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# Regulatory Takings and the Constitutionality of Commercial Rent Regulation in New York City

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# NOTE

## REGULATORY TAKINGS AND THE CONSTITUTIONALITY OF COMMERCIAL RENT REGULATION IN NEW YORK CITY

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† Cornell Law School, J.D. Candidate 2019; New York University, B.A. 2015. Thank you to the magnificent staff and friends on the *Cornell Law Review*, without whom this Note could never have come to fruition. Special thank you to Professors Kevin M. Clermont and Robert C. Hockett for making my time at Cornell so unforgettable and intellectually rewarding. Finally, enormous thanks to Dean Eduardo M. Peñalver for challenging me and generously taking the time to discuss this Note together.

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## INTRODUCTION

In recent years, the plight of small businesses in New York City has become a contentious topic. Although the city and its current mayoral administration share a long-standing commitment to affordable housing,<sup>1</sup> the city's small businesses—an integral and defining feature of the urban landscape—have suffered immensely. In the past decade, local establishments have largely given way to a homogenous landscape of empty storefronts and national chain stores.<sup>2</sup> The loss of local business occurs with such staggering frequency that there is an entire thriving blog subculture documenting their “vanishing”<sup>3</sup> and the Center for an Urban Future publishes an annual report on the growth of chain businesses in the city.<sup>4</sup> Pro-development advocates assert that this “vanishing” merely

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<sup>1</sup> It is worth noting that the success of this commitment is open to debate. Compare William Neuman, *De Blasio Says City Will Hit Affordable-Housing Goal 2 Years Early*, N.Y. TIMES (Oct. 24, 2017), <https://www.nytimes.com/2017/10/24/nyregion/de-blasio-affordable-housing-goal-2-years-early.html> [https://perma.cc/K8V3-L2LG] (reporting that the de Blasio administration would meet its goal of creating or preserving 200,000 units of affordable housing by 2024 two years early, in 2022), with J. David Goodman, *De Blasio Expands Affordable Housing, but Results Aren't Always Visible*, N.Y. TIMES (Oct. 5, 2017), <https://www.nytimes.com/2017/10/05/nyregion/de-blasio-affordable-housing-new-york-city.html> [http://perma.cc/JE49-3BRU] (explaining that many beneficiaries of the Mayor's affordable housing plan are angry with the extensive rezoning the city promoted to build new housing, and do not feel that their apartments are indeed “affordable,” despite qualifying as such under the Mayor's plan). Even if the apartments are adequately affordable for residents, the demand for them vastly overshadows the supply. Cf. Goodman (noting that the city held lotteries for approximately 5,000 apartments in 2017, but that tens of thousands of residents apply for such apartments).

<sup>2</sup> See Christian González-Rivera, Ctr. for an Urban Future, STATE OF THE CHAINS (2017) [hereinafter STATE OF THE CHAINS], [https://nycfuture.org/pdf/CUF\\_StateOfChains\\_2017.pdf](https://nycfuture.org/pdf/CUF_StateOfChains_2017.pdf) [https://perma.cc/RA5L-WA96].

<sup>3</sup> See, e.g., JEREMIAH'S VANISHING N.Y.C., <http://vanishingnewyork.blogspot.com/> [http://perma.cc/FXG2-39QR] (extensively documenting and lamenting the disappearance of small businesses in New York). Jeremiah Moss, the owner of the blog, recently published a book on the same topic, which *The New York Times* describes as “chronic[ing] how (and why) a city of diners and delis morphed into a string of interchangeable blocks filled with forgettable stores of the sort that could be found in a Long Island strip mall.” Ronda Kaysen, *A Book from a Blogger About Disappearing New York*, N.Y. TIMES (Aug. 11, 2017), <https://www.nytimes.com/2017/08/11/realestate/a-book-from-a-blogger-about-disappearing-new-york.html> [http://perma.cc/V7T5-S2YB]; see also EV GRIEVE, <http://ev-grieve.com/> [http://perma.cc/QZ7F-MHJ2] (local news blog from Manhattan's East Village documenting, among other events, the closure of small businesses). See STATE OF THE CHAINS, *supra* note 2.

represents a sort of creative destruction that the city naturally experiences.<sup>5</sup> However, critics point out that most of these businesses were perfectly viable—even thriving—but were pushed out by a local commercial law regime that favors large landlords and strips small commercial tenants of all bargaining power.<sup>6</sup> This imbalance, they suggest, is what results in commercial rents that can increase close to ten-fold when it comes time to renew leases.<sup>7</sup>

In response to this perceived injustice, small business advocates have proposed the Small Business Jobs Survival Act (SBJSA) in the New York City Council.<sup>8</sup> The Act proposes various protective measures and seeks to increase small commercial tenant bargaining power.<sup>9</sup> However, the bill's current incarnation languished at the committee stage until October 2018, when it finally received its first hearing.<sup>10</sup> A primary reason for the near decade-long inability of the bill to make it to hearings—and the current uncertainty as to whether it will make it to a vote—in City Council is the position, held by some council members and real-estate advocates, that the proposed

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<sup>5</sup> See Brad Hoylman, *Our Community Cannot Afford the Cost of 'High-Rent Blight,'* CHELSEA NOW (July 5, 2017), <http://chelseanow.com/2017/07/our-community-cannot-afford-the-cost-of-high-rent-blight/> [http://perma.cc/FZG9-QJ9U].

<sup>6</sup> See Max Rivlin-Nadler, *Law that Would Help NYC from Being Strangled by Chain Stores Is Deserted by City Council,* VILLAGE VOICE (Sept. 30, 2016), <https://www.villagevoice.com/2016/09/30/law-that-would-help-nyc-from-being-strangled-by-chain-stores-is-deserted-by-city-council/> [http://perma.cc/D2U2-K5AX].

<sup>7</sup> See, e.g., Steven Kurutz, *Bleecker Street's Swerve from Luxe Shops to Vacant Stores,* N.Y. TIMES (May 31, 2017), <https://www.nytimes.com/2017/05/31/fashion/bleecker-street-shopping-empty-storefronts.html?mcubz=1> [http://perma.cc/XD8U-D9T5] (noting that, in 2008, rent for a unit on Bleecker Street skyrocketed from \$7,000 per month to \$45,000 per month as soon as the tenant's lease expired).

<sup>8</sup> See *SBJSA*, TAKE BACK NYC (2015), <http://takebacknyc.nyc/sbjasa/> [https://perma.cc/XG58-FB7B].

<sup>9</sup> See Small Bus. Cong., *The Small Business Jobs Survival Act*, SAVE NYC JOBS, <https://www.savenycjobs.com/jobs-survival-act> [http://perma.cc/KVH8-SSRA] (proposing legislation to empower small businesses in the city and combat their decline).

<sup>10</sup> See Jenny Dubnau, *Why New York Needs Commercial Rent Control*, METROPOLITAN COUNCIL ON HOUSING (Sept. 2015), [http://metcouncilonhousing.org/news\\_and\\_issues/tenant\\_newspaper/2015/september/why\\_new\\_york\\_needs\\_commercial\\_rent\\_control](http://metcouncilonhousing.org/news_and_issues/tenant_newspaper/2015/september/why_new_york_needs_commercial_rent_control) [http://perma.cc/A97B-LMAQ]; see also Tanay Warerkar, *City Council Debates Small-Biz Bill at Heated Hearing*, CURBED NY (Oct. 23, 2018, 9:11 AM), <https://ny.curbed.com/2018/10/23/18013348/small-business-jobs-survival-act-mom-pop-nyc-council> [https://perma.cc/5RXS-RFA7]. It is worth noting that various versions of the SBJSA have been floating around City Council since the 1980s. Needless to say, no version of the bill made it to the floor of City Council for a vote, despite what is at times widespread support. See *infra* Part III.

legislation is unconstitutional.<sup>11</sup> However, public debate on the bill and related measures has reemerged in the recent mayoral election and its aftermath.<sup>12</sup>

This Note surveys the current status of small businesses and commercial tenant law in New York City and discusses whether or not the SBJSA and commercial rent control are constitutional in light of current regulatory takings jurisprudence. Part I surveys the history of land use regulations in the city, the introduction of residential rent control, and the city's brief flirtation with commercial rent control in the mid-20th century. Part II explains the decline and current state of small businesses and the commercial law regime in the city, including the SBJSA proposal. Part III describes the origins and current state of regulatory takings law in light of the Supreme Court's 2017 decision in *Murr v. Wisconsin*. Part IV evaluates whether the SBJSA is constitutional in light of that recent takings jurisprudence. Finally, this Note concludes that the SBJSA would constitute a regulatory taking when it comes to commercial spaces that are free-standing or under separate ownership from the residential units above them in mixed-use structures. However, when a commercial space in a mixed-use building is under the same ownership as the residential units in that building, then the SBJSA would not constitute a regulatory taking. This appears to be a paradoxical result, but it is one that is nonetheless grounded in current regulatory takings law. Ultimately, the possibility of the municipal government having to provide compensation to even some commercial landlords for regulatory takings would likely render the SBJSA impracticable and prohibitively costly. Therefore, this Note recommends that City Council and small-business advocates seek other avenues to curb the decimation of small business in

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<sup>11</sup> Cf. Abigail Savitch-Lew, *Trepidation Around Proposal for Regulating Store Rents in NYC*, CITYLIMITS.ORG (June 13, 2016), <https://citylimits.org/2016/06/13/trepidation-around-proposal-for-regulating-store-rents-in-nyc/> [<http://perma.cc/6RAL-3HKJ>] (quoting a local real estate advocate, John Banks, as referring to the SBJSA as unconstitutional).

