Commercial Rent Regulation: Preserving the Diversity of Neighborhood Commercial Districts*

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INTRODUCTION

The displacement of small, community-serving businesses in neighborhoods undergoing gentrification is not a new phenomenon. Most vulnerable to displacement are commercial tenants who operate independent rather than chain or franchise establishments and who offer low-priced or low-volume goods and services to the immediate neighborhood rather than to a regional clientele. These businesses face the threat of eviction because they are unlikely to be able to afford the major rent

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1. "Gentrification" is a relatively new term to explain an old phenomenon. It describes a process whereby a lower income population is displaced by a more affluent group that begins to see a neighborhood as desirable. Gentrification has two aspects: forcing out present residents and pricing out future generations of traditional residents.

Revitalization of a neighborhood is not always undesirable—change can create many new opportunities. Yet as a result of the large-scale urban renewal programs of the 1950's and 1960's, there is an increased awareness that such change may dislocate the existing population and erode the traditions and character of the neighborhood itself. This process is of increasing concern in the 1980's as affluent people "reclaim" the central city as their own. Although urban residential neighborhoods and their adjoining commercial areas inevitably will undergo change, a neighborhood's traditional population and way of life should inform future planning efforts.

2. See J. Jacobs, The Death and Life of Great American Cities (1961). It was the loss of diversity in urban neighborhoods that fueled Jane Jacobs' attack on the "steamroller" urban renewal programs of the 1950's and 1960's. For a more recent account of one community's efforts to preserve its neighborhood commercial district, see Keating, The Elmwood Experiment: The Use of Commercial Rent Stabilization to Preserve a Diverse Neighborhood Shopping District, 28 WASH. U.J. URB. & CONTEMP. L. 107, 111-24 (1985).

3. Regional businesses, by definition, attract more traffic to an area than do neighborhood-serving establishments, such as corner "mom-and-pop" stores. Increased traffic, in turn, creates a demand for more parking in the area and may affect adversely the pedestrian orientation of the neighborhood commercial strip. See, e.g., Berkeley Planning Dep't, Memorandum to Planning Commission on Draft Regulations for Telegraph Area Commercial District 2 (Jan. 20, 1988) [hereinafter Memorandum to Planning Commission I].
increases that accompany lease renewals. Because these small businesses often provide essential goods and services to the immediate neighborhood, supply diversity, and contribute to the character of an urban commercial area, their disappearance is cause for serious concern.

Zoning by local government is the common regulatory response to preserve small independent businesses in cities experiencing gentrification. Regulation of the use of property through zoning in business and commercial areas is a well-recognized police power of local governments. Commercial rent regulation, the subject of this Comment, is an alternate urban planning strategy designed to prevent displacement caused by gentrification. Commercial rent control is a scarcely used but innovative means to preserve an area’s unique nature and locally oriented businesses.

Berkeley, California is the first American city in thirty years to have enacted any type of commercial rent control program. Between 1982 and 1987, rent and eviction controls were enacted that applied to three Berkeley neighborhoods—the Elmwood, Telegraph Avenue, and West Berkeley manufacturing and special industrial districts. Of the three commercial rent stabilization ordinances, the Telegraph Avenue ordinance in particular has received much attention from the Berkeley community and its landowners and commercial tenants, from cities such as

5. Id. at 110-11. For a description of use quotas as a nontraditional zoning technique to establish the number of businesses of a particular type that may locate in a neighborhood commercial district, see Comment, Playing the Numbers: Local Government Authority to Apply Use Quotas in Neighborhood Commercial Districts, 14 ECOLOGY L.Q. 325 (1987). See also infra text accompanying notes 220-22. For an historical perspective on use quotas, which normally are used to manage the number of gas stations, liquor stores, and adult uses in an area, see Babcock & Smith, Zoning By The Numbers, PLANNING, June 1985, at 12.
7. The Elmwood Commercial Rent Stabilization and Eviction Protection Ordinance, more commonly known as Measure I, which established commercial rent control in the Elmwood district, was adopted by Berkeley voters in June 1982. Berkeley, Cal., Ordinance 5468-N.S. (1982). The Elmwood ordinance marked the first time that an American city had enacted rent and eviction controls that applied only to a single neighborhood. For an excellent treatment of the process and purpose of Berkeley’s first commercial rent control program in the Elmwood shopping district, see Keating, supra note 2.
8. Initially, the Berkeley City Council enacted an urgency ordinance, Berkeley, Cal., Ordinance 5640-N.S. (Feb. 26, 1985), and extended it several times, id. at 5657-N.S. (May 21, 1985); id. at 5688-N.S. (Oct. 1, 1985). The City Council then adopted a permanent rent and eviction control ordinance for the Telegraph Avenue area, effective March 1, 1986. Id. at 5708-N.S. (Jan. 21, 1986).
9. The West Berkeley ordinance was designed to protect industrial spaces traditionally used by small businesses, artists, and craftspeople. Such spaces were rapidly being converted to large office, retail, and research complexes. The ordinance was intended to be temporary and to remain in effect only until the completion of an area plan that would enunciate a new long-term land use and zoning policy. Id. at 5804-N.S. § 3 (Oct. 21, 1986).
New York and San Francisco, and recently from the federal courts\textsuperscript{10} and the California Legislature.\textsuperscript{11} The Telegraph Avenue ordinance instituted a program of mandatory mediation and arbitration to determine commercial rent levels and provided a set of strong eviction protections to prevent the displacement of local businesses.\textsuperscript{12}

Although Berkeley merchants praised commercial rent regulations for providing the measure of stability needed to ensure the survival of their small businesses,\textsuperscript{13} these regulations upset the conventional landlord-tenant relationship and, thus, were targets for challenge in both the courts and the Legislature. Indeed, in 1987, barely two years after its enactment, Berkeley's Telegraph Avenue rent arbitration and eviction ordinance was tested in federal court\textsuperscript{14} and its eviction section found unconstitutional under a contract clause challenge.\textsuperscript{15}

The California Legislature recorded its opposition to commercial rent control by enacting legislation that preempted Berkeley's three landmark ordinances as of January 1, 1988 and banned any similar commercial rent control statewide.\textsuperscript{16} Yet, the situation that prompted Berkeley to enact commercial rent control regulations remains.

As is often true of untested legislation, the Telegraph Avenue ordinance was flawed.\textsuperscript{17} Unfortunately, however, the Legislature cut short Berkeley's innovative attempt to address a local land use issue. Far from being a post mortem, this Comment reviews Berkeley's experience with commercial rent regulation to focus attention on the problem of and possible solutions to the gentrification-induced disappearance of independent businesses from commercial streets.

\begin{itemize}
\item \textbf{10.} See \textit{Ross v. City of Berkeley}, 655 F. Supp. 820 (N.D. Cal. 1987). In \textit{Ross}, the court held that the ordinance's eviction section abridged the property owners' rights under the contract clause because it prevented Telegraph Avenue property owners from reentering their property at the end of their tenants' lease term. See \textit{U.S. CONST.} art. I, § 10, cl. 1.
\item \textbf{11.} The Costa-Keene-Seymour Commercial Property Investment Act of 1987, 1987 Cal. Stat. ch. 824, § 2 (codified at \textit{CAL. CIV. CODE} §§ 1954.25-.31 (West Supp. 1988)), generally bars all California localities from enacting or enforcing any type of rent or eviction controls, including mandatory arbitration and mediation, on commercial property.
\item \textbf{12.} See infra notes 69-82 and accompanying text.
\item \textbf{14.} \textit{Ross}, 655 F. Supp. 820.
\item \textbf{15.} Id. at 844.
\item \textbf{17.} The \textit{Ross} court found the eviction section of the ordinance unconstitutional against a contract clause challenge because it did not permit owner-occupancy evictions at the end of a lease term. \textit{Ross}, 655 F. Supp. at 844. To comply with the court's decision, the Berkeley City Council amended the Telegraph Avenue ordinance on July 28, 1987 (effective August 28, 1987) to allow for owner-occupancy evictions. Berkeley, Cal., Ordinance 5827-NS § 1 (codified at \textit{BERKELEY, CAL., MUN. CODE} § 13.82.090 (1987)).
\end{itemize}
Section I of the Comment discusses the situation that faced Telegraph Avenue merchants and recounts the debate over the solution chosen—commercial rent regulation. It also outlines the history of commercial use regulation and rent control in Berkeley and briefly explores the provisions and purposes of the Telegraph Avenue ordinance. Section II details the mechanisms of the three Berkeley ordinances. Section III provides a legal analysis of *Ross v. City of Berkeley,* and Section IV outlines the legislation that now preempts commercial rent regulation in California. Based on this discussion, the Comment concludes in Section V by examining the consequences of deregulation in the three formerly controlled areas and suggesting possible alternatives for protecting the diversity and character of commercial districts.

I

GENTRIFICATION AND THE TELEGRAPH AVENUE ORDINANCE

A. *The Gentrification of Telegraph Avenue*

The commercial street is perhaps the greatest source of vitality and character in a city neighborhood.18 Berkeley's Telegraph Avenue, a commercial street connecting the Berkeley community with the University of California campus, embodies the unique historical relationship between the city and the campus. Ironically, the Avenue's prime location and infamy threaten to destroy its character.

During the 1960's, Telegraph Avenue gained national attention as student protests surged off the University's Sproul Plaza into the streets and onto the nation's television screens. Telegraph Avenue became a memorable street, capturing the essence of the counterculture. Nearly twenty-five years after Free Speech, antiwar, and People's Park protests catapulted Telegraph Avenue to national attention, the Avenue is still known for its street vendors, outdoor art, and colorful history. One rapidly changing aspect of Telegraph Avenue, however, is the number of small, independent, and community-serving businesses on the Avenue.19

Telegraph Avenue's notoriety, as well as its proximity to other Berkeley neighborhoods and to the U.C. Berkeley campus, has fostered a perception of the Avenue as a profitable business location. This percep—


tion has led to an influx of chain stores and franchises, such as Mrs. Field's cookies, and a consequent displacement of small businesses, such as Ma's Revolution health food coop.

B. The Debate over the Telegraph Avenue Controls

Telegraph Avenue merchants perceived gentrification as a serious and immediate threat to their commercial existence. City officials also were alarmed at the displacement of local merchants from one of the City's main commercial strips. Amidst serious debate, the Berkeley City Council enacted an innovative program of commercial rent arbitration and eviction protections in the Telegraph Avenue commercial area in February 1985.

Before the ordinance was enacted in 1985, many Telegraph Avenue businesses were subject to precipitous rent increases or summary evictions at the end of their lease terms. Thus, Telegraph Avenue merchants covered by the newly enacted controls were afforded a measure of stability needed to ensure the survival of their small, locally based businesses. Many merchants believed that the ordinance, which mandated rent mediation in certain circumstances, provided their landlords with the necessary incentive to negotiate over rents and lease terms. The eviction protections, however, were seen as the most important part of the ordinance from the merchants' standpoint.

Many Berkeley residents viewed commercial rent control as a way to ensure that community-serving businesses, which contributed to the character of the city and met the daily needs of residents, were not displaced by chain stores. They pointed to the number of chain stores that opened on the Avenue before the regulations were enacted as proof that,

20. In 1985, for instance, Presto Prints, a chain one-hour photograph processing store, took over the space that had been occupied for at least 20 years by the locally owned Berkeley Commercial Photo Store. Id. at 39.


