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December 21, 2018

VIA E-MAIL

Amy Chan, City Manager
Cupertino City Hall
10300 Torre Ave.
Cupertino, CA 945014-3202

Re: Vallco Town Center Project—Reservation of Rights and Protest Regarding Fees

Dear Ms. Chan:

I am submitting this letter on behalf of Vallco Property Owner LLC (“Vallco”), the developer and owner of the Vallco Town Center Project (the “Project”). The Project covers the 50.82-acre Vallco Mall property that makes up the Project site. Pursuant to Government Code section 66020, this letter serves as notice of Vallco’s protest of certain fees included by the City of Cupertino (the “City”) as conditions of approval in the City’s September 21, 2018 Approval Letter for the Vallco Town Center SB 35 Project Application (the “Project Approval”).¹ In accordance with Condition of Approval #38 of the Project Approval and the Mitigation Fee Act, this letter constitutes Vallco’s protest of certain fees made within 90 days of the Project’s approval date.

Vallco’s primary protest relates to the Below Market Rate (BMR) Housing Mitigation Fee; however, unfortunately, as discussed below, the Project Approval does not specify the amount of the other fees or provide sufficient detail for our client to ascertain how these fees would be applied to the Project.

¹ Government Code section 66020 states that the protest shall be made to the “governing body.” Here, the Project was approved under SB 35, which is a ministerial approval process that requires action at a staff level based only on objective standards. Under the statute, the City Council has no approval authority. For this reason, this letter is directed to the City Manager as she has effectively been the “governing body” for purposes of the SB 35 approval and imposing fees. As with the underlying approval, neither the City Council nor any other discretionary decision-making body has any role in determining the fees. Nonetheless, to ensure transparency, we are sending a courtesy copy of the letter to the City Council.

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Vallco is therefore submitting this letter to reserve its rights to challenge the application of certain additional fees to the project. Vallco also reserves the right to file additional protest letters upon the City's subsequent determination of the amount of these fees. Furthermore, pursuant to the requirements of SB 35, the only applicable fees (and calculation practices and/or methodologies) are those in place as of March 27, 2018, the date of Vallco's Project application.

In accordance with the procedural requirements of Government Code section 66020, Vallco will tender the required payment when due under protest and will satisfy any conditions that have been imposed under protest. Vallco's compliance with any of the Project Approval requirements (including the submission of this letter) is subject to a full reservation of rights to seek all available administrative or judicial relief therefrom and to seek full restitution and refund of any amounts paid to the City in excess of what is allowed under state or federal law.

The remainder of this letter sets forth the factual elements and legal basis for the protest.

A. Protest of the BMR Housing Mitigation Fee

Vallco's concern regarding the City's BMR Housing Mitigation Fee is two-fold. First, Vallco should be afforded a full credit for the approximately 1,200,000 square feet of existing retail uses and that credit should be applied against any new use, including office. Second, the BMR Housing Mitigation Fee is based on the premise that a project impacts the need for affordable housing; however, in this circumstance, the Project includes an unprecedented 1,201 below market rate units, which will fully offset the Project-wide impacts on affordable housing demand. This reduction in impacts should be recognized when assessing the BMR Housing Mitigation Fee applicable to the Project as a whole.

A.1. Factual Background

A.1.1. Project Demolition and Development

The Project entails demolition of approximately 1,200,000 square feet of existing retail buildings. The redeveloped Project will contain approximately 430,939 square feet of new retail along with 2,402 residential units and 1,981,447 square feet of office uses. 1,201 (50%) of the residential units are to be provided as BMR units.

A.1.2. The City's BMR Housing Fee Program

The City's BMR Housing Fee is authorized by Chapter 19.172 of the Municipal Code. Administration of the program is detailed in the City's *Below Market Rate (BMR) Housing Mitigation Program Procedural Manual* (the "BMR Manual"), which was adopted by the City by resolution on May 5, 2015. The Housing Fee is premised on the purported increase in demand for affordable

housing generated by new development. The City documented this “nexus” in two studies, one study for new housing and the other study for non-residential development (collectively, the “Nexus Study”). The City’s BMR Housing Fees apply to both residential and non-residential development and are based on the square footage of new development.