<sup>12</sup> See, e.g., David Cruz, *Fiery Debate for 14th Council District Seat Addresses Past and Present*, NORWOOD NEWS (Aug. 28, 2017), <http://www.norwoodnews.org/id=24139&story=fiery-debate-for-14th-council-district-seat-addresses-past-and-present/> [<http://perma.cc/5MMD-EYW2>] (documenting a heated debate over the SBJSA between candidates for a City Council district in the Bronx in the lead-up to the 2017 municipal elections); see also, e.g., Ed Litvak, *(Voter Guide) Mary Silver – City Council District 2*, LO-DOWN (Sept. 5, 2017, 7:54 AM), <http://www.thelodownny.com/leslog/2017/09/voter-guide-mary-silver-city-council-district-2.html> [<http://perma.cc/FN3H-KCWQ>] (explaining the pro-SBJSA position of a candidate for the City Council district encompassing Murray Hill in Manhattan).

the city. This conclusion has implications far beyond New York City, affecting any municipality that wishes to introduce commercial rent regulation.

## I

### HISTORICAL BACKGROUND

#### A. History of Land Use Regulations in New York City

The earliest years of New York City were defined by dense, mixed-use residential development below Wall Street. However, beyond the small community on the southern tip of Manhattan, most of the island was sprawling, meandering farm land with no apparent order.<sup>13</sup> Manhattan and its surrounding locales, today's boroughs, mostly remained this way until the introduction of the Commissioner's Plan of 1811. The plan imposed the grid system upon the entire island, opening pathways to development and presaging the city's colossal growth in the coming century.<sup>14</sup> Indeed, in 1810, a year before the Commissioner's Plan was enacted, the city's population was 96,373.<sup>15</sup> By 1920, following decades of heavy immigration, the city's population was 5,620,048.<sup>16</sup> Naturally, the previously bucolic farmland north of Wall Street gave way to large-scale development to accommodate the teeming masses of the new metropolis. But despite the guiding hand of the grid system, the new development was unruly. The absence of a comprehensive zoning scheme resulted in crowded, smoggy neighborhoods comprising residential, commercial, and industrial developments in close proximity to one another.<sup>17</sup> Further, as buildings were able to grow ever-higher with the

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<sup>13</sup> See Jessica Dailey, *When Wall Street Was a Wall: A 1660 Map of Manhattan*, CURBED N.Y. (May 6, 2013, 11:50 AM), <https://ny.curbed.com/2013/5/6/10246784/when-wall-street-was-a-wall-a-1660-map-of-manhattan> [http://perma.cc/5Y6D-U8ZX].

<sup>14</sup> See Artis Q. Wright, *Designing the City of New York: The Commissioners' Plan of 1811*, N.Y.C PUBLIC LIBR. (July 30, 2010), <https://www.nypl.org/blog/2010/07/30/designing-city-new-york-commissioners-plan-1811> [http://perma.cc/M8X7-Y847].

<sup>15</sup> N.Y.C. Dep't of City Planning, *Total and Foreign-Born Population: New York City, 1790–2000*, CITY OF N.Y. [https://www1.nyc.gov/assets/planning/download/pdf/data-maps/nyc-population/historical-population/1790-2000\\_nyc\\_total\\_foreign\\_birth.pdf](https://www1.nyc.gov/assets/planning/download/pdf/data-maps/nyc-population/historical-population/1790-2000_nyc_total_foreign_birth.pdf) [http://perma.cc/WD5S-VEDV].

<sup>16</sup> *Id.*

<sup>17</sup> See, e.g., Kelly Richman-Abdou, *Jacob Riis: The Photographer Who Showed "How the Other Half Lives" in 1890s NYC*, MASHABLE (May 21, 2017), <https://mymodernmet.com/jacob-riis-how-the-other-half-lives/> [https://perma.cc/R53Z-2SCB] (describing and showcasing the work of Jacob Riis, pioneering photojournalist and muckraker whose work documented the squalor of Manhattan's Lower East Side in the 1890s).

introduction of the steel-frame building and skyscraper, many streets became drowned in darkness.<sup>18</sup>

It was in response to these concerns that the nation's first comprehensive municipal zoning code was created: New York's 1916 Zoning Resolution.<sup>19</sup> The 1916 resolution regulated the height and size of new construction and established a separation of residential and industrial areas.<sup>20</sup> As zoning caught on nationally, it faced numerous legal challenges; however, the Supreme Court ultimately upheld the constitutionality of zoning regulations in *Village of Euclid v. Amber Realty Co.*<sup>21</sup>

## B. Modern Era

In the years after *Euclid*, the city and New York State began to experiment with more expansive regulation of real estate. In fact, the city had a commercial rent control law that was enacted by the state in 1945 in response to wartime pressures.<sup>22</sup> As a recent article on the debate over commercial rent control explains:

In 1945, responding to the wartime emergency that had spurred skyrocketing rents and eviction rates, the New York State legislature enacted a law that limited when a commercial tenant could be evicted and instituted restrictions on rent increases. Landlords could not raise rents by more than 15 percent above 1943 or 1944 rent levels if it would lead to a profit of more than 8 percent. The law was challenged repeatedly in the courts, and ultimately the legislature allowed it to expire in 1963.<sup>23</sup>

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<sup>18</sup> See Lisa Santoro, *The Equitable Building and the Birth of NYC Zoning Law*, CURBED N.Y. (Mar. 15, 2013, 12:37 PM), <https://ny.curbed.com/2013/3/15/10263912/the-equitable-building-and-the-birth-of-nyc-zoning-law> [http://perma.cc/5THU-65KD] (describing the construction of the massive Equitable Building in Lower Manhattan). The design and construction of the steel-frame structure was entirely unregulated and, at the time of completion, it was the largest office building in the world; the public backlash against the structure was a major impetus in introducing the nation's first comprehensive zoning plan in New York. *Id.*

<sup>19</sup> See *id.*; N.Y.C. DEP'T OF CITY PLANNING, *Zoning Background*, CITY OF N.Y. <https://www1.nyc.gov/site/planning/zoning/background.page> [http://perma.cc/Y4KM-JZHJ].

<sup>20</sup> Bd. of Estimate and Apportionment, *1916 Building Zone Resolution*, CITY OF N.Y. (last updated Mar. 2004), <https://www1.nyc.gov/assets/planning/download/pdf/about/city-planning-history/zr1916.pdf> [http://perma.cc/7TKD-S54R].

<sup>21</sup> See 272 U.S. 365, 395, 397 (1926) (holding that zoning ordinances are constitutional exercises of state police power as long as they bear a rational relation to the health, safety, and general welfare of the community).

<sup>22</sup> See Dubnau, *supra* note 10.

<sup>23</sup> Savitch-Lew, *supra* note 11.