22. See infra text accompanying notes 55-61 & 77-82.

23. Berkeley, Cal., Ordinance 5640-N.S. (Feb. 26, 1985). The goals of the ordinance were identified as reducing the impact of rent increases, evictions, and turnovers, encouraging small responsive Berkeley businesses, and reducing "pressures" on local businesses. Id. at § 3.

24. Telegraph Avenue Survey, supra note 19, at 11-13, 16-19; O'Toole, Berkeley Will Study Campus Area Business, Oakland Tribune, Dec. 19, 1985, at B-1, cols. 1-2. Business leases, which formerly ran for terms of 10 to 20 years, by 1985 often were renewable for only two- or three-year terms. Id.

25. See Faucher, supra note 21, at 1, col. 5; see also infra note 73.

26. See infra note 73.

27. See O'Toole, supra note 24.
without regulation, Telegraph Avenue's character would be lost. Addition-
ally, neighborhood activists valued maintaining community-serving
stores owned by local merchants because such businesses might be more
responsive to community needs. Planners in other cities also were look-
ing to commercial rent and eviction regulations as one answer to the
neighborhood gentrification problem.

On the other hand, the Telegraph Avenue ordinance was opposed
by the real estate industry, some landlords, and others who believed that
the commercial controls would deter investment not only along Tele-
graph Avenue, but throughout the city as a whole. These opponents
viewed commercial controls as potentially devastating to the business cli-
mate in the city. Additionally, they argued that the ordinance helped
only a select group—those merchants already leasing space on the Ave-
nue. Eviction controls not only would keep out chain stores, but also
would make it difficult for new “mom-and-pop” businesses to locate on
Telegraph Avenue. Moreover, because commercial rent controls applied
to all existing businesses, the large chain stores were receiving, in effect, a
subsidy. Finally, opponents claimed that both the immediate neighbor-
hood and the city benefit from the higher rents and from increased real
property and sales taxes. Thus, they concluded that marginal busi-
nesses should not be preserved artificially.

28. Id.
29. In May 1985, Mayor Koch and the New York City Council created the Small Retail
Business Study Commission and charged it with “considering the extent to which rising com-
mercial rents are generating significant hardships for New York City consumers and retail
merchants, and to appraise the policy options for ameliorating such hardships.” New York
City Small Retail Business Study Commission, Final Report I-1 (June 1986).
San Francisco had intended to enact an ordinance requiring landlords to give commercial
tenants advance notice of their intention to terminate a lease. Interview with Susan Lee,
Mayor’s Office of Housing and Economic Development, San Francisco, Cal. (June 29, 1988).
The proposed ordinance, however, was superseded by the state ban on commercial rent regu-
30. In attempting to secure financing for an admittedly risky hotel project in downtown
Berkeley, for example, a mortgage banker found that the only investor to consider the deal
“decided that the shadow of rent control extending further to encompass the site” provided a
disincentive to financing the project. C. Carr, Commercial Rent Control’s Affect [sic] on Ma-
ajor Investment Decisions (Aug. 2, 1985) (presentation to Telegraph Avenue Plan
Subcommittee).
31. “A patchwork quilt of local rules will paralyze new commercial real estate invest-
ment,” said one opponent, California State Senator Barry Keene, author of the state legislation
that preempts commercial rent control. Meibert, supra note 13, at A-5, col. 1.
32. Cooper & Reddy, U.S. Court Rules Out Part of Commercial Rent Control, Daily
Californian, Feb. 27, 1987, at 6, col. 4.
33. Thus, although the primary goal of the ordinance was to encourage and reduce “press-
sures” on small Berkeley-based businesses, all businesses—large and small, chain and in-
dependent—would receive the same rent and eviction protections, whether or not their
presence on the Avenue furthered the ordinance’s goals.
34. O’Toole, supra note 24.
35. See, e.g., Stern, Change Inevitable as Berkeley Rent Control Dies, Oakland Tribune,
Jan. 13, 1987, at B-5, col. 1; see also infra notes 209-15 and accompanying text.
COMMERCIAL RENT REGULATION

Despite compelling arguments against relying on a virtually untested law, Berkeley was not timid in adopting neighborhood commercial rent regulation. It is not surprising, in light of Berkeley's well-known history of residential rent regulation and land use innovation, that the city's voters and elected officials would extend into the commercial sector controls with which they were familiar from its residential programs.

C. Commercial Use Regulations and Rent Control in Berkeley Prior to the Telegraph Avenue Ordinance

Only three cities in the United States have ever enacted commercial rent control ordinances: New York City, from 1945 to 1963,36 Albany, New York, during 1948,37 and Berkeley, on four separate occasions.38 In 1978, when Berkeley voters approved an initiative mandating citywide commercial and residential rent control for one year, Berkeley became the first American city in thirty years to enact commercial rent controls. The initiative required residential and commercial landlords to rebate eighty percent of their Proposition 13 property tax savings to their tenants and to restrict future rent increases to cost pass-throughs in excess of the landlords' twenty percent share of the tax savings.39 In 1980, the commercial provisions of this ordinance lapsed, but a much stricter rent control initiative superseded the residential provisions.40

Since 1973, Berkeley has attempted to preserve its residential neighborhoods and to control the contiguous commercial districts.41 Berkeley

37. 1948 N.Y. Laws ch. 679; see also Keating, supra note 2, at 124.
38. Puerto Rico also enacted commercial rent and eviction controls in 1946. See Rivera v. R. Cobian Chinea & Co., 181 F.2d 974 (1st Cir. 1950).
39. Berkeley, Cal., Mun. Code §§ 7.44.010-.140 (1987). This ordinance can be distinguished from the later commercial rent control ordinances in that its primary purpose was to pass on Proposition 13 tax relief to tenants, rather than to prevent displacement of merchants. Keating, supra note 2, at 137. This measure was ruled constitutional, surviving a contract clause challenge in Rue-Ell Enterprises, Inc. v. City of Berkeley, 147 Cal. App. 3d 81, 194 Cal. Rptr. 919 (1983). In Rue-Ell, the court found that the ordinance did not substantially impair a commercial landlord's preexisting leases because it was in effect for only one year and entitled the tenants to only a partial rebate of property tax windfalls. Id. at 88-89, 194 Cal. Rptr. at 924.
41. See, e.g., Groch v. City of Berkeley, 118 Cal. App. 3d 518, 522-25, 173 Cal. Rptr. 534, 536-39 (1981) (upholding as constitutional a neighborhood preservation initiative ordinance that sought to preserve neighborhood character by requiring, inter alia, extensive citizen notice and review procedures before any housing could be demolished); Historic Preservation
also has strictly limited the amount of land that is commercially zoned and has tightly regulated the use of land in its commercial districts. Since 1978, the Berkeley Planning Commission has rezoned commercial districts as "restricted neighborhood commercial districts" to provide locations for businesses serving the surrounding neighborhoods.42

While supporting rezoning and other measures, residents of Berkeley's Elmwood district concluded that zoning and other traditional land use techniques were insufficient to prevent displacement of that area's existing businesses, which are concentrated in a two-block commercial strip several blocks to the east of Telegraph Avenue.43 The prospective 1981 closing of the city's last surviving soda fountain,44 brought on by a doubling in rent by the building's new owners, inspired the formation of a neighborhood group, the Elmwood Preservation Alliance, which pressed for further protective regulation to preserve the existing small businesses in the district.45

By 1982 the problems of gentrification had become so serious in the Elmwood district that Berkeley's second program of neighborhood commercial rent control appeared on the June ballot and was approved overwhelmingly by Berkeley voters.46 As enacted, the ordinance was


42. In November 1982, Berkeley voters enacted the neighborhood-sponsored "Neighborhood Commercial Preservation Ordinance" (Measure V). Berkeley, Cal., Ordinance 5506-N.S. (Nov. 2, 1982) (codified at BERKELEY, CAL., MUN. CODE §§ 22.12.010-.120 (1987)). The initiative was designed to encourage regional businesses to locate in Berkeley's central business district and to allow for greater neighborhood participation in the city's review of use permits in neighborhood commercial districts. Keating, supra note 2, at 119. In May 1984, the Berkeley City Council adopted an innovative rezoning scheme for the Elmwood Commercial District that was meant to carry into effect Measure V. Berkeley, Cal., Ordinance 5603-N.S. (May 1984). See Comment, supra note 5, at 330-32 (discussion of Berkeley's use quota ordinance). The ordinance's key innovation was the adoption of numerical limits for several types of commercial uses within the zoning district. Id. at 331. One of the recognized purposes of the ordinance was "to promote a balance of uses in the district 'by controlling the number and size of uses which have increased in number at the expense of district commercial diversity.'" Id. (citing Memo from Planning Commission to the Mayor and Members of Council 2 (Mar. 20, 1984)).

43. The Elmwood district has been characterized as a "vibrant relic of Main Street past." Stern, Berkeley Merchants Fear Loss Of Rent Control, Oakland Tribune, June 17, 1987, at B-1, col. 5. It encompassed 84 stores in 1982. Keating, supra note 2, at 111.

44. Ozzie's soda fountain sports genuine red Naugahyde stools and offers such delicacies as grilled cheese sandwiches and potato chips. Stern, supra note 43, at B-1, col. 5. Some feel, however, that such quaint establishments belong in a museum, rather than in a prime commercial location. Id. at B-8, col. 5; see infra note 211.

45. Keating, supra note 2, at 117.

46. The Elmwood Commercial Rent Stabilization and Eviction for Good Cause Ordinance, Berkeley, Cal., Ordinance 5468-NS, passed by an impressive 58% to 42% margin on June 8, 1982. Keating, supra note 3, at 124; see BERKELEY, CAL., MUN. CODE §§ 13.80.010-.160 (1987). As the court noted in Ross, however, several significant differences exist between the first rent control initiative and the Elmwood ordinance. Foremost, the temporary initiative "was not so much of a commercial rent control scheme as it was a limited form of property tax
intended to protect commercial tenants in the Elmwood district from rent increases which are not justified by landlord's cost increases; to enable those tenants to continue serving residents of the Elmwood district without undue price increases, expansion of trade, ... or going out of business; and to test the viability of commercial rent stabilization as a means of preserving businesses which serve the needs of local residents in Berkeley neighborhoods, outside the downtown business district.47

Section 16 of the Elmwood ordinance specifically required the Planning Department to recommend to the City Council whether the "scope of the Ordinance should be expanded to include other neighborhood shopping districts in the City of Berkeley outside the downtown business district."48

D. The Process and Purposes of the Telegraph Avenue Ordinance

The problems in the Telegraph Avenue area came to the attention of Berkeley's Mayor, Eugene "Gus" Newport, in the context of the disappearance of neighborhood businesses and the gentrification of the city's commercial districts. In late 1984, thirteen Telegraph Avenue merchants requested a meeting with Mayor Newport to discuss the rent increases and arbitrary evictions that they perceived to be threatening to small Telegraph Avenue businesses and to ask the city government to intervene to protect existing businesses.49

Concerned by the rapid change that the Avenue was undergoing, the mayor outlined for the City Council "a number of recent changes in the character of the Telegraph Avenue business district which [he] believed might warrant an extension of the Elmwood ordinance to the Telegraph business district."50 Existing businesses whose leases were coming

relief; its purpose was not to prevent the displacement of merchants." Ross v. City of Berkeley, 655 F. Supp. 820, 823 (N.D. Cal. 1987) (citing Keating, supra note 2, at 137). The Elmwood ordinance, on the other hand, was not a temporary measure. Rather, it was enacted for the primary purpose of preserving small businesses through rent and eviction regulation. BERKELEY, CAL., MUN. CODE § 13.80.020 (1987).

