



PUBLIC INTEREST LAW PROJECT

INCLUSIONARY ZONING IN CALIFORNIA (April 2017)

CBIA v. San José* Decision Removes Constitutional Uncertainty & Interim Strategies for Addressing *Palmer v. City of Los Angeles

The Public Interest Law Project (PILP) is California non-profit support center on public interest law focusing on affordable housing and development law since 1996. Its experienced staff assists local legal services programs, affordable housing developers, and community groups by providing expertise in housing policy, litigation and legislation. PILP represented intervening low income tenants and California affordable housing groups in defending of San Jose's inclusionary housing ordinance against the constitutional attack of the California Building Industry Association and was involved as amicus or co-counsel in many previous challenges to inclusionary zoning in California.¹

California Building Industry Assn. v. San Jose

The California Supreme Court unanimously and without qualification upheld San Jose's 15% inclusionary housing ordinance in *California Building Industry Assn. v. City of San José*, 61 Cal. 4th 435 (2015), freeing communities to adopt mixed-income housing ordinances to address critical shortages of affordable housing. The case settled the question of the constitutionality of inclusionary zoning for 170 jurisdictions in California. And with the U.S. Supreme Court's denial of CBIA's request for certification for review in 2016 (577 U. S. ___; 136 S.Ct. 928 (2016)), the decision established the benchmark for measuring the validity of inclusionary zoning ordinances throughout the country. It affects all communities of California that have adopted or are considering adoption of inclusionary housing programs.

CBIA contended San Jose's law lacked sufficient justification and, therefore, constituted an unconstitutional "exaction" resulting in a taking of property. The California Supreme Court ruled that the need for affordable housing and the goal to increase diversity of housing opportunity throughout the city provided ample justification for the adoption of the inclusionary requirement.

¹ E.g., *Home Builders Assn. v. City of Napa*, 90 Cal.App.4th 188 (2001), *Building Industry Assn of Central California v. City of Patterson*, 171 Cal.App.4th 886 (2009), and *Building Industry Assn of Central California v. County of Sacramento* (Sacramento County Superior Court, 2005).

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Inclusionary laws, the Court said, come within the community's "broad authority, under its general police power, to regulate the development and use of real property within its jurisdiction to promote the public welfare" of the community or the region.

Specific Holdings

- **Inclusionary Requirements Are Land Use Regulations, not "Exactions."**
Inclusionary zoning is not an "exaction" because it does not require a conveyance of a property interest. Inclusionary housing ordinances are land use regulations that merely restrict the use of property by limiting the price of some units.
- ***Building Industry Ass'n of Central Calif. v. City of Patterson*, 171 Cal.App.4th 886 (2009) Disapproved.** The Court rejected CBIA's contention that under *Patterson* (and *San Remo Hotel v. San Francisco*) inclusionary housing requirements or in lieu fees are justified only if the need for affordable housing "was caused by or attributed to" the impact of new housing development.
- **Inclusionary Ordinances Are Valid if they are Reasonably Related to Legitimate Public Purposes.** The Court found that "unquestionably constitutionally permissible purposes" for adoption of an inclusionary requirement include:
 - 1) Increasing the number of affordable housing units in a community when there is an insufficient number in relation to the community's "current and future needs," including regional needs under the Housing Element Law
 - 2) Assuring new affordable housing units "are distributed throughout the city as part of mixed-income developments" in order to:
 - "Obtain the benefits that flow from economically diverse communities"
 - "Avoid the problems that have historically been associated with isolated low income housing."
- ***In Lieu Fees Are Not Exactions.*** In-lieu fees as an alternative to on-site inclusionary requirements are not "mitigation fees" or exactions and, therefore, are not required to be related to some impact of new housing development.

Nexus Study Not Required

A “nexus” or *impact* study is unnecessary for determining the inclusionary percentage or the in-lieu fee amount because under the holding of the case, the community is not required to show that new housing development is the cause of the need for affordable housing. Most communities will conduct an economic study or analysis to assess the workability of the inclusionary percentage for residential developments. But, they do not conduct a formal nexus study because neither the inclusionary percentage nor the in-lieu fee must be based on the impact of residential development on the need for affordable housing. They are based on the existing need for affordable housing.

