LEGAL ISSUES ASSOCIATED WITH INCLUSIONARY HOUSING ORDINANCES

Institute for Local Self Government

A variety of legal issues may be raised when a locality adopts a regulation that requires new developments to include affordable housing. This paper provides an overview of the sources of, and limitations on, the authority of local agencies to adopt inclusionary housing programs:

- Police Power: Source of Authority to Adopt Inclusionary Programs
- Takings Issues
- Substantive Due Process and Equal Protection
- Special Considerations Associated With Fees
- The Costa-Hawkins Act

The paper concludes with a summary of best practices for avoiding liability.

I. POLICE POWER: AUTHORITY FOR INCLUSIONARY PROGRAMS

The authority for local governments to adopt inclusionary zoning ordinances and most other land use policies is the "police power." This power emanates from the Tenth Amendment to the United States Constitution, and entitles communities to take actions and adopt laws and policies that protect the public's health, safety and welfare.[1]

A. SCOPE OF AUTHORITY IN CALIFORNIA

The California Constitution provides that cities and counties "may make and enforce within their limits all local, police, sanitary, and other ordinances or regulations not in conflict with the general laws."[2] In the field of land use regulation, courts have liberally construed this power:

[1] *See Euclid v. Amber Realty Company*, 272 U.S. 365 (1926) (holding that local governments may protect the general welfare through enactment of residential zoning ordinances).

[2] Cal. Const. article XI, § 7. *Miller v. Board of Public Works*, 195 Cal. 477 (1925).

EDITOR'S NOTE

This selection was developed by the staff of the Institute for Local Self Government. The idea was to provide a brief overview of the sources of authority and common initial challenges associated with inclusionary programs. The section within this paper that addresses the takings issue was developed as part of the Institute's ongoing efforts on the takings issue, which is funded by the Resources Legacy Fund (www.resourceslegacyfund.org). The Institute is also grateful to Mike Rawson of the Affordable Housing Law Project and the Western Center on Law and Poverty for providing an advance copy of his paper on this issue (entitled Inclusionary Zoning – Legal Issues*), which was funded in part by the San Francisco Foundation.*

> "[C]ounties and cites have plenary authority to govern, subject only to the limitation that they exercise this power within their territorial limits and subordinate to state law. Apart from this limitation, the police power...is as broad as the police power exercisable by the legislature itself."[3]

The police power is also "elastic," meaning that it expands to meet the changing conditions of society.[4] Moreover, legislative acts adopted under the police power are presumed justified and entitled to great judicial deference.[5] Land use regulations are generally constitutional unless they are "clearly arbitrary and unreasonable" and have no substantial relation to the public health, safety, morals, or general welfare."[6] Courts have found that a wide variety of local concerns legitimately fall within the general welfare, including socio-economic balance,[7] rent control[8] and growth management.[9] Inherent in the police power, then, is the power to condition development with particular characteristics that further the general welfare of the community.

But this authority is not unlimited. Federal and state laws – especially state-mandated local planning laws and fair housing laws – place significant limitations on local discretion to make housing decisions. Generally, these laws not only restrict exclusionary or discriminatory land use policies, but also require communities to affirmatively plan for inclusion of affordable housing. For example, cities and counties must adopt a housing element that "makes adequate provision for the housing needs of all economic segments of the community."[10] California's fair housing laws also expressly prohibit discriminatory land use polices[11] and discrimination against affordable housing[12] and the state's "anti-Not-In-My-Back-Yard" law requires local government to approve certain affordable housing developments unless certain rigorous findings are made.[13]

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[3] *Candid Enterprises, Inc. v. Grossmont Union High School Dist.*, 39 Cal. 3d 878, 886 (1985).

[4] *See Euclid* at 387, *Agins v. City of Tiburon*, 447 U.S. 255, 260-63 (1980), and *Penn Central Transp. Co. v. New York City*, 438 U.S. 104, 124 (1978).

[5] *Consolidated Rock Products v. City of Los Angeles*, 57 Cal. 2d 515 (1962).

[6] *Euclid* at 395; and *see Miller* at 490.

[7] *Village of Belle Terre v. Boraas*, 416 U.S. 1, 4-6 (1974).

[8] *Birkenfeld v. City of Berkeley*, 17 Cal. 3d 129 (1976).

[9] *DeVita v. County of Napa*, 9 Cal. 4th 763 (1995).

[10] Cal. Gov't Code § 65580 and following.

[11] Cal. Gov't Code § 12955 and following.

[12] Cal. Gov't Code § 65008.

[13] Cal. Gov't Code § 65589.5.

B. STATUTORY AUTHORITY FOR INCLUSIONARY HOUSING

In addition to the police power, there are specific instances when inclusionary programs are actually required or implicitly authorized under California law:

- ***Community Redevelopment Law.*** Local redevelopment areas must include affordable housing project if housing is developed in the area. Thirty percent of all redevelopment agency developed housing and fifteen percent of all non-agency developed housing must be affordable to lower- and moderate-income households.[14]

- ***Coastal Zone.***[15] New housing developed in the coastal zone must "provide housing units for persons and families of low or moderate income" where feasible. If including the housing within the development is not feasible, the developer must provide the housing at another location within the community unless it would be infeasible.[16]

- ***Least Cost Zoning Law.***[17] Communities must zone sufficient vacant land with appropriate standards to meet the housing needs identified in the community's housing element for all income levels.

- ***Housing Element Law.*** Local agencies must conduct an analysis of "assisted housing developments" that are eligible to change from affordable to market rate housing within the next 10 years. Assisted housing development is defined to include multifamily rental units that were developed under a local inclusionary housing program.[18]

II. TAKINGS ISSUES

Takings claims are perhaps the most often raised constitutional challenge to inclusionary housing programs.[19] There are several common misperceptions about what constitutes a taking. Much of this confusion derives from the fact that courts have been unable to articulate a uniform standard for judging taking claims, opting instead for a case-by-case

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[14] Cal. Health & Safety Code § 33413(b)(1).

[15] Cal. Gov't Code § 65590.

[16] Cal. Gov't Code § 65590(d).

[17] Cal. Gov't Code § 65913.1

[18] *See* Cal. Gov't Code § 65583(a)(8).

[19] The term derives from the Takings Clause of the Fifth Amendment of the U.S. Constitution, which states that public agencies may not take property for public use without paying just compensation. To the same effect is article 1, section 19 of the California Constitution: "Private property may be taken or damaged for public use only when just compensation, ascertained by a jury unless waived, has first been paid."

determination.[20] Despite this uncertainty, the reasonable application of an inclusionary housing program seldom rises to the level of an unconstitutional taking for three reasons:

- ***Building Affordable Housing is an Important Government Interest.*** Public agencies are advancing an important governmental interest in providing affordable housing. Regulations that advance such interests are on firmer legal ground than those that are more arbitrary in nature.

- ***Legislatively Imposed Conditions.*** Most inclusionary requirements are adopted by ordinance, which courts treat with deference. Courts reserve increased scrutiny – sometimes called heightened scrutiny – for those cases where the local agency is imposing a condition on a single landowner as part of an adjudicative decision.

- ***Property Remains Economically Viable.*** Inclusionary housing ordinances are applied only to projects where the property owner is proceeding with an economically viable use (residential units). Thus, it is difficult for the developer to assert that the ordinance denies all economic use of property.

These three reasons, however, are not guarantees. The possibility remains that an inclusionary housing ordinance may be implemented in a manner that causes a taking of property. The two types of takings challenges that are most common are "substantially advance" claims and "condition on development" cases. A third type of challenge, "denial of economic use," is theoretically possible but in most instances unlikely. Each is addressed below.

A. "SUBSTANTIALLY ADVANCE" CLAIMS

A land use regulation may constitute a taking if it fails to substantially advance a legitimate state interest.[21] A regulation may not unreasonably or arbitrarily restrict property. Courts determine whether there is a logical relationship - or "nexus" - between the purpose and effect of the regulation.[22] Put another way, the means by which the government imposes the regulation must be reasonably related to the end it is trying to achieve. A regulation is usually upheld when this connection can be drawn.

Most "substantially advance" claims are judged under a deferential standard of review, meaning that courts will defer to public agency regulation (and thus find no taking) unless the regulation is arbitrary or has no relation to a valid

[20] *Tahoe-Sierra Preservation Council v. Tahoe Regional Planning Agency*, 535 U.S. 302 (2002).

[21] *Agins v. City of Tiburon*, 447 U.S. 255 (1980).

[22] *Santa Monica Beach, Ltd. v. Superior Court*, 19 Cal. 4th 952 (1999).

public purpose. Given the latitude to regulate land use afforded local agencies under the police power, public agencies will usually prevail against such challenges to inclusionary housing programs.

For example, in *Home Builders Association of Northern California v. City of Napa (Napa)*, the challengers claimed the inclusionary housing ordinance was invalid because the inclusionary requirement would not meet its stated objective. The challengers argued that the ordinance would actually decrease the number of housing units because it would make building housing more difficult. The court rejected this argument, noting that both state statutes and case law recognize that creating affordable housing for low- and moderate-income families is a legitimate state interest.[23] Moreover, the court stated that by "requiring developers in City to create a modest amount of affordable housing (or to comply with one of the alternatives) the ordinance will necessarily increase the supply of affordable housing."[24] Thus, the Napa ordinance was sufficiently related to the stated purpose to substantially advance a legitimate state interest.[25]

B. FEES AND CONDITIONS ON DEVELOPMENT

A second type of takings challenge is that the condition imposed on the development amounts to an unconstitutional exaction. Conditions on development – such as dedications and (in California) fees – are treated as a special category under takings law. Conditions on development will usually survive judicial challenge when they are adopted legislatively and apply to a broad class of landowners.[26]

But fees and dedications that are imposed on a project-by-project basis must meet a more stringent test. The agency must demonstrate that there is a "nexus" *and* "rough proportionality" between the condition imposed and the impact of the development. This is also commonly referred to as the *Nollan-Dolan* standard, or heightened scrutiny.[27] This is a tougher, but not impossible, standard for public agencies to overcome. The reason for the

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[23] *Home Builders Association of Northern California v. City of Napa*, 90 Cal. App. 4th 188, 195 (2001). *See* Cal. Gov't Code §§ 65913.9 (finding housing for all is a matter of statewide concern) and 65580(d) (declaring local agencies have a responsibility to promote housing for all segments of the community). *See also* 4 Witkin, *Summary of California Law*, Real Property § 54 (summarizing state housing and urban development law). *Santa Monica Beach, Ltd. v. Superior Court*, 19 Cal. 4th at 970.

[24] *Napa*, 90 Cal. App. 4th at 196.

[25] This is not to say that a substantially advance challenge would never succeed. Napa involved a facial challenge, meaning that the challenger had to show that there is no way that the ordinance could be applied constitutionally. The city had included an adjustment mechanism within the ordinance, which allowed developers to apply for a reduction, adjustment or waiver. The court concluded the ordinance could not result in a taking on its face because the city could adjust its provisions to avoid an unconstitutional result. *See Napa*, 90 Cal. App. 4th at 194.

[26] *See San Remo Hotel v. City and County of San Francisco*, 27 Cal. 4th 643 (2002).

stricter standard is that courts are concerned that local agencies might "leverage" their permit approval authority to obtain excessive conditions from a single property owner. Local agencies can address this concern by legislatively adopting conditions that apply to a broad class of landowners.

In *Napa*, the court determined that the inclusionary housing program was not subject to heightened scrutiny precisely because the measure was adopted legislatively:

> Here, we are not called upon to determine the validity of a particular land use bargain between a governmental agency and a person who wants to develop his or her land. Instead we are faced with a facial challenge to economic legislation that is generally applicable to all development in [the] City.[28]

The California Supreme Court also recently addressed this issue in *San Remo Hotel v. City and County of San Francisco*.[29] The case involved a fee on the conversion of single resident occupancy hotels (an important source of low-income housing in San Francisco) to tourist hotels. The city requires that the hotel owners replace the lost affordable units on another site or pay an in-lieu fee. Again, the issue was the applicable level of judicial review. The hotel owners argued that heightened scrutiny should apply because the ordinance only affected hotel owners in the city instead of all landowners equally.

The California Supreme Court rejected the argument – finding that the increased level of scrutiny should be reserved for those *ad hoc* decision-making processes where the dangers of agencies leveraging their permit approval authority were the greatest. In doing so, the California Supreme Court laid out a blueprint for development fees for local agencies: courts will defer to legislatively imposed fees that apply without "discretion or discrimination," such that the method of imposing the fee gives no discretion to the public agency in the imposition or calculation of the fee, and the ordinance is generally applicable to a class logically subject to its strictures.[30]

C. DENIAL OF ECONOMIC USE CLAIMS

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[27] *Nollan v. California Coastal Commission*, 483 U.S. 825 (1987); *Dolan v. City of Tigard*, 512 U.S. 374 (1994). *See also Erhlich v. City of Culver City*, 12 Cal. 4th 854 (1996) (extending heightened scrutiny requirement to fees imposed on an individual or discretionary basis). *See also Santa Monica Beach, Ltd. v. Superior Court*, 19 Cal. 4th 952 (1999).

[28] *Napa*, 90 Cal. App. 4th at 197.

[29] *San Remo Hotel*, 27 Cal. 4th 643 (2002).

A possible, but unlikely challenge, to an inclusionary housing program would be that the financial impact of the inclusionary housing denies the owner of all economic use of the property. Such claims are usually evaluated by three criteria: 1) the economic impact of the regulation; 2) the degree of interference with "investment-backed" expectations; and 3) the character of the action.[31] Most regulations, however, will not be deemed a taking under this test. Only those that have the effect of severely diminishing the value of property will be a taking.

Inclusionary housing ordinances are seldom vulnerable to such challenges because, almost by definition, they do not deny all economic use of property. Instead, they merely place a condition on building housing – a very substantial use of property. Some have argued that a regulation constitutes a taking under this test where it denies a more beneficial use of property (such as the opportunity to develop free of the inclusionary requirement). However, there is no constitutional right to maximize the profit from the use of property. Thus, a regulation that denies the most profitable use, but leaves the property owner with an economically viable use, is not a taking.

III. OTHER CONSTITUTIONAL CHALLENGES

In addition to takings challenges, two other less common constitutional challenges to inclusionary housing programs are substantive due process claims and equal protection claims.

A. SUBSTANTIVE DUE PROCESS

The 14th Amendment to the U.S. Constitution provides that no state may "deprive any person of life, liberty, or property without due process of law."[32] This guarantee prevents public agencies from "enacting legislation that is 'arbitrary' or 'discriminatory' or lacks 'a reasonable relation to a proper legislative purpose.'"[33]

Opponents to inclusionary housing sometimes argue that such policies fail the reasonable relationship test because they do not assure a "fair

[30] *Id.* at 668-669.

[31] *Penn Central Transp. Co. v. New York City*, 438 U.S. 104, 124 (1978). These factors are sometimes mischaracterized as a balancing test. Nothing in the *Penn Central* decision indicates that the factors should be balanced against one another.

[32] Article I, section 7 of the California Constitution contains similar due process guarantees.

[33] *Kavanau v. Santa Monica Rent Control Bd.*, 16 Cal. 4th 761, 771 (1997) (*citing Nebbia v. New York*, 291 U.S. 502, 537 (1934)).

return" on their investments.[34] This argument relies on cases where courts have determined that rent control ordinances may violate the due process clause if they prevent investors from receiving a fair return on their investments.[35] Such arguments will generally fail for two reasons:

- ***Substantive Due Process Not Applicable to Most Economic Damage Claims.*** Substantive due process applies mostly to "'personal decisions relating to marriage, procreation, contraception, family relationships, child rearing, and education,' as well as with an individual's bodily integrity."[36] Although courts have created a small exception for highly regulated industries, the use of substantive due process to extend constitutional protection to economic and property rights has been largely discredited.[37]

- ***Takings Provides a More Appropriate Remedy.*** When there is a more appropriate remedy that "'provides an explicit textual source of constitutional protection' against a particular sort of government behavior, 'that Amendment, not the more generalized notion of substantive due process, must be the guide for analyzing such a claim.'"[38] In other words, when the Takings Clause provides constitutional protection, a substantive due process claim may be precluded.[39] The Takings Clause more directly relates to land use regulation than substantive due process.

Nevertheless, there are instances where novel challenges are forwarded that attack inclusionary requirements as price controls that violate the due process clause. For example, in the *Napa* case, the Home Builders Association contended that the inclusionary zoning ordinance was invalid under the due process clause because "the inclusionary zoning law provides no mechanism to make a fair return for property owners who are forced to sell or rent units at an amount unrelated to market prices." The court doubted that developers are entitled to a "fair return" under the due

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[34] Opponents of inclusionary zoning ordinances who use rent control cases to convince the courts that these cases apply in the zoning context must show that inclusionary zoning is similar to rent control. However, "it could be argued that rent control is essentially a species of price control rather than a land use regulation," *Santa Monica Beach, Ltd. v. Superior Court*, 19 Cal. 4th 952, 967 (1999).

[35] *See* discussion in *Napa*, 90 Cal. App. 4th 188, 198 (2001).

[36] *Armendariz v. Penman*, 75 F.3d 1331, 1318-1319 (9th Cir. 1996).

[37] *Id.*

[38] *Albright v. Oliver*, 510 U.S. 266, 273 (1994) (*quoting Graham v. Connor*, 490 U.S. 386, 395 (1989)).

[39] *Armendariz*, 75 F.3d at 1324.

process clause, but did not address the issue in great detail.[40] The court noted that the "fair return" standard developed in evaluating restrictions placed on regulated industries such as railroads and public utilities. Although it has since been used in assessing rent control ordinances,[41] the *Napa* court stated that no authority existed to extend this protection to a housing developer.[42]

B. EQUAL PROTECTION ISSUES

Although the issue is sometimes raised in connection with litigation, inclusionary housing programs seldom raise equal protection issues. Under the Equal Protection Clause of the U.S. Constitution, land use regulations may not deprive a person of equal protection of the laws.[43] This is not to say that an equal protection issue is raised each time a land use regulation affects individuals differently. Inherently, land use regulation is a system classifying property. As a result, nearly every regulation affects owners differently. What is significant for the equal protection analysis is the extent to which such distinctions are based upon personal characteristics that are otherwise protected.

Courts generally use one of three levels to analyze equal protection claims: strict scrutiny for laws that make a distinction based on a suspect classification (such as race or national origin); intermediate scrutiny for when a law makes a distinction based on quasi-suspect classifications (such as gender); and the rational basis test for all other distinctions.

Most social and economic legislation – including inclusionary housing – will usually be reviewed under the rational basis standard. Courts will uphold a local land use regulation under the rational basis test if it bears a rational relationship to a legitimate governmental interest.[44] Almost all successful equal protection challenges of land use regulations allege that a regulation has been applied in an unequal, discriminatory manner.[45]

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[40] *Napa*, 90 Cal. App. 4th at 199 ("...[W]e are not aware of...any case that holds a housing developer is entitled to "fair return" on his or her investment").

[41] *Id.* (citing *Fisher v. City of Berkeley*, 37 Cal. 3d 644, 679 (1984)).

[42] *Id.* The court in *Napa* stopped short of holding that the "fair return" standard did not apply in inclusionary zoning cases because it could find the Napa ordinance facially valid on other grounds.

[43] U.S. Const. amend. XIV; Cal. Const. art. I, § 7.

[44] *See Construction Industry Association of Sonoma County v. City of Petaluma*, 522 F.2d 897, 906 (9th Cir. 1975), *cert. denied*, 424 U.S. 934 (1976). Only if a land use regulation intentionally discriminates against a "suspect class" of persons (for example, racial or ethnic minorities) or denies someone a "fundamental right" (for example, the right to live as a family) will it be held to the much tougher "strict scrutiny" test. Under that test, the local agency would have to show that the regulation served a "compelling governmental interest."

Accordingly, inclusionary requirements should be based on a sound analysis of the need for affordable housing and apply uniformly to all similarly situated developers. All exemptions or categories of alternative performance should likewise have a clear basis and clear standards for eligibility.

IV. SPECIAL CONSIDERATIONS FOR FEES

In-lieu fees are another area where legal issues are raised in connection with inclusionary housing ordinances. Inclusionary housing programs typically include such fees as an option for developers. Such programs usually require a developer to include a certain percentage of affordable housing within the project, or as an alternative, to pay a fee in lieu of building the housing.

A. MITIGATION FEE ACT

One issue that arises in connection with in-lieu fees is whether the agency must comply with the Mitigation Fee Act (also called "AB 1600" fees after the Mitigation Fee Act's adopting legislation).[46] The Mitigation Fee Act regulates the adoption, levy, collection and challenge to development fees imposed by local agencies and applies to fees imposed on a broad class of projects on a project-specific basis.[47]

Under takings law and California's Mitigation Fee Act, the imposition of fees to mitigate the impacts of a development must be based on facts that establish a nexus between the need for and amount of the fee and the stated impacts. Thus, local agencies will often produce a "nexus study" assessing the impacts of development and the costs of effective mitigation before enacting an ordinance that imposes a fee.

The Mitigation Fee Act, however, does not technically extend to "in-lieu" fees because the fee is an alternative to the condition that affordable units be

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[45] *See Longtin's California Land Use*, 2002 Update at §1.32[3], 27-29. *See also Village of Willowbrook v. Olech*, 528 U.S. 1073 (2000).

[46] *See* Cal. Gov't Code §§ 66000 and following.

[47] *See* Cal. Gov't Code § 66000(b).

included within the development. Having said this, a public agency is still well advised to have an identifiable basis for setting the in-lieu fees for inclusionary housing ordinances. A well-documented fee study that carefully explains its assumptions and conclusions will be more credible to the development community and the public. A good study will:

- Identify and quantify the adverse impacts that development has on the availability of affordable housing in the jurisdiction;
- Use local data rather than statewide data to justify the fee whenever possible;
- Use reasonable estimates where hard data is unavailable or prohibitively expensive; and
- Provide the basis for a sound but simple way of calculating the in-lieu fee to assist those affected and the public in understanding the fee.

The Mitigation Fee Act's template for designing an impact fee study can serve as a useful starting point. An ordinance should be based on sufficient facts and analysis to demonstrate the need for affordable housing in the community and the relationship or nexus of the inclusionary obligation to fulfillment of the need.

New fees sometimes are criticized as singling out developers to bear burdens that should be imposed on the public at large. Staff should anticipate this criticism by documenting the full range of existing and planned public resources devoted to the program financed by the fee.

B. CHALLENGES TO FEES AS TAXES AND FEE RESTRICTIONS

This kind of challenge is similar to the Mitigation Fee Act challenge, inasmuch as it singles out the in-lieu fee portion of an inclusionary housing ordinance. In *Napa*, the challengers also contended the in-lieu fee was a tax, subject to various constitutional restrictions relating to how taxes are imposed. The court, in an unpublished portion of the opinion, rejected those claims. Here are the salient arguments from the public agency perspective:

- The in-lieu fee is an option under the ordinance and therefore does not have the "compulsory" element of being a tax.[48]
- The in-lieu fee does not violate Proposition 62 (and Proposition 62 does not apply to charter cities[49]) and is not a special tax.[50]

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[48] *See Loyola Marymount University v. Los Angeles Unified School Dist.*, 45 Cal. App. 4th 1256, 1267 (1996); *Trent Meredith, Inc. v. City of Oxnard*, 114 Cal. App. 3d 317, 328 (1981).

