply it to rent control cases, where no discretionary permitting is involved. The Ninth Circuit lead the charge in elevating the standard of review, finding that some features of rent control failed to "substantially advance" legitimate state interests, and therefore caused a regulatory taking.[17]

There were three serious and related problems with the "substantially advance" test, which had its roots in the substantive due process regime of the *Lochner* era. First, it conflated the takings and due process clauses. The former is intended to prevent severe economic impacts on property, unless government pays for the resulting loss. The latter is designed to prevent arbi-

14. 483 U.S. 825 (1987).

15. 512 U.S. 374 (1994).

16. For instance, the state could not demand that you relinquish your first amendment rights in exchange for a building permit or zone change, even where it might be able to deny the permit or change outright. Similarly, it cannot demand that you cede a portion of your property to the state as a condition for receiving a discretionary permit, unless the condition is substantially related to the regulatory purpose behind the permitting scheme. *See infra* at 33.

17. After submission of this article, the Supreme Court decided *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 2655, which held that heightened review under the "substantially advance" prong was inappropriate in most takings cases.

trary and capricious government action. One cannot bring a due process claim if the more explicit takings clause would apply.[18] Moreover, the repudiation of economic substantive due process generally should apply equally to rent control as to other economic regulation. But, by merging it into the takings clause, activist courts found cover to resurrect *Lochner.*

Second, it put courts in the business of making normative judgments as to which state interests were important enough to protect with economic regulation. Thus, in *Cashman v. Cotati,*[19] the Ninth Circuit apparently thought that maintaining affordable housing for incoming tenants of mobilehome spaces was an important interest, but protecting the investments of outgoing tenants was not.[20] Third, it required courts to make economic judgments about the efficacy of particular regulatory schemes. *Cashman* also illustrates this point. The court held that vacancy control (maintaining regulated rent levels for new tenants) would not in fact benefit incoming tenants of mobilehome parks because they would be paying a rent premium as part of the purchase price of the mobilehome. "Unlike ordinary rent control ordinances, an ordinance that permits incumbent tenants to capture a premium based on the present value of the reduced rent fails to substantially advance a state's interest in creating or maintaining affordable housing."[21] The court rejected out of hand the district court's finding that no such premium existed. Unless the rent control law, on its face, prohibited the creation and capture of such a premium, the court held, the state must prove the impossibility that such a premium could occur.[22]

These standards, which the Ninth Circuit created without theoretical or precedential support, pretty much doomed mobilehome rent control. As during the *Lochner* era, they effectively transferred from the legislature to the courts the business of making economic policy. But as the Supreme Court admon-

18. *Armendariz v. Penman,* 75 F.3d 1311 (9th Cir. 1996).

19. 374 F.3d 887 (9th Cir. 2004).

20. *See also Pennell v. San Jose,* 485 U.S. 1, 15 (1988) (Scalia, J., dissenting) (unconstitutional to consider tenant hardship as a criterion in determining rent increase). *But see Carson Harbor Village Ltd. v. City of Carson,* 37 F.3d 468, 472 (9th Cir. 1994), *overruled by* 104 F.3d 1133 (protecting investments of existing mobilehome tenants was legitimate state goal).

21. 374 F.3d at 896.

22. *Id.* at 898-99. *See Chevron USA, Inc. v. Lingle,* 363 F.3d 846, 849 (9th Cir. 2004) ("application of the 'substantially advances' test is appropriate where a rent control ordinance creates the possibility that an incumbent lessee will be able to capture the value of the decreased rent in the form of a premium").

ished in *Duquesne Light Co. v. Barasch*,[23] "[t]he economic judgments required in rate proceedings are often hopelessly complex .... The Constitution is not designed to arbitrate these economic niceties." Except, apparently, in rent control cases.

III.

THE TAKINGS CLAUSE

The landlord-tenant relationship is a hybrid.[24] At common law, tenancy was considered an estate in land; hence early analysis relied on property law doctrines. Modernly, a lease is viewed as a form of contract, and proceeds to analysis under contract law. Rent control cases thus use doctrinal rules from both areas, as well as a third – rate regulation. Other than the fact that land is involved, rent control is no different than other forms of price control. Constitutional doctrines under the takings and due process clauses used in utility rate regulation are also applied to rent control.

Because rent control is an amalgam of land use regulation and price control, the law is often murky. This is compounded by courts' frequent failure to delineate the precise constitutional theory involved. They often use takings and due process theories interchangeably, and have even created a synthesized term - "confiscation" - which masks underlying theory.

The fifth amendment protects property in two ways; against unreasonable regulatory interference and against expropriation. The former is stated in the due process clause;[25] the latter in the takings clause.[26] While the takings clause may have been intended to deal solely with the government's exercise of its eminent domain power (expropriation), rather than its police power (regulation), it was early applied to both. The theory is that regulation that "goes too far"[27] ought to be treated as the functional equivalent of eminent domain, albeit by "inverse condemnation." This extension, however, requires courts to determine exactly when regulation becomes condemnation; *i.e.*, just how far is

23. 488 U.S. 299, 314 (1989).

24. *See Lindsey v. Normet*, 405 U.S. 56, 72 (1972) (recognizing the "unique factual and legal characteristics of the landlord-tenant relationship that justify special statutory treatment").

25. Fifth Amendment ("nor shall any person . . . be deprived of life, liberty, or property, without due process of law").

26. Fifth Amendment ("nor shall private property be taken for public use, without just compensation").

27. *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393 (1922).

"too far"? In other words, when has government (impermissibly) used its police power to regulate property when it should have used its eminent domain power to condemn the property and convert it to public use?

The answer to that question "depends largely 'upon the particular circumstances [of each] case.'"[28] "In engaging in these essentially ad hoc, factual inquiries, the Court's decisions have identified several factors that have particular significance. The economic impact of the regulation on the claimant,. . . the extent to which the regulation has interfered with distinct investment-backed expectations, [and] the character of the governmental action."[29]

The three *Penn Central* factors play out in several ways. The third – character of governmental action – distinguishes between two kinds of takings: possessory and regulatory. The former occurs when government occupies property; the latter when it regulates property uses. "A "taking" may more readily be found when the interference with property can be characterized as a physical invasion by government."[30] The first two factors (economic impact and expectations) are found in regulatory takings cases and are mostly fact-based. To guide the analysis, the Supreme Court has further refined the analysis into "categorical" and "non-categorical" strands, depending upon the severity of impact; the former applied to total extinction of value. Along the way there are several variations, such as regulatory exactions. Although this process results in doctrinal complexity, it may be necessary in order to provide lower courts with sufficient guidance and to respond to the nuances of modern regulation.

Before turning to possessory and regulatory takings doctrine, it is useful to mention a threshold issue – the meaning of "property." If an economic interest does not constitute property in the constitutional sense, it is not protected by the takings clause (but may be by other clauses). "Not all economic interests are 'property rights'; only those economic advantages are 'rights' which have the law back of them."[31] Moreover, "property interests . . . are not created by the Constitution. Rather, they are created and their dimensions are defined by existing rules or understandings

28. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

29. *Id.*

30. *Id.*

31. *United States v. Willow River Power Co.*, 324 U.S. 499, 502-03 (1945).

that stem from an independent source such as state law."[32] These are important points to keep in mind in reading rent control cases, since lower courts often impose their own conception of "property" rather than identify its contours according to state law.

A. *Constructing and Deconstructing "Property" in the Fifth Amendment*

Property may be an illusive concept requiring source definition when it comes to intellectual property, as in *Monsanto*, but we don't normally have such trouble when dealing with tangible property.[33] Yet even real property has contours that must be identified before engaging a takings analysis, because sometimes what is "taken" is less than the whole of a parcel or less than a fee. It may simply be an opportunity or expectation of gain. Whether an interest in property is protectable under the takings clause depends on whether it is within the owner's "reasonable 'investment-backed expectation.'"[34]

1. Background Principles

This notion of defining fifth amendment property gained currency in *Lucas v. South Carolina Coastal Council*.[35] There, the Court recognized that even total deprivation of development rights is constitutional where a proposed use would not have been permitted under pre-existing state property law. Pre-existing or "background principles" of state law inhere in an owner's title. Thus, where a regulation deprives the owner of a desired use, nothing has been taken if that use was not "sufficiently bound up with the reasonable expectations of the claimant to constitute 'property' for Fifth Amendment purposes."[36]

When it comes to rental housing, leasing the property for financial gain is invariably an expected – and protected – use. The issue becomes more complicated when the economic interest is shared between landlord and tenant. That can be the case with condominiums and mobilehomes, where land and improvements

32. *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1001 (1984).

33. *See Block v. Hirsh*, 256 U.S. 135, 155 (1921) ("that tangible property is also visible tends to give a rigidity to our conception of our rights in it that we do not attach to others less concretely clothed").

34. *Penn Cent. Transp. Co. v. City of New York City*, 438 U.S. 104, 127 (1978).

35. 505 U.S. 1003 (1992).

36. *Penn Central*, 438 U.S. at 125.

are subject to "divided ownership."[37] The Ninth Circuit first considered the issue of ground leases in *Richardson v. Honolulu*,[38] which invalidated a local ordinance giving condominium owners the right to transfer their price-controlled ground leases upon sale of their units. Landowners argued this provision allowed the tenant "to capture the present value of the below market land rent," by capitalizing it into the selling price of the improvement. The court discussed this "rent control premium" in a series of mobilehome rent control cases, most recently *Cashman v. Cotati*.[39] Mobile homes are similar to condominiums in that the structure is owned by one party while the land is owned by another. Although not quite as fixed to the land as condominiums, "mobile" homes are anything but, with few ever being moved from their first location.[40]

Because the ground tenant (structure owner) is at the mercy of the ground owner upon lease renewal, a substantial rent increase can deplete the condominium or mobile home of much or all of its value. Here's an example: suppose a new mobile home costs $50,000 at the dealer and $10,000 to move and mount on a mobile home pad. Suppose further the initial pad lease is $250 per month. Now assume there are no limits on rents and the mobilehome park owner raises the rent by $70 per month above market rents. The present value of that additional rent stream is less than the cost of moving the mobile home,[41] so the tenant would (rationally) pay it rather than move, even though the new rent was above comparable rents elsewhere. Indeed, if there were a zoning-imposed scarcity of available mobile home spaces, the ground owner could not only capture the cost of moving the home, but its replacement value as well (since an ousted tenant would have no place to move it , the mobile home would have no or negative value). In the example, the park owner could theoretically triple the rent to nearly $700 per month before the mo-

37. *See* Werner Hirsch and Joel Hirsh, *Legal - Economic Analysis Of Rent Controls In A Mobile Home Context: Placement Values And Vacancy Decontrol*, 35 UCLA L. REV. 399, 419 (1988).

38. 124 F.3d 1150 (9th Cir. 1997).

39. 374 F.3d 887 (9th Cir. 2004). The first case in this genre was *Hall v. Santa Barbara*, 833 F.2d 1270 (9th Cir. 1986).

40. For a discussion of this phenomenon, *see Galland v. City of Clovis*, 16 P.3d 130, 134-3524 Cal. 4th 1003, 1009 (2001).

41. At a discount rate of 6% over a 20 year period, the present value of a $70/mo income stream is roughly $9,800.

bile home owner would (rationally) defect.[42] Condominiums with ground leases are an even clearer example of this phenomenon – capture of structure value by ground owner – since they cannot be moved at any price. Rent control is often imposed to prevent this naked wealth transfer from tenant to landlord.

In *Richardson* and the mobile home cases, the Ninth Circuit held that the outgoing tenant's right to sell her unit on site, coupled with "vacancy control" (continuation of controlled rents upon in-place sale of the unit), had the effect of "capturing" the present value of below market future rents for the ground leases and transferring that value from landlord to tenant.[43] Although the court never discusses whether this capitalized present value (the "premium") is part of the ground owner's "property" rights in the first place, it implicitly concludes it is because the court then goes on to find a taking of property.[44]

This is a difficult economic problem. The cost of a service (ground lease) and the product that uses that service (condominium unit or mobile home) are inextricably linked, as anyone who has priced cell phones with and without 1- or 2-year service contracts can attest. Single family homes provide another example. The selling price (value) depends, *inter alia*, on current and foreseeable mortgage rates, property tax rates, insurance and utility fees, etc.

If the tax rate doubled, what effect would that have on the market value of the house? The present value of the additional tax stream would be reflected almost perfectly in the selling

42. The present value of $700 mo., at a 6% discount rate over 20 years is $60,000 — the hypothetical cost of buying another mobile home and moving it into place.

43. If rent control merely denied ground owners the ability to capture structure value or relocation costs, but otherwise permitted market rate increases, then there wouldn't be a wealth transfer in either direction. But this hypothetical scenario is unrealistic since there's no way to determine how the market would function in the absence of ground owners exploiting their ability to capture value. Perhaps cost of living increases can approximate this idealized "market rent." Indeed, many rent control laws are structured just that way. See Kenneth Baar, *The Right to Sell the "Im"mobile Manufactured Home in Its Rent Controlled Space in the "Im"mobile Home Park: Valid Regulation or Unconstitutional Taking?*, 24 URB. LAW. 157 (1992)

44. Some cases (*e.g., Hall*) hold that a rent control premium is a distinct interest in property that is taken from the land owner and given to the tenant. Other cases (*e.g., Cashman*) employ the premium construct to find that legislative goals (e.g., affordable housing) cannot be achieved. *See Ventura Mobilehome Owners Ass'n v. City of San Buenaventura*, 371 F.3d 1046 (9th Cir. 2004) for a comparison of the two approaches. In either case, if the premium is not part of the land owner's fifth amendment property rights to begin with, it is hard to see how she it has been "taken" from her.

price. This is what happened (in a reverse sense) after passage of California's Proposition 13 in 1978. Tax savings were capitalized almost immediately into selling prices and a huge boom in the housing market ensued.[45] What if Proposition 13 was repealed tomorrow and property taxes doubled to their pre-1978 rate? Housing values would plummet. Economically, this is equivalent to the state "capturing" the value of below-market tax rates, and transferring this (quantifiable) amount from the homeowner to itself.

Is that a taking? Of course not, because the "background principles" of property law in every state include the right to raise taxes. In other words, the landowner does not have a "property" right to a particular tax rate, or to the savings from reduced taxes. By extension, does the owner of a ground lease have a "property" right to capture the value of the tenant-owned improvement by charging above market rent increases?

