



Impact of Recent Changes to the Surplus Land Act

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IMPACT OF RECENT CHANGES TO THE SURPLUS LAND ACT

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Introduction

The availability and affordability of land for development has a significant impact on the supply of affordable housing. The aim of the Surplus Land Act (the "Act") is to increase the availability of real property in California for affordable housing development by requiring the prioritization of affordable housing when selling or leasing public lands no longer necessary for agency use. Government Code § 54220 *et seq.* "The Surplus Land Act advances state land use policy objectives by mandating a uniform approach to the disposition of local government land that is no longer needed for government use. . . .[T]he statute addresses the shortage of sites available for affordable housing development as a matter of statewide concern." *Anderson v. City of San Jose* (2019) 42 Cal.App.5th 683, at 693. In recent years, the applicability and efficacy of the Act, originally enacted in 1968, has been addressed and adjusted through case law and legislative amendments.

In 2014, AB 2135 added Government Code Section 54222.5. Under this provision, when the local agency issues a notice of availability and an interested party responds to develop housing on the site for low- and moderate-income households, at least 25% of the proposed development must be income restricted for lower income households. This bill also added Section 54233, which requires that if the property is not successfully sold or leased during the defined 90-day negotiation process, the land is sold or leased outside of the scope of the Act, and at least 10 residential units are developed on the property, at least 15% of the units must be income restricted for lower income households.

In 2019, the Sixth District Court of Appeal addressed the applicability of the Act, holding that the Act applies to both charter and general law cities. *Anderson v. City of San Jose* (2019). The inquiry concerning the applicability of the Act to charter cities arose out of the state constitutional grant of power known as "home rule." Under home rule, charter cities maintain "sovereignty over municipal affairs." While recognizing the municipal interest in disposing of surplus government property, the District Court concluded that "the well-documented shortage of sites for low- and moderate-income housing and the regional spillover effects of insufficient housing demonstrate 'extramunicipal concerns' justifying statewide application of the Act's affordable housing priorities." Additionally, the District Court concluded that the Act is sufficiently tailored to avoid unnecessary interference with local government because a charter city still maintains discretion over certain aspects, such as whether the land is deemed surplus and the price of the land, and the city is not required to sell the property to any particular buyer.

In 2019, the legislature extensively revised the Act through the adoption of AB 1486. In addition to other revisions, AB 1486 defines or redefines the scope of the following:

1. expanding the definition of local agencies subject to the Act to include joint powers authorities, redevelopment successor agencies, housing authorities, other political subdivisions of the state and any instrumentality of those agencies that is empowered to acquire and hold real property;
2. expanding the definition of what constitutes surplus land to, among others, include former redevelopment agency properties;

3. limiting what constitutes agency use of property to explicitly disallow commercial or other revenue generating uses;
4. narrowly defining exempt surplus land;
5. adding requirements that public agencies must make findings that property is either exempt surplus land or surplus land before beginning negotiations for disposition;
6. adding penalties for disposing of surplus land in violation of the Act that increase with multiple violations.

The 2019 amendments also targeted transparency of information. For example, AB 1486 requires the Department of Housing and Community Development ("HCD") to maintain a listing of all of the notices of available surplus lands throughout the state. AB 1255, enacted in 2020, expanded the central inventory requirement in Section 54230 to include both cities and counties, added additional information requirements for the central inventory, made the information a matter of public record, and requires that the information be reported to HCD annually.

The revised Act as of 2021 broadens the scope of public land made available for affordable housing and reforms standardized inventories of available public land and entities that should receive notice. However, the Act also imposes the regulatory process on sites that are not appropriate for housing and the efficacy is limited by the realities of affordable housing financing and contract negotiations. This paper will summarize the requirements under the Act as provided in the statute and as interpreted by the HCD Surplus Land Act Guidelines (the "Guidelines"). It will further analyze the potential efficacy of the Act, as amended and as interpreted by HCD, in promoting the disposition and proper use of surplus land and the development of affordable housing. This paper focuses on the disposition of land for the purpose of developing affordable housing, but there are also provisions of the Act for disposing of land for open-space and use by a school district.

