



# STAFF REPORT

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December 13, 2023

File Number 0170-12; 0600-10; A-3489

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## SUBJECT

**SETTLEMENT OF TOUCHSTONE LITIGATION AND FIRST AMENDMENT TO PURCHASE AND SALE AGREEMENT FOR MUNICIPAL PARKING LOT #1 PROJECT**

## DEPARTMENT

City Attorney's Office

## RECOMMENDATION

Request the City Council Approve Resolution No. 2023-164 to (1) authorize the settlement of the litigation titled *Touchstone MF Fund I, LLC v. City of Escondido*; and (2) approve the First Amendment to Purchase & Sale Agreement.

Staff Recommendation: Approval (City Attorney's Office: Michael R. McGuinness, City Attorney)

Presenter: Michael R. McGuinness, City Attorney

## FISCAL ANALYSIS

At this time, the City Council is only being asked to approve a settlement of the Lawsuit (described in detail below) and First Amendment to the Purchase & Sale Agreement with Touchstone MF Fund I, LLC. The City Council is not being asked to, and may not, consider any particular new project for the site or the value to the City of any such new project as part of this agenda item. If the City Council approves this settlement, future site-related matters will come to it for consideration including a new application for development of the property and Development Agreement.

The specific value of the Lawsuit settlement is difficult to identify but the damages alleged in the action and potential recoverable attorney's fees amount to several million dollars. A complete resolution of the Lawsuit removes the exposure to all litigation attorney's fees and costs including discovery, expert, trial and potential appeal costs and a significant period of time where the property is tied up in litigation.

Further, as part of the settlement, and given the time period elapsed since the original Purchase & Sale Agreement and development project were considered, the parties have agreed to increase the value of the subject property from the initial sales price of \$1,590,000 to the negotiated value of \$1,815,475. The proceeds of the sale will be received upon close of escrow as provided for in the original purchase and sale agreement.

No other fiscal analysis or benefits from the settlement or potential new project will be evaluated or realized unless and until a new project is advanced to the City Council for consideration.



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### PREVIOUS ACTION

On December 18, 2018, the City and Touchstone MF Fund I, LLC (“Touchstone”) executed an Agreement of Purchase and Sale and Joint Escrow Instructions (“2018 PSA”) relating to City-owned real property located at 137 Valley Parkway, Escondido, California, also known as Municipal Parking Lot 1 (“Property”). See Attachment “1”. Touchstone thereafter filed an Application for certain development entitlements including a Master and Precise Development Plan, including a Density Bonus Application, a Class 32 exemption in accordance with the California Environmental Quality Act (“CEQA”), and Development Agreement (“Application”) which was processed by City staff.

The Planning Commission recommended approval of the Application. The Application was denied by the City Council at a public hearing on October 9, 2019. On June 2, 2020, Touchstone filed a Complaint against the City alleging Breach of Contract and seeking Declaratory Relief arising out of and related to the denial of the Application. The City thereafter filed a Cross-complaint against Touchstone alleging Breach of Contract and seeking Declaratory Relief (both actions will be referred to collectively herein as the “Lawsuit”). The Lawsuit has been litigated for over three years and is still pending.

### BACKGROUND

#### Previous Project

In 2016, the City and Touchstone began formal discussions with City staff regarding a potential residential development in an existing municipal parking lot located at 137 Valley Parkway, Escondido, also known as Municipal Parking lot 1 (“Aspire Project” or “Project”). In March 2016, the City and Touchstone entered into an Exclusive Negotiating Agreement (“ENA”) to further develop the Project proposal. The ENA was amended and extended several times as the Project progressed and changed.

On September 19, 2018, the City Council approved an Agreement of Purchase and Sale and Joint Escrow Instructions (“2018 PSA”) which became effective on December 18, 2018. The purchase price for the property was \$1,590,000 based on an appraisal done in 2018.

In its final iteration, the Project was a proposed six-story, mixed-use structure containing 131 apartment units, approximately 4,289 square feet of commercial space, underground parking, and an outdoor common area with a pool for residents. The proposed structure would be 67 feet in height with parapet walls and a tower element that extended up to 75 feet in height. The apartment units varied from studios to 2-bedroom units.

On August 27, 2019, the Escondido Planning Commission approved a motion to recommend the Project by a vote of 6-1. On October 9, 2019, the City Council held a public hearing on the Application. Further, the council was asked to consider Ordinance No. 2019-13 approving a Development Agreement which *inter alia* allowed for an allocation of density from the Downtown Density Transfer Program. The City Council voted 3-2 to deny the application.



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Soon thereafter, the City and Touchstone disputed the ability of Touchstone to file a new application for entitlements. In general, Touchstone claimed it had the right to file a new, revised application based on the language of the 2018 PSA, past practices and the escrow time period. The City maintained, among other arguments, that the 2018 PSA explicitly and implicitly did not allow for additional, revised applications after the October 9, 2019 hearing denying the Project, the City had the right under the 2018 PSA to reject the Project, Touchstone did not have the property owner's consent to file a new project application, and it had fully satisfied all of the obligations required of it in the 2018 PSA.