There are two ways to answer that question. One is to do as instructed by the Supreme Court – examine pre-existing state law to determine the contour of property rights. It may very well be that the state, when it created divided estates (condominiums are a relatively recent form of land ownership) did not repose in the landowner any expectation of capturing a part of the improvement's value through rent increases or otherwise. If that's the case, then there is no property interest involved in the condominium and mobilehome rent control cases, and courts should dismiss the takings claims outright. California courts follow this approach.[46]

A second way to answer the question of property rights in mixed land/improvement ownership forms is to conclude, as a matter of law, that the aggregated future value is the land owner's exclusive property. Of course this would be an exercise in "natural law," since nothing in the constitution or other positive law defines property in this (or any other) way. This second approach has been adopted by the Ninth Circuit. The capitalized value of future rental streams, as well as the capitalized value of future rental savings (the difference between controlled and un-

45. *See* Kenneth Rosen, *The Impact of Proposition 13 on House Prices in Northern California*, 90 JOURNAL OF POLITICAL ECONOMY 200 (1982) ("each dollar decrease in relative property taxes appeared to increase relative property values by about seven dollars"). *See also* sources collected at Mary LaFrance, *Constitutional Implications of Acquisition Value Real Property Taxation: The Elusive Rational Basis*, 1994 UTAH L. REV. 817, 862, n.207 (1994).

46. *See Casella v. City of Morgan Hill*, 280 Cal. Rptr. 876, 879 (1991).

controlled rents), are both the "property" of the landowner, even where it captures part or all of the structure's value. The Ninth Circuit seems to have created a new property right, followed by its holding that "capture" by the tenant is a taking.

2. Fractional Property

Another definitional issue concerns the various dimensions of property. Property is commonly described in spatial terms (e.g., metes and bounds), but also by time and uses. If a physical slice of real property is converted to public use, say a public easement, we would analyze the impact and character of government action on that isolated piece. It is no defense to a possessory taking that some or most of the parcel remains in control of the owner. The piece taken is indeed "taken." In possessory takings cases, it does not matter whether the space "occupie[d] is bigger than a breadbox.[47]

What if the portion taken is not physically discrete, but a particular use, as when property is downzoned? Property has functional dimensions too. Is a newly forbidden use a discrete property interest that has been "categorically" (entirely) taken? The short answer is no, at least in regulatory takings cases. Because regulation, by its very nature, extinguishes an identifiable use, a concept of fractional takings would effectively prohibit all economic regulation. Regulatory "'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."[48]

A similar rule applies to rent and price controls generally. If the differential between regulated and market prices is conceived as a discrete property interest (from an owner's perspective, this value is lost to regulation), that interest is fully extinguished by the price regulation. If it were separate fifth amendment property, it would be a categorical taking. But, "defining the property interest taken in terms of the very regulation being challenged is circular,"[49] hence not part of takings law.

47. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 438, n.16 (1982).

48. *Penn Central*, 438 U.S. at 130.

49. *Tahoe-Sierra Pres. Council v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 331 (2002), quoting *Concrete Pipe & Products of Cal., Inc. v. Construction Laborers Pension Trust*, 508 U.S. 602, 644 (1993) ("To the extent that any portion of property is taken, that portion is always taken in its entirety; the relevant question, however, is whether the property taken is all, or only a portion of, the parcel in question").

Nor is property normally sliced into discrete temporal pieces. A moratorium, however short, fully extinguishes those forbidden uses while in effect. Even delay, say while a building permit was being processed, would deny all use during the interim. Yet, here too, property cannot be fractionated to yield a total taking of use and time slices.[50]

But the rejection of fractional takings theory still leaves us with the problem of defining the property interest that should be analyzed. "Because our test for regulatory taking requires us to compare the value that has been taken from the property with the value that remains in the property, one of the critical questions is determining how to define the unit of property 'whose value is to furnish the denominator of the fraction.' "[51]

Since property is generally defined by state law, it would make sense to look there to determine what interests can be severed from tangible and intangible property. Where state law recognizes a conceptually distinct interest and protects it as separate property, it would make sense for the fifth amendment to incorporate that understanding. Thus, easements on real property can be created and exchanged as separate property. Accordingly, the taking of an easement is an actionable possessory taking.[52] Leaseholds and time shares in possession of real property are also known to state law; hence occupation by the state for even a short time is a taking.[53] But the time period of regulatory delay is not a distinctly recognized property right under state law (how do you sell or exchange that?), so cannot be severed from the larger property estate for fractional takings analysis.

In short, courts ordinarily analyze property according to its state-created dimensions. Unless a part of the "background principles" of state law, courts will treat affected property interests in their whole sense, rather than as a series of fractional interests, each of which alone might be extinguished by regulatory action. "[W]here an owner possesses a full 'bundle' of property rights, the destruction of one 'strand' of the bundle is not a taking because the aggregate must be viewed in its entirety."[54]

Treating rental property as a series of fractional interests, such as the right to remain in possession or the capitalized value of

50. *Id.*
51. *Keystone Bituminous Coal Ass'n. v. DeBenedictis*, 480 U.S. 470, 497 (1987).
52. *Nollan v. Cal. California Coastal Comm'n*, 483 U.S. 825 (1987).
53. *United States v. General Motors Corp.*, 323 U.S. 373 (1945).
54. *Andrus v. Allard*, 444 U.S. 51, 65-66 (1979).

future rent savings, has been a favored tactic of rent control opponents. While it has achieved some success,[55] the Supreme Court has squarely rejected it.[56] But the urge dies hard, and remnants of the theory can be seen in recent cases from the Ninth Circuit. Instead of fractionalizing the property, the court carved up the regulatory scheme into discrete elements, and subjected them in isolation to heightened scrutiny. Once again it required the Supreme Court's intervention to set the Circuit straight.[57]

B. *Possessory Takings*

1. General Rule

Permanent physical occupation of private property by government or government-authorized third parties is the clearest example of a law that effectively transfers interest in property. Physical occupation is the functional equivalent of "ouster" of the owner.[58] Government cannot obtain by its police power what in actuality is a condemnation of fee.

a) Permanent physical occupation destroys all attributes of property ownership

Possessory takings are *per se* invalid because they destroy all attributes of ownership in the property so occupied.[59] In *Loretto*, the court held that a law which required landlords to permit cable installations on their rental properties was a permanent physical occupation. A permanent physical occupation is a taking without regard to the government or public interests involved, or the amount of property occupied (the cable facilities would have taken up 1.5 cubic feet of property). Compensation is required.

b) The right to exclude is important but not dispositive

"The right to exclude others" is "one of the most essential sticks in the bundle of rights that are commonly characterized as property."[60] In *Kaiser-Aetna*, the United States attempted to subject a private marina to a public navigational servitude. By

55. *E.g., Hall v. Santa Barbara*, 833 F.2d 1270 (9th Cir. 1986).
56. *Yee v. Escondido*, 503 U.S. 519, 527 (1992).
57. See *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 2655 (2005)
58. *Pumpelly v. Green Bay Co.*, 80 U.S. (13 Wall) 166 (1871); *St. Louis v. Western Union Tele. Co.*, 148 U.S. 92, 98-99 (1893).
59. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 435-36 (1982).
60. *Kaiser Aetna v. United States*, 444 U.S. 164, 176 (1979).

denying the owners of the marina their right to exclude the public, the government had destroyed the value associated with private use. But later cases have qualified the right to exclude. Most importantly, when a property owner voluntarily opens her property for use by others (e.g., by renting it), her right to exclude is partially waived.

(1) An Owner Who Invites Third Parties Onto Her Property For Business Purposes Cannot Claim An Absolute Right To Exclude

In *FCC v. Florida Power Corp.*,[61] the Supreme Court upheld the federal Pole Attachment Act, which regulated the rents utility companies could charge for use of their poles by others. The court held the Act was not a possessory taking. So long as the owner was not required to lease space in the first place, its right to exclude was not extinguished. "[R]equired acquiescence is at the heart of the concept of occupation. . . . it is the invitation, not the rent, that makes the difference. The line which separates these cases from Loretto is the unambiguous distinction between a commercial lessee and an interloper with a government license."[62]

Subsequently, the Pole Attachment Act was amended to require utility companies to lease space on their poles to cable companies and others. The 11th circuit held the amended Act constituted a possessory taking.[63] The taking did not violate the fifth amendment, however, because the Act established an adequate procedure for compensation.

(2) The Right to Exclude is Commonly Restricted by Anti-Discrimination Laws

A landlord's once-absolute dominion over her property has given way to a variety of common law and statutory rules restricting her use of property.[64] To some extent, these anti-discrimina-

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61. 480 U.S. 245 (1987).

62. *Id.* at 252-53. *See also Pruneyard Shopping Ctr. v. Robbins*, 447 U.S. 74 (1980) (affirming a California Supreme Court ruling requiring a private shopping center to allow individuals to solicit signatures on its property).

63. *Gulf Power Co. v. United States*, 187 F.3d 1324, 1329 (11th Cir. 1999) (because the Act "requires a utility to acquiesce to a permanent, physical occupation of its property, we conclude that the Act's mandatory access provision effects a per se taking of a utility's property under the Fifth Amendment").

64. *See, e.g.*, Civil Rights Act of 1866, (42 USC §§ 1981-1982); Fair Housing Act, (42 U.S.C. §§ 3601-3631); *Marina Point, Ltd. v. Wolfson*, 640 P.2d 115, 117 (1982).

tion laws form background principles of state property law, such that landlords who acquire property with these restrictions in place do not have a fifth amendment right to exclude for the prohibited reasons. Also, because the landlord-tenant relationship is traditionally heavily regulated, newly enacted restrictions of this form do not frustrate investment backed expectations.[65]

2. Rent Control

a) Tenant Eviction Protection

Protection against eviction is a common feature of many rent control laws. Protecting tenants from excessive rent increases may be a futile gesture if tenants can be easily evicted. Eviction protection can also exist in the absence of rent regulation.

Protecting tenants against eviction, especially after expiration of their lease term, effectively transforms their leasehold into one of indefinite duration. It obviously restricts the landlords' rights to exclude and regain possession. But, at least where the landlord retains the right to change her property from rental to private use, there is no forced occupation.[66]

In *Seawall Associates v City of New York*,[67] the court held a law requiring building owners to maintain them as Single Room Occupancy units constituted a physical taking due to the severity of the forced controls. The law required the SRO property owners to rehabilitate their buildings, make every SRO unit in the building habitable, and to lease every unit to a "bona fide" tenant at controlled rents. Further, an owner was presumed to have violated the regulation if any unit remained unrented for 30 days (anti-warehousing provision), resulting in severe fines. Since the owners were forced to accept occupation of the properties, the resulting deprivation was sufficient to constitute a physical taking.[68]

b) The Special Case of Mobilehome Protection

Mobilehome rent control presents a special case because tenants of spaces in mobilehome parks are simultaneously owners of their homes, in which they have substantial investments of

65. *Cf. Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 124 (1978).

66. *Nash v. Santa Monica*, 37 Cal. 3d 97, 688 P.2d 894 (1984). *See generally* Karl Manheim, *Tenant Eviction Protection and the Takings Clause*, 1989 WIS. L. REV. 925 (1989).

67. 74 N.Y. 2d 92, 542 N.E.2d 1059 (N.Y. 1989).

68. *Id.* 74 N.Y.2d at 102.

their own. Mobilehome owners also tend to be retired, elderly or on fixed income — groups that may need extra protection from the vicissitudes of the marketplace.

When a park tenant leaves or is evicted, she faces the prospect of removing her home, abandoning it, or selling it to the incoming tenant. The first two options may destroy the homeowner's equity in her unit. Mobilehomes are tantamount to permanent fixtures; their presumed mobility is largely illusory because of the high cost to move, and the lack of vacant spaces (many jurisdictions limit through zoning the availability of mobilehome spaces).[69]

This reality spawns two different forms of regulation— the familiar law protecting mobilehome tenants from arbitrary eviction; and the right to sell a mobile home in place to a new tenant. This latter form essentially allows an outgoing tenant to transfer her tenancy and right to possession. The Ninth Circuit thought this created a possessory taking.[70]

The issue reached the Supreme Court in *Yee v. City of Escondido*.[71] The Court ruled that an ordinance that protected tenants of mobilehome park from eviction, and gave them the right to sell their units *in situ,* did not constitute a possessory taking because the park owners voluntarily rented their land to mobile home owners. At least on the face of the regulatory scheme, owners were not compelled to use their properties as mobilehome parks. They could evict and regain possession, but just could not do so as a means of selecting new tenants. While the "right to exclude" is doubtless "one of the most essential sticks in the bundle of rights that are commonly characterized as property,"[72] the Court did not find that right to have been taken from park owners.

c) Regulating Ground Leases

Ground leases are similar to spaces in mobilehome parks in that the tenant typically owns her home and is captive to exploitive rent increases by the landlord. In *Richardson v. City &*

69. *See generally Adamson Cos. v. City of Malibu*, 854 F. Supp. 1476 (C.D. Cal. 1994); Kenneth Baar, *supra*, n. 43, at 158.

70. *See Hall v. Santa Barbara*, 833 F.2d 1270 (9th Cir. 1987). *But see Eamiello v. Liberty Mobile Home Sales*, 208 Conn. 620, 546 A.2d 805 (1988) and *Thompson v. Merlino Enterprises, Inc.*, 208 Conn. 656, 545 A.2d 1094 (1989) (upholding similar law that did not include rent control).

71. 503 U.S. 519 (1992).

72. *Id.* at 528.

County of Honolulu,[73] the City used its condemnation power to convert apartments into condominiums, transferring title to the tenant in possession upon payment of just compensation. In addition, the ordinance regulated ground rent of the newly converted units. As in *Yee*, when the owner/tenant sold her unit, the successor would also enjoy regulated rent. The ground lessor claimed this permitted the seller to capitalize the value of below-market rents, thereby transferring a discrete interest from lessor to lessee without compensation.

Yee had decided that such a feature did not constitute a possessory taking. But, according to *Richardson*, this transfer of rent savings, to the extent it vitiates any public purpose, causes a regulatory taking. This point is more fully discussed in the next section.

C. *Regulatory Takings*

The basic rule for regulatory takings was stated in *Agins v. Tiburon*[74]: a land use ordinance is constitutional unless it fails to "substantially advance legitimate state interests or denies an owner economically viable use of his land."[75]

The "viable use" standard has been the principal focus of regulatory takings claims since *Agins*. It requires an economic analysis of potential uses, comparing those permitted before the challenged regulation was enacted with those allowed afterwards. In performing this analysis, it is important to remember that not all economic interests are protected under the takings clause. In order to constitute "fifth amendment property," an interest must be one that the state recognizes and protects.[76]

The "substantially advance" prong has gained prominence in recent years as a potent weapon for challenging rent control as well as other property regulation. This analysis is essentially a remnant of economic substantive due process. Its expansion may herald a return to the *Lochner* era of judicial activism.

1. Economic Impact

Inquiry into the economic effect of a regulation proceeds along two lines. The first, called "categorical takings," is where a regu-

73. 124 F.3d 1150 (9th Cir. 1997).
74. 447 U.S. 255 (1980).
75. *Id.* at 260.
76. *See* Section IIB, *supra*.

lation leaves property without economically viable use. The latter, called "non-categorical" takings, is where the economic impact may be severe, but does not destroy all value. Both are "essentially ad hoc, factual inquiries."[77]

a) Categorical Takings

A regulation that deprives a property owner of all economically beneficial or productive use of land effects a taking requiring just compensation.[78] The Court has never actually found a taking under this standard, but has occasionally assumed deprivation of all value in order to reach other issues.