Surplus Land Act Today

Statute and HCD Guidelines Summary

The Act regulates both how local agencies dispose of and inventory real property owned in fee simple by the local agency that is no longer necessary for agency use (the surplus land). Local agencies include "every city, whether organized under general law or by charter, county, city and county, district, including school, sewer, water, utility, and local and regional park districts of any kind or class, joint powers authority, successor agency to a former redevelopment agency, housing authority, or other political subdivision of this state and any instrumentality thereof that is empowered to acquire and hold real property." Government Code § 54221(a)(1).

Land Disposition Under the Act. Generally, under the Act, there are three types of land: land necessary for agency use, land no longer necessary for agency use but exempt from most provisions of the Act ("exempt surplus land"), and land no longer necessary for agency use that is not exempt ("surplus land"). The Act defines "agency use" to include land being used or land with a planned use as evidenced by an adopted written plan. Agency use as defined excludes commercial or industrial uses and activities, including nongovernmental retail, entertainment, or

office development, and property disposed of for "the sole purpose of investment or generation of revenue." Government Code § 54221(c).

When the land is not necessary for agency use, prior to any action towards disposition, the local agency must declare the land as either surplus or exempt surplus land at a regular, public meeting. "Disposition" includes the sale or lease of land. However, "disposition" excludes leases if the land is leased for less than five years or if development or demolition will not occur. HCD Surplus Land Act Guidelines § 102(h)(1), April 2021. The decision that the land is either surplus or exempt surplus must be supported by written findings. A copy of the written findings for an exemption must be sent to HCD by the local agency at least 30 days before a sale or lease of the land. While this declaration must be made before an action towards disposition, there are some actions a local agency can take prior to declaring the land surplus or exempt surplus including commissioning appraisals, exercising due diligence, and conducting studies to determine the best use of the property. Government Code § 54222(f).

If the proposed use of the property meets the requirements under Section 54221(f)(1) and the local agency declares the land as exempt surplus, the disposition is not subject to additional requirements under the Act. There are eleven exemptions. For example, land that is subject to a valid legal restriction prohibiting housing that is not imposed by the local agency is exempt surplus land. Government Code § 54221(f)(1)(H). Another exemption applies when a site is put out for open, competitive bid for one of two types of development. One eligible development is a housing development in which 100% of the units are affordable to low- or moderate-income households for 55 years for rental units and 45 years for ownership units. At least 75% of the units must be restricted to lower income households. Alternatively, a site would qualify as exempt surplus land if the purpose of the disposition is to develop a mixed-use development on a site larger than one acre that consists of at least 300 housing units, 25% of which are restricted to lower income households for 55 years for rental units and 45 years for ownership units. Notably, this exemption still requires that the local agency invite local public entities within the site's jurisdiction and "housing sponsors" (defined in Health and Safety Code § 50074) to submit a bid prior to disposition. Government Code § 54221(f)(1)(F), (G).

When land is no longer necessary for agency use and does not qualify for an exemption, the local agency is required to declare the land as surplus. Once a local agency declares land is surplus, it must send the notice of availability ("NOA") to local public entities within the site's jurisdiction, "housing sponsors," and HCD, noting that the land can be used "for the purpose of developing low- and moderate-income housing." Government Code § 54222. The Guidelines state that the notice of availability should be in the form provided by HCD. HCD Surplus Land Act Guidelines § 201, April 2021. The form includes requests for the site information, the local agency's minimum asking price (if any), the property value at the most recent appraisal, and other information the local entity wants to convey about the site. This may include reasonable conditions or restrictions since one of the grounds listed in the Guidelines for a local agency to reject an offer includes when the "interested entity is not responsive to a local agency's reasonable conditions or restrictions as described in the NOA. . .and such conditions and restrictions are reviewed by HCD." Guidelines § 202(b)((4)(C).

