U. S. Court of Appeals Docket No. 06-56306
Lower Court Case No. CV 02-02478 FMC (RZx)

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

DANIEL GUGGENHEIM, SUSAN GUGGENHEIM AND MAUREEN H. PIERCE
Plaintiff-Appellants,

vs.

CITY OF GOLETA, et al.
Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA, LOS ANGELES
District Court Case No. CV 02-02478 FMC (RZx)

PETITION FOR PANEL REHEARING AND REHEARING EN BANC

Decision: September 28, 2009
Panel: Alfred T. Goodwin, Andrew J. Kleinfeld, and Jay S. Bybee, Circuit Judges

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STATE STATUTES

I. FRAP RULE 35 STATEMENT

This Petition seeks rehearing to correct a split Panel decision (Bybee, J., Goodwin, J., Kleinfeld, J. dissenting) that conflicts with precedent regarding facial takings challenges to mobile home rent control regulation. The Panel decision improperly applies—and therefore conflicts with—*Penn Central Transportation Co. v. City of New York*, 438 U.S. 104 (1978) and rehearing is necessary to secure and maintain uniformity of decision. In addition, rehearing is warranted to address the following questions of exceptional importance:

1. Is a plaintiff still required to prove that no set of circumstances exists under which a rent control regulation would be valid in order to prevail on a facial takings claim?

2. Does interference with distinct, investment-backed expectations remain a key factor in a *Penn Central* analysis of a facial takings claim?

3. Does the property owner's continuing ability to receive a fair return on investment under a mobile home rent control regulation remain a viable defense to a facial takings claim?

4. Is rent control regulation now considered a regulatory taking on the theory that such regulation is almost a physical taking, singling out mobile home park owners and forcing them to rent space at below market rates?

5. Should the City be allowed to defend its regulation on the merits, if

the Court of Appeals finds that the district court's *sua sponte* judgment should be reversed?

These are questions of exceptional importance not only to the parties, but also to the many cities and counties throughout the nation that have adopted rent control ordinances in reliance on precedent upholding governmental authority to regulate rents. The Panel decision repeatedly criticized rent control, (Slip Opinion ("SO"), pp. 13847-48, 50-51, 65-66) but such policy decisions rest with the legislative branch. Moreover, precedent regarding facial takings challenges to rent control regulation should not be changed solely on the opinion of two Justices. Rehearing, particularly rehearing en banc, is necessary to preserve uniformity of decision on this exceptionally important issue.[1]

II. INTRODUCTION

The Panel decision appears to be the first to apply the *Penn Central* factors to find a mobile home rent control regulation invalid on its face. The Panel held Defendant City of Goleta's ("City") mobile home rent control ordinance to be invalid on its face as a taking even though (1) the ordinance allows the Plaintiffs mobile home park owners ("Park Owners") to achieve a fair rate of return on investment; and (2) the ordinance does not interfere with *any* distinct investment-backed expectations.

[1] The City respectfully requests an opportunity for additional briefing and argument on rehearing to address the new law created in the Panel decision.

This unprecedented holding rests on the theory that mobile home rent control ordinances cause a "wealth transfer" from park owners to incumbent tenants based on the "transfer premium." SO, p. 13846. The theory is that under rent control, a prospective purchaser of a mobile home in a rent-controlled park will pay more for the mobile home than it is worth simply because it so located; the difference between the value of the coach and the purchase price is the "transfer premium." SO, p. 13847. There are myriad flaws with the Panel's reliance on this theory, which will be explained below. But it is worth noting at the outset that the "wealth transfer" theory has appeared before in different guises, and the United States Supreme Court has rejected it.

In the theory's prior incarnations, rent control opponents argued that the "wealth transfer" constitutes a physical taking. See, e.g., *Hall v. City of Santa Barbara*, 833 F.2d 1270 (9th Cir. 1986). But the Supreme Court flatly rejected that argument in *Yee v. City of Escondido*, 503 U.S. 519, 527 (1992). Undeterred, rent control opponents then claimed that even if not a physical taking, the rent control "wealth transfer" constitutes a regulatory taking because such a transfer does not substantially advance a legitimate governmental interest. See, e.g., *Richardson v. City and County of Honolulu*, 124 F.3d 1150 (9th Cir. 1997). Once again, the Supreme Court rejected the challenge to rent control, holding in *Lingle v. Chevron U.S.A., Inc.*, 544 U.S. 528, 532 (2005), that the "substantially

advances" test is not applicable to a takings claim.

