No. 10-1125

In the Supreme Court of the United States

DANIEL GUGGENHEIM, SUSAN GUGGENHEIM, AND MAUREEN H. PIERCE,

v.

CITY OF GOLETA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE NATIONAL FEDERATION OF INDEPENDENT BUSINESS SMALL BUSINESS LEGAL CENTER AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

In *Palazzolo v. Rhode Island*, 533 U.S. 606 (2001), this Court rejected the proposition that "postenactment purchasers cannot challenge a regulation under the Takings Clause." *Id.* at 626. In this case, a divided *en banc* panel of the Ninth Circuit distinguished *Palazzolo* on the basis that the plaintiff there had acquired the property by operation of law (instead of purchasing it) and held that the fact that petitioners had purchased the property subject to the challenged regulation was "fatal to [petitioners'] claim."

Is the purchaser of property subject to a regulatory restriction foreclosed from challenging the restriction as a violation of the takings clause?

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Other Authorities

INTRODUCTION AND INTERESTS OF *AMICUS CURIAE*[1]

In 2008, there were 5,911,663 small businesses in the United States.[2] Office of Advocacy, U.S. Small Business Administration, Small Business Profile, 1 (Feb.2011) *available at* http://www.sba.gov.sites/ default/files/files/us10.pdf. These businesses employed 59,693,991 people, amounting to 49.6 percent of private-sector jobs. *Id.* These small business owners hold substantial amounts of real estate. National Federation for Independent Business, Small Business Credit in a Deep Recession, 18 (2010). Ninety-five percent of small employers own their primary residence, their business premises or their investment real estate; fifty-five percent own two and eighteen percent own all three. *Id.* at 19-21. Forty-nine percent of small employers whose businesses reside on commercial real estate, own all or part of the building and/or the land on which their business is located. *Id.* at 19.

Despite the significant contributions that small businesses make to the U.S. economy, state and local governments "frequently fail to consider costs imposed on small businesses as a result of new or expanded regulations." James L. Huffman & Elizabeth

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[1] The parties have consented to the filing of this brief. In accordance with Rule 37.6, *amicus* states that no counsel for any party has authored this brief in whole or in part, and no person or entity, other than *amicus* and its counsel has made a monetary contribution to the preparation or submission of this brief.

[2] Small businesses are defined by the Small Business Administration as businesses with fewer than five hundred employees.

Howard, *The Impact of Land Use Regulations on Small and Emerging Businesses*, 5 J. Small & Emerging Bus. L. 49, 50 (2001). Land-use regulations significantly impact small businesses by "influenc[ing] property acquisition costs, construction expenses, operating costs, employee salaries, and legal fees required to start and operate a small business." *Id.* at 50-51.

Small businesses are less able to mount timely legal challenges to burdens on their property than larger companies with greater resources. "Regulations that impose burdensome costs on small business and which function as barriers to entry can work to the competitive advantage of large businesses." *Id.* at 69. Because the costs of land-use regulations are relatively fixed, economies of scale allow larger businesses to better deal with the costs of the regulations. *Id.* at 68.

The National Federation of Independent Business Small Business Legal Center is a nonprofit, public interest law firm established to provide legal resources and be the voice for small businesses in the nation's courts through representation on issues of public interest affecting small businesses. The National Federation of Independent Business (NFIB) is the nation's leading small business association, representing members in Washington, D.C., and all 50 state capitals. Founded in 1943 as a nonprofit, nonpartisan organization, NFIB's mission is to promote and protect the right of its members to own, operate and grow their businesses.

NFIB represents over 300,000 member businesses nationwide, and its membership spans the spectrum of business operations, ranging from sole proprietor enterprises to firms with hundreds of employees. While there is no standard definition of a "small business," the typical NFIB member employs 10 people and reports gross sales of about $500,000 a year. The NFIB membership is a reflection of American small business.

NFIB regularly monitors for significant cases that are likely to affect the rights of small businesses. This is one such case. If allowed to stand, the decision below would eliminate any incentive for small businesses to buy land encumbered by suspect ordinances or other burdens that the buyer perceives as vulnerable to challenge in court. This is a change in the law that not only threatens the liquidity of the commercial real estate market, but also threatens to stifle the efficient formation of new businesses by reducing the supply of available commercial properties. This change will also depress market values of existing properties subject to suspect regulatory burdens, jeopardizing the financing of many small businesses who borrow against the value of their real property.

