



Legislation Details (With Text)

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**Title:** PUBLIC HEARING TO CONSIDER A RESOLUTION TERMINATING DEVELOPMENT AGREEMENT WITH FOCAL STRATEGIC INVESTMENTS, LLC, ON BASIS OF CHARGES OF MATERIAL DEFAULT NON-TIMELY PERFORMANCE (CITY COUNCIL)

**Sponsors:**

**Indexes:**

**Code sections:**

**Attachments:** 1. Exhibit 1 - (Ex G) - Focal Schedule of Performance, 2. Exhibit 2 - 3076\_001 (Default Notice), 3. Exhibit 3 - 3077\_001 (E-mail), 4. Exhibit 4 - Executed DA, 5. Exhibit 5 Reso for Focal DA Termination (2)

Date	Ver.	Action By	Action	Result
1/14/2020	1	City Council		

**Report to Mayor and City Council**

Tuesday, January 14, 2020

Special Orders of the Day

**SUBJECT:**

**PUBLIC HEARING TO CONSIDER A RESOLUTION TERMINATING DEVELOPMENT AGREEMENT WITH FOCAL STRATEGIC INVESTMENTS, LLC, ON BASIS OF CHARGES OF MATERIAL DEFAULT NON-TIMELY PERFORMANCE (CITY COUNCIL)**

**I. SUMMARY**

On November 30, 2018, the City entered into a Development Agreement (the “DA”) with Focal Strategic Investments, LLC (“Focal”) for the development of two one-story buildings totaling 13,557 square feet on a 0.66 acre lot, which will be used for commercial cannabis operations including the cultivation of cannabis, manufacturing of cannabis products, and storage of residual materials from cannabis cultivation (the “Project”).

The DA incorporated a Schedule of Performance for the submission of plans and design review applications, which Schedule is attached hereto at Exhibit No. 1. To date, Focal has not submitted Project site plans and design review applications to the City within the timeframes required, much less timely fulfilled the other obligations following such review and approval of those plans. Project site plans and design review applications were supposed to be done within 30 days after the DA’s effective date, or January 4, 2019. Focal is thus more than one year in arrears on the Project Schedule and has not cured

such timeliness defaults.

City has issued Focal multiple Notices of Default, engaged Focal in a “meet and confer” process to discuss issues of default, and issued a final “Notice of Termination” setting the DA for possible termination by the City Council pursuant to the terms of the DA. All such correspondence relating to default and potential DA termination from the City to Focal are attached hereto as Exhibit No. 2.

Simultaneous with the pending discussions of default, Focal informed the City that it plans to undertake various internal corporate organizational assignments that, pursuant to the terms of the DA, would require approval by the City Council. If such corporate assignments were undertaken without City approval, they would also qualify as grounds for default under the DA.

## **II. RECOMMENDATION**

TAKE the following actions:

1. OPEN the public hearing, TAKE public testimony, CLOSE the public hearing.
2. ADOPT Resolution No. 20-013, entitled “A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF CARSON, CALIFORNIA, MAKING FINDINGS OF DEFAULT AGAINST FOCAL STRATEGIC INVESTMENTS, LLC, AND ACCORDINGLY TERMINATING THAT DEVELOPMENT AGREEMENT BETWEEN THE CITY AND FOCAL DATED NOVEMBER 30, 2018 LOCATED AT 17505 S. MAIN STREET”

## **III. ALTERNATIVES**

TAKE another action the City Council deems appropriate.

## **IV. BACKGROUND**

### **City’s Commercial Cannabis Program**

The City’s Commercial Cannabis Operation Permit Regulatory Program as contained in Chapter 15 of Article VI of the Carson Municipal Code authorizes no more than four (4) commercial cannabis centers (“Permits”).

A commercial cannabis center may include indoor cultivation, mixed-light cultivation, manufacturing, testing and/or (wholesale) distribution. Applications for Permits were accepted by the City and subject to an initial review for adherence to local and state requirements. The City’s cannabis consultant reviewed the applications. Five Permit applications were eligible to be sent to the Cannabis Permit Committee (“CPC”) for review based on specified criteria (“Merit List”).

The CPC convened on August 2 and 13, 2018 and recommended that two applicants be

issued a Permit. At the September 4, 2018 City Council meeting, a resolution to approve the CPC's recommendations based on Merit List criteria was provided for consideration. The City Council upon receipt of CPC recommendations made a final determination and issued two Cannabis Operation Permits (Resolution No. 18-128) based on Merit List factors, *including one Permit granted to Focal*. Therefore, due to awarding a Permit to Focal, the City foreclosed itself from opportunities to negotiate with an alternative developer (i.e., one of the other competitive Permit applicants).

