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To

John Nagel, City Attorney

From

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RE

File No. 16-0233: Appeal of Special Development Permit and Vesting Tentative Map Approvals

I. Issue Presented

The City of Sunnyvale's Planning Commission approved an application for a Special Development Permit and a Vesting Tentative Map to permit residential development, new commercial uses, and the expansion of the Grand Hotel at 803 W. El Camino Real. An appellant challenged the approval on several grounds, one of which was because the Planning Commission did not require on-site affordable units in connection with the development of new rental housing. The City has asked if it can require on-site rental housing as a condition of project approval in connection with a Special Development Permit and a Vesting Tentative Map.

II. Summary

Sunnyvale's affordable housing ordinance (Sunnyvale Municipal Code (SMC) Chapter 19.67, Below Market Rate Ownership Housing) exempts all rental housing developments from the City's affordable housing requirements (SMC Section 19.67.030(b)). Additionally, the Costa-Hawkins Rental Housing Act (Civil Code Section 1954.50 *et seq.*) provides that rental restrictions may be imposed only if a project receives a direct financial contribution or a regulatory incentive from the City, *and* the owner agrees to rental restrictions by contract. Here, the City approved the owner's application for a Special Development Permit and a Vesting Tentative Map, but it did not provide a direct financial contribution or another form of assistance that would enable the City to impose rental restrictions. Therefore, neither the Sunnyvale Municipal Code nor the Costa-Hawkins Act allows the City to require the inclusion of affordable rental housing in this project.

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III. Background

On April 25, 2016, the Planning Commission approved De Anza Properties' application for a Special Development Permit and a Vesting Tentative Map to subdivide three existing lots into 11 separate lots and to construct a mixed-use development with 49 residential units (40 rental (apartments) and nine for-sale units), approximately 5,662 square feet of commercial space, and an expansion of the Grand Hotel adding 51 rooms.

Condition of Approval GC-7 requires the developer to enter into a Below Market Rate (BMR) Housing Agreement with the City to provide one BMR dwelling unit for sale and pay a fractional in-lieu fee of .13 units in compliance with the requirements of SMC Chapter 19.67 and the City's BMR Program Guidelines for the nine for-sale units.

The developer has expressed its intent to rent the remaining 40 units in the project, and Condition of Approval GC-7 does not require the developer to provide any BMR rental units in the project. If the developer sells the units in the future, Condition of Approval GC-8 provides that the conversion will be subject to the provisions of SMC Chapter 19.67, and on-site BMR ownership housing will be required at that time.

During the April 25, 2016 Planning Commission hearing on the project, the appellant requested that the Planning Commission require the provision of BMR rental units as a condition of project approval. The Planning Commission did not impose such a condition, and the appellant has appealed this decision to the City Council, asking that the City require affordable rental housing on-site before the 40 rental residential units in the project are made available for sale and the provisions of Condition of Approval GC-8 become effective.

IV. Discussion

The Sunnyvale Municipal Code exempts all rental housing developments from its affordable housing requirements. Additionally, the Costa-Hawkins Act precludes the City from requiring BMR rental units or in-lieu fees as a condition of project approval, unless a project receives a direct financial contribution or a regulatory incentive from the City, and the owner agrees to the rental restrictions by contract. As discussed below, none of these elements are satisfied here, so the City may not require on-site affordable rental housing as a condition of approving the project. Additionally, the project application was a "pipeline project" when the City adopted its Housing Impact Fees Ordinance and is therefore exempt from its provisions. The project is required to provide BMR for-sale units at the time units in the project are offered for sale, but under current State law and the Sunnyvale Municipal Code, the City cannot require other affordable housing conditions.

a. State Law Generally Precludes Mandatory Below-Market Rate Rental Units.

The Costa-Hawkins Act provides that the owner of residential real property may establish the initial rate for a dwelling unit unless a specific exception occurs. (Civ. Code § 1954.53(a).) In 2009, the Court of Appeal held that the Costa-Hawkins Act precludes public agencies from

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requiring the developer of a residential rental development to rent units at a specified below market rate. (*Palmer/Sixth Street Properties, L.P. v. City of Los Angeles* (2009) 175 Cal.App.4th 1396 ("*Palmer*").) Although public agencies may adopt and enforce inclusionary zoning ordinances that require below market rate for-sale units, the California Supreme Court has recognized that, unless the California legislature amends state law, public agencies may not require on-site BMR rental units unless a specified exception applies. (*California Building Industry Assn. v. City of San Jose* (2015) 61 Cal.4th 435, 450, fn. 6.)

b. *The Sunnyvale Municipal Code Exempts Rental Housing Developments from Its Affordable Housing Requirements.*