NFIB and its membership oppose such a change, and urge this Court to grant certiorari and reverse the decision below.

STATEMENT

In *Palazzolo v. Rhode Island*, 533 U.S. 606 (2001), this Court rejected the proposition that "postenactment purchasers cannot challenge a regulation under the Takings Clause." *Id.* at 626. In this case, a di-

vided *en banc* panel of the Ninth Circuit found petitioners to be barred because the ordinance was "promulgated long before [petitioners] bought their land." Appendix to Petition in No. 10-1125 ("Pet. App.") at 14a. Because the Ninth Circuit's holding "directly contravenes Supreme Court precedent" *Id.* at 35a (Bea. J. dissenting), this Court should grant certiorari.

In 1979, Santa Barbara County, California adopted a rent control ordinance for mobile homes. *Id.* at 4a n.1. The ordinance limits the ability of park owners to increase rent of existing tenants; owners may only do so once a year, or at the termination of a lease term. *Id.* at 6a n.5. In addition, the amount of the increase is determined through arbitration. *Id.* Park owners may automatically raise rent by 75 percent of the local consumer price index, and may seek additional increases for various reasons provided in the ordinance. *Id.* When a tenant sells his or her mobile home to a new tenant, the park owner may only increase the rent by 10 percent. *Id.*

In 1997, eighteen years after the enactment of the ordinance, petitioners Daniel and Susan Guggenheim and Maureen H. Pierce purchased a mobile home park. *Id.* at 6a. The Guggenheims believed that they could free their land from the ordinance either through the grant of a zoning variance, political action targeted toward repealing the regulation in its entirety, or court action to invalidate the law. *Id.* at 41a.

Five years later, the City of Goleta (hereinafter "Goleta") incorporated the land on which the mobile

home park is located. *Id.* at 6a. Goleta subsequently adopted the Santa Barbara County code. *Id.* at 7a. That same year, the Guggenheims sued Goleta claiming that the rent control ordinance constituted a taking. *Id.* at 8a. The Guggenheims argued that by locking in rent at below market prices and allowing tenants to sell their homes to buyers who will still enjoy the benefits of the controlled rent, the "ordinance shifts much of the value of ownership of the land from the landlord to the tenant." *Id.* The Guggenheims' expert's report opined that without the ordinance rents for sites in their mobile home part would average $13,000 per year, but less than $3,300 with the ordinance. *Id.* at 8a-9a.

After a protracted procedural course, the District Court for the Central District of California granted Goleta's motion for summary judgment. *Id.* at 142a. The Ninth Circuit reversed, but decided to hear the case *en banc*. *Id.* at 9a-10a. A divided *en banc* panel vacated its earlier decision and affirmed the judgment of the district court. *Id.* at 10a. *The en banc* majority stated that *Palazzolo* was of "no help to the Guggenheims." *Id.* at 14a. The court distinguished the plaintiff in *Palazzolo* by noting that he acquired title by operation of law and "not because he bought the property for a low price reflecting the economic effect of the regulation." *Id* at 15a. In contrast, the Guggenheims owned the mobile home park "at all relevant times." *Id* at 16a. Analyzing the Guggenheim's claim under this Court's decision in *Penn Central Transportation Co.* v. *New York City*, 438 U.S. 104 (1978) the majority held that "the extent to which the regulation has interfered with distinct investment-backed expectations is fatal to the Guggen-

heims' claim." *Id.* at 18a (internal quotations omitted). In other words, because they purchased the park after the enactment of the ordinance, the Guggenheims "had no concrete reason to believe that they would get something much more valuable, because of hoped-for legal changes." *Id* at 20a.

Furthermore, the majority distinguished *Palazzolo* on the ground that the takings claim there was "as applied" and the property passed to the plaintiff before the claim was ripe. *Id.* at 15a-16a. Therefore, "justice may require that title transfers during the ripening period not bar the action." *Id.* The majority found that the Guggenheim's facial challenge does not warrant an extension of time "because the only time that matters is the time the ordinance was adopted." *Id.* at 16a.