For a discussion of the mechanics of the Elmwood ordinance, see infra notes 62-68 and accompanying text.

48. Id. § 13.80.160.
49. Interview with Sean Gordon, Aide to Mayor Newport (Mar. 29, 1987); see also Defendant's Memorandum of Points and Authorities in Opposition to Plaintiffs' Motion for Summary Judgment at 5, Ross, 655 F. Supp. 820 (N.D. Cal. 1987) (No. C-85-7321-MHP) [hereinafter Defendant's Opposition Brief]. At that meeting, the Mayor learned that numerous businesses were subject to sharply increased rents, which threatened their ability to remain on the Avenue. Declaration of Sean Gordon at 3, Ross, 655 F. Supp. 820 (N.D. Cal. 1987) (No. C-85-7321-MHP) (sworn Oct. 2, 1986). For instance, the only grocery store serving the area south of campus had been subject to a 400% rent increase. A sporting goods store that had been on the Avenue for 68 years was to be replaced by a chain sporting goods store. Id. 50. Ross, 655 F. Supp. at 824.
due were subject to precipitous rent increases.\textsuperscript{51} Indeed, the market rate for commercial space on Telegraph Avenue was rising from one dollar or less per square foot to approximately three dollars per square foot.\textsuperscript{52} Because of this increase in rent, locally owned, independent businesses faced displacement by stores that could afford such rates—largely chain stores and franchises.\textsuperscript{53} Finally, a broad range of retail uses was being replaced with a much narrower range of uses, principally food related.\textsuperscript{54}

With the City Council's approval, the mayor appointed an ad hoc committee to study the problems of the Telegraph Avenue commercial district and "to investigate the various policy options available to the City to regulate rental practices in the Telegraph Avenue district. The mayor indicated that possible courses of action 'could range from the development of an area plan to development of a commercial rent stabilization measure for this area.'"\textsuperscript{55} The mayor's committee met several times and, as part of "an area planning process," developed a set of recommendations to regulate rents, evictions, and use changes in the area for a ninety-day period.\textsuperscript{56} The City Council adopted the recommendations as an urgency ordinance\textsuperscript{57} on February 26, 1985,\textsuperscript{58} and the Planning Commission was charged with drafting the final ordinance.\textsuperscript{59} On January 21, 1986, the City Council, based on a proposal by the Planning Commission, enacted a permanent rent and eviction control ordinance for the Telegraph Avenue commercial district, which became effective

\textsuperscript{51} See id.
\textsuperscript{52} Id.
\textsuperscript{53} Id. During this period, small businesses just starting out had a distressingly high failure rate. For instance, a cafe on Telegraph went out of business in only four months and the owners lost their life savings because they were not able to survive financially as a new community business. Gordon interview, supra note 49.
\textsuperscript{54} Ross, 655 F. Supp. at 824.
\textsuperscript{55} Id.
\textsuperscript{56} Report of the Ad Hoc Committee on Telegraph Avenue to Mayor and City Council 1-3 (Feb. 15, 1985); see also Ross, 655 F. Supp. at 824.
\textsuperscript{57} See CAL. GOV'T CODE § 36,934 (West 1988) (defining "urgency ordinance").
\textsuperscript{58} Berkeley, Cal., Ordinance 5640-N.S. (Feb. 26, 1985); see supra note 8.
\textsuperscript{59} Ross, 655 F. Supp. at 825. The Planning Commission established a Telegraph Avenue subcommittee to study the conditions in the Telegraph Avenue area. The subcommittee was given three responsibilities: (1) discerning the pattern of rent increases and evictions in the Telegraph Avenue area, (2) developing a plan for the regulation of specific types of uses in the district, and (3) formulating a permanent approach to leasehold conditions in the area. The subcommittee, which met weekly for nine months, specifically identified three goals of the proposed ordinance: (1) reducing the impact of rent increases, evictions, and turnovers; (2) encouraging small, responsive Berkeley businesses; and (3) reducing "pressures" on local businesses. Thus, the overall purposes of the ordinance were not merely to preserve uses, but to preserve the kinds of small independent businesses that had served the community and were being threatened by the gentrification of Berkeley neighborhoods. See Declaration of Denise Pinkston, Ross, 655 F. Supp. 820 (N.D. Cal. 1987) (No. C-85-7321-MHP) (sworn Oct. 2, 1986).
March 1, 1986. The stated purpose of the final ordinance was "to preserve the unique character of the Telegraph Avenue Area commercial district and to prevent displacement of businesses by excessive rent increases and/or evictions."61

II
THE MECHANICS OF COMMERCIAL RENT AND EVICTION CONTROLS

Although the primary purpose of the three commercial rent control ordinances was to prevent the displacement of small independent businesses, the rent control provisions of the Elmwood ordinance were tailored to protect the unique character of the area. Those provisions, therefore, varied substantively and procedurally from the rent control provisions of the later Telegraph Avenue and West Berkeley ordinances. All three ordinances mandated rent regulation and eviction control. The Elmwood ordinance, however, imposed rent ceilings, whereas the Telegraph Avenue ordinance and the similar West Berkeley ordinance instituted a program of rent arbitration and mediation. All three ordinances imposed similar eviction controls.

A. The Rent Regulations

To accomplish its purposes, the Elmwood ordinance subjected all commercial premises within the two-block Elmwood district, including newly constructed and rehabilitated units, to rent and eviction regulation.63 Leases, however, were not subject to the ordinance until they expired.64 When renegotiating or entering into new leases, landlords were entitled to charge a base rent (the rent charged on October 1, 1981) plus increases based on maintenance and operating expenses, property taxes, fees, and improvements.66 Additionally, landlords were guaran-
Landlords were entitled to increase rents after giving tenants thirty-days written notice and informing them of the cost increases involved.

Unlike the Elmwood ordinance, the Telegraph Avenue ordinance did not establish a rent ceiling, but instead provided for rent mediation and binding arbitration to determine commercial rent levels. Certain rent increases, including those not exceeding the Consumer Price Index for the Oakland/San Francisco Standard Metropolitan Statistical Area and those reduced to writing by the parties, were not subject to the arbitration process. Additionally, rents were decontrolled—i.e., not subject to the arbitration process—when property was vacated. All other rent increases were to be submitted to an arbitrator upon petition of either the tenant or the landlord, to be evaluated on the basis of eighteen enumerated criteria. The criterion to be given “particular weight” was the extent to which the business contributed to the overall uniqueness and diversity of Telegraph Avenue. Either party was entitled to appeal the

67. BERKELEY, CAL., MUN. CODE § 13.80.060(A) (1987). Administration of the fair return provision was delegated to the Berkeley Board of Adjustments (a zoning appeals board appointed by the City Council), which was required to promulgate fair return regulations. Id. § 13.80.060(C). See Keating, supra note 2, at 139-53 for a discussion of how to calculate a fair return.


69. Id. §§ 13.82.060, .070, .110; see Ross, 655 F. Supp. at 826.

The West Berkeley ordinance, which was modeled after the Telegraph Avenue regulations, also provided for rent mediation and binding arbitration to determine commercial rent levels. See BERKELEY, CAL., MUN. CODE §§ 13.86.010-160 (1987).

70. Id. § 13.82.060(B).

71. Id. § 13.82.070(A). The following are the 18 criteria by which an arbitrator was to evaluate a commercial rent level (with “particular weight” to be given to the first):

(i) The extent to which a business contributes to the uniqueness and diversity of the Telegraph Avenue Area and to the availability of goods and services in the Telegraph Avenue Area and the city.
(ii) The location of the business.
(iii) The size of the rented space.
(iv) Services provided by the landlord and tenant.
(v) The condition of the unit.
(vi) Rent increases in the present or most recently expired rental agreement.
(vii) Liabilities relating to the use of the rented space created by the landlord or tenant.
(viii) The history of performance or lack of performance of lease obligations by the parties.
(ix) The terms of the existing or most recently expired lease.
(x) The amortized cost of reasonable capital improvements by the landlord or tenant to the premises.
(xi) The good will built up for the business by the tenant.
(xii) Changed circumstances since the prior lease was executed.
(xiii) The market rent for comparable commercial spaces.
(xiv) Market rents for similar types of commercial uses.
(xv) Existing rent for comparable uses and spaces in the area.
(xvi) Availability of reasonable relocation opportunities in the Telegraph Avenue area or in reasonably close proximity to the area.
(xvii) Rent received by the tenant from subtenants.
(xviii) All other relevant factors.

Id. Thus, there was no predetermined ceiling on rents or percentage increases.
arbitrator's ruling to the superior court within sixty days.\textsuperscript{72}

\section*{B. The Eviction Controls}

According to one architect of the Telegraph Avenue controls, the enactment of strong eviction protections was seen as the cornerstone of the program to prevent displacement of small local businesses.\textsuperscript{73} The Telegraph Avenue and West Berkeley ordinances borrowed their protective eviction sections largely from the Elmwood ordinance.\textsuperscript{74} "Good cause" for eviction or for failure to renew a lease was limited to certain breaches by the tenant enumerated in the ordinances, such as failure to pay rent, substantial lease violation, or refusal to renew or extend an expired lease.\textsuperscript{75} Importantly, the ordinances did not permit owner occupancy as a just cause for lease nonrenewal.\textsuperscript{76}

Once it was decided that a program of rent and eviction controls was to be adopted for the Telegraph Avenue area, the most fractious issue for the Planning Commission became whether owner occupancy should be recognized as a good cause for recovery of possession.\textsuperscript{77} The Telegraph Avenue subcommittee of the Planning Commission, which included Telegraph Avenue property owners, merchants, and city officials, finally recommended to the full Commission that owner occupancy be

\begin{itemize}
\item \textsuperscript{72} Id. § 13.82.110(D)(3).
\item \textsuperscript{73} Sean Gordon, aide to Berkeley Mayor Newport, has stated that the real problem for Telegraph merchants was not escalating rents so much as it was the inability to negotiate long-term leases. Gordon interview, supra note 49. Gordon, a key member of the Telegraph Avenue Committee, therefore advocated rent mediation and strict eviction controls rather than a rent ceiling.
\item During 1984, while a temporary ordinance was in effect, Gordon and City Manager Daniel Boggan, Jr., successfully mediated disputes between several Telegraph Avenue merchants and their landlords. After the adoption of the final ordinance, there were no arbitrations. Gordon saw this as a sign of success. The ordinance, by exempting voluntary agreements between landlords and merchants from the ordinance's arbitration procedure, encouraged merchants and their landlords to arrive at such agreements. Gordon saw the fostering of negotiation as the main goal of the ordinance and was satisfied that, until its demise, the ordinance had done just that.
\item \textsuperscript{74} Compare BERKELEY, CAL., MUN. CODE § 13.80.090 (1987) (Elmwood) with id. § 13.82.090 (Telegraph Avenue) and id. § 13.86.080 (West Berkeley).
\item The Telegraph Avenue ordinance, for example, specified the following grounds for eviction: (1) failure to pay rent; (2) substantial lease violation; (3) committing a nuisance on the premises; (4) using the premises for an illegal purpose; (5) refusal to renew or extend an expired lease; and (6) refusal to provide the landlord access to make repairs or improvements or to show the premises to prospective buyers or tenants. Id. § 13.82.090.
\item The Elmwood ordinance permitted an owner to evict to recover possession for the purpose of removing the rental unit from commercial use, whereas the Telegraph ordinance omitted this provision. Compare id. § 13.80.090(G) with id. § 13.82.090.
\item The Berkeley City Council, as part of its settlement agreement with the Rosses, amended the Telegraph Avenue ordinance to allow for owner-occupancy evictions. The amendment became effective on August 28, 1987. See Berkeley, Cal., Ordinance 5827-NS (July 28, 1987) (codified as amended at BERKELEY, CAL., MUN. CODE § 13.82.090 (1987)).
\item Declaration of Denise Pinkston, supra note 59, at 2-4; see Ross, 655 F. Supp. at 825.
\end{itemize}
excluded as a ground for eviction because of the potential for fraud and abuse (e.g., landlords not really intending to occupy the property themselves). A heated debate among members of the Planning Commission ensued, with some expressing the view that exclusion of owner occupancy as a just cause for eviction would be unfair to owners, while others claimed that allowing owner-occupancy evictions would open a huge loophole in the ordinance's protections. The Commission was unable to come to an agreement on the matter and forwarded the ordinance to the City Council with no recommendation on the owner-occupancy provision.

