

Fordham Environmental Law Review

Volume 6, Number 3

2011

Article 6

Lead Us Not Into Penn Station: Takings, Historic Preservation, and Rent Control

William A. Fischel*

*

Copyright ©2011 by the authors. *Fordham Environmental Law Review* is produced by The Berkeley Electronic Press (bepress). <http://ir.lawnet.fordham.edu/elr>

LEAD US NOT INTO PENN STATION: TAKINGS, HISTORIC PRESERVATION, AND RENT CONTROL

WILLIAM A. FISCHEL*

I am going to discuss the double issue of rent control and historic preservation, or landmarks preservation. In titling my remarks, I had in mind the humorous way that children saying the Lord's Prayer confuse "lead us not into temptation" with "lead us not into Penn Station." I decided to take this double meaning to refer to the origin of New York City's Landmarks Preservation Law,¹ which was occasioned by the 1964 demolition of the original Pennsylvania Station in New York City. New York's ordinance subsequently swept the country as a model for landmarks preservation.

I am also going to make the reference to the "temptation" of using regulation to achieve goals that should be better accomplished by deliberate eminent domain proceedings, or at least with some form of indirect compensation. I believe, by the way, that the owners of Grand Central Terminal, the subject of the Supreme Court decision, *Penn Central Transportation Co. v. New York City*,² in fact, received just compensation. It was not technically "just compensation," because payment was not made in money, but Penn Central was offered transferrable development rights, which turned out to be quite valuable, and so this decision does not offend my sense of justice.

I also want to give a pitch for my book, *Regulatory Takings: Law, Economics and Politics*, which Harvard University Press will publish in July of this year. I want to talk about the two major themes of that book, and then apply them to rent control and landmarks preservation.

The two major themes of the book are fairness and the capacity for judicial review. I believe, having surveyed a large amount of takings territory, including eminent domain cases, constitutional conventions, and modern economic theory, that just compensation boils down to a question of fair treatment by the government. Although that is an unexciting proposition, it has important implications. Many economic analyses of the takings issue conclude that it is about economic efficiency. But I don't think takings are about economic efficiency. Rather, I think they are about fairness. Paying additional attention to takings—taking them a little more seriously—would probably make

* Professor of Economics, Dartmouth College; Ph.D. 1973, Princeton University; A.B. 1967, Amherst College. The author emphasizes that these remarks are only lightly edited to preserve the flavor of oral commentary.

1. NEW YORK, N.Y., ADMIN. CODE §§ 25-301 to -321 (1992).

2. 438 U.S. 104 (1978).

for a somewhat more efficient state of the world, but that's not the reason that the judges should invoke the Takings Clause.

This, of course, borrows from Professor Frank Michelman's 1967 Harvard Law Review classic survey of the territory, *Property, Utility and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law*.³ I commend it to you as a classy, intelligent Article, and I build on it. I should say that Professor Michelman does not necessarily agree with what I have to say. Indeed, it seems to me that Michelman wrote this classic Article more than twenty-five years ago, and, ever since then, has been defending himself against his admirers. I think it is a great Article and I want to take it somewhere, and Frank keeps backpedaling a little bit here and there, I think.

The other theme that I examine in my book is the limitations of judicial review under the Constitution. This is a problematic enterprise. The judges are both limited in their capacity and their legitimacy to review matters of property rights. The Constitution, while containing references to property, does not define property, and it is clearly a document for self-government by people. So, what those of us who think takings is an important issue really want to ask ourselves is this: where should judges deploy their scarce political capital, given that they can not do everything they want to do?

My view is that property is usually protected from excess regulation by two possibilities—"exit" and "voice." They come from Albert Hirschman's classic book, *Exit, Voice, and Loyalty*.⁴ Judges do not have to be concerned about property when it can exit from the jurisdiction. I mean "exit" in a very broad sense of elastic supply, if you like your economics definitions, or as the ability to withhold resources or to remove them from the threat of regulation. Exit is taken very seriously by government officials, and in my book I give many examples of it.

My casual example is the City of Berkeley, where I lived several years ago. Berkeley has very stringent regulations on apartments and on the development of property, all in the interest of promoting the well-being of the poor. That is to say that Berkeley is interested in keeping rents down to help the poor. However, Berkeley does not regulate the price of food. There is a simple reason why Berkeley does not regulate the price of food—there would be no food supply if regulations kept the price too low.

In fact, since the food industry is a highly competitive one, any price regulation on food would probably cut off supplies within the City of Berkeley very quickly, and that disciplines the otherwise pro-regula-

3. Frank I. Michelman, *Property, Utility and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law*, 80 HARV. L. REV. 1165 (1967).