The Panel decision represents the third bite at the takings apple. In this latest version of the "wealth transfer" argument, the split Panel declared the City's mobile home rent control ordinance facially invalid under *Penn Central*. This conclusion completely changes the law in the area of facial regulatory takings claims, making rehearing, particularly rehearing en banc, necessary.

III. FACTUAL BACKGROUND: THE PARK OWNERS PURCHASED THE PARK SUBJECT TO RENT CONTROL

Park Owners purchased Rancho Mobile Estates mobile home park in 1997; the park at that time was located in an unincorporated portion of the County of Santa Barbara. SO, p. 13814. When they purchased, the County had a rent control ordinance in place regulating rents for mobile home parks. *Id*. In fact, that version of the ordinance had been in place since 1987. *Id*.

In February 2002, the City incorporated, and Rancho Mobile Estates fell within the new City's boundaries. As required under California law (Cal. Gov't Code § 57376), the new City immediately adopted the County's Ordinance Code, including the rent control ordinance without change, titled "Mobilehome Control" ("Ordinance"). The Ordinance is similar to other such regulations throughout California. It allows an automatic, annual rent increase of up to 75% of the increase in the Consumer Price Index, or 5%, whichever is less. SO, p. 13812; Ordinance §§ 11A-5(a)(2); (a)(3); (d)(B); (g). The Ordinance also includes a

detailed discretionary rent increase provision. SO, pp. 13814-18; Ordinance §§ 11A-4, 11A-5.[2]

A month after the City's incorporation, Park Owners brought this action, alleging both state and federal claims, including facial challenges to the Ordinance on takings, due process and equal protection grounds. Procedurally, the case has a convoluted history. SO, pp. 13814-13818. The Park Owners appeal from a judgment based on the court's *sua sponte*, pre-trial Order to Show Cause why judgment should not be entered in the City's favor.[3]

IV. LEGAL BACKGROUND: *PENN CENTRAL'S* THREE PART TAKINGS TEST

The Panel decision purports to apply the *Penn Central* test in finding the Ordinance facially invalid. It is therefore necessary to understand *Penn Central's* facts and holding. In *Penn Central,* the Supreme Court considered an as-applied challenge to an ordinance that placed restrictions on the development of individual historic landmarks. *Penn Central*, 438 U.S. at 107. The property owner in that case had entered into a contract with a developer to build a multi-story office building atop the terminal; under the agreement, the developer would pay the property owner $1 million a year during construction and at least $3 million a year

[2] The City has attached a complete copy of Chapter 11A as an addendum to this Petition for the Court's convenience.

[3] Park Owners also appealed the district court's ruling on their takings, equal protection and due process claims. Because the Panel decision followed precedent and correctly affirmed the district court's ruling on the due process and equal issues, the City does not present them for rehearing.

thereafter. *Id.* at 116. After being denied permission to construct the building, the property owner brought a lawsuit claiming the ordinance as applied was a taking. The Supreme Court held that no taking had occurred. *Id.* at 117-18.

In reaching that holding, the Court identified "several factors that have particular significance" as follows:

> The economic impact of the regulation on the claimant, and particularly, the extent to which the regulation has interfered with distinct investment-backed expectations are, of course, relevant considerations. . . . So too is the character of the governmental action.

Id. at 124. Under *Penn Central,* therefore, a regulatory takings analysis focuses on: (1) the regulation's economic impact; (2) the regulation's interference with distinct, investment-backed expectations; and (3) the character of the governmental action. Cases finding a *Penn Central* taking are exceedingly rare, and only involve "extreme circumstances." *U.S. v. Riverside Bayview Homes,* 474 U.S., 121, 126 (1985).

V. ARGUMENT

A. The Panel Decision Improperly Found A Facial Taking Without Requiring The Property Owner To Prove That No Circumstances Exist Under Which The Ordinance Could Be Valid.