Berkeley's city manager submitted a separate report to the City Council in which he argued in favor of excluding owner occupancy as a good cause for eviction. He reasoned that owners might be encouraged to mask true ownership through paper transactions because they could then rent property to new tenants at uncontrolled rent levels. The report also indicated that alternatives to the prohibition of owner-occupancy evictions, such as compensation for evicted businesses and penalties for bad-faith evictions, would be inadequate. On January 21, 1986, when the Berkeley City Council adopted the Telegraph Avenue ordinance, it excluded owner occupancy as a good cause for recovery of possession.

III

THE CONSTITUTIONAL CHALLENGE TO COMMERCIAL RENT CONTROL

Although the Elmwood ordinance had been in effect for several years, none of Berkeley's commercial rent control programs was challenged in court until Arthur and Grace Ross filed suit against the city in federal district court, alleging that the Telegraph Avenue ordinance prevented them from regaining possession of their rental property either by evicting their tenants or by refusing to renew the lease upon its expiration. The court granted summary judgment to the plaintiffs on their contract clause claim. Later, it granted summary judgment to the
defendant on the takings and due process claims and certified three constitutional issues for interlocutory appeal to the Ninth Circuit Court of Appeals. By the time the amended opinion was released, however, it was clear that the California Legislature would preempt the ordinance—rendering an appeal pointless—and the parties settled. Thus, as the district court admitted when it certified the issues and as the Ninth Circuit's acceptance intimated, many legal issues were left uncertain.

Although commercial rent control is now preempted in California by state legislation, it is instructive to examine briefly the district court's opinion as a guide for other communities to design and implement future land use measures. In the past two decades, land use regulation has come to involve a broad range of activities never contemplated when it was first introduced in the late 1800's in this country. Sixty years after Village of Euclid v. Ambler Realty Co., the United States Supreme Court—which for decades left land use issues primarily to the state courts—once again is providing a constitutional guide to local land use regulations. Accordingly, land use law is now in a state of flux: lawyers and planners who grapple with thorny urban problems must be cognizant of the constitutional implications of their actions. Berkeley's

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86. Id. at 844; see infra note 101.
88. See, e.g., D. HAGMAN, URBAN PLANNING AND LAND DEVELOPMENT CONTROL LAW § 29, at 68-69 (1971). State and local agencies, for instance, are now turning to land use regulations to preserve property that is historic, scenic, or environmentally sensitive. Local governments also are using land use laws as a means by which they can attach conditions to new developments to mitigate the adverse impacts of such developments. See, e.g., Russ Building Partnership v. City and County of San Francisco, 188 Cal. App. 3d 977, 234 Cal. Rptr. 1 (1987) (upholding the assessment of transit impact fees on new office developments to offset the impact of thousands of new office workers on the transit system).
89. In 1926, the Court ruled that local zoning laws were constitutional. Village of Euclid v. Ambler Realty Co., 272 U.S. 365 (1926). Two years later, the Court limited the state's regulatory powers by ruling that a constitutional zoning ordinance could be unconstitutionally applied to a specific parcel of land. Nectow v. City of Cambridge, 277 U.S. 183 (1928).
91. See Nollan v. California Coastal Comm'n, 107 S. Ct. 3141 (1987) (criticizing California land use law and ruling that the nexus between the condition imposed on a development and the impact of that development was not sufficiently close to allow the Coastal Commission to require a property owner to grant a beachfront easement to the public in exchange for a building permit); First English Evangelical Lutheran Church v. County of Los Angeles, 107 S. Ct. 2378 (1987) (overturning California case law by ruling that a property owner is entitled to damages under the fifth amendment for temporary takings of private property).
92. "After all, a policeman must know the Constitution, then why not a planner?" San
Telegraph Avenue ordinance provides an excellent case study of the potential challenges to an innovative land use regulation.

**A. Background**

Arthur and Grace Ross were the owners and lessors of the building that houses Espresso Roma, a successful “international style” cafe situated adjacent to the University of California campus in the Telegraph Avenue commercial area. In 1980, the cafe was a marginal business. Thus, when Arthur Ross bought the property and doubled the rent, the tenant of the cafe declined to enter into a new lease. Instead, Ross entered into a five-year lease with two Berkeley students. The lease did not contain any provision for extension or renewal in the absence of an express agreement.

After several years of concentrated effort, the cafe became a popular and lucrative business. The Rosses notified the cafe tenants six months prior to the expiration of the lease that it would not be renewed when it expired in June 1985. The tenants, however, did not vacate the premises when the lease term expired nor were they subject to eviction, because the Telegraph Avenue ordinance, which had been enacted during the lease term, excluded owner occupancy as a good cause for eviction.

The Rosses sued the City of Berkeley in federal district court, claiming that the ordinance unconstitutionally deprived them of possession of their premises under the contract clause, the due process clause, and the
The gravamen of plaintiffs' complaint was that, by failing to acknowledge owner occupancy as good cause for nonrenewal of a commercial lease, the ordinance unconstitutionally upset the contractual agreement reached between lessor and lessee and deprived the owner of property without due process or just compensation. The court granted plaintiffs' motion for summary judgment on their contract clause claim while granting summary judgment for the city on the plaintiffs' taking and due process claims.

B. The Legal Disposition

1. The Takings Claim

The Rosses did not prevail on their claim that the ordinance effected an unconstitutional taking of their property without just compensation.

Generally, government may regulate the use of private property, but if the regulation "goes too far" it will be recognized as a taking for which just compensation is due. The district court, however, decided the takings issue on procedural grounds. Although the court found that the governmental action did amount to a taking of property that advanced a legitimate governmental interest, the court concluded that the


100. Ross, 655 F. Supp. at 823.

101. Id. at 844. The court granted summary judgment to defendants, the nonmoving party, because plaintiffs' failure to raise a genuine dispute of fact with respect to both the legislative irrationality of the defendant's enactment under the Due Process Clause as well as their exhaustion of the City's administrative processes available for just compensation under the Takings Clause obviates the need for further consideration of either claim, and entitles the City to judgment.

102. See id. at 836-42 for discussion of plaintiffs' takings claim. It should be noted that the United States Supreme Court recently reaffirmed that residential rent controls are not per se takings. Pennell v. City of San Jose, 108 S. Ct. 849, 857 n.6 (1988). Courts may be unsympathetic, however, to analogizing residential rent control to commercial rent control. See, e.g., Ross, 655 F. Supp. at 833-34 (as justification for impairment of contract, preserving a shopping district's diversity vastly less compelling than preventing evictions of elderly and disabled persons from their homes).

103. See Pennsylvania Coal Co. v. Mahon, 260 U.S. 393 (1922). The takings clause of the fifth amendment states: "nor shall private property be taken for public use without just compensation." U.S. CONST. amend. V. This clause is made applicable to the states through the fourteenth amendment. See D. MANDELKER AND R. CUNNINGHAM, PLANNING AND CONTROL OF LAND DEVELOPMENT 50 (2d ed. 1979).
plaintiffs' just compensation claim was not ripe for consideration. Plaintiffs had not invoked the ordinance's arbitration provisions and thereby failed to determine whether administrative remedies could provide just compensation.

A threshold question in a takings analysis is whether the claim involves a physical occupation—a so-called *Loretto* taking—or a regulatory taking. This initial inquiry is significant because a permanent physical occupation is considered a taking on its face, whereas a regulation is subject to a balancing test. A permanent physical occupation destroys three critical property rights: "the rights to possess, use and dispose of [the property]." Applying these factors, the *Ross* court found that "plaintiffs have suffered a taking through defendant lessees' state-authorized permanent occupation of their property, and are thus due just compensation." The court was particularly concerned that the ordinance had impaired plaintiffs' right to alienate their property and that the cafe's present tenants, through Espresso Roma's corporate structure, conceivably could transfer their right to remain on the property to third parties. As the court itself noted, however, whether the commercial rent regulation worked a permanent physical invasion is far from clear. Whether courts in the future will decide that commercial eviction protections go so far as to effect a permanent physical invasion remains an open question.

The second inquiry required of a takings analysis is whether the tak-
ing, once established, advances a legitimate governmental interest. In *Hawaii Housing Authority v. Midkiff*, the Supreme Court held that the "public use" requirement is "coterminous with the scope of a sovereign's police powers." In *Midkiff*, the Court suggested a very deferential standard in reviewing a legislature's judgment of what constitutes a public use: "deference to the legislature's 'public use' determination is required 'until it is shown to involve an impossibility.'" The *Ross* court, following *Midkiff*, held that commercial rent control promotes a legally valid public purpose.

When a court finds that property has been taken physically for a legitimate public use, the property owners are entitled to just compensation for their loss. The court first must look to the compensation available through the administrative processes of the respective government. The compensation due the Rosses, the court held, must reflect not only the property's rental value, but also the value of the reversionary interest in the property. Because the plaintiffs had not yet petitioned for any rental adjustment under the ordinance, the court ruled that the

115. *Id.*
116. *Id.* (citing Old Dominion Land Co. v. United States, 269 U.S. 55, 66 (1925)).
117. *Ross*, 655 F. Supp. at 840. The court seems to have reached this holding reluctantly. "Under [the] exceedingly deferential [Midkiff] standard, this court cannot conclude that Berkeley could not have rationally believed that its prohibition of owner occupancy evictions would promote its objective of preserving the ambience and character of the Telegraph Avenue commercial district." *Id.* at 839-40 (citing Penn Cent. Transp. Co. v. New York City, 438 U.S. 104, 129 (1978) (preserving the character and "desirable aesthetic features of a city" a valid exercise of the state's police power)). The court also suggested that the Ninth Circuit, in dicta, may have formulated a less deferential standard than "rationality" in cases in which the taking did not occur pursuant to a deliberate exercise of the state's power of eminent domain. *See Hall v. City of Santa Barbara*, 797 F.2d 1493, 1502 (9th Cir. 1986). Briefly, the *Hall* court stated in a footnote that it makes sense to give greater deference to the legislature when it deliberately resorts to eminent domain and to afford less deference in cases in which the legislature may not have intended to engage in a compensable transaction, such as inverse condemnation. *Id.* at 1503 n.25.

118. *Hall*, 797 F.2d at 1500. If a court finds that a regulation does not advance a legitimate public purpose, the property owner is entitled to damages for an interim taking, as well as invalidation of the legislation. First English Evangelical Lutheran Church v. County of Los Angeles, 107 S. Ct. 1378 (1987).