Addressing *Palmer v. City of Los Angeles* to Facilitate Affordable Rental Housing

1. Two Prong San Jose Approach

San Jose undertook adoption of its inclusionary housing program *after* the *Palmer/Sixth Street Properties, L.P. v. City of Los Angeles*, 175 Cal.App.4th 1396 (2009) decision, which held that local inclusionary ordinances could not apply to newly constructed rental housing because any restrictions on setting the initial rent for newly constructed units was prohibited by the state Costa-Hawkins Act (Civil Code §§ 1954.50-1954.535). Despite the deep economic downturn, in 2010 San Jose confronted a severe shortage of housing affordable to its workforce and lower income families. The City recognized the importance of ensuring that, as the city continued to grow, residential development in all neighborhoods included sufficient affordable ownership *and rental* housing. It therefore embraced a two-fold strategy to address the dual challenges of the affordable housing need and the *Palmer* decision.

First, the City included a provision in its ordinance that provided the inclusionary housing requirements would apply to rental housing in the future should either a court or the Legislature overturn or supersede the *Palmer* case. As of this writing the Legislature is considering adoption of AB 1505 which would overturn *Palmer*, allowing localities to apply their inclusionary housing requirements to rental housing developments.

Second, it began a process of crafting an affordable housing fee ordinance that would apply to rental housing development. Today, because of the *CBIA* decision, San Jose’s inclusionary ordinance applies to new developments of ownership housing, and it

has adopted an impact fee ordinance placing a fee on new rental housing projects to be used to finance the construction of affordable rental projects.

2. Overlay/Density Bonus Alternative for Addressing *Palmer*

One alternative to an impact fee that some jurisdictions have employed to facilitate the development of affordable rental housing while *Palmer* applies is adoption of a zoning overlay ordinance and/or “super” density bonus ordinance. Under this mechanism, the community amends its zoning ordinance to allow increased density and/or regulatory incentives and concessions greater than those mandated by state Density Bonus Law (Government Code §65915) in exchanged for a proportion of units in a rental development being affordable to and reserved for lower income households, either within the development or off site.

3. Use of In-Lieu Fees from For-Sale Housing (including condominiums) for Off-Site Rental Housing

Most jurisdictions with inclusionary ordinances, especially after the *Palmer* decision, designate most or all of the in-lieu fees collected to the production of affordable rental housing developed off-site. This is permissible because the basis for the underlying inclusionary/in-lieu fee requirement is the need for affordable housing in the community, which almost always greater for lower income rental housing.

4. Affordable Housing Fee for Condominium Developments Used as Rental Housing

Most multifamily rental housing is developed as condominiums so that if the developer later decides to sell the units as condominiums there is no need to seek a conversion permit. While inclusionary requirements can be applied to the units ultimately offered for sale, if the units are market as rentals, *Palmer* would prohibit application of inclusionary rent restrictions. Many local governments address these adopting affordable housing impact fee ordinances that expressly apply to condominium developments where the units will not be sold.

In summary, inclusionary housing policies may now be adopted and applied in California for new ownership housing developments, and rental housing developments can facilitate development of new affordable housing through imposition of impact fees or provision of density or regulatory incentives.

SUMMARY OF COMMENTS

1. **We AGREE** with: increasing coastal zone in lieu fees; a local bond measure to create a local source of revenue for affordable housing; expanding one-for-one replacement of affordable units city-wide; and dedicating additional resources to PRHIP. **HOWEVER, all of these recommendations need FIRMER COMMITMENTS AND TIMELINES FOR COMPLETION.**
2. **We DISAGREE** with: CEQA reform; inclusionary housing for ownership developments only; changing the definition of moderate income; and adoption of specific plans with Program EIR's.
3. **MISSING from the City's recommendations** are critical housing production policies, such as housing impact fees (linkage fees), boomerang funds and community land trusts
4. **Also missing**, are critical renter protections and anti-displacement policies, such as REAP, rent control and just cause.