4. ALBERT O. HIRSCHMAN, *EXIT, VOICE, AND LOYALTY* (1970).

tory City Council. I do not think that the California Supreme Court needs to protect Berkeley's food store owners.

The second protection from excessive regulation is that of "voice," by which Hirschman meant a general ability to participate in and influence the political process. Interest groups, bicameralism, and other features of the federal government are excellent ways of providing voice. If you read *The Federalist* Number Ten⁵ a little more carefully than many of my colleagues do, you will see that James Madison was really a structuralist. Madison favored large republics because they offer the opportunity for people to protect themselves by participating in the polity. They do this to guard against the arbitrary results of majoritarian sentiments.

So, if exit and voice work so well, why should judges do anything for property? The answer is that there are two areas where exit and voice do not work very well. Exit does not work where the asset being regulated is immovable or otherwise inelastic in supply, as economists like to say. The paradigm of that, of course, is land. That is why the government could tax land up to 100 percent of its value, as Henry George urged.⁶ Economists actually favor this kind of tax because it is efficient. But because land cannot exit, being immovable, it is also vulnerable to excessive regulation.

The other aspect that makes land somewhat more vulnerable than other types of property is that voice is ineffective in some government structures because the individuals who are adversely affected by the regulation live outside the jurisdiction. Here, of course, I am referring to local government land-use regulation. So, the paradigm case for where judges should spend some of their scarce constitutional capital is suburban growth controls. These will not be discussed here. Robert Ellickson reviewed suburban growth controls some time ago in the *Yale Law Journal*,⁷ if you care to look at what I believe to be the correct standard.

Instead, I will examine rent control and landmarks preservation to determine how they fit my model of where judges should intervene. Moreover, I will discuss the kinds of structures that are protective of landowners, and where the protections might fail.

To a large extent, rent control and landmarks preservation confirm my voice model at the state and national level. There is scarcely any statewide rent control. It is almost exclusively local. There has been only one instance of national rent control in peacetime, Richard

5. THE FEDERALIST No. 10 (James Madison).

6. HENRY GEORGE, *PROGRESS AND POVERTY* (Robert Schalkenbach Foundation 1955). George argued that "the whole value of land may be taken in taxation, and the only effect will be to stimulate industry . . . and to increase the production of wealth." *Id.* at 414.

7. Robert C. Ellickson, *Suburban Growth Controls: An Economic and Legal Analysis*, 86 *YALE L.J.* 385 (1977).

Nixon's 1971 general wage and price controls.⁸ These controls quickly became extremely unpopular, and after a while the entire regulatory scheme was eliminated by the political process. So, landowners have protection at the state and national level in this area.

Landmarks preservation is undertaken by the federal government, but typically in a way that is procedurally more protective of property owners. Furthermore, the federal government offers indirect compensation for preservation in the form of tax breaks and subsidies for maintenance, which mitigate its burdens, even if they do not alleviate them entirely.

Rent control is undertaken almost entirely at the local level. The issue that I would like to address regarding rent control is not why we have rent control at all, but rather why we do not have more rent control. Rent control seems like a good way for a majoritarian government to give benefits to a large group of tenants at the expense of an unloved, probably unrepresented group of landlords at the local level.

However, landlords have one important political protection at the local level. In a world in which there are property taxes, homeowners begin to realize that rent control diminishes the value of apartment buildings, which will cause more of the property tax burden to fall on owner-occupied homes. Therefore, the reason why rent control is relatively rare in the United States is partly that homeowners are usually a majority and are concerned about their share of the property taxes, and because homeowners do not like to see deteriorated buildings and other consequences that sometimes result from stringent rent controls.

As a result of these political and economic considerations, we see rent control in its severe form only where renters are a large majority of the population (i.e., New York City and Washington, D.C.), and in states, like California, where homeowners' property taxes are kept at a very low level.⁹ In most other cities, rent control is relatively moderate, and partly for that reason economists have a rather difficult time gathering statistically reliable evidence that rent control has all of the dire effects that they claim it does. For example, economists predict that if rental prices are held below equilibrium, an extreme shortage of apartments will result. Nobody will want to be a landlord, and therefore tenants will be worse off. But, these lessons have actually

8. Exec. Order No. 11,615, 3 C.F.R. 602 (1971), *revoked*, Exec. Order No. 11,695, 3A C.F.R. 150 (1973).

9. California has unusually low property taxes because of Proposition 13, a voter initiative that was passed in 1978. Proposition 13 imposed a statewide maximum tax rate of one percent and substantially retarded the amount that assessed values could increase as a result of inflation. Property tax revenues fell to less than half of what they had been previously. See generally ARTHUR O'SULLIVAN ET AL., *PROPERTY TAXES AND TAX REVOLTS: THE LEGACY OF PROPOSITION 13* (1995). Proposition 13 was said to have triggered rent control because tenants did not receive as large a windfall from property tax reductions as they had been promised.

been learned in an intuitive sense by the controllers of rent. As a result, the dire predictions of economists do not come true. Politicians intuitively believe the predictions and do not permit rent control to become too severe in most jurisdictions.