119. *Ross*, 655 F. Supp. at 840. "[A] court cannot determine whether a municipality has failed to provide 'just compensation' until it knows what, if any, compensation the responsible administrative body intends to provide." *Id.* at 841 (quoting MacDonald, Sommers & Frates v. Yolo County, 106 S. Ct. 2561, 2566-67 (1986)); *see also* Pennell v. City of San Jose, 108 S. Ct. 849 (1988) (in takings cases the constitutionality of a statute should be decided only when the factual setting makes such a decision ripe and, therefore, necessary).


121. The court certified for immediate appeal the question whether, under the less deferential standard that was enunciated in *Hall*, 797 F.2d at 1504, plaintiffs had sufficiently exhausted the city's administrative processes for just compensation. *Ross v. City of Berkeley*, No. C-85-7321-MHP (N.D. Cal. June 11, 1987) (order certifying opinion for immediate appeal).
claim for just compensation was not ripe for adjudication.\textsuperscript{122}

2. \textit{The Substantive Due Process Claim}

Plaintiffs also claimed that they were deprived of their property in violation of their fundamental substantive rights under the fourteenth amendment.\textsuperscript{123} Close judicial scrutiny of economic legislation, as employed in \textit{Nectow v. City of Cambridge},\textsuperscript{124} one of the first zoning cases considered by the Supreme Court, has been rejected categorically in a long line of cases.\textsuperscript{125} An extremely deferential standard of review has been used for forty years: legislation will be held an invalid exercise of the sovereign's police power only if the court cannot conceive of any rational relation between an economic enactment and a legitimate governmental objective.\textsuperscript{126} Although the \textit{Ross} court noted that dicta in several recent Supreme Court cases may throw traditional substantive due process analysis into question,\textsuperscript{127} it felt bound to defer to legislative judgment. The court stated that it could not conclude "that the Telegraph Avenue ordinance is so irrational that it violates plaintiffs' substantive due process rights."\textsuperscript{128}

\textsuperscript{122} \textit{Ross}, 655 F. Supp. at 841. The court was especially concerned that the ordinance's 18 criteria for determining commercial rent levels would not sufficiently take into account "an owner's loss of his or her reversionary interest in possession." \textit{Id.} Whether or not commercial rent control—or any other land use regulation for that matter—constitutes a taking is now of particular import to local agencies. Since \textit{Ross} was decided, the Supreme Court has held that the remedy for a temporary taking is not limited to nonmonetary relief, such as invalidation of the regulation, but may include monetary compensation as well. See \textit{supra} note 118. "Before this court can determine that the City has denied just compensation for the taking of plaintiffs' property, plaintiffs must invoke the City's rent arbitration procedure and test the discretion invested in the arbitrator to adequately compensate them for their loss." \textit{Ross}, 655 F. Supp. at 841.

\textsuperscript{123} See \textit{Ross}, 655 F. Supp. at 842-44, for the court's disposition of the due process claim.

\textsuperscript{124} 277 U.S. 183 (1928).


\textsuperscript{127} The court noted in its opinion that there is significant uncertainty surrounding constitutional analysis of substantive due process claims in the wake of \textit{Williamson County Regional Planning Comm'n v. Hamilton Bank}, 473 U.S. 172, 198-99 (1985). \textit{Ross}, 655 F. Supp. at 842-44. The district court suggested that dicta in \textit{Williamson} supports the notion that, absent the deliberate procedure of eminent domain, a taking would constitute a per se violation of substantive due process. \textit{Ross}, 655 F. Supp. at 844.

In \textit{Nollan v. California Coastal Commission}, decided subsequent to \textit{Ross}, Justice Scalia raised questions as to the correct inquiry when property regulations are challenged as violative of substantive due process. 107 S. Ct. 3141, 3147 n.3. In \textit{Pennell v. City of San Jose}, however, Chief Justice Rehnquist reiterated that the standard, first enunciated in \textit{Nebbia}, for determining whether a state price-control regulation is constitutional under the due process clause is whether the price control is arbitrary, discriminatory, or demonstrably irrelevant to the policy. 108 S. Ct. 849 (1988).

\textsuperscript{128} \textit{Ross}, 655 F. Supp. at 844.
3. *The Contract Clause Claim*

The United States Constitution provides that "[n]o State shall . . . pass any . . . Law impairing the Obligation of Contracts . . . ."\(^{129}\) Although absolute on its face, it has long been recognized that the language of the contract clause does not act as a complete bar to legislative interference with existing contractual obligations, but rather must be accommodated within the inherent police power of the state.\(^ {130}\)

Contract clause analysis is articulated as a three-part inquiry.\(^ {131}\) The threshold question is whether there is a substantial impairment of the contract.\(^ {132}\) If the state regulation constitutes a substantial impairment, the court must determine whether there is a significant and legitimate public purpose behind the regulation.\(^ {133}\) Third, once a significant public purpose has been identified, the court also must be satisfied that the legislation is based on reasonable conditions and is of a character appropriate to the legislature's public purposes.\(^ {134}\) If the challenged legislation interferes with a contract between private parties, the courts defer to legislative judgment as to the necessity and reasonableness of the particular measure, as is customary in reviewing economic and social regulations in other contexts.\(^ {135}\) Given the severity of the contractual impairment, the Ross court analyzed this third prong of the test "with some degree of care."\(^ {136}\) Under this heightened level of scrutiny, the court found that the exclusion of owner occupancy as a just cause for eviction rendered the eviction section of the ordinance unconstitutional under the contract clause, at least as to leases entered into before the enactment of the Elmwood ordinance in 1982.\(^ {137}\)

The Ross court noted, furthermore, that the Supreme Court has suggested several factors that bear on substantiality of impairment. The factors include (1) whether the state has restricted plaintiffs to gains they reasonably expected from the contract and (2) the extent to which the

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133. Legitimate public purposes include remedying general social and economic problems. See Keystone, 107 S. Ct. at 1251; Energy Reserves, 459 U.S. at 411.
137. Id. at 835.
enterprise entered into by the contracting parties was subject to state regulation at the time of the agreement.\textsuperscript{138}

The district court ruled that the Telegraph Avenue ordinance severely upset the contractual expectations of the parties in \textit{Ross} and did so in a field that had not been regulated previously. In the court's words, "[P]laintiffs could not have reasonably foreseen the impending legislative nullification of their right to recover possession of their commercial premises [after the five-year lease term expired] until the passage, some two years after execution of the lease, of the Elmwood commercial rent and eviction control ordinance."\textsuperscript{139}

The court dismissed Berkeley's 1978 temporary commercial rent control ordinance and its myriad land use restrictions as of a different nature, insufficient to put the Rosses on notice of the impending regulation.\textsuperscript{140} The court held, therefore, that the ordinance substantially impaired the Rosses' contractual rights. Thus, the ordinance had to be justified by a significant and legitimate public purpose in order to withstand contract clause scrutiny.

As in the takings clause analysis, the court found that, under a deferential standard, the Telegraph Avenue ordinance furthered the significant and legitimate public purpose of preserving the ambience and character of the Telegraph Avenue shopping district.\textsuperscript{141} As the court went on to note, however, "preserving a neighborhood shopping district's diversity—while not an illegitimate subject for legislative enactment"—is

\textsuperscript{138} \textit{Id.} at 828.

\textsuperscript{139} \textit{Id.} at 830. The City of Berkeley asserted that Ross had never expressed any interest in running a cafe; therefore, no valid expectation was impinged when the ordinance prevented him from reentering his property to run a business. See Defendants' Opposition Brief, \textit{supra} note 49, at 34. Plaintiffs vigorously contested this assertion. The court concluded that, whatever Ross's subjective intent, by entering into a five-year lease Ross did not waive his right to reenter the premises. \textit{Ross}, 655 F. Supp. at 828 & n.8.

\textsuperscript{140} \textit{Ross}, 655 F. Supp. at 830. "Considering the holdings in \textit{Energy Reserves} and \textit{Allied Structural Steel}, it is evident that prior regulation must share more in common with the challenged legislation than merely the industry in which it operates to bar a subsequent finding of substantial impairment." \textit{Id.} at 831.

Although commercial real estate was a regulated field, the nature of previous legislation did not foreshadow strict eviction controls:

Berkeley's nullification of an owner's right to recover possession at the end of a lease, while operating within an industry previously subject to regulation, is entirely unrelated in nature to the City's prior legislative efforts to zone for commercial uses or provide for the partial rebate of property tax windfalls.

\textit{Id.} (footnote omitted).

\textsuperscript{141} The court stated that,

in light of the deference with which this court must scrutinize the legislation in question and its obligation to refrain from evaluating the wisdom of the enactment as a matter of policy, it cannot be concluded that Berkeley's desire to preserve the ambience and character of the Telegraph Avenue shopping district sufficiently exceeds the City's police power that it facially fails to justify the enactment's impairment of contract.

\textit{Id.} at 834; see \textit{supra} notes 113-17 and accompanying text.
not a particularly compelling purpose either.\textsuperscript{142} The relative insignificance of the legislation's purpose, in the court's view, weighed heavily in the decision.

An enactment that substantially impairs the obligation of contracts must be based "upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption."\textsuperscript{143} Although the court found the eviction section of the ordinance overbroad and based on a public purpose of "limited social significance,"\textsuperscript{144} it also recognized that the standard under which the reasonableness of the regulations should be reviewed is hardly settled law.\textsuperscript{145} The Supreme Court has stated clearly, however, that judicial review is less stringent where the state is not a contracting party.\textsuperscript{146} Stressing the heightened need for judicial oversight when "the State's self-interest is at stake," the Court has adopted "a dual standard of review."\textsuperscript{147} The Court would defer to legislative interference in the contracts of private parties, but would scrutinize more closely state abrogations of governmental obligations.\textsuperscript{148} This standard is certainly more deferential than the standard the \textit{Ross} court used to analyze the Telegraph Avenue ordinance, yet the determination of this issue was dispositive of the case at the district court level.

This lesser standard for private contracts was reaffirmed recently in \textit{Keystone Bituminous Coal Association v. DeBenedictis}.\textsuperscript{149} In \textit{Keystone}, the Court stated that although the severity of the impairment affects the level of scrutiny, a law that totally impairs an existing contract is not invalid under the contract clause if that act furthers a legitimate public purpose. Judicial review, moreover, must not "second-guess" the legislature's determination of the most appropriate ways of dealing with the problem; rather, it must "properly defer to legislative judgment as to the necessity and reasonableness of a particular measure."\textsuperscript{150}

\textsuperscript{142} \textit{Ross}, 655 F. Supp. at 833-34.
\textsuperscript{143} \textit{Id.} at 834.
\textsuperscript{144} \textit{Id.} at 835-36.
\textsuperscript{145} The court admitted that, as to the contract clause claim, there are substantial grounds for difference of opinion regarding the degree of scrutiny appropriate for the judicial review of legislation impairing contracts to which the state is not a party. \textit{Ross v. City of Berkeley}, No. C-85-7321-MHP, slip op. at 2 (N.D. Cal. June 11, 1987) (order certifying opinion for immediate appeal) (citing \textit{Keystone Bituminous Coal Ass'n v. DeBenedictis}, 107 S. Ct. 1232, 1253 (1987); \textit{Allied Structural Steel v. Spannaus}, 438 U.S. 234, 244, 247 (1978)).
\textsuperscript{146} \textit{United States Trust Co. v. New Jersey}, 431 U.S. 1, 26 (1977).
\textsuperscript{147} \textit{Id.}
\textsuperscript{148} \textit{Id.} at 26 & n.25.
\textsuperscript{149} 107 S. Ct. 1232 (1987).
\textsuperscript{150} \textit{Id.} at 1253. At issue in \textit{Keystone} was a state law that prohibited coal mining that caused subsidence damage to preexisting public buildings, dwellings, and water courses. Petitioners, who owned or controlled substantial coal reserves under protected property, alleged that the law impaired their rights under the contract clause by denying them the right to hold surface owners to contractual waivers of liability for surface damage. The Court held that the contract clause, as opposed to other provisions of the fourteenth amendment, has not been read literally so as to obliterate the valid exercise of the police power. \textit{Id.} at 1251. Thus, even
The district court in *Ross*, by contrast, appears to have substituted its own judgment for that of the City Council. The court found that the owner-occupancy provision was not a reasonable means for the city to diversify and preserve community-serving businesses and that the ordinance was overbroad. The district court's finding, contrary to the Supreme Court mandate, second-guessed legislation it held to be a legitimate exercise of public authority.