Thus the concept of commercial rent control is not entirely foreign to New York City. The debate on commercial rent control was rekindled in the 1980s, when early forms of the SBJSA emerged; however, it was not until recently, when the survival of its small businesses was in serious jeopardy, that the city revisited the idea of commercial rent regulation in earnest.<sup>24</sup>

## II

### THE DECLINE OF SMALL BUSINESS AND THE SEARCH FOR AN EXPLANATION

#### A. Vanishing Mom and Pop

In an editorial published on November 19, 2017, the editorial board of *The New York Times* pointed to the “scourge of store closings that afflicts one section of the city after another.”<sup>25</sup> Something strange appears to be happening in New York: a metropolis that was once a city of neighborhoods, each containing “shops that met most residents’ basic needs, from groceries to shoes, from newspapers to haircuts,” appears to be vanishing.<sup>26</sup> Some commentators seem to suggest that the city changes by nature and people are merely getting frustrated with what they see as the old New York vanishing to yield to the new.<sup>27</sup> Yet the facts are indisputable: New York City’s small businesses have been disappearing with staggering frequency.<sup>28</sup>

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<sup>24</sup> Although the SBJSA’s current incarnation, see *infra* Part III, was the first modern, comprehensive plan introduced in City Council to protect small business through a form of commercial rent regulation, the topic has been debated in city politics for quite some time. See, e.g., *Pro & Con: Should the City Have Commercial Rent Control?; Croissants, Cobblers, and Free-Market Forces*, N.Y. TIMES (July 7, 1985), <http://www.nytimes.com/1985/07/07/weekinreview/pro-con-should-city-have-commercial-rent-control-croissants-cobblers-free-market.html?page-wanted=all&mcubz=1> [<http://perma.cc/B2MR-75AK>] (describing a 1980s, Kochera debate on commercial rent control and pointing to problems facing small businesses, such as “[w]hen the rent on a store triples,” that are only different from today’s problems in degree). For a more in-depth discussion of the problems facing small businesses in the 2010s, see *infra* Part II.

<sup>25</sup> Editorial, *Why Is New York Full of Empty Stores?*, N.Y. TIMES (Nov. 19, 2017), <https://www.nytimes.com/2017/11/19/opinion/nyc-empty-stores.html> [<http://perma.cc/A25T-ZRSD>].

<sup>26</sup> *Id.*

<sup>27</sup> See, e.g., Justin Davidson, *Which New York is Yours? A Fierce Preservationist and a Pro-Development Blogger Debate*, N.Y. MAG.: INTELLIGENCER (May 1, 2015), <http://nymag.com/daily/intelligencer/2015/05/new-york-landmarks-law-debate.html> [<https://perma.cc/FAB2-ZLFJ>] (debate between preservationist Jeremiah Moss of *Jeremiah’s Vanishing New York* and popular pro-development blogger Nikolai Fedak of *New York YIMBY* (Yes in My Back Yard)).

<sup>28</sup> Cf., e.g., Tatiana Schlossberg, *Bodegas Declining in Manhattan as Rents Rise and Chains Grow*, N.Y. TIMES (Aug. 3, 2015), <https://www.nytimes.com/>



The decline in small business has coincided with a massive increase in the amount of commercial storefront vacancies<sup>29</sup> and the amount of chain stores in the city. The Center for an Urban Future's 2017 *State of the Chains* report shows that the city (all five boroughs) had 7,317 national chains in 2017, an increase of 1.8% from the prior year and the ninth consecutive year of net increases in national chain stores throughout the city.<sup>30</sup> Brooklyn, which has been experiencing rapid gentrification, saw a 3.1% increase, the largest increase in any of the five boroughs. As of December 2017, Dunkin' Donuts was the national retailer with the most locations in New York City, maintaining 612 stores.<sup>31</sup> In short, the number of chain stores in New York is growing at an alarming rate. Given that these stores are renting predominantly in pre-existing retail space (rather than in new construction), it means that the spaces they occupy were once home to smaller, long-standing local businesses.<sup>32</sup>

Interestingly, it is not only small businesses in lower-income parts of the city that are hurting; the "vanishing" phenomenon is prevalent in many of the city's ritzier locales, even going so far as to affect some of the larger chains that might

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2015/08/04/nyregion/bodegas-declining-in-manhattan-as-rents-rise-and-chains-grow.html?\_r=2 [http://perma.cc/AR7N-GK2B] (documenting the decline in bodegas in the city).

<sup>29</sup> See Vacant N.Y.C., <http://map.vacantnewyork.com/> [http://perma.cc/L39Y-VX27] (interactive map documenting the vacant storefronts throughout the city).

<sup>30</sup> STATE OF THE CHAINS, *supra* note 2.

<sup>31</sup> *Id.* (noting that this is also the ninth year Dunkin' Donuts topped the list of chains in New York City with the most locations). As of 2017, the chains with the most growth in New York City were food-related, with retailers in that category comprising 41% of New York City's growth in national chain locations in the last decade. It is worth noting that some cities, such as San Francisco, have recognized and attempted to curb the growth of chains that harm local businesses by enacting restrictions on "formula businesses." See generally Mark Bobrowski, *The Regulation of Formula Businesses and the Dormant Commerce Clause Doctrine*, 44 URB. LAW. 227, 233–240 (2012) (providing background on the emergence and purposes of restrictions on formula businesses).

<sup>32</sup> Indeed, in its review of the book *Vanishing New York: How a Great City Lost Its Soul*, the book form of the blog discussed *infra* subpart III.B, *The New York Times* distills Jeremiah Moss's essential claim to be that, "New York, in its current . . . form, is at ease with a disturbingly paradoxical identity, as a place that says yes to every branch of Dunkin' Donuts and no to the people whose fortunes consign them to working there." See Ginia Bellafante, *Tracking the Hyper-Gentrification of New York, One Lost Knish Place at a Time*, N.Y. TIMES (Sept. 27, 2017), [https://www.nytimes.com/2017/09/27/books/review/vanishing-new-york-jeremiah-moss.html?\\_r=0](https://www.nytimes.com/2017/09/27/books/review/vanishing-new-york-jeremiah-moss.html?_r=0) [http://perma.cc/UD8Y-JGTH].

have initially wrought the change.<sup>33</sup> Bleecker Street in the West Village, whose western section was one of Manhattan's most coveted commercial strips, tells a representative tale. On the few western blocks of Bleecker Street, 44 long-standing, small neighborhood businesses have closed since 2001.<sup>34</sup> Bleecker Street was one of the most famous retail streets in Manhattan, renowned for its small, whimsical, and creative shops.<sup>35</sup> As the neighborhood began to gentrify, it became a luxury shopping district where the once-creative shops were replaced by high-fashion designer stores "selling \$400 T-shirts."<sup>36</sup> As Steven Kurutz explains in his article in the *Times* about Bleecker's story:

During its incarnation as a fashion theme park, Bleecker Street hosted no fewer than six Marc Jacobs boutiques on a four-block stretch, including a women's store, a men's store and a Little Marc for high-end children's clothing. Ralph Lauren operated three stores in this leafy, charming area, and Coach had stores at 370 and 372-374 Bleecker. Joining those brands, at various points, were Comptoir des Cotonniers (345 Bleecker Street), Brooks Brothers Black Fleece (351), MM6 by Maison Margiela (363), Juicy Couture (368), Mulberry (387) and Lulu Guinness (394). . . . Today, every one of those clothing and accessories shops is closed.<sup>37</sup>

He further remarks:

In the heart of the former shoppers' paradise—the five-block stretch running from Christopher Street to Bank Street—more than a dozen retail spaces sit empty. Where textured-leather totes and cashmere scarves once beckoned to passers-by, the windows are now covered with brown construction paper, with "For Lease" signs and directives to "Please visit us at our other locations."<sup>38</sup>

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<sup>33</sup> See STATE OF THE CHAINS, *supra* note 2; see also Kurutz, *supra* note 7 (documenting the decline of small business in the West Village, an upscale neighborhood in downtown Manhattan).

<sup>34</sup> BRAD HOYLMAN, BLEAKER ON BLEEKER: A SNAPSHOT OF HIGH-RENT BLIGHT IN GREENWICH VILLAGE AND CHELSEA, [https://www.nysenate.gov/sites/default/files/press-release/attachment/bleaker\\_on\\_bleecker\\_0.pdf](https://www.nysenate.gov/sites/default/files/press-release/attachment/bleaker_on_bleecker_0.pdf) [http://perma.cc/F58T-9AU8] (NY State Senate report documenting the causes and rampancy of small business decline and empty storefronts in downtown Manhattan).

<sup>35</sup> See Kurutz, *supra* note 7 (explaining that Bleecker was once home to many unique small stores, including "antiques stores . . . a pet store called the Bird Jungle; the Biography Bookshop; and Nusraty Afghan Imports, where an immigrant named Abdul Nusraty had been selling rugs, jewelry and antiquities since 1979").

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*

As this phenomenon became noticeable throughout the entire city, people began to ask what was happening—and how it could be fixed.