The Carson voters by a margin of almost 2:1 at the November 6, 2016 General Municipal Election approved taxes on commercial cannabis activities.

At the September 4, 2018 City Council meeting, Resolution 18-130 was approved to set the interest rate on unpaid cannabis taxes at 5%, to set commercial cannabis operation tax rates at 18% of proceeds and at \$25 per square foot of cultivation, with the intention of securing a total of four million dollars or more over a three year period from individual commercial cannabis centers (four centers maximum).

### Focal Development Agreement

Pursuant to the CPC and Council process described above, on November 30, 2018, the City entered into a DA with Focal for the development of the Project. The Project was anticipated to involve the construction of two, one-story buildings totaling 13,357 square feet that would be 20 feet tall up to the top of the parapet. The building to the east of the Project site immediately fronting South Main Street was planned to be approximately 7,600 square feet and include a cultivation area, small lobby area, and storage area. The building on the west site of the Project site was planned to be approximately 5,757 square feet and would include a cultivation area, manufacturing area for manufacturing of cannabis products, and a storage area. The proposed Project was anticipated to include cannabis cultivation, harvesting, drying, extraction, packaging, and production of cannabis products. These products would be distributed to licensed facilities and dispensaries eligible to receive such products, in compliance with State of California and the City of Carson laws and regulations.

State Law allows cities to enter into DAs with private parties. A DA is a legal, binding contract between a city and any person or entity having a legal or equitable interest in a property. The agreement must clearly outline conditions, terms, restrictions and requirements. Additionally, approval of Focal's DA was accompanied by a number of discretionary approvals and *anticipated* discretionary approvals, including:

- Zoning Text Amendment (ZTA) to expressly allow commercial cannabis within Industrial zones (zoning code presently silent);
- Variance (VAR) - to permit reduced parking and front yard setback - administrative review and approval pursuant to the Development Agreement;
- Mitigated Negative Declaration; and
- Site Plan & Design Review (DOR) - administrative review and approval pursuant to the Development Agreement (to permit final layout and design of the

development).

Focal's DA outlined and anticipated a number of public benefits that would accrue to the City, such as local hiring, social justice programs, Focal's participation in community facilities districts and payment of City development impact fees. Further, a significant public benefit of the Project was expected from applicable taxes and fees: Manufacturing: 18% of proceeds; Cultivation: 18% of proceeds plus \$25.00 per square foot for space utilized as cultivation area; Distribution: 18% of proceeds; and, Testing: 18% of proceeds. *At the time of DA approval, the revenues generated for the City by the Project were estimated roughly at \$1,000,000 or more annually.*

DA Provisions Most Relevant to This Hearing

To deliberate upon the allegations of default pending against Focal pursuant to this hearing, at least three provisions of the Focal DA are key:

1. The Focal DA incorporated a "Schedule of Performance" for the submission of plans and design review applications, and other Project development benchmarks, which Schedule is attached hereto at Exhibit No. 1.
2. The importance of Focal's adherence to the DA's Schedule of Performance is bolstered by the terms of DA Section 17.10, which reads:

"Time of Essence. Time is of the essence in: (i) the performance of the provisions of this Agreement as to which time is an element; and (ii) the resolution of any dispute which may arise concerning the obligations of the Developer and the City as set forth in this Agreement."
3. DA Article 12 holds that a corporate assignment above the level of "Triggering Percentages" shall be subject to City approval of an assignment and assumption agreement "in a form reasonably approved by the City." The relevant provisions read as follows:

"Neither party shall have the right to assign this Agreement or any interest or right thereunder without the prior written consent of the other party; however, notwithstanding the above, the Developer's assignment of its rights and obligations under this Agreement to another entity which is owned or controlled (directly or indirectly) by the Developer which assignee shall own, develop or operate the Site pursuant to the provisions of this Agreement, is permitted without the City's approval (a "Permitted Transfer"). The term "assignment" as used in this Agreement shall not include successors-in-interest to the City that may be created by operation of law.

As used in this Section, the term "transfer" shall include the transfer to any person or group of persons acting in concert of more than seventy percent (70%) of the present equity ownership and/or more than fifty percent (50%) of the voting control of the Developer (jointly and severally referred to herein as the "Trigger Percentages") or any general partner of the Developer in the aggregate, taking all transfers into account on a cumulative basis, except transfers of such ownership or control interest between

members of the same immediate family, or transfers to a trust, testamentary or otherwise, in which the beneficiaries are limited to members of the transferor's immediate family.”

A complete copy of the executed DA between the City and Focal is attached hereto for Council's reference at Exhibit No. 4.