The next steps depend on the receipt of a notice of interest and the success of the negotiations. If the local agency receives a notice of interest within 60 days of the issuance of the notice of

availability, it must engage in good faith negotiations with the responding party for at least a 90-day period. The HCD Guidelines provide that the 90-day negotiation period begins the first day after 60-day period to receive notice of interests expires, even if responses are received prior to the expiration of the full 60 days. Guidelines § 202(a)(1)(B). Parties responding to the notice of availability must propose a residential development for low- and moderate-income households that restricts at least 25% of the total number of units developed on the parcel to be affordable to lower income households. If the local agency receives multiple notices of interest to purchase or lease the land, the local agency may enter concurrent negotiations with responding parties. However, the Act regulates the order of priority based on which interested party proposes the greatest number of units affordable to low- and moderate-income households. If parties offer the same number of affordable units, priority is determined based on the proposal with the "deepest average level of affordability for the affordable units." Government Code §§ 54222.5, 54227(a). The local agency disposing of property must notify HCD after the negotiations and prior to the sale or lease of the property of the details of the negotiation on a form provided by HCD. When a local agency opts to sell or lease the property to a party that does not have priority, the proposed disposition summary to HCD must include "an adequate written explanation." Guidelines § 400(b)(3).

Land Disposition Outside of the Act. The local agency can still sell or lease the surplus property if it does not receive any notices of interest within 60 days of issuing the notice of availability or if the negotiations with interested parties fail. Generally, this disposition falls outside of the scope of the Act, but Government Code Section 54233 provides that if 10 or more residential units are proposed on a site, at least 15 percent of the total number of residential units developed on the site must be restricted to lower income households, and that a covenant be recorded on the property to this effect.

Districts. Some elements of the Act differ for districts in relation to other local agencies. For example, for districts that are not supplying public transportation, agency use may include commercial or industrial uses or activities, or property disposed of for the sole purpose of investment or generation of revenue. In order to qualify as an agency use, the district must take an action at a public meeting to declare that the use will either "directly further the express purpose of agency work or operations;" or is "expressly authorized by a statute governing the local agency." Government Code § 54221(c)(2)(B).

Inventory. Counties and cities are required to make a central inventory by December 31 of each year including surplus land and land in excess of foreseeable needs in the jurisdictions' urbanized areas and urban clusters. The property description and present use must be reported to HCD by April 1 of each year. This inventory requirement is only applicable to cities and counties. Government Code § 54230.

Greater Statutory Framework

Housing Authorities. The amendments to the Act expanded the definition of "local agency" to include a variety of local agencies including housing authorities. Housing authorities are created and governed by the California Housing Authorities Law (Health and Safety Code §§ 34200 *et seq.*) The Housing Authorities Law sets out the powers and authorities of housing authorities and governs various aspects of the operation of housing authorities.

Health and Safety Code Section 34312.3(b) grants housing authorities the power to sell, lease or otherwise dispose of real property without complying with any provision of law concerning disposition of surplus property if the proceeds of the sale or lease, net of the cost of sale, are used directly to assist a housing project for persons of low income. A housing authority relying upon Health and Safety Code Section 34312.3 for purposes of property disposition is required to hold a public hearing before disposing of the property. The public hearing is the only procedural requirement for disposition of property pursuant to Section 34312.3(b).

The explicit language of Health and Safety Code Section 34312.3 is consistent with Government Code Section 54226, which states that no provision of the Act will be applied when it conflicts with any other provision of statutory law. Given that housing authorities are generally charged with creating and providing housing for low-income households, in most instances, when a housing authority is disposing of property it is likely to fall under Health and Safety Code Section 34312.3(b) and thus not be subject to the Act.

In addition to Health and Safety Code Section 34312.3, the Housing Authorities Law provides a priority for disposition of property no longer needed that emphasizes the use of the property for affordable housing. Health and Safety Code Section 34315.7 requires that housing authorities first dispose of property that is not disposed in accordance with Health and Safety Code Section 34312.3 for purposes consistent with Government Code Section 50568 (discussed below), to developers for the development of low- and moderate-income housing, to developers for market rate housing and then finally at public auction to the highest bidder. HCD is required to adopt regulations governing the disposing of property by housing authorities, but no regulations have been adopted since Health and Safety Code Section 34315.7 was adopted in 1980. The specificity of the Housing Authorities Law regarding disposition of surplus property presents an argument that the Housing Authorities Law conflicts with and therefore overrides the Act.

Surplus Real Property Act. The Surplus Real Property Act (Government Code §§ 50568 *et seq.*) provides another alternative for disposition of property. Government Code Section 50570 explicitly overrides the Act if a local agency leases or sells real property to a specific subset of nonprofits for the purposes of housing for low- and moderate-income households. The entities allowed to acquire property under this statute include limited dividend housing corporation, nonprofits formed exclusively to provide housing for low- and moderate-income households and housing corporations organized pursuant to the Community Land Chest Law. The deed or lease disposing of property pursuant to the Surplus Real Property Act must provide that the ownership of the property reverts to the local agency when the majority ownership interest of the land is no longer held by an eligible entity. A local agency using the Surplus Real Property Act must hold a public hearing before transferring the property and make findings that the transfer complies with the statutory requirements.

