



# Ninth Circuit Reverses Course: Rent Control Ordinance Does Not Constitute Regulatory Taking

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More than a year ago, the Ninth Circuit Court of Appeals issued its controversial regulatory takings opinion in *Guggenheim v. City of Goleta*, holding that the City of Goleta's rent control ordinance constituted a taking. Last week, the Court reversed itself, holding that the Guggenheims have no takings claim against the City.

The Guggenheims, the owners of a mobile home park, claimed that the City of Goleta's rent control ordinance had the effect of transferring the vast majority (as much as 90 percent) of the property's value to the tenants, constituting a regulatory taking. The Ninth Circuit issued the initial *Guggenheim* opinion in September 2009, siding with the owners. The Court remanded the case for a trial on the amount of compensation the owners should be awarded. At the time, the opinion was hailed by property rights advocates as a rare victory in federal takings jurisprudence.

Nearly six months after publishing its opinion, however, the Ninth Circuit granted a request from the City, ordering an *en banc* hearing (a new hearing before a larger panel of judges). Just as 2010 was winding to a close, the Ninth Circuit issued its new *Guggenheim* opinion, reversing its earlier decision, and holding that **Goleta's ordinance does not constitute a taking.**

## Regulatory Takings, Some Background

A "regulatory taking" occurs when government regulation goes too far, "taking" property away from its owner. At one end of the spectrum, takings claims are easy to understand. Where a government regulation eliminates all economically viable use of property, it constitutes a taking. But government regulation rarely eliminates all economic uses of property.

In cases where a regulation leaves some potential economic value in the property, the test is more complicated. In *Penn Central Transportation Co. v. New York City*, 438 U.S. 104 (1978), the Court held that takings claims should be analyzed by looking at three factors: (i) the economic impact of the regulation on the claimant; (ii) the extent to which the regulation has interfered with investment-backed expectations; and (iii) the character of the governmental action.

But before courts ever address the Penn Central test, regulatory takings claims must overcome huge procedural hurdles. In particular, a federal takings claim generally is not ripe unless the owner first exhausts all state court remedies. In exhausting state-court remedies, owners typically wind up with a final state-court decision on the merits which federal courts then conclude has a *res judicata* – or conclusive – effect on the subsequent federal lawsuit. In other words, a property owner faces the ultimate "Catch 22": if the owner litigates to a final decision on the merits in state court, the federal claim is barred, and if the owner fails to litigate to a final decision on the merits in state court, the federal claim is not ripe.

Thus, not surprisingly, federal regulatory takings claims only rarely proceed to a hearing on the merits. In fact, **prior to Guggenheim, the Ninth Circuit had never reached the merits of a Penn Central claim.**

### **The Original Guggenheim Opinion**

When the Ninth Circuit navigated its way through all of the procedural obstacles, reached the merits, and found that a taking had occurred, the original *Guggenheim* opinion understandably generated some buzz. Of particular importance, the court held that failure to proceed to a final decision in state court is not always fatal to a federal claim.

The court held that the City's rent control ordinance flunked the *Penn Central* test, and the case was remanded to the trial court to determine how much compensation the mobile home park owner would be paid by the City of Goleta. But before the compensation hearing could occur, the Court ordered the new, *en banc* hearing.

### **The New Guggenheim Opinion**

Following the *en banc* hearing, the Ninth Circuit reached a different conclusion. The Court concluded that the Guggenheims failed to establish the "investment-backed expectations" required to state a takings claim under *Penn Central* because the rent control ordinance preexisted the Guggenheims' purchase of the property.

While the decision tends to fall in line with the general conception that proving a regulatory taking is extremely difficult, the fact that the Ninth Circuit waded through the procedural landmines and reached the merits is hugely significant. Merely by reaching the merits of the takings claim, the Ninth Circuit broke new ground, meaning the decision still qualifies as a "victory," at least of sorts, for property owners.

### **Lessons Learned**

Despite the Ninth Circuit's finding that the City's rent control ordinance did not constitute a taking, government agencies still must be aware of the risks of exposure to regulatory takings claims. The simple fact that the Court reached the merits is hugely significant, and it may signal a turning of the tide for federal takings claims.

With respect to the ordinance at issue in *Guggenheim*, the Ninth Circuit may well have reached a different conclusion had the ordinance been enacted while the Guggenheims owned the property. Thus, cities and counties contemplating similar rent control ordinances should weigh carefully the degree to which the ordinance will effect a transfer of value from the property's owner to the tenants.

Where that transfer is substantial, agencies should anticipate legal challenges, with owners who can establish the necessary "investment-backed expectations" trumpeting the Guggenheim decision as proof that a taking occurred. Time will tell whether the lower courts actually read such an implied holding into the *Guggenheim* decision.

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