(1) Public Interest

In *Lucas,* the Court held that total destruction of value was compensable irrespective of the strength of the state's interest. There, all parties agreed that Lucas' property on an environmentally sensitive beach was an extremely valuable public resource, and that discouraging new construction in that area was necessary. However, the Court ruled that legislative actions to prevent harmful use would not relieve the State from paying just compensation. Regulations that remove all economically beneficial or productive uses (and consequently leave the property in a substantially natural state) have a heightened risk of conscripting private property for public service.

(2) Use vs. Value

In *Tahoe Sierra Preservation Council v Tahoe Regional Planning Agency ("TSPC")*[79], the District Court held (relying on *Lucas)* that property bereft of viable "uses" has been categorically taken, even if the property otherwise has value. There, a temporary moratorium prevented all development pending enactment of a comprehensive zoning plan. Although the affected properties retained significant value during the period, and some were sold, none could actually be "used" productively during the moratorium.

This is an odd result. If the premise for regulatory takings is that land use restrictions go so far as to be the functional equivalent of condemnation, then it would seem that value is the

77. *Penn Central,* 438 U.S. at 124.
78. *See Lucas v. S.C. South Carolina Coastal Council,* 505 U.S. 1003 (1992).
79. 34 F. Supp. 2d 1226 (D. Nev., 1999).

key, not use. Indeed, most cases rely on value; where "use" is the term employed, it is usually meant to describe value.

The Ninth Circuit reversed.[80] It first rejected the notion that the property should be temporally divided, treating the period of the moratorium as a distinct (and extinguished) interest. Next it held that the affected properties retained both use and value. Since neither is subject to temporal subdivision for takings purposes, the fact that the properties could be developed once the moratorium expired proved they had productive use. And of course, present value is simply a composite of future uses. So, even during a moratorium, property retains significant value and can be traded. The Supreme Court affirmed.[81]

(3) Duration

The District Court in *TSPC* also held that a categorical taking need not be a permanent one. Even a temporary restriction (in that case a planning moratorium) that denies all economically viable use is a categorical taking. Again, the distinction between use and value is critical. Property retains significant value during temporary moratoria because everyone expects some productive use to be allowed once planning is complete. Both in the economics and appraisal literature, value is based on *potential* uses as much as on present ones. Indeed, courts typically have no trouble taking planning moratoria into account in land valuations. But if, as the District Court ruled, the takings clause requires that property be developable at all times, then total use restrictions of any duration would be *per se* unconstitutional.

The Ninth Circuit and Supreme Court rejected the argument that temporary use restrictions constituted temporary takings. The issue is more fully discussed below.

b) Non-Categorical Takings

"The categorical rule would not apply if the diminution in value were 95% instead of 100%. Anything less than a 'complete elimination of value,' or a 'total loss' . . . would require the kind of [multi-factor] analysis applied in *Penn Central*."[82] Outside of the special case of "categorical takings," the Supreme Court has had considerably difficulty in defining when a regulation "goes

80. 216 F.3d 764 (1990).

81. *Tahoe-Sierra Preservation Council v. Tahoe Regional Planning Agency*, 535 U.S. 302 (2002).

82. *Id.* at 330.

too far." It has held, however, that total destruction of value is not necessary. An owner who does not suffer total destruction simply loses the benefit of the court's categorical formulation.[83] How far short of total loss will suffice is still unknown. But the Court has identified several factors that will inform the decision.

(1) Penn Central Factors

Regulatory takings cases involve "essentially ad hoc, factual inquiries,"[84] requiring "complex factual assessments of the purposes and economic effects of government actions."[85] In *Penn Central*, the Court identified several factors that have particular significance: (1) the economic impact of the regulation on claimant; (2) the extent to which the regulation interferes with distinct investment-backed expectations; (3) the character and purpose of the governmental action; (4) whether the claimant's interests constitute property for fifth amendment purposes.[86] Other factors include: (5) whether the regulation would interfere with traditional as opposed to new uses which could not have been the owner's primary expectation; (6) whether the regulation is reasonably necessary to achieve a substantial public purpose; and (7) whether the regulations provide some mitigating benefits.

(2) Rent Control

In *Kavanau v Santa Monica Rent Control Board*,[87] the California Supreme Court elaborated on the *Penn Central* factors, emphasizing that a balance of landlord and tenant interests is required in rent control cases. "[I]nquiry in any particular case is 'essentially ad hoc' and 'a question of degree [that] . . . cannot be disposed of by general propositions.'"[88] The subjectivity of takings analysis is confirmed by statements from the Supreme Court.[89]

Open-ended "ad-hoc" analysis is particularly problematic in the context of rent control, which often comes before courts un-

83. *Lucas*, 505 U.S. at 1019.
84. *Penn Cent. Transp. Co.*, 438 U.S. at 124.
85. *Yee v. Escondido*, 503 U.S. 519, 523 (1992).
86. 438 U.S. at 126.
87. 16 Cal. 4th 761 (1997).
88. *Id.* at 774 (citations omitted).
89. *See Andrus v. Allard*, 444 U.S. 51, 65 (1979) (evaluation of whether a taking has occurred calls "as much for the exercise of judgment as for the application of logic"); *Agins v. City of Tiburon*, 447 U.S. at 260-61 (the inquiry involves a weighing of public and private interests).

favorably disposed to this form of regulation. Indeed, according to *Kavanau*, the factors identified so far by the Supreme Court are neither exhaustive nor binding. Rather, "a court should apply them as appropriate to the facts of the case it is considering."[90] Almost certainly, some lower courts will seize upon this invitation to do creative constitutional analysis. At the very least, they may encounter considerable difficulty in balancing.[91] But, lest the point be overstated, most courts applying the multifactor analysis of *Penn Central*, including *Kavanau*, uphold the rent control laws before them.[92]

c) *Background Principles*

As noted earlier, a regulatory takings analysis requires a court to determine both the uses permitted after and before enactment. For instance, in *Lucas*, a recent prohibition on development left coastal property without economically viable use. This would ordinarily constitute a categorical taking unless, of course, the property could not have been put to productive use even before the law's enactment. In other words, if the value of the land was zero, both before and after the Coastal Act was adopted, no constitutional deprivation would occur.

(1) *Property is defined by state law*

Although the takings clause protects property, it does not define it. "Property interests . . . are not created by the Constitution. Rather, they are created and their dimensions are defined by existing rules or understandings that stem from an independent source such as state law."[93]

Because the state defines property in the first instance, only uses permitted when property is acquired are protected by the takings clause. For example, in *Lucas*, if the property owner would have been unable to build under common law principles existing at the time he acquired his property, he could not complain of subsequent codification of those restrictions by statute. If the property was not usable at the time of acquisition, it would

90. 16 Cal. 4th at 776.

91. *See, e.g., Guimont v. Clarke*, 121 Wash. 2d 586, 854 P.2d 1 (1993).

92. *See, e.g., Sadowsky v. City of New York*, 732 F.2d 312 (2nd Cir. 1984); *Rent Stabilization Ass'n v. Dinkins*, 805 F. Supp. 159 (S.D.N.Y. 1992); Gibbs v. Southeastern Investment Corp., 705 F. Supp. 738 (D. Conn. 1989); *Tirolerland, Inc. v. Lake Placid 1980 Olympic Games, Inc.*, 592 F. Supp. 304 (N.D.N.Y. 1984).

93. *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1001 (1984).

matter not that Lucas paid nearly $1 million for the parcel. Only "reasonable investment-backed expectations" are protected by the takings clause.[94]

Accordingly, in *Lucas*, the Supreme Court remanded to state court for determination of whether pre-existing common law would have treated Lucas' improvement of coastal property as an abatable nuisance. In which case, the use and value of his property under "background principles" would have been nearly zero.

(2) After acquired property

Until recently, it was thought that owners could not complain of property restrictions in existence at the time they acquired their properties.[95] "In legal terms, the owner who bought with knowledge of the restraint could be said to have no reliance interest, or to have assumed the risk of any economic loss. In economic terms, it could be said that the market had already discounted for the restraint, so that a purchaser could not show a loss in his investment attributable to it."[96]

This flows from the notion that not all property interests are protected by the fifth amendment. "Where the State seeks to sustain regulation that deprives land of all economically beneficial use, we think it may resist compensation only if the logically antecedent inquiry into the nature of the owner's estate shows that the proscribed use interests were not part of his title to begin with."[97]

The same rule has applied in rent control cases.[98] Presumably, the price a landlord pays for property reflects any use and rent

94. *Eastern Enterprises v. Apfel*, 524 U.S. 498, 532 (1998).

95. *See Concrete Pipe & Products v. Constr. Laborers Pension Trust*, 508 U. S. 602 (1993) (one who buys with knowledge of a restraint assumes risk of economic loss); *Ruckelshaus v. Monsanto*, 467 U.S. 986 (1984); *Carson Harbor Village Ltd. v. City of Carson*, 37 F.3d 468 (9th Cir. 1994).

96. *Loveladies Harbor, Inc. v. United States*, 28 F.3d 1171, 1177 (Fed. Cir. 1994). *Carson Harbor* approached the issue somewhat differently, holding that plaintiff lacked standing to facially challenge a law in existence when it acquired the property. 37 F.3d at 476.

97. *Lucas*, 505 U.S. at 1027. *See Avenal v. United States*, 100 F.3d 933, 938 (Fed. Cir. 1996).

98. *See, e.g., Fragopoulos v. Rent Control Bd. of Cambridge*, 408 Mass. 302, 308 (1990) ("government is not required to compensate an individual for denying him the right to use that which he has never owned"); *Loeterman v. Brookline*, 524 F. Supp. 1325, 1329 (D. Mass. 1981) (owners who purchased newly-converted condominium after effective date of condominium conversion ordinance precluding the

limitations that exist at the time of purchase. As a result, she cannot complain that those restrictions were unconstitutional.[99]

This area of takings law was thrown into disarray by the Supreme Court's decision in *Palazzolo v. Rhode Island.* [100] Palazzolo succeeded to ownership of a coastal wetlands property after the corporation that had acquired it, of which he was sole shareholder, had its charter revoked. In between the corporation's acquisition and his succession to title, the state prohibited the filling of coastal wetlands. The Rhode Island Supreme Court held that Palazzolo could not challenge the intervening regulation since development was precluded by "background principles" in his title, which undermined any investment-backed expectations.

Without calling into question these basic principles, a sharply divided Court held they could not automatically bar challenges to regulations enacted prior to acquisition. "[A] regulation that otherwise would be unconstitutional absent compensation is not transformed into a background principle of the State's law by mere virtue of the passage of title. . .. A law does not become a background principle for subsequent owners by enactment itself."[101]

The justices sharply disagreed over the significance of restrictions already in place when property is acquired. Justice Stevens thought that property owners lacked standing to assert claims of their predecessors. It is inconsistent to treat a pre-sale regulation as compensable taking of property, but then hold that a later transfer of title conveyed the full estate, so that the new owner could claim *her* property was taken.[102] Justice O'Connor also thought that acquisition of title after enactment of the challenged law remained a relevant consideration in the multi-factored *Penn Central* analysis. "[I]nterference with investment-backed expectations is one of a number of factors that a court must examine. Further, the regulatory regime in place at the time the claimant acquires the property at issue helps to shape the reasonableness

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eviction of existing tenants continuing to occupy the apartment had "no legitimate expectation of occupying the unit themselves").

99. *Creppel v. United States*, 41 F.3d 627, 632 (Fed. Cir. 1994) ("[i]n such a case, the owner presumably paid a discounted price for the property. Compensating him for a "taking" would confer a windfall"). *See also Flynn v. City of Cambridge,* 383 Mass. 152, 160, 418 N.E.2d 335, 339-40 (1981) (same in context of rent control).

100. 533 U.S. 606 (2001).

101. *Id.* at 629-30.

102. *Id.* at 642.

of those expectations."[103] Justice Breyer agreed.[104] Justices Ginzberg and Souter dissented altogether. The upshot is that Justice Kennedy's pronouncement about the ability to challenge pre-existing laws garnered only four solid votes.[105]

Lower courts have had some trouble applying *Palazzolo*. The Ninth Circuit distinguished it in *Daniel v. County of Santa Barbara*,[106] which held an owner could not challenge a taking of her predecessor's property. The county had exacted the dedication of a public easement as a condition for permitting the prior owner to develop the property. Such a maneuver was later held invalid in *Nollan v. Cal. Coastal Comm'n*.[107] Nonetheless, that claim was foreclosed in *Daniel* since she had purchased the property with notice of the dedication and the "price paid for the property presumably reflected the market value of the property minus the interests taken."[108]

Perhaps the best treatment of this problem is to focus on when a takings claim becomes ripe. In a facial challenge, which asserts that mere enactment of a law (use restriction or invasion) causes a taking, the claim ripens and may expire (per the statute of limitations) before the property changes hands.[109] In that case, subsequent owners have no claim. But, in an as-applied challenge, which challenges application of a law to particular facts, the claim does not ripen until the law is actually applied to the property,[110] even if the law had been enacted before plaintiff's acquisition. In that case, the likelihood of reduced development potential of property may affect the buyer's investment-backed expectations, but it is not dispositive.[111]

Without this sort of distinction it becomes hard to apply the "background principles" and "investment-backed expectations" doctrines in takings cases, especially since property is defined by

103. *Id.* at 633.

104. *Id.* at 654-55.

105. Both Justice Kennedy's majority opinion and Justice Scalia's concurrence (533 U.S. at 637) suggest that positive law does not create background principles; only common law. Moreover, once the state creates a property interest, any retrenchment on that interest is forever open to challenge, even by subsequent generations who had no expectation of using the property in the foreclosed manner.

106. 288 F.3d 375 (9th Cir. 2002).

107. 483 U.S. 825 (1987).

108. *Id.* at 383. *See also Air Pegasus v. United States*, 60 Fed. Cl. 448 (Ct. 2004) (*Palazzolo* merely rejected a *per se* rule; it did not create a contrary one).

109. *See Levald, Inc. v. City of Palm Desert*, 998 F.2d 680, 687 (9th Cir. 1993).

110. *See id.* at 688.

111. *Cf. Travis v. County of Santa Cruz*, 33 Cal. 4th 757 (Cal. Sup. Ct. 2004).

state law, rather than by a court invoking natural law concepts of "property" rights.

d) Fractionalization (partial takings)

Regulation that depletes all value will cause a categorical regulatory taking. If the value of property is merely reduced, no taking usually occurs. But if the quantum of reduced value can be conceptually separated from the rest of the property, then that discrete piece has been wholly destroyed. This is the concept — or trick — of fractionalization.

The general rule stated in *Penn Central* is that property cannot be fractionalized (divided into discrete parts) for regulatory takings analysis, lest every regulation be deemed to deny all economic use of the regulated interest.[112] Nonetheless, fractionalization is appropriate in possessory takings cases. It is not necessary that government occupy the entirety of a parcel; if it invades even a small piece, it exercises dominion over it akin to the taking of an easement.[113]

But fractionalization is inappropriate in regulatory takings cases. Consider rent control. If a regulation reduces rents $100 below market value, it has wholly destroyed the value of that $100. Is this a categorical taking? If so, then price control would be *per se* unconstitutional.