Government Code §§ 25539.4 and 37364. Exempt surplus property under the Act includes a property that is disposed of pursuant to either Government Code Section 25539.4 or Section 37364, which provide similar disposition processes for counties (Section 25539.4) and cities (Section 37364). Cities and counties may sell property at less than fair market value if the city or county determines that the property can be used to provide housing to low- and moderate-income households. To qualify for disposition pursuant to Sections 25539.4 and 37364, at least 80% of the property disposed of must be used for the development of housing and at least 40% of the

total number of units developed on any parcel must be affordable to households whose incomes are equal to or less than 60% of area median income and at least 1/2 of those units must be affordable to very low-income households. The affordable units developed must be restricted by a regulatory agreement with a term of at least 30 years.

Using Section 25539.4 or Section 37364 for the disposition of larger properties poses some challenges. The statutes are explicit that at least 80% of the area of any parcel of property disposed of must be used for the development of housing and that 40% of the units developed on any parcel must be affordable; however, parcel is not defined. If the local agency disposes of the property as a single parcel and the developer subdivides the property into multiple parcels to create parcels that are developed 100% with affordable housing and 100% with market rate housing, has the intent of the statute been met if the overall development complies with the 40% affordable requirement? Given that most affordable housing financing requires separate parcels for affordable development, any mixed-use development faces challenges under these statutes. To date, there are no cases interpreting these statutes.

Economic Development Conveyances. Legislation enacted in the wake of the dissolution of redevelopment agencies sets forth processes and procedures for local agencies to increase jobs, create economic opportunity, and generate tax revenue for all levels of government and to inform the public before approving specified economic development subsidies. Notably, these procedures are substantially similar to the procedures previously relied on by redevelopment agencies.

In adopting Government Code Sections 52200 *et seq.*, the Legislature declared: (1) “whenever the creation of economic opportunity in cities and counties cannot be accomplished by private enterprise alone, without public participation and assistance in the acquisition of land, in planning and in the financing of land assembly, in the work of clearance, and in the making of improvements necessary therefor, *it is in the public interest to advance or expend public funds for these purposes*, and to provide a means by which economic opportunity can be created;” and (2) “that *the creation of economic opportunity* and the provisions for appropriate continuing land use and construction policies with respect to property acquired, in whole or in part, for economic opportunity *constitute public uses and purposes* for which public money may be advanced or expended and private property acquired, and are governmental functions of state concern in the interest of health, safety, and welfare of the people of the state and cities and counties” Government Code §§ 52200.4(b) and (c), emphasis added. Economic opportunities in the legislation include:

1. Development agreements or other agreements that create, retain, or expand new jobs, in which the legislative body finds that the agreement will create or retain at least one full-time equivalent, permanent job for every \$35,000 of local agency investment in the project after full capacity and implementation.
2. Development agreements that increase property tax revenues to all property tax collecting entities, in which the legislative body finds that the agreement will result in an increase of at least 15% of total property tax resulting from the project at full implementation when compared to the year prior to the property being acquired by the local agency.

3. Creation of affordable housing, if a demonstrated affordable housing need exists in the community, as defined in the approved housing element or regional housing needs assessment.
4. Projects that meet the green-house gas reduction goals set forth in SB 375 and have been included in an adopted sustainable communities' strategy or alternative planning strategy or a project that specifically implements the goals of those adopted plans.
5. Transit priority projects, as defined in Section 21155 of the Public Resources Code.

Government Code Section 52201 also sets out procedural requirements for sale or lease of properties for an economic opportunity. Specifically, Government Code Section 52201 requires that before property is sold or leased for an economic opportunity, the sale or lease shall first be approved by the legislative body by resolution after a noticed public hearing (with notice of hearing published in a newspaper of general circulation once a week for at least two successive weeks prior to the hearing with at least a 5-day gap between publications). In addition, at the time of the first publication, the city must make available for inspection the transfer document (lease or sale agreement) and a report summarizing the details of the transaction, the estimated value of the interest to be leased or conveyed, determined at the highest and best uses permitted under the general plan or zoning. In addition, the report must include an explanation of why the sale or lease of the property will assist in the creation of economic opportunity, with reference to all supporting facts and materials relied upon in making this explanation. This property disposition process mirrors the process that governed disposition of property by redevelopment agencies.