**C. The Decision's Impact**

Any takings, due process, or contract clause analysis involves a determination of whether the contested regulation promotes a legitimate state interest or, more fundamentally, who should bear the burden of achieving a social benefit—a private party or the public at large. In the broadest sense, therefore, the fight over commercial rent control reflects the tension between the right of property owners to control and enjoy their property and the need, in an increasingly developed world, for coherent city and regional planning, which may impinge on the rights of property owners. The *Ross* court found the Telegraph Avenue ordinance to be of limited social significance, and this proved determinative in its view of how the burdens and benefits of planning for the Telegraph Avenue area should be allocated.

The immediate impact of the *Ross* decision was to invalidate the eviction section of the Telegraph Avenue ordinance as to leases executed prior to 1982. The remainder of the ordinance—the mediation and

though the regulation operated as a substantial impairment of a contractual relationship, the imposition of liability on the coal companies was found to protect a significant and legitimate public interest in preventing subsidence damage. Because the state was not a contracting party, the state's determination of the most appropriate means by which to handle the problem would not be second-guessed. The Court thus held that the impairment of petitioners' right to enforce the damage waivers was amply justified by the public purpose served by the law. *Id.* at 1253.

151. *Compare* Pennell v. City of San Jose, 108 S. Ct. 849, 856 (1988) ("it is axiomatic that the Fifth Amendment's just compensation provision is designed to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole") (citation omitted) with Keystone, 107 S. Ct. at 1252 ("It is petitioners' position that... they have a constitutionally protected legal right to make a shamble of... buildings and cemeteries... [Pennsylvania] has a strong public interest in preventing this type of harm, the environmental effect of which transcends any private agreement between contracting parties.").

152. Defendant proposed that the court's holding on the unconstitutionality of the owner-occupancy provision be limited to leases formed prior to the passage of the Elmwood ordinance in 1982. *Ross* v. City of Berkeley, No. C-85-7321-MHP, slip op. at 23 (N.D. Cal. June 11, 1987) (order denying motions for reconsideration). Defendant argued that enactment of the Elmwood ordinance put all potential lessors in Berkeley on notice that they would be contracting with their lessees subject to further regulation of commercial evictions. *Id.* at 23-24. The court did not reach the merits of this argument. Instead, it limited the application of its opinion to contracts formed prior to 1982, on the grounds that the only lease it had before it (the Espresso Roma lease) was executed in 1981, before the Elmwood controls were enacted. *Id.* at 24.
arbitration provisions—was left intact. And when the City Council amended the ordinance to provide for owner-occupancy evictions, which it did subsequent to the Ross decision, the eviction section presumably met the district court’s test for constitutionality. As discussed in the following Section, however, the ordinance survived the court battle only to perish in the California Legislature. The Ross decision and ensuing statewide legislation preempting commercial rent control now represent significant departures from the traditional approach of yielding to local control over land use decisions.

IV
THE LEGISLATIVE ATTACK: A STATEWIDE BAN ON COMMERCIAL RENT REGULATION

In September 1987, the California Legislature, by an overwhelming majority, adopted legislation (popularly referred to as the Keene bill) that sealed the fate of commercial rent regulation in the state.\footnote{The Costa-Keene-Seymour Commercial Property Investment Act of 1987, 1987 Cal. Stat. ch. 824, § 2 (codified at Cal. Civ. Code §§ 1954.25-.31 (West Supp. 1988)).} In essence, the Legislature barred local governments from enacting or enforcing \textit{any} type of rent or eviction controls, including mandatory arbitration and mediation, on commercial property. During the preceding six months, the Legislature had debated the wisdom of commercial rent regulation, including whether such regulation was of sufficient state concern to warrant statewide legislation.\footnote{See infra notes 159-66 and accompanying text.} This Section summarizes the legislative history of the Keene bill, its major provisions, and its implications for preservation of neighborhood shopping districts.

A. The Losing Fight

The Keene bill\footnote{The Costa-Keene-Seymour Commercial Property Investment Act of 1987 was sponsored in the Senate by Senator Barry Keene as S.B. 692 and in the Assembly by Assemblymember Jim Costa as A.B.- 1020. The Senate approved the bill by a 24-8 vote, and the Assembly passed it by a vote of 50-15. Hoge, Commercial Rent Control Dies, Daily Californian, Sept. 1, 1987, at 1, col. 1; State Senate votes to ban commercial rent control, Oakland Tribune, June 23, 1987, at B-1, col. 4.} was sponsored by the California Commercial Council,\footnote{Besides the California Commercial Council, the bill was supported by the California Association of Realtors, the California Chamber of Commerce, the Building Owners and Man-} and endorsed by a long list of real estate groups and developers.\footnote{157. Besides the California Commercial Council, the bill was supported by the California Association of Realtors, the California Chamber of Commerce, the Building Owners and Man-} Berkeley was the only city directly affected when the law took
effect on January 1, 1988, because it was the only community in the state ever to regulate commercial rents.

The hearings on the bill were acrimonious. The debate focused largely on two issues: whether commercial rent regulation was a matter of statewide concern or an issue to be left to local control and whether the bill should preempt only local rent controls or, more broadly, any local or state controls on the rental of commercial property, such as mandatory arbitration and mediation programs.

Proponents of the bill argued that rent controls could deter investment in, and improvement of, commercial property and create a bad business climate statewide. Opponents of the bill, including the City of Berkeley, argued that the bill would intrude upon the traditional authority of local governments over land use regulation and would preempt local efforts to preserve the character and quality of

agers Association of California, the California League of Savings Institutions, and the California Mortgage Bankers Association. Judiciary Committee Report, supra note 156, at 1.

158. CAL. CIV. CODE § 1954.27(a) (West Supp. 1988).

159. The tone of the hearings was captured by Gil Ferguson, an Orange County legislator, "who would hold up a drawing of a hammer and sickle whenever Berkeley city officials got up to speak." Rauber, *One Cappuccino Place to Go*, East Bay Express, Aug. 28, 1987, at 23, col. 5.

160. Under the "municipal affairs" provision of the state constitution, a subject must be one of statewide concern before the Legislature can preempt the area. CAL. CONST. art. XI, § 5. The constitution also gives charter cities, such as Berkeley, the power to make and enforce regulations in respect to municipal affairs, subject only to restrictions in their charters. Id. § 5(a). Local regulation of municipal affairs supersedes all inconsistent state law, but in areas not deemed municipal affairs, charter cities are subject to general laws. Id. Thus, when local and state regulations conflict, a finding that a matter is of statewide concern means that state law will prevail and, by definition, the matter is not a municipal affair. See Sato, *Municipal Affairs in California*, 60 CALIF. L. REV. 1055, 1072-73 (1972).

An attack on the constitutionality of the Keene bill was brought in Alameda County Superior Court. That action, filed by the Espresso Roma tenants, alleged that the Keene bill violates the municipal affairs doctrine on two grounds. The first was that the state did not act affirmatively to occupy the legislative field. Their second argument was that the Keene law contained no suggestion of any legislative intent to bar local restrictions on commercial evictions and only purported to outlaw rent regulations. See Boot, *Officials File Suit to Overturn State Law Barring Rent Control*, Daily Californian, Jan. 21, 1988, at 1, col. 3. This argument did not survive a demurrer at the superior court level. Ross v. Espresso Roma Corp., Order No. 634 208-3 (Alameda Super. Ct. Feb. 19, 1988). Because the tenants settled, they did not appeal this issue. Interview with Don Jelinek, attorney for Espresso Roma tenants (May 3, 1988).


162. See, e.g., id. at 5. Some went further in remarking on the bill. Assemblyman Charles Bader, for example, angrily told a delegation of commercial rent regulation supporters that "[s]uch controls are ludicrous and absolutely asinine." Meibert, *Berkeley Bid Fails on Commercial Rent Control*, Oakland Tribune, July 14, 1987, at B-1, col. 2.

163. Other opponents of the bill included the League of California Cities, the New Berkeley Chamber of Commerce, the City and County of San Francisco, and several other California cities, including Oakland, Santa Monica, and West Hollywood. Judiciary Committee Report, supra note 156, at 1.
COMMERCIAL RENT REGULATION

When it became clear that the Legislature was intent on preempting rent controls on commercial property, opponents of the bill turned their attention to limiting the scope of the legislation to permit mandatory arbitration and mediation programs. Proponents of the bill argued that such programs operate to a landlord's detriment by unilaterally extending the lease. The City of Berkeley, however, contended that its mediation and arbitration program resolved rent disputes without unduly interfering with a landlord's property interests.

The opposition arguments did not receive a sympathetic ear from the Legislature, which ultimately found that "[b]ecause the impact of [commercial real property] controls goes beyond the local boundaries within which the controls are imposed, the adverse economic consequences become [a matter of statewide concern]."

B. The Provisions of the State Law

The purpose of the state statute is to prohibit public entities from enacting or enforcing—after January 1, 1988—any measure constituting commercial rental control. The law defines the term "commercial rental control" to include any governmental controls on the rental rate for the property (thereby prohibiting rent controls) or on the term of the lease (thereby prohibiting "just cause" eviction controls and preempting mandatory arbitration and mediation programs). The statute also preempts local arbitration and mediation programs, whether prior to or after the expiration of a lease. Specifically, it prohibits "any control or system of controls which would select, mandate, dictate or otherwise designate a specific tenant or person with whom the owner must negotiate on the formation, extension or renewal of a tenancy." Thus, the legislation goes much farther than simply prohibiting price controls—it also prevents public entities from enacting or enforcing eviction protections or mandatory arbitration and eviction programs.