A.1.3. Credit for Replacement of Demolished Square Footage

As stated in the City’s BMR Manual, the Housing Mitigation Program applies to all projects that result in an increase of gross floor area or an increase in the number of net new units. Excepted from the Mitigation Program is “new gross floor area that is replacing demolished or destroyed gross floor area.”² For instance, if an existing development is demolished and subsequently rebuilt as part of a new project, the City’s housing impact fee will only apply to the new gross square footage. This policy recognizes that fees can only legally be charged for impacts caused by development and that substituting a new building for an old building with the same square footage does not create any new impact on the need for affordable housing.

All of the existing square footage for the Project will be replaced either with new retail uses or with office or residential uses. Because the Project will remove the existing affordable housing impacts associated with approximately 1,200,000 square feet of retail, it should receive full “credit” for this existing square footage when assessing the City’s affordable housing fee in accordance with the City’s BMR Manual.

Although not stated in the conditions of approval or elsewhere, the City has taken the position that Vallco can only receive credit on a “like-for-like” basis. That is, that Vallco can only use the credit for the demolished retail for new retail uses. We strongly disagree with this position.

A.1.4. Provision of On-Site BMR Units

According to the BMR Manual, providing 15% affordable units (split between 9% very low income and 6% low income) would be equivalent to paying the BMR Housing Fee. Because 50% of the units in the Project are affordable, under the City’s policies, the additional 35% BMR units should be considered to reduce the demand for affordable housing. The City has not indicated that it would provide any credit for the additional BMR units in determining the BMR Housing Mitigation Fee.

² See BMR Manual, pp. 2, 9.

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A.2. Legal Basis for Protest of BMR Housing Mitigation Fee

As this Council appreciates, and is affirmed by case law and the Mitigation Fee Act, without an impact, there is no nexus to levy a fee. The Mitigation Fee Act requires the amount of mitigation fees to bear a reasonable relationship to the impact of the development. Consequently, the City must 1) provide a credit for the total square footage of demolished retail, even if some of the retail is being replaced by office use, and 2) provide a credit for the excess BMR units (and for the excess affordability of those units) included in the Project. Based on these factors, it is our view that Vallco should not pay any BMR Housing Mitigation fees for the Project.

A.2.1. The City's Unwritten "Like-for-Like" Policy Violates the Mitigation Fee Act

The City's unwritten "like-for-like" policy runs counter to requirements of the Mitigation Fee Act. The logic of giving credit for demolished square footage applies regardless of whether the new use is the same or different from the original use: there was an impact that is being removed and replaced, so the fee can only be levied on the net new impacts. Applying the City's BMR Manual policies, the Vallco Redevelopment Project's final housing impact fee calculation clearly exempts the 430,939 square feet of new retail from the final impact fee calculation. In addition, the BMR Manual should properly be interpreted as providing a credit for the remaining approximately 770,000 square feet of pre-existing retail space that will be demolished and redeveloped as office and residential uses. Failing to properly account for this approximately 770,000 square feet of demolished space as part of the proposed Project's housing impact fee calculation and applying the current retail square footage fee amount of \$11.88 per square foot would result in an overcharge to Sand Hill of at least \$9,147,600 that would not have a nexus to the impact. Such an overcharge would violate the Mitigation Fee Act.

Further, the actual overcharge would also exceed the above-stated amount when considering the conclusions on which the affordable housing fees are based. The Nexus Study concluded that due to lower wages earned by retail employees, retail use actually has the most significant impact on the demand for affordable housing. For example, the Nexus Study found that the average compensation for a retail/restaurant worker in Santa Clara County is approximately \$33,000 per year, whereas the average office worker earns approximately \$94,000. Although the City set the retail fee at approximately half of the office fee, this was done for the policy rationale of encouraging retail and associated tax revenues—the lower fee for retail does not reflect a lower impact. In fact, the Nexus Study found that the maximum fee the City could legally charge was approximately 72% higher than the maximum fee it could charge for office. Therefore, to properly consider the net impact on the demand for affordable housing, the City should give a credit for the additional 770,000 square feet

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based on the per square foot office rate of \$23.76, which would result in a total credit of over \$18,000,000.