## B. Reasons for the Decline of Small Business

In looking for explanations for the marked decline in small business in the city, it is common to hear that the retail landscape is simply changing due to online shopping and that these businesses are no longer viable.<sup>39</sup> However, what is surprising about many of the closures is that the shuttered businesses were, in fact, thriving and beloved local institutions—places that anchored their communities. The fact that many of these businesses were financially viable suggests that there must be a different cause for the decline of small business in the city other than the changing retail landscape.<sup>40</sup>

And, indeed, there is another cause: exorbitant rent increases when it comes time for businesses to renew their leases have played a leading role in the decline of small business in New York.<sup>41</sup> As State Senator Brad Hoylman, who represents the district comprising Manhattan's Chelsea neighborhood, explains,

A trend has emerged: landlords, in the pursuit of higher and more reliable rents, don't renew the lease of longtime businesses. They then keep the space vacant, holding out for the payout of a long-term lease from [a] luxury retail or corporate chain, which can take months, or even years. The result is a glut of empty storefronts or chain stores and high-end national retailers, to the detriment of local small businesses.<sup>42</sup>

Thus it is not uncommon to see landlords increase rents ten-fold on otherwise healthy businesses that are simply unable to withstand the increase.<sup>43</sup> Jeremiah Moss has fastidi-

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<sup>39</sup> See *Why Is New York Full of Empty Stores?*, *supra* note 25 (“On one level, there’s just so much the city can do. Online shopping is here to stay, and it takes an inevitable toll on brick-and-mortar stores.”).

<sup>40</sup> For a seminal discussion of the importance of small business in urban communities, see generally JANE JACOBS, *THE DEATH AND LIFE OF GREAT AMERICAN CITIES* (1961).

<sup>41</sup> See Edward Helmore, *New York's Vanishing Shops and Storefronts: 'It's Not Amazon, It's Rent'*, *GUARDIAN* (Dec. 24, 2017, 4:00 PM), <https://www.theguardian.com/business/2017/dec/24/new-york-retail-shops-amazon-rent> [http://perma.cc/M6RW-36BR]; see also *Why Is New York Full of Empty Stores?*, *supra* note 25.

<sup>42</sup> Hoylman, *supra* note 5.

<sup>43</sup> See, e.g., Luis Ferré-Sadurní, *Sunshine Cinema, a Beloved Manhattan Theater, Goes Dark*, *N.Y. TIMES* (Jan. 21, 2018), <https://www.nytimes.com/2018/01/21/nyregion/sunshine-movie-theater-closing.html?smid=TW-nytmetro&smtyp=cur> [http://perma.cc/PJX9-BQGL] (providing a recent example of the closure of a

ously documented the death of beloved local businesses in his popular blog, *Jeremiah's Vanishing New York*.<sup>44</sup> In his decade of maintaining the blog, Moss has documented the closure of thousands of small businesses in New York City, many of which had large and dedicated clienteles but suffered exorbitant rent hikes.<sup>45</sup> As Tim Wu noted in *The New Yorker*:

In the West Village, rent spikes are nearly universally reported as the reason so many storefronts have closed over the past few years. Cafe Angelique reportedly closed when its sixteen-thousand-dollar rent increased to forty-two thousand dollars. A Gray's Papaya [a long-standing local hot dog mini-chain] on Eighth Street closed after its owner reported a rent increase of twenty thousand dollars per month.<sup>46</sup>

Some are beginning to characterize this phenomenon of rampant vacancy as "high-rent blight."<sup>47</sup> In other words, pros-

popular and financially healthy independent movie theater in Manhattan's Lower East Side). The theater was forced to close after its building was sold to a new developer who planned to raise the rent well beyond its previous \$8,000 per month rate at the end of its lease; the theater could easily make its previous rent, but not the increased price. *Id.*

<sup>44</sup> See JEREMIAH'S VANISHING N.Y.C., *supra* note 3.

<sup>45</sup> Particularly noteworthy is Moss's story of the "vanished" Cafe Edison in Manhattan's Theater District. Cafe Edison was a beloved cafe popular with the show-business crowd. See Michael Schulman, *An Activist For New York's Mom-and-Pop Shops*, NEW YORKER (June 26, 2017), <https://www.newyorker.com/magazine/2017/06/26/an-activist-for-new-yorks-mom-and-pop-shops> [http://perma.cc/X559-4EA8]. Moss broke the news that the beloved cafe would be forced to close when its landlord denied it a lease renewal after 34 years in the space. Jeremiah Moss, *Cafe Edison*, JEREMIAH'S VANISHING N.Y.C. (Nov. 6, 2014), <http://vanishingnewyork.blogspot.com/2014/11/cafe-edison.html> [http://perma.cc/U6BD-QKNY]. In a remarkable effort to save the business and demonstrate that the cafe had sufficient support in the community to make its rent, Moss organized a lunch mob with some 600 people, which garnered the express support of Manhattan Borough President Gale Brewer, New York State Senator Brad Hoylman, and Manhattan District 3 Council Member Corey Johnson. The protests received global coverage on NPR and the BBC. The support was not enough to convince the landlord to renew the lease. See Jeremiah Moss, *Cafe Edison is Closing*, JEREMIAH'S VANISHING N.Y.C. (Dec. 16, 2014), <http://vanishingnewyork.blogspot.com/2014/12/cafe-edison-is-closing.html> [http://perma.cc/K3LV-7NGW] (discussing Cafe Edison's dedicated clientele); see also Tim Wu, *Why Are There So Many Shuttered Storefronts in the West Village?*, NEW YORKER (May 24, 2015), <https://www.newyorker.com/business/currency/why-are-there-so-many-shuttered-storefronts-in-the-west-village> [http://perma.cc/XH66-G8FB] (discussing rent hikes).

<sup>46</sup> See Wu, *supra* note 45.

<sup>47</sup> See, e.g., *id.* ("Abandoned storefronts have long been a hallmark of economic depression and high crime rates, but the West Village doesn't have either of those. Instead, what it has are extremely high commercial rents, which cause an effect that is not dissimilar. 'High-rent blight' happens when rising property values, usually understood as a sign of prosperity, start to inflict damage on the city economics that Jane Jacobs wrote about." (referencing Jane Jacobs, famed urbanist and West Village denizen who wrote extensively in the 1960s on the small

perous districts of the city bear the physical hallmarks of “blight” not because they are impoverished, but rather because few, if any, businesses can afford the rent; these neighborhoods are victims of their own ostensible success in attracting astronomically high rents. In the words of the inimitable perennial candidate Jimmy McMillan: “The rent is too damn high.”<sup>48</sup>

### III

#### BIRTH OF THE SMALL BUSINESS JOBS SURVIVAL ACT

##### A. The Act

As the situation for New York’s small businesses becomes increasingly dire, the question of what, if anything, should be done has become a contentious topic, garnering recognition from some of the city’s leadership.<sup>49</sup> It was with this issue in mind that legislators introduced the SBJSA to City Council. The most noteworthy extant proposal to address the crisis of small businesses in the city, the Act “applies to independently owned and operated New York City businesses, with no more

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businesses that made the neighborhood such a success)); *see also, e.g.*, Ilya Marritz, *There Seem to Be a Lot of Empty Storefronts*, WNYC NEWS (Mar. 23, 2017), <http://www.wnyc.org/story/there-seem-be-lot-empty-storefronts-problem/> [<http://perma.cc/KQB8-ZNP5>] (discussing high rent blight in the Manhattan’s East Village and more generally); Alanna Schubach, *Storefront Map: Where Have NYC’s Retail Shops Gone?*, BRICK UNDERGROUND (Mar. 24, 2017), <https://www.brickunderground.com/live/vacant-storefront-nyc> [<http://perma.cc/KM5S-ULQE>] (discussing, with the founder of Vacant New York, the website’s interactive map of empty storefronts and the concept of high-rent blight); Alissa Walker, *Full Bank Accounts, Empty Storefronts: The Economics of High-Rent Blight*, GIZMODO (May 26, 2015, 5:40 PM), <https://gizmodo.com/full-bank-accounts-empty-storefronts-the-economics-of-1706993230> [<http://perma.cc/BHB6-PN2X>] (discussing high-rent blight).

<sup>48</sup> Christian Royer, *Rent Is Too Damn High Party Debate*, YOUTUBE (Oct. 18, 2010), <https://www.youtube.com/watch?v=kcsNbQRU5TI> [<https://perma.cc/UKF8-8QND>].