Black letter law holds that on a facial challenge to an ordinance, the plaintiff must prove that "no set of circumstances exists under which the [a]ct would be valid." *United States v. Salerno,* 481 U.S. 739, 745 (1987); see also, *Sprint Telephony PCS v. County of San Diego,* 543 F.3d 571 (9th Cir. 2008) (confirming that for all facial challenges outside of the First Amendment context, the *Salerno*

standard applies). The Panel decision concedes as much, citing *Salerno's* standard as controlling the Park Owners' facial challenge. SO, p. 13836. But although the Panel sets forth the *Salerno* standard, it does not apply it to Park Owners' takings claim. Nowhere in the decision does the Panel make the *Salerno* finding, and nowhere in the record do the Park Owners make a *Salerno* showing. Rehearing is necessary to require Park Owners to make the showing required before finding an ordinance invalid on its face.

B. In Analyzing *Penn Central's* Economic Impact Factor, The Panel Decision Departed From Precedent To Find A Taking Even Though The Ordinance Allows A Fair Rate Of Return.

The Panel's decision places almost exclusive weight on *Penn Central's* economic impact factor, concluding that the Ordinance's economic impact on Park Owners was so significant as to be a taking. Noting that the Park Owners "'would have earned more—perhaps much more—if'" not for the Ordinance, the Panel finds a taking because the "wealth transfer from the Park Owners to their tenants is a naked transfer accomplished by the mere enactment of the [Ordinance]." SO, pp. 13851, 54. This is not supported by *Penn Central* and marks a departure from precedent holding that the relevant focus when analyzing a takings claim is on both diminution of value *and* the ability to receive a fair return on investment, and not on whether the regulation limits the property owner's ability to achieve maximum profits.

1. The Proper Focus In Analyzing Economic Impacts Is On Diminution In Value And Fair Return On Investment.

As this Circuit explained in *Garneau v. City of Seattle*, 147 F.3d 802, 807-08 (9th Cir. 1998), a plaintiff bringing a facial takings claim "must show that the diminution in value is so severe" that the regulation has "essentially appropriated their property for public use." This standard is rarely met because it is well-settled that even a substantial decrease in value does not constitute a taking. See, e.g., *Concrete Pipe and Products of California v. Construction Laborers Pension Trust For Southern California*, 508 U.S. 602, 645 (1993) (46% payment of shareholder equity not serious enough to be a taking); *Village of Euclid v. Ambler Realty Co.* (1926) 272 U.S. 365, 384 (reduction of $10,000 per acre to $2,500 per acre not a taking); and *Hadacheck v. Sebastian*, 239 U.S. 394, 405 (1915) (reduction of $800,000 to $60,000 not a taking). The Panel, however, failed to follow this precedent.

Courts have also looked to fair rate of return on investment in considering takings challenges. Indeed, in rejecting the takings claim, the *Penn Central* Court observed that the property owner "not only profit[ted] from the Terminal but also obtain[ed] a 'reasonable return' on investment." *Penn Central*, 438 U.S. at 136. In *Manufactured Home Communities, Inc. v. City of San Jose*, 420 F.3d 1022, 1028, 1031 (9th Cir. 2005) the Ninth Circuit held that it was bound by California's state court determination that a rent control regulation was valid because it provided a

fair rate of return on investment.

In this case, the Panel discounted the uncontroverted evidence showing that (1) the Ordinance that the City adopted was the same as the ordinance in place when the Park Owners purchased (SO, p. 13814); (2) the Park Owners' purchased the park for a lower price because of rent control regulation (SO, p. 13856); (3) the Park Owners earned a reasonable return on investment under the Ordinance, approximately 10% a year (SO, p. 13853) and (4) the value of Park Owners' property had in fact appreciated significantly. (ER 1396). Given this uncontroverted evidence, a compelling argument can be made to a trier of fact that the Ordinance had no economic impact whatsoever on Park Owners' property.

2. The Wealth Transfer Theory Departs From Precedent In Focusing On Only One Element Of The Park Owners' Property Interest.

Another flaw in the Panel's reasoning is that the wealth transfer theory itself departs from precedent because it focuses on only one element of the Park Owners' property interest. It analyzes the Park Owner's property interest in the profits potentially recoverable from selling individual pads in the park. This theory improperly focuses on individual segments of the land and individual elements of the Park Owners' property interests, and not on the property in its totality. This is contrary to precedent.