- It is also not a property-related fee[51] (or imposed as an incident of property ownership) and is thus exempt from Proposition 218.[52]
- Even if the ordinance were a tax, it is not on property, but on the privilege of developing land.
- Even if the ordinance were a tax, it has none of the incidents of a property tax.[53]

Having a well-documented fee study and findings that establish that the in-lieu fee is indeed an option should cause any legal analysis to begin and end with the first bullet.

V. COSTA-HAWKINS ACT ISSUES

An issue that is arising with some frequency is whether the Costa-Hawkins Rental Housing Act ("Costa-Hawkins Act")[54] preempts a local agency's authority to set maximum rents on inclusionary rental units. Some have argued that the Costa-Hawkins Act prohibits local agencies from regulating rents on inclusionary units. If a court upheld this argument, the affordability requirements imposed on inclusionary rental units would be meaningless. Landlords could simply ignore the affordability

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[49] *Burbank-Glendale-Pasadena Airport Authority v. City of Burbank*, 64 Cal. App. 4th 1217, 1226-27 (1998); *Fisher v. County of Alameda*, 20 Cal. App. 4th 120, 125-30 (1998); *Fielder v. City of Los Angeles*, 14 Cal. App. 4th 137 632-35 (1993); *see also Santa Clara County Local Transportation Authority v. Guardino*, 11 Cal. 4th 220, 260-61 (1995) (acknowledging that ballot materials advised voters that Proposition 62 is inapplicable to charter cities).

[50] *Terminal Plaza Corp. v. City & County of San Francisco*, 177 Cal. App. 3d 892, 905-7 (1986) (stating that fees are not taxes when they are: 1) limited to amounts necessary to construct affordable housing, 2) not imposed for general revenue purposes, 3) not imposed upon land generally, but on the privilege of developing residential property, and 4) not compulsory, because a developer retains the option not to develop). *See also* Cal. Gov't Code § 66024 (requiring challenger to pay fee before initiating legal challenge).

[51] *See* Cal. Const. art. XIIID, § 2.

[52] *See* Cal. Const. art. XIIID, § 1(b) (expressly exempting fees or charges as a condition of property development). Any in-lieu fees for inclusionary housing, if paid by a developer, are paid as a condition of property development.

[53] *See Flynn v. San Francisco*, 18 Cal. 2d 210, 214 (1941) (whether a particular enactment amounts to a tax on property must be determined by its incidents, and from the natural and legal effect of the language of the act); *City of Oakland v. Digre*, 205 Cal. App. 3d 99, 106-7 (1988) (describing characteristics of property taxes: tax ownership per se without conditions; often measured by the size and type of the property taxed; levied without regard for the use to which the property is put; generally due and payable annually at a set time; and generally secured by the property taxed); *Terminal Plaza Corp. v. City & County of San Francisco*, 177 Cal. App. 3d 892, 907 (1986) (holding that a fee imposed upon the privilege of development is a regulatory fee, not tax on property).

[54] Cal. Civ. Code §§ 1954.50-1954.535. The Costa-Hawkins Act was enacted in 1995 to "establish a comprehensive statewide scheme to regulate local residential rent control." *Cobb v. City and County of San Francisco Residential Rent Stabilization and Arbitration Board*, 98 Cal. App. 4th 345 (2002).

controls and set their own rents. Although the language of the Costa-Hawkins Act does not address this issue squarely, as is described more fully below, the more plausible conclusion is that the Costa-Hawkins Act does not apply to inclusionary rental units.[55]

The Costa-Hawkins Act was adopted to limit the authority of local agencies to adopt rent control programs by providing property owners the sole authority to establish the rental rates for dwelling units constructed after February 1, 1995. The Act, however, includes one important exception; it does not apply to rental units when:

> [t]he owner has otherwise agreed by contract with a public entity in consideration for a direct financial contribution or any other forms of assistance specified in Chapter 4.3 (commencing with Section 65915) of Division 1 of Title 7 of the Government Code.[56]

Chapter 4.3 – often referred to as the "Density Bonus Law" – encourages low-income housing in exchange for incentives such as increasing the number of permitted units within a zoning designation, relaxing development or architectural design standards, approving mixed development, providing infrastructure, "writing down" land costs or subsidizing the cost of construction.[57] In other words, a rental unit is not subject to the Costa-Hawkins Act if it has been built under a contract with a public agency in exchange for a financial contribution or other form of assistance included in the Density Bonus Law.[58]

The legislative history of the Costa-Hawkins Act also indicates that the Act was not intended to apply to inclusionary programs. There are at least four "sponsor statements"[59] from co-author Assemblyman Phil Hawkins stating that the Costa-Hawkins Act would only affect five cities that had "extreme vacancy control," meaning that they had adopted rent controls that

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[55] The Costa-Hawkins Act only applies to rental units and is therefore not an issue for owner-occupied units.

[56] *See* Cal. Civ. Code § 1954.53(a)(2).

[57] Cal. Gov't Code § 65916.

[58] It is less clear to what extent similar incentives provided outside of the Density Bonus Law are similarly excepted. A good argument exists that such units are similarly excepted because the Costa-Hawkins Act refers only to the "forms" of assistance mentioned in the Density Bonus Law, not to actual assistance. *See* Cal. Civ. Code § 1954.52(a)(2). Assuming that the "or" is disjunctive, the Costa-Hawkins Act should not apply to rental units created under an inclusionary agreement where the developer has received financial assistance or incentives from the local agency, whether or not such assistance originated under the color of a density bonus law.

[59] Courts may consider "sponsor statements" in determining legislative intent. *See Nadia El Mallakh, Does the Costa-Hawkins Act Prohibit Local Inclusionary Zoning Programs?*, 89 Cal. L. Rev. 1847, 1866 (2001) (*citing Lopez v. Tulare Joint Union High Sch. Dist.*, 34 Cal. App. 4th 1302, 1324 n.6 (1995); Kern v. County of Imperial, 226 Cal. App. 3d 391, 401 n.8 (1990).

required rents to remain the same even when a tenant voluntarily or lawfully vacated a unit. At the time, more than 70 local agencies had inclusionary rental programs, which were not deemed extreme rent control by the author.[60]

The conclusion that the Costa-Hawkins Act does not apply to inclusionary rental housing is also supported by language in the housing element law.[61] One of the law's requirements (in effect at the Costa-Hawkins Act's passage) is that local agencies must analyze existing "assisted housing developments" that are in danger of transitioning out of low-income status. "Assisted housing developments" are defined to include "multifamily rental units that were developed pursuant to a local inclusionary housing program."[62] If the Costa-Hawkins Act prohibits the regulation of rents on inclusionary units, this provision of the housing element law would be meaningless: local agencies would be required to account for a source of housing that they could not manage. Such a result would conflict with the general rule that the Legislature is presumed to be aware of existing law and that a court's duty is to give effect to all law if possible.[63]

Despite this reasoning that inclusionary rental programs are outside of the reach of the Costa-Hawkins Act, the issue is ultimately one of statutory construction that would benefit from clarification by the courts or the Legislature. To date, the issue has been presented to at least two California courts, but neither had the opportunity to reach the merits of the issue. In one case against the County of Santa Cruz, a court of appeal decision applied a 90-day statute of limitations to a Costa-Hawkins claim.[64] The second case was dismissed when the City of Santa Monica amended its ordinance.[65]

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[60] *Id.*

[61] Cal. Gov't Code § 65580 and following.

[62] *See* Cal. Gov't Code § 65583(a)(8).

[63] *In re Lance W.*, 37 Cal. 3d 873, 891 n. 11 (1985) ("The adopting body is presumed to be aware of existing laws and judicial construction thereof (*Bailey v. Superior Court*, 19 Cal.3d 970, 978, fn. 10 (1977)) and to have intended that its enactments be constitutionally valid. (In re Kay (1970) 1 Cal.3d 930, 942.)"). *See also Halbert's Lumber , Inc. v. Lucky Stores*, 6 Cal. App. 1233, 1238-39 (1992) (discussing sequence for applying rules of statutory construction).

[64] *See Travis v. County of Santa Cruz*, 100 Cal. App. 4th 609 (2002), *rev. granted.*

[65] El Mallakh, *supra* at 1851. The City of Santa Monica's solution was unique. The ordinance was amended to permit developers to meet their mandatory affordable housing obligations by either (1) paying a fee or (2) in lieu of paying a fee, develop affordable units that qualify for a density bonus under state law. In other words, where most inclusionary ordinances require the developer to build housing or pay an in-lieu fee, Santa Monica reversed this process; developers must pay a fee or build in-lieu housing. Santa Monica, Cal., Code § 9.56.050.

VI. PROACTIVE MEASURES TO AVOID LITIGATION

A. CREATE REALISTIC EXPECTATIONS IN THE GENERAL PLAN

An up-to-date and comprehensive general plan, supported by a master environmental document, lays a solid foundation for all land use regulation. These documents also create realistic expectations among landowners by describing the community's vision for development. A clear statement within the general plan that demonstrates the community's commitment to affordable housing and use of inclusionary policies helps set such expectations. Provided with this direction, landowners are more likely to propose new land uses that are consistent with the vision articulated in the general plan, which reduces the potential for litigation.

B. IMPLEMENT INCLUSIONARY REQUIREMENT LEGISLATIVELY

Some jurisdictions have imposed inclusionary requirements on the basis of general statements of policy in their housing element or other housing strategy documents. This can lead to the kind of individualized ad hoc application that invites takings or other legal challenges. Local agencies are on firmer ground if they impose conditions of development legislatively (by ordinance).

C. PROVIDE INCENTIVES AND ALTERNATIVES.

Including significant incentives and regulatory concessions for developers that comply with the inclusionary requirement will also make such regulations easier to accept. In *Napa*, the court cited the city's use of expedited processing, fee deferrals, loans or grants and density bonuses with approval. Many of these incentives – such as density bonuses and expedited processing – are inexpensive to provide and can be very significant to a developer. One study has shown that a such programs can offset the developer's costs in providing the inclusionary units.[66]

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[66] Andrew G. Dietderich, *An Egalitarian Market: The Economics of Inclusionary Zoning Reclaimed*, 24 Fordham Urb. L.J. 23 (1996).

D. INCLUDE A VARIANCE TO ACT AS A SAFETY VALVE

Local agencies should consider including a variance or adjustment process as part of an inclusionary housing ordinance. As a general rule, landowners must seek a variance, if one is offered, before going to court. A procedure that allows for exceptions in cases of extreme economic hardship ensures that the agency has the opportunity to modify its policies to avoid unfair results.

Indeed, the inclusion of a waiver provision was important to the *Napa* court's finding that the inclusionary ordinance did not constitute a taking on its face. While the process should be clear and easy to use, the onus should be on the developer to demonstrate that a reduction or waiver of inclusionary requirements is necessary. The variance or waiver provision should set standards for the extent of the reduction if it is determined that the terms of the ordinance should be modified. For example, many agencies permit a reduction or waiver only to the extent that the developer can show that the inclusionary requirement would violate the California or U.S. Constitutions.

E. USE FINDINGS TO DEMONSTRATE NEXUS

"Findings" are written explanations of why – legally and factually – a public entity is making a particular decision. Findings need to explain how and why the regulation involved meets the constitutionally or statutorily required standard.[67] An inclusionary housing ordinance should contain findings that demonstrate the need for affordable housing and explain how the ordinance will address that need. Findings may be based on public input, studies and other objective sources of information. In *Napa*, for example, the court noted that the city supported its position with 700 pages of reports and materials that the city had relied on in adopting the ordinance.[68]

Good findings depend on good information. Many local agencies conduct a nexus study to establish the need for a fee. There are many existing sources of data that demonstrate the need for affordable housing. For example, the housing element often includes the community's allocated share of the regional need for housing affordable to lower income households. Local jurisdictions that receive certain entitlement funds from the U. S. Department of Housing and Urban Development must prepare

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[67] *Findings 101: Explaining a Public Agency Decision, Western City*, May 2000, at 13.

[68] *Napa*, 90 Cal. App. 4th 188, 193 (2001).

an analysis of impediments to fair housing. This analysis can provide data supporting inclusionary zoning as a means of combating housing segregation. There are many other sources of information, including the local public housing authority, social services offices and homeless services providers.

F. ADDRESS COSTA-HAWKINS ACT ISSUES

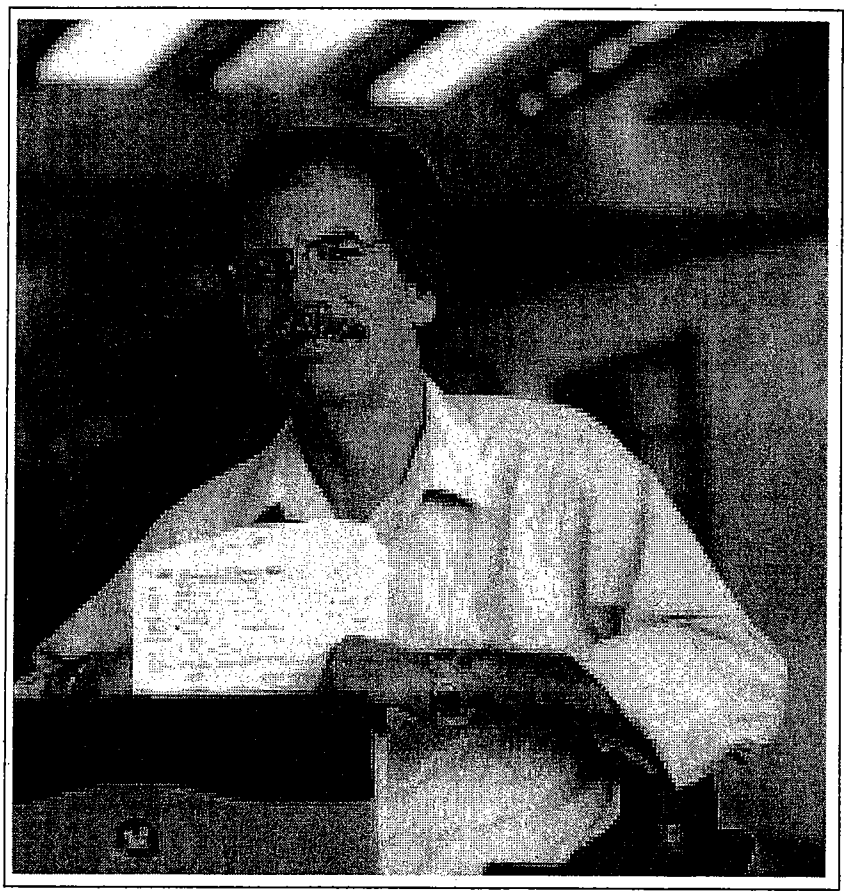
While the Costa-Hawkins Act should not apply to inclusionary rental units, absent clarifying legislation or a court opinion, there is no way to be fully certain. One strategy a local agency can employ to minimize risk in this regard is to provide assistance, such as an increased number of units, relaxed design standards or subsidies, for inclusionary units and require a contract between the agency and the developer to develop the inclusionary rental units *(See Part V above)*.

G. BE FAIR

Finally, consider the fairness of an agency's approach to inclusionary housing. Courts often view their fundamental role as dispensing justice. A public agency will have an easier time in the courtroom if the regulation was adopted with significant public involvement and ample opportunities to avoid unjust results.

Part VI

A Sample Ordinance



The Faces of Affordable Housing

Nick Renteria

"Living in affordable housing has helped me manage to get started in my business. Now I can see growing it in a way that I can provide for my family."

Nick was born is Zacatecas, Mexico and moved to Santa Barbara in 1972. He lives with his family and works in accounting and tax preparation. One of the best things about his job is building relations with clients and being able to help and talk with them as friends. Nick's most memorable life experience is graduation from Santa Barbara Business College. Nick lives in an 11 unit family complex that serves as a good example of the Housing Authority's efforts to build within the urban core and along transportation corridors. Ten of the units are townhouse in design and one is fully accessible for the handicapped. Build in the style of a European Village by the Housing Authority in 1995, it offers affordable housing that is close to shopping, public transportation and local schools.

– Housing Authority of the City of Santa Barbara - 2002 Calendar

ANNOTATED SAMPLE INCLUSIONARY HOUSING ORDINANCE

This selection consists of a sample inclusionary housing ordinance. The word "sample" is chosen carefully because this is not intended to be –nor should it be mistaken for- a "model" ordinance. Instead, it is presented as a potential starting point for local agencies in California considering adopting or revising an inclusionary housing ordinance.

A REFERENCE TOOL, NOT A TEMPLATE

The ordinance presented here is probably not in the best form to actually be incorporated into a local municipal code. It was designed to be more of a teaching device than an actual ordinance. As a result, provisions have been included that many agencies would normally exclude or include in a different ordinance. For example, at least two of the people who reviewed the ordinance (recognized below) recommended that we omit the section of the ordinance that applied to commercial development. It would be cleaner, they argued, if the fee on development was encompassed in a separate ordinance instead of combined with the provisions and process of a typical inclusionary housing ordinance. Their recommendation is a good one, but we nevertheless left the provision in to raise the issue as an option for local agencies.

This ordinance may also be a little heavy on detail. In practice, many agencies adopt less detailed ordinances and then develop a set of implementation procedures to deal with day-to-day implementation issues. This two-step process affords local agencies the opportunity to design programs more carefully and even seek additional input from those most likely to be affected by the ordinance. It also allows the flexibility to manage the inclusionary program over several decades. As a reference tool, however, the Sample Ordinance, addresses several of these underlying issues in an effort to highlight many of the issues that are likely to arise after the initial adoption of an inclusionary housing ordinance.

Another feature of the ordinance is the Drafting Notes, which provide practice tips and references that discuss policy choices and legal issues that arise in connection with specific provisions. The issues are raised with the hope that they may be useful in helping tailor an ordinance to fit the needs of a specific community.

In short, this sample document is offered to further the discussion of inclusionary housing in California. The Institute believes that there are still many improvements and corrections that could be made, and would welcome any comments or suggestions that anyone would have.

THANK YOU TO OUR REVIEWERS

Several individuals lent their valuable time and considerable expertise by reviewing the Sample Ordinance and offering helpful suggestions. Each deserves a great deal of credit for raising issues and questions on early drafts and shaping the final product:

- **Richard Judd**, Goldfarb and Lipman (San Francisco)
- **Michael Colantuono**, Colantuono, Levin & Rozell (Los Angeles)
- **Susan Cleveland**, Deputy City Attorney, San Francisco
- **Iris Yang**, Shareholder, McDonough, Holland & Allen (Sacramento)
- **Craig Labadie**, City Attorney, City of Concord
- **Michael Rawson**, California Affordable Housing Project (Oakland)

Despite these acknowledgements, the participation by the reviewers is not an endorsement of the sample ordinance. All final decisions as to content were made by the staff of the **Institute for Local Self Government**. As explained above, some of the comments and suggestions we received were not included in the final version. Thus, to the extent that there are any mistakes or errors, the Institute bears sole responsibility.

ANNOTATED SAMPLE INCLUSIONARY HOUSING ORDINANCE[1]

Chapter 10-10 of the Municipal Code

SECTION 10-10-100. PURPOSE.

The purpose of this Chapter is to:

(a) Encourage the development and availability of housing affordable to a broad range of Households with varying income levels within the City as mandated by State Law, California Government Code Sections 65580 and following.

(b) Promote the City's goal to add affordable housing units to the City's housing stock in proportion to the overall increase in new jobs and housing units;

(c) Offset the demand on housing that is created by new development and mitigate environmental and other impacts that accompany new residential and Commercial Development by protecting the economic diversity of the City's housing stock, reducing traffic, transit and related air quality impacts, promoting jobs/housing balance and reducing the demands placed on transportation infrastructure in the region;

(d) [*Identify additional local policies, especially in the General Plan, which this ordinance serves, to provide a stronger policy basis and deeper record to support the ordinance.*]

SECTION 10-10-110. FINDINGS.[2]

The City Council finds and determines:

(a) Both California and the City face a serious housing problem that threatens their economic security. Lack of access to affordable housing has a direct impact upon the health, safety

DRAFTING NOTES

[1] VOLUNTARY VERSUS MANDATORY PROGRAMS. The Sample Ordinance provides a mandatory compliance procedure for inclusionary housing. Some agencies have adopted voluntary programs, but anecdotal evidence suggests that they have been less effective in producing Inclusionary Units.

[2] FINDINGS. Findings describe how the ordinance addresses the community's need for affordable housing. The findings should reference the general plan policies to be implemented by the ordinance and should refer to and incorporate by reference any economic studies or other reports on which the ordinance is based. Findings should include a description of the reasons why the local agency has decided to take the action. Findings should be as specific to the jurisdiction as possible. *See Findings 101: Explaining a Public Agency Decision, Western City*, May 2000, at 13 (www.westerncity.com/Findings101May00.htm).

and welfare of the residents of the City. The City will not be able to contribute to the attainment of State housing goals or to retain a healthy environment without additional affordable housing. The housing problem has an impact upon a broad range of income groups including many who are not impoverished by standards other than those applicable to California's and the City's housing markets, and no single housing program will be sufficient to meet the housing need.

(b) The [*insert source,*][3] has determined that [*insert relevant facts specific to the locality, for example: "65 percent of the new Households in the City will have Very Low-, Low- or Moderate-Incomes"*]. A lack of new Inclusionary Units will have a substantial negative impact on the environment and economic climate because (i) housing will have to be built elsewhere, far from employment centers and therefore commutes will increase, causing increased traffic and transit demand and consequent noise and air pollution; and (ii) City businesses will find it more difficult to attract and retain the workers they need. Inclusionary housing policies contribute to a healthy job and housing balance by providing more affordable housing close to employment centers.

(c) Among City groups with especially significant housing needs are: [*insert groups, for example: (1) families earning less than 80 percent of the median county income ($38,000 per year for a family of four) and (2) families earning less than 110 percent of the median county income ($52,000 per year for a family of four) and desiring to purchase their first home*].

(d) Development of new commercial projects and market-rate housing encourages new residents to move to the City. These new residents will place demands on services provided by both the public and private sectors. Some of the public and private sector employees needed to meet the needs of the new residents or Commercial Development earn incomes only adequate to pay for affordable housing. Because affordable housing is in short supply within the City, these employees may be forced to live in less than adequate housing within the City, pay a disproportionate share of their incomes to live in adequate housing within the City, or commute ever-increasing distances to their jobs from housing located outside the City. These circumstances harm the City's ability to attain goals articulated in the City's General Plan and strain the City's ability to accept and service new market-rate housing development.

DRAFTING NOTES

[3] SOURCES OF DATA. There are many sources of data that can demonstrate the need for affordable housing. This information can be incorporated into findings by reference. For example, the City's Housing Element will include the community's allocated share of the regional need for housing affordable to lower income households. For HUD entitlement jurisdictions, the Analysis of Impediments to Fair Housing Choice (AI) in the local Consolidated Plan can provide data supporting inclusionary zoning as a means of combating housing segregation. There are many other sources of information, including the local public housing authority, councils of government, developers, social services offices and homeless services providers.