The dissent found that the majority misapplied this Court's analysis of regulatory takings claims by "impermissibly" picking out one of three *Penn Central* factors and converting a three-factor balancing test into a "one-strike-you're-out checklist." *Id.* at 26a (internal quotations omitted). Citing Justice O'Connor's concurrence in *Palazzolo* in which she stated that no one factor is "talismanic," *Palazzolo*, 533 U.S. at 634, the dissent stated that the extent of interference with investment-backed expectations is "*one* factor that points toward the answer to the question whether the application of a particular regulation to particular property 'goes too far.'" Pet. App. at 28a-29a. The dissent then analyzed the petitioners' claims under all three *Penn Central* factors finding that the ordinance effected a taking. *Id.* at 29a. Addressing the investment-back expectations of mobile home park

owners the dissent stated that the majority's opinion fails to provide support as to why a facial challenge should be analyzed differently than an as-applied challenge. *Id.* at 37a. In addition, the dissent chided the majority for adopting

> a static and somewhat simplistic view of law, politics and economics by failing to recognize that the Guggenheims had a reasonable expectation of freeing their land from the Ordinance through political or legal means, and by failing to acknowledge that this belief could influence the price they were willing to pay for the land.

Id. at 42a-43a.

REASONS FOR GRANTING THE PETITION

This Court should grant the petition and review the decision below because the rule announced in that decision would take away from small businesses a vital and oft-used tool that encourages the alienability of real property. The absence of that tool will depress the prices of land subject to suspect zoning ordinances, reduce the supply of viable commercial properties, and jeopardize the financing of small businesses that borrow against the value of their land.

I. Prior to the Decision Below, Small Businesses Regularly Challenged Pre-Existing Burdens On Their Land

Small businesses frequently buy land previously used for other purposes. It is not uncommon for such

a buyer to encounter a pre-existing burden on the land that did not sufficiently affect the prior owner to induce him to challenge the burden at the time it was initially enacted. Prior to the decision below, the mere fact that an ordinance pre-dated the sale of that land was not an obstacle to the subsequent purchaser challenging that ordinance in court.

Numerous cases illustrate this process. For example, in *City of Sherman* v. *Wayne*, 266 S.W.3d 34, 39-40 (Tex. App. 2008), James Wayne purchased a 9.3 acre parcel in Sherman, Texas from the Texas National Guard, which he planned to use for a truck driving school. A 1964 city zoning ordinance prohibited all commercial and industrial uses on the property, but the Guard had operated an armory and truck depot there for 35 years without that ordinance being enforced. *Id.* at 39. Mr. Wayne interpreted the city's inaction against the Guard to mean that the property was "grandfathered-in" and not subject to the zoning ordinance. *Id.* at 39-40. Only after he bought the land did Mr. Wayne learn that the City planned to enforce the zoning ordinance against his truck driving school. *Id.* at 40. After the city denied Mr. Wayne a zoning modification and special use permit, he sued. *Id.*

At trial, the jury found that the ordinance rendered the market value of the property zero. *Id.* Without the ordinance, the jury found the property to be worth $250,000. *Id.* The trial court entered a judgment in favor of Wayne holding that the ordinance amounted to a regulatory taking and awarded him $250,000 in damages. *Id.*

On appeal, the city argued that Mr. Wayne's claim lacked merit because Mr. Wayne "owns exactly what he bought—an old armory building on 9.3 acres of land zoned for residential use." *Id.* at 47. But the Texas Court of Appeals refused to consider that fact dispositive: "the simple fact that Wayne purchased the property years after the zoning ordinance was enacted does not bar his taking claim." *Id.* at 47 (citing *Palazzolo*, 533 U.S. at 626-29). To the contrary, the court found that Mr. Wayne purchased the property on the "firm belief" that the city would not enforce the zoning ordinance and that the "property could not be sold without incurring a loss." *Id.* at 46. Mr. Wayne's judgment was affirmed. *Id.* at 51.