Notably, Government Code Section 52200.6 provides that the economic opportunity process is an alternative to any authority of a city, county or city and county to create an economic opportunity to sell or lease property for economic development, found in the Constitution, state law, local ordinance or charter but then goes on to state that the economic opportunity statutes do not limit or in any way affect the application of any other such laws. The language in this section appears contradictory and leaves open the question of whether a conveyance of property for an economic opportunity as defined in the Government Code that complies with the procedures set forth in Section 52201 conflicts with the Act making the Act inapplicable under Section 54226. Arguments can be made that nothing in Government Code Section 52201 prevents a local agency from complying with the requirements to offer the property to housing providers since those requirements are procedural and Government Code Section 52201 focuses on the final use of the property. However, it is unlikely that property used for affordable housing is going to meet the definition of economic opportunity, except for the creation of affordable housing given the tax-exempt status of most affordable housing. So, there is a potential argument that the statutes conflict and thus the Act does not apply to properties disposed of for an economic opportunity.

Risk of Getting it Wrong

Prior to AB 1486, there were no specific penalties for failure to comply with the Act. Now, the Act includes a penalty provision that requires the local agency to deposit 30% of the purchase price received in a fund to provide low-income housing for the first violation of the Act and 50%

of the purchase price received for any violation thereafter. Government Code § 54230.5. HCD can assess the penalty if the local agency has not corrected a violation after being given 60 days to cure or correct the violation. However, the violation of the Act does not invalidate the transfer or conveyance of the real property. Government Code § 54230.6.

Government Code Section 54220.5 requires a local agency to provide HCD with a description of the notices of availability, the negotiations conducted with negotiating agencies, and a copy of any restrictions recorded against the property prior to disposition of surplus land. A penalty is only allowed if HCD notifies the local agency of a violation within 30 days of receiving the required notices from the local agency. Government Code § 54230.5(b). If HCD provides a notice of violation, the local agency must have at least 60 days to respond before HCD can impose penalties. The local agency can respond by correcting the violation or providing HCD with findings explaining the reasons its process for disposing of the land complies with the Act. The failure to provide the required notices does not invalidate the transfer or conveyance of the real property.

If a local agency is assessed a fine, the amount of the fine must be deposited into a local housing trust fund and spent within five years of deposit for purposes of financing new affordable housing units within the same jurisdiction as the surplus land. If the fines are not spent within five years, the funds are then deposited into the State Building Homes and Jobs Trust Fund or the Housing Rehabilitation Loan Fund and can only be used to finance affordable housing in the local jurisdiction where the surplus land is located.

The Guidelines also require that local agencies provide HCD with copies of any resolution determining that the property is exempt from the Act at least 30 days prior to the disposition, although this is not a requirement of the Act. The resolution must include written findings supporting the declaration. Guidelines Section 400(e). Section 54222.3 states that the Act does not apply to the disposal of exempt surplus land, so it is unclear what authority HCD has to review determinations of exempt surplus land. The Guidelines do not make clear whether HCD believes that it can assess penalties if it disagrees with a determination that a property is exempt surplus property.

Efficacy of the Surplus Land Act

The amendments to the Act are designed to provide opportunities for public land to be used for affordable housing. At a time when the state is facing a severe housing crisis the goals of the amendments are laudable but fail to consider the realities of how public agencies use and dispose of real property. Additionally, at a time when the state has also significantly limited cities' ability to address economic development needs, the broad-brush approach of the amendments serves to deprive cities of yet one more economic development tool. Following on the dissolution of redevelopment agencies, this approach leaves many cities with few options for developing balanced communities that address not only the housing needs of the community but also the need for jobs and services.