(e) The California Legislature has required each local government agency to develop a comprehensive, long-term general plan establishing policies for future development. As specified in the Government Code (at Sections 65300, 65302(c), and 65583(c)), the plan must: (i) "encourage the development of a variety of types of housing for all income levels, including multifamily rental housing;" (ii) "[a]ssist in the development of adequate housing to meet the needs of low- and moderate-income households;" and (iii) "conserve and improve the condition of the existing affordable housing stock, which may include addressing ways to mitigate the loss of dwelling units demolished by public or private action."

(f) The citizens of the City seek a well-planned, aesthetically pleasing and balanced community, with housing affordable to Very Low-, Low- and Moderate-Income Households. Affordable housing should be available throughout the City, and not restricted to a few neighborhoods and areas. However, there may also be trade-offs where constructing affordable units at a different site than the site of the principal project may produce a greater number of affordable units without additional costs to the project applicant. Thus, the City finds that in certain limited circumstances, the purposes of this Chapter may be better served by allowing the Developer to comply with the inclusionary requirement through alternative means, such as the payment of in-lieu fees, development of offsite housing or dedication of land. For example, if a project applicant can produce a significantly greater number of affordable units off-site, then it may (but not always) be in the best interest of the City to permit the development of affordable units at a different location than that of the principal project.

(g) Federal and state funds for the construction of new affordable housing are insufficient to fully address the problem of affordable housing within the City. Nor has the private housing market provided adequate housing opportunities affordable to Moderate-, Low- and Very Low-Income Households.

(h) The City Council established an Affordable Housing Task Force[4] that was charged with recommending an appropriate affordable housing program. The Task Force conducted an investigation, held hearings and solicited comments from the community regarding a range of options. On _____, the Task Force presented a number of recommendations, including a proposed inclusionary housing ordinance. The Planning Commission accepted the Task

DRAFTING NOTES

[4] DESCRIPTION OF PROCESS. This finding would be applicable if the City engaged in a stakeholder or other public input process to develop the inclusionary housing ordinance. Such findings are not essential if the local agency has developed a good record that describes the need for affordable housing and its nexus to new development. However, findings are also a place to highlight the "good facts" that helped a local agency reach a particular decision, particularly when there is a chance that the ordinance might be challenged. One appellate court, for example, noted that the City of Napa had employed a consensus process in developing an inclusionary housing ordinance. *See Home Builders Association of Northern California v. City of Napa*, 90 Cal. App. 4th 188 (2001).

Force's Final Report on _____. The City Council gave conceptual approval to an inclusionary housing program and directed staff to develop an ordinance that reflected the recommendations of the Task Force. Based on the findings of the Task Force, the City Council finds that it is necessary to adopt an inclusionary housing ordinance in order to address the City's housing crisis.

(i) The City is aware that there may be times when the inclusionary housing requirements make market-rate housing more expensive.[5] In weighing all the factors, including the significant need for affordable housing, the City has made the decision that the community's interests are best served by the adoption of the inclusionary housing ordinance.

(j) [*To the extent that an ordinance includes a fee on commercial development, include findings required by the Mitigation Fee Act (see Note 16). Such findings will be specific to each community. In most cases, findings are based on a supporting nexus study that demonstrates the connection between new commercial development and the need for affordable housing.*]

SECTION 10-10-120. DEFINITIONS.[6]

As used in this Chapter, the following terms shall have the following meanings:

(a) **Affordable Rent** means monthly rent that does not exceed one-twelfth of 30 percent of the maximum annual income for a Household of the applicable income level (Moderate-, Low- or Very Low-Income).

(b) **Affordable Ownership Cost** means a sales price that results in a monthly housing cost (including mortgage, insurance and home association costs, if any) that does not exceed one-twelfth of 30 percent of the maximum annual income for a Household of the applicable income (Moderate-, Low- or Very Low- Income).

DRAFTING NOTES

[5] EFFECT OF INCLUSIONARY ORDINANCE ON HOUSING PRICES. Whether or not inclusionary housing policies actually make new homes more expensive is debatable. Developers often argue that consumers of new market rate housing must pay higher prices to cover the cost of inclusionary housing. Inclusionary housing advocates counter that the long-term impact is to reduce the value of raw land – that is, the developer will pass on the additional cost to the original landowner in the form of a lower purchase price. The Sample Ordinance raises the issue here merely to underscore that the legislative body considered the potential economic consequences and, on balance, determined that the community's interests are best served by the adoption of the ordinance.

[6] DEFINITIONS GENERALLY. This section defines all key terms used in the ordinance. Although some definitions simply clarify the terms in the ordinance, others will have a significant effect on the scope and implementation of the ordinance. Since ordinances are sometimes challenged for being vague, a good rule is to define as many terms as possible to limit misunderstanding. All definitions should be consistent with terms used in existing local agency ordinances and policies, such as the general plan, zoning ordinances and other housing policies.

(c) **Alternative Housing Proposal** means a proposal to build Inclusionary Units in lieu of paying a fee on Commercial Development as provided in Section 10-10-140(b).

(d) **Area Median Income** means the median Household income as provided in Section 50093(c) of the California Government Code.

(e) **City** means the City of _____.

(f) **City Manager**[7] means the City Manager of the City or his or her designee.

(b) **Commercial Development** means the construction of any commercial or industrial project, as defined by Section [*insert section number*] of the Zoning Code, for which a tentative map or building permit application was received after [insert effective date of ordinance].

(h) **Construction Cost Index** means [*insert reference to local construction cost index such as the Engineering News-Record San Francisco Building Cost Index*]. If that index ceases to exist, the City Manager will substitute another Construction Cost Index, which, in his or her judgment, is as nearly equivalent to the original index as possible.

(i) **Developer** means any person,[8] firm, partnership, association, joint venture, corporation, or any entity or combination of entities, which seeks City approvals for all or part of a Residential or Commercial Development.

(j) **Household** means one person living alone or two or more persons sharing residency whose income is considered for housing payments.

(k) **Inclusionary Housing Plan** means a plan for a residential or Commercial Development submitted by a Developer as provided by Section 10-10-240(b).

(l) **Inclusionary Housing Agreement** means a written agreement between Developer and the City as provided by Section 10-10-240(c).

(m) **Inclusionary Unit** means a dwelling unit that must be offered at Affordable Rent or available at an affordable housing cost to Moderate-, Low- and Very Low-Income Households.

DRAFTING NOTES

[7] CITY MANAGER'S ROLE. The Sample Ordinance delegates most of the implementation authority – such as entering into Affordable Housing Agreements and waiver and adjustment determinations – to the City Manager. However, such delegation can vary. Depending on the organizational structure of the local agency, such authority can be delegated to the Planning Commission, Housing Authority Director or Community Development Director.

[8] DEFINITION OF "PERSON." Many local agencies already have an adequate definition of "person" in their code, in which case, "firm... entities," can be deleted.

(n) **Low-Income Household** means a Household whose annual income does not exceed the qualifying limits set for "lower income households" in Section 50079.5 of the California Government Code.[9]

(o) **Market-rate Unit** means a dwelling unit in a Residential Development that is not an Inclusionary Unit.

(p) **Moderate-Income Household** means a Household whose income does not exceed the qualifying limits set for "persons and families of low or moderate income" in Section 50079.5 of the California Government Code.

(q) **Off-Site Unit** means an Inclusionary Unit that will be built separately or at a different location than the main development.

(r) **On-Site Unit** means an Inclusionary Unit that will be built as part of the main development.

(s) **Residential Development** means the construction of any residential dwelling units where the tentative map, parcel map or, for project not processing a map, the building permit was received after [*insert effective date of ordinance*].[10]

(t) **Very Low-Income Household** means a Household whose income does not exceed the qualifying limits set for "very low income households" in Section 50079.5 of the California Government Code.

DRAFTING NOTES

[9] INCOME HOUSEHOLD DEFINITIONS. Definitions that cross-reference the California Health & Safety Code should make local action to update income levels unnecessary. *See* Cal. Health & Safety Code §§ 50079.5, 50093, 50105 and 50106. These standards are published in the California Code of Regulations. *See* Cal. Code of Regs. tit. 25, §§ 6926 – 6932. Many public funding sources rely on statutory income and housing or rental cost definitions in providing funds for affordable housing. Thus, unless the local agency is addressing a specific local need, it is usually helpful if local agencies include these statutory definitions to assure consistency with state and federal housing programs. However, communities whose affordability characteristics differ from those of the county of which they are a part may choose to accept the funding complications and other complexities involved in defining their own affordability thresholds. Such provisions should be carefully drawn and be based upon a record that justifies selection of the threshold so defined.

[10] EFFECTIVE DATE. Note that this provision is being used to set the effective date of the ordinance. The inclusionary requirements will apply to all map applications received after the effective date.

[11] RESIDENTIAL INCLUSIONARY REQUIREMENT. The California Department of Housing and Community Development (HCD) may require a showing that the inclusionary requirement will not unduly constrain the development of affordable housing. *See* Cal. Gov't Code § 65583(a)(4). Consequently, the existence of clear standards and procedures make it easier to demonstrate that the requirements will result in additional affordable housing. Most local agencies in California that

(continued on next page)

SECTION 10-10-130. RESIDENTIAL DEVELOPMENT.[11]

For all Residential Developments of 7 or more units, at least 15 percent of the total units must be Inclusionary Units restricted for occupancy by Moderate-, Low- or Very Low-Income Households.[12] The number of Inclusionary Units required for a particular project will be determined only once, at the time of tentative or parcel map approval, or, for developments not processing a map, prior to issuance of a building permit. If a change in the subdivision design results in a change in the total number of units, the number of Inclusionary Units required will be recalculated to coincide with the final approved project.

(a) **Calculation**. For purposes of calculating the number of affordable units required by this Section, any additional units authorized as a density bonus under California Government Code Section 65915(b)(1) or (b)(2) will not be counted in determining the required number of Inclusionary Units. In determining the number of whole Inclusionary Units required, any decimal fraction less than 0.5 shall be rounded down to the nearest whole number, and any decimal fraction of 0.5 or more shall be rounded up to the nearest whole number.

(b) **Type of Inclusionary Units.**[13] At least one-third of the Inclusionary Units (or 5 percent of the total development) must be restricted to occupancy by Low-Income Households. An additional one- third of the Inclusionary Units (or 5 percent of the total development) must

DRAFTING NOTES

have adopted inclusionary housing programs have imposed an inclusionary requirement between 10 and 20 percent of the total units, though the range is from 5 to 60 percent. Other variations in application include:

- ***Special Provisions for Senior Housing.*** For example, the City of Napa requires that 50 percent of all units designated for senior residents be affordable.
- ***Different Requirements for Single and Multiple Family Housing.*** On the theory that multifamily units are more affordable than single-family units, some agencies adopt a higher requirement for single-family units. The local agency should lay out the justification for different treatment in the findings section.
- ***Location.*** Local agencies can target certain areas when the record supports such action. Some agencies increase the inclusionary requirement in their downtown or redevelopment zones. The rationale for such distinctions should be explained in supporting materials submitted to the decision-maker and incorporated by reference into the findings. In coastal areas, staff should consider whether the local coastal plan imposes special requirements and cite the policies of the Coastal Act even if it does not. *See* Gov't Code § 65590.

[12] THRESHOLD SIZE. Minimum project size varies widely among California local agencies, but most range from 5 to 20 units. Thresholds are adopted to make small projects more feasible. An increasing number of local agencies are applying inclusionary requirements to all projects, including small ones, but only require that a proportional fee be paid on small projects (in which case, the fee ceases to be "in-lieu," and becomes the primary condition of development). *See* Note 16, below.

be restricted to occupancy by Very Low-Income Households. To encourage additional development of Low- and Very Low-Income housing, the following equivalents shall be used in determining compliance:

(1) Each Very Low-Income unit is equivalent to 2 units affordable to Moderate-Income Households.

(2) Each Low-Income unit is equivalent to 1.5 units affordable to Moderate-Income Households.

(c) Sequence of Inclusionary Units.[14] The first Inclusionary Unit occupied in any Development must be restricted to occupancy by a Low- or Very Low-Income Household; the second Inclusionary Unit must be restricted to occupancy by a Very Low-Income Household; and the third Inclusionary Unit must be restricted to occupancy by a Moderate-, Low- or Very Low-Income Household. This sequence repeats for the fourth, fifth and sixth Inclusionary Units occupied. The City Manager may approve an alternative sequence when the Developer elects to take advantage of the equivalents provided in subsection (b)(1) and (b)(2) of this Section. The sequence for projects that include 7 of more Inclusionary Units will be specified in the Inclusionary Housing Plan and Inclusionary Housing Agreement required by Section 10-10-240(b).

For Residential Developments of at least 7 and not more than 42 units, the first Inclusionary Unit occupied must be restricted to occupancy by a Moderate- Income Household, the second to occupancy by a Very Low-Income Household, and the third to occupancy by a Low-Income Household. This sequence repeats for the fourth, fifth and sixth Inclusionary Units occupied. The City Manager may approve an alternative sequence when the Developer elects to take advantage of the equivalents provided in subsection (b)(1) and (b)(2) of this Section. The sequence for projects of more than 42 units will be specified in the Inclusionary Housing Plan and Inclusionary Housing Agreement required by Section 10-10-240(b).

DRAFTING NOTES

[13] INCENTIVES FOR LOWER INCOME UNITS. Developer reluctance to build low- and very low-income units can sometimes be offset with incentives. The Sample Ordinance allows a Developer to reduce the effective inclusionary requirement from 15 to 10 percent by building additional very low-income units in lieu of moderate income units. Alternatively, in markets where the needs of moderate-income households are sufficiently addressed, local agencies can also accomplish this goal by simply requiring that all inclusionary units be affordable to either low- and very low-income households.

[14] SEQUENCING FOR SMALL PROJECTS. This purpose of this provision is to assure that a balance of moderate-, low- and very low-income households. Without such a provision, some Developers may build all the moderate- and low-income units first. A more flexible alternative would be to develop the sequencing as part of the Affordable Housing Plan, which would eliminate the need to codify the sequencing requirements as part of the ordinance.

10-10-140. COMMERCIAL DEVELOPMENT.[15]

(a) Approval of a tentative map or building permit for Commercial Development requires the payment of a fee[16] to the Affordable Housing Trust Fund for each 5,000 square feet of new commercial space within any 12-month period that is constructed or converted to a new use. The City Council may annually review the fee authorized by this Section, and may,

DRAFTING NOTES

[15] APPLICATION TO COMMERCIAL DEVELOPMENT. Whether to impose an inclusionary housing fee on commercial development is a policy choice. Statewide, most inclusionary ordinances apply only to residential development. The Sample Ordinance combines a residential inclusionary requirement and a commercial "linkage" fee. A more cautious approach would be to adopt two separate ordinances, one for commercial development and a second for residential development. That way, if either the commercial or residential requirement is struck down, the non-challenged requirement is less likely to be "tainted" by the process. While a standard severability clause that accompanies most ordinances can serve this function from a technical standpoint, the dual ordinance approach may be preferable from a political and implementation standpoint.

[16] FEES IMPOSED AS CONDITION OF DEVELOPMENT. The fee on commercial development is not an in-lieu fee, but a fee established under the Mitigation Fee Act. *See* Cal. Gov't Code § 66000 and following. Thus, the agency must establish a connection, or nexus, between the demand for affordable housing that will occur as a result of the development and the purpose of the fee. *See Commercial Builders of Northern California v. City of Sacramento*, 941 F.2d 872 (9th Cir. 1991) (upholding fee on nonresidential building to offset burdens caused by low-income workers moving to area to fill jobs created by project). The Mitigation Fee Act requires the following findings:

- The purpose of the fee is to offset the demand for housing that is created by the new development.
- Funds will be used for the construction of units for moderate-, low- and very low-income households. To the extent possible, incorporate supporting information included in the General Plan and any environmental impact report prepared with respect to the General Plan.
- The fee is reasonably related to the commercial development. (Put another way, show that the commercial development will benefit from the greater stock of affordable housing).
- The need for the public facility is a reasonably related to the commercial development. (The added commercial development creates a demand for additional affordable housing units).
- There is a reasonable relationship between the amount of the fee and the cost of the affordable housing units.

See Cal. Gov't Code §§ 66001(a) and (b); *Garrick Development Co. v. Hayward Unified School Dist.*, 3 Cal. App. 4th 320 (1992). The amount of the fee should not exceed the estimated reasonable cost of providing the service or facility on which the fee is imposed. *See* Cal. Gov't Code § 66005. Further guidance for establishing fees is found in *San Remo Hotel v. City and County of San Francisco*, 27 Cal. 4th 643 (2002) (holding that courts must defer to legislatively enacted fees that are generally imposed on a class "logically subject to its strictures" and applied by formula without discretion on the part of the local agency).

based on that review, adjust the fee amount by resolution.[17] For any annual period during which the City Council does not review the fee authorized by this subsection, fee amounts will be adjusted once by the City Manager based on the Construction Cost Index. The amount of the fee required for a specific development will be determined only once, at the time of tentative or parcel map approval, or, for developments not processing a map, prior to issuance of a building permit. If a change in design results in a change in square footage, the amount of the fee will be recalculated.[18]

(b) **Alternative Housing Proposal**. In lieu of paying a fee to the Affordable Housing Trust Fund and to the extent permitted by the City's General Plan, zoning ordinance and other applicable laws, a Developer may propose an Alternative Housing Proposal to build Inclusionary Units on the site of the Commercial Development or on another site sufficiently close to the Commercial Development site to serve the housing demand created by the development. Developers making an Alternative Housing Proposal must do so by submitting an Affordable Housing Plan and enter into an approved Inclusionary Housing Agreement as provided by Section 10-10-240.

SECTION 10-10-150. EXEMPTIONS.

The requirements of this Chapter do not apply to:

(a) The reconstruction of any structures that have been destroyed by fire, flood, earthquake or other act of nature provided that the reconstruction of the site does not increase the number of residential units by more than 6 or increase the interior floor area of a non-residential structure by more than 4,999 square feet.

(b) Developments that already have more units that qualify as affordable to Moderate-, Low- and Very Low-Income Households than this Chapter requires.[19]

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[17] PROCEDURE FOR ADOPTING AND INCREASING FEES. The Mitigation Fee Act specifies the process for setting and increasing fees. *See* Cal. Gov't Code §§ 66016-66018.5.

[18] CONSISTENCY BETWEEN ALTERNATIVE HOUSING PROPOSALS AND RESIDENTIAL DEVELOPMENTS. The intention of the Sample Ordinance is to allow a developer to submit an acceptable Affordable Housing Plan in lieu of paying the commercial fee. Some of the provisions in the remainder of the ordinance will need clarification in the context of the Alternative Housing Proposal. For example, Section 10-10-200 requires that the Inclusionary Units be similar in quality and bedroom size to Market Rate Units, which is an unhelpful distinction when applied to the underlying commercial development. The required Affordable Housing Plan and subsequent agreement (Section 10-10-240) is the appropriate place within the Sample Ordinance to address these issues.

[19] NONPROFIT HOUSING ASSOCIATIONS. Some inclusionary ordinances exclude nonprofit housing associations, but without further definition, "nonprofit" is probably not an effective screen. Some for-profit developers have formed affiliated nonprofits. Moreover, nothing prevents a nonprofit developer from developing a project that is solely market rate units.

(c) Housing constructed by other government agencies.

(d) Other Exemptions. [*Insert other appropriate exemptions, such as churches*[20] *or schools*].

SECTION 10-10-200. AFFORDABLE HOUSING STANDARDS.

Inclusionary Units built under this Chapter must conform to the following standards:

(a) **Design.**[21] Except as otherwise provided in this Chapter, Inclusionary Units must be dispersed throughout a Residential Development and be comparable in infrastructure (including sewer, water and other utilities), construction quality and exterior design to the Market-rate Units. Inclusionary Units may be smaller in aggregate size and have different interior finishes and features than Market-rate Units so long as the interior features are durable, of good quality and consistent with contemporary standards for new housing. The number of bedrooms must be the same as those in the Market-rate Units, except that if the Market-rate Units provide more than four bedrooms, the Inclusionary Units need not provide more than four bedrooms.[22]

(b) **Timing.** All Inclusionary Units must be constructed and occupied concurrently with or prior to the construction and occupancy of Market-rate Units or development. In phased developments, Inclusionary Units may be constructed and occupied in proportion to the number of units in each phase of the Residential Development.

(c) **Duration of Affordability Requirement.** Inclusionary Units produced under this ordinance must

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[20] RELIGIOUS USE EXEMPTION. Local agencies electing to exempt church uses should do so in a manner that does not distinguish religious from non-religious uses that are otherwise similar in order to avoid problems under the Religious Land Use and Institutionalized Persons Act. *See* 42 U.S.C. § 2000cc.

[21] DESIGN STANDARDS. Design standards are included to guard against the use of inferior materials and designs in the Inclusionary Units. Some agencies also specify minimum square footage or sizes for certain types of housing (for example, of two bedroom minimums for owner-occupied units). But design standards should be considered carefully. Such standards make the Inclusionary Units more expensive to construct (particularly when the local agency may be contributing financial assistance to the project). For example, requiring that the inclusionary units be of similar size to market rate units might be cost prohibitive in some large single-family home developments. On the other hand, too few standards may result in some (not all) developers producing substandard units. Local agencies will need to balance these competing interests to fit the needs of their communities.

[22] NUMBER OF BEDROOMS. The Sample Ordinance contemplates affordable units with up to four bedrooms. In most communities, affordable units are usually made up of two and three bedrooms, which can limit the opportunities for larger-sized low-income families to find comfortable accommodations.

be legally restricted to occupancy by Households of the income levels for which the units were designated for a minimum of 55 years for rental units and 45 years for owner occupied units.[23]

SECTION 10-10-210. IN-LIEU FEES.[24]

For Residential Developments of 14 or fewer units,[25] including Inclusionary Units, the requirements of this Chapter may be satisfied by paying an in-lieu fee to the Affordable Housing Trust Fund as provided in Section 10-10-310. The fee will be sufficient to make up the gap between (i) the amount of development capital typically expected to be available based on the amount to be received by a Developer or owner from Affordable Housing Cost or Affordable Rent and (ii) the anticipated cost of constructing[26] the Inclusionary Units. The City Council may annually review the fee authorized by this Section by resolution, and may, based on that review, adjust the fee amount. For any annual period during which the City Council does not review the fee authorized by this subsection, fee amounts will be adjusted once by the City Manager based on the Construction Cost Index.

(a) Timing of Payment. The fee must be paid within ten calendar days of issuance of a building permit for the Development or the permit will be null and void.[27] For phased developments,

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[23] DURATION. Duration periods vary from 20 years to permanent restrictions. The Sample Ordinance incorporates the affordability periods in the state Redevelopment Law. *See* Cal. Health and Safety Code § 33413(c). When a city or county (but not necessarily charter city) provides incentives such as those provided in Section 10-10-230, the duration should probably not be less than 30 years to be consistent with a strict reading of the Density Bonus Law. *See* Cal. Gov't Code § 65915(c). Local agencies are prohibited from offering incentives that would undermine the intent of the Density Bonus Law. *See* Cal. Gov't Code § 65917. A court could interpret anything less than a 30-year affordability period as undermining the intent of the Density Bonus Law.