*Allegations of Default Against Focal; Notices of Default*

Contrary to the fundamental DA provisions outlined above, Focal has (1) significantly fallen into delinquency of the Project timeframes under the DA Schedule of Performance (Exhibit No. 1), and (2) proposed an internal transfer of Focal's corporate ownership and control that will be a default of the DA absent express City approval.

Focal has fallen far behind schedule on the deadlines for submittal of Project site plans and design review applications, which were supposed to be done within 30 days after the DA's effective date, or January 4, 2019. (See, Exhibit No. 1 hereto.) Thus, Focal is more than a year beyond the initial deadlines set in the DA's Schedule of Performance.

Focal is particularly in default of its submission deadlines for site plans, design review applications, construction plans, and all approvals attendant to those items. For some time, Focal claimed that it emailed City Staff on April 14, 2019 with further questions regarding the planning process, but received no response. (See, Focal Email dated October 17, 2019, in Exhibit No. 3 hereto.) City Staff has reviewed its files, and found that this is incorrect. In point of fact, City Staff did receive Focal's email of April 14, 2019, and responded to it on April 18, 2019. (See, City Email dated April 18, 2019, in Exhibit No. 3 hereto.) Staff's response included a link to application forms to be completed and a list of submittal requirements. Furthermore, City Staff left a voicemail to Focal on April 23, 2019, as a follow-up. (*Id.*) Nonetheless, Focal has still not submitted the required Project applications to the City, much less timely fulfilled the other obligations following such review and approval of those plans.

The Schedule of Performance sets individual dates for individual tasks, and as demonstrated by the Schedule at Exhibit No. 1, Focal has not fulfilled any of the required task deadlines following May 31, 2018. The Schedule can also be viewed from a “cumulative” perspective, in that Focal has fallen so far behind schedule on the deadlines for submittal of Project site plans and design review applications that it is difficult to perceive how Focal can now bring Project construction into compliance with the scheduled timeframes, which were supposed to start within 30 days after the DA's effective date, or January 4, 2019. Consistent with taking a “cumulative” view of the Schedule of Performance, as well as a task-based perspective, DA Section 11.3.3 expressly states that City Council authorization is needed to extend timeframes beyond 180 cumulative days-a threshold that Focal is significantly beyond:

“The City Manager shall have authority to approve extensions of time without City Council action not to exceed a cumulative total of 180 days.”

Similar language is repeated in the Schedule of Performance (Exhibit No. 1). Thus, an extension of the dates for Focal's initial submissions alone would equal more than 180-

days, and thus would require City Council approval, notwithstanding any issues of default.

Exacerbating Focal's timeliness defaults is the fact that, as far as the City is aware, Focal remains unable to secure Project financing. During a "meet and confer" process, Focal expressed financial difficulties in seeking Project financial backing from Focal's Korean investment sources. (See, Focal Email dated October 17, 2019, at Exhibit No. 3) While this might not be a basis for default in itself, these facts reinforce the evidence that Focal has been, and will continue to be, in default of Project deadlines.

Finally, in the course of several communications and "meet and confer" discussions with Focal, Focal notified the City that it was undertaking, or had undertaken, an internal corporate reorganization. In particular, on November 19, 2019, Focal announced:

"[We are notifying City of Carson regarding change in ownership of interest in FOCAL Strategic Investments LLC. Timothy Kim is no longer working with FOCAL Strategic Investments LLC and has been removed from General Manager position and he transferred his ownership interest to Kyung Ho Hwang (Carl Hwang). He will be the General Manager of the Focal Investments LLC and will be in charge of all the on going business. He now has 45% of interests in FOCAL and 55% of interests are held by Jungyoon Hwang.]"

(See, Focal Emails dated November 19 and 25, 2019, at Exhibit No. 3) On November 27, 2019, the City notified Focal that it may not assign its corporate interests at the level of the "Triggering Percentages" defined in DA Article 12 without prior written consent of the City, and advised Focal that corporate restructuring undertaken in contravention of Article 12 may be a further basis for default of the DA. (See, City Letter dated November 27, 2019, at Exhibit No. 2) Focal has acknowledged that its corporate restructuring meets the DA's "Triggering Percentages," thus requiring City approval, or else Focal faces default. (See, Focal Email dated November 27, 2019, in Exhibit No. 3 ["we understand that we are in a situation where in "Triggering Percentages" of the ownership changes."].)