In *Hall v. Santa Barbara*, and *Ross v. City of Berkeley*,[114] the courts held that a tenant's ability to assign her tenancy meant she could capture ("monetize") the discounted present value of future rent savings. This was seen as a discrete property interest, which was severed from the remainder of the property and transferred to the tenant when she vacated.[115] The theory was re-

112. This is known as the "denominator problem;" *i.e.*, in measuring the extent of regulatory impact, should the court look at the effect on the property as a whole, or on just that fraction whose use is regulated. In *Penn Central,* the Court refused to divide the owner's interest into ground rights and air rights. The City's landmark preservation law prevented Penn Central from building atop Grand Central station. The owner's economic interest in erecting a 55-story building was completely extinguished, but its property overall retained significant value.

113. *See Nollan; Loretto; Creppel v. United States*, 41 F.3d 627, 631 (Fed. Cir. 1994).

114. 655 F. Supp. 820 (N.D. Cal. 1987). A Ninth Circuit panel reached a similar conclusion in *Azul Pacifico, Inc. v. Los Angeles*, 948 F.2d 575 (9th Cir. 1991), *vacated* 973 F.2d 704 (9th Cir. 1992).

115. A similar result was reached in *Richardson v. City and County of Honolulu*, 124 F.3d 1150 (9th Cir. 1995), but based on the law's failure to substantially advance a legitimate state interest, rather than on a theory of fractionalization. *See infra.*

jected in *Yee*[116] and elsewhere.[117] But some courts persist in using it.[118] The New York Court of Appeals has even suggested that a particular use might be considered "a discrete twig out of (the owner's) fee simple bundle of rights."[119] Consequently, prevention of that particular use "may well be sufficient to constitute a taking."[120] This is dangerous and fertile ground, for it transmutes non-categorical cases (which balance a variety of factors) into categorical ones, and threatens every form of economic regulation.

Still, the claim should have been put to rest by *Tahoe-Sierra Pres. Council (TSPC)*. . The "'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.' We have consistently rejected such an approach to the 'denominator' question."[121]

2. Substantially Advance Prong

The *Agins* rule states that a law failing to "substantially advance legitimate state interests" will cause a taking. On its face, this rule seems to invite judges (and juries) to determine for themselves the efficacy of economic regulation. As such, it bears resemblance to the *Lochner* era, where courts routinely disregarded public policy choices made by legislatures and substituted their own views of the public good.

Fortunately, the Supreme Court has been sparing in its use of this prong of the takings clause. Lower courts, however, have not been at all shy in using it to invalidate regulatory laws.[122]

a) Origins of the "substantially advance" prong

When the "substantially advance" test first entered takings jurisprudence in *Agins*, it appeared without discussion and with ci-

116. *Yee v. City of Escondido*, 503 U.S. 519,at 528-29 (1992).

117. *See, e.g., Casella v. City of Morgan Hill*, 230 Cal. Rptr. 876, 879-81 (Cal. Ct. App. 1991).

118. *See Manocherian v. Lenox Hill Hospital*, 643 N.E.2d 479, 485-86 (N.Y. 1994) (holding tenancy protection for corporate lessees amounted to taking of reversionary interest).

119. *Seawall Associates v. City of New York*, 74 N.Y.2d 92, 109, 542 N.E.2d 1059, 1067 (N.Y. 1989).

120. *Id.* at 110.

121. 535 U.S. at 331.

122. As noted, *supra*, n. 2, in Lingle v. Chevron, the Supreme Court recently qualified the use of the "substantially advance" prong, and limited heightened review under this test to exactions and other unconstitutional conditions cases.

tation only to *Lochner*-era substantive due process cases. The references were to *Euclid v. Ambler Co.*[123] and *Nectow v. Cambridge.*[124] Since then, the Court has often repeated the language from *Agins*, but never used it to invalidate a regulatory law under the takings clause. Indeed, *Euclid*, the progenitor of the "substantially advance" test, equated it with the deferential "arbitrary and unreasonable" test.[125] But, it was this synthesis of due process and takings doctrine that spawned an era of judicial activism.

As noted below (section on Due Process), the Supreme Court has often merged due process and takings doctrines.[126] This would not be so problematic if current due process standards were employed, since they are exceedingly deferential to legislative choices when it comes to economic regulation. In fact, this is how the Supreme Court basically treats the "substantially advance" standard in most takings cases. The single exception, discussed below, is with regulatory exactions, where government uses its licensing discretion to exact property or money from applicants.[127]

However, lower courts have assumed a broader mission in enforcing the "substantially advance" standard. And it is under that prong of *Agins* that many recent rent control cases have been tried.

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123. 272 U.S. 365 (1923) (upholding residential zoning ordinance).

124. 277 U.S. 183, 188 (1928) (invalidating a Cambridge zoning ordinance, as applied to plaintiff's property. "The governmental power to interfere by zoning regulations with the general rights of the land owner by restricting the character of his use, is not unlimited, and other questions aside, such restriction cannot be imposed if it does not bear a substantial relation to the public health, safety, morals, or general welfare").

125. *Euclid*, 272 U.S. at 395 (the facts of the case "preclude us from saying, as it must be said before the ordinance can be declared unconstitutional, that such provisions are clearly arbitrary and unreasonable, having no substantial relation to the public health, safety, morals, or general welfare")

126. For a good discussion of why this creates doctrinal disarray, *see Kavanau v. Santa Monica Rent Control Bd.*, 16 Cal. 4th 761 (1997).

127. As Judge William Fletcher wrote in *Chevron v. Cayetano*, 224 F.3rd 1030, 1043 (9th Cir. 2000) (Fletcher, J., concurring):

> An ordinary rent control law is constitutionally indistinguishable from a price control law. Rent control involves a price charged for real property, just as price control involves a price charged for personal property. The constitutional test for ordinary rent and price control laws is the same, regardless of whether the laws are challenged under the Due Process Clause or the Takings Clause. The test has been variously formulated, but it essentially requires that the law be "reasonable" and "not confiscatory.".

b) *The rational basis standard*

"Substantially advance" is terminology one would expect under heightened scrutiny.[128] As Justice Kennedy remarked in *Eastern Enterprises v. Apfel*,[129] close scrutiny requires that a court make a normative judgment about the efficacy of economic regulation, thus creating an "uneasy tension with our basic understanding of the Takings Clause, which has not been understood to be a substantive or absolute limit on the Government's power to act".[130] Accordingly, most courts agree that the "substantially advance" test should be applied deferentially, as with rational basis review under the due process clause.[131]

An exception to deferential review under the takings clause occurs in the case of exactions, discussed below. Otherwise, the qualitative analysis prong of *Agins* ought not be used to resurrect *Lochner*. But it has, at least in the Ninth Circuit.

(1) City of Monterey v. Del Monte Dunes[132]

After the City of Monterey repeatedly denied Del Monte Dunes' various development applications, the landowner filed a takings claim. The case was tried to a jury on the theory that the City's repeated denials failed the qualitative *Agins* test. The jury agreed and awarded damages for an uncompensated taking. The Supreme Court affirmed, although not because the qualitative standard required heightened scrutiny.

First, the jury was instructed to use a reasonable relation standard in assessing plaintiff's claim.[133] Second, the Supreme Court noted it had never required application of heightened scrutiny

128. *See Nollan v. Cal. Coastal Comm'n*, 483 U.S. 825, 841 (1987).

129. 524 U.S. 498 (1998).

130. *Id.* at 545 (Kennedy, J., concurring).

131. *See Commercial Builders of N. Cal. v. Sacramento*, 941 F.2d 872, 874 (9th Cir. 1991) (rejecting argument that *Nollan* materially changes level of scrutiny; no Circuit Court of Appeals has interpreted *Nollan* "as changing the level of scrutiny to be applied to regulations that do not constitute a physical encroachment on land"); *Kavanau*, 16 Cal. 4th at 781 (noting "similarity of this takings standard to the due process requirement that a regulation 'have a reasonable relation to a proper legislative purpose'").

132. 526 U.S. 687 (1999).

133. *Id.* at 701 ("if the preponderance of the evidence establishes that there was no reasonable relationship between the city's denial of the . . . proposal and legitimate public purpose, you should find in favor of the plaintiff. If you find that there existed a reasonable relationship between the city's decision and a legitimate public purpose, you should find in favor of the city"). The Court found no error with this instruction, especially because the City had proposed it itself.

outside the context of exactions. Third, the Court expressly declined to extend one of the elements of heightened scrutiny to ordinary regulatory decisions.[134]

This is not to suggest that application of heightened scrutiny under the qualitative strand is a settled question. Some jurists are still confused about when to apply it.[135] Also, in *Eastern Enterprises v. Apfel*, four members of the Court applied heightened scrutiny to invalidate the Coal Industry Retiree Health Benefit Act. The Act required Eastern Enterprises to fund health benefits for over 1,000 miners who had worked for the company prior to 1966. The four thought the Act was improperly severe, disproportionate and extremely retroactive and therefore worked an as-applied unconstitutional taking. Five justices rejected the takings claim, but one of them (Kennedy) found the Act invalid on substantive due process grounds.

(2) Hotel & Motel Ass'n of Oakland v. City of Oakland

The Ninth Circuit also applied the "substantially advance" test deferentially in *Hotel & Motel Ass'n of Oakland v. City of Oakland*.[136] There, Oakland enacted "performance standards" and eliminated non-conforming use exemptions for hotels. Citing *Del Monte Dunes*, the Association claimed it had a right to have a jury determine if the ordinances substantially advanced any legitimate state interest. Both the district court and Ninth Circuit disagreed. They held, as a matter of law, that the City's interest (health and safety) was legitimate, and the means were appropriate. "A reasonable relationship exists between this regulatory action and the public purpose it is meant to serve."[137]

c) Heightened Scrutiny of Rent Control

While the *Agins'* standard is applied deferentially in most takings cases, rent control generates a difference in opinion. The issue in most of these cases is not so much whether protecting tenants is a legitimate state interest; most cases hold that it is. Rather, the question is whether rent control, or a particular feature of it, "substantially advances" that interest.

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134. 526 U.S. at 703.

135. *See, e.g.*, *Parking Ass'n of Georgia v. Atlanta*, 515 U.S. 1116 (1995) (Thomas, J., dissenting from denial of cert.) (finding uncertainty in the scope of the heightened review under *Agins*).

136. 344 F.3d 959 (9th Cir. 2003).

137. *Id.* at 968.

A divergence seems to be developing between ordinary apartment rent controls and those involving mobilehomes and other ground leases. In the latter cases, courts have seized upon the so-called "premium" issue. When a ground lease expires, a vacating tenant can't simply collect her possessions and move on. She typically will have structural improvements that must be left in place, or moved at prohibitive cost. At least where the ground owner intends to re-lease the property, an incoming tenant will likely want to purchase the improvement.

The transaction between vacating tenant (improvement owner) and incoming tenant (improvement buyer) is conceptually distinct from the ground lease relationship between the latter and the landlord. But it is not economically distinct. The purchase price will be heavily influenced by the ground rent. If the rent level is regulated, the incoming tenant might be willing to pay more for the improvement. This capitalized value of future rent savings would then inflate the purchase price. The outgoing tenant can theoretically capture this "premium" and sever it from the landlord-tenant relationship.

The converse is also true. If the ground rent is unregulated, and significant increases are imposed or anticipated, the incoming tenant will pay less for the improvement. In this way, landlords can capture for themselves much of the value of the outgoing tenant's investment in his improvement. For example, in *Richardson v City and County of Honolulu,*[138] the Ninth Circuit observed that condominium ground leases often experience "renegotiated rent several hundred times greater than the initial fixed rent."[139]

The issue becomes politically charged because many ground tenants (*e.g.*, mobilehome owners) are elderly and living on fixed incomes. They can see their entire life savings vaporize if they are unable to sell their units on-site along with regulated ground rents. Resolution of this complex economic issue requires a delicate balancing of the interests of land- and improvement-owners. But, under the "substantially advance" test, the Ninth Circuit has reached an easy outcome – the mere potential for a premium will render a rent law unconstitutional.

138. 124 F.3d 1150 (9th Cir. 1997).
139. *Id.* at 1163.

The discussion below first traces the "substantially advance" test in ordinary rent control cases, and then moves to ground lease cases.

(1) Traditional Rent Control and Tenant Protection

Seawall Associates v City of New York,[140] was the first case to read *Agins* as requiring heightened scrutiny in tenant protection cases. Owners of single room occupancy (SRO) housing argued that a five year moratorium on conversion, alteration, and demolition constituted a taking. The court examined the purpose of the legislation and found that the regulation of the SRO housing did not substantially advance a government interest. The intent of the legislation was to prevent warehousing of SRO units and the moratorium would prevent the stock of low cost housing from decreasing. However, the means and ends lacked the required close nexus;[141] the obligations placed on the SRO property owners were only conjecturally related to the complex social problem of homelessness.[142]

Seawall was followed by *Manocherian v Lennox Hill Hospital*.[143] The court found the intent of a rent control law was to preserve a unique benefit for the Hospital by maintaining below market rentals for hospital employees. The Court held this was an impermissible state end as its benefit was not shared by the public at large. There was limited general welfare benefit to maintaining subsidized housing for not-for-profit hospitals. And it impermissibly burdened a limited group of private apartment owners by requiring them to provide subsidized housing.

Manocherian is in tension with *Arcadia Development Corp. v. City of Bloomington*.[144] There a Minnesota court found that redistributing the "benefits and burdens of economic life or otherwise to restore an equitable balance to an economic relationship" is a legitimate state interest. Moreover, it is substantially ad-

140. 74 N.Y. 2d 92, 542 N.E.2d 1059 (N.Y. 1989).

141. The city had a study which indicated that the ban on converting, destroying and warehousing SRO units would have a minimal effect on the homeless or the homeless low income families. In fact, there was no requirement that the units would be rented to either group.

142. Further, this law had a buy out provision, where for $45,000 per SRO unit a property owner could remove her property from the regulation, which undermined the purpose of the law. Thus, the fee was seen as a tax on a few landowners as opposed to a general obligation.

143. 84 N.Y. 2d 385, 643 N.E.2d 479 (N.Y. 1994).

144. 552 N.W.2d 281 (Ct. App. Minn. 1996).

vanced by laws protecting certain classes of tenants.[145] The Washington Supreme Court wasn't as confident in *Garneau v. Seattle*.[146] It rejected the use of heightened scrutiny in reviewing Seattle's Tenant Relocation Assistance Ordinance. But, just to be on the safe side, the court analyzed the ordinance under heightened "essential nexus" and "rough proportionality" standards. anyway. The ordinance survived review.