[24] CALCULATING IN-LIEU FEES. The amount of the fee can be a function of a number of characteristics, including number of market-rate units constructed (most common), new parcels created, square footage or property value. The fee should be proportional to the cost of the affordability gap between the cost of construction price and the ability of a moderate-, low- or very low-income household to pay for a home, plus the reasonable cost of administering the City's Inclusionary Housing program. For example, if the cost of constructing an affordable unit is $200,000 and the maximum price that the low-income household can afford is $140,000, then the affordability gap is $60,000. If the cost of administering the program is calculated at $1,500 per unit, applying the 15 percent inclusionary requirement yields a fee of $9,225 per unit (note that the affordability gap – and thus the fee (will differ for moderate- and very low-income households). For rental units, the affordability gap is the difference between the rent stream necessary to pay the cost of development and maintenance of the rental project over its useful life and the rent stream that could be expected from a project charging affordable rents.

[25] CAP FOR IN-LIEU FEE ALTERNATIVE. The Sample Ordinance limits the application of the in-lieu fee option to projects that include 14 or fewer units. Some communities have set even lower ceilings. Setting a cap allows small project Developers who can accomplish economies of scale and better sustain the burden of providing and administering units themselves to retain a degree of

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payments may be made for each portion of the Development within ten calendar days of a Building Permit for that phase. When payment is delayed, in the event of default, or for any other reason, the amount of the in-lieu fee payable under this Section will be based upon the fee schedule in effect at the time the fee is paid.

(b) Effect of No Payment. No final inspection for occupancy will be completed for any corresponding Market-rate Unit in a Residential Development unless fees required under this Section have been paid in full to the City.

SECTION 10-10-220. ALTERNATIVES.[28]

(a) Developer Proposal.[29] A Developer may propose an alternative means of compliance in an Affordable Housing Plan as provided in Section 10-10-240 according to the following provisions.

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flexibility, while requiring that larger projects place Inclusionary Units on-site. Setting such limits is a policy consideration. Here, a 14-unit project size demarks the boundary because it equates to the project size that would require the inclusion of 2 affordable units at the 15 percent inclusionary requirement. It will also be useful to include some rationale for the ceiling chosen in the record of the adoption of the ordinance, perhaps via the staff report.

[26] COST OF CONSTRUCTING VERSUS MEDIAN HOME PRICE. The Sample Ordinance sets the fee as a function of the cost of constructing the Inclusionary Unit. In some cases, local agencies have set the fee based on the median price only to find out that the cost of constructing the unit is higher.

[27] TIMING OF PAYMENT. Requiring that the in-lieu fee be received upon issuance of the building permit increases the likelihood that the corresponding inclusionary units can be built at the same time as the market-rate project. This requirement is not generally available for fees imposed directly on development (as opposed to an in-lieu fee) because the Mitigation Fee Act provides that local agencies cannot require fees before the final inspection or upon issuance of a certificate of occupancy. *See* Cal. Gov't Code § 66007.

[28] PROVIDING ALTERNATIVES. In *Homebuilders Association of Northern California v. City of Napa*, 90 Cal. App. 4th 188 (2001), the California court of appeal expressed approval of the inclusion of several alternatives within the city's ordinance. However, this approval does not mean that local agencies must include alternatives, or if they do, that they have to provide a menu of alternatives. The Sample Ordinance includes two of the most common alternatives offered to developers: off-site construction and land dedication (in-lieu fees are also an option, but are treated separately here). Other alternatives include credit transfer programs that allow Developers to transfer Inclusionary Units between development projects and accepting rehabilitated units for the inclusionary requirement. If the local agency elects to accept rehabilitated units they should be prepared to address the often complex and thorny issues that are often raised with such programs. *See* Cal. Gov't Code § 65583.1(c).

[29] ALTERNATIVES AND JUDICIAL SCRUTINY. One ongoing issue in this area of the law is the extent to which a particular action will receive deferential scrutiny or heightened scrutiny from courts under the Takings Clause as it applies to conditions on development. In general, courts will apply

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(1) *Off-Site Construction.*[30] Inclusionary Units may be constructed off-site if the Inclusionary Units will be located in an area where, based on the availability of affordable housing, the City Manager finds that the need for such units is greater than the need in the area of the proposed development.

(2) *Land Dedication.*[31] In lieu of building Inclusionary Units, a Developer may choose to dedicate land to the City suitable for the construction of Inclusionary Units that the City Manager reasonably determines to be of equivalent or greater value than is produced by applying the City's current in-lieu fee to the Developer's inclusionary obligation.

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heightened scrutiny to project-specific conditions because of the increased possibility of the local agency unfairly leveraging its permit approval authority. *See Dolan v. City of Tigard*, 512 U.S. 374 (1994). In contrast, actions that are legislatively adopted and apply equally to a broad class of landowners will receive deferential treatment. *See San Remo Hotel v. City and County of San Francisco*, 27 Cal. 4th 643 (2002). Developer-proposed alternatives often require case-by-case evaluation. However, because the Developer has voluntarily submitted the proposal, judicial scrutiny should remain deferential to local agency actions where the option to take the legislatively adopted conditions remains open. Nevertheless, the law in this area is not fully developed and local agencies that attempt to use the process to leverage additional concessions for Developers may find their actions subject to increased scrutiny.

[30] OFF-SITE CONSTRUCTION OF UNITS. The Sample Ordinance favors the development of On-Site Units by granting such projects incentives that are not available to projects that include Off-Site Units. Another option is to require a higher inclusionary percentage for Off-Site Units because such units are usually cheaper to produce. For example, if the on-site requirement is 15 percent, the off-site requirement could be 20 or 25 percent. But local agencies should not rely too heavily on such alternatives. Inclusionary programs may have exclusionary effects in cases when Developers are routinely permitted to develop off-site (and the off-site locations are concentrated in one area), or when a single Developer locates all of the Inclusionary Units in one area of the project. In extreme cases, such practices may be discriminatory. Local land use actions that deny individuals or groups of individuals the enjoyment of residence, landownership, tenancy or any other land use because of the intended occupancy by persons or families of low-, moderate- or middle-income are unlawful. *See* Cal. Gov't Code § 65008(a). Any allowance of Off-Site Units should keep this prohibition in mind.

[31] LAND DEDICATION. Land dedication can be a particularly attractive option for a Developer. In many cases, however, such lands are not ideally located to further the goals of inclusionary housing. The Sample Ordinance attempts to address these issues by highlighting the issues most likely to make the deal unattractive from a policy point of view. Local agencies electing to include a land dedication alternative should also consider incorporating an appraisal process to avoid disputes about what constitutes "equivalent or greater value." For example, both the Developer and the City could have the property appraised and if there is more than a 10 percent difference between the valuations, then the two appraisers agree on a third-party appraiser to evaluate the appraisals. Alternatively, the ordinance could reserve to the City the power to determine the value of the property for these purposes, subject to an administrative appeal and, ultimately, judicial review.

(3) *Combination.* The City Manager may accept any combination of on-site construction, off-site construction, in-lieu fees and land dedication that at least equal the cost of providing Inclusionary Units on-site as would otherwise be required by this Chapter.

(b) Discretion. The City Manager may approve, conditionally approve[32] or reject any alternative proposed by a Developer as part of an Affordable Housing Plan. Any approval or conditional approval must be based on a finding that the purposes of this Chapter would be better served by implementation of the proposed alternative(s). In determining whether the purposes of this Chapter would be better served under the proposed alternative, the City Manager should consider (i) whether implementation of an alternative would overly concentrate Inclusionary Units within any specific area and, if so, must reject the alternative unless the undesirable concentration of Inclusionary Units is offset by other identified benefits that flow from implementation of the alternative in issue; and (ii) the extent to which other factors affect the feasibility of prompt construction of the Inclusionary Units on the property, such as costs and delays, the need for an appraisal, site design, zoning, infrastructure, clear title, grading and environmental review.

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[32] CONDITIONAL APPROVALS. In some cases, conditional approvals receive increased judicial scrutiny to the extent that they involve a local agency imposing specialized conditions on a single development. Under the Sample Ordinance, the conditional approval is an alternative to the baseline inclusionary requirement. Thus, the likelihood of such scrutiny is decreased. In any event, local agencies should base conditional approvals on clear regulatory objectives.

[33] COSTA-HAWKINS RENTAL HOUSING ACT. One issue that must be considered in connection with rental units is the potential application of the Costa-Hawkins Rental Housing Act, which prohibits local agencies from setting price controls on rental units built after 1995. *See* Cal. Civ. Code §§ 1954.50- 1954.53. (The Act does not apply to "for sale" inclusionary units). The question arises, then, whether the Costa-Hawkins Act limits the authority of local agencies to control subsequent pricing of inclusionary rental units. The better, albeit not certain answer, is that the Act's legislative history indicates that that it places no such limits on inclusionary rental units. Statements made by the sponsors of the bill and in the legislative analysis indicated that the bill would apply only to five cities that had "extreme vacancy control" provisions. Further comments indicated that the 70 cities and counties with "moderate" rent control (including, presumably, inclusionary programs) would not be affected by the Act. While this history seems to bolster the conclusion that inclusionary rental programs are not be affected by the Act, absent a clarifying court opinion or legislative act, there is no way to be certain. For a full discussion of this analysis, and its drawbacks, *see* Nadia I. El Mallakh, *Does the Costa-Hawkins Act Prohibit Local Inclusionary Zoning Programs?* 89 Cal. L. Rev. 1847 (2001).

Another Way of Looking At the Costa-Hawkins Issue. Even if the Costa-Hawkins Act were applicable to rental inclusionary units, the Act provides another potential safe harbor: it does not apply to rental units where "the owner has otherwise agreed by contract with a public entity in consideration for a direct financial contribution or any other forms of assistance specified" by the Density Bonus Law. Cal. Civ. Code § 1954.52(a)(2) (referring to Cal. Gov't Code § 65915). A reasonable reading of this provision suggests that inclusionary rental units may be exempted from the Act if (1) there is a contract between a Developer and the public entity for the construction of

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SECTION 10-10-230. INCENTIVES FOR RENTAL[33] AND ON-SITE[34] HOUSING.

In accord with Chapter [*local density bonus ordinance*], the City may provide one or more of the following incentives to a Developer who elects to satisfy the inclusionary housing requirements of this Chapter by producing rental units or owner-occupied housing units on the site of a Residential or Non-Residential Development.

(a) **Modified Development Standards to Increase Density.** Modification in development, zoning or architectural design requirements, provided that such modifications exceed the minimum building standards provided in the Uniform Building Code [and similar codes], as incorporated into the Municipal Code in Section ____ that will allow for increased density, including, but not limited to, a reduction in setback, square footage and parking requirements.

(b) **Mixed Use Zoning.** Approval of mixed use zoning in conjunction with a Development if such uses are compatible with the existing or planned development in the area where the proposed Development will be located.

(c) **Fee Reductions.** [35] A pro-rata refund of the conditional use or other fees required by Section ____, environmental review fees required by Section ____ and the building permit fee required by Section ____ for the portion of the Development devoted to Inclusionary Units:

(d) **Expedited Processing.** Eligibility for expedited processing of development and permit applications for the Residential Development. [*describe applicability to local processes*]

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inclusionary units; and (2) the local agency offers a financial contribution or another "form of assistance" specified in the Density Bonus Law. The plain language refers only to the *forms* of assistance specified in the Density Bonus Law, not to projects where assistance was actually provided under the law. Thus, the incentives enumerated in the Sample Ordinance are consistent with the terms of the state Density Bonus Law. When drafting the incentives section, local agencies should be aware that they may not offer incentives in a way that undermines the intent of the state Density Bonus Law. *See* Cal. Gov't Code § 65917. Thus, drafters should incorporate their density bonus ordinance to ensure consistency between the two ordinances.

[34] INCENTIVES FOR OWNER-OCCUPIED UNITS. Limiting incentives for on-site for-sale units (as opposed to Off-Site Units or the payment of in-lieu fees) makes the option of building on site units more attractive.

[35] FEE REDUCTIONS. Most planning fees are cost recovery fees. Such fees are limited insofar as the local agency can only charge enough to recoup the cost of processing applications. If there is a break for a particular applicant, then some other source of funds is needed to pay for the services that are provided. Thus, local agencies should identify the source – such as set asides or general funds - that will account for the loss of revenue. Local agencies that try to compensate by setting fees slightly higher on other applications risk having the fee challenged as an unconstitutional tax.

(e) **Financial Assistance.** To the extent budgeted by the City Council and otherwise available, financial assistance for the inclusionary housing component of the Development may be in the form of loans or grants from sources as may be available to the City.[36]

SECTION 10-10-240. COMPLIANCE PROCEDURES.

(a) **General.** Approval of an Inclusionary Housing Plan and implementation of an approved Inclusionary Housing Agreement is a condition of any tentative map, parcel map or building permit for any Development for which this Chapter applies. This Section does not apply to exempt projects or to projects where the requirements of the Chapter are satisfied by payment of a fee under Sections 10-10-140 or 10-10-210.

(b) **Inclusionary Housing Plan.** The City Manager must approve, conditionally approve or reject the Inclusionary Housing Plan within 60 days of the date of a complete application for that approval.[37] If the Inclusionary Housing Plan is incomplete, the Inclusionary Housing Plan will be returned to the Developer along with a list of the deficiencies or the information required. No application for a tentative map, parcel map or building permit to which this Chapter applies may be deemed complete until an Inclusionary Housing Plan is submitted to the City Manager.[38] At any time during the review process, the City Manager may require from the Developer additional information reasonably necessary to clarify and supplement the application or determine the consistency of the proposed Inclusionary Housing Plan with the requirements of this Chapter. The Inclusionary Housing Plan must include:

(1) The location, structure (attached, semi-attached, or detached), proposed tenure[39] (for-sale or rental), and size of the proposed market-rate, commercial space and/or Inclusionary Units and the basis for calculating the number of Inclusionary Units;

(2) A floor or site plan depicting the location of the Inclusionary Units;

(3) The income levels to which each Inclusionary Unit will be made affordable;

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[36] FUNDING SOURCES. Redevelopment set-aside funds may be one such source of funds.

[37] PERMIT STREAMLINING ACT. Approval of the Inclusionary Housing Plan and the Inclusionary Housing Agreement should occur within the time lines provided by the Permit Streamlining Act. *See* Cal. Gov't Code § 65950. Generally, this requirement is 180 days. However, there are instances where faster time lines (60 or 90 days) may apply. For example, a 60 day time line applies for certain publicly financed affordable housing projects. *See* Cal. Gov't Code § 65950(a)(2).

[38] DEVELOPMENT APPLICATIONS. The requirements of the Inclusionary Housing Plan should be included on any list of requirements. *See generally* Cal. Gov't Code § 65940 and following.

[39] DEVELOPER CHOICE OF RENTAL VERSUS FOR-SALE UNITS. Developers may satisfy all or a portion of the inclusionary requirement by constructing rental housing. *See* Cal. Gov't Code § 65589.8.

(4) The mechanisms that will be used to assure that the units remain affordable for the desired term, such as resale and rental restrictions, deeds of trust, and rights of first refusal and other documents;

(5) For phased Development, a phasing plan that provides for the timely development of the number of Inclusionary Units proportionate to each proposed phase of development as required by Section 10-10-200(c) of this Chapter.

(6) A description of any incentives as listed in Section 10-10-230 that are requested of City;

(7) Any alternative means designated in Section 10-10-220(a) proposed for the Development along with information necessary to support the findings required by Section 10-10-220(b) for approval of such alternatives; and

(8) Any other information reasonably requested by the City Manager to assist with evaluation of the Plan under the standards of this Chapter.

(c) Inclusionary Housing Agreement.[40] The forms of the Inclusionary Housing Agreement, resale and rental restrictions, deeds of trust, rights of first refusal and other documents authorized by this subsection, and any change in the form of any such document which materially alters any policy in the document, must be approved by the City Manager or his or her designee prior to being executed with respect to any Residential Development or Affordable Housing Proposals. The form of the Inclusionary Housing Agreement will vary, depending on the manner in which the provisions of this Chapter are satisfied for a particular development. All Inclusionary Housing Agreements must include, at minimum, the following:

(1) Description of the development, including whether the Inclusionary Units will be rented or owner-occupied;

(2) The number, size and location of Very Low-, Low- or Moderate-Income Units;

(3) Inclusionary incentives by the City (if any), including the nature and amount of any local public funding;

(4) Provisions and/or documents for resale restrictions, deeds of trust, rights of first refusal or rental restrictions;

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[40] INCLUSIONARY HOUSING AGREEMENT. This requirement assures that there is a contract between the Developer and public entity for purposes of the Costa-Hawkins Act. *See Costa-Hawkins Rental Housing Act*, Note 33 above. A standard agreement should be produced that can be modified to fit the terms and needs of individual projects.

(5) Provisions for monitoring the ongoing affordability of the units, and the process for qualifying prospective resident Households for income eligibility; and

Any additional obligations relevant to the compliance with this Chapter.[41]

(a) Recording of Agreement.[42] Inclusionary Housing Agreements that are acceptable to the City Manager must be recorded against owner-occupied Inclusionary Units and residential projects containing rental Inclusionary Units. Additional rental or resale restrictions, deeds of trust, rights of first refusal and/or other documents acceptable to the City Manager must also be recorded against owner-occupied Inclusionary Units. In cases where the requirements of this Chapter are satisfied through the development of Off-Site Units, the Inclusionary Housing Agreement must simultaneously be recorded against the property where the Off-Site Units are to be developed.

SECTION 10-10-250. ELIGIBILITY FOR INCLUSIONARY UNITS.

(a) General Eligibility. No Household may occupancy an Inclusionary Unit unless the City or its designee[43] has approved the Household's eligibility, or has failed to make a determination of eligibility within the time or other limits provided by an Inclusionary Housing Agreement or resale restriction. If the City or its designee maintains a list or identifies eligible Households, initial and subsequent occupants will be selected first from the list of identified Households, to the maximum extent possible, in accordance with any rules approved by the City Manager. If the City has failed to identify a Household as an eligible buyer for the initial sale of an Inclusionary Unit that is intended for owner-occupancy 90 days after the unit receives a completed final inspection for occupancy, upon 90 additional days' notice to the City and on satisfaction of such further conditions as may be included in City-approved restrictions (which may include a further opportunity to identify an eligible buyer), the owner may sell the unit at a market price, and the unit will not be subject to any requirement of this Chapter thereafter.

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[41] ADDITIONAL PROVISIONS IN AGREEMENT. Drafting an agreement to restrict the use of property and placing conditions on title often involves complex issues of property and contract law. The elements of the Sample Ordinance merely provide a starting point for addressing these issues. Local agencies should consult with local agency counsel to determine what additional provisions, if any, should be included here.

[42] RECORDING. Because the primary effect of the Inclusionary Housing Agreement is to restrict the use of some of the units on the site, it should be a recordable instrument. Recording requirements vary, however, and it is advisable to consult with the local County Recorder's office in establishing forms for these purposes.

[43] CITY DESIGNEE. In some cases, it may be more efficient for the city to delegate such tasks to a local housing authority or nonprofit housing organization.

(b) Conflict of Interest.[44] The following individuals are ineligible to purchase or rent an Inclusionary Unit: (i) City employees and officials (and their immediate family members) who have policy-making authority or influence regarding City housing programs and do not qualify as having a remote interest as provided by California Government Code Section 1091;[45] (ii) the Project Applicant and its officers and employees (and their immediate family members); and (iii) the Project Owner and its officers and employees (and their immediate family members).

(c) Occupancy. Any Household who occupies a rental Inclusionary Unit or purchases an Inclusionary Unit must occupy that unit as a principal residence.

10-10-260. OWNER-OCCUPIED UNITS.

(a) Initial Sales Price. The initial sales price of the Inclusionary Unit must be set so that the eligible Household will pay an Affordable Ownership Cost.

(b) Transfer.[46] Renewed restrictions will be entered into on each change of ownership, with a 45-year renewal term, upon transfer of an owner-occupied Inclusionary Unit prior to the expiration of the 45-year affordability period.

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[44] CONFLICT OF INTEREST. The conflict of interest provision is inserted into the Sample Ordinance to promote public confidence in the program. Such provisions, however, are not necessarily common in inclusionary housing programs. Indeed, there may be several reasons not to include such a provision. For example, it may unfairly affect the ability of individuals (either for themselves or family members) from lower income backgrounds to run for elected office or apply for certain positions. Some local agencies actually build in a preference for eligible local agency staff to increase the likelihood that city staff resides within the community. Local agencies including this provision should make a record of the rationale for this restriction, such as promoting public confidence in affordable housing programs, discouraging fraud and abuse, and noting that the burden to the affected individuals is small given the relatively small portion of the market affected by the regulation. Moreover, local agencies that have adopted local conflict of interest codes should check this provision for consistency.

[45] REMOTE INTERESTS. Cal. Gov't Code § 1091(b)(12) includes in the definition of "remote interest" that of an elected officer in any Section 8 housing assistance payment contract under specified conditions.

[46] MANAGEMENT OF OWNER-OCCUPIED UNITS. It is probably impossible to draft an ordinance that would address every possible contingency when it comes to transferring property. Indeed, managing the resale of property often involves unique, time-intensive transactions that underscore the need for the local agency to remain committed to the implementation of an inclusionary policy in order for it to retain effectiveness.

(c) **Resale.**[47] The maximum sales price permitted on resale[47] of an Inclusionary Unit designated for owner-occupancy shall be the lower of: (1) fair market value or (2) the seller's lawful purchase price, increased by the lesser of (i) the rate of increase of Area Median Income during the seller's ownership or (ii) the rate at which the consumer price index increased during the seller's ownership. To the extent authorized in any resale restrictions or operative Inclusionary Housing Agreement, sellers may recover at time of sale the market value of capital improvements made by the seller and the seller's necessary and usual costs of sale, and may authorize an increase in the maximum allowable sales price to achieve such recovery.[48]

(d) **Changes in Title.** Title in the Inclusionary Unit may change due to changes in circumstance, including death, marriage and divorce. Except as otherwise provided by this Subsection, if a change in title is occasioned by events that changes the financial situation of the Household so that it is no longer income-eligible, then the property must be sold to an income-eligible Household within 180 days. Upon the death of one of the owners, title in the property may transfer to the surviving joint tenant without respect to the income-eligibility of the Household. Upon the death of a sole owner or all owners and inheritance of the Inclusionary Unit by a non-income-eligible child or stepchild of one or more owners, there will be a one year compassion period between the time when the estate is settled and the time when the property must be sold to an income-eligible Household. Inheritance of an Inclusionary Unit by any other person whose Household is not income-eligible shall require resale of the unit to an income-eligible Household as soon as is feasible but not more than 180 days.