#### *Procedural Background Leading to This Hearing*

The DA sets forth a specific process for its default and termination. Preliminarily, the defaulting party is entitled to (i) notices of default and a 30-day opportunity-to-cure any alleged defaults (DA § 11.5), (ii) a "meet and confer" process lasting at least 10 days (DA § 11.6.1), (iii) a final "formal" default notice (DA § 11.6.1), and finally (iv) if defaults have still not been cured, then a "Termination Notice" that sets the matter for hearing before the City Council within 30 days thereafter (DA § 11.6.3).

Commencing on April 8, 2019, City Staff issued its first "Notice of Default" to Focal based upon unmet Project deadlines. In order to follow the preliminary termination procedures outlined above, that letter was followed by multiple correspondence and notices from the City to Focal in order to fulfill all the DA's procedural requisites for default and termination. All such City correspondence are attached hereto at Exhibit No. 2 in the following order:

- A "Notice of Breach of Development Agreement" and request to initiate 10-day "meet and confer" discussions dated October 11, 2019. As required by the DA, the parties held a "meet and confer" discussion on October 28, 2019, which was

attended on the City's behalf by John Raymond, Assistant City Manager, Saied Naaseh, Community Development Director, Alvie Betancourt, Planning Manager, and Lona Laymon, City Attorneys' Office.

- A "Notice of Breach of Development Agreement/Final Notice of Default" and termination of "meet and confer" procedures dated November 15, 2019. This Notice memorialized the "meet and confer" discussions between City Staff and Focal on October 28, 2019, including Focal's timeliness defaults and inability to obtain Project financing. This Notice also terminated the 10-day "meet and confer" process required by the DA.
- A correspondence in re "Focal Corporate Assignment Issues" was sent by the City to Focal on November 27, 2019. This letter was largely sent to Focal in response to the announcement that it was undergoing an internal corporate restructuring. (See, Focal Email dated November 19, 2019, at Exhibit No. 3.) As noted to Focal in the City's November 27 letter: "Please be advised, that corporate restructuring undertaken by Focal in contravention of Article 12 may be a further basis for default under the DA."
- Further City correspondence to Focal dated December 5, 2019, responding to various questions in re the default and cure procedures, and matters of corporate reorganization.
- Finally, the December 23, 2019, Notice of "City Council Public Hearing on Agreement Default, Corporate Assignment Issues and Notice of Termination."

All such City notices and correspondence are attached hereto at Exhibit No. 2.

With these preliminary procedural matters fulfilled, the Council is now able to consider and decide upon the allegations of default against Focal, and if the requisite findings for DA termination are supported by substantial evidence, the Council may terminate the DA and the DA's authorizing ordinance.

#### Hearing & Findings Needed For Termination

Prior to any termination of the DA, "a termination hearing shall be conducted" at which Focal shall have the right to present evidence to demonstrate that it is not in default and to rebut any evidence presented in favor of DA termination. (DA § 11.6.3.) Termination of the DA may be accomplished by adoption of Resolution No. 20-013 (Exhibit No. 5), based upon the findings outlined below.

#### ***Findings of a default or a condition of default must be based upon substantial evidence supporting the following three findings:***

1. That a default in fact occurred and has continued to exist without timely cure;
2. That the Non-Defaulting Party's (in this case, the City's) performance has not excused the default; and

3. That such default has, or will, cause a material breach of this Agreement and/or a substantial negative impact upon public health, safety and welfare, or the financial terms established in the Agreement, or such other interests arising from the Project.
4. Such other evidence and facts as presented to the Council in this Staff Report, the Exhibits hereto, or at the public hearing.

It is proposed that the following facts and evidence support these required findings:

Finding No. 1: That a default in fact occurred and has continued to exist without timely cure. *Supporting evidence:*

1. The Focal DA incorporated a “Schedule of Performance” for the submission of plans and design review applications, and other Project development benchmarks, which Schedule was incorporated into the DA as Exhibit “G”. DA Section 17.10 requires that “Time is of the essence in: (i) the performance of the provisions of this Agreement as to which time is an element; and (ii) the resolution of any dispute which may arise concerning the obligations of the Developer and the City as set forth in this Agreement.”
2. Focal has significantly fallen into delinquency of the Project timeframes under the DA’s Schedule of Performance. Focal is particularly in default of its submission deadlines for site plans, design review applications, construction plans, and all approvals attendant to those items. Deadlines for initial submittals of Project site plans and design review applications were supposed to be done within 30 days after the DA’s effective date, or January 4, 2019. Thus, Focal is more than a year beyond the initial deadlines set in the DA’s Schedule of Performance.
3. As far as the City is aware, Focal remains unable to secure Project financing, and thus continues to suffer delays in Project implementation.
4. DA Section 11.3.3 expressly states that City Council authorization is needed to extend Project timeframes beyond 180 cumulative days. Focal’s last missed Project deadline was more than a year ago. Thus, absent Council authorization, Focal’s delinquency in Project deadlines exceeding 180 days qualifies as a default.
5. To date, Focal has not fulfilled any of the required task deadlines following May 31, 2018, and thus such delays in Project performance remain uncured.
6. DA Article 12 holds that a corporate assignment above the level of “Triggering