In recognition of the *Palmer* decision, the City amended SMC Chapter 19.67 to exempt all rental housing developments from its affordable housing requirements and to limit its applicability to for-sale housing. Therefore the Planning Commission did not require that the 40 rental residential units include affordable housing, but rather provided that if the 40 proposed rental units are sold, SMC Chapter 19.67 will apply, and on-site BMR ownership units will be required at the time of sale.

c. *None of the Exceptions to the Costa-Hawkins Rental Housing Act Apply to This Approval.*

Under the Costa Hawkins Act, the City may limit rents if the rental property's owner has otherwise agreed by contract "in consideration for a direct financial contribution or any other forms of assistance specified in Chapter 4.3 (commencing with Section 65915) of Division 1 of Title 7 of the Government Code." (Civ. Code § 1954.53(a)(2).) Government Code Section 65915 is the state Density Bonus Law, and it identifies forms of assistance that, if requested by the applicant and approved, would permit a public agency to impose rent limits. These forms of assistance include density bonuses, specified parking reductions, and "concessions and incentives."

Developers are entitled to one to three "concessions and incentives" depending on the amount of affordable housing proposed in the development. "Concessions and incentives" include modifications of normal development standards, other "regulatory incentives," and non-residential uses that result in actual cost reductions that make affordable housing feasible. (Government Code Section 65915(k); see definitions in Attachment 1.) No discretionary approval may be required for a concession or incentive (*Id.* at § 65915(j)(1)), and concessions and incentives may be denied only if the City is able to demonstrate, by substantial evidence, that they are not needed for the proposed affordable housing, violate state or federal law, or have a specific, adverse environmental impact (*Id.* at § 65915(d)(1)).

Here, the Planning Commission has approved a Special Development Permit (SDP) that provides for an increase in lot coverage from 35% to 54%, a reduction in upper story setback distance from 15 feet to 13.5 feet, and 126 parking spaces (six of which as valet/tandem spaces) when 124 standard parking spaces are otherwise required. The Special Development Permit also entitles

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the developer to build a mixed-use project with residential, commercial, and hotel uses in the C-2 / ECR zone.

The appellant asserts that the City's approval of the SDP is a "concession or incentive" that would allow the City to require affordable rental housing. However, although the SDP allows for mixed-use zoning and modifications of development standards, it is not a "concession or incentive" as defined in state Density Bonus Law. The developer has not proposed to include affordable housing in the project and then requested "concessions or incentives" to make the affordable housing feasible. The SDP is a discretionary permit authorized by the Sunnyvale Municipal Code and may be approved or denied by the City based on findings that provide much more authority to the City than available under Density Bonus Law. For instance, the conditions of approval require specific contributions from the developer (such as enhanced landscaping, additional sidewalk improvements, and a parking management plan) that directly mitigate the impacts of the modifications granted via the SDP, conditions which would not be permitted under Density Bonus Law. Similarly, the developer applied for, and received, an SDP to allow residential uses in the C-2 / ECR zone, a use that is specifically permitted with a use permit. This is not the equivalent of permitting a residential project to incorporate non-residential uses to make affordable housing feasible, as contemplated by the State Density Bonus Law.

Because the City has not provided financial assistance, nor a form of assistance specified in Density Bonus Law, no exemption from the Costa-Hawkins Act applies, and the City cannot require affordable rental housing in the project.

d. *The Project is Exempt from the City's Housing Impact Fees.*

Public agencies may impose impact fees justified by a nexus study to offset the impact to affordable housing created by market rate housing development. The City adopted such housing impact fees in SMC Chapter 19.75 in 2015. However, SMC Section 19.75.020(b) exempts projects that had filed a complete development application by September 14, 2015. Here, the project's application was deemed complete before September 14, 2015, so it is exempt from the payment of Housing Impact Fees.

V. Conclusion

Because the Sunnyvale Municipal Code exempts rental housing from its BMR requirements, and the City is not providing the developer with a direct financial contribution or another form of specified assistance, the Costa-Hawkins Act precludes the City from requiring BMR rental units as a condition of project approval.

ATTACHMENT 1

Definition of Incentives and Concessions

Government Code Section 65915(k):

1. A reduction in site development standards or a modification of zoning code requirements or architectural design requirements that exceed the minimum building standards approved by the California Building Standards Commission as provided in Part 2.5 (commencing with Section 18901) of Division 13 of the Health and Safety Code, including, but not limited to, a reduction in setback and square footage requirements and in the ratio of vehicular parking spaces that would otherwise be required that results in identifiable, financially sufficient, and actual cost reductions.
2. Approval of mixed-use zoning in conjunction with the housing project if commercial, office, industrial, or other land uses will reduce the cost of the housing development and if the commercial, office, industrial, or other land uses are compatible with the housing project and the existing or planned development in the area where the proposed housing project will be located.
3. Other regulatory incentives or concessions proposed by the developer or the city, county, or city and county that result in identifiable, financially sufficient, and actual cost reductions.