DRAFTING NOTES

[47] RESALE PRICE. Typically, the resale price will be the original sales price plus the percentage increase in the construction cost index (or other type of index). Some local agencies may add an equity sharing or maintenance credit. However, such pricing assumes that prices will always increase. There have been instances when a decline in a real estate market has been so severe that the fair market value of a home dropped below the inclusionary program price. The Sample Ordinance introduces a degree of flexibility so that the ordinance need not be amended in cases where the affordable price exceeds fair market value.

[48] EQUITY SHARING. One issue that often arises is the extent to which owner-occupants can capture any appreciation or equity in their units above the set indexed resale price. Many occupants believe that they, like any other homeowner, should be able to capture the equity gains associated with their home. However, such a policy would limit the ability of the local agency to retain its stock of affordable housing. Some local agencies have developed policies that allow owners to capture a portion of the equity (for example, capped at 10 percent) provided that they properly maintain their homes. The drawback to such programs, however, is that the units become less affordable to moderate-, low- and very low-income households with each new sale.

SECTION 10-10-270. RENTAL UNITS.

Rental units will be offered to eligible Households at an Affordable Rent. The owner of rental Inclusionary Units shall certify each tenant Household's income to the City or City's designee at the time of initial rental and annually thereafter. The owner must obtain and review documents that demonstrate the prospective renter's total income, such as income tax returns or W-2s for the previous calendar year, and submit such information on a form approved by the City.

(a) Selection of Tenants. The owners of rental Inclusionary Units may fill vacant units by selecting income-eligible Households from the Section 8 Housing Choice Voucher Waiting List maintained by the City or City's designee. Alternatively, owners may fill vacant units through their own selection process, provided that they publish notices of the availability of Inclusionary Units according to guidelines established by the City Manager.[49]

(b) Annual Report. The owner shall submit an annual report summarizing the occupancy of each Inclusionary Unit for the year, demonstrating the continuing income-eligibility of the tenant. The City Manager may require additional information if he or she deems it necessary.[50]

(c) Subsequent Rental to Income-Eligible Tenant. The owner shall apply the same rental terms and conditions to tenants of Inclusionary Units as are applied to all other tenants, except as required to comply with this Chapter (for example, rent levels, occupancy restrictions and income requirements) or with other applicable government subsidy programs. Discrimination against persons receiving housing assistance is prohibited.

(d) Changes in Tenant Income. If, after moving into an Inclusionary Unit, a tenant's Household income exceeds the limit for that unit, the tenant Household may remain in the unit as long as his or her Household income does not exceed 140 percent of the income limit. Once the tenant's income exceeds 140 percent of the income limit, the following shall apply:

DRAFTING NOTES

[49] PUBLISHING GUIDELINES. Usually, guidelines require the owner to identify the available unit, state income requirements, indicate where applications are available, state when the application period opens and closes and provide a telephone number for inquiries. The guidelines can also designate specific newspapers and other media in which a unit's availability may be advertised. Some local agencies require that at least one notice be published in a Spanish (or other language) newspaper of general circulation. Care must be taken in selecting which non-English publications will be required to avoid claims of ethnic or national origin discrimination. It is typically sufficient if publication(s) are selected on the basis of Census data reflecting the languages spoken by non-English speakers in or near the jurisdiction.

[50] REPORTING. Local agencies can require reporting semi-annually, quarterly or even monthly. Some ordinances require that the local agency be notified each time a vacancy occurs. An annual report provides a way of obtaining rental information in a way that is less burdensome on the property owner and, perhaps, City staff.

(1) If the tenant's income does not exceed the income limits of other Inclusionary Units in the Residential Development, the owner may, at the owner's option, allow the tenant to remain in the original unit and redesignate the unit as affordable to Households of a higher income level, as long as the next vacant unit is re-designated for the income category previously applicable to the tenant's Household. Otherwise, the tenant shall be given one year's notice to vacate the unit. If during the year, an Inclusionary Unit becomes available and the tenant meets the income eligibility for that unit, the owner shall allow the tenant to apply for that unit.

(2) If there are no units designated for a higher income category within the Development that may be substituted for the original unit, the tenant shall be given one year's notice to vacate the unit. If within that year, another unit in the Residential Development is vacated, the owner may, at the owner's option, allow the tenant to remain in the original unit and raise the tenant's rent to market-rate and designate the newly vacated unit as an Inclusionary Unit affordable at the income-level previously applicable to the unit converted to market rate. The newly vacated unit must be comparable in size (for example, number of bedrooms, bathrooms, square footage, etc.) as the original unit.

SECTION 10-10-300. ADJUSTMENTS, WAIVERS.[51]

The requirements of this Chapter may be adjusted or waived if the Developer demonstrates to the City Manager that there is not a reasonable relationship between the impact of a proposed Residential Development and the requirements of this Chapter, or that applying the requirement of this Chapter would take property in violation of the United States or California Constitutions.

(a) Timing. To receive an adjustment or waiver, the Developer must make a showing when applying for a first approval for the Residential Development, and/or as part of any appeal that the City provides as part of the process for the first approval.

DRAFTING NOTES

[51] TAKINGS DETERMINATION. Local agencies should include an adjustment provision as part of an inclusionary housing ordinance. As a general rule, landowners must exhaust their administrative remedies, if one is offered, before going to court. The adjustment procedure allows for exceptions in cases of extreme economic hardship, thereby ensuring that the agency has the opportunity to modify its policies to avoid unfair results. Indeed, the inclusion of a waiver provision was important to the *Napa* court's finding that the inclusionary ordinance did not constitute a taking on its face. *See Homebuilders Association of Northern California v. City of Napa*, 90 Cal. App. 4th 188 (2001). While the process should be clear and easy to use, the burden should be on the developer to demonstrate that a reduction or waiver is essential. The variance or waiver provision should set standards for the extent of the reduction if it is determined that the terms of the ordinance should be modified. For example, many agencies permit a reduction or waiver only to the extent that the developer can show that the inclusionary requirement would violate the state or federal constitutions.

(b) Considerations. In making a determination on an application to adjust or waive the requirements of this Chapter, the City Manager may assume each of the following when applicable: (i) that the Developer is subject to the inclusionary housing requirement or in-lieu fee; (ii) the extent to which the Developer will benefit from inclusionary incentives under Section 10-10-230; (iii) that the Developer will be obligated to provide the most economical Inclusionary Units feasible in terms of construction, design, location and tenure; and (iv) that the Developer is likely to obtain other housing subsidies where such funds are reasonably available.

(c) Decision and Further Appeal. The City Manager, upon legal advice provided by or at the behest of the City Attorney,[52] will determine the application and issue a written decision. The City Manager's decision may be appealed to the City Council in the manner and within the time set forth in Section [*insert section for standard appeals*].

(d) Modification of Plan. If the City Manager, upon legal advice provided by or at the behest of the City Attorney, determines that the application of the provisions of this Chapter lacks a reasonable relationship between the impact of a proposed residential project and the requirements of this Chapter, or that applying the requirement of this Chapter would take property in violation of the United States or California Constitutions, the Inclusionary Housing Plan shall be modified, adjusted or waived to reduce the obligations under this Chapter to the extent necessary to avoid an unconstitutional result. If the City Manager determines no violation of the United States or California Constitutions would occur through application of this Chapter, the requirements of this Chapter remain applicable.

10-10-310. AFFORDABLE HOUSING TRUST FUND.[53]

(a) Trust Fund. There is hereby established a separate Affordable Housing Trust Fund ("Fund"). This Fund shall receive all fees contributed under Sections 10-10-140, 10-10-210 and 10-10-220 and may also receive monies from other sources.

DRAFTING NOTES

[52] LEGAL ADVICE. Some ordinances merely require that the City Manager consult with legal counsel. However, the ordinance should specify that the agency counsel is providing legal advice in the capacity of the agency's attorney in order to minimize the risk that the attorney may have to testify (which could infringe on attorney-client communication) in any subsequent procedure if the challenger elects to file suit.

[53] AFFORDABLE HOUSING TRUST FUND. This section should specify the purpose of the fund, the department or official responsible for the fund, the use of the fees and any limitations that will be imposed on the fund. Local agencies that plan to collaborate with a nonprofit housing authority should designate the degree to which the authority can use the funds (for example, whether the funds can be used for the authority's administrative costs).

(b) **Purpose and Limitations.** Monies deposited in the Fund must be used to increase and improve the supply of housing affordable to Moderate-, Low-, and Very Low-Income Households in the City. Monies may also be used to cover reasonable administrative or related expenses associated with the administration of this Section.

(c) **Administration.** The fund shall be administered by the City Manager, who may develop procedures to implement the purposes of the Fund consistent with the requirements of this Chapter and any adopted budget of the City.

(d) **Expenditures.** Fund monies shall be used in accordance with City's Housing Element, Redevelopment Plan, or subsequent plan adopted by the City Council to construct, rehabilitate or subsidize affordable housing or assist other governmental entities, private organizations or individuals to do so. Permissible uses include, but are not limited to, assistance to housing development corporations, equity participation loans, grants, pre-home ownership co-investment, pre-development loan funds, participation leases or other public-private partnership arrangements. The Fund may be used for the benefit of both rental and owner-occupied housing.

(e) **City Manager's Annual Report.**[54] The City Manager shall report to the City Council and Planning Commission on the status of activities undertaken with the Fund as provided by Section 66006(b) of the California Government Code. The report shall include a statement of income, expenses, disbursements and other uses of the Fund. The report should also state the number and type of Inclusionary Units constructed or assisted during that year and the amount of such assistance. The report will evaluate the efficiency of this Chapter in mitigating City's shortage of affordable housing and recommend any changes to this Chapter necessary to carry out its purposes, including any adjustments to the number of units to be required.

10-10-320. ENFORCEMENT.[55]

(a) **Penalty for Violation.** It shall be a misdemeanor to violate any provision of this Chapter. Without limiting the generality of the foregoing, it shall also be a misdemeanor for any

DRAFTING NOTES

[54] CITY MANAGER'S ANNUAL REPORT. The annual report acts as a reporting and compliance monitoring mechanism that can facilitate compilation of an organized, readily accessible source of data that can be used to demonstrate the effectiveness of the inclusionary ordinance in future housing elements. However, the provision in the Sample Ordinance that the report evaluate the efficiency of the inclusionary housing ordinance is not required by the Mitigation Fee Act. *See* Cal. Gov't Code § 66006(b).

[55] ENFORCEMENT. This section sets objective standards for monitoring compliance and imposes penalties for noncompliance. *See* Cal. Gov't Code § 36900 (all violations of city ordinances are misdemeanors unless by ordinance they are made infractions).

person to sell or rent to another person an affordable unit under this Chapter at a price or rent exceeding the maximum allowed under this Chapter or to sell or rent an affordable unit to a Household not qualified under this Chapter. It shall further be a misdemeanor for any person to provide false or materially incomplete information to the City or to a seller or lessor of an Inclusionary Unit to obtain occupancy of housing for which he or she is not eligible.

(b) Legal Action. The City may institute any appropriate legal actions or proceedings necessary to ensure compliance with this Chapter, including: (i) actions to revoke, deny or suspend any permit, including a Building Permit, certificate of occupancy, or discretionary approval; (ii) actions to recover from any violator of this Chapter civil fines, restitution to prevent unjust enrichment from a violation of this Chapter, and/or enforcement costs, including attorneys fees; (iii) eviction or foreclosure; and (iv) any other appropriate action for injunctive relief or damages. Failure of any official or agency to fulfill the requirements of this Chapter shall not excuse any person, owner, Household or other party from the requirements of this Chapter.

10-10-330. MINIMUM REQUIREMENTS.

The requirements of this Chapter are minimum and maximum requirements, although nothing in this Section limits the ability of a private person to waive his or her rights or voluntarily undertake greater obligations than those imposed by this Chapter.[56]

DRAFTING NOTES

[56] MINIMUM AND MAXIMUM REQUIREMENT. This provision underscores the uniform application of this ordinance. A local agency is most vulnerable to a takings challenge if it has imposed inclusionary requirements on an individualized or ad hoc basis. A developer can always volunteer to go beyond the minimum application of the ordinance, but the local agency should probably not require it without specific findings that justify the action. Thus, in defining the conditions of the ordinance as both a minimum and a maximum, the local agency reduces the risk that conditions will be specially imposed on individual developments.

SAMPLE HEARING NOTICE

PUBLIC NOTICE: INCLUSIONARY HOUSING ORDINANCE

About Inclusionary Housing Requirements. The subject of the public hearing is a land use planning device known as inclusionary housing requirements. Inclusionary housing requirements can take many forms, but the basic concept is that development proposals include affordable housing. State law requires that every local jurisdiction provide for its fair share of affordable housing.

Most inclusionary housing ordinances apply to residential development proposals and involve developers including a certain percentage of affordable housing units in their overall proposal to produce market-rate units. Some inclusionary housing ordinances also apply to non-residential development proposals, on the theory that non-residential development generates additional demand for affordable housing stock. Inclusionary ordinances can be voluntary or mandatory.

Who Lives in Affordable Housing? There are a number of misconceptions about who benefits from affordable housing in a community. Affordable housing helps teachers, firefighters, police officers... live near where they work in a community... Moreover, studies show that a lack of affordable housing can constrain economic growth in an area, causing potential new businesses to look elsewhere to locate.

Issues for Discussion. Some of the issues that are likely to be discussed at a public hearing on inclusionary housing requirements include:

- *What role can an inclusionary housing ordinance play in helping our community provide affordable housing?*
- *Should the ordinance be voluntary or mandatory (and if voluntary, what kinds of incentives should the local agency use to encourage participation)?*
- *What percentage of a proposed development should be set aside for affordable housing?*
- *Under what circumstances should a developer be allowed to provide affordable housing off-site from a proposed development?*

Public input on these issues will be most helpful at the public hearing. You can also provide input in writing prior to the hearing.

THE SIX PARTS OF THE CALIFORNIA INCLUSIONARY HOUSING READER

SUPPORT FOR THIS PUBLICATION PROVIDED BY

McDONOUGH, HOLLAND & ALLEN
Attorneys at Law

and the

League of California Cities

OTHER JOBS HOUSING LINKAGE PROGRAMS
JOBS HOUSING LINKAGE ANALYSIS
NAPA COUNTY

ATTACHMENT 2

PRELIMINARY

FEE CITIES

Jurisdiction	Yr. Adopted	Current Fee Levels per SF	Thresholds & Exemptions	Build Option/ Other	Market Strength	Comments
City of Palo Alto	1984 Updated in March 2002.	• Commercial & Industrial $15.00	No Minimum Threshold. Churches; colleges and universities; comm'l recreation; hospitals, convalescent facilities; private clubs, lodges, fraternal org.'s; private educational facilities; and public facilities are exempt.	Yes	Very Substantial	Fee is adjusted annually based on CPI.
City and County of San Francisco	1981 Updated fees in 2002.	• Office $14.96 • Hotel $11.21 • Retail $13.95	25,000 gross SF threshold. Excludes: redevelopment areas and Port.	Yes, may contribute land for housing.	Very Substantial	$40 million raised
City of Menlo Park	1998	• Commercial & Industrial $10.00. • Warehousing, printing, assembly $5.45.	10,000 gross SF Threshold. Churches, private clubs, lodges, fraternal orgs and public facilities are exempt.	Yes, may provide housing on- or off-site.	Very Substantial	Fee is adjusted annually based on CPI.

MEDIUM FEE CITIES

Jurisdiction	Yr. Adopted	Current Fee Levels per SF	Thresholds & Exemptions	Build Option/ Other	Market Strength	Comments
City of Mountain View	2001	• Office/Industrial $6.00 • Hotel $2.00 • Retail $2.00	Fee is 50% less if building meets thresholds: Office <10,000 sf Hotel <25,000 sf Retail <25,000 sf	Yes	Very Substantial	
County of Marin	2003	• Office/R&D $7.19 • Retail/Rest. $5.40 • Warehouse $1.95 • Hotel/Motel $1,746/room • Manufacturing $3.74	No minimum threshold.	Yes, preferred.	Substantial	
City of Oakland	2002	• Office/ Warehouse $4.00	25,000 sf exemption	Yes - Can build units equal to total eligible sf times .0004	Moderate	Fee will be effective July 1, 2005. Fee due in 3 installments. Fee will be adjusted with an annual escalator tied to residential construction cost increases.
City of Berkeley	1993	• All Commercial $4.00 • Industrial $2.00	7,500 SF threshold.	Yes.	Substantial.	Fee has not changed since 1993; may negotiate fee downward based on hardship or reduced impact.
Town of Corte Madera	2001	• Office $4.79 • R&D lab $3.20 • Light Industrial $2.79 • Warehouse $0.40 • Retail $8.38 • Com Services $1.20 • Restaurant $4.39 • Hotel $1.20	No Minimum Threshold.	NA	Substantial	
f Sunnyvale	1984	• Industrial & Office $8	Applies only to projects with FAR exceeding 0.35 to 1 FAR. Applies to specific areas in City only.	NA	Very Substantial	Fee had not changed since the 1980's, until fee was recently raised from $7.19.

City of Santa Monica	1984 Updated fees in 2002.	• Office only • $3.87 per square foot for first 15,000 sf • $8.61 per square foot in excess of 15,000 sf.	15,000 sf exemption for new construction, 10,000 sf exemption for additions.	N/A	Very Substantial	

LOW FEE CITIES

Jurisdiction	Yr. Adopted	Current Fee Levels per SF	Thresholds & Exemptions	Build Option/ Other	Market Strength	Comments
City of Alameda	1989	• Office $3.63 • Retail $1.84 • Warehouse $0.63 • Hotel/Motel $931 per room	No Minimum Threshold. Publicly owned and used for public purpose.	Yes. Program specifies number of units per 100,000 square feet.	Moderate	Fee may be adjusted by CPI.
City of Cupertino	1993	• Office & Industrial $2.13.	No Minimum Threshold.	NA	Very Substantial	Fee is adjusted annually based on CPI. Update in process.
City of Petaluma	2003	• Commercial $2.08 * • Industrial $2.15 * • Retail $3.59 * (See Comments)	Fee is 50% less if located in redevelopment project area	NA	Moderate/ Substantial	* Fee will be phased-in over 3 years beginning 2005. Fees listed are full fees, starting in 2007.
City of San Diego	1990 Fees reduced in mid 90s; have not been readjusted.	• Office $1.06 • Hotel $0.64 • R&D $0.80 • Retail $0.64 • Manufacturing $0.64 • Warehouse $0.27	No Minimum Threshold. No Exempted uses. Does exclude some geographic areas.	Can dedicate land or air rights in lieu of fee.	Substantial	Since 1990, $33 million raised. Update in process.
City and County of Napa	County 1994 City 1999	• Office $1.00 • Hotel $1.40 • R&D $0.80 • Industrial $0.50 • Warehouse $0.20/0.30 • Wine Production $0.50	No Minimum Threshold. Non-profits are exempt.	Units or land dedication; on a case by case basis.	Moderate/ Substantial	There is a companion fee 1% of construction costs on all residential construction. Update in process.
City and County of Sacramento	1989	• Office $0.99 • Hotel $0.94 • R&D $0.84 • Commercial $0.79 • Manufacturing $0.62 • Warehouse/Office $0.36 • Warehouse $0.27	No Minimum Threshold. Service uses operated by non-profits are exempt.	Pay 20% fee plus build at reduced nexus. (No meaningful given amount of fee).	Moderate	Applies to all non-residential construction; alternate fees for North Natomas area. Since 1989, raised more than $11 million.
City of Livermore	1999	• Retail $0.81 • Service Retail $0.61 • Office $0.52 • Hotel $397 per room • Manufacturing $0.25 • Warehouse $0.07 • Business Park $0.52 • Heavy Industrial $0.26 • Light Industrial $0.16	No Minimum Threshold. Church; private or public schools.	Yes; negotiated on a case-by-case basis.	Moderate	
City of Pleasanton		• Commercial $0.50 sq. ft.	No Minimum Threshold	NA	Moderate	

Programs Pending: San Mateo
San Rafael
Walnut Creek

CITY OF WALNUT CREEK

Agenda Item No. 5

AGENDA REPORT

DATE: FEBRUARY 15, 2005

TO: CITY COUNCIL

FROM: COMMUNITY DEVELOPMENT DEPARTMENT - HOUSING

SUBJECT: IMPOSITION OF A FEE ON COMMERCIAL DEVELOPMENT FOR AFFORDABLE HOUSING

STATEMENT OF ISSUES: On January 4, 2005, Council heard a presentation on the Jobs Housing Linkage Analysis, program 13.19 of the Housing Element, from staff and the consulting firm Keyser Marston Associates (KMA). The presentation provided an overview of the draft Commercial Development Fee Ordinance that has been recommended for adoption by the Planning Commission, and provided an opportunity for Council to study the issue. That fee is being presented to the City Council for adoption

STAFF RECOMMENDATION: The Planning Commission and staff are recommending that the City Council adopt the proposed fee on commercial development for affordable housing.

DISCUSSION: The ordinance and fee resolution would apply a $5 per square foot fee to new or expanded commercial uses (retail, office, R&D, medical, and hospital uses) and conversion of non-commercial space to commercial space. The ordinance provides an exemption for the first 500 square feet of a commercial project, and provides exemptions or fee reductions for residential/commercial mixed-use projects to encourage development. The Planning Commission and staff are recommending in favor of the ordinance for the following reasons:

- A Jobs-Housing Nexus Study completed in mid-2004 indicates that there is a nexus between Commercial Development and demand for affordable housing in Walnut Creek, and moreover, that a linkage fee is legally supportable up to a maximum of $28.41 for Office, $21.48 for Retail, $19.06 for Medical, and $17.12 for Hotel.

- Development in Walnut Creek has the market strength to sustain the proposed fee for affordable housing without deterring new feasible projects.

- A linkage fee would provide another financial resource to create affordable workforce housing in Walnut Creek, thereby increasing the limited pool of funds, and the City's

ability to leverage non-local resources. For every City dollar committed to an affordable housing project, the project can leverage from $5 to $8 from federal, state or private resources.

- The fee would be part of a comprehensive plan to address affordable housing need; it requires that the commercial development community participate in the affordable housing solution as residential developers are now asked to do through the inclusionary housing ordinance and residents are asked to do through the use of general fund and CDBG funds.

Council Questions: KMA presented an overview of the Linkage Fee Analysis and answered questions from Council on the methodology.

Council pointed out that during the period from 1990 to 2000, much of the housing that was built was senior housing. Staff researched this and found that about 423 units of 676 multifamily units were senior units at Rossmoor. This finding does not effect the linkage fee analysis but it does indicate that workforce housing production was relatively low in the Nineties.

Council also raised a question regarding Table II-6 in the Linkage Analysis. Council indicated the total production estimate of 648,612 square feet from 1990 to 2006 seemed high. Staff reviewed the project pipeline and Table II-6 and requested that KMA make a few revisions to correct the Table. The revised Tables and cover memorandum from KMA are in Attachment 3 to this report. The changes corrected misclassification of new retail space as office, and corrected dates of construction completion, which resulted in a slightly lower total construction figure. These changes result in a change of the ratio of new housing production to new housing demand. However, this has no bearing on the rest of the analysis, and does not impact the conclusions of the Linkage Analysis.