California courts appeared to adopt heightened scrutiny in *152 Valparaiso Assoc. v. City of Cotati*.[147] The Court of Appeal stated that rental regulations require special scrutiny of the results produced and not merely the intentions of the regulation, because of the danger that private property will be taken for an alleged public use by local electoral majorities. The rent board denied rent increases on gentrifying capital improvements that had the effect of driving the poor, the elderly, students and people on fixed income out of the city. The court held the Board's rule failed to substantially advance a legitimate state interest, and it denied landlords any return on these capital improvement investments.[148]

The heightened scrutiny regime in California came to an end in *Santa Monica Beach v. Santa Monica Rent Control Bd.*[149] In a test case filed by the Pacific Legal Foundation (PLF), the landlord argued that rent control in Santa Monica had benefited mainly middle income and affluent tenants, rather than the poor, elderly, and minorities. This, he claimed, undercut the rationale for rent control. Although the Court of Appeal agreed heightened scrutiny should apply, and that rent control might be unconstitutional as a result,[150] the state Supreme Court reversed, holding "the heightened intermediate scrutiny standard" does not apply.[151] "Rather, the standard of review for generally applicable rent control laws must be at least as deferential as for generally applicable zoning laws and other legislative land use

145. *Id.* at 287.

146. 897 F. Supp. 1318 (W.D. Wash. 1995).

147. 56 Cal. App. 4th 378, 65 Cal. Rptr. 2d 551 (Cal. Ct. App. 1997).

148. But the Court of Appeal rejected an unusual claim by a property owner that, because he was unable to rent his units at the permitted rates, the rent law did not substantially advance a legitimate interest. *See Jones v. City of Berkeley Rent Stabilization Bd.*, No. A074395 (unpublished decision from the Court of Appeal, First District, 1997). Following *152 Valparaiso*, Cotati repealed its general rent control law and replaced it with one limited to mobilehomes. *See infra.*

149. 19 Cal. 4th 952, 968 P.2d 993 (1999).

150. 917 P.2d 623, 53 Cal.Rptr.2d 784 (1996).

151. 19 Cal. 4th at 967, 968 P.2d at 1003.

controls. Thus, the party challenging rent control must show that it constitutes an arbitrary regulation of property rights." As with deferential review generally, "those challenging the constitutionality of a legislative scheme of price control must show that 'no conceivable set of facts could establish a rational relationship between the regulation and the government's legitimate ends.'"[152]

(2) Ground Lease Rent Control

At first, the *Agins* standard was also applied deferentially in ground lease cases. In *Westwinds Mobile Home Park v. City Of Escondido*,[153] one of many cases challenging Escondido's mobilehome rent control law, park owners sought "close scrutiny" of a meager rent increase. The court drew a distinction between regulatory and possessory takings claims, holding that the *Nollan/Dolan* standard was applicable only in the latter.[154] Nonetheless, applying deferential review, the court held that the rent increase was not supported by the evidentiary record. This was based on traditional review of agency decisions (in California by way of Writ of Administrative Mandamus, Cal. Code Civ. Pro. § 1094.5), and not based on a taking.

(a) Richardson

Property rights advocates then turned to federal court, where they had considerably more success. The string started with *Richardson v City and County of Honolulu*.[155] Honolulu regulated rents of ground leases for both existing and future tenants; *i.e.*, there was no vacancy decontrol. Vacating tenants could sell their condominiums to successors under rent control. Owners argued this feature "create a premium, which an owner-occupant can capture when she sells."[156] The Ninth Circuit agreed. The court reasoned:

> "The absence of a mechanism that prevents lessees from capturing the net present value of the reduced land rent in the form of a

152. *Id.* at 102; *See also Steinbergh v. City of Cambridge*, 604 N.E.2d 1269 (Mass. 1992) (rejecting heightened scrutiny).

153. 30 Cal.App.4th 84, 35 Cal.Rptr.2d 315 (1994).

154. *Accord, Blue Jeans Equities West v. San Francisco*, 3 Cal. App. 4th 164, 169-170, 4 Cal. Rptr. 2d 114, 117-18 (Cal. Ct. App. (1992) (heightened scrutiny not applicable to nonphysical, regulatory takings); *Sandpiper Mobile Village v. City of Carpinteria*,10 Cal. App. 4th 542, 549-551, 12 Cal. Rptr. 2d 623, 627-28 (Cal. Ct. App. (1992).

155. 124 F.3d 1150 (9th Cir. 1997).

156. *Id.* at 1165.

> premium, means that the Ordinance will not substantially further its goal of creating affordable owner-occupied housing in Honolulu. Incumbent owner occupants who sell to those who intend to occupy the apartment will charge a premium for the benefit of living in a rent controlled condominium. The price of housing ultimately will remain the same. The Ordinance thus effects a regulatory taking."[157]

There was remarkably little authority cited in the opinion for the use of heightened scrutiny. The court had earlier rejected that standard of review in assessing a companion ordinance condemning the fee and transferring it to individual condominium owners.[158] Instead, the court simply cited *Nollan* without analysis and proceeded to find that the law "will not substantially further its goal of creating affordable owner-occupied housing in Honolulu."[159] Of course, the ordinance was *rationally* related to a legitimate state interest — protecting the investments that current owners had in their homes.[160] But, apparently it was not *substantially* related to any court-approved purpose.

(b) Chevron I

Heightened review was next applied in *Chevron U.S.A. v Cayetano*.[161] The Ninth Circuit held that a Hawaii statute limiting rents that an oil company could charge its lessee dealers would be unconstitutional if the act failed to substantially advance a legitimate state interest. The Court noted that although the rent cap could help the lessee dealers by lowering their costs, there was no evidence that they would pass along the savings to consumers through lower retail prices.

In adopting heightened scrutiny, the court rejected an admonition from Justice Rehnquist in *Keystone Bituminous Coal Associ-*

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157. *Id.* at 1166. The court used minimum scrutiny in upholding the constitutionality of a companion ordinance that converted leasehold interests in condominium units to fee interests, through the use of the City's condemnation power.

158. For an interesting development on this point, *see County of Wayne v. Hathcock*, 684 N.W.2d 765 (Mich. 2004). Applying heightened scrutiny to the "public use" requirement under the state constitution, the Michigan Supreme Court ruled that the county's condemnation power could not be used to redevelop land adjacent to an airport into a business and technology park.

159. 124 F.3rd at 1166. The court also cited to Justice Scalia's concurring opinion in *Pennell v. San Jose,* 485 U.S. 1, 20 (1988), which seemed beside the point.

160. With vacancy decontrol a ground landlord can raise the rent for an incoming tenant to any level, thus depressing the price she would willing to pay for the surface improvement (condominium).

161. 224 F.3d 1030 (9th Cir. 2000).

ation v. DeBenedictis[162]: "Our inquiry into legislative purpose is not intended as a license to judge the effectiveness of legislation. . . the [constitutional requirement] is satisfied if . . . the . . . [State] Legislature rationally could have believed that the [Act] would promote its objective."[163] The Ninth Circuit held that deferential review was limited to condemnation cases, and inapplicable to inverse condemnation.[164]

The court's principal authority was prior Ninth Circuit cases employing heightened scrutiny. It also found support in Supreme Court takings cases, but only from issues the Court expressly declined to reach. For instance, in *Pennell v. San Jose*,[165] the Court upheld a rent control ordinance against a due process claim, using a deferential standard of review. The Court declined to reach the takings claim because it was unripe. From this, the Ninth Circuit panel concluded that heightened review of rent control laws was an open and fertile question. In *Yee v. City of Escondido*,[166] the Court similarly declined to decide the regulatory takings claim, but upheld the mobilehome rent control law (including the vacancy control provision) against a possessory claim. In dicta, Justice O'Connor opined that a severable premium "might have some bearing on whether the ordinance causes a regulatory taking, as it may shed some light on whether there is a sufficient nexus between the effect of the ordinance and the objectives it is supposed to advance."[167]

Finally, the *Chevron* majority cited to *Del Monte Dunes* as justification for heightened scrutiny. It cited the Supreme Court's approval of "jury instructions given by the trial court regarding the 'substantially advances' test [as] consistent with the Court's previous general discussions of regulatory takings liability." However, as noted earlier, those instructions employed a "reasonable relationship" standard,[168] so it is hard to see the case supporting the majority's activist approach. Nor did the dicta in *Yee* provide analytical support. It merely noted that some nexus is required between means and ends in regulatory takings cases

162. 480 U.S. 470 (1987).

163. *Id.* at 511, n.3.

164. *Keystone* was a regulatory takings (inverse condemnation) case.

165. 485 U.S. 1 (1988).

166. 503 U.S. 519 (1992).

167. *Id.* at 530.

168. 526 U.S. 687, 700 (1999).

as it was in due process cases.[169] But there was no hint of heightened scrutiny in Justice O'Connor's statement.[170]

The *Chevron* majority's use of precedent was questionable,[171] and its failure to provide any theoretical support for heightened scrutiny left one with the impression that naked judicial activism was at play.

(c) Chevron II

In *Chevron I*, the Ninth Circuit remanded for further factual development. Although the District Court used heightened scrutiny under the "substantially advance" test, the record was unclear whether the challenged law did or did not benefit gasoline consumers. At trial on remand, the District Court weighed the economic testimony for itself and made projections of future sales and prices. It found that consumer prices would increase, as argued by Chevron, rather than stabilize, as argued by Hawaii. Hence the law failed to "substantially advance" the law's consumer protection purpose and was therefore a taking. The Ninth Circuit affirmed a second time.[172]

In *Chevron II*, the court reiterated that the "more deferential, due process standard does not apply to regulatory takings claims challenging land use regulations, including rent control ordinances." Instead, courts are to use the "reasonable relation" standard, which the court read as an "intermediate level of review, more stringent than the rational basis test used in the due process context."[173] Again, the court cited only to exaction cases and dicta in *Yee*. It was the "inconsistent nature of the [Supreme] Court's precedent"[174] that permitted the Ninth Circuit to

169. As Judge Fletcher notes, "it is a long way from the quoted passage in *Yee* to the panel's holding in this case." *Chevron v. Lingle*, 363 F.3d 846, 860 (9th Cir. 2004) (Fletcher, J., dissenting).

170. Indeed, later in *Del Monte Dunes*, the Supreme Court candidly acknowledged that it had "not provided "a thorough explanation of the nature or applicability of the requirement that a regulation substantially advance legitimate public interests outside the context of required dedications or exactions." 526 U.S. at 704.

171. The *Chevron* court cited to other cases purportedly analyzing rent control under the "substantially advance" test. 363 F.3d 846. But each case cited upheld the challenged law, and it does not appear that the courts used heightened scrutiny at all, but rather just repeated the standard litany of *Agins*. *Agins v. Tiburon*, 447 U.S. 255 (1980).

172. *Chevron v. Lingle*, 363 F.3d 846 (9th Cir. 2004).

173. *Id.* at 853-54.

174. *Id.* at 851.

promote its own standard. That standard is virtually strict scrutiny under the takings clause.

While the court's use of heightened scrutiny was previously limited to laws which resulted in the outgoing tenant monetizing future rent savings (the "premium" issue), thereby negating rent savings by incoming tenants, the *Chevron* cases expanded the doctrine to scenarios where premiums were entirely conjectural. Heightened scrutiny would be applied wherever "uncertainty about market reaction accounts for *the possibility* that [outgoing tenants] will retain a benefit from the reduced rent, i.e., a premium."[175]

This approach is at odds with settled law, going back as far as *Euclid v. Ambler*, the source of the "substantially advance" test, which declined to speculate as to economic effects in constitutional cases.[176] Indeed, the prohibition against economic conjecture underlies the elaborate ripeness requirement in takings cases.[177]

(d) Cashman

The Ninth Circuit's adventure continued and went farther astray in *Cashman v. City of Cotati*,[178] the latest case to invalidate a ground lease rent control law. Typical to such laws, Cotati regulated rents for existing tenants and maintained those levels for incoming tenants, subject to various rent increase allowances. This "vacancy control" provision, when coupled with the right of a departing tenant to sell her mobilehome *in situ*, means that the improvement's selling price can be influenced by projected rents. The court has described these twin features as creating a "premium," which the outgoing tenant takes with her, to the detriment of the land owner (who loses the right to raise rents) and the incoming tenant (who may lose the benefit of reduced rents by having to pay more for the improvement).

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175. *Id.* at 858 (emphasis added).

176. 272 U.S. at 395 ("where the equitable remedy of injunction is sought . . . upon the broad ground that the mere existence and threatened enforcement of the ordinance, by materially and adversely affecting values and curtailing the opportunities of the market, constitute a present and irreparable injury, the court will not scrutinize its provisions, sentence by sentence, to ascertain by a process of piecemeal dissection whether there may be, here and there, provisions of a minor character, or relating to matters of administration, or not shown to contribute to the injury complained of").

177. As noted, *supra* n.17, the Supreme Court reversed the Ninth Circuit in *Lingle v. Chevron*, 125 S.Ct. 2074 (2005).

178. 374 F.3d 887 (9th Cir. 2004).

In an earlier mobilehome rent control case from the Circuit, *Hall v. Santa Barbara*, Judge Kozinski suggested that the premium was a separate property right that was completely extinguished by operation of the law. However, that line of reasoning was rejected by the Supreme Court in *TPSC* and other cases. So, when the opportunity for heightened scrutiny re-emerged under the "substantially advance" test, the court seized it.[179]

In *Cashman*, the mobilehome park owner alleged that outgoing tenants, upon selling their homes, could capture part or all of the present value of future rent savings due to rent control. Thus, new tenants would not benefit at all from rent control, undermining the City's stated purpose in enacting the law. The District Court granted summary judgment for the park owner, relying on *Richardson*, and held that the vacancy control provision was unconstitutional. But while the appeal was pending, the Ninth Circuit decided *Chevron I* and remanded *Cashman* to reconsider whether the correct standard had been applied.

At trial on remand, the District Court accepted expert testimony indicating there was no rent control premium in Cotati and incoming tenants in fact benefited from lower rents.[180] Accordingly, the court concluded that the law's means were substantially related to its ends. The court vacated its earlier judgment and found the law constitutional. The Court of Appeals reversed. It held that summary judgment in favor of the park owner was required because the facts (and economic reality) of mobilehomes in Cotati were irrelevant. "[O]nly . . . the economic 'principles of premiums'" matters,[181] "not its application in specific circumstances."[182] "[T]he possibility of a premium . . . undermines the City's interest in creating or maintaining affordable housing."[183]

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179. The Ninth Circuit's approach to the premium issue is at odds with that taken by other courts. *See, e.g., Casella v. City of Morgan Hill*, 280230 Cal. Rptr. 876, 879 (Cal. Ct. App. 3d 43, 49 (1991); *Eamiello* v. *Liberty Mobile Home Sales,* 208 Conn. 620, 546 A.2d 805 (Conn. 1988).

180. One expert witness testified that "mobile homes subject to rent control in Cotati sold at a substantial discount rather than a premium." *Cashman*, 379 F.3d *Id.* at 903. Another testified that "even with vacancy control, the initial costs of mobilehome ownership for prospective purchasers . . . will be lower than these costs in the absence of vacancy control." *Id.* at 904.

181. *Id.* at 899.