**SECTION #1
POLICIES TO IMPLEMENT IMMEDIATELY**

City's Policy Recommendations		Comments	Proposed Revisions
1.1	Encourage the preservation of existing affordable housing stock, consistent with the adopted Housing Element.	No real commitment/status quo	
1.2	Encourage Project-Based Vouchers in new affordable developments.	No real commitment/status quo	
1.3	Continue to waive developer impact fees for new affordable developments in accordance with the LBMC.*	No real commitment/status quo	
1.4	Promote the City's Density Bonus Program to all multi-family housing developers.*	No real commitment/status quo	
1.5	Continue to partner with developers and other community stakeholders in the pursuit of grant funding and other third party resources such as Metro, federal, state, county, etc., for affordable housing development, support services, and mobility enhancements and programs that support new housing development.	No real commitment/status quo	
1.6	Explore the potential development of student and	Need to define "student" and "workforce	Need to define "student" and "workforce



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	workforce housing on school and college/university campuses, and other adequately-zoned sites.	housing” to ensure that limited resources go to those most in need.	housing” to ensure that limited resources go to those most in need.
1.7	Track Federal and State legislative activities and support legislation that increases funding for affordable housing.	No real commitment/status quo	
1.8	Support CEQA reform through City’s legislative actions that encourages the production of affordable and workforce housing. *	This is very problematic, as CEQA reform is not needed and CEQA provides critical protections that should not be weakened.	Do not approve this recommendation.
1.9	Create and maintain a database of publicly held land that may provide opportunities for affordable and workforce housing development.	This is already required by state law. Status quo.	

**SECTION #2
EXISTING LEGISLATIVE REQUIREMENTS AND PENDING INITIATIVES IN PROCESS**

City’s Policy Recommendations		Comments	Proposed Revisions
2.1	Adopt an ordinance that supports the development of accessory dwelling units in accordance with new State law.	Unclear how this will have a real impact on our housing crisis.	
2.2	Implement State law that reduces parking requirements for affordable housing projects near transit.	Required by state law.	
2.3	Conduct a financial analysis and nexus study to review the viability of the Coastal Zone in-lieu fee (LBMC 21.61), and consider revisions to the fee structure.	<p>We support this. The City’s existing in lieu fees are set too low and do not result in one-for-one replacement of units demolished or converted in the coastal zone. State law requires one for one replacement of units lost in the coastal zone, so increasing the fees will bring the City into compliance with State law.</p> <p>Moreover, the City made a legally binding commitment in its latest Housing Element to complete this by 2015.</p>	<p>On page 125 of the City’s 2013-2021 Housing Element, the City made the following legally binding commitment: “By the end of 2015, conduct a financial analysis and nexus study to review the viability of the Coastal Zone in lieu fee and consider revisions to the fee structure, if necessary, as part of the FY 2016-2017 budget process and master fee schedule.”</p> <p>The City has not yet done this, so it should set clear timelines and complete this immediately.</p>
2.4	Review and update the Condominium Conversion	We support this, though condominium	



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<p>Ordinance (LBMC 21.60); include first-right or opportunity to purchase; limit conversions when vacancy rates are low; consider directing resulting fees into Housing Trust Fund.</p>	<p>conversions are not currently very active in LB, so this will not address our immediate housing crisis.</p>	
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**SECTION #3
NEW INITIATIVES FOR DEVELOPMENT AND IMPLEMENTATION**