One Council member was concerned about how the proposed ordinance would affect hospitals, particularly John Muir's planned expansion. The Planning Commission had asked John Muir representatives about the cost of the proposed Phase IV development. Based on their answer, the proposed linkage fee would be about 1.5% of the construction cost. The Planning Commission determined that when this cost was born over time through financing mechanisms, it would amount to a minimal impact to the project. Additionally, it was noted that John Muir is one of the largest employers in the City and the proposed expansion will have an impact on the demand for affordable housing in Walnut Creek.

In terms of administering the ordinance, Council requested that the administrative procedures prioritize applicants for affordable units who live or work in Walnut Creek at the time they apply. These guidelines are also currently within the Inclusionary Ordinance administrative procedures.

OVERVIEW OF ORDINANCE AND FEE RESOLUTION: Attachment 1 to this report is a Draft Commercial Linkage Fee Ordinance. On January 4th, Council reviewed the Ordinance and provided comments on each of the sections. Council's comments are included in the Discussion section under each Section heading.

Sec 10-13.102. Requirement: The proposed fee would be applied to net new square footage, excluding parking structures, of all *Commercial Uses*, *Research and Development Industrial Uses*, and the specific *Community Uses* of Hospitals, and Emergency Medical Care/No Inpatient. The

"requirement" section of the proposed ordinance also sets the timing for payment at the issuance of a building permit, unless conditioned or approved by the Community Development Director to allow payment prior to Certificate of Occupancy.

Discussion: At the January 4th Council meeting, it was discussed whether to include churches or other Community Facility Use classifications under the ordinance; but no agreement was reached. One Council member expressed concern about hospitals being included and suggested that they be exempt from the ordinance.

Sec 10-13.103.B. Exemptions: the exemptions listed, include:

- Reconstruction of original Commercial Project square footage due to natural disaster (net new square footage will be subject to the fee)
- Project applications that have already been deemed complete (Design Review, Use Permit, re-zoning, etc.)
- Replacement of existing applicable project square feet that is demolished (ordinance would only apply to net new space)
- The first cumulative 500 square feet of expansions or new construction on applicable projects after the effective date of the ordinance
- Parking structures

Discussion: Council members discussed the 500 s.f. exemption limit. One Council member felt it was too low, one Council member felt it could be higher, but 1500 s.f. was too high, another member felt that 1500 s.f. would be acceptable, and one member would like to have no size exemptions. The Council did not reach consensus on this issue.

Sec 10-13.103.C. Calculation of the Fee. This section explains how the fee would be calculated and refers to a fee amount that would be established in a Council Resolution. Attachment 2 is the proposed Fee Resolution which sets the fee at $5.00 per square foot. The proposed Resolution also establishes a maximum of five years within which to review the fee level, as proposed by the Planning Commission.

Discussion: Two Council members felt the fee of $5/sf was fair, one member felt is was fair if hospitals were exempted, and another member raised the possibility of having a range of fees for different types of uses, as some other municipalities require. One possible alternative is to have just two fee levels, one for hospitals and one for all others uses.

Sec. 10-13.104. Adjustments. A waiver or reduction in fees is proposed, if a developer can document to the City that there is no reasonable nexus between the fee and the proposed project, subject to the Community Development Director's concurrence and approval. An example of where this might apply would be a mini-storage facility use that has no employees, or one occasional employee, and could not be re-tenanted for an employee-based use without a major tenant improvement; otherwise the fee would apply. Fee reductions or waivers would be based on building construction rather than the proposed initial tenant.

Discussion: The Council was in agreement with this section as proposed.

Sec. 10-13.105. Mixed Use Projects. This section provides a way to encourage mixed-use development by allowing credit toward the housing impact fee for projects that will be providing Inclusionary Housing Units.

For mixed-use projects of less than 65% residential square footage, credit toward the linkage fee would be applied on a three-to-one basis for Inclusionary Unit floor space to commercial floor space within the mixed-use project. For example, a two-story project of residential over commercial might include one Inclusionary Unit of 1,000 square feet, and 10,000 square feet of commercial space. The Inclusionary Unit's 1,000 square feet would be multiplied by 3, resulting in 3,000 square feet. Then 3,000, plus the 500 initial square foot exemption, would be subtracted from 10,000 square feet of commercial space, to arrive at 6,500 square feet of commercial to which the linkage fee would apply. In this example, the total fee would be $32,000.

Discussion: Council felt that the application of this incentive was somewhat confusing and maybe unnecessary. Some members felt there did not need to be an incentive to encourage mixed-use development because it will occur in any case. Should Council desire, the mixed-use project section could be removed from the ordinance.

Sec. 10-13.106. Conversions. The ordinance defines any space that is converted to a Commercial Development Project as net new commercial square footage, to which a fee would then be applied.

Discussion: Council split on the issue of converted space— two members felt that space that converted from a non-commercial use to a commercial use could be exempt from the ordinance, and two members felt it should be included because a conversion of use from non-commercial to commercial would result in net new commercial square footage, and that is precisely what is subject to the ordinance.

Sec. 10-13.107. Use of Funds. This section is required to generally describe to what purpose and use the funds will be put. All funds generated from the proposed fee would be used to create new affordable residential units for workef households. Funds must be committed to a project within five years of receipt.

Discussion: Council had no comments to change this section; but one member suggested adding more specific language about how the funds could be used. The City Attorney indicated that the specific uses should be designated in the budgeting process, not in the ordinance.

Sec. 10-13.108. Alternative to Payment of a Fee. This section allows the developer to build affordable housing within Walnut Creek instead of paying the fee, subject to Council approval.

Discussion: Council had no changes to this section.

ENVIRONMENTAL REVIEW: A Negative Declaration for this project was posted on November 17th and the public comment period ended on December 7, 2004. No comments were received.

FINANCIAL IMPACTS: If the proposed ordinance and fee resolution are adopted, it is estimated that additional revenues of approximately $375,000 or more per year may be raised for affordable housing programs. There would be some additional staff effort in implementing the ordinance and monitoring compliance but the impact would be minimal.

ALTERNATIVES: The Council may choose to continue the hearing on the item, or direct staff to make revisions to the ordinance and resolution, or not approve the ordinance and resolution.

ATTACHMENTS:
Attachment 1: Ordinance Imposing a Fee on Commercial Development
Attachment 2: Commercial Development Fee Resolution
Attachment 3: KMA Memorandum and Revised Linkage Analysis Tables
Attachment 4: Public Correspondence regarding the Ordinance

COUNCIL ACTION NEEDED: Move to introduce and waive further reading of the ordinance imposing a fee on commercial development for affordable housing.

Prepared by: Laura Simpson, Housing Program Manager

Valerie Barone, Department Director

Approved by: _____
City Manager

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ATTACHMENT 1

ORDINANCE NO.

AN ORDINANCE OF THE CITY OF WALNUT CREEK ADDING CHAPTER 13 TO TITLE 10 OF THE MUNICIPAL CODE RELATING TO IMPOSING A FEE ON COMMERCIAL DEVELOPMENT FOR AFFORDABLE HOUSING PURPOSES

The City Council of the City of Walnut Creek does ordain as follows:

Section 1. Findings.

a. Persons of low and moderate income are experiencing increasing difficulty in locating and maintaining adequate, safe and sanitary affordable housing within the City of Walnut Creek. As noted in the City's Housing Element, a regional shortage of affordable housing is contributing to overpayment for housing accommodations. According to the Association of Bay Area Governments' Regional Housing Needs Projections, the City of Walnut Creek needs to provide additional housing affordable to persons of low and moderate income who are expected to become residents of the City.

b. Development of new commercial projects encourages new residents to move to the City. Some of the employees needed to meet the needs of new commercial development earn incomes only adequate to pay for affordable housing. Because affordable housing is in short supply within the City, these employees now may be forced to live in less than adequate housing within the City, pay a disproportionate share of their incomes to live in adequate housing within the City, or commute ever-increasing distances to their jobs from housing located outside the City. These circumstances harm the City's ability to attain goals articulated in the City's General Plan.

c. Prices and rents for affordable housing remain below the level needed to attract adequate new construction. At the same time, escalating land costs and rapidly diminishing amounts of land available for development hinder the provision of affordable dwelling units solely through private action. Federal and State housing finances and subsidy programs are not sufficient by themselves to satisfy the affordable housing needs.

d. An April 2004 report, as amended to include the addendum of December 2004, prepared by Keyser Marston Associates, Inc., documented the linkage between new and expanded workplace buildings, the employees that work in them, employee households, and the housing demands of these households. New housing affordable to persons identified in the study is not now being added to the supply in sufficient quantity to meet the needs of the new employee households associated with new or expanded workplace buildings. The study also identifies the gap in housing costs per square foot of commercial development that needs to be filled to meet the needs for affordable housing for the buildings' workers. The City Council is imposing the fee established by this

ordinance in order to partially close this gap by using the fee to provide for increased affordable housing.

f. The City Council has considered the proposed Negative Declaration together with all comments received during the public review process. The City Council finds on the basis of the whole record before it (including the Initial Study and all comments received) that there is no substantial evidence that the project will have a significant effect on the environment and that the Negative Declaration reflects the City Council's independent judgment and analysis. The documents and other material which constitute the record of proceedings upon which this decision is based are maintained by the custodian of records, the City Clerk, at 1666 N. Main St., Walnut Creek.

Section 2. Negative Declaration.

The City Council hereby adopts the Negative Declaration.

Section 3.

Chapter 13 (commencing with section 10-13.101) is hereby added to Title 10 of the Walnut Creek Municipal Code to read as follows:

Chapter 13. Fee on Commercial Development for Affordable Housing

Sec. 10-13.101. Purpose.

The purpose of this chapter is to facilitate the development and availability of housing affordable to a broad range of households with varying income levels within the City. It is intended in part to implement state policy that declares that local governments have a responsibility to exercise their powers to facilitate the development of housing to adequately provide for the housing needs of all economic segments of the community. It is also intended to implement the program in the Housing Element of the General Plan that calls for the study of a jobs/housing linkage fee to facilitate affordable housing projects. The goal of this chapter is to impose a fee on new commercial development that partially funds the need for affordable housing created by the workforce of this new development.

Sec. 10-13.102. Definitions.

For the purposes of this chapter "commercial development projects" shall mean those projects consisting of new construction or net new gross square footage for all the use classifications defined under section 10-2.1.403 B, Commercial Use Classifications, of this code, those uses defined as Research Development Industry under section 10-2.1.403 C of this code, those uses defined as Hospital and Acute Medical Care under section 10-2.1.403 E of this code, and any use determined to be a commercial use by the Zoning Administrator pursuant to section 10-2.1.401of this code.

Sec. 10-13.103. Commercial Development Project Housing Impact Fee.

A. Requirement. A housing impact fee is hereby imposed on all commercial development projects.. No application for a building permit for a commercial development project shall be approved, nor shall any such commercial development project be constructed, without compliance with this chapter. The fee imposed by this chapter shall be collected at the time of the issuance of a building permit. The collection of fees may be delayed until the certificate of occupancy is issued, if approved by the Community Development Director. No certificate of occupancy shall be issued for a commercial development project that has not paid a fee required under this chapter.

B. Exemptions. Notwithstanding subsection A, this chapter shall not apply to the following:

1. Reconstruction of any building that was destroyed by fire, flood, earthquake or other act of nature, so long as the square footage does not exceed the square footage before the loss.

2. Any project for which an application for Design Review Commission approval was deemed complete prior to the date of adoption of the Ordinance.

3. Replacement for commercial use gross floor area previously on the site but demolished within one year prior to the filing of a complete application for the new construction.

4. Expansions or new construction of less than 500 square feet.

5. Parking lots or parking structures.

C. Calculation of the fee. The housing impact fee shall be charged on a square foot basis for all net new gross floor area. The amount of the fee shall be established by resolution of the City Council.

Sec. 10-13.104. Adjustments.

A. The requirements of this chapter may be adjusted or waived if the developer demonstrates that an insufficient nexus exists between the proposed use and the housing impact fee. The developer shall submit documentation demonstrating this with a request for an adjustment or waiver in writing to the Community Development Director no later than the date it files its initial development application with the city. The developer shall provide such additional information as may be required by the Community Development Director to make a determination on the request. The determination of the Community Development Director may be appealed to the City Council as provided in section 1-4.01 et seq. of this code.

B. The requirements of this chapter may be adjusted or waived if the developer demonstrates that applying this chapter would take property in violation of the United

States and/or California Constitutions. The developer shall submit a request for an adjustment or waiver in writing to the Community Development Director no later than the date it files its initial development application with the city. The developer shall provide such additional information as may be required by the Community Development Director to make a determination on the request. The determination of the Community Development Director may be appealed to the City Council as provided in section 1-4.01 et seq. of this code.

Sec. 10-13.105. Mixed Use Projects.

A. If the commercial development project also includes housing, and the project is 65% residential square footage or more, then the commercial space will be exempt from this chapter.

B. In any other mixed-use project, the Inclusionary Unit square footage will be multiplied times a factor of three (3) and the commercial development project net new commercial square footage shall then reduced by that amount. The housing impact fee will apply to the balance of the commercial space.

Sec. 10-13.106. Conversions.

If a development is exempt from the fee at initial construction, but later converts to a commercial development project, the converted square footage will be deemed net new commercial square footage and the housing impact fee shall be paid be a condition of the building permit or certificate of occupancy.

Sec. 10-13.107. Use of Funds.

All funds derived from this chapter shall be placed in a separate account and used solely to increase the supply of housing affordable to worker households of very low, low and moderate income.

Sec. 10-13.108. Alternative to payment of a housing impact fee.

As an alternative to payment of the housing impact fee, a developer of a nonresidential development project may submit a request to mitigate the impacts of such development through the construction of residential units, the dedication of land for affordable housing, or provision of other resources. Such requests may be granted in the sole discretion of the City Council, if the City Council determines that such alternative will further affordable housing opportunities in the city to an equal or greater extent than payment of the housing impact fee.

Section 4.

The fee imposed by Section 2 of this ordinance shall take effect on the 60th day following adoption of this ordinance.

Section 5. Effective Date.

This Ordinance shall take effect on the 31st day following its adoption.

H:\LauraSimpson\commercial linkage fee\Ordinance.doc

ATTACHMENT 2

RESOLUTION NO. 05-

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF WALNUT CREEK ESTABLISHING AN AFFORDABLE HOUSING FEE ON COMMERCIAL DEVELOPMENT

WHEREAS, there is a reasonable relationship between the need for affordable housing and the impacts of commercial development within the City. There is also a reasonable relationship between the fee's use and the impacts of commercial development. Development of new commercial projects encourages new residents to move to the City. Some of the employees needed to meet the needs of new commercial development earn incomes only adequate to pay for affordable housing. Because affordable housing is in short supply within the City, these employees might otherwise be forced to live in less-than-adequate housing within the City, pay a disproportionate share of their incomes to live in adequate housing within the City, or commute ever-increasing distances to their jobs from housing located outside the City. These circumstances harm the City's ability to attain goals articulated in the City's General Plan.

WHEREAS, the Municipal Code has been amended by adding Chapter 13 to Title 10 (commencing with section 10-13.101) to require developers of commercial projects to pay a fee to mitigate the impact on the need created for affordable housing by the commercial development; and

WHEREAS the Municipal Code as amended allows the City Council by resolution to set this housing impact fee; and

WHEREAS, the City has had prepared a Jobs Housing Nexus Analysis ("Nexus Study") done by Keyser Marston Associates dated April 2004, and as amended to include the addendum of December 2004, to satisfy to the Mitigation Fee Act (Government Code Section 66000, et seq.); and

WHEREAS, the Nexus Study has found that there is a nexus between new commercial floor area, the creation of jobs, and the demand for low and moderate income housing for new employees; and

WHEREAS, the fee will be used solely to increase the supply of housing affordable to very low-, low-, and moderate-income employees; and

WHEREAS, the fees will be placed in a separate fund and used exclusively for the development of affordable housing within the City.

NOW, THEREFORE, the City Council of the City of Walnut Creek resolves as follows:

1. The housing impact fee authorized by Municipal Codes section 10-13.103 is hereby set at $5.00 per square foot.

2. The housing impact fee will be reviewed at least every five years.. If the housing impact fee is not reviewed or changed at such a time, the existing fee shall remain in effect.

3. Effective Date. The fee established in this Resolution shall take effect on the 60th day following the adoption of this Resolution.

H:\LauraSimpson\commercial linkage fee\FeeReso11_10.doc

ATTACHMENT 3

KEYSER MARSTON ASSOCIATES INC.

GOLDEN GATEWAY COMMONS
55 PACIFIC AVENUE MALL
SAN FRANCISCO, CALIFORNIA 94111
PHONE: 415 / 398-3050
FAX: 415 / 397-5065
WWW.KEYSERMARSTON.COM

MEMORANDUM

To: Laura Simpson
City of Walnut Creek

From: Kate Earle Funk

Date: February 4, 2005

Subject: Revised Tables

Following this cover memo are revised tables for Section II of our report. The revisions primarily concern past and on-going construction activity in Walnut Creek. The tables have been revised based on information provided by City staff. Some of the earlier tables had some buildings either inappropriately classified as office when they were, in fact, retail structures and also some date of construction inconsistencies.

Information on construction activity both past and in the "pipeline" was provided in the report to illustrate the rate at which Walnut Creek was producing jobs and worker households associated with new construction, and how that rate compared to new housing units produced. As noted in Table II-3, past housing unit production information has also been amended to acknowledge units built for seniors. All these changes will result in changes in the ratio of new housing production to new housing demands. Since this portion of the analysis does not take into account affordability, it has no bearing on the rest of the analysis and in no way impacts the conclusions of the nexus analysis.

The final report will be revised to incorporate these revised tables and the text will be adjusted accordingly.

TABLE II-2 (Revised 2/05)
NON-RESIDENTIAL CONSTRUCTION ACTIVITY 1990-2000
JOBS HOUSING NEXUS ANALYSIS
CITY OF WALNUT CREEK

Square Feet Building Area

YEAR[1]	OFFICE	RETAIL	SMALL[2]	OTHER[3]	ALL BUILDING TYPES	COMMUNITY FACILITIES[4]
1/1/90-8/31/92					86,683	
9/1/93-8/31/95		20,369			20,369	
9/1/95-8/31/97		42,000	11,174		53,174	
9/1/97-8/31/99	13,721	52,587	2,104		68,412	127,043
9/1/99-8/31/01	50,065	2,885	4,844	41,061	98,855	
Total (1990-2001)	63,786	117,841	18,122	41,061	327,473	127,043
Annual Average	5,799	10,713	1,647	3,733	29,770	11,549

Source: CIRB and City of Walnut Creek. There was no hotel/motel or industrial development during this time period. Incomplete projects are excluded from the analysis.

[1] Construction prior to 1993 was exempt from the Growth Limitation Plan. The City began to track building activity in net new square footage in 1993, based on two year increments. For the purpose of this analysis, building activity for 1990-August 1993 is based on building permit data from Construction Industry Research Board and reflects the lag between permit issuance and building completion. Data is available by permit valuation, which was converted to square feet. Building alteration and additions are excluded from the analysis.

[2] Includes projects smaller than 2,500 sq ft.

[3] A storage facility expansion that was not included in the jobs-housing nexus due to minimal employment.

[4] Kaiser Medical Center expansion. (Community Facility square footage is not tracked under the Growth Limitation Plan.)

TABLE II-4 (Revised 2/05)
RESIDENTIAL UNITS -- PERMITTED, 1990-1999
JOBS HOUSING NEXUS ANALYSIS
CITY OF WALNUT CREEK

TOTAL UNITS (Per City) 1990-1999[1]

Year	Single Family	Multiple-Family	Total
1990	72	63	135
1991	42	244	286
1992	17	92	109
1993	19	0	19
1994	14	36	50
1995	30	49	79
1996	57	36	93
1997	20	63	83
1998	46	37	83
1999	27	56	83
Total	**344**	**676**	**1,020**
Annual Average	34	68	102
Senior Units	43	426	469
Total Excl. Senior Units	***301***	***250***	***551***

TOTAL UNITS BY AFFORDABILITY LEVEL, 1990-1999[2]

Affordability Level	With Deed Restrictions		Total Affordable[4]	
	Units	% Share	Units	% Share
Very Low: < 50% Median Income[3]	20	56%	31	13%
Low: 50 - 80% Median Income[3]	16	44%	48	19%
Moderate: 80 - 120% Median Income[3]			169	68%
Total Affordable Units Constructed	**36**	**100%**	**248**	**100%**
Affordable Units as Share of Total Units Constructed		**4%**		**24%**

[1] Sources: City of Walnut Creek, Community Development Department (March 17, 2003) based on figures prepared for the State Department of Finance. Single-family units include second units. Counts are net of any demolitions or removals. Excludes units gained through annexation.

[2] Affordable unit count is based on the City's prior Housing Element. Includes new units that are assumed to have long term income and affordability restrictions. Specifically, the left column excludes the Tice Oaks Senior Apartment project (an acquisition rehab project that preserved affordable units, but did not produce net new affordable units) & Ivy Hill Apts (construction began 2000, completed 2002) and Montego Senior Apartments (these affordable units are restricted to senior citizens; it is unlikely that workers are eligible for the units). "The Oaks" (LIHTC and CDBG funds) is included.

[3] First Time Homebuyer program may not have income restrictions on resale.

[4] Includes the restricted units plus affordable units identified in the Housing Element. Market rate rentals are assumed to be affordable to moderate income based on prevailing current rent levels for new units.

Prepared by: Keyser Marston Associates, Inc.
Filename: 21101.005\Macro Analysis Tables feb 2005.xls

TABLE II - 6 (Revised 2/05)
NON-RESIDENTIAL CONSTRUCTION: PIPELINE AND PER GROWTH LIMITATION PLAN
JOBS HOUSING NEXUS ANALYSIS
CITY OF WALNUT CREEK

Square Feet Building Area

Building Type	A Construction Completed 1990-8/2001[1]	B Completed Since 9/2001 and Pipeline (SF)[2]	C Balance of Allowable Development Thru 2006 (= GLP[3]-A-B)	Total Projected Construction (SF) 2001-2006[4] (=B+C)
Office	63,786	152,492	83,816	236,308
Retail	117,841	223,828	83,816	307,644
Small	18,122	3,575	25,000	28,575
Other	41,061	0	0	0
Total[5]	327,473	379,895	192,632	572,527
Annual Avg	29,770			95,421

1 See Table II-2; period is eleven years.

2 Includes projects completed since 2001 and "Under construction", "Approved" and "Under Review" from reservation and construction pipeline reports

3 Allows 900,000 square feet of commercial development from 1993 to 2006 (excluding community facilities, ie Kaiser Medical Center). Allowable square footage is allocated equally between office and retail with 25,000 SF reserved for small projects.