Nevertheless, it was equally the intent of the Legislature that nothing in the legislation should diminish other lawful powers of public entities, such as powers under the state planning and zoning laws, the

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164. Id. at 9; Hoge, supra note 155, at 1, col. 1. Although San Francisco and other cities reportedly were considering enacting some sort of commercial controls, the legislation was aimed at Berkeley, the only city in the state actually to have adopted such controls.
165. Judiciary Committee Report, supra note 156, at 3, 10.
166. CAL. CIV. CODE § 1954.25 (West Supp. 1988); see supra note 160.
168. Id. § 1954.26(f).
169. Id.; see Judicial Committee Report, supra note 156, at 5-6.
171. Id. § 1954.30.
172. Id. § 1954.29(a).
police power to abate nuisances, \textsuperscript{173} certain contracted-for controls, \textsuperscript{174} power to regulate residential rents, \textsuperscript{175} and power to mitigate the impact of construction on or alteration of any commercial real property. This limitation, however, does not excuse any actions taken for "the clear or systematic purpose" of circumventing the legislation. \textsuperscript{176} Although the term "clear or systematic" has yet to be construed by the courts, this provision potentially could affect situations far removed from Telegraph Avenue-type commercial rent controls designed to promote local businesses and to preserve the character of a neighborhood. \textsuperscript{177}

1. Permissible Control by Contract or Agreement

Commercial rent controls are permissible if they are the subject of a contract or agreement signed by both the public entity and the developer in consideration for a "direct financial contribution" from the public entity to the developer. \textsuperscript{178} Examples of "direct financial contribution" include land write-downs (discounting the price of the land) and commercial or industrial development bonds. \textsuperscript{179}

Another legal method of imposing commercial rent controls is to include them as a subject of a development agreement. \textsuperscript{180} A development agreement \textsuperscript{181} is a contract between a city or county and a developer that freezes the developer's rights early in the development process. This ensures that the developer may proceed with her project under the laws

\textsuperscript{173} Id. § 1954.28(b).
\textsuperscript{174} Id. § 1954.28(d).
\textsuperscript{175} The Legislature declared its intent that this legislation should not apply or be interpreted to apply to local residential rent controls. Id. § 1954.25. Specifically, the legislation neither enlarges nor diminishes in any way any power of a public entity to regulate the rental rate or the ownership, conveyance, or use of any property used as a dwelling unit, residential hotel, or mobilehome park space or dwelling unit. Id. § 1954.27(b)(6).
\textsuperscript{176} Id. § 1954.29(a).
\textsuperscript{177} Public entities that assess fees against a developer to mitigate the impacts of development of commercial property should pay particular attention to this section of the statute. Consider the following situation. To offset the adverse impact of commercial projects on the availability of existing childcare services, a city routinely issues use permits conditioned on the dedication to childcare of no less than a certain number of square feet of space, to be rented at a rate set to ensure that childcare operators will be able to afford to rent and remain in the space. Moreover, the rental rate can be adjusted no more frequently than annually, and the increase cannot exceed a designated amount. This could be a "clear or systematic" circumvention of the preemptive legislation, even though the purpose of the action is to ensure the viability of childcare facilities and not to protect neighborhood commercial districts.
\textsuperscript{178} CAL. CIV. CODE § 1954.28(d) (West Supp. 1988).
\textsuperscript{179} The City of Berkeley, the League of Cities, and others unsuccessfully lobbied the Legislature to allow "indirect" financial contributions, such as density bonuses, to serve as consideration. Because this amendment was rejected, "indirect" financial contributions are not adequate consideration, leaving this exception to the ban on commercial rent controls quite narrow.
\textsuperscript{180} CAL. CIV. CODE § 1954.28(d) (West Supp. 1988).
existing at the time of the contract. The developer usually obtains such an agreement in exchange for paying specified development mitigation fees to the city or county.

Finally, any written contract between a redevelopment agency and an owner or developer of commercial real property within a redevelopment project area is exempt from the commercial rent legislation.\textsuperscript{182} All of the contracts referred to in this subsection, however, are not enforceable against a person who becomes an owner without actual knowledge of the contract and who became an owner more than thirty days prior to the recording of the contract with the county recorder.\textsuperscript{183}

2. The Notice Provision

The legislation allows public entities to establish a modest requirement that would enable a tenant to obtain notice from the landlord as to the landlord’s intent to renew the lease at the end of the lease term.\textsuperscript{184} If local governments decide to enact such notice requirements, however, they must follow certain guidelines established by the legislation. For instance, a tenant would be required to deliver a negotiation notice—an offer or solicitation of an offer to renew—at least 270 days before the expiration of the lease term.\textsuperscript{185} The landlord then would be required to deliver an impasse notice—a notice that the lease will not be extended or renewed—no later than 180 days before the expiration date.\textsuperscript{186} The delivery of an impasse notice, however, would not preclude further negotiation.\textsuperscript{187}

The purpose of this section of the statute is to permit local notice ordinances while preempting any enactment containing broader provisions.\textsuperscript{188} Thus, the legislation explicitly does not create or impose a duty

\begin{itemize}
\item \textsuperscript{182} Cal. Civ. Code § 1954.28(d) (West Supp. 1988). Thus, the legislation does not preempt a provision of the California Health and Safety Code that requires redevelopers to give special preference to businesses that have been displaced by the redevelopment project. Cal. Health & Safety Code § 33,339.5 (West 1988). See Judiciary Committee Report, supra note 156, at 7 (pointing out that an earlier version of the bill apparently would have preempted this provision of the redevelopment law).
\item \textsuperscript{183} Cal. Civ. Code § 1954.28(d) (West Supp. 1988).
\item \textsuperscript{184} Id. § 1954.30. The City of San Francisco lobbied for a notice provision exception to the bill, but when the bill was passed, the exception that was included was more restrictive than the one proposed by the city. Accordingly, the local ordinance was dropped. Lee interview, supra note 29.
\item \textsuperscript{186} Id. § 1954.31(a)(2).
\item \textsuperscript{187} Id.
\item \textsuperscript{188} The Commercial Leasing Task Force of San Francisco’s Small Business Advisory Commission had proposed a notice ordinance wherein, if a landlord failed to provide notice of his or her intention not to renew a lease by a specified date, the commercial tenancy would be extended beyond the expiration date of the lease by one day for each day the notice was late. Judiciary Committee Report, supra note 156, at 10. The Legislature declined to adopt this proposal and, instead, opted for a notice provision that would not allow for unilateral extension of the lease.
\end{itemize}
to extend a lease or to negotiate an extension of a lease. Additionally, the provision specifically preempts notice statutes that extend any lease without the mutual consent of the parties or that prevent eviction upon expiration of the lease.

C. Impacts of the Legislation

Although there was no evidence that commercial rent control was spreading to other California communities, commercial rent regulations are now banned in all California jurisdictions. The myriad exceptions to the legislation attest to the fact that, although its scope is statewide, it was in fact directed not only at one small area, Telegraph Avenue, but at one parcel of land, the Espresso Roma property. This is not surprising—the main proponents of the legislation were the owners of the Espresso Roma property.

Even if the specter of commercial rent controls was a matter of statewide concern because such controls could depress land values and render commercial property an unattractive investment, mandatory arbitration and eviction programs deserved a chance to succeed. Indeed, in Berkeley, the mediation and arbitration requirement was deemed a great success. Disputes were settled routinely at the informal mediation stage, and no dispute ever reached the point of formal arbitration. The provisions encouraged landlords and merchants to negotiate new leases. Mandatory mediation and arbitration programs were an unworthy target of statewide preemption.

V. THE RESPONSE

On January 1, 1988, all commercial rental controls were lifted in the three protected Berkeley commercial districts. Judging from the number of rent hikes and evictions that have occurred or are expected to occur in the initial period of deregulation, the commercial regulations

190. Id. § 1954.31(c)(1).
191. Id. § 1954.31(c)(3).
192. Of course, nothing in the Keene bill prevents a bilateral agreement to send a dispute to arbitration. Voluntary arbitration, however, is not nearly as successful as the mandatory procedure. For instance, after the statewide legislation came into effect on January 1, 1988, the City of Berkeley and the city’s Chamber of Commerce offered a voluntary arbitration service to those affected by the loss of the rent controls. Although the service was offered free of charge, only three landlords or merchants took part in the program. Interview with Catherine Lew, Aide to Berkeley Mayor Loni Hancock (Feb. 15, 1988).
193. Although the state legislation did not go into effect until January 1, 1988, the Berkeley City Council amended the Telegraph Avenue ordinance on July 28, 1987 (effective August 28, 1987) to allow for owner-occupancy evictions. See supra note 76 and accompanying text. This amendment was taken to conform to the court’s ruling in the Ross case.
194. See infra notes 195-208 and accompanying text.
evidently did serve to stabilize the controlled areas. Because the economic forces that led to the implementation of commercial rent controls remain, alternative responses aimed at preserving small independent businesses must be designed and tested. It is instructive to mention briefly several strategies that have been attempted in Berkeley.

A. The Effects of Commercial Rent Control and Deregulation on Three Commercial Districts

It is evident from the threatened or realized rent increases and evictions and from "going out of business" signs that are appearing in the three Berkeley commercial areas that commercial rent regulations had a significant effect on the character of the areas. The Elmwood district, which had been subject to rent controls for the longest period—since 1982—reflects the loss of its protections to a greater degree than the Telegraph Avenue or West Berkeley districts, which came under rent regulation much later.

In the two-block Elmwood district, most of the businesses face rent increases, in some cases up to two or three times the present rent, and a half dozen or more shops may close immediately as controls disappear. The Elmwood stores threatened by rent increases include the twenty-five-year-old Elmwood Bookshop, the Ivy Shoppe, a women's and children's clothing store, which has operated in Elmwood for more than forty years, and the Mug Shop, a ceramics studio, which moved to a lower rent area of Berkeley after being on College Avenue for twenty-two years.

In West Berkeley, where artists have moved into old warehouses and former industrial plants "only to have to fight off office developers, who follow the artists into reviving neighborhoods—and price them out," the artists have lost their reprieve. Half of the twenty artists in one building are currently facing rent increases. Neighborhood activists are working with a committee of the city Planning Commission to change the master plan for West Berkeley in order to preserve existing artists' warehouses. If artists are forced out before the new plan is writ-

196. Id. at B-4, col. 4. The 62-year-old bookstore proprietor saw his rent double to an unmanageable $980 per month. Id.
197. Id. at B-1, col. 1. The 81-year-old owner of the shop was paying $500 per month in rent for property that arguably could have garnered rent of $2,200 per month in 1982. Id. at B-4, col. 4; see also Boehm, Commercial Rent Hikes Already Forcing Local Business Closures, Daily Californian, Jan. 18, 1988, at 1, col. 2.
198. Stern, supra note 35, at B-1, col. 1. The landlord plans to move a delicatessen into the newly vacant space. Id. at B-4, col. 1.
199. Id. at B-5, col. 2.
200. One tenant already has received notice of a 33% rent hike. Other artists who also are without leases may be subject to similar increases. Id.
ten “it’s more or less the writing on the wall for the demise of arts and crafts and small industry in West Berkeley.”

The changes on Telegraph Avenue mirror those in the Elmwood district. The president of the Telegraph Avenue Merchants’ Association has called the loss of commercial rent controls “disastrous” to the character of the Avenue; he predicts that at least eight merchants in the area soon will go out of business. Vacant storefronts and a high business turnover rate are also predicted, as merchants find that their sales cannot support the high rents. One symbol of the changing face of Telegraph Avenue is the eviction of a family-owned Mexican restaurant, La Villa Hermosa, a landmark whose outside wall sports a mural of the People’s Park battle painted by a community activist and whose inside wall depicts the heroes of Mexico.

Perhaps the greatest irony of the deregulation is that while Telegraph Avenue and the other districts are feeling the effects of the statewide preemption of commercial rent regulations, Espresso Roma, the target of the legislation, continues to be operated by the tenants. Under an out-of-court settlement, the owners will not retake possession until January 1, 1989.