Indeed, *Penn Central* rejected an argument that a regulation was a taking because it interfered with the property owner's "air rights," or the ability to build

up. The Court stated that "'[t]aking' jurisprudence does not divide a single parcel into discrete segments and attempt to determine whether rights in a particular segment have been entirely abrogated. . . this Court focuses rather both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole." *Penn Central*, 438 U.S. at 130-31; see also, *Keystone Bituminous Coal Ass'n v. DeBenedictis*, 480 U.S. 470, 498 (1987). In *Andrus v. Allard*, 444 U.S. 51, 65-66 (1979), the Supreme Court viewed the right to sell property as just one element of the owner's property interests. The Panel decision conflicts with this precedent.

C. In Analyzing *Penn Central's* Expectations Factor, The Panel Decision Departed From Precedent And Found A Taking Even Though The Ordinance Did Not Interfere With Any Distinct, Investment-Backed Expectations.

The Panel's decision regarding *Penn Central*'s investment-backed expectations factor is equally a departure from precedent. Indeed, the Panel decision creates dangerous new law in effectively rendering investment-backed expectations—which *Penn Central* described as a key factor—irrelevant.

1. The Ordinance Does Not Interfere With Any Distinct, Investment-Backed Expectations.

Under *Penn Central*, a key focus in any takings analysis must be on the regulation's *interference* with *expectations* that are (1) *distinct* and (2) *investment-backed.* The question is whether a law "so frustrate[s] distinct investment-backed expectations as to amount to a 'taking.'" *Penn Central*, 438 U.S. at 127. The purpose behind this requirement "is to limit recoveries to property owners who can

demonstrate that 'they bought their property in reliance on a state of affairs that did not include the challenged regulatory regime.'" *Cienega Gardens v. United States*, 331 F.3d 1319, 1346 (Fed. Cir. 2003). A reasonable investment-backed expectation "must be more than a 'unilateral expectation or an abstract need.'" *Ruckelhaus v. Monsanto Co.*, 467 U.S. 986, 1005 (1984).

Park Owner did not prove the existence of *any* interference with reasonable, investment-backed expectations. Notwithstanding the lack of any such interference, the Panel decision found the Ordinance invalid on its face. This is a startling departure from precedent.

2. The Panel decision misapplied *Palazzolo v. Rhode Island.*

In making this unprecedented leap, the Panel relied on *Palazzolo v. Rhode Island*, 533 U.S. 606 (2001). *Palazzolo* addressed whether a takings challenge to a land use regulation could be rejected simply because the pre-regulation landowner, a sole shareholder corporation, transferred the land to its sole shareholder individually after the regulation was adopted. The Supreme Court held that this technical change in ownership did not act as a per se bar to preclude the shareholder from bringing a takings claim.

Notably, Justice O'Connor's concurrence in *Palazzolo* makes it clear that *Palazzolo* does not modify the *Penn Central* test or render the lack of investment-backed expectations irrelevant. Justice O'Connor wrote:

> Today's holding does not mean that the timing of the

> regulation's enactment relative to the acquisition of title is immaterial to the *Penn Central* analysis. Indeed it would be just as much error to expunge this consideration from the takings inquiry as it would be to accord it exclusive significance.

Palazzollo, 533 U.S. at 633. The Panel decision does the very evil that Justice O'Connor cautions against: it effectively expunges the investment-backed expectations factor. In his dissent, Justice Kleinfeld discusses the flaws in the Panel's *Palazzolo* interpretation explaining that:

> [T]he [*Palazzolo*] Court held that the plaintiff could pursue a claim for compensation, 5 to 4. Five justices wrote for the Court that a regulatory takings claim 'is not barred by the mere fact that title was acquired after the effective date of the state-imposed restriction.' Justice O'Connor's concurrence states that the claim was not barred in the circumstances presented in that case. Her stated rule rejects treating a change of ownership before or after the enactment of the regulation as *per se* barring or not barring a takings claim. Instead, courts 'must attend to those circumstances which are probative of what fairness requires in a given case.' The four dissenters and Justice O'Connor agreed that acquiring title after the taking could bar a takings claim.

SO, p. 13877-78.

Applying Justice O'Connor's advisement to consider what is fair when analyzing the *Penn Central* factors, Justice Kleinfeld noted that because the Park Owners "benefited from a lower purchase price reflecting the burden of the rent control ordinance when they bought the trailer park, fairness does not require that they be compensated." SO, p. 13879. That is because "the Guggenheims 'got exactly what they bargained' for when they purchased the Park—a mobile home park subject to a detailed rent control ordinance. The City took nothing from what they bought." SO, p. 13855.