Application to Former Redevelopment Sites

The inclusion of former redevelopment agency properties in the definition of surplus property also removes the one remaining asset that survived redevelopment dissolution and directly contradicts the requirements of the redevelopment dissolution statutes. Under the dissolution statutes, properties covered by the long-range property management plans were designated either to be transferred to another public agency for government use, to be sold expeditiously for the maximum value or to be held by the city for future development consistent with the redevelopment plan. Properties that were designated for sale and future development are subject to the Act. However, the Act does not create an expeditious sales process, nor does it emphasize sale for the maximum value. Properties held for future development consistent with the redevelopment plan may be designated for non-residential uses in the redevelopment plan, yet the Act would require that these properties be offered for affordable housing.

Application to Former Military Bases

The amendments also fail to consider real world examples of property disposition that are not well suited to the Act's process or requirements. Many communities in California have closed military bases covering hundreds or thousands of acres of property. Cities and counties obtained title to these properties pursuant to the Base Realignment and Closure Act that provided opportunities for local communities to receive title to the former military property either as a public benefit conveyance, which requires that the property be used for public uses, or economic development conveyances. The purpose of the economic development conveyance is to provide communities that suffer the often devastating economic impacts of base closure the opportunity to reuse the property for job and revenue generating uses to allow the local community to recover from the base closure. As part of the base closure and land conveyance process, properties at former military bases are required to be offered to homeless providers first before property is conveyed to the local jurisdiction. So, for most closed bases, a process similar to the Act's requirements has already occurred, and many bases contain a significant number of sites devoted to homeless and affordable housing. However, there is now an argument to be made that the amendments to the Act would apply to the disposition of former base properties. Offering the properties for affordable housing purposes in many instances contradicts the base reuse plans that are approved by the federal government as a condition of the conveyance of the property to the local jurisdiction.

Because most former military base property is conveyed to the local jurisdiction pursuant to the federal statutes that govern base closure and because the property is subject to a recorded agreement between the applicable branch of the military and the local government, there is an argument that can be made that Section 54226 (which states that no provision of the Act shall apply when it conflicts with any other provision of statutory law) would exempt most former base properties. However, HCD at least initially appears to disagree with this position.

The amendments to the Act also limit options for base closure communities to implement interim uses of former base property. Many closed bases have 20- or 30-year timelines for reuse to account for absorption rates and development cycles. Interim leasing of former military buildings provides an option for short term benefits while the development process proceeds. Many closed bases have successful lease programs that not only provide economic benefits but

also prevent the abandoned military buildings from further deteriorating. For example, the City of Alameda has successfully leased many former Navy hangers to create what is known through the Bay Area as Spirit Alley with brew pubs, wineries, distillers and other users. As these leases come up for renewal and base closure communities consider interim uses of existing buildings, these communities will be forced to adhere to the Act's requirements before leasing property, unless the term of the lease is less than 5 years or no development or demolition will occur. Because the HCD Guidelines do not define development, cities are left to determine whether tenant improvements constitute development. This is an open question that begs for quick resolution.

Existing Agreements

Government Code Section 54234 of the Act provides exemptions for certain transactions that were already contemplated at the time that the amendments to the Act were enacted. If a local agency entered into an exclusive negotiating agreement with a prospective buyer or lessee or other legally binding agreement as of September 30, 2019 the amendments to the Act do not apply if the disposition of the property is completed no later than December 31, 2022. For former redevelopment agency properties, whether held in the Property Trust Fund or covered by a long-range property management plan, the amendments do not apply if an exclusive negotiating rights agreement with a prospective buyer or lessee or other legally binding agreement is entered into no later than December 31, 2020 and the land is disposed of no later than December 31, 2022. If the disposition or contemplated development is challenged in court, the dates for disposition are extended to the date that is six months following the conclusion of the litigation.

Currently both Anaheim and Santa Monica are involved in disputes regarding the interpretation of these provisions. Santa Monica entered into an exclusive negotiating rights agreement with a developer in 2015 with a developer for a 3-acre site. The exclusive negotiating agreement expired in 2015 and was not renewed but the parties continued to informally negotiate. In July 2020 the City Council authorized staff to engage in formal negotiations with the same developer. A citizens group opposed to the proposed development challenged the City's action restarting negotiations on the basis that the City failed to comply with the Act. The developer sought guidance from HCD and received a letter from HCD which found that a written agreement is not required to meet the requirements of Section 54234 and that the oral exclusive negotiating agreement was sufficient to meet the requirements. The citizens group is challenging the City's disposition in court.

