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PROPERTY OWNER SINGING THE "IN LIEU BLUES"; CALIFORNIA COURT OF APPEAL NOT LISTENING

The Court of Appeal for the Second Appellate District has determined that a developer's payment of an affordable housing fee "in lieu" of providing affordable onsite units does not constitute a Fifth Amendment taking, is not an exaction for purposes of the Mitigation Fee Act, and is not a special tax under the California Constitution. Instead, a court should defer to a locality's determination that an inclusionary ordinance and in-lieu fee promotes the general welfare, and need not necessarily relate to any particular development's impact on the need for affordable housing.

BACKGROUND

616 Croft Ave., LLC v. West Hollywood arose out of an approval by the City of West Hollywood ("City") of a project that demolished two single-family homes and replaced them with an 11-unit infill condominium development. The City's approval was conditioned on the developer's ("Croft") compliance with the City's inclusionary ordinance applicable to for-sale housing projects. Like many inclusionary ordinances, the City's ordinance requires developers to set aside a portion of their newly constructed units to be sold at affordable prices or, alternatively, to pay an in-lieu fee for the purpose of funding an equivalent number of affordable units if so requested by the developer. To secure the City's approval of its permits in 2005, Croft signed an affidavit pledging to pay the in-lieu fee. It also agreed that should the City's fee schedule be revised prior to obtaining the building permits, Croft would be subject to the new fees. The permits were scheduled to expire in 2007.

The City extended its approval of the permits on several occasions. During this time, the City revised its fee schedule and Croft agreed again, in writing, to be subject to the new fee as a condition of the City's permit renewal. By the time Croft finally requested its permits in 2011, the in-lieu fees it owed nearly doubled, totaling $540,393.28. Croft paid the fees "under protest" pursuant to the Mitigation Fee Act (Gov. Code, §§ 66000–66025). Croft then sued the City and lost at the trial court.

On appeal, Croft argued that the fees were invalid both on their face and as applied to Croft's project under the Takings Clause of the Fifth Amendment based on the line of cases commonly referred to as *Nollan* and *Dolan* (*Nollan v. California Coastal Comm'n.* (1987) 483 U.S. 825; *Dolan v. City of Tigard* (1994) 512 U.S. 374). Croft also argued that the City failed to carry its burden to show that the fees were reasonably related to the deleterious public impact caused by the development.

THE COURT OF APPEAL'S HOLDING

The court rejected the developer's facial challenge to the City's ordinance and fee schedule as barred under the 90-day statute of limitations set out by Government Code section 65009. The court explained that the 90-day limitation applies even if the facial challenge is part of an as-applied challenge. Regarding the as-applied challenge, the court of appeal rejected the developer's argument that the City bore the burden of proving its fee was reasonable under both the Mitigation Fee Act and the California Constitution as special taxes masquerading as fees.

The court explained that the Mitigation Fee Act applies when "a monetary exaction other than a tax or special assessment… is charged by a local agency to the applicant in connection with approval of a development project for the purpose of defraying all or a portion of the cost of public facilities related to the development project." (Gov. Code, § 66000, subd. (b).) In determining that the City's ordinance was not an exaction subject to the Mitigation Fee Act, the court relied upon a 2015 California Supreme Court decision that held a similar affordable housing provision did not constitute an exaction. (*California Building Industry Assn. v. City of San Jose* (2015) 61 Cal.4th 435, 443–444.) Instead, the *San Jose* court concluded that San Jose's ordinance, which required a number of affordable units be set aside, qualified as a land use regulation permissible within the city's broad police power. The court of appeal applied the *San Jose* court's reasoning to the in-lieu fees because the fees were a voluntary alternative to West Hollywood's housing set-aside requirement. So long as the City offers the property owner at least one means of satisfying the ordinance that does not violate the takings clause, the ordinance would be legal. Because the underlying inclusionary requirement is a constitutional regulation pursuant to the City's police power and the in-lieu fee is a voluntary option, the validity of the in-lieu fee does not depend on whether it is reasonably related to the Croft development's impact under *Nollan* and *Dolan*, and the Mitigation Fee Act is inapplicable. As a land use regulation, the fee was permissible as long as it did not constitute a physical taking or deprive Croft of a viable economic use of the property.

Consistent with other courts before it, the court of appeal further rejected Croft's argument that the fees were special taxes and that the City had the burden to demonstrate the fee's validity under the California Constitution. Citing *Terminal Plaza Corp. v. City and County of San Francisco* (1986) 177 Cal.App.3d 892, the court noted that the fees were not deposited into the general fund or used to pay for public services; did not impact general government spending; were not imposed on the land, but rather on the development; and were not compulsory, since the fees were an alternative to a set aside.

The court also rejected Croft's alternative argument that the City's municipal code required that the City demonstrate that the fee was reasonably related to the impacts of the development. The West Hollywood Municipal Code allows for the reduction or waiver of the in-lieu fee "based upon the absence of a reasonable relationship between the impact of that person's commercial or residential development project on the demand for affordable housing." The court of appeal rejected the notion that this language shifted the burden to the City to show such reasonableness without evidence that it was the City's intent to accept that burden.

Finally, the court clarified that, in light of the *San Jose* decision, the relevant inquiry was not whether the particular in-lieu fee paid by Croft was reasonably related to the development's impact on affordable housing. Instead, the question was whether the fee schedule itself, which laid out the in-lieu fee, "reasonably related to the overall availability of affordable housing in West Hollywood." Since Croft did not dispute the validity of the fee schedule, the court of appeal refused to look at whether the evidence presented demonstrated such reasonableness.

FUTURE IMPLICATIONS

Localities seeking solutions to produce affordable housing, such as onsite dedications and in-lieu fees, should make clear findings that such actions are an exercise of the police power, appropriate supporting findings, and that such actions are not pursued as fees under the Mitigation Fee Act or as special taxes under the California Constitution. Notwithstanding California law, localities may still wish to ensure inclusionary ordinances and in-lieu fees are reasonably related to the impacts of individual projects by preparing a nexus study in connection with adoption of an inclusionary ordinance, in light of Justice Thomas' interest in addressing whether broad legislative programs are subject to the *Nollan* and *Dolan* strict scrutiny standard (as expressed in his dissent from and concurrence with the Supreme Court's rejections of petitions for certiorari in *Parking Association v. City of Atlanta* (1995) 515 U.S. 1116 and *California Building Industry Assn. v. City of San Jose* (2016) 136 S. Ct. 938, respectively).

For more information on this case, inclusionary ordinances, and drafting appropriate findings, please contact Karen Tiedemann, Barbara E. Kautz, Caroline Nasella, Eric S. Phillips, Justin D. Bigelow, or any other attorney at Goldfarb & Lipman LLP at 510-836-6336.

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