Thus, in most jurisdictions, rent control generally gets exit and voice protection. However, there are several relatively rare instances where exit and voice do not work, and judges have to spend some of their political capital.

Now, let me turn to landmarks preservation. Unlike rent control, landmarks preservation can have compensation in the form of reciprocity. This reciprocity is most obvious when entire neighborhoods are designated landmarks or are subject to historic preservation regulations. In such instances, the political voice of the neighborhood is important. There is an imposition of a regulatory cost, but there is also the conferral of a benefit. Since the benefit and the cost are roughly the same, neighborhood landmarks preservation and historic preservation are surely not areas that judges should spend a lot of time on.

But, what about the isolated landmark? Here we have a problem with reciprocity. A landmark is a building that provides something that almost all of us would characterize as a public benefit. Having an ordinary building is not regarded as a harmful thing. But consider the building owner who hired a famous architect, or built a nice building, and thus benefitted the public. Individual landmark designation imposes a special burden on this owner.

I think this imposition is unfair, and I think that most of the progenitors of New York City's Landmarks Preservation Law thought it was unfair, too. That is why they offered transferrable development rights. It is also why the Costonis Plan for Chicago,¹⁰ now all but forgotten, was a very good idea. In fairness, building owners have created a public benefit, and the public should give them something in exchange for maintaining their good behavior into the future.

There are, however, some landmarks preservation laws that have gone too far, an example of which is the Philadelphia Historic Buildings, Structures, Sites, Objects, and Districts Ordinance.¹¹ I say this guardedly because I do not know the law very well. I only know it from the Boyd Theater case.¹² The Pennsylvania Supreme Court first got it right. In effect, the court interpreted the Philadelphia landmarks law as a benefit extraction, which requires compensation under traditional eminent domain laws. But then the Court got it wrong and reversed itself after rehearing the case.

10. John J. Costonis, *The Chicago Plan: Incentive Zoning and the Preservation of Urban Landmarks*, 85 HARV. L. REV. 574 (1972).

11. PHILADELPHIA, PA., PHILADELPHIA CODE, § 14-2007(1)-(8) (1989).

12. *United Artists' Theater Circuit, Inc. v. City of Philadelphia*, 595 A.2d 6 (Pa. 1991), *rev'd*, 635 A.2d 612 (Pa. 1993).

The Pennsylvania Supreme Court got it wrong because there apparently was no transferrable development right. Therefore, there was no reciprocity. Essentially, the owners of the Boyd Theater were told, "You've got a nice-looking theater. We've enjoyed it for years and we want to keep on enjoying it for years, and it's your dime, not ours." This is a case where the exit and voice option has been attenuated enough that judges should spend some of their scarce political capital to help the property owner.

There is one other thing that might discipline landmarks preservation laws in the long run. It is the possibility that because sometime in the future a building might be designated a landmark or otherwise subjected to uncompensated regulation, landlords will begin hiring mediocre architects or asking good architects to design mediocre buildings that will not be landmarked.

Now, this idea struck me as a little bit far-fetched. I do not know much about architects and architecture, but a few years ago, I came across a column by *The New York Times* architectural critic, Paul Goldberger. Goldberger is a proponent of historic preservation, but he concluded his column with a caveat, indicating a concern about what landmarking says about the future. He wrote that "[a] city evolves over time and the city that contains not enough new buildings is as robbed of the reality of time as the one that contains not enough old ones."¹³ Therefore, Goldberger is concerned a little bit about the future.

In summary, I think judicial application of the regulatory takings doctrine should help the property owner. By assuring that a well-designed building will not become a burden to its owner in the future, compensation would promote the design of attractive structures in the present. I realize that transferrable development rights are not formal compensation. I know that eminent domain law requires monetary compensation. Nonetheless, our sense of fairness is satisfied when we give owners something in return. Since fairness is what this regulatory takings issue is all about, transferrable development rights are a satisfactory solution, as long as the development rights are not trivial ones. The temptation to be guarded against is the Philadelphia scheme, which offers no reciprocity.

13. Paul Goldberger, *A Commission That Has Itself Become a Landmark*, N.Y. TIMES, Apr. 15, 1990, § 2, at 36.