<sup>49</sup> *See, e.g.*, Sarina Trangle & Ivan Pereira, *Council Speaker Melissa Mark-Viverito Releases Proposals to Bolster Retail Sector*, AMNEWYORK (Dec. 14, 2017, 12:01 AM), <https://www.amny.com/real-estate/mark-viverito-retail-proposals-1.15444258> [<http://perma.cc/68GE-GP3L>] (discussing efforts by the exiting City Council speaker to combat the decimation of small business in the city). For an example of this contentiousness, one need only look to the public outrage over the proposed startup “Bodega,” which sought to “disrupt” the corner bodega business by placing around the city what are essentially glorified vending machines that allow customers to pay using their iPhones. Many members of the public found the name “Bodega” to be offensive in light of the precarious position of small businesses (particularly actual bodegas) in the city’s current commercial climate. *See Emily Nonko, Bodega Owners Don’t Think New Yorkers Will Shop at a Vending Machine Called ‘Bodega,’* VILLAGE VOICE (Sept. 18, 2017), <https://www.villagevoice.com/2017/09/18/bodega-owners-dont-think-new-yorkers-will-shop-at-a-vending-machine-called-bodega/> [<http://perma.cc/4RP8-US6J>].

than 100 employees, where such business is not dominant in its field.”<sup>50</sup> Under the SBJSA, commercial tenants have a guaranteed right of renewal of their 10-year leases, unless the tenant fails to pay rent in a timely manner or engages in another behavior in breach of contract with the landlord.<sup>51</sup> Then:

If the landlord agrees to renew the lease, he and the tenant can negotiate the rent or either party can compel non-binding mediation. If after 90 days of negotiations and/or mediation there is no agreement, the tenant must initiate arbitration in order to retain the right to renew. The arbitrator’s rent determination is binding [unless the tenant refuses to pay that amount in rent] and based on considerations including, the rental market in the area, the condition of the space and services provided, the landlord’s maintenance costs, and the extent to which the business is bound to a particular location.<sup>52</sup>

If the tenant does not agree to the rent determined by the arbitrator, then the tenant can remain in possession of the space at a rent no greater than a 10% increase than the average of the previous year’s rent.<sup>53</sup> If a new prospective tenant approaches the landlord with a bona fide offer, then the original tenant has the right of first refusal and can choose to sign a lease at the rate agreed between the landlord and the prospective bona fide purchaser.<sup>54</sup> In other words, the landlord cannot simply enlist a third party to make an above-market offer solely for the purpose of pushing out the original tenant.

## B. Legislative Attempts to Pass the SBJSA

Although its current iteration is from 2009, the SBJSA has existed in one form or another in City Council since the 1980s.<sup>55</sup> Remarkably, no City Council speaker has ever permitted the Act to make it to the floor of City Council for a vote.<sup>56</sup>

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<sup>50</sup> See Dina Botwinick et al., *Saving Mom and Pop: Zoning and Legislating for Small and Local Business Retention*, 18 J.L. & POL’Y 607, 628–29 (2010) (describing the SBJSA but referring to it as the “Small Business Act”).

<sup>51</sup> See *Creating a Small Business Lease Program*, LEGIS. RES.CTR., <http://legistar.council.nyc.gov/LegislationDetail.aspx?ID=1825175&GUID=AFE9C183-5929-43FB-80AE-C7595CB610BD> [<http://perma.cc/2GSV-GJQ3>] (official version of the bill as introduced in City Council four years ago).

<sup>52</sup> Botwinick et al., *supra* note 50, at 628–29 (footnotes omitted).

<sup>53</sup> See *Creating a Small Business Lease Program*, *supra* note 51 (SBJSA § 22-905(e)(3)(g) as introduced).

<sup>54</sup> See *id.*

<sup>55</sup> See Dennis Lynch, *Oops, They Did It Again! Council Snubs S.B.J.S.A.*, VILLAGER (Oct. 6, 2006), <http://thevillager.com/2016/10/06/oops-they-did-it-again-council-snubs-s-b-j-s-a/> [<http://perma.cc/8GGG-TERF>].

<sup>56</sup> *Id.*

The first hearing on this 2009 iteration took place in October 2018; however, at present, it is uncertain if it will make it to a floor vote, despite what appears to be widespread support.<sup>57</sup>

It is not entirely clear why a bill with widespread support cannot make it to the floor of City Council for a vote, or even why it took so long for a simple hearing. Opponents of the bill in City Council and on the Real Estate Board of New York, a real estate trade association, suggest that it is not within the power of government to impose controls over commercial property leases.<sup>58</sup> Proponents of the bill, on the other hand, take the more cynical view that the City Council is beholden to powerful real estate interests in the city. As Max Rivlin-Nadler for *The Village Voice* argued:

[City Council] won't even allow the legislation to go before a committee hearing, even though 27 councilmembers support it. Why? In short, because it would supremely piss off the powerful real estate interests that all major politicians in New York City must answer to, which makes it a total nonstarter. Debating the Small Business Jobs Survival act would start a conversation about the future of the city that no ambitious politician actually wants to have.<sup>59</sup>

It is for precisely this reason that “the [SBJSA] has become symbolic for its proponents of the Council’s inability—or unwillingness, depending [on] who you ask—to tackle the inequities in commercial tenant-landlord relationships in this city.”<sup>60</sup>

### C. Renewed Calls for the SBJSA

As pointed out in the prior section, the SBJSA has languished since City Council legislators introduced its current iteration in 2009. However, as noted in Part II, the health and status of small businesses in the city have become considerably more precarious in the interim.<sup>61</sup>

Recognition of this fact has led to renewed calls from various municipal leaders and activists for passage of the SBJSA. Debate over the dangers facing small businesses and the ap-

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<sup>57</sup> *Id.* (explaining that the current iteration has “27 sponsors, or one sponsor over the 26-vote halfway mark needed to pass it in the 51-member Council.”); see Warerkar, *supra* note 10 (documenting the October 2018 City Council hearings).

<sup>58</sup> *Id.*

<sup>59</sup> Rivlin-Nadler, *supra* note 6. This article was written before the October 2018 hearing, but the essential point—that some believe City Council is beholden to real estate interests—remains the same.

<sup>60</sup> Lynch, *supra* note 55.

<sup>61</sup> See generally *supra* Part II (explaining the accelerated rate at which small businesses have been disappearing since the bill was introduced in 2009).

propriate solution to those dangers played a role in New York's recent municipal elections.<sup>62</sup> The result of the election has been the empowerment of a municipal government that claims it is progressive and finally granted a hearing on the SBJSA.<sup>63</sup> Whether it will ultimately vote on and pass the bill remains to be seen.

Unsurprisingly, the possibility that the SBJSA will become a reality in City Council is still being met with considerable backlash, with many of the city's real estate interests suggesting that the Act is not only undesirable but also possibly unconstitutional.<sup>64</sup> One of the primary arguments against the SBJSA is that it is a regulatory taking in light of takings jurisprudence.<sup>65</sup> Opponents believe that commercial rent regulations so dramatically diminish the value of a landlord's property that their imposition constitutes a regulatory taking for which landlords must be compensated.<sup>66</sup> The following Parts of this Note examine doctrinal developments in regulatory takings law and their potential implications for the passage of the SBJSA.

#### IV

##### THE LAW OF TAKINGS

###### A. Origin of Regulatory Takings Doctrine, the “Denominator Problem,” and Conceptual Severance

The Fifth Amendment's “Takings Clause” states that, “private property [shall not] be taken for public use, without just

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<sup>62</sup> See, e.g., Cruz, *supra* note 12 (documenting heated debate over SBJSA between City Council candidates in the Bronx); Marni Halasa, *The City Council Must Vote on the S.B.J.S.A.*, VILLAGER (Oct. 19, 2017), <http://thevillager.com/2017/10/19/the-city-council-must-vote-on-the-s-b-j-s-a/> [<http://perma.cc/8APL-SYVV>] (City Council District 3 candidate expressing support for the SBJSA); Litvak, *supra* note 12 (explaining pro-SBJSA position of a city council candidate from Murray Hill); Rich Bockmann, *Majority of City Council Speaker Candidates Back Commercial Rent Control*, REAL DEAL (Nov. 2, 2017, 8:30 AM), <https://therealdeal.com/2017/11/02/majority-of-city-council-speaker-candidates-back-commercial-rent-control/> [<http://perma.cc/5DWA-HEXS>] (noting that six out of eight candidates for Speaker of City Council supported some form of commercial rent control, including the ultimate victor, Corey Johnson).

<sup>63</sup> See, e.g., Warerkar, *supra* note 10; Editorial, ‘A New Progressive Era’ in New York City, N.Y. TIMES (Jan. 1, 2018), <https://www.nytimes.com/2018/01/01/opinion/bill-de-blasio-inauguration.html> [<http://perma.cc/Z7CU-YMVD>] (explaining de Blasio's commitment to “a new progressive era” in his inaugural speech, in which he was sworn in by Senator Bernie Sanders). At the inauguration, the city's reelected public advocate and comptroller spoke and “emphasiz[ed] their progressive credentials.” *Id.*

<sup>64</sup> See, e.g., Lynch, *supra* note 55.

<sup>65</sup> See Savitch-Lew, *supra* note 11.