182. *Id.*

183. *Id.* In an earlier case, *Hacienda Valley Mobile Estates v. City of Morgan Hill*, 353 F.3d 651 (9th Cir. 2003), the court noted that mobilehome rent control laws (even with vacancy control) do not always result in a premium. Accordingly, the court was constrained in *Cashman* to hold that the theoretical possibility of a premium was all that mattered, not whether one actually existed in fact.

The Court of Appeals also held the entire rent control law unconstitutional, not just the vacancy control provision. It reasoned that an incoming tenant could pay a premium for an on-site mobilehome in a rent controlled environment, to secure stable rents, even when initial rents were unregulated. That the only evidence on this point was testimony that buyers will pay *less*, not *more*, for mobilehomes under rent control, was besides the point to the court. The theoretical possibility of a premium was sufficient to render the entire rent control law unconstitutional.[184] Unless the law precluded this possibility, it was facially unconstitutional.

The logical flaw in the court's analysis is alarming. If a rent law fails to "substantially advance" its stated purpose of maintaining affordable housing, because incoming tenants' rent savings are captured by the outgoing tenants' premium, then the existence of a premium would seem to be a *sine qua non* of that failure. Where no premium exists, the incoming tenants will presumably benefit from the rent control law, thereby satisfying even a stringent "substantially advance" test. By relying on "principle" and "possibility," while dismissing as immaterial whether a premium actually exists or not, the court concedes that it uses the premium issue as a subterfuge to engage in its own economic policy-making.[185]

It is ironic that the Ninth Circuit has used the "substantially advance" test as the excuse for its activism. As noted earlier, that test is the direct descendent of substantive due process land use cases. Yet, due process doctrine has matured into the most deferential of all constitutional tests. Under due process "there is no requirement that the statute actually advance its stated purpose; rather, the inquiry focuses on whether "'the governmental body *could* have had no legitimate reason for its decision.'"[186]

184. In the first case, the District Court had initially concluded the same, but amended its judgment to enjoin only the vacancy control provision, since that would eliminate any premium. The Court of Appeals held the trial court "abused its discretion" in amending the judgment in this manner. 374 F.3d at 894-895.

185. Previous cases held that existence of a premium was relevant only to a facial takings claim, rather than as, applied. *See Levald, Inc. v. City of Palm Desert*, 998 F.2d 680, 689 (9th Cir. 1993). In other words, mere enactment of the ordinance gives rise to the alleged injury, not its particular application. Nonetheless, proof of the injury is required.

186. *Levald, Inc. v. City of Palm Desert*, 998 F.2d 680, 690 (9th Cir. 1993) (citing *Minnesota v. Clover Leaf Creamery Co.*, 449 U.S. 456, 464 (1981)). *See also Williamson v. Lee Optical of Oklahoma, Inc.*, 348 U.S. 483, 487-88 (1955) ("The law need not be in every respect logically consistent with its aims to be constitutional. It is

Cashman also turns the *Agins* test on its head. No longer are courts to look at the economic impact of regulation. Rather, economic theory determines the constitutionality of a law under the takings clause. If that theory posits that the legislature's stated goals might not be achieved, those goals cannot be pursued. *Cashman* operates on the presumption that judges are better economists than economists are, and therefore the latter's testimony is irrelevant. In the new *Lochner* era, it is theory that counts, not facts. If any credible theory can be found that undermines an economic regulation, it is a sure bet that the Ninth Circuit will find it.

D. *Unconstitutional Conditions*

Heightened scrutiny under the takings clause has been held appropriate in a class of cases sometimes referred to as "unconstitutional conditions." The doctrine is not limited to takings cases, but the discussion here mainly is.[187] An unconstitutional conditions claim is seldom found in rent control cases. But since it underlies the use of heightened scrutiny in the "substantially advance" test, it is described to explicate the limits of that test.

1. Discretionary Benefits and Relinquished Rights

A State cannot impose unconstitutional conditions on the receipt of a public benefit. This occurs when the state attaches impermissible strings to the grant of a discretionary government benefit. The doctrine is implicated in the takings area when a benefit (*e.g.,* building permit, rent increase) is granted, but on the condition that the recipient relinquish a right in exchange. The doctrine's purpose is to prevent government from using its benefits largesse to exact concessions. Since so much of modern life depends on some government benefit (e.g., driver's license, professional license), it would be rather convenient for government to exact money and concessions as part of the permitting process that it could not otherwise demand.

There are some important prerequisites to use of the doctrine. First, the public benefit granted must be a discretionary one; *i.e.*, one the state could withhold under applicable substantive law. Building permits are a good example. A state can deny a build-

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enough that there is an evil at hand for correction, and that it might be thought that the particular legislative measure was a rational way to correct it").

187. For a more thorough analysis of the field, *see* Kathleen M. Sullivan, *Unconstitutional Conditions*, 102 HARV. L. REV. 1413, 1415 (1989).

ing permit if it has a rational reason for doing so and so long as denial doesn't deprive the property of viable economic use. If the recipient is otherwise constitutionally entitled to the permit or benefit (e.g., parade permit), then any restrictions imposed would be tested under applicable substantive law rather than the unconstitutional conditions doctrine.

Second, the condition attached to the benefit must be the relinquishment of a constitutional right. For instance, in *Ruckelshaus v. Monsanto*,[188] a pesticide producer sought permission from the EPA to market its product. Permission to do so was a discretionary government benefit since Monsanto had no constitutional right to make and distribute its pesticide. Denial of permission would likely be rationally related to some health and safety concern. But, the EPA granted permission on the condition that Monsanto divulge the pesticide's chemical composition, a protectable property interest (trade secret), and allow others to use it. Monsanto argued this forced relinquishment was a taking of its property.

The facts of *Monsanto* trigger the unconstitutional conditions doctrine. But mere application of the doctrine does not mean that the condition is unconstitutional. Rather, it means that the condition must be related to the regulatory purpose behind the discretionary benefit. In the case of Monsanto, the Court held that disclosure was related the EPA's charge to protect public health.

Monsanto employed a relational standard (between condition imposed and regulatory purpose) of *rational basis*. Subsequent takings cases have employed a stricter standard; *i.e.*, *substantially advancing*. As Justice Scalia noted in *Nollan v California Coastal Commission*,[189] the Court is "inclined to be particularly careful about the adjective where the actual conveyance of property is made a condition to the lifting of a land-use restriction, since in that context there is heightened risk that the purpose is avoidance of the compensation requirement, rather than the stated police-power objective."[190]

188. 467 U.S. 986 (1984).
189. 483 U.S. 825 (1987).
190. *Id.* at 841.

2. Exactions

The unconstitutional conditions doctrine is applied to regulatory exactions; *e.g.*, where government demands money or property in exchange for a permit. The government can do this, but only if: (1) "an essential nexus exists between legitimate state interests and the permit conditions;" and (2) the degree of exaction is proportional to the public burden caused by grant of the permit.

a) Essential Nexus - Nollan

In *Nollan v. California Coastal Commission*,[191] the court applied the unconstitutional conditions doctrine and found the agency's asserted public interest was not substantially advanced by the condition imposed on Nollan's development permit. There was no nexus between the condition (requiring Nollan to dedicate a lateral public easement across his beachfront) and the public purpose (maintaining ocean views for the public from the landward side of the property). Development of Nollan's coastal land did not affect any barrier to public viewing that would be eased by the easement.

b) Rough Proportionality - Dolan

In *Dolan v. City of Tigard*,[192] the city required, as a condition for a building permit, that the owner set aside a portion of her property for use as a public greenway and floodplain and to deed another portion for use as a public bikeway. The Court found that both conditions satisfied the essential nexus test of *Nollan*. However, the extent of the exactions was greater than necessary to relieve the public burden imposed by development of the property.

Dolan requires that there be "rough proportionality" between the extent of exaction and the reason for it. For instance, although Dolan's larger store would attract more traffic, the City failed to quantify the impact and accordingly could not show that the required public bikeway was necessary to offset that impact.

While "rough proportionality" does not require mathematical precision, it does require some evidentiary basis in the administrative record for the conclusion reached that a particular exaction is appropriate.

191. 483 U.S. 825 (1987).
192. 512 U.S. 374 (1994).

c) *Monetary Exactions - Ehrlich*

In *Ehrlich v City of Culver City*,[193] the California Supreme Court extended the *Nollan/Dolan* standard to exactions consisting of money, rather than property. The City imposed a development mitigation fee on a property owner who wanted to convert a parcel from recreational to residential use. The court agreed that the fee was sufficiently related to the City's interest in providing recreational facilities, but that the amount of the fee had not been shown to be proportional to the injury caused by conversion.

3. Individual Adjudicative Discretionary Actions

Both *Nollan* and *Dolan* involved discretionary permits awarded by individualized adjudicatory agency action. It is in such cases where the prospect of "regulatory leveraging" is most acute. The risk of exaction (or as Justice Scalia put it, "extortion") is far less when restrictions are imposed by *legislative* action; *i.e.*, across the board.

The point was amplified by Chief Justice Rehnquist in *Dolan*:

> "[Typical] land use regulations . . . differ in two relevant particulars from the present case. First, they involved essentially legislative determinations classifying entire areas of the city, whereas here the city made an adjudicative decision to condition petitioner's application for a building permit on an individual parcel. Second, the conditions imposed were not simply a limitation on the use petitioner might make of her own parcel, but a requirement that she deed portions of the property to the city. In Nollan, supra, we held that governmental authority to exact such a condition was circumscribed by the Fifth and Fourteenth Amendments. Under the well-settled doctrine of "unconstitutional conditions," the government may not require a person to give up a constitutional right—here the right to receive just compensation when property is taken for a public use—in exchange for a discretionary benefit conferred by the government where the benefit sought has little or no relationship to the property.[194]

According to this passage, legislatively imposed restrictions do not trigger the heightened review of *Nollan/Dolan*. A few notable cases make the point succinctly.

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193. 12 Cal. 4th 854, 911 P.2d 429 (Cal. 1996).

194. 512 U.S. at 316.

a) Ehrlich v. City of Culver City

Ehrlich aptly explains the difference between individualized discretionary permit actions, and restrictions of general application; only the former trigger heightened scrutiny. The landowner challenged both a mitigation fee imposed as a condition of a development permit, and the city-wide "Art in Public Places" ordinance. The latter was uniformly required of all development; hence not subject to heightened review. The court explained:

> "The intermediate standard of judicial scrutiny formulated by the high court in Nollan and Dolan is intended to address just such indicators [of leveraging] in land use 'bargains' between property owners and regulatory bodies — those in which the local government conditions permit approval for a given use on the owner's surrender of benefits which *purportedly* offset the impact of the proposed development. It is in this paradigmatic permit context — where the individual property owner-developer seeks to negotiate approval of a planned development — that the combined Nollan and Dolan test quintessentially applies."[195]

b) Lambert v City and County of San Francisco

In *Lambert v. City and County of San Francisco*,[196] the court held that the *Nollan/Dolan* standard applies only "when an issuing agency demands some sort of exaction as a condition of issuing a conditional use permit."[197] San Francisco's planning commission denied an application to convert long term residential units to tourist use. The city had passed the regulation in response to the shortage of housing for low income and elderly residents. The Court stated a general rule that no taking results from down-zoning of property that limits potential for development. Lambert argued that the City would have granted the use permit if he had paid $600,000. However, since the city did not take the $600,000 and did not grant a conditional use, the only issue was whether the denial was proper. Finally, the court concluded that the regulation advanced a legitimate government interest.

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195. *Erlich*, 911 P.2d at 438.

196. 57 Cal.App.4th 1172, 67 Cal.Rptr.2d 562 (Cal Ct. App. 1997), *review dismissed and cause remanded* (July 28, 1999).

197. *Id.* at 1181.

c) *Arcadia Development Corp. v. City of Bloomington*

In *Arcadia Development Corp. v. City of Bloomington,*[198] the court took the issue head on and squarely ruled that *Nollan/Dolan* "applies only to adjudicative determinations that condition approval of a proposed land use on a property transfer to the government, which, standing alone, would clearly constitute a taking. Accordingly, cases interpreting Dolan have confined its 'rough proportionality' analysis to adjudicative land-dedication situations or to classic 'subdivision exaction' cases."[199]

d) *San Remo Hotel v. San Francisco*

In *San Remo Hotel v. City and County of San Francisco,*[200] the California Supreme Court reiterated that heightened scrutiny under the "substantially advance" test does not apply to generally applicable legislative determinations.

> "The 'sine qua non' for application of Nollan/Dolan scrutiny is thus the 'discretionary deployment of the police power' in 'the imposition of land-use conditions in individual cases.' Only 'individualized development fees warrant a type of review akin to the conditional conveyances at issue in Nollan and Dolan.'"[201]

In sum, the "substantially advance" test is inapposite to rent control cases.

E. *Temporary vs Permanent Takings*

As with much of takings jurisprudence, the Supreme Court has never "provided . . . a definitive statement of the elements of a claim for a temporary regulatory taking."[202] The lack of guidance has caused some confusion in the lower courts.

1. Doctrinal Origins

a) *San Diego Gas & Electric v. City of San Diego*

The modern concept of "temporary" takings first appeared the year following *Agins* in Justice Brennan's dissent in *San Diego Gas & Electric Co. v. City of San Diego.*[203] In his view, once a

198. 552 N.W.2d 281 (Minn. Ct. App. 1996).
199. *Id.* at 286. *See also Clajon Prod. Corp. v. Petera*, 70 F.3d 1566, 1578-79 & 1579 n.21 (10th Cir. 1995).
200. 27 Cal.4th 643, 41 P.3d 87 (2002), *aff'd* 125 S. Ct. 2491 (2005).
201. *Id.* at 670.
202. *City of Monterey v. Del Monte Dunes*, 526 U.S. 687, 704 (1999).
203. 450 U.S. 621 (1981).

regulation was adjudicated a taking, compensation would be due "for the period commencing on the date the regulation first effected the 'taking,' and ending on the date the government entity chooses to rescind or otherwise amend the regulation."[204]

In Justice Brennan's view, *all* regulatory takings were, by definition, "temporary, since the agency could always repeal or modify the restriction.[205] Thus, the label "temporary" or "permanent" is irrelevant to the constitutional analysis, except for measuring damages. However, to say that all regulatory takings are temporary is not to say that all temporary use restrictions are takings.

Two separate subdoctrines of takings law reinforce the distinction. The first is the requirement of final agency action before a takings claim ripens. The very notion of finality is incompatible with a theory of liability for interim measures. The second is the Court's rejection of "fractional takings." Property rights cannot be divided into separate segments for determining whether regulation leaves an economically viable use. Just as property must be considered as a whole in terms of its physical and use attributes it must be considered as a whole in temporal terms. Time slicing property rights to establish total denial of use for a particular time segment is no more valid than slicing a parcel into surface, subsurface, and air rights to establish total denial of use for a discrete physical segment.

b) *First English Evangelical Lutheran Church v. County of Los Angeles*

In *First English*, the Supreme Court held that just compensation must be paid for temporary takings; invalidation of the offending law would not suffice.[206] To this extent, *First English* overruled the California rule (stated in *Agins v. City of Tiburon*[207]) that invalidation was the exclusive remedy.