In Anaheim, HCD has challenged the city's disposition of the Angels Stadium property. HCD's initial determination was that the Act as amended applied to the disposition although the agreement in Anaheim was entered into in December 2019 before the amendments to the Act were effective. HCD's position is that application of the amendments to the Act, which became effective January 1, 2020, to an agreement entered into in December 2019 is a permissible retroactive application of the statute. This position appears to be based on the language in Section 54234 that exempts certain transactions if there was a legally binding agreement entered into as of September 30, 2019. HCD argues that this language evidences sufficient legislative intent to make the statute retroactive in all other circumstances.

HCD also asserts that the Stadium property is not exempt, even though the property is subject to a legally binding agreement that restricts the use of the property. Section 54221(f)(1)(G) exempts property that is subject to a valid legal restriction that prohibits housing that is not imposed by the local agency. The City has argued that the lease, which has been in place in one form or another since 1966, limits the use of the property to uses that prohibit housing. HCD has taken the position that the lease is a voluntary agreement entered into by the City and thus the restriction is imposed by the City. HCD appears to ignore that the lease is a two-party agreement, and the lessee has rights under the lease. The City of Anaheim is contesting HCD's preliminary findings.

The amendments to the Act fail completely to address multi-phased disposition agreements that may have disposition dates that extend beyond the outside dates for disposition in Section 54234. Many redevelopment agency dispositions and development agreements provided for phased disposition over the course of years or decades. The developers in these agreements rely upon commitments in the disposition and development agreement in proceeding with each phase of the project. A strict reading of Section 54234 would mean that these long-term agreements would be in jeopardy if the property was not fully disposed of by December 31, 2022. Such a reading would result in an impairment of contract that is unlikely to withstand court challenge, but to date is untested.

Contract Negotiations

The Guidelines limit a local agency's ability to reject an offer for the following reasons:

1. A local agency and purchaser/lessee cannot agree on sales price or lease terms.
2. When priority is given to a competing offer that includes a greater number of affordable units or, in case of a tie in the number of units, the lowest average level of affordability consistent with Government Code Section 54222.5; or
3. When the interested entity is not responsive to a local agency's reasonable conditions or restrictions as described in the NOA as reviewed by HCD.

Notably, the Guidelines fail to effectively reflect the amendment to Government Code Section 54233 which clarifies that the parties must come to mutually satisfactory sales price and *terms* or lease terms. Sales terms, in addition to price, are integral to disposition but are not identified in the Guidelines as a reason to reject an offer. The Guidelines' constraint on a local agency's ability to accept or reject an offer does not reflect the reality of land sales. In negotiating contracts, a local agency must also have the ability to reject bids due to other terms such as hazardous materials obligations, liability sharing, title concerns, or the proposed development schedule. While the Guidelines fail to sufficiently take the role of sale terms into account, both the Act and the Guidelines are clear that the local agency is not required to sell or lease the property for less than fair market value. Government Code § 54226; Guidelines § 202(a)(2)(C). The Act and Guidelines require local agencies to prioritize affordable housing development when disposing of surplus property, but these regulations do not require the local agency to enter into an agreement in which it does not agree with the price. The parties are required to engage in “good faith negotiations” which the Guidelines define as dealing “honestly and fairly with the

other party throughout the negotiation process whether or not the negotiation results in a contract.” Guidelines § 102(m). If the local agency and interested party fail to agree to a sale or lease price, then the negotiations can fail at the expiration of the 90-day good-faith negotiation period, and the local agency will still be in compliance with the Act. Failure to enter into an agreement with an interested party is not evidence of bad faith negotiations in itself. While it is not clearly defined how "priority" is expressed in contract negotiations, the Guidelines require the local agency to provide HCD "an adequate written explanation" if it opts to dispose the property to an entity that does not have first priority. Guidelines § 400(b)(3). The standards of an adequate written explanation are not defined in the Guidelines.

Good faith negotiations are also referenced in the Guidelines with regards to following the proposed negotiation timeline: "minor departures from this sample do not constitute per se bad faith, and differences in the timeline may be justified with prior notice to HCD." It is not clear when HCD would intervene if HCD disagrees with the variation in the timeline. Nor is it clear what the standards are for a "minor departure." Guidelines § 202(a)(1)(F).