Business closings are still the exception. According to the executive director of the New Berkeley Chamber of Commerce, a group that supported the commercial controls, it is still “business as usual” for most store owners. He estimates that only five percent of merchants protected by the controls will be affected significantly by their demise—some

201. Id.
202. Boehm, supra note 197, at B-1, col. 3.
203. Id.
204. Boot, New Rent Law Allows Local Eatery Eviction, Daily Californian, Jan. 8, 1988, at 1, col. 6. La Villa Hermosa, run by the Castellanos family, was evicted after 13 years of business to enable the landlords to remodel their spacious property. Oakland Tribune, Jan. 8, 1988, at B-1, col. 5.
205. While Senator Keene, the bill’s sponsor, claimed that the bill was not aimed at Berkeley but at its potential imitators (including San Francisco), Berkeley merchants charged that Keene’s bill not only targeted them, but was initiated by and for the financial benefit of Arthur Ross, owner of the Espresso Roma property. Stern, supra note 43, at B-8, cols. 4-5.
206. Although the Ross case was dismissed from federal court in July 1987, the suit continued in state court. The Berkeley City Council, responding to the district court decision, amended the Telegraph Avenue ordinance so that owner occupancy became a just cause for eviction, allowing the Rosses to pursue an unlawful detainer action in state court. The tenants countered that the property owners breached an oral contract promising compensation for the time and energy the tenants spent establishing the cafe’s “goodwill”—its reputation, clientele, and popularity. See Boehm, Jury Takes Coffee Break In Espresso Roma Trial, Daily Californian, Mar. 23, 1988, at 3, col. 1; see also Boehm, Judge Declares Mistrial In Suit Over Roma Cafe, Daily Californian, Mar. 25, 1988, at 1, col. 5 (fair resolution difficult because of “highly sensitive” nature of dispute). After the state court battle ended in a mistrial, the parties agreed to an out-of-court settlement. Under the settlement, the Rosses will take control of their property on January 1, 1989. Boehm, Cafe Roma Owners to Relinquish Property, Daily Californian, May 25, 1988, at 2, col. 4.
207. Boehm, supra note 197, at 2, col. 5.
merchants simply will have to move their businesses “down the street.”

B. The Problem of Legitimate Goals

The legitimacy of commercial rental controls depends in large part on whether the goals to be achieved through their application are justifiable. In Berkeley's case, the legitimacy of its commercial rental controls must be tested by facing the question of whether quaint, family operated or locally owned stores—Ozzie's Fountain, the Ivy Shoppe, La Villa Hermosa—should be preserved through the aid of commercial rent controls or some other means, such as use quotas, when they cannot be sustained by the market. In other words, are there sound reasons to preserve businesses other than the fact that they can pay market rents? This question has no easy answer because it addresses an area that is filled with tensions and tradeoffs. Although it is impossible to determine which values should prevail in every situation, the tradeoffs should be made explicit in order to address the tensions. Competing forces include preserving the tradition and character of the neighborhood as opposed to fostering change, expressing concern for displaced merchants and inconvenienced neighbors versus securing the rights of property owners to use their property or to obtain its highest rental value, allocating the burden of preserving neighborhood businesses to landlords rather than to the greater public, and favoring locally owned businesses over nonlocal businesses.

Berkeley has a strong economic market caused, in part, by the limited amount of land zoned for commercial uses and the increasing affluence of the city’s residents. Consequently, commercial rents are soaring in many areas of Berkeley. Although some owners and tenants believe that lifting of commercial rental controls will change the distinctive character of the areas, many believe that in the long run supply and demand should set commercial rents: "Businesses that can't compete in the..."
marketplace should be in museums, not subsidized by artificially low rents.'”

On the other hand, though commercial rental controls may seem “anti-business,” in Berkeley the controls were initiated by local merchants and community members as a way to keep chain stores and franchises—the stores most able to pay uncontrolled rents—from locking local entrepreneurs out of the local market. Multilocation businesses make money by catering to a large market, whereas small businesses generally must develop a special niche in the local market. The range of goods and services that are provided by small businesses may strengthen a local economy and lead to the desired diversity in an area. These businesses, however, are the most vulnerable to changing economic conditions and slow periods.

The Elmwood controls may have exacted too high a price from landlords in keeping nonviable businesses alive. The mediation and arbitration provisions of the Telegraph Avenue and West Berkeley ordinances, however, provided more balanced regulation of the landlord-tenant relationship. By requiring that landlords sit down with tenants to negotiate new rent levels and lease terms, the mediation and arbitration provisions preserved the landlord's right to obtain a reasonable rent while giving locally oriented businesses a chance to survive.

Perhaps the “successful little neighborhood business” is largely a thing of the past, at least in “hot” commercial markets in rapidly changing areas. If this is true, the problem merits attention from those who live in, shop in, and plan for such communities. Members of these communities should have a say in directing the change. This does not mean that change should be stopped; rather, government should provide citizens, merchants, and property owners with opportunities for guiding change. Perhaps the most unfortunate aspect of the Keene bill is that it preempted one solution and failed to provide alternatives to address a growing urban problem.

shop, whose rent increased from $400 to $1500 per month, acknowledged that although he does not relish the rent increase, the new rent is realistic. Id. The rent hikes, however, will cause Elmwood to lose its neighborhood feel. He continued, “I'm afraid we'll see places like Mrs. Field's Cookies and La Petite Boulangerie—high turnover businesses. It will probably get ugly.’” Id. at col. 4.

211. Stern, supra note 43, at B-8, col. 4. “'They've got a quaint soda fountain like Ozzie's at Disneyland,'” said a lobbyist for the California Association of Realtors and the California Commercial Council. Id.

212. See Daily Californian, Apr. 9, 1987, at 4, col. 1 (editorial in support of commercial rent control).

213. See Defendant's Opposition Brief, supra note 49, at 6-7.

214. See supra note 209.

215. The success of the Keene bill may be attributed, at least in part, to the prevailing view that businesses must function within market strictures. This principle, however, has numerous exceptions in the form of tax credits, worker safety regulations, and pollution control laws. The issue, then, is when exceptions or limits to this “principle” should be recognized.
C. Alternatives

Although it is widely conceded that commercial rent controls provide the strongest protection for small businesses, several strategies have been suggested either to slow the initial impact of deregulation or to provide long-term protections for neighborhood businesses.\footnote{216}{A New York City realtor, concerned that commercial rent stabilization would spread to his city, offered several alternatives to commercial rent control, including "rezoning Manhattan; requiring all new residential buildings to set aside a certain amount of square footage for commercial usage; and mediation by local real estate boards." R. Rosenberg, \textit{You Can't Afford to Ignore Commercial Rent Controls}, \textit{REAL ESTATE TODAY}, at 36, col. 3 (June 1984).}

Berkeley city officials and the city's Chamber of Commerce developed a plan to help merchants survive the initial period after rent control.\footnote{217}{Boehm, \textit{City to Offer Rental Advice to Merchants}, Daily Californian, Dec. 1, 1987, at 1, col. 1.} The plan offers free tenant-landlord mediation services, free listing of available commercial properties and brokers for tenants who need to relocate, and free training to help business owners negotiate mediation provisions into their new leases.\footnote{218}{Id.} This plan is limited, however, because it does not require that landlords participate in mediation. In thriving markets, most landlords probably will be unwilling to enter mediation voluntarily.\footnote{219}{As evidence that voluntary arbitration is of limited practical value, only three tenants and no landlords have asked for mediation services. \textit{See supra} note 192.}

The unique nature of Telegraph Avenue and other commercial areas may be preserved in part through use quota zoning. Quota zoning limits the number and type of uses in an area.\footnote{220}{See Comment, \textit{supra} note 5. Quota zoning, however, is not coupled with eviction protections. A particular use might be preserved, but ownership is not secured. For this reason, quota zoning is not as effective as commercial rent control in preserving a neighborhood's character.} The Berkeley City Council recently amended the city's zoning ordinance to provide for quota zoning in the Telegraph Avenue commercial district.\footnote{221}{Berkeley, Cal., Ordinance 3018-N.S. (June 21, 1988); \textit{see} Berkeley Planning Dep't, Memorandum to Planning Commission on Telegraph Area Commercial Zoning—Reclassification of Properties from C-1 to C-1(7) District (July 22, 1988) [hereinafter Memorandum to Planning Commission II]. The City Council acted on the recommendation of a Berkeley City Planning Commission subcommittee, which is comprised of merchants, residents, and city officials. Memorandum to Planning Commission I, \textit{supra} note 3; \textit{see also} Boehm, \textit{Telegraph Avenue Plan May Aid Small Businesses}, Daily Californian, Jan. 22, 1988, at 1, col. 3-4. The ordinance was subject to review by several city commissions, including the Board of Adjustments (Berkeley’s board of zoning appeals), the Transportation Commission, and the Planning Commission. In addition, several public hearings were held before the City Council took action on the measure. Boehm, \textit{supra}, at 4, col. 4; \textit{see Memorandum to Planning Commission II, supra}, at 1-2.} The ordinance, which
resembles a conventional zoning ordinance except that it specifies the maximum number of each permissible type of business, limits the number of fast food restaurants to eighteen, cafes and coffee houses to ten, and barber or beauty shops to six. It permits only five novelty shops in the area and limits the number of “dessert establishments,” including stores that sell ice cream, frozen yogurt, cookies, candy, and other sweets. Use quotas, which were instituted in the Elmwood district prior to commercial rent control, probably will provide diversity in the Telegraph Avenue Commercial District, even if they do not preserve existing businesses. With the demise of commercial rent controls, quota zoning—despite its shortcomings—is perhaps the most effective means to preserve diverse neighborhood uses.

CONCLUSION

As urban living becomes desirable again for the affluent in our society and as urban rents soar concomitantly, the character of many neighborhood commercial districts is threatened. Although it can be argued that businesses that cannot survive in a changing market should not be sustained artificially, the disappearance of independent, community-serving businesses from neighborhood commercial districts should not be ignored. In addition to the aesthetic quality of many neighborhood shopping districts, such districts are valuable because their local

222. Berkeley, Cal., Ordinance 3018-N.S. § 9G.4(g), (h), (j).
223. Id. § 9G.4(f). This quota applies to “retail stores wherein over 50% of its stock consists of miscellaneous and unrelated non-essential items intended mainly for household adornment or for personal adornment or pleasure.” Id.
224. The total number of dessert establishments “shall not exceed thirteen.” Id. § 9G.4(i).
225. The question does arise, however, whether use quotas, implemented to preserve diversity, instead will eliminate innovative and creative uses. See Memorandum to Planning Commission I, supra note 3, at 2.
226. Specific plans are another technique suggested to preserve the character of neighborhood commercial areas. In California, city planners and developers develop specific plans as a bridge between the local general plan and individual development proposals. Specific plans include both planning policies and regulations for the particular area. Specific plans also must show existing and proposed land uses by parcel, making them useful tools for guiding the development and redevelopment of neighborhood commercial areas. See Cal. Gov’t Code §§ 65,450-65,553 (West 1988). See generally Cal. Office of Planning and Research, Specific Plans: How Some Communities Use Them (1981).
merchants traditionally have offered neighborhood residents essential goods and services.

In Berkeley, local merchants, neighborhood activists, and city officials attempted to protect the character and diversity of three commercial areas through the innovative use of mandatory mediation and arbitration and eviction controls. Although California localities are now prohibited from enacting such controls, Berkeley's experiment may suggest possible courses of action to other communities who are concerned with protecting the diversity of commercial uses and providing stability to existing businesses in periods of escalating commercial rents. Land use law is no longer restricted to "Euclidian" zoning; it should be explored to its limits to preserve important resources, including neighborhood commercial districts.

227. See supra note 89.