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204. *Id.* at 653. The term "temporary taking" was first used to describe condemnations of leaseholds. *See, e.g., Commissioner v. Gillette Motor Transp.*, 364 U.S. 130 (1960); *United States v. Peewee Coal*, 341 U.S. 114 (1951); *United States v. Petty Motor Co.*, 327 U.S. 372 (1946); *United States v. General Motors Corp.*, 323 U.S. 373 (1945). In the one case in which the term described a restriction on use, rather than appropriation or seizure, no taking occurred. *See United States v. Central Eureka Mining Co.*, 357 U.S. 155, 179 (1958) (government order closing gold mine for 3 years did not amount to a taking).

205. 450 U.S. *at* 657 (describing the "temporary reversible quality of a regulatory 'taking'").

206. 482 U.S. 304 (1987).

207. 24 Cal. 3d 266 at 271, 598 P.2d 25 at 27 (Cal. 1979).

The notion of temporary takings can be seen as an effort to limit government's liability for takings, rather than to expand it. It gives government the option of rescinding or terminating whatever action is causing a taking, or to maintain it and pay compensation equivalent to condemnation of a fee. But to note that takings may be temporary is not the same as holding that temporary interferences with property are takings. *First English* leaves the *Agins* standard undisturbed for determining when a taking occurs.

2. Regulatory Delay

a) Agins

Agins is best known for establishing the modern test for regulatory takings. But the case also acknowledges a fact of life for regulators — delay. Among the claims asserted was that pre-condemnation delay and the abandonment of condemnation proceedings "were so unreasonable as to provide a separate basis for an action for inverse condemnation." *Agins v. City of Tiburon.*[208] The Supreme Court disagreed. "Mere fluctuations in value during the process of governmental decision-making, absent extraordinary delay, are 'incidents of ownership.' They cannot be considered as a 'taking' in the constitutional sense."[209]

In sum, only "*irreparable injury* [inflicted] upon the landowner" causes a taking.[210] Under *Agins,* so long as at the *end* of the planning process the owner retains the right to enjoy or profit from the property, no taking occurs.

b) How long can an agency delay

In *First English*, the Court reiterated that "normal delays in obtaining building permits" are not temporary takings.[211] In fact, regulatory delay may not even be justiciable. In *Williamson County v. Hamilton Bank*,[212] the developer claimed that denial of a subdivision plat, after an eight year planning process, constituted a temporary taking. Although the Court granted certiorari

208. *Id.* at 277-78.

209. *Agins v. Tiburon,* 447 U.S. at 263, n.9 (citations omitted).

210. *Id.* at 263. The requirement of "irreparable injury" originated in *Pumpelly v. Green Bay Co.*, 13 Wall. 166, 177-178 (1872), where the Court held police power enactments could not permissibly inflict "irreparable and permanent injury [subjecting property] to total destruction" without having to pay compensation.

211. 482 U.S. at 321.

212. 473 U.S. 172 (1985).

precisely to resolve the issue of temporary takings,[213] it dismissed the case as premature because the County had not reached a "final decision" regarding allowable use of the parcel.[214]

Although normal delays do not cause regulatory takings, extraordinary delays can. In *Mills Land and Water Company v City of Huntington Beach*,[215] the court found a temporary taking where the city had delayed for almost twenty years in approving a Local Coast Program, which prevented any meaningful development.

c) Moratoria

Most courts have held that planning moratoria of reasonable duration are constitutional.[216] However, in *Tahoe Sierra Preservation Planning Council*, the district court held that moratoria of any length were categorically unconstitutional. There, the Tahoe Regional Planning Agency imposed a two-year moratorium on development, to enable it to craft a zoning plan as mandated by congress. The court held that although the use restrictions were only temporary (lasting about 2½ years) and indispensable for orderly planning, the moratorium constituted a "temporary taking" which was compensable. It held that moratoria were not included within the *First English* exception for "normal delays."[217]

The Supreme Court reversed. Justice Stevens' majority opinion reasoned that property can no more be divided into temporal slices than functional or use slices. In neither case does deprivation amount to a taking unless the property as a whole is ren-

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213. *Id.* at 185.

214. *Id.* at 186.

215. 89 Cal.Rptr.2d 52 (Cal.Ct.App. 1999).

216. *See Santa Fe Village Venture v. City Of Albuquerque*, 914 F. Supp. 478, 483 (D.NM, 1995); *S.E.W. Friel v. Triangle Oil Co.*, 76 Md. App. 96, 103, 543 A.2d 863, 866 (Md. Ct. Spec. App. 1988); *Guinnane v. City and County of San Francisco*, 197 Cal. App. 3d 862, 241 Cal. Rptr. 787 (Cal. Ct. App. 1987). *See also* Frank Michelman, *The Jurisprudence of Takings*, 88 COLUM. L. REV. 1621 (1987) ("the First English decision does not reach regulatory enactments, even totally restrictive ones, that are expressly designed by their enacters to be temporary").

But there remains a difference between a temporary moratorium and restrictions of indefinite duration. *See, e.g., Seawall Associates v. City of New York*, 74 N.Y.2d 92, 100; 542 N.E.2d 1059, 1061 (1989), invalidated a 5-year moratorium that was "renewable for additional five-year periods as the City Council deems necessary." *See also Steel v. Cape Corporation*, 111 Md. App. 1, 677 A.2d 634 (Md. App. 1996) (invalidating six-year "moratorium" enacted in 1994 that replaced a permanent development ban enacted in 1971).

217. *Tahoe Sierra*, 34 F.Supp.2d at 1249.

dered valueless. "Logically, a fee simple estate cannot be rendered valueless by a temporary prohibition on economic use, because the property will recover value as soon as the prohibition is lifted."[218] Thus, even where a moratorium prohibits all viable *use* for a prescribed period of time, its *value* remains largely intact. This is not true, however, of government action that *permanently* takes all value (*e.g.*, *Lucas*, *First English*), even where the taking is later rescinded. In *temporary* takings cases it matters whether the temporary nature of government action is known when the act occurs, or only afterwards. In the former instance, the property will retain market value; in the latter, it will not (at least when suit is filed).

d) Illegal delays

In *Landgate, Inc. v California Coastal Commission*,[219] the landowner charged that a two year delay in the issuance of a development permit constituted a compensable taking. What sets this case apart from other cases of regulatory delay is that defendant agency had no jurisdiction over the property in the first place and had illegally prevented development.

The California Supreme Court held that the Coastal Commission made a good faith error and even if there is some diminishment of value during the process, a reasonable regulatory process designed to advance legitimate government interests is not a taking. Mere postponement pending resolution of a legal dispute is not enough to deny all economically viable uses. In fact, there was no basis for an as applied challenge until the regulatory agency had made a final decision. However, the court warned that the government cannot evade the requirements of the Fifth Amendment by fabricating a legal dispute, the administrative assertion of authority must advance legitimate government purposes. The fact that the landowner has to exhaust his administrative actions and wait for judicial determination of the validity of preconditions, is not a taking and is merely part of the normal development process.

A similar result was reached in *Buckley v. California Coastal Commission*,[220] where the Coastal Commission had again incorrectly asserted jurisdiction. Although denial of a permit by the Commission vas void, there was no temporary taking.

218. 535 U.S. at 332.
219. 17 Cal.4th 1006, 953 P.2d 1188 (Cal. 1998).
220. 68 Cal.App.4th 178, 80 Cal.Rptr.2d 562 (Cal. 1998).

IV.
DUE PROCESS CLAUSE

The due process clause has been the traditional vehicle for review of rate regulation, including rent control.[221] This remains true today, but mostly insofar as procedural due process is implicated by rate setting. For normative standards, courts have begun to look away from due process and towards the takings clause.

Substantive due process standards are discussed here because some courts still conflate due process and takings concepts when passing on rent control.[222] Ultimately, however, distinguishing the two claims is important in rate cases.[223]

A. *The Theory of "Confiscation"*

Rate regulation, including rent control, is said to be unconstitutionally "confiscatory" if regulated rates are set too low. The Supreme Court has experimented with several different formulations for the normative standard of when rates are so low as to be confiscatory, but most failed to survived the demise of economic due process.

Although the term is widely used, there is no textual constitutional prohibition against "confiscation" as such. That term originated as a blend of constitutional protections for property

221. *Pennell v. City of San Jose*, 485 U.S. 1 (1988); *Birkenfeld v. City of Berkeley* 17 Cal.3d 129, 130 Cal.Rptr. 465 (1976).

222. *See Kavanau*, 16 Cal.4th at 771 ("courts sometimes employ overlapping terminology and standards, treating the two clauses as a single constitutional protection of private property rights"). *See also* Rotunda & Nowak, *Treatise on Constitutional Law* (2d ed. 1992) § 15.12, p. 505, n. 59 ("Early Supreme Court opinions concerning utility rate regulation were written in terms of 'due process of law', but those opinions are now understood as establishing principles identical to those inherent in the takings clause").

For a comprehensive discussion on the relationship between due process and takings analysis in the context of rate regulation, see *Tennoco Oil Co. Inc. v. Dept. of Consumer Affairs*, 876 F.2d 1013 (1st Cir. 1989). 876 F.2d 1013. *See also Texaco Puerto Rico, Inc. v. Ocasio Rodriguez* (D. P.R. 1990) 749 F. Supp. 348, 353 ("the circuit's first step was to disentangle what it found to be this court's improper amalgamation of substantive due process and takings clause analyses"); *Smoke Rise, Inc. v. Wash. Suburban Sanitary Comm'n* (D. Md. 1975) 400 F. Supp. 1369, 1381 ("a claim of *deprivation* of property without due process cannot be blended as one and the same with the claim that property has been taken for public use, without just compensation").

223. *See Mountain Water Co. v. Montana Dep't of Public Serv. Regulation*, 919 F.2d 593 (9th Cir. 1990).

under the due process and takings clauses.[224] Conflation is hardly surprising given that the takings clause is made applicable to the states through the 14th amendment's due process clause. Moreover, due process concepts were often invoked in early takings cases as a source of normative law.

While these constitutional guarantees may once have been interchangeable, they now protect against distinctly different governmental actions and employ different substantive standards.[225] As stated by the California Supreme Court in *Kavanau*, "the due process protection focuses on the government's means and purpose. . . . The takings protection focuses on the impact of the government's action."[226]

Confiscation occurs under the due process clause where the rate setting agency acts arbitrarily or fails to give due consideration to the economic interests of the regulated entity.[227] In contrast, a taking occurs where rates are set so low as to render the regulated property valueless, or nearly so.[228]

Not only do the normative standards differ, so too do the available remedies and procedures under the two clauses. Just compensation is constitutionally required in takings cases. Damages may be available in due process cases under 42 U.S.C. § 1983, but only if the defendant is suable under that statute; states are not.[229]

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224. *See Covington and Lexington Turnpike Road Co. v. Sandford*, 164 U.S. 578, 597 (1896).

225. *See Nollan v. California Coastal Comm'n*, 483 U.S. 825, 835, n.3 (1987) ("no reason to believe . . . [that] the standards for takings challenges, due process challenges, and equal protection challenges are identical"); *see also Yee v. City of Escondido*, 503 U.S. 519, 532-37 (1992) (distinguishing between takings and due process claims); *Pennell v. City of San Jose*, 485 U.S. 1, 10 (1988) (same).

226. 16 Cal.4th at 771.

227. *CalFarm v. Deukmejian*, 258 Cal.Rptr. 161, 166 (1989) (citing *Nebbia v. New York*, 291 U.S. 502, 539 (1934)).

228. *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 312 (1989) (rate is confiscatory if it "jeopardize[s] the financial integrity of the compan[y]"); *First English Evangelical Lutheran Church v. County of Los Angeles*, 482 U.S. 304, 318 (1987) (denial of "all use of property" is a taking).

229. *Will v. Mich. Dept. of State Policeigan*, 491 U.S. 58 (1989). *See generally* L. Berger, *Public Use, Substantive Due Process And Takings — An Integration* (1995) 74 NEB. L. REV 843, 844 ("since the [due process and takings clauses] have entirely different purposes and underlying policies, appropriately the remedies for their breach should necessarily be quite different from each other"); Ross McFarlane, *Testing The Constitutional Validity Of Land Use Regulations* (1982) 57 WASH. L. REV. 715, 727 ("blending of substantive due process and takings into a single limitation on land use regulations" improperly "affect[s] the remedy applied)."

1. Modern Standard for Confiscation

Since the end of the *Lochner* era, courts have mostly taken a hands-off approach to substantive protection under due process. Two standards have emerged, one for economic regulation generally, and one geared toward rate regulation.

The general rule was stated in *Nebbia v. New York*.[230] "Price control, like any other form of regulation, is unconstitutional only if arbitrary, discriminatory, or demonstrably irrelevant to the policy the Legislature is free to adopt, and hence an unnecessary and unwarranted interference with individual liberty."[231]

This is the familiar and deferential rational basis standard. As such, it is concerned more with procedural than substantive elements of regulatory action. Thus, due process is violated where the rate setting agency acts in an arbitrary or capricious manner,[232] or fails to fairly consider the interests of both the public and the regulated company.[233]

The substantive rule was stated in *Federal Power Comm'n v. Natural Gas Pipeline Co.*,[234] a rate is too low if it is "so unjust as to destroy the value of [the] property for all the purposes for which it was acquired," and in so doing "practically deprive[s] the owner of property without due process of law."[235]

This standard — destruction of value — is also found in regulatory takings doctrine. Indeed, the takings clause is emerging as the preferred vehicle for normative review of rate orders.

Theoretically, the same approaches should be used in rent control cases. In *Santa Monica Beach*, the California Supreme Court declined to "decide whether the standard of review for rent control legislation is identical to the rational relationship test employed in other price control schemes." But it did hold that "the standard of review for generally applicable rent control laws must be at least as deferential as for generally applicable zoning

230. 291 U.S. 502 (1934).

231. *Id.* at 539.

232. *CalFarm*, 258 Cal.Rptr. at 163.

233. *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 611 (1944). Some courts quite candidly apply heightened review to rent control laws under substantive due process. *See e.g., Guimont v. Clarke*, 121 Wash.2d 586, 609 (1993) (finding tenant relocation assistance law violated due process because it was "unduly oppressive on the landowner"). Such cases are vestiges of an earlier era. Because they do not rely on the notion of confiscation, or otherwise employ price control analysis, they are beyond the scope of this paper.

234. 315 U.S. 575 (1942).

235. *Id.* at 585.

laws and other legislative land use controls. Thus, the party challenging rent control must show 'that it constitutes an arbitrary regulation of property rights.'"[236]

Nonetheless, some courts remain fairly proactive in protecting property under the due process clause, especially in rent control cases. They will be described below.

a) Zone of Reasonableness

All that is required for price control to satisfy substantive due process is that the regulated rate be within a "broad zone of reasonableness."[237] Although this is a deferential standard, the very term suggests both upper and lower limits as to what courts will consider reasonable.