4 Assumes the GLP maximum allowable square footage for the time period 2001-2006.

5 See Table II-2. Includes 86,663 SF (all building types) for 1990-8/31/1993.

Prepared by: Keyser Marston Associates, Inc.
Filename: 21101.005\Macro Analysis Tables feb 2005.xls

TABLE II -7 (Revised 2/05)
ESTIMATED JOB GENERATION 2001-2006
JOBS HOUSING NEXUS ANALYSIS
CITY OF WALNUT CREEK

Building Type	Anticipated Construction (SF)[1]	Density Factor SF/Employee[2]	Projected Jobs
Office	236,308	220	1,074
Retail	307,644	400	769
Small	28,575	300	95
Total	***572,527***	***300***	***1,938***

1 See Table II - 6

2 City of Walnut Creek General Plan (1989)

Prepared by Keyser Marston Associates, Inc.
File name: 21101.005\Macro Analysis Tables feb 2005.xls

TABLE II - 8 (Revised 2-05)
PROJECTED EMPLOYMENT GROWTH, RESIDENTIAL UNIT DEMAND
JOBS HOUSING NEXUS ANALYSIS
CITY OF WALNUT CREEK

ABAG PROJECTIONS	Jurisdictional Boundary Jobs
Projected Job Growth - Per ABAG[1]	
2000	56,280
2010	62,350
Increase	6,070
Worker Households @ 1.65	3,679
Projected Households/Housing Units - Per ABAG[1]	
2000	30,301
2010	32,680
Increase	2,379
Relationship Housing Units to New Worker Households	0.65 :1
CITY PROJECTIONS (2001-2006)	
Jobs Associated with GLP Projections[2]	1,938
Worker Households @ 1.65	1,175
Projected Housing Supply	
Units Completed or in Pipeline[3]	888
Additional Units Under GLP[4]	1,205
Total	2,093
Relationship of Housing Units to New Worker Households	1.78 :1

1 ABAG Projections 2003

2 See Table II-7

3 Includes completed projects such as Ivy Hill Apts, "Under construction", "Approved" and "Under Review" from City's recent pipeline reports. (Housing Element, Summary of Progress toward RHND.)

4 Equals 2,500 units allowed under Growth Limitation Plan less units constructed since 1993. Excludes all development on BART property.

Prepared by: Keyser Marston Associates, Inc
Filename: 21101.005\Macro Analysis Tables feb 2005.xls

ATTACHMENT 4: PUBLIC CORRESPONDENCE

cc: Council
Mike
Valerie
Laura

The Mayor and City Council of Walnut Creek
1666 North Main St.
Walnut Creek, CA 94596

Dear City Council, January 31, 2005

I live in Walnut Creek and strongly support the ordinance before you that will assess a fee on new commercial development to be used for affordable housing. The short-term beneficiaries of this will be those who take advantage of the affordable housing. In the long run, though, we all benefit from this by promoting a city with a diverse citizenry where the teachers, police force and retail workers can all afford to live in the city where they work.

A few thoughts about the commercial development linkage fee:

- Every other segment of the community already contributes (at least indirectly) to the effort to provide affordable housing. Why shouldn't new commercial development? Residential developers must include affordable units or pay a fee and WC residents contribute through programs paid for by the City's general fund.
- Many other Bay Area cities already have similar fees. For example, Palo Alto assesses $15 per sq. foot and Pleasanton assesses $2.28 per sq. foot.
- Walnut Creek can obtain at least $5 in federal and private funding for every dollar it spends on affordable housing (this is an estimate per a consultant's report).

Also, I feel strongly that Kaiser and John Muir *should not* be exempt from this fee should it pass.

I hope you all will vote for this assessment. While the funds it will generate will still not meet the growing need for affordable housing in this increasingly expensive region, it's a very good start.

Sincerely,

Caedmon Bear
2024 Walnut Blvd.
Walnut Creek, CA 94597
(925) 934-3442

cc: Council
Mike
Valerie
Laura
Clerk

2644 San Carlos Drive
Walnut Creek, CA 94598

January 29, 2005

Mayor and City Council of Walnut Creek
1666 North Main Street
Walnut Creek, CA 94596

Dear Mayor Skrell and City Council Members:

I am writing to urge you to adopt the commercial development linkage fee of $5 per square foot an new development, and not to exempt John Muir and Kaiser. Much as the two medical facilities contribute to the city, they are far from disinterested benefactors, and they should still pay their way. The medical technicians, clerical assistants, practical nurses, orderlies, etc., that they employ need affordable housing as much as the waitstaff and other modestly-paid employees of other employers. To leave out two of Walnut Creek's biggest three employers would favor them unfairly. All employers should contribute to the provision of affordable housing equally.

Walnut Creek is desirable enough a location to command a fee of this magnitude without inhibiting its economic activity.

Please vote yes on the linkage fee without exception.

Sincerely,

Jeanne-Marie Rosenmeier

01/25/05

cc: Council
Mark
Valerie
Laura
Clerk

Dear Sir or Madam:

I am writing this letter to support the Diablo Greens proposal to impose a fee on commercial development over 500 sq. ft.

It would greatly benefit the community by providing much needed affordable housing to those who really need it. Many other cities in the Bay Area have such fees and it would take little to no effort to bring this fee to a well established financial center like Walnut Creek.

Please consider this ordinance at the 02/15 meeting in Walnut Creek.

Thank you,

Valentin Lorien
1869 Lacassie Av, Apt. 2
Walnut Creek, CA 94596

Council
Muir
Clerk
Valerie B
Yana

Diablo Greens

Commercial Linkage Fee Talking Points

- A Jobs-Housing Nexus Study commissioned by the city found a connection between jobs and the need for affordable housing.
- The Jobs-Housing Nexus Study found that linkage fees of up to $28 per square foot would still not meet the increased need for affordable housing in Walnut Creek. But at least a $5 fee is a start.
- Because Walnut Creek has such vibrant commercial activity, it can support the imposition of a $5 fee.
- For every dollar the City spends on affordable housing, it can obtain at least $5 from federal or private funding sources.
- The City is committed to finding ways to provide housing for its workforce. A linkage fee could provide a valuable additional funding mechanism.
- Every other segment of the community already contributes to the effort to provide affordable housing. Residential developers must include affordable units in new development, or pay an in-lieu fee. The residents of Walnut Creek contribute through several programs paid for by the City's general fund.
- Most other important cities in the Bay Area already have such fees.

One unsettled issue is whether or not to exempt John Muir Hospital and Kaiser (two of Walnut Creek's three largest employers) from the fee. The Diablo Greens have not taken a stand on this question. My feeling is that their employees need affordable housing as much as anyone, and so the fee should be imposed on their building projects too. (Remember our concept of "true-cost" pricing.) If you care to comment on the proposed exemption for the big medical facilities, please do.

Ask the City Council to please vote to pass the ordinance imposing a commercial development linkage fee.

Sincerely,

Lloyd Scaff

Mr. Lloyd Scaff
2449 Pine Knoll Dr Apt 2
Walnut Creek, CA 94595-2192

1/29/05

cc: Council
Mike
Clark
Valerie
Laura

Mayor and City Council
of Walnut Creek,

As a resident of Walnut Creek I am asking you to please Vote to pass the ordinance imposing a commercial development linkage fee.

I believe for our city to remain, and continue to prosper this ordinance should be passed.

Thank You,

Louis J. Villano
1370 Second Ave.
Walnut Creek, Ca. 94597

Mayor & City Council
Walnut Creek, CA.

cc: Council
Mike
Valerie
Laura
Clerk

Dear Friends,

I urge you to adopt a $5/sq.FT. fee on large commercial development in Walnut Creek. It could do much to help the City provide some affordable housing, which is badly needed.

I understand that many other cities in California already have such a fee — it makes sense for us.

I'm sure most of my fellow Rossmoor residents will also be in favor of this fee.

Sincerely,
Robert J. Hanson

Mr. Robert Hanson
Apt 3
2600 Saklan Indian Dr
Walnut Creek, CA 94595-3057

cc: Council
Mike
Valerie
Laura
Clerk

January 28, 2005

Mayor and City Council
Walnut Creek
1666 North Main Street
Walnut Creek, CA 94596

Dear City Officials,

As a resident of Walnut Creek and as a past practicing urban planner I am writing in support the ordinance that would assess a fee on new commercial development. I understand that the proceeds of the fee would be used for affordable housing.

Walnut Creek certainly can afford the five dollar per square foot assessment. We need to assist in provide housing for our work force. It's time for new development to participate like the rest of the community.

Sincerely,

William F. Klein
1744 Carmel Drive, #201
Walnut Creek, CA 94596

CONTRA COSTA HOUSING Trust Fund INITIATIVE

January 3, 2005

To: Mayor Gary Skrel
Mayor Pro Tem Kathy Hicks
Councilmember Susan McNulty Rainey
Councilmember Gwen Regalia
Councilmember Charlie Abrams

From: Marti Buxton, Director
Contra Costa Housing Trust Fund Initiative

Re: **Proposed Walnut Creek Commercial Linkage Fee**

Dear Mayor Skrel and Councilmembers:

I am writing on behalf of the Contra Costa Housing Trust Fund Initiative in support of the proposed Walnut Creek Commercial Linkage Fee. The Housing Trust Fund (HTF) is a countywide coalition of business, nonprofit, labor, faith and public representatives working to establish dedicated revenue sources to address affordable housing needs throughout the 19 cities and the unincorporated areas of Contra Costa. The HTF is led by a Steering Committee that was established in last year. Both former City Manager Don Blubaugh and Senior Housing Specialist Laura Simpson provided excellent advice and direction during the establishment of the HTF Steering Committee and we continue to value their counsel.

The goal of the HTF Initiative is to have at least one dedicated revenue source in place by the end of this year. Last year David Rosen and Associates analyzed in detail numerous revenue sources and recommended that the HTF pursue only a few. The Commercial Linkage Fee was by far the most "straight forward" in that there is a clear nexus between the construction of buildings that will house employees and the need for those employees to have housing. Ideally, employees will be able to live and work in the same community, an ideal that enriches the quality of life for everyone.

The funds generated by the Walnut Creek Commercial Linkage Fee will, of course, remain in the City of Walnut Creek and fund the construction of sorely needed affordable housing within the city limits. It is our hope that the successful implementation of this fee in Walnut Creek will encourage other communities to adopt a commercial linkage fee that will provide funding for affordable housing throughout the county.

The Housing Trust Fund Initiative thanks you for your consideration of the commercial linkage fee and requests your support.

Sincerely,

Marti Buxton, Director
Contra Costa Housing Trust Fund Initiative

CC: Laura Simpson, Senior Housing Specialist

The Contra Costa Town Hall Coalition

P.O. Box 273808
Concord, CA 94527-3808

Voice (925) 935-2958
Fax (925) 280-4511

January 4, 2005

Mayor Pro Tem Kathy Hicks, Mayor Gary Skrel, Councilwoman Gwen Regalia, Councilman, Councilman Charlie Abram and Councilwoman Susan McNulty Rainey
City Hall
1666 No. Main Street
Walnut Creek, Ca. 94596

Dear Mayor and City Council:

The Contra Costa Town Hall Coalition is a group of bi-partisan citizens located throughout the county, including Walnut Creek, that want to help direct public policy in a fiscally responsible and family friendly way. We are not sponsored by any industry or lobbying group, nor do we have any ideological axe to grind. We are public-spirited citizens that simply care about our community.

We are writing today to express our dismay over a legislative proposal to charge commercial developers a fee of some five dollars per square foot for the purposes of contributing to affordable housing. This proposal, largely taken from San Francisco, which has had such a fee in place for over a decade, has been a failure there.

Many businesses have moved to more business friendly environments in the East Bay. Walnut Creek in particular has been a beneficiary of such business-unfriendly policies in San Francisco. In makes no sense to start importing failed urban policies from a city whose policies are notoriously hostile to business and whose housing policy has left that city in total disarray.

The idea that commercial developers are responsible for the need of affordable housing is flawed from the outset. Developers of commercial centers are a net tax gain to local communities. They do not create "need" for housing that cannot be largely absorbed locally.

New commercial construction benefits cities by contributing millions of dollars annually.

They do this first and foremost by adding to the real property tax base. When a vacant lot is turned in a commercial strip center of let's say, 50,000 square feet that center will have an assessed value of approximately $15,000,000.

The property value has gone up 30-50 fold as compared to the vacant lot. This increase in value will in turn increase real property tax revenue by that identical astronomical factor due to Proposition 13. Real taxes are assessed at 1.25% of the property value.

Additionally, in our hypothetical fifty thousand foot center, it is estimated that some 200 new permanent jobs will be created (4-6 employees per 1,000 square feet of commercial development). Moreover, this will not only directly benefit the local residents who will be hired on as employees, it will also benefit the city in new and expanded: payroll taxes, new property taxes, new sales taxes from sales of merchandise. Moreover, there will be still new revenue from the sales then created by the new employees who will then shop elsewhere in Walnut Creek.

The actual tax benefits from our 50,000 square foot center could easily be a million dollars annually. *These are net benefits.*

Commercial centers are not public service consumers. They don't use social services, they don't use our parks, and they don't use our court system, our hospitals or our schools. Commercial development is clearly a net tax revenue asset for the City of Walnut Creek. Commercial projects are already hiring our youth as store clerks and warehouseman and give many other jobs to seniors as accountants and managers.

Additionally, local jobs created by commercial development will help literally clear the air by minimizing traffic commutes. If anything, this activity should be encouraged by the city by offering developers tax incentives, not tax deterrents.

Why should the city now vote to penalize those very entrepreneurial developers who bring so many myriad benefits to the city? Is it just because San Francisco already does so? Or is just because developers are simply easy prey and this makes it politically tempting? Why on earth would the city want to penalize the commercial developers? They're not causing or creating the problem. They're solving it. They are already paying for far more than their fair share in revenues than they consume.

Affordable housing is indeed a fine public purpose, but we shouldn't extort businesses that create local jobs and more revenue for the city. Why doesn't the city merely earmark a percentage of the expected increased tax revenues from the commercial project for affordable housing without charging the developer an additional premium?

San Francisco's business climate is decaying and its housing programs are a failure. San Francisco is no model for Walnut Creek. Thank you.

Sincerely,

Adam Sparks
Chairman

Cc: Downtown Business Association, Chamber of Commerce, Building Industry Association, Contra Costa Times

Cevina Targum
1011 Ygnacio Valley Rd Apt 9
Walnut Creek CA 94598-1850

cc: Council
Mike
Laura

Feb. 4, 2005

Mayor + City Council:

I am writing to ask you to support the Ordinance imposing a linkage fee ($5.00) on new commercial development - to help build affordable housing units. This is not a new idea - other cities have done this and your own Planning Commission and City staff have endorsed this. There are many solid, middle-class people who support schools + the arts + public improvements, who support various retail stores etc. who are now on a fixed income which is not enough to cover housing costs. These people are always the backbone of any community. They have

supported Walnut Creek for many years and deserve to be helped now. We need to keep them in our community not only for stability - but to encourage a variety of people to live here. Cities thrive on variety - and we are no exception. We need the old & young... those of moderate means & those of affluence. We need people who care about our City - and in order to keep a valuable segment of our community here - we need to do as other cities have done - provide affordable housing.

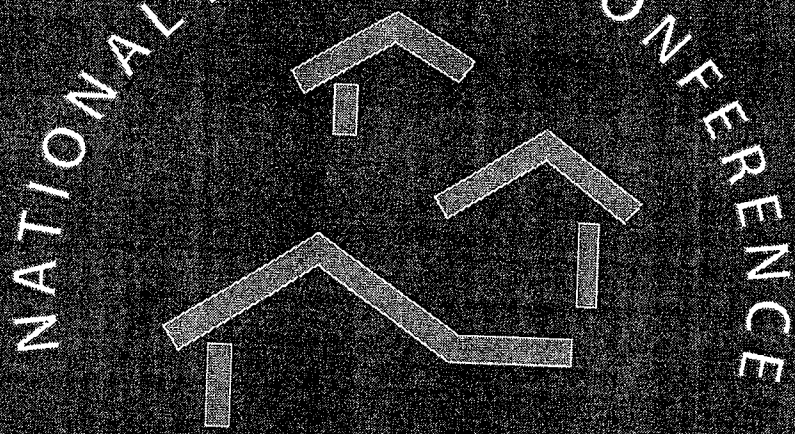
Sincerely

Corine Jorgensen
Resident. Thirty-Three Years

NHC Affordable Housing Policy Review

VOLUME 3 • ISSUE 1 NATIONAL HOUSING CONFERENCE FEBRUARY 2004

Inclusionary Zoning: The California Experience



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NHC Affordable Housing Policy Review

NHC Affordable Housing Policy Review seeks to offer a balanced nonpartisan view of complex housing policy issues. This publication encourages discussion and commentary from all who choose to engage in a responsible dialogue on the housing needs of this nation. Published on an occasional basis, *NHC Affordable Housing Policy Review* provides insight into NHC's positions on key housing concerns and also includes other housing industry policy perspectives.

With respect to this publication, the National Housing Conference makes no claim that the recommendations it contains represent a complete list of possible policy proposals. The articles in this publication represent the point of view of the individual contributors and the positions expressed are the authors' own.

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VOLUME 3 • ISSUE 1 NATIONAL HOUSING CONFERENCE FEBRUARY 2004

Inclusionary Zoning: The California Experience

The United Voice for Housing

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NHC Affordable Housing Policy Review is published by the National Housing Conference (NHC), a nonprofit 501(c)(3) membership association dedicated to advancing affordable housing and community development causes. A membership drawn from every industry segment forms the foundation for NHC's broad, nonpartisan advocacy for national policies and legislation that promote suitable housing in a safe, decent environment. NHC members consist of nationally known experts in affordable housing and housing finance, including state and local officials, community development specialists, builders, bankers, investors, syndicators, insurers, owners, residents, labor leaders, lawyers, accountants, architects and planners, and religious leaders. **NHC is the United Voice for Housing.**

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The California Affordable Housing Law Project of the Public Interest Law Project is a nonprofit California corporation that provides statewide support, including litigation, policy advocacy, consultation and training for local legal services and other public interest law programs. Our areas of expertise include housing, public benefits, health and civil rights. Our housing attorneys specialize in land use and planning, state housing element and redevelopment laws, and preservation of affordable housing units.

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The California Coalition for Rural Housing (CCRH) is a statewide network of nonprofit housing developers, legal service providers and public housing agencies that support the production of decent, safe and low-cost housing for rural and low-income Californians. CCRH advocates at all levels of government and provides technical assistance to community groups and nonprofits on housing issues.

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The Non-Profit Housing Association of Northern California (NPH) works to advance affordable housing as the foundation for thriving individuals, families and neighborhoods. As the collective voice of those who finance, build, operate and support affordable housing, NPH promotes the proven methods offered by the nonprofit housing sector and focuses government policy on housing solutions.

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David Rosen founded David Paul Rosen & Associates (DRA) in 1980. DRA is a national real estate economic and public policy consulting firm based in Oakland, California. DRA is a leading firm in developing and assessing inclusionary housing programs nationwide.

Inclusionary Zoning: The California Experience

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Inclusionary Zoning: The California Experience

Introduction

By Nico Calavita

The impetus for the publication of this review was provided by the recently released report, *Inclusionary Housing in California: 30 Years of Innovation*, authored by the California Coalition for Rural Housing and the Non-Profit Housing Association of Northern California. This report confirms what many observers had suspected all along, that during the recent past the number of inclusionary housing programs in California has proliferated. No data had been collected since 1996. At that time, there were 75 inclusionary housing programs in California (Calavita and Grimes 1998). According to this new survey, as of March 2003, there were 107 cities and counties using inclusionary housing in California, one-fifth of all localities in the state. The City of San Diego adopted inclusionary housing in the summer of 2003, the largest city in the country with inclusionary housing, too late to be counted. At least a dozen more cities are considering inclusionary housing, including Los Angeles. Clearly, inclusionary housing has emerged as a powerful tool to expand the supply of affordable housing in California. At a time when public sector subsidies for affordable housing are even more limited in a context of skyrocketing housing costs, a market-based approach such as inclusionary housing is all the more appealing.

With inclusionary housing, construction of low- and moderate-income housing is linked to construction of housing in the marketplace, by mandating developers to provide the affordable units in an otherwise market-driven development. In doing so, inclusionary housing not only generates units affordable to low- and moderate-income families, but also provides opportunities for racial and economic integration. With inclusionary housing, affordable housing units are built concurrently with market-rate housing, sidestepping community opposition to the siting of low-income housing within their boundaries.

Inclusionary housing programs originated in the Washington, D.C metropolitan area in the early 1970s when Fairfax County, Virginia and Montgomery County, Maryland adopted inclusionary housing. Fairfax County's ordinance was invalidated by the Virginia Supreme Court, but the County subsequently modified the ordinance, which has been in successful operation for almost 15 years. In contrast, Montgomery County's Moderately Priced Dwelling Unit program has been hugely successful, producing more affordable units than any other single local government in the country.

The program that has generated the most visibility and controversy at the state level is the court-mandated inclusionary housing program in New Jersey. With the landmark 1983 Mount Laurel II decision, requiring local governments to use "affirmative governmental devices...including...mandatory set-asides," the New Jersey Supreme Court forced recalcitrant localities to address economic and racial integration through fair-share housing plans. In that context, inclusionary housing has become the central component of almost all regional fair-share plans in New Jersey.

In Massachusetts, the 1975 Zoning Act, popularly known as the "anti-snob zoning" law, allows developers to sidestep zoning and other regulations when proposing affordable projects in communities that have failed to produce their "fair share" of such housing. This provision has helped provide affordable housing, but not as much as "true inclusionary housing" could provide (Ziegler 2002).

Outside the New Jersey Supreme Court-inspired inclusionary housing then, California appears to be the leading state in fostering inclusionary housing programs that are locally and voluntarily adopted. As such, the California experience needs to become an integral part of the current debate on inclusionary housing. The housing crisis, especially acute in certain parts of the country, and declining government resources fostered by huge budget deficits at the state and federal levels, make inclusionary housing an increasingly appealing mechanism to produce affordable housing in other jurisdictions as well. The California experience can significantly contribute to that debate and provide invaluable lessons for states and localities contemplating inclusionary housing. In addition to the aforementioned report, another recent California publication that has addressed inclusionary housing in California is the *California Inclusionary Housing Reader*, published also in 2003 by the Institute for Local Government, the research arm of the League of California Cities. The goal of the *Reader* was to "help community leaders evaluate whether inclusionary housing ordinances are for their community" (page iv). The *Reader* does not advocate inclusionary housing, but it certainly legitimizes it in the eyes of local jurisdictions, and goes as far as providing a sample inclusionary housing ordinance. Inclusionary housing has definitely arrived in the Golden State.

With this publication, the 30-year experience of inclusionary housing in California is brought to the attention of a national audience through the sponsorship of the National Housing Conference. It attempts to provide a concise, comprehensive, up-to-date, state of the art account of inclusionary housing in California. It is organized as follows: First, the origins and evolution of inclusionary housing are presented, together with a discussion of the controversy surrounding inclusionary housing, especially the issue of who pays for its costs. Second, the findings of the 2003 survey are presented, followed by a brief analysis of the constitutionality of inclusionary housing. The report concludes with an analysis of the market implications of inclusionary housing.