D. In Considering *Penn Central's* Character Of Governmental Action Factor, The Panel Decision Departs From Precedent In

Finding The Ordinance Akin To A Physical Invasion Of The Property That Singles Out Mobile Home Park Owners And Forces Them To Rent Space At Below Market Value.

Just as the Panel's conclusions regarding *Penn Central's* investment-backed expectations and economic impact factors depart from precedent, so do the Panel's conclusions regarding *Penn Central's* "character of the governmental action" factor.

In analyzing this factor, the Panel criticized the City's policy decision to enact rent control—contrary to *Lingle's* teaching—and reached two unprecedented conclusions: (1) that the rent control ordinance "looks much more like a classic taking than a mere regulatory burden;" and (2) that rent control unfairly singles out mobile home park owners by forcing them to rent space at below market rates.

With respect to the first conclusion, the Panel compares rent control to a physical taking: according to the Panel, the Ordinance gives tenants "the right to convey the home with the right to remain on the site at a much-reduced rent." SO, p. 13863. According to the Panel, this makes the Ordinance a regulatory taking. SO, p. 13862-63. Under this reasoning, if a governmental action can be characterized as almost a physical taking, it is *ipso facto* a regulatory taking. This is a dangerous new rule.

The Panel's conclusion is an end run around the holding of *Yee v. City of Escondido* that rent control is not a physical taking. It essentially compresses the regulatory takings analysis into a single question: "is the character of the action

almost a physical invasion? If yes, then it is a regulatory taking." Such a simplistic formulation of the regulatory takings analysis is contrary to precedent holding that there are separate analyses for *Loretto* per se takings and regulatory takings, blurring the distinctions between those analyses.

With respect to the second conclusion, the Panel writes that the Ordinance is a taking because it has "[s]ingle[ed] out mobile home park owners . . . and forc[ed] them to rent their property at a discount of 80 percent below its market value." SO, p. 13866. There are at least two flaws in this argument.

First, it ignores the fact that mobile home parks are different from typical rental housing in that the park owner owns the pad and the tenant owns the mobile home, but rents the space below it from the park owner. Because mobile homes are in fact not readily-movable, the mobile home owners/tenants are a captive audience, making mobile home parks a monopolistic market. Mobile home park owners are not being singled out unfairly, they are being regulated as a group that is distinct from other rental housing.

Second, it ignores the fact that in *Yee*, the Supreme Court rejected the "forced to rent" argument. *Yee*, 503 U.S. at 527-28. Here, Park Owners are not forced to rent at below market rents. Rather, they knowingly purchased a park subject to the challenged regulation (at a lower price due to the regulation), and then chose to continue operating that property as a mobile home park (at a rate of

10% return on investment per year). It is difficult to see how "justice" and "fairness" (*Penn Central*, 438 U.S. at 49) require payment of compensation to Park Owners.

E. The Panel Decision Improperly Remanded The Case Back For Damages Determination.

Although the City contends that rehearing is necessary to reverse the Panel's decision that created new, unprecedented law regarding regulatory takings challenges, as an alternative argument, the City contends that the remand order is improper. The procedural posture of this appeal is unusual: Park Owners' appealed from the district court's *sua sponte* pre-trial Order to Show Cause why judgment should not be entered in the City's favor. If the Court declines to reverse the Panel decision on the merits, at a minimum the remand order should be modified so that the City, as a defendant in this lawsuit, is allowed an opportunity to defend its Ordinance on the merits, at the trial court level.

VI. CONCLUSION

To preserve uniformity of decision on these questions of exceptional importance, the City respectfully requests rehearing, particularly rehearing en banc.

Dated: October 9, 2009

Respectfully Submitted,

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CERTIFICATE OF COMPLIANCE

Counsel of Record hereby certifies that pursuant to Circuit Rule Rule 40-1(a), the Memorandum of Points and Authorities is produced using at least 14-point Times New Roman type including footnotes and contains approximately 4,910 words, which is less than the total words permitted by the Rules of Court. Counsel relies on the word count of the computer program used to prepare this brief.

Dated: October 9, 2009

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