A.2.2. The Mitigation Fee Act Requires the City to Consider All On-Site BMR Units When Determining the BMR Housing Mitigation Fee

When assessing the net new impact of demand for affordable housing, the City must also recognize the 1,201 below market rate units that the Project will provide. The purpose of the BMR Housing Mitigation Fee is to mitigate affordable housing demand generated by the new development. To ignore the fact that the Project will include far greater on-site affordable units than the City has determined would offset the impact of market rate units defies the basic premise of the fee and violates the requirements of the Mitigation Fee Act. Because 50% of the units in the Project are affordable to lower income households, and 15% of which are affordable to very low income households (in excess of the BMR Manual's requirement), the deeper affordability of the base 15% and the additional 35% of the units should be viewed as reducing the demand for affordable housing. Consequently, the City should reduce the fee further in recognition of the additional 35% affordable units and the deeper affordability of the base 15%.

B. Reservation of Rights to Protest Other Fees

The Project Approval contained two conditions concerning development fees. Condition 6 provides the following:

FEES

The Applicant shall pay all applicable fees, taxes and bonds per the City's adopted fee schedule and/ or Municipal Code, at the time of building permit issuance including, but not limited to:

- a. Building Permit Fees
- b. Third -party Consultant Costs plus any administration fees
- C. Below Market Rate Housing Mitigation Fees
- d. Transportation Impact Fees
- e. Parkland Dedication Fees
- f. Storm Drain Fees

And Condition 38 provides, in full:

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NOTICE OF FEES, DEDICATIONS, RESERVATIONS OR OTHER EXACTIONS

The determination set forth herein may include certain fees, dedication requirements, reservation requirements, and other exactions. Pursuant to Government Code Section 66020(d)(1), these notes constitute written notice of a statement of the amount of such fees, and a description of the dedications, reservations, and other exactions. The Applicant is hereby notified that the 90 -day approval period in which these fees, dedications, reservations, and other exactions, may be protested pursuant to Government Code Section 66020(a) begins as of the date of project approval. If the Applicant fails to file a protest within this 90 -day period complying with all of the requirements of Section 66020, the Applicant will be legally barred from later challenging such exactions.

Contrary to the City's assertion in Condition 38 that it has provided "written notice of a statement of the amount of such fees, and a description of the dedications, reservations, and other exactions," nowhere in the Project Approvals has the City specified the amount of fees to be paid. Instead, the fee related conditions are vague and open ended and do not specify the fee amounts.

As a precondition of imposing a fee, the Mitigation Fee Act requires local agencies to provide a statement specifying the amount of the fee.³ The City has not done that here. Therefore, the 90-day period to protest a fee on a development project under Government Code section 66020 has not yet begun and Condition 38 of the Project Approval is without effect with respect to any of the fees described in Condition 6.

With regard to the Parkland Dedication Fees, Vallco's understanding is that the City does not charge fees based on the City's practice the Project will be determined to contain sufficient (if not an excess of) dedicated parkland that no fee will be required. But because the City has not yet determined the amount of any fees, we reserve the right to protest the Parkland Dedication Fee along with other yet-to-be imposed fees including the Transportation Impact Fees and Storm Drain Fees. We further reserve the right to supplement these comments at the time the actual fee amounts are identified.

C. Conclusions

Based on the foregoing, Vallco requests the following from the City:

- 1.) Written confirmation that in imposing the Affordable Housing Fee, the City will fully credit Vallco for (i) all demolished retail and not limit the credit to "like-for-like" replacement and (ii) all excess BMR units and affordability levels.

³ Gov't Code §§ 66001(b), 66020(d)(1).

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& Bass LLP

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- 2.) Written confirmation that the open space provided by the Project satisfies the Parkland Dedication requirements and, while the parties will collaborate to determine the location and nature of dedication, no Parkland Dedication Fee will be imposed.
- 3.) Written confirmation that the City can only impose the Affordable Housing Fees (if any), the Transportation Impact Fees, and the Storm Drain Fees (and there were no other fees in place as of March 27, 2018) and thus has not yet imposed these fees in accordance with the Mitigation Fee Act; revision of Condition 38 in accordance with this acknowledgement; and acknowledgement of Vallco's right to challenge those fees when they are imposed.
- 4.) A statement of the amount of the other fees to be imposed.

Thank you for your consideration of these matters.

Sincerely,



Miles Imwalle

CC: Mayor Scharf and Members of the City Council
Aarti Shrivastava, Assistant City Manager
Rocio Fiero, Acting City Attorney
Timm Borden, Director of Public Works
Reed Moulds, Vallco Property Owner LLC