Similarly, in *Vernon Park Realty, Inc* v. *City of Mount Vernon*, 121 N.E.2d 517, 518-19 (N.Y. 1954), a small realty company bought a lot adjacent to a railroad station from a railroad, wishing to open a new shopping center. The property had been zoned as residential 24 years earlier, but the city had allowed a parking garage and gas station to operate there. *Id.* When the realty company was denied a variance, the realty company sued. *Id.* at 519.

The city justified the ordinance "by reason of the congested traffic and parking conditions." *Id.* The New York Court of Appeals rejected this rationale stating that a solution to the traffic problem did "not lie in placing an undue and uncompensated burden on the individual owner of a single parcel of land in the guise of regulation, even for a public purpose." *Id.* The court found that the ordinance "operate[d] to destroy the greater part of the value of the property"

by precluding "the use for which [the property] is most readily adapted." *Id.* at 520.

The New York Court of Appeals also rejected the city's argument that the realty company's purchase of the land with notice of the ordinance precluded suit. *Id.* The court held that the "purchase of property with knowledge of the restriction does not bar the purchaser from testing the validity of the zoning ordinance since the zoning ordinance in the very nature of things has reference to land rather than to owner." *Id.* The court specifically ruled that "[k]nowledge of the owner cannot validate an otherwise invalid ordinance." *Id.*

In *Shatz* v. *Phillips*, 471 S.W.2d 944, 945 (Tenn. 1971) Sylvain and Elaine Shatz ran a scrap metal business in Union City, Tennessee. A building they used to assemble, process, and pack for sale different kinds of non-ferrous scrap, such as aluminum, copper, and brass, was zoned to permit industrial uses *except* "[t]he storage and/or salvaging of junk and other used material." *Id.* at 945-46. The Shatzes first used the building after the zoning ordinance was enacted, and continued until they were eventually cited by a building inspector. *Id.* at 945.

The Shatzes challenged the ordinance as arbitrary and capricious, and won in the trial court and in the intermediate appellate court. *Id.* The Supreme Court of Tennessee also affirmed, finding no rationale for singling out junk salvage in the zoning scheme. *Id.* at 947. The court rejected the city's argument that the Shatzes claim should fail because they knew of the ordinance when they took possession of the prop-

erty: "The [Shatzes] had the right to dispute the validity of Section 11—2003(b) as it applied to their use of the property after they had taken possession of it." *Id.* at 948.

The above rulings are just a sampling of the general rule applied both before and after this Court's ruling in *Palazzolo* that landowners may challenge regulatory burdens enacted prior to their purchase of the land. *See, e.g., La Salle National Bank* v. *City of Evanston*, 179 N.E.2d 673, 676 (Ill. 1962) ("A zoning ordinance cannot be sustained if in violation of the constitution, no matter how long or by whom it has been recognized as legal, and the fact that the purchaser . . . may have acquiesced in the classification will not estop him from testing its validity"); *State ex. rel. Shemo*, 765 N.E.2d 345, 352-353 (Ohio 2002) (citing *Palazollo* in rejecting the argument that a purchaser or successive titleholder is deemed to have notice of an earlier enacted land restriction, and is therefore barred from claiming the restriction effects a taking); *Kropf* v. *City of Sterling Heights*, 215 N.W.2d 179, 184 (Mich. 1974) (an otherwise unconstitutional ordinance does not lose this character and immunize itself from attack simply by the transfer of property from one owner to another); *City of Rome* v. *Pilgrim*, 271 S.E.2d 189, 191 (Ga. 1980) ("the mere fact that a zoning regulation is in effect at the time property is purchased does not preclude the purchaser from attacking its constitutionality").

II. The Decision Below, By Stripping Buyers of the Ability to Challenge Pre-Existing Burdens, Will Disrupt The Commercial Real Estate Market To The Disadvantage of Small Businesses