<sup>66</sup> See *id.*



compensation.”<sup>67</sup> Beginning with the seminal case *Pennsylvania Coal Co. v. Mahon* in 1922,<sup>68</sup> regulatory takings doctrine is the “idea that a regulation’s diminution of private property value can result in a taking” that falls under the Fifth Amendment’s prohibition and thus requires compensation from the government.<sup>69</sup>

The controversy in *Mahon* involved a regulation in Pennsylvania coal mining country that allowed the surface, support layer, and ore below the ground of an estate in land to be split among multiple owners. Some forty years prior to the litigation, the defendant, Pennsylvania Coal Company, sold the surface rights to a parcel of land, retaining the rights to the support and ore beneath it in accordance with state law and waiving liability for any damage caused by the coal mining beneath the surface.<sup>70</sup> Later, Pennsylvania passed the Kohler Act, making it illegal to engage in below-surface mining that could cause any structure above ground to sink. The Kohler Act thus destroyed any previously existing contract or property rights relating to the ore beneath the surface.<sup>71</sup> The defendant coal company, faced with the lawsuit seeking to enjoin its mining, asserted that this regulation went beyond the mere incidental fluctuations of property values that are the inevitable result of government regulation; rather, the company argued, this regulation rose to the level of a taking for which the company must be compensated if the regulation were to be constitutional.<sup>72</sup> The Court ultimately held that the Kohler Act constituted a taking, insofar as it wholly destroyed the defendant’s property interest. Writing for the majority, Justice Holmes recognized that:

The general rule at least is that while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking. . . . We are in danger of forgetting that a strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change.<sup>73</sup>

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<sup>67</sup> U.S. CONST. amend. V.

<sup>68</sup> 260 U.S. 393 (1922).

<sup>69</sup> See Hannah Jacobs, *Searching for Balance in the Aftermath of the 2006 Takings Initiatives*, 116 YALE L.J. 1518, 1522 (2007).

<sup>70</sup> See *Mahon*, 260 U.S. at 412; see also Laura J. Powell, *The Parcel As A Whole: Defining the Relevant Parcel in Temporary Regulatory Takings Cases*, 89 WASH. L. REV. 151, 156 (2014) (surveying the history of regulatory takings doctrine).

<sup>71</sup> *Mahon*, 260 U.S. at 412–13.

<sup>72</sup> See *id.* at 400–04.

<sup>73</sup> *Id.* at 415–16.

In short, Holmes and the majority of the Court held that, in cases involving regulatory takings, the presiding court should look to any diminution in value that is caused by the regulation in question.<sup>74</sup> However, diminution in value must by nature be a diminution *as a fraction of some entire value*. What, precisely, that entire value is became a critical issue whose resolution would have a significant impact on the outcome of takings cases.

Holmes and the majority evaluated diminution in value relative to the value of the property right in the ore.<sup>75</sup> Taken from this perspective, the diminution in value was the total value of the ore, making this a clear case of when the regulation “goes too far” and “will be recognized as a taking.”<sup>76</sup> The dissent, penned by Justice Brandeis, asserts that the diminution in value must take into account the value of the property as a whole:

[V]alues are relative. If we are to consider the value of the coal kept in place by the restriction, we should compare it with the value of all other parts of the land. That is, with the value not of the coal alone, but with the value of the whole property. The rights of an owner as against the public are not increased by dividing the interests in his property into surface and subsoil. The sum of the rights in the parts can not be greater than the rights in the whole.<sup>77</sup>

The interpretive dispute between Holmes and Brandeis—that is, the question of what exactly is being diminished by the government regulation—has come to be known as the “denominator problem.”<sup>78</sup> “Conceptual severance” is the term given to Holmes’ notion that a parcel of land comprises parts and the diminution in value can be evaluated in relation to a “severed” part that is the target of the regulation in question. Brandeis, on the other hand, suggests that we must look at what has come to be known as the “parcel as a whole.”<sup>79</sup> Of course, depending on how the “denominator” at issue is defined, the effect of the regulation can be enormous (and thus easily found to be a taking), or small (and thus unlikely to be considered a taking).

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<sup>74</sup> See *id.* at 413, 415.

<sup>75</sup> See *id.* at 414–16.

<sup>76</sup> See *id.*

<sup>77</sup> *Id.* at 419 (Brandeis, J., dissenting).

<sup>78</sup> See Steven J. Eagle, *The Four-Factor Penn Central Regulatory Takings Test*, 118 PENN. ST. L. REV. 601, 622–24 (2014).

<sup>79</sup> See *id.*

## B. The Rejection of Conceptual Severance

The Court did not confront the denominator problem head-on until many decades later, with its landmark decision in *Penn Central Transportation Co. v. New York City*.<sup>80</sup> In *Penn Central*, the then-newly conceived New York City Landmarks Preservation Commission designated Grand Central Terminal as a landmark, preventing the owners of the terminal from constructing a 50-story modern office building on top of the historic station.<sup>81</sup> Penn Central, the company that owned Grand Central, sued New York City, claiming that the landmark designation and concomitant restrictions on its property use constituted a taking of the company's air rights for which it must be compensated.<sup>82</sup> Thus, the applicable "denominator problem" in *Penn Central* was whether the diminution in value should be viewed in relation to merely the air rights (i.e., conceptual severance), in which case it would be considerable diminution, or in relation to the air rights in addition to the historic structure and rail operations (i.e., parcel as a whole), in which case the diminution would be less severe.<sup>83</sup> Ultimately, the Court rejected the conceptual severance doctrine. Writing for the majority, Justice Brennan held:

"Taking" jurisprudence does not divide a single parcel into discrete segments and attempt to determine whether rights in a particular segment have been entirely abrogated. In deciding whether a particular governmental action has effected a taking, this Court focuses rather both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole .....<sup>84</sup>

The Court continued, pointing out that although takings inquiries are "essentially ad hoc, factual inquiries,"<sup>85</sup> there are nonetheless several factors that are particularly important, namely:

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<sup>80</sup> *Penn. Cent. Transp. Co. v. New York City*, 438 U.S. 104 (1978). As an aside, *Penn Central* shows us that New York City's regulation of its built landscape has long implicated and influenced takings law.

<sup>81</sup> *Id.* at 115-17.

<sup>82</sup> *Id.* at 119.

<sup>83</sup> Penn Central argued that, if the Court would conceptually sever its air rights above the property, the restriction on its use of air rights above Grand Central constituted a complete diminution in value. However, the Court pointed out that the air rights could still be sold to neighboring buildings, albeit at a much lower profit than could be realized if Grand Central itself could use them. *See id.* at 136-37.

<sup>84</sup> *Id.* at 130-31.

<sup>85</sup> *Id.* at 124.

The economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations are, of course, relevant considerations. So, too, is the character of the governmental action [important]. A “taking” may more readily be found when the interference with the property can be characterized as a physical invasion by government . . . than when interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good.<sup>86</sup>

Thus, in *Penn Central*, the Court expressly rejected the notion of conceptual severance espoused by Justice Holmes in the *Mahon* decision.

In a case decided in the years following *Penn Central*, the Court added some more nuance to takings doctrine, distinguishing between physical and nonphysical government invasions. In *Loretto v. Teleprompter Manhattan CATV Corp.*,<sup>87</sup> the Court held that when the character of a government action is a permanent physical occupation of property, the Court will find that a taking has occurred, regardless of whether the invasion serves an important public benefit or has only minimal economic impact on the owner.<sup>88</sup> It is worth noting, however, that there can be physical invasions that are not necessarily permanent and are thus not subject to the per se taking rule. Such regulations fall instead under *Penn Central*'s ad hoc balancing test.<sup>89</sup>

### C. The *Murr* Decision

In its 2016 term, the Court made another foray into regulatory takings law in the case *Murr v. Wisconsin*,<sup>90</sup> elaborating on the rule articulated in *Penn Central*. This recent decision set forth a new test for determining what the “denominator” is in takings analysis.

*Murr* involved siblings who inherited adjacent lots in a scenic area along the St. Croix River in Wisconsin.<sup>91</sup> Under Wisconsin law, individual lots could not be used for separate building sites unless they had at least one acre of land suitable

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<sup>86</sup> *Id.* (citations omitted).

<sup>87</sup> 458 U.S. 419 (1982).

<sup>88</sup> *See id.* at 426, 434–35, 438 (holding that a nondescript but permanent wire installation on plaintiff-landlord's apartment building in New York constituted a taking).

<sup>89</sup> *See Penn Central*, 438 U.S. at 124–25.

<sup>90</sup> 137 S. Ct. 1933 (2017).