### Litigation.

On June 2, 2020, Touchstone filed a lawsuit against the City titled *Touchstone MF Fund I, LLC v. City of Escondido*, San Diego Superior Court Case No. 37-2020-00020856-CU-BC-NC. Touchstone alleged, in essence, that the City's refusal to accept a new development application for the project site constituted several wrongs including: (1) a breach of the 2018 PSA and/or waiver of its provisions; and (2) a violation of state housing laws including the State Density Bonus Law and Housing Crisis Act.

On July 22, 2020, the City filed its Cross-complaint against Touchstone alleging a breach of the 2018 PSA for failure to consent to terminate escrow after the Project was denied by council action and breach of the implied covenant of good faith and fair dealing for its acts, omissions and conduct related to obstructing the closure of escrow

The Lawsuit has been litigated for over three years and while still pending, discovery and motion practice has been stayed for purposes of this proposed settlement. If the matter does not settle, the stay will be immediately lifted and the parties will appear before the court to set dates for further motions and jury trial. It is anticipated that regardless of the outcome of the Lawsuit before the trial court, one of the parties will file an appeal. As a result, final resolution of the Lawsuit could be years away and the disposition of the property will be stalled during that time due to the pending litigation.

The parties to the Lawsuit have been in extensive and complicated settlement negotiations over an extended period of time to resolve the matter in the best interests of each party. The result of those negotiations has been a proposed settlement of the Lawsuit by entering into a settlement agreement and mutual release of claims as well as simultaneously amending the 2018 PSA to allow for Touchstone to engage another developer to file the appropriate application to develop the Property.

This settlement does not in any way commit the Planning Commission or City Council to a course of action, decision or approval in whole or in part as to any development application for the Property, except as otherwise required by state law. Instead, a new developer will be required to follow all conditions for a development project in the City and the City's discretion to approve or deny the project remains unqualified and absolute.



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### Settlement of Litigation.

Settlement of the Lawsuit includes two principal components:

#### A. Stay & Dismissal of The Lawsuit.

The first component of the settlement will be authorizing the City Manager to execute a Settlement Agreement and Mutual Release of claims. The proposed Settlement Agreement is attached to the Staff Report as Attachment “2” and the Resolution as Exhibit “A.”

In summary, the Settlement Agreement substantively allows for the following between the parties:

1. The Parties will agree to file a stipulation with the court to further stay the Lawsuit for 30 months and cooperate with the court and each other to maintain a stay of the case;
2. Touchstone will file a dismissal of its lawsuit with prejudice against the City and the City will dismiss its Cross-complaint at the earlier of (1) the conclusion of the 30-month stay; (2) the close of escrow provided for in the First Amendment to the Purchase and Sale Agreement (“First Amended PSA”); or (3) the termination of the First Amended PSA;
3. The parties mutually release and waive any claims to litigation costs and attorney’s fees recoverable against the other in the Lawsuit; and
4. The settlement agreement is conditioned upon the execution of the First Amended PSA.

#### B. First Amendment to the Purchase & Sale Agreement.

The second component of the settlement will be authorizing the City Manager to execute a First Amended PSA with Touchstone. The First Amended PSA is attached to the Staff Report as Attachment “3” and to Resolution No. 2023-164 as Exhibit “B.”

In summary, the First Amended PSA amends the original 2018 PSA in the following substantive ways:

1. The Closing Date for the sale will be forty-five (45) days following the earlier of the issuance of (1) a building permit for a project, or (2) twenty-four (24) months after the First Amended PSA is effective, but may be extended and tolled if there is a third-party challenge to the project of the First Amended PSA;
2. The Purchase Price for the Property is increased to \$1,815,475;
3. Touchstone agrees to indemnify the City if the California Department of Housing and Community Development (“HCD”) finds that the Agreement is subject to the California Surplus Lands Act (“SLA”) or a violation of the SLA and if it does not so indemnify, the City may terminate the Agreement;
4. Touchstone will allow KB Escondido LLC to submit an application for entitlements for the Property and the City has no obligation to approve said application;



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5. The City has the right, at its option, to terminate this First Amended PSA if escrow is not closed by the Closing Date (including extensions and tolling);
6. The developer will file an application for entitlements within ninety (90) days of the effective date of the First Amended PSA and is permitted more than application up until the Closing Date;
7. The escrow holder will return an existing escrow extension deposit of \$20,000 to Touchstone; and
8. The balance of the 2018 PSA will remain in effect.

### Conclusion.

The Property transaction envisioned by the 2018 PSA has been stalled for over 4 years at this time and the Property cannot be sold or developed until the Lawsuit is resolved. The Settlement Agreement and First Amended PSA allow for an opportunity to minimize the risk of exposure to the Lawsuit damages claimed by Touchstone, to free-up the Property for another development opportunity to assist with developing much needed housing, particularly housing that can assist with economic development in the downtown area, and to allow the existing City Council to weigh in on a new application for entitlements at the Property site.

### **RESOLUTIONS**

- a. Resolution No. 2023-164
- b. Resolution No. 2023-164 Exhibit "A"
- c. Resolution No. 2023-164 Exhibit "B"

### **ATTACHMENTS**

- a. Attachment "1" – Original 2018 Agreement of Purchase and Sale and Joint Escrow Instructions
- b. Attachment "2" – Settlement Agreement and Mutual Release
- c. Attachment "3" – First Amendment to Purchase and Sale Agreement