Prior to the decision below, a buyer of a parcel of land subject to a pre-existing burden could take a calculated risk and negotiate a discounted purchase price that handicapped the reality of the existing burden against the probability of getting the burden lifted in court. *See* Carol N. Brown, *Taking the Takings Claim: A Policy and Economic Analysis of the Survival of Takings Claims After Property Transfers*, 36 Conn. L. Rev. 7, 61-62 (2003) ("If [parties to a land deal] were secure that the takings claim was alienable, they might negotiate a purchase price that reflects the discounted value of the property in its regulated state plus the value of the takings claim. . . . Even if unsuccessful, the successive interest holder, understanding that the right to pursue the takings claim is no guarantee of success, would have negotiated a purchase price . . . at which the successive interest holder would be satisfied to possess the property in its regulated state"). In the language of *Penn Central*, the "investment-backed expectations" of the buyer's likelihood of successfully challenging the ordinance is baked into the purchase price. *See also Palazzolo*, 533 U.S. at 637 (Scalia, J., concurring) ("The 'investment-backed expectations' that the law will take into account do not include the assumed validity of a restriction that in fact deprives property of so much of its value as to be unconstitutional").

But with a rule against alienability of takings claims in place—such as the one endorsed by the court below—a buyer in need of unregulated land will have no choice but to look elsewhere. This is a losing proposition for all involved.

The seller of the burdened land will either have to challenge the regulation himself—an investment he may not be able to make—or sell into the limited pool of remaining buyers who are not affected by the ordinance. Selling into lesser demand of course results in an inferior price, as the cases in this area demonstrate. *See e.g. Chusud Realty Corp.* v. *Village of Kensington*, 22 A.D.2d 895, 897 (N.Y. App. Div. 1964) (Plaintiffs property was worth $40,000 to $120,000 if confined to the allowable uses under zoning restrictions but worth $670,000 if used as plaintiff desired.); *Moeller* v. *City of Moline*, 200 N.E.2d 93, 96 (Ill. App. 1964) (Defendant's expert conceded that plaintiff's property would be worth maximum of $7,500 if zoned residential and $12,000 if zoned industrial as plaintiff wished, whereas plaintiff's expert valued property at $6,800 if residential and $17,000 to $20,000 if zoned industrial.)*; Bolger* v. *Village of Mount Prospect*, 141 N.E.2d 22, 25 (Ill. 1957) (Appraiser valued plaintiffs' property at $29,025 for residential purposes under the challenged ordinance and $116,100 for business purposes. Realtor estimated property's worth at 15,000 for residential purposes and $110,000 for commercial development).

A lower market price means more limited financing options for a small business that borrows against its land to finance its operations. A recent NFIB survey revealed that 63 percent of small businesses who

own their business premises borrow against it. *See* National Federation for Independent Business, National Small Business Poll, Vol. 8, Issue 7 (2008). Those business owners whose land is subject to a regulatory burden that cannot be transferred will have a hard time maintaining that financing if the decision below stands.

The flip side of the same coin is that buyers seeking suitably-zoned plots for their business will have fewer options to choose from. This reduced supply will increase prices for unburdened land, thus also increasing barriers to entry for entrepreneurs seeking to start or expand their small businesses. *See, e.g.,* Dep't of City Planning and the Cmty. Redevelopment Agency of the City of Los Angeles, Los Angeles' Industrial Land: Sustaining a Dynamic City Economy 4, 11 (Dec. 2007), *available at* http://cityplanning.lacity.org/Code_Studies/LanduseProj/Industrial_Files/Attachment%20B.pdf. ("Competition for industrially zoned land in Los Angeles is extremely high; industrial land in the City has the lowest vacancy rate in the nation, remaining consistently below two percent. Yet the supply of these critical job-producing areas is becoming increasingly scarce... With the regional Los Angeles economy thriving, industrial space will remain at a premium...."); District of Columbia Office of Planning, Industrial Land in a Post-Industrial City, District of Columbia Industrial Land Use Study: A Detailed Investigation of Industrial Land in the District of Columbia and role of Production, Distribution and Repair Industries in the District Economy 4, 70 (Aug. 2006) *available at* http://communityinnovation.berkeley.edu/presentation/industrial/DC-industrial-land-in-a-post-industrial-

city.pdf. ("Developable land of any type is scarce in Washington, DC and industrial land even more so...Unlike the suburban markets, where industrial space...generally remains after the larger leases are signed, small space leases are at a premium in the District").

In sum, a rule barring the alienability of takings claims hurts both the holders and buyers of land burdened by suspect ordinances. As petitioners here explain, this not the law, but if it were the law, it would have dire consequences for many small businesses, and for the 49.6 percent of private sector workers they employ.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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