<sup>91</sup> *Id.* at 1940.

for development.<sup>92</sup> Further, adjacent lots under common ownership could not be sold or developed as separate lots if they did not meet the requirement of having at least one acre of land suitable for development.<sup>93</sup> The Murrs sought to build a cabin on one of the lots and sell the other lot to fund the construction of the cabin.<sup>94</sup> However, because neither of the lots contained more than an acre of land suitable for development, the local rule prohibited them from selling or developing either parcel individually, effectively merging them into one parcel.<sup>95</sup> The Murrs brought suit against the State of Wisconsin, alleging that this functional merger diminished the value of their property and thus constituted a regulatory taking.<sup>96</sup> The case eventually made its way to the Supreme Court on a denominator-problem issue—namely, whether the diminution in value should be viewed as a portion of one of the Murrs' lots or both.<sup>97</sup> If the denominator was only one of the lots, then the diminution would be quite large and would most likely constitute a regulatory taking.<sup>98</sup> However, if the denominator were both the lots taken as one merged lot, then the diminution in value would be less severe and less likely to constitute a taking.<sup>99</sup>

Writing for the majority, Justice Kennedy pointed out that, “[a] central dynamic of the Court’s regulatory taking jurisprudence . . . is its flexibility.”<sup>100</sup> Because of this flexibility, “the Court has declined to limit the parcel in an artificial manner to the portion of property targeted by the challenged regulation.”<sup>101</sup> Kennedy further noted:

[Another] concept about which the Court has expressed caution is the view that property rights under the Takings Clause should be coextensive with those under state law. Although property interests have their foundations in state law, . . . States do not have the unfettered authority to “shape and define property rights and reasonable investment-backed ex-

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<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> *Id.* at 1941.

<sup>95</sup> *Id.*

<sup>96</sup> *See id.*

<sup>97</sup> *See id.* at 1943–44.

<sup>98</sup> *See id.* at 1941–42.

<sup>99</sup> *Id.* The trial court analyzed the diminution in value out of the two lots combined and found that the diminution was thus not sizable enough to constitute a taking. *Id.* at 1941. The appellate court affirmed, holding that the trial court properly focused on the Murrs’ “property as a whole.” *Id.*

<sup>100</sup> *Id.* at 1943.

<sup>101</sup> *Id.* at 1944.

pectations,” leaving landowners without recourse against unreasonable regulations.<sup>102</sup>

It is for these reasons that the Court held that “no single consideration can supply the exclusive test for determining the denominator.”<sup>103</sup> In other words, *Murr* put forth a flexible, ad hoc balancing test. However, the Court recognized that the inquiry must be guided by some clear factors in order to be workable. The Court thus proceeded to amend the *Penn Central* test to set forth the factors that must be considered in determining the denominator in takings analysis.<sup>104</sup> Namely,

[C]ourts must consider . . . [T]he treatment of the land under state and local law; the physical characteristics of the land; and the prospective value of the regulated land. The endeavor should determine whether reasonable expectations about property ownership would lead a landowner to anticipate that his holdings would be treated as one parcel, or, instead, as separate tracts.<sup>105</sup>

Stated differently, the denominator test is an objective test of whether reasonable expectations about property ownership would lead a landowner to anticipate his holdings to be treated as one parcel or as separate tracts. The three factors enumerated above are used to guide the analysis. Using these new factors, the Court affirmed the ruling of the state courts and found that the regulations at issue did not effect a taking.<sup>106</sup>

## V

### THE CONSTITUTIONALITY OF THE SBJSA UNDER TAKINGS ANALYSIS

Takings law has the potential to be damning for the viability of any commercial rent regulation proposal, particularly the

<sup>102</sup> *Id.* at 1944–45 (citation omitted) (citing *Palazzolo v. Rhode Island*, 533 U.S. 606, 626–27 (2001)).

<sup>103</sup> *Id.* at 1945.

<sup>104</sup> *See id.* at 1945–46. For a discussion of how the *Murr* test might not have made the denominator inquiry clearer at all, see generally Richard A. Epstein, *Disappointed Expectations: How the Supreme Court Failed to Clean Up Takings Law in Murr v. Wisconsin*, 11 N.Y.U. J.L. & LIBERTY 151, 183–89 (2017) (explaining that *Murr* “dodged the hard questions latent in applying the ‘parcel-as-a-whole’ test”).

<sup>105</sup> *Murr*, 137 S. Ct. at 1945.

<sup>106</sup> *See id.* at 1948–50. The Court reasoned that the property’s treatment under state law made it reasonable to expect that the lots would be treated as a single property. Further, the physical characteristics (namely, the contiguity) of the lots makes it reasonable to expect that their potential uses might be limited. Finally, the restriction on either individual lot is mitigated by the benefits of having one large, integrated property.

SBJSA. Despite the pessimistic position of proponents of the SBJSA that the New York City Council is nothing more than a shill for the real estate industry, the argument that commercial rent control is unconstitutional (absent just compensation) might hold some water. In short, if commercial landlords in New York are restricted in the ways in which they can use their property under the Act, they will be able to make some compelling legal claims that the Act constitutes either a categorical, per se taking or an ad hoc regulatory taking that requires the balancing test laid forth in *Penn Central* and *Murr*.

It is first necessary to evaluate whether the government regulation that would be instituted by the SBJSA is more accurately characterized as a permanent physical invasion or as a nonphysical balancing of societal interests. If the SBJSA is best characterized as the former, then it will likely constitute a categorical, per se taking. If the SBJSA is the latter, then it is subject to the ad hoc balancing outlined in *Penn Central* and its progeny.

#### A. The SBJSA and Categorical Takings

Although *Loretto's* physical taking rule is somewhat narrow, there is an argument to be made that it applies in the commercial rent regulation context: when the government forces a landlord to allow a tenant to remain at a lower rent than the landlord would prefer (or could otherwise get at fair market value), it constitutes a per se taking. This argument does seem compelling on its face. However, the SBJSA's fundamental requirements that small commercial tenants have a right of renewal and that there exist a more tenant-friendly negotiation process do not seem to be the type of physical invasions that are within the contemplation of *Loretto*, which dealt with a government installation of a wire on the plaintiff's building.<sup>107</sup>

Furthermore, even if the SBJSA is a physical invasion by the government, it is doubtful that it constitutes a permanent physical invasion. Proponents of the bill would likely point out that it is irrelevant because, no matter what, the landlord seeks to have a tenant in the space. Thus, having a tenant that simply pays less rent is not truly a permanent physical invasion. In other words, regardless of the outcome, there would be a tenant in that space. Further, the SBJSA permits the land-

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<sup>107</sup> See *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 421-22 (1982).

lord to get a new tenant if there is a bona-fide offer after negotiations with the previous tenant collapse.<sup>108</sup> This latter point tilts in favor of the argument that even if there is an invasion, it is not a permanent one.

On the other hand, opponents of the bill might suggest that landlords should not be forced to offer their space to tenants when they no longer find it economically viable. The reality is that even previous tenants can stay in place indefinitely. Opponents of the SBJSA will likely assert that to require landlords to do so—that is, to require them to continue allowing an undesired tenant who can indefinitely renew the lease to occupy the space—is precisely the type of permanent physical invasion that is within the contemplation of *Loretto*. To analogize the situation to *Loretto*, one wire kept on a landlord's building by the government and another wire kept on the building by the landlord are two very different things, even if they appear to be the same.

Although the latter argument is compelling, ultimately it does not seem as if the physical presence of a particular commercial tenant is the harm. Rather, the harm alleged is solely economic: the inability of the landlord to collect as high a rent on the property as desired. In other words, opponents of the SBJSA believe that, under the Act, landlords suffer a nonphysical taking that renders them unable to fully use their property to seek higher, market rate rents on commercial space. Such an argument must be evaluated under the *Penn Central* and *Murr* line of cases.

## B. Ad Hoc Regulatory Takings and the SBJSA

If the SBJSA is merely adjusting the benefits and burdens of economic life to promote the common good, rather than imposing a permanent physical invasion on property, then it is subject to the ad hoc balancing and denominator analysis set forth in *Penn Central* and *Murr*.<sup>109</sup> As suggested above, the denominator question can have an enormous—indeed, most likely a dispositive—effect on whether the Act constitutes a taking.

At the outset, it is worth noting that commercial storefronts in New York City can either be owned as (1) free-standing commercial buildings, (2) as separate, individual par-

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<sup>108</sup> See *Creating a Small Business Lease Program*, *supra* note 51.

<sup>109</sup> See *supra* Part III.



cells that happen to be part of a larger building,<sup>110</sup> or (3) as part of a unified, mixed-use parcel that includes both residential and commercial space under a single owner.<sup>111</sup> As the following subsections explain, the first two will be treated similarly when it comes to denominator analysis, but the latter must be treated differently.