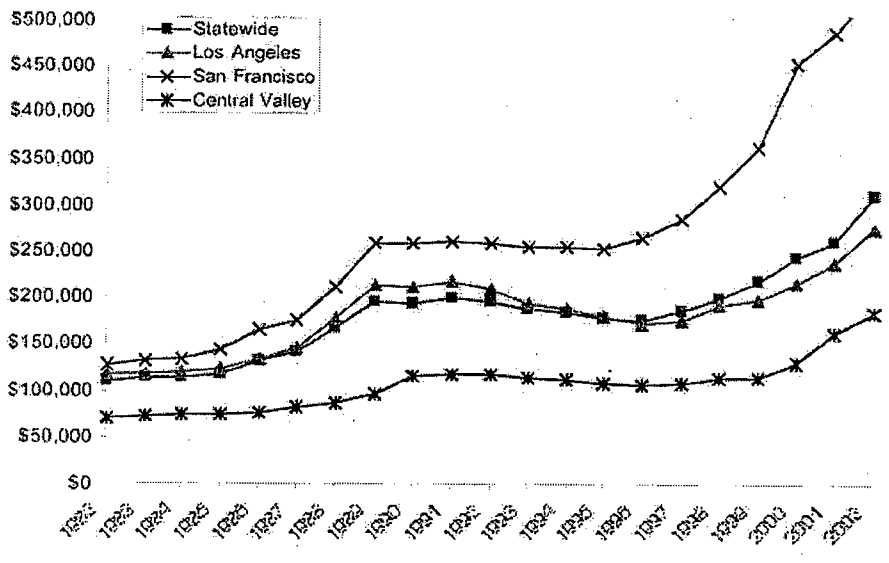
Origins and Evolution of Inclusionary Housing in California

By Nico Calavita

Origins

The primary reason behind the spread of inclusionary housing programs in California is high housing costs. The upward spiral in housing prices began after the recession of the early 1970s and has continued, almost unabated, ever since. The highest increases have occurred during the last five years, a time when inclusionary housing programs have proliferated. Since 1982, housing prices in the San Francisco Bay Area have risen more steeply than in other parts of the state, generating the largest number of inclusionary housing programs (see Figure 1).

Figure 1: Median house price in California, 1982-2002, in 2000$



Sources: CA Department of Finance, California Association of Realtors.

Several factors have been cited as contributing to the rapid increases in housing costs in California.

- Heavy in-migration during the 1970s and 1980s, and the inability of the housing industry to keep up with demand (Levy 1991). While not fueled by in-migration as in the past, California will continue to grow rapidly adding more than a half-million additional people to its population every year for the next 20 years.

- NIMBYism. Successful opposition on the part of residents to new residential development-especially higher density-both at the periphery and in urbanized communities, limits housing construction (Fulton 1999, Myers and Park 2002).

- Declines in investment in public infrastructure at the state and local levels reduces the availability of developable land. One result is unusually high development impact fees. While the full amount is not necessarily passed on to consumers-fees tend to reduce land prices (Nelson and Moody 2003)-high fees usually result in higher housing costs. The main cause of the infrastructure deficit at the local level is Proposition 13, passed in 1978, that limited property tax revenues.

- Proposition 13 has another significant deleterious effect on the housing market. Fiscally impoverished cities engage in "fiscal zoning" that encourages commercial land uses that generate sales taxes while discouraging housing perceived as a fiscal drain because of the need for services that it generates.

- Many existing metropolitan regions such as Los Angeles and San Diego were developed on coastal plains and mesas. The remaining land is highly constrained from an environmental standpoint, especially in terms of slopes and biology. Natural habitat preserve systems developed under the statewide Natural Communities Conservation Planning Program (NCCP) preempt large tracts of land from development. In southern San Diego County, for example, the Multispecies Conservation Program (MSCP), the first program approved under the NCCP in 1991, preserves 172,000 acres of land.

In California then, market pressures, residents' opposition to housing, fiscal zoning, and regulatory exigencies have reinforced one another to drive up the cost of housing. In August 2003, the median price of a single family home broke through the $400,000 barrier reaching a record monthly high of $404,870.

Policy Making Environment

California General Plan Law requires that all localities adopt a General Plan and that the "Housing Element" be certified by the Department of Housing and Community Development (HCD), the only General Plan element that requires state approval. The Housing Element is a five-year plan that makes adequate provision for the housing needs of "all segments of the community" and identifies potential housing sites "for all income levels" (Section 65583 of Government Code).

The problem is that, while incentives exist to have Housing Elements certified by the state-such as accessibility to state funds or avoidance of litigation-a certified element does not guarantee that affordable housing will be built. In 2003, a Housing Element Working Group was established with the assignment of producing a comprehensive package to reform Housing Element Law. All legislators who had introduced Housing Element related bills have agreed to put on hold their efforts until this working group completes its task. This effort represents the most promising attempt to date to reform Housing Element Law to make it more effective and fair.

In the absence of a clear state mandate, an overriding government structure defining inclusionary housing programs, strong fiscal incentives and compelling court decisions as in New Jersey, inclusionary housing programs in California are adopted locally and subject to the vagaries of changing state and local political and economic circumstances.

Evolution

During the late 1960s and 1970s, the desirability of growth was increasingly questioned, prompting the passage of growth limitation measures on the part of localities adversely impacted by growth problems (Reilly 1973). In California, several bedroom communities clustered in the San Francisco Bay Area passed growth control measures that limited the annual number of residential building permits. To ward off possible legal challenges to their programs, cities like Petaluma and Davis passed de facto inclusionary housing programs, by favoring developers that would include affordable units in their projects.

During the 1970s, the City of Irvine and Orange County passed inclusionary housing programs in response to a severe imbalance between jobs and housing, and subsequent legal challenges. These lawsuits sought to stop additional rezonings to job-producing land uses and to produce more affordable housing units. In both jurisdictions, the major landowner, the Irvine Company, was able to influence the process that led to the enactment of inclusionary housing programs that were extremely flexible and dependent on cost offsets. These included density bonuses, reduced parking standards and the availability of government low-cost financing such as Community Development Block Grants and Section 8 new construction assistance. While producing a large number of units, the two programs did not enforce resale or long-term affordability controls leading to the loss of the inclusionary housing units, a sobering lesson for future inclusionary housing programs.

In 1980, during the Democratic administration of Jerry Brown, the Housing Element was strengthened by mandating that the determination of local housing needs be based on the locality's share of the regional housing need. This language was interpreted by HCD as an obligation "to zone affirmatively for regional housing needs" (Burton 1981). HCD prepared a "Model Inclusionary Housing Ordinance" that was presented to local jurisdictions as an essential mechanism to bring their Housing Element in compliance with state law (Mallach 1984). About 30 inclusionary housing programs were adopted during the late 1970s and early 1980s, some of them outside the San Francisco Bay Area and Orange County. Inclusionary housing programs proliferated so rapidly in California at the beginning of the 1980s that an observer noted that "New Jersey adopted inclusionary housing but California implemented it" (Burton 1981).

In 1983, with the advent of the administration of Republicañ Governor George Deukmejian, HCD lessened its advocacy of inclusionary housing programs, reducing the ability of local policy makers and housing advocates to use state law as leverage to foster inclusionary housing programs.

During the early and mid 1990s, HCD's hands-off stance toward inclusionary housing turned into outright hostility. Overregulation became the culprit for the deep recession of that period and for high housing costs. Thus, inclusionary housing became "a constraint

or an exaction on new development" (Coyle 1991) and local governments were discouraged from adopting inclusionary housing. At minimum, a jurisdiction was to measure the potentially deleterious impact of inclusionary housing on housing development. Letters to jurisdictions considering inclusionary housing included the following: "While we cannot endorse this approach to facilitate lower income housing production, if the City has implemented a program that acts as a governmental constraint, the City must analyze the effect that the action has on housing development" (Badenhaausen 1995).

Cities considering inclusionary housing at this time decided to create programs that would provide cost offsets to developers, including financial assistance and regulatory relief. Regulatory relief may include density increases, impact fee waivers or deferral, fast-track permit approval, reduced parking requirements, relaxed design restrictions (such as reduced street widths or setbacks) or other regulatory concessions. Cost offsets, however, did not weaken developers' resolve to oppose inclusionary housing. In San Diego, for example, the value of the offsets was determined by an inclusionary housing task force and housing affordability requirements were based on the value of the offsets. Even though the industry representative agreed to such a conciliatory approach, the building industry repudiated it and fired its representative, effectively killing the proposal (Calavita and Grimes 1998).

During the early and mid 1990s, 30 new programs were passed, with all of them including either regulatory relief or financial incentives and 18 of them providing both. In 1996, there were 75 inclusionary housing programs in California (Calavita and Grimes 1998).

Beginning in 1996, a boom period for the California economy generated many jobs and not enough housing. It is generally accepted that a healthy balance between jobs and housing mandates one new residential unit for every 1.5 jobs created. But during the late 1990s, the number of jobs created vastly outnumbered housing construction. In San Francisco, the ratio was 6.5 new jobs to one new home; in Los Angeles six to one; in San Diego and Orange Counties, 4.5 to one; in Santa Clara and San Mateo Counties, 10 to one. Even worse, housing construction lagged behind the levels of the 1980s. During the 1990s, one housing unit was built for every 3.72 additional residents; during the 1980s, it was one housing unit for every additional 2.95 additional residents (Meyers and Park 2002). The result was skyrocketing housing prices and many more inclusionary housing programs approved in the state. In 1999, HCD softened its stance toward inclusionary housing, evaluating inclusionary housing programs in the context within which they were adopted and discouraging programs with standards so strict and inflexible that would actually discourage housing production.

In 2001, the case of *Home Builders Ass'n v. City of Napa 90 Cal.App.4th 188* was decided. As the contribution to this publication by Deborah Collins and Michael Rawson outlines, the Napa case established that inclusionary housing is a constitutionally valid extension of a jurisdiction's zoning powers. This case is especially important because in California there are no laws that expressly authorize, require or otherwise place limits on the adoption of inclusionary housing outside of redevelopment areas and areas impacted by the Coastal Act. As such, the Napa case represents a watershed moment in the legal history of inclusionary zoning.

Developer Opposition, the Incidence Controversy and Cost Offsets

Not surprisingly, developers typically oppose inclusionary housing. They oppose it on ideological grounds, viewing it as an additional government intrusion in their affairs at a time when they feel besieged by government regulations and, especially in California, very high development impact fees. They steadfastly point out the seeming unfairness of inclusionary housing by maintaining that the costs they incur in building affordable housing units is passed down to homebuyers or renters of market-rate units, thus decreasing their ability to afford market-rate housing. Such a position, however, is highly controversial.

Economists point out that there are three parties who may bear the costs of regulations that increase the cost of development such as inclusionary housing, development impact fees and other forms of "exactions" that help mitigate the costs that development generates. Besides market-rate renters and homebuyers, developers and the seller of raw land to the developer can, under various circumstances, absorb all or part of the cost of exactions.

If the demand for housing is elastic, i.e. sensitive to changes in price, then developers will be unable to pass down the cost increases to homebuyers or renters and will have to reduce their profits. If developers do not own the land at the time of enactment of an inclusionary housing program or development impact fees, then they may bargain with landowners for a lower price.

These arguments have remained largely theoretical, but research on "incidence" (i.e., who pays the cost of exactions) is starting to emerge. In his analysis of impact fees, Yinger (1998) found that such fees led to a drop in the cost of land. Empirical work by Ihlanfeld and Shaughnessy (2002) found that development impact fees reduced land prices by the amount of the fee paid, but also raised housing prices by half of that amount. This increase is open to interpretation and may be related to the benefits of the public facilities provided (Nelson and Moody 2003). Given the fact that inclusionary housing does not provide benefits for the homebuyers, this finding may suggest that inclusionary housing costs are passed backwards to the landowner only, but additional evidence is necessary. For now, it would be safe to concur with Watkins (1999) who "surmises that the impact fee will always be split between all the players in the development process" (Nelson and Moody 2003:6), with the respective share depending on the elasticity of the market.

To reduce the potential impacts of inclusionary housing on developers, land sellers or homebuyers, options that would reduce the cost of development such as cost offsets, incentives or alternative compliance can be provided. The contribution by David Rosen at the end of this publication, employed a land residual analysis to show that cost offsets can, under most market circumstances, make inclusionary housing feasible without affecting land costs or developers' profits. More generally, Rosen's piece demonstrates one way for local governments to assess the relative impact of inclusionary housing on development costs. Since the analysis is static relative to land prices, there is an argument to be made that absent incentives, the key input of land costs could decline within a city with a broad inclusionary housing policy.

Similarly, Hagman (1982) has argued that incentives and cost offsets keep land costs high. With land costs being the principal cause of skyrocketing housing prices in California, "the argument against inclusionary housing would probably lose much of its power if it became widely known that, in the long run, landowners and not homebuyers

bear the cost of inclusionary housing (Calavita and Grimes, 1998: 152). This issue awaits further research.

What follows is an excerpt from the report *Inclusionary Housing in California: 30 Years of Innovation*, authored by the California Coalition for Rural Housing and the Non-Profit Housing Association of Northern California. The report lays out the findings of a survey conducted by the two organizations in late 2002 and early 2003 to reassess the use of inclusionary housing practices across California. As of March 2003, one-fifth of all localities in California (107 cities and counties) reported using such practices. This represents nearly a 67 percent increase since 1994, when researchers first identified 64 inclusionary policies or ordinances. In addition to providing a snapshot of local inclusionary practices across the state, the article addresses key questions about how successful local policies implement inclusionary housing.

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Inclusionary Housing in California: 30 Years of Innovation*

By the California Coalition for Rural Housing and the Non-Profit Housing Association of Northern California

Introduction

Over the last three decades, as the housing crisis in California has intensified and spread throughout the state, more and more communities have turned to inclusionary housing practices to create affordable housing for their residents and workers. It is an emergent trend in other states as well. As of March 2003, one-fifth of all localities in California (107 cities and counties) reported using such practices. This represents nearly a 67 percent increase since 1994, when researchers first identified 64 inclusionary policies or ordinances. At least a dozen other jurisdictions are in the process of adopting or considering adopting inclusionary housing.

Generally, inclusionary housing practices require or encourage developers to ensure that a certain percentage of a new residential housing project will be priced affordably. While not a substitute for a broader affordable housing strategy, inclusionary housing practices are generally thought to address economic and racial segregation by creating more economically diverse communities, particularly in suburban jurisdictions. By providing housing options for lower wage workers in high-cost communities, inclusionary housing can also help reduce commutes and address local mismatches between available jobs and housing supply.

In the absence of a statewide approach to inclusionary housing, each jurisdiction in California is free to choose whether or not inclusionary practices are needed or would be effective in that local context. This freedom has spawned virtually endless variation in program design, as each jurisdiction molds inclusionary housing practices to match its local needs and political reality. Although the term "inclusionary zoning" is sometimes used interchangeably with inclusionary housing, in fact, not all inclusionary practices are zoning overlays.

Given the pressing need for solutions, the diversity of inclusionary practice in California, and the increasing importance of inclusionary housing, the California Coalition for Rural Housing (CCRH) and the Non-Profit Housing Association of Northern California (NPH) conducted a survey to determine how local inclusionary housing programs are structured, as well as their relative effectiveness. The resulting report was intended to inform policy makers and the public about the central policy decisions in creating an effective inclusionary housing program. This understanding is crucial because inclusionary housing has the potential to create at least 15,000 units of affordable housing in California annually, nearly doubling the current rate of affordable housing production, according to the authors' calculations. To date, inclusionary housing has created over 34,000 affordable homes and apartments in the state.

*This article is an excerpt from *Inclusionary Housing in California: 30 Years of Innovation* by the California Coalition for Rural Housing (CCRH) and Non-Profit Housing Association of Northern California (NPH). Additional information about the report is available online at www.calruralhousing.org and www.nonprofithousing.org.

Beyond the debate on the general fairness or advisability of inclusionary housing lies a set of practical questions and concerns for policymakers and advocates. What makes a program effective? What are appropriate goals for a policy or ordinance? What are the key variables or features in balancing developer concerns and community needs? In essence, what works?

In designing effective inclusionary programs, the most significant policy points are:

1. Size of the inclusionary percentage;
2. Income targeting of the housing;
3. Alternatives to construction on-site;
4. Developer incentives; and
5. Length of affordability.

The report addresses all of these key features, as well as presents examples and case studies to supplement the statistical profiles. While not offering a model ordinance or policy, the statistical profile and individual case studies provide powerful guidance to policymakers and advocates that can inform local planning and decisionmaking.

Central to all these decisions are a few key considerations. First, the political realties of adopting a policy or ordinance often pit for profit developers against "social-equity" advocates, with developers pushing for maximum flexibility and advocates striving for certainty. The extent to which developers actually have to produce the units or take actions to ensure production of an equivalent number of units depends largely on the flexibility of the program.

While alternatives may be crucial to ensure financial feasibility and political acceptability, too much flexibility can negate any positive policy impact. If in-lieu fees or land dedication requirements are set too low, developers will consistently opt out of construction. Allowing off-site construction and design differences threaten some of the potential benefits of inclusionary programs, such as simultaneous development of market- and below market-rate units, functional and aesthetic integration of affordable units into new neighborhoods, and minimization of neighborhood opposition. However, if builders cannot or will not build, then an inclusionary program is rendered virtually meaningless. Accordingly, program design and revision must consider both the benefits and potential limitations of each policy detail.

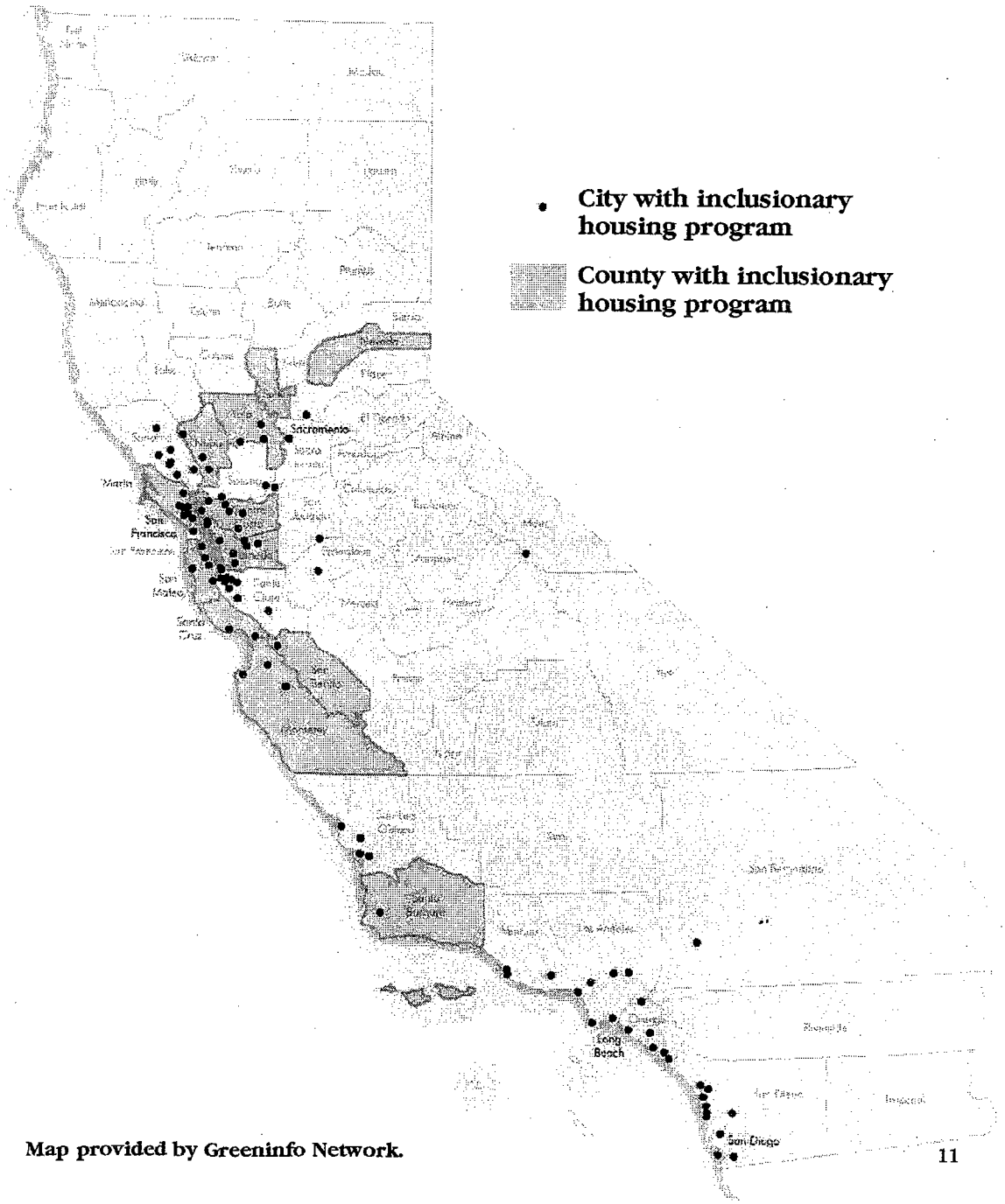
SMART GROWTH AND INCLUSIONARY HOUSING

Inclusionary housing practices relate to efforts to curtail sprawl and create "smart growth." State law requires all jurisdictions to provide density bonuses as a means of incenting affordable housing. Such bonuses also encourage higher density construction, a key outcome for reducing sprawl and encouraging transit. Unfortunately, in practice, development standards such as high rear and front yard setbacks and parking requirements can undermine a developer's ability to use the density bonus effectively.

The relationship to sprawl and growth is even more confusing in jurisdictions with "permit-metering." In these instances, local policies or ordinances attempt to slow growth by imposing caps on the number of residential permits that be issued each year. This often creates a highly competitive permit application process in which affordable housing inclusion can become a bargaining tool, such as in Livermore or Morgan Hill. While the overall constraint on housing supply is problematic for affordable housing, the policies often attempt to mitigate the impacts by increasing the number of affordable units that are produced under these circumstances.

Research Methodology

CCRH and NPH initiated the 2002/03 survey to reassess the use of inclusionary housing practices across California. The survey questionnaire used in CCRH's 1994 study was modified, updated and expanded to include detail on housing production and other program features. Local advocates, planning officials and academics were consulted in these revisions and a final questionnaire was distributed by mail in early April 2002. All planning agencies listed in the California Planners' Information Network were contacted, including 58 counties and 467 cities (San Francisco is counted as both a city and county).



Map provided by Greeninfo Network.

To increase the response rate, two rounds of follow-up surveys were conducted. In June 2002, the questionnaire was again mailed and telephone contact was made with nonresponding jurisdictions reported to have local programs. In January 2003, a short follow-up survey was prepared and forwarded to responding jurisdictions seeking additional information on methodology for determination of in-lieu fees, total fees collected, income targeting goals and production numbers. In total, 98 jurisdictions returned completed questionnaires accounting for 92 percent of known programs in California. Based on previous studies and Internet searches of jurisdiction Web sites, another nine jurisdictions that did not return completed questionnaires are judged to have some form of inclusionary housing.[1]

Findings