City's Policy Recommendations	Comments	Proposed Revisions
<p>3.1 Begin exploring a local bond measure as a one-time source to capitalize the Housing Trust Fund.</p>	<p>We support this, though a firmer commitment and timeline is needed.</p>	<p>We support this, though a firmer commitment and timeline is needed.</p>
<p>3.2 Immediately begin the development of an inclusionary housing policy to encourage mixed-income housing. Focus an inclusionary ordinance on homeownership units until such time as the legality of rental units is determined.</p>	<p>There are legally permissible ways to create rental units through an inclusionary housing (IH) policy, so rental units should be included in this policy and studies undertaken to support this policy.</p> <p>AB 1505 (Bloom) clarifies any uncertainties with respect to IH in rental projects and this bill is expected to pass.</p> <p>170 cities in CA have IH for both rental and ownership developments.</p>	<p>Add rental developments to this IH policy and any underlying studies.</p> <p>Work with housing policy experts to better understand how to include rental developments in an IH policy.</p> <p>IH should be "required," not just "encouraged."</p>
<p>3.3 Investigate the possibility of establishing a local document recording fee to fund affordable housing (Philadelphia model).</p>	<p>We generally support this, though it may require state legislation to become a reality. More research and information is needed.</p>	
<p>3.4 Investigate the possibility of dedicating resources from the City to support the production of affordable and workforce housing during the annual budget process.</p>	<p>Define workforce housing, to ensure that limited resources go to those most in need.</p>	
<p>3.5 Modify the Housing Trust Fund Ordinance to include a more equitable distribution of resources amongst income categories (EL, VL, L, and Mod.) in conjunction with the establishment of any new revenue sources. Modernize the Ordinance to ensure that it promotes economic diversity while addresses the needs of the community's most vulnerable residents.</p>	<p>Define the new income targeting categories to ensure that limited resources go to those most in need. Currently, 50% of Housing Trust Funds are dedicated to ELI households, who are the most in need. This should be maintained.</p>	
<p>3.6 Modify the moderate-income definition from 80% -120%</p>	<p>The City should not modify a long standing definition of</p>	<p>Do not approve this</p>



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	of AMI to 80%-150%.	<p>moderate income, which is used by HUD, the State of CA and other jurisdictions.</p> <p>The city's limited resources should not be used to subsidize housing for those earning nearly \$100,000.00 a year.</p> <p>Affordable projects in the city will not be competitive for tax credits and other funding sources with this proposed new definition, as tax credits are competitive and awarded to projects with deep affordability.</p> <p>Trickle down housing theory is a myth. Studies have shown that it takes decades for new market rate housing to have any impacts on housing markets for lower income households.</p>	recommendation.
3.7	Encourage the adoption of Specific Plans with Program EIRs as applicable throughout the City, which provide regulatory relief and more rapid entitlement procedures.	This is very problematic unless it includes affordable housing requirements and anti-displacement protections. (Long term downtown plan are residents are suffering massive displacement from this kind of specific plan.)	Do not approve this recommendation.
3.8	Consider expanding one-for-one replacement of lower-income units (currently offered in Coastal Zone only through LBMC 21.61).	We support this.	
3.9	Develop and offer first-time homebuyer programs (including Police, Fire, and Teacher, down payment and second mortgage) as new revenue sources allow.*	Why is the City singling out three job classifications for housing assistance? This is arbitrary. The City's limited resources should be allocated to those most in need.	
3.10	Encourage adoption of regulations to allow and incentivize the use of shipping container construction for housing.*	More research and investigation is needed.	
3.11	Develop a plan to include micro-units as a method for encouraging housing production.*	We support this.	
3.12	Support separate efforts to study the potential for short term rental (vacation rentals) regulations.	We support this.	
3.13	In accordance with the adopted Housing Element, ensure sufficient resources remain available to implement the	We support this.	

	City's Proactive Rental Housing Inspection Program (PHRIP).		
3.14	Explore the feasibility and mechanics of using new structures such as the enhanced infrastructure financing district (EIFD) tool to capitalize the Housing Trust Fund with new revenue resources for the creation of affordable housing.	We do not support this unless it includes strong affordable housing requirements for those most in need and anti-displacement protections for existing residents.	
3.15	Explore and propose an Article 34 referendum to ensure maximum leveraging of State resources for affordable housing developments.	Additional information needed.	
3.16	Provide necessary City staffing resources to effectively manage the growth of affordable housing contemplated by these policy recommendations through the annual budget process as resources allow.	No comment.	