Promoting Housing Affordability and Integration

The Act requires that at least 25% of the units developed on the surplus property disposed of for affordable housing be affordable to lower income households. Although the language of the statute promotes integration of affordable and market rate housing, the realities of financing affordable housing almost ensure that any surplus property disposed of for affordable housing will either have to be subdivided or will have to be 100% affordable in order to access the full complement of public funding sources, including low-income housing tax credits. In some instances, developers have approached cities for approval to build the required affordable units off site and use the entire surplus property for market rate housing. The Act does not appear to allow for an off-site option since the Act and the Guidelines both state that not less than 25% of the total units developed on the parcel are to be affordable. Development of the affordable units off site might achieve the same goals of the Act and provide additional flexibility for both cities and developers. However, the risk of penalties is too great for cities to allow off site affordable units without either legislative amendments or guidance from HCD.

Further, it is HCD's position that even if the surplus land is subdivided, the recorded covenant cannot be released from any of the parcels disposed of under the Act until the relevant term has run (55 years for rental housing, 45 years for ownership). HCD requires local agencies' affordability restrictions be in the "form prescribed by HCD." The current HCD form covenant limits the local agencies' ability to impose thoughtful, project specific assurances that the affordable housing will be developed and that the overall project will be financeable. It is currently unclear how much local agencies can revise the form so that it would still be acceptable to HCD. However, as currently published, the form covenant is a paragraph that merely describes the 15 percent affordability requirement provided in the Act.

Proposed Changes to the Surplus Land Act

Several bills are pending in the Legislature making further amendments to the Act. Assembly Member Ting is sponsoring AB 1271, which is now a two-year bill, that would include an exemption from the Act for military base properties and other properties greater than 5 acres as

long as the development proposals for the property includes at least 1,200 housing units and at least 25% of those units are affordable to lower income households. AB 1271 also includes a metering requirement if the proposed development includes commercial that would require that every time 25% of the commercial development is complete, at least 25% of the affordable units must be available for occupancy. The Ting bill was challenged by labor union interests that wanted a skilled workforce requirement for the exemption, resulting in the bill being put on hold until next year. It is not clear whether AB 1271 will be taken up again when the legislative session continues in 2022.

SB 719 provides a limited exemption from the Act for the disposition of property at the former Tustin Air Force Base as long as at least 20% of the housing units developer are affordable to low- and moderate-income households and 15% of the units are affordable to lower income households. SB 719 appears to also be a two-year bill and is not proceeding to a vote in the 2021 session.

SB 791 would establish the California Surplus Land Unit within HCD for the purpose of facilitating development and construction of housing on surplus land. The unit would provide advice, technical assistances and facilitate agreements between housing developers and local agencies that are disposing of surplus land. The unit would also work with other state financing agencies, such as CalHFA and TCAC to assist housing developers in obtaining funding for construction of housing on surplus lands.

AB 1180, which was enacted July 2021, expands the definition of exempt surplus land to include land transferred by a local agency to a federally recognized California Indian tribe. This bill will go into effect January 1, 2022.

Conclusion

Although the amendments to the Act are intended to encourage the development of affordable housing on property no longer needed for public use, the broad sweep of the amendments to the Act has also resulted in public agencies having limited flexibility to address their myriad of needs and goals with the use of public land. The amendments have resulted in confusion regarding how the amended Act interacts with other statutes such as the redevelopment dissolution law, laws pertaining to economic development, and military base closure laws. Additionally, although the Act makes clear that it does not usurp local agencies' land use authority, certain provisions in the Act limit local agencies' ability to include in the terms of any sale or lease requirements regarding uses that would prohibit or limit residential uses, requiring careful navigation between the local agency's regulatory and proprietary functions.

The HCD Guidelines impose additional burdens on local agencies, including requirements to use HCD forms for notices of availability and covenants restricting use of property disposed of after completion of the Act's process and adding additional reporting requirements. The many requirements in the Act can result in significant staff time ensuring compliance. Given the relative novelty of the amendments, it is yet to be determined how effective the Act is in fostering the development of more affordable housing. Additional supply of land should support the development of affordable housing, however, although available land is one barrier to the

creation of affordable housing, without sufficient sources of financing, land alone cannot solve the State's housing crisis.