Percentages” shall be subject to City approval of an assignment and assumption agreement “in a form reasonably approved by the City.” Nonetheless, on November 19, 2019, Focal informed the City that it was undertaking, or had undertaken, an internal corporate reorganization. On November 27, 2019, Focal acknowledged that its corporate restructuring meets the DA’s “Triggering Percentages,” thus requiring City approval in order to cure any violations of DA Article 12, or else Focal faces default.

7. Multiple notices of default and opportunities to cure were issued by the City. Nonetheless, no required Project submissions have been proffered by Focal.
  
8. Such other evidence and facts as presented to the Council in this Staff Report, the Exhibits hereto, or at the public hearing.

Finding No. 2: That the Non-Defaulting Party’s (in this case, the City’s) performance has not excused the default. *Supporting evidence:*

1. The City has never agreed to waive, release or excuse any default of the DA by Focal. The City has issued multiple notices of default and demands to cure each default identified herein without equivocity.
  
2. City Staff and the City Attorney timely responded to Focal inquiries and communications in order to facilitate timely Project performance by Focal. At no time has the City turned-away, delayed or disapproved Project entitlement submissions by Focal. Nonetheless, Focal has still not submitted the required Project applications to the City, much less timely fulfilled the other obligations following such review and approval of those plans.

Finding No. 3: That such default has, or will, cause a material breach of this Agreement and/or a substantial negative impact upon public health, safety and welfare, or the financial terms established in the Agreement, or such other interests arising from the Project. *Supporting evidence:*

1. Focal has fallen so far behind schedule on the deadlines for submittal of Project site plans and design review applications that it is difficult to perceive how Focal can now bring Project construction into compliance with the scheduled timeframes, which were supposed to start within 30 days after the DA’s effective date, or January 4, 2019. The Council finds that Focal’s delinquencies in Project performance are inherently “material” breaches given the length of such delinquencies (exceeding a year) and the resulting delay or loss of public benefits that were supposed to accrue to the community under the DA.

2. Focal's DA outlined and anticipated a number of public benefits that would accrue to the City, such as local hiring, social justice programs, Focal's participation in community facilities districts and payment of City development impact fees. Further, a significant public benefit of the Project was expected from applicable taxes and fees: Manufacturing: 18% of proceeds; Cultivation: 18% of proceeds plus \$25.00 per square foot for space utilized as cultivation area; Distribution: 18% of proceeds; and, Testing: 18% of proceeds. Focal's default of the DA would abrogate or delay these public benefits and revenue streams to the City.
  
3. The identity of the Project developer was of particular importance to the City in awarding the DA to Focal. Focal's change of corporate ownership and control has been proposed without proof of (i) the financial strength and capability of the proposed transferee to perform the obligations under the DA; and (ii) the proposed transferee's experience and expertise in the planning, financing, development, ownership, and operation of developments like the Project.
  
4. The DA was awarded through a competitive process overseen by the City's Cannabis Permit Committee ("CPC") for review based on specified criteria (the "Merit List"). The CPC received five applications for cannabis projects in the City, but was limited to awarding only two such applications. At the September 4, 2018, City Council meeting, based on the CPC's recommendations, the City Council determined to issue two Cannabis Operation Permits, with one being granted to Focal. Therefore, due to awarding the DA and related cannabis permit to Focal, the City foreclosed itself from opportunities to negotiate with an alternative developer (i.e., one of the other competitive permit applicants). Focal's defaults intensify this scenario of "lost opportunity" faced by the City by leaving the Project site vacant, and public benefits pursuant to the DA abrogated, while the City could have otherwise proceeded with an alternative developer capable of timely project performance.

## **V. FISCAL IMPACT**

Cannabis tax revenue to the City from the Focal Strategic Investments, LLC commercial cannabis center was to be based on an 18% proceeds tax as well as a \$25.00 tax per square foot for space utilized as cultivation area. It is difficult to project the revenues generated for the City as the market for cannabis products is unsettled. At the time of granting the entitlements, the revenues generated for the City by the Project were roughly estimated at \$1,000,000 or more annually. Termination of the DA, and hence the Project, eliminates these potential revenue streams. However, if the DA is terminated, another project/use on this site could generate additional revenues for the City as well as other public benefits. The projected revenues and public benefits from this unknown source would be pure speculation.