The lower end defines the point below which rates are so low as to be confiscatory. The regulatory takings standard apples here. So too does the rational basis due process standard of arbitrary and capricious. Thus, if a rate is set lower than necessary to accomplish the law's stated purpose, it is arbitrary and hence unconstitutional.[238] This might occur, for instance, where regulated rates prevent the property owner from attracting and maintaining capital. When that occurs, the regulated entity (e.g., public utility) will eventually be driven out of business, and unable to provide the public service that formed the basis for regulation in the first place.

The zone of reasonableness has a lower end. In theory, it also has an upper end. That is presumably where rates are so high as to defeat the regulatory purpose. But that problem doesn't appear to raise any constitutional issues, and so is absent from the caselaw.

Where, within the zone of reasonableness, an agency selects a specific rate is really a matter of legislative discretion.[239] At most, it may raise procedural due process issues; *i.e.*, whether the agency has given due consideration to the competing interests of

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236. *See Santa Monica Beach v. Santa Monica Rent Central Board*, 19 Cal. 4th 952, 968 P.2d 993 (1999).

237. *Permian Basin Area Rate Cases*, 390 U.S. 747, 770 (1968), 88 S.Ct. 1344, 1361; *20th Century Ins. Co. v. Garamendi* 8 Cal.4th 216, 294 (1994), 32 Cal.Rptr.2d 807, 856 (1994).

238. *Federal Power Comm'n v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585-586 (1942).

239. *Federal Power Comm'n Co. v. Hope Natural Gas Co.*, 320 U.S. at 603 ("the fixing of 'just and reasonable' rates involves a balancing of the investor and the consumer interests").

provider and consumer. Indeed, most due process rate cases are decided on the basis of procedural concerns, rather than normative evaluations of particular rates.[240]

b) Fair Return Requirement

Regulated rates must provide the company or owner a "fair return." The term was coined during the *Lochner* era, when the Supreme Court held that public utilities were constitutionally entitled to a fair return on the value of their investments.[241] As employed in those cases, this typically required that rates be set at or near market levels.[242]

Even after the abandonment of *Lochner*, rate regulation cases continued to employ the *fair return* terminology, or its equivalent — "just and reasonable return on property." But market-level returns are no longer required. Indeed, the modern Court refuses to set any particular standard. This is because "neither law nor economics has yet devised generally accepted standards for the evaluation of rate-making orders."[243] Thus, the constitution "within broad limits leaves the States free to decide what rate setting methodology best meets their needs"[244] And they've "employed a veritable smorgasbord of administrative standards by which to determine rent ceilings.[245]

As currently understood, "fair return" is the antonym of "confiscation." Any rate (or rent) that falls within the broad zone of reasonableness also provides a fair return. But it is an unfortunate term for constitutional analysis. Courts tend to think of themselves as protectors of "fairness." As a result, many rent control laws have fallen under the rubric of fair return.

2. Particular Problems in Confiscation

a) Determining the rate base and rate of return

Whether a landlord is earning a "just and reasonable rate of return" depends both on the "rate" and on the "rate base." For

240. *See, e.g., Birkenfeld v. Berkeley*, 17 Cal.3d 129, 550 P.2d 1001 (1976) (invalidating rent control law because rent agency was precluded from considering rent increase requests in a timely fashion).

241. *Allgeyer v. State of Louisiana*, 165 U.S. 578 (1897); *Smyth v. Ames*, 169 U.S. 466 (1898).

242. *See Duquesne*, 488 U.S. at 308.

243. *Permian Basin Area Rate Cases*, 390 U.S. at 790.

244. *Duquesne*, 488 U.S. at 316.

245. *Fisher v. Berkeley*, 37 Cal. 3d 644, 679-80, 209 Cal.Rptr. 682, 712 (1984).

instance, a profit of $10,000 per year is quite healthy if the property is a single family house worth $100,000, but paltry if the property is a multi-unit building worth $1,000,000. It is a 10% versus a 1% rate of return. Obviously, the constitutionality of a particular rate or rent level cannot be determined without first determining the appropriate rate base.[246]

Capital improvements made to the property typically increase the rate base (as it does with utility rate regulation). But what if those improvements are neither wanted by nor benefit the tenants. If all improvements were entitled to earn the specified rate of return, the landlord could increase rents dramatically by "improving" the property. This becomes an easy way to "gentrify" a building.

In utility cases, the Supreme Court has ratified the "used and useful" theory. This means an improvement need not be included in the rate base unless it "is used and useful in service to the public."[247] Rent control laws may similarly disallow improvements or unnecessary expenses unless they somehow improve the premises. It may be prudent for the landlord to obtain pre-authorization from the rent agency, where that is available.

b) Unprofitable and loss operations

"Rates which enable [a] company to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for the risk assumed certainly cannot be con-

246. Debt service complicates the equation. Assume the $1 million apartment building has an $800,000 mortgage. Even if the rent agency decides to use a 10% rate of return, is she entitled to $20,000 in rent on her $200,000 equity, or $100,000 on the full value of her property?

The problem with the former is that debt service becomes a compensable item of operating expense. Thus, if the landlord has a 7% 30-year mortgage on her $800,000 loan, her mortgage payments will be $64,000 per year, but if she took out a 12% loan (say during a period of high interest rate), then her payments will be $99,000 per year. Why should the tenants pay more simply because the landlord has a high rate or made a bad investment?

As a result, most rent formulas exclude debt and debt service. In the example, the rate of return would be applied against the full value of the property (the rate base). The landlord would pay debt service and expenses out of her rental income. If a 10% rate of return is applied to a $1 million rate base, she earns $100,000 per year, which she gets to divide between herself and her debt service. If she has a 7% loan, she'll have $36,000 for profit and expenses (which turns out to be an 18% return on her $200,000 investment). If she has a 12% loan, then she'll wind up with $1,000 in profit (a .5% return on investment). In short, the landlord is responsible for her own investment decisions.

247. *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 302 (1989).

demned as invalid, even though they might produce only a meager return on the so called 'fair value' rate base."[248] This suggests two things: (1) some positive income stream is constitutionally required, but (2) no particular level of profitability is.[249]

Forced loss operations, at least over the long term, would tend to destroy the value of property.[250] But that does not mean all aspects of a regulated enterprise need be profitable. Whether a regulation of prices is reasonable or confiscatory depends on the bottom line. "[I]t is the result reached not the method employed which is controlling."[251] Thus, so long as the overall rate is constitutional, the fact that particular line items may not generate adequate returns is irrelevant. For instance, a landlord might be denied a rent increase for a capital improvement or other expense, so long as the rent level overall is non-confiscatory. "There is no constitutional or other requirement that all reasonable expenses and prudent investments must be allowed."[252] Indeed, a "regulated firm has no constitutional right even against a loss."[253]

c) *Rate Moratoria*

It is not uncommon for regulatory agencies to freeze, or even roll-back, rents or other rates. This usually occurs when price controls are first enacted in an industry to give the agency time to develop a rate setting methodology.

Rate freezes of limited duration are generally upheld.[254] Rollbacks to rates existing on an earlier date can also be constitutional. But constitutionality (for both freeze and rollback)

248. *Federal Power Comm'n*, 320 U.S. at 605, *See also Duquesne Light Co. v. Barasch*, 488 U.S. at 310.

249. Regulated rents must provide enough "net operating income" (NOI) to cover reasonable expenses, including debt service. But, imprudent expenses and extraordinary debt service need not be covered. There is no constitutional requirement that a landlord earn a profit.

250. *See, e.g., Mekuria v. Washington Metro. Area Transit Authority*, 45 F.Supp.2d 19 (D.D.C. 1999) (construction of monorail station, which prevented vehicle and pedestrian access to business, caused a taking because of resulting total rental loss).

251. *Federal Power Comm'n*, 320 U.S. 591, 602 (1944).

252. *20th Century*, 32 Cal.Rptr.2d at 833.

253. *Id.* at 873; it "has no constitutional right to a profit." *Id.* at 876 (citing *Jersey Central*, 810 F.2d at 1180-81); *Park Avenue Tower Assoc's v. City of New York*, 746 F.2d 135, 140 (2d Cir. 1984) (court defined the standard as whether the owner was precluded "from realizing any profit whatsoever;" a "reasonable return" was not constitutionally required).

254. *See generally Permian Basin Area Rate Cases*, 390 U.S. 747 (1968) (upholding 7 year freeze on rate filings), and cases collected in *CalFarm*, 48 Cal.3d at 819-20.

presupposes that rates on the base date were non-confiscatory.[255] There must also be some mechanism for relief as required in individual cases.[256] Rent control cases are in accord.[257] Of course even valid rates of return can become confiscatory if frozen long enough.[258, 259]

Rent increases that are phased in over time are somewhat similar to freezes. Gradual increases protect tenants from excessive rents. But they also deny immediate full relief to landlords. Such a compromise would ordinarily lie within the agency's discretion to select rates from within the *zone of reasonableness*. It is a different situation of course if, during the phase-in period, rates are below confiscatory levels.

In *Kavanau v. Santa Monica Rent Control Bd.*,[260] the court held that a 12 % annual limit on rent increases deprived the landlord of a fair return. This might have been a correct result were the rents so far below confiscatory levels that a 12% increase failed to bring them up. The court erred however, by including in the rate base unnecessary expenses and the cost of debt service. It also treated capital improvements as an expense, thereby allowing for full cost recovery each year over the improvements' useful life. (The court ordered a 60% rent increase which the landlord was unable to collect because it raised regulated rents above market level.)

As *Kavanau* demonstrates, lower courts are often not familiar with the arithmetic of rate regulation. Perhaps it is for this rea-

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255. *Id.*

256. *Id.*; *Birkenfeld v. City of Berkeley*, 17 Cal.3d 129, 130 Cal. Rptr. 465 (1976).

257. *See, e.g., The Greystone Hotel Co. v. City of New York*, 13 F.Supp.2d 524 (D. N.Y.S.D. 1998) (three year denial of rent increase was not a taking). *But see Adamson Cos. v. City of Malibu*, 854 F.Supp. 1476 (C.D. Cal. 1994) (comprehensive scheme employing rent rollback and freeze partially violated due process).

258. *Fisher v. City of Berkeley*, 37 Cal. 3d 644, 683, 693 P.2d 261 (1984) (although rent control "may properly restrict landlords' profits on their rental investments, it may not indefinitely freeze the dollar amount of those profits without eventually causing confiscatory results"); *Cotati Alliance for Better Housing v. City of Cotati*, 148 Cal.App.3d 280, 293, 195 Cal.Rptr.825, 828 (1983) ("If the net operating profit of a landlord continues to be the identical number of dollars, there is in time a real diminution to the landlord which eventually becomes confiscatory").

259. There's a difference between freezing rates and freezing rates of return. The former keeps the rates constant over time. As operating expenses increase, profits decrease. The latter freezes profits, so that there is an exact correlation between increases in expenses and increases in rates. Rate freezes are likely to become confiscatory much sooner than rate of return freezes. But those too can be held invalid as inflation erodes the buying power of frozen profits.

260. 19 Cal.App.4th 730, 23 Cal.Rptr.2d 724 (1993).

son that prevailing doctrine leaves these matters to specialized agencies with the requisite expertise.

B. *Preference for Takings Analysis*

In addition to the due process inquiry, rates can be found confiscatory in another sense – if they are set so low as to constitute a regulatory taking. The takings clause is now the preferred substantive standard for assessing rate orders.[261] This is because an "explicit textual source of constitutional protection . . . preempts a more generalized substantive due process claim" brought under the Fourteenth Amendment.[262]

However, as shown above, the takings standard is a fairly difficult one to meet. It requires that the property be deprived of virtually "all viable economic use,"[263] or at least that some "deep financial hardship" be imposed.[264] Mere reduction in value resulting from regulation does not constitute a taking.[265]

As a result, some courts persist in using due process norms — and old ones at that — in reviewing orders of rent setting agencies. Some have even equated — once again — the two clauses.[266] Even when admonished not to do so, lower courts' inclination towards substantive due process persists. For instance, heightened scrutiny under the "substantially advance" prong of regulatory takings is strongly reminiscent of the *Lochner* era. It invites courts to make their own judgments of economic rationality and which social interests deserve state protection. Just as protecting the economic and physical health

261. *Duquesne*; *Armendariz v. Penman*, 75 F.3d 1311, 1325-26 (9th Cir. 1996) (constitutional protection against takings for private use grounded solely in the Takings Clause).

262. *Id.* at 1321-22. *See also Macri v. King County*, 110 F.3d 1496, 1500 (9th Cir. 1997) (holding that constitutional protection against land use restrictions that do not "substantially advance legitimate state interests" grounded solely in Taking Clause); *20th Century*, 32 Cal.Rptr.2d at 855-860.

263. The *Lucas* and *Agins* standards are now routinely employed by rate setting agencies. *See, e.g., Re Competition for Local Exchange Service* (Cal. PUC 1995) 165 P.U.R.4th 127.

264. *20th Century*, 32 Cal.Rptr.2d at 832 (citing *Jersey Central Power & Light v. F.E.R.C.*, 810 F.2d 1168, 1182 (D.C. Cir. 1987)).

265. *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104 (1978).

266. *See, e.g., Kavanau* at Slip Op. at 14, 16 (state action that "ignor[es] the due process rights of private citizens . . . must, perforce, result in a taking of property"). The California Supreme Court disagreed. *Kavanau v Santa Monica Rent Control Board*, 16 Cal.4th 761 (Cal. 1997) (when there is a due process violation with an available due process remedy, then there is no need to continue with a takings inquiry).

of bread makers was an illegitimate goal in *Lochner*, protecting the investments of mobilehome owners was held in *Cashman* to not outweigh the ground owner's right to capture future value.

V.
CONCLUSION

Second generation rent control laws[267] began appearing a quarter-century ago in cities with housing shortages or inflated markets. They invariably limit landlord profits and often affect property rights. Because private property is considered sacrosanct in America, these impacts spur a high volume of litigation. But the Supreme Court has made clear on several occasions that rent control is generally constitutional. But just when municipal officials think that a particular challenge has run its course, a new spate of cases emerges with innovative claims. The new theories, such as fractional property rights, are often successful at first, but ultimately rejected by the Supreme Court.

Rent control may be unwise and economically inefficient (there are many arguments suggesting both), it may benefit the wrong classes of tenants (some argue it causes gentrification), and it may be unfair (singling out particular segments of society to provide social subsidies), but these are political arguments, not legal ones. Unless courts are to supplant the role of legislatures in formulating economic policy, they must defer to those judgments and avoid policy making in their legal opinions. As a general matter, rent control is constitutional. Hence, the judicial function should be carefully circumscribed. Adventurism and *laissez faire* activism is no more justified under the takings clause than it is under economic substantive due process. The *Lochner* era should remain in our past, not in our future.

267. Early, or first-generation, laws appeared following World War I and II. They were often perceived as temporary measures responding to housing emergencies. Modern, or second-generation, laws are more permanent features of general housing regulation.