1. *Freestanding Commercial Buildings and Commercial Spaces Owned Separately in Mixed-Use Buildings*

In addition to freestanding commercial buildings, New York is home to innumerable mixed-use residential-commercial structures that are spliced up, with the commercial spaces and residential spaces under separate ownership.<sup>112</sup> In such a situation, there is no complicated denominator problem implicated by the SBJSA. In other words, there is no ambiguity in what the parcel as a whole is; there is no way to conceptually sever one portion of the property from the other. Thus, in evaluating whether the SBJSA would constitute a regulatory taking when applied to small businesses located on these types of properties, it is only necessary to apply the *Penn Central* analysis to the value of the commercial space.

If the SBJSA were to pass in City Council, owners of these types of properties would have a very compelling argument that the Act constitutes a taking under the *Penn Central* analysis. As evidenced by the astronomically higher rents collected by landlords after the leases of small business expire (often tens of times higher), it is clear that landlords' "investment-backed expectations"<sup>113</sup> are dramatically curtailed if they are forbidden from attracting market rents. For instance, a landlord who is able to attract a market rent ten times higher than that paid by a current, small business tenant would be able to show that the SBJSA diminishes the value of the property by 90%.

Although proponents of the SBJSA may argue that the benefit to society of ensuring that small businesses can stay in their spaces outweighs this cost, the reality is that the SBJSA does not truly guarantee that they will be able to stay. Rather, it merely gives them the right of renewal and the ability to go to

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<sup>110</sup> One such example is a ground-floor commercial condominium in a large, mixed-use building in which the residential condominiums above are owned separately from the commercial condominium below.

<sup>111</sup> See SPECIAL INITIATIVE FOR REBUILDING AND RESILIENCY, N.Y.C., A STRONGER, MORE RESILIENT NEW YORK ch. 4 at 70–71 [hereinafter REBUILDING AND RESILIENCY].

<sup>112</sup> See *id.*

<sup>113</sup> *Penn. Cent. Transp. Co. v. New York City*, 438 U.S. 104, 124 (1978).

arbitration with their landlord.<sup>114</sup> In light of this, it seems likely that owners of freestanding commercial spaces and owners of commercial spaces that are owned separately from the mixed-use structures in which they are housed will be able to show that the SBJSA constitutes a taking, almost entirely diminishing the market value of their property. This alone is enough to make the SBJSA prohibitively expensive because it is not feasible to compensate the landlords for this loss.

## 2. *Commercial Spaces in Mixed-Use Structures Under Unified Ownership*

Mixed-use structures, containing both commercial and residential spaces, can be—and commonly are—part of a building under unified ownership.<sup>115</sup> These types of properties present an altogether different inquiry, reintroducing the need for denominator analysis.

Opponents of the SBJSA who own mixed-use buildings, housing both commercial and residential spaces, will likely argue that the appropriate denominator here is the commercial space alone, rather than the commercial space plus the various residential units above. This is because if the denominator is merely the commercial space, they will be able to show almost complete diminution in value, as with the types of property in subsection one above. That is, if we are concerned with the diminution in value only of the commercial space whose use is severely restricted by the SBJSA, then it seems likely that the SBJSA would constitute a taking. On the other hand, if the denominator in this takings analysis is the value of the commercial space in addition to the various (very expensive) residences above it in the mixed-use building, then the diminution will be comparatively small. Stated more clearly, the landlord's inability to realize the maximal value that the market can get for a commercial space will be deemed to have less of an impact in evaluating whether a taking has occurred. If the diminution is comparatively small, then it is almost certain that the SBJSA will not constitute a taking under the *Penn Central* test.

It is difficult to see why this situation is any different from *Penn Central*'s failed argument to have the court conceptually sever its air rights from the value of the parcel as a whole. The rejection of conceptual severance set forth in *Penn Central* seems to guarantee that the diminution in value under the

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<sup>114</sup> See *supra* subpart III.B.

<sup>115</sup> See REBUILDING AND RESILIENCY, *supra* note 111.

SBJSA would be considered relative to both the commercial and residential space together. In other words, to say that commercial space in a mixed-use building should be considered separately from residential space in the same building seems very much akin to the argument that Grand Central's airspace should be considered separately from the building itself—an argument that the Court squarely rejected. Thus, it does not seem like the SBJSA would constitute a regulatory taking for owners of mixed-use buildings that house both commercial and residential units.

However, recognizing this, any rational landlord in a world in which the SBJSA passed would simply attempt to restructure the building ownership such that the commercial and residential space were entirely separate, rather than one parcel.<sup>116</sup> It is in this situation that the *Murr* test becomes relevant. In other words, a landlord who owns two separate parcels—commercial and residential—housed in one building will argue that they should be treated as separate. This is precisely like the Murrs' argument that their adjacent parcels should be treated as separate.<sup>117</sup> In this instance, the parcels are simply vertically rather than horizontally contiguous pieces of property.

If the parcels are treated separately, then the SBJSA would diminish the value of the commercial space enough that it would likely constitute a taking. Per *Murr*, then, one critical question in such a situation arises: Would a landlord's reasonable expectations about property ownership lead the landowner to anticipate the commercial and residential spaces in a mixed-use building to be treated as one parcel or as separate tracts? If it is the former, the SBJSA will likely not constitute a taking; if it is the latter, then it almost certainly will.

To evaluate this denominator problem, it is necessary to use the factors laid out in *Murr*.<sup>118</sup> Turning first to the treatment of the land under state and local law, proponents of the bill will likely succeed in pointing out that ownership of commercial and residential space in a single building would reasonably lead the owner to expect these components to be treated as one. This somewhat blends into the second factor: the physical characteristics of the land. In this scenario, we are dealing with a single building that has simply been subdivided into different pieces. The commercial and residential

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<sup>116</sup> For instance, by turning the building into a condominium in which the commercial and residential units are owned as separate parcels unto themselves.

<sup>117</sup> See *supra* subpart III.C.

<sup>118</sup> See *Murr v. Wisconsin*, 137 S. Ct 1933, 1944–45 (2017).

portions are vertically contiguous to one another—they are literally housed under one roof and owned by the same person, thus making it even more reasonable to expect them to be treated as one than the adjacent tracts in *Murr*. Turning finally to the prospective value of the regulated land, this factor seems to lean towards viewing them as one parcel. When the commercial and residential components are considered as one parcel, their combined value would be worth significantly more than each parcel separately, and any diminution in the value of the commercial space would not affect the value of the residential space.<sup>119</sup> Indeed, they would exhibit the same “complementarity” as the tracts in *Murr*.<sup>120</sup>

In summary, it can be said that a landowner who owns both the commercial and residential portions of a mixed-use structure would reasonably expect the two parts to be treated as one tract. The result is somewhat paradoxical: the mere fact that separate commercial and residential components of one building happen to be owned by the same person will likely mean that the regulation of the commercial space does not result in a taking. On the other hand, it would constitute a taking if the commercial space and residential space were owned by separate individuals. Nonetheless, this seems to be the result that current takings law compels under *Murr*.

#### CONCLUSION

The decline in small businesses is one of the most significant and important challenges that the city faces in the coming years. After some (albeit unfinished) success in addressing the housing affordability crisis in the city during its first term, the de Blasio administration should turn its focus to the equally precarious position of the city’s small businesses. Although it is difficult to imagine a better impetus for action than the endangerment of thousands of New Yorkers’ livelihoods, stronger commercial rental protections also serve the interests of the community more generally. This appears to be a fact that is increasingly recognized in City Council.<sup>121</sup>

In order to combat this, some City Council legislators have proposed the SBJSA. However, the bill has struggled to get to the floor of City Council for a vote despite enjoying support from most councilmembers. This failure is largely because of opponents’ claims that the Act, without compensating land-

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<sup>119</sup> See *id.* at 1948.

<sup>120</sup> See *id.* at 1949.

<sup>121</sup> See Lynch, *supra* note 55.

lords for the large diminution in value of their property, constitutes an unconstitutional regulatory taking.

In light of the current state of regulatory takings law, this argument likely holds true for commercial parcels that are free-standing or under different ownership from the mixed-use structures in which they are located; however, it is likely that the SBJSA does not constitute a regulatory taking when commercial and residential portions of a mixed-use building are under the same ownership.

Although the SBJSA might not amount to a regulatory taking when applied to every commercial space in New York, its application to even some of them would likely make it prohibitively costly. Thus, to address the rising affordability crisis for New York's small businesses, the city should instead find alternative solutions that do not involve forms of commercial rent control. This could mean providing more subsidies to small business owners directly, or it could mean providing tax and other incentives to landlords to encourage rentals to small businesses and discourage maintaining empty storefronts in the city. This should provide important guidance to both New York and other cities that are concerned with the state of small businesses within their boundaries.

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