Document hosted at JDSUPRA
http://www.jdsupra.com/post/documentViewer.aspx?fid=c127afb7-738b-47a4-8831-1bb9844415de

Real Estate Perspective @ manatt

August 19, 2009

Appellate Advice On What Is NOT a "Reasonable" In-Lieu Fee

Michael M. Berger

Herewith, a fascinating tale of impact fees, a development agreement, and a city's power to radically change the former in light of the latter – and whether anyone but the parties should know about the outcome.

Every now and then, a piece of litigation blazes across the firmament, showing up on everyone's radar screen. *Building Industry Assn. of Central California v. City of Patterson*, 171 Cal.App.4th 886 (2009) is such a case.

The case began innocently enough when Morrison Homes, Inc. inked a development agreement with, and obtained vesting tentative subdivision tract maps from, the City of Patterson. As is fairly common, the City had an affordable housing requirement for new residential developments, which developers could bail their way out of at a cost of $734 per house. The development agreement, which otherwise froze regulations as of the date of its signing, allowed an increase in this in lieu fee if the increase was "reasonably justified." Three years later, the City increased the in lieu fee from $734 per house to $20,946 per house and sought to apply the increased amount to Morrison's projects.

The developer sued; the trial court upheld the City; the developer appealed. Held: reversed. But that's only part of the story. Read on.

What had happened is that the City changed its ways of computing the in lieu fees. The initial fee was determined by using what the City called a "leverage" approach, i.e., using the fees to obtain federal loans and grants. When the City decided to drop that approach and focus on actual construction costs and the difference between market rate housing and low to moderate

Our Practice

Manatt has a broad background in all areas of real estate practice that give our domestic and foreign clients the edge to succeed. Our professionals are recognized as some of the premier real estate and development advisors in the nation who promote the transactional expertise, market insight and government advocacy ... more

Practice Group Overview
Practice Group Members

Info & Resources

Subscribe
Unsubscribe
Newsletter Disclaimer
Manatt.com

Document hosted at JDSUPRA
http://www.jdsupra.com/post/documentViewer.aspx?fid=c127afb7-738b-47a4-8831-1bb9844415de

income housing, it concluded that it needed $73.5 million to construct its fair share of subsidized housing. Spreading that cost over the number of unentitled units left in the City produced the much larger number. (Acknowledging the games that can be played with numbers, the Court of Appeal noted that, if this developer's remaining units were the only unentitled market rate units in the City, then the per unit in lieu fee would have been $343,458. But I digress. Or do I?)

The developer had doubly protected itself from changes in the law. First, it had a vesting tentative tract map. Under California law, a "vesting" map freezes local regulations as of the date it is accepted. (Govt. Code §§ 66498.1, 66474.2) Second, Morrison had a development agreement, which should have done the same. The appellate court noted that the parties had agreed that any conflict between the two was governed by the development agreement, and that agreement allowed for a change in the in lieu fee if it was "reasonably justified."

The court rejected Morrison's argument that the City was restricted to changes that used the original "leverage" mode of analysis, as nothing in the agreement restricted the way in which the City could make the determination. The question thus boiled down to the meaning of "reasonably justified."

The City apparently took a "sky's the limit" approach in its argument, urging that the contractual provision authorizing it to make changes automatically freed it from any legal requirements that would have otherwise applied. Morrison countered that the words could not be so loosely read as to leave the City wholly untethered. The court agreed:

"Here, we conclude that an objectively reasonable person would expect the term 'reasonably justified' to mean that any increase in the affordable housing in-lieu fee would conform to existing law. In other words, part of the way one would show a fee is reasonably justified is to show that it does not violate established legal principles. The contrary interpretation, which would conclude that the term did away with applicable legal requirements, would create much greater change in the relationship between the parties. An objectively reasonable person would expect more explicit language to implement such a change. Thus, it is too great a leap to infer that the term 'reasonably justified' demonstrates an intention to waive applicable legal requirements." (171 Cal.App.4th at 896.)

Morrison urged that the proper standard of review was provided by the U.S. Supreme Court's decisions in *Nollan v. California Coastal Commn.*,, 483 U.S. 825 (1987), and *Dolan v. City of*

Document hosted at JDSUPRA
http://www.jdsupra.com/post/documentViewer.aspx?fid=c127afb7-738b-47a4-8831-1bb9844415de

Tigard, 512 U.S. 374 (1994) and the California Supreme Court's decision in *Ehrlich v. City of Culver City*, 12 Cal.4th 854 (1996), i.e., a heightened level of scrutiny that would examine the City's action in light of its nexus and proportionality to the burdens imposed on the City by Morrison's development.

Feeling bound by the California Supreme Court's analysis of a rent control ordinance in *San Remo Hotel v. City & County of San Francisco*, 27 Cal.4th 643 (2002), the court concluded that the proper test was whether "there is a reasonable relationship between the amount of the fee, as increased, and 'the deleterious public impact of the development.'" (171 Cal.App.4th at 898.) The answer was no, as the court found nothing in the record that tied the increase to any adverse impacts associated with the project but, instead, simply an arithmetical projection based on general regional housing studies:

"The record in this matter reveals no reasonable relationship between the extent of City's affordable housing need and development of either (1) the 214 residential lots that constitute the two subdivisions owned by Developer or (2) the 3,507 unentitled lots identified in the Fee Justification Study. Instead, the Fee Justification Study reveals that the in-lieu fee of $20,946 per market rate unit was calculated based on an allocation to City of 642 affordable housing units, out of the total regional need for affordable housing identified in the 2001-2002 Regional Housing Needs Assessment for Stanislaus County. No connection is shown, by the Fee Justification Study or by anything else in the record, between this 642-unit figure and the need for affordable housing associated with new market rate development. Accordingly, the fee calculations described in the Fee Justification Study . . . do not support a finding that the fees to be borne by Developer's project bore any reasonable relationship to any deleterious impact associated with the project." (171 Cal.App.4th at 899.)

The Court of Appeal reversed, directing the trial court to invalidate the new in lieu fee, but leaving any other remedy for further determination.

That's when the fun started. Evidently the Court of Appeal did not think it had done anything particularly momentous, as it did not certify the opinion for publication. Under California's rules, the opinion would therefore be res judicata as to the City of Patterson, but not even worth the consideration given student law review notes as to any other city.

Word got around – perhaps aided by the fact that the local wing of the Building Industry Association was a co-plaintiff with the

Document hosted at JDSUPRA
http://www.jdsupra.com/post/documentViewer.aspx?fid=c127afb7-738b-47a4-8831-1bb9844415de

developer. As allowed by Rule 8.1120, Cal. Rules of Court, anyone may ask a Court of Appeal to publish an opinion not originally slated for publication. This is done by letter, letting the court know how highly prized its words will be if they are only allowed to see the light of day, because they deal with important or previously unsettled issues. So, twelve days after filing, such a request appeared on the docket. Then the floodgates opened, resulting in these docket entries:

2009	Filed request to publish opinion.	Several different requests filed by: Paul Campos /Home Buil Tracy T. Carver/Hearthstone; Fred Bell/BIA Desert Champte Yoder/Shea Homes; Roger A. Grable/Manatt; David A. Turner/David A. Turner Homes (to jak)
2009	Filed request to publish opinion.	multiple requests by : Christopher E. Skiff/The Manse; Dixie Wells/Di-Mac Development, Inc.; Anthony E. Wells/Stonegat Orcutt Venture, LLc. (to jak)
2009	Filed request to publish opinion.	by J. Michael Armstrong, Principal/Senior Vice President of B American Incorporated. (JAK)
2009	Filed request to publish opinion.	by atty David Lanferman/applts Building Industry Associatio central california and Morrison Homes. (to jak)
2009	Filed request to publish opinion.	Mulitple requests by several different interested parties in th Home Building Industry. (to jak)
2009	Filed request to publish opinion.	multiple requests from several interested parties in the build Industry. (to jak)
2009	Filed request to publish opinion.	Multiple (34) reqs from interested parties in the building Ind JAK
2009	Received:	Multiple (36) requests for publication of the opinion from interested parties in the building industry. (JAK)
2009	Received:	Multiple (9) requests for publication of the opinion from inte parties in the building industry. (JAK)
2009	Received:	Multiple (17) requests for publication of the opinion from interested parties in the building industry. (JAK)
2009	Received:	One (1) Oppositon from (League of California Cities) to the requests for Publication of the opinion from interested partie (JAK)
009	Received document entitled:	3 different untimely requests for publication . placed in file.
009	Order granting publication filed.	pursuant to multiple requests filed by Applt cousnel and vari interested parties The opinion filed 1/30/09 is order publishe with the exception of parts I and IIB (jak)

Note that, after a few days, the clerk got to the point of simply entering the requests in bulk, as the number of publication requests shot past 100. The League of California Cities tried to put its corporate finger in the dike, but it was too late, and the

Document hosted at JDSUPRA
http://www.jdsupra.com/post/documentViewer.aspx?fid=c127afb7-738b-47a4-8831-1bb9844415de

opinion was ordered published.

The City then tried to attract the Supreme Court's attention, seeking review of the intermediate court. A group called the Public Interest Law Project wrote to the Supreme Court asking that the now published opinion be de-published. Intriguingly, that request did not urge that the appellate court got it wrong, but that the case was only about how the City of Patterson had screwed up in applying one specific development agreement and that other cities would not do that and that therefore there was no need for this opinion to see the light of day.

But there was a need for published appellate authority. According to the letter seeking de-publication, more than 170 California communities have affordable housing requirements. As the Court of Appeal pointed out here, such requirements may be satisfied in a number of ways. That is why the fee is called an "in lieu" fee; it is in lieu of actually building the affordable housing units. In this case, for example, the options were:

"(1) build affordable housing units; (2) develop senior housing within the project; (3) obtain a sufficient number of affordable residential unit credits from other residential developments within City; or (4) pay an in-lieu fee at the time the building permit is issued for a market rate housing unit." (171 Cal.App.4th at 890.)

The only extant published opinion was decided after a demurrer was sustained and dealt with the facial validity of the ordinance. (*Homebuilders Assn. of Northern California v. City of Napa*, 90 Cal.App.4th 188 [2001].) The *Patterson* opinion discussed the mode of analysis necessary when an as-applied challenge is made and tried on the merits. Because of the publication of the opinion, all parties to such controversies now have judicial guidance, which is usually a good thing.

The California Supreme Court denied review and refused to de-publish the opinion.

back to top

For additional information on this issue, contact:

Michael M. Berger Mr. Berger is one of California's preeminent appellate lawyers and is co-chair of Manatt's Appellate Practice Group. One of the top land use and condemnation lawyers in the United States, his appellate cases have involved planning, zoning, eminent domain, various kinds of business litigation, landslides, contract, due process, equal protection, defective construction, nuisance, insurance and environmental law.

Document hosted at JDSUPRA
http://www.jdsupra.com/post/documentViewer.aspx?fid=c127afb7-738b-47a4-8831-1bb9844415de

ATTORNEY ADVERTISING pursuant to New York DR 2-101(f)

Albany | Los Angeles | New York | Orange County | Palo Alto | Sacramento | San Francisco | Washington, D.C.

© 2009 Manatt, Phelps & Phillips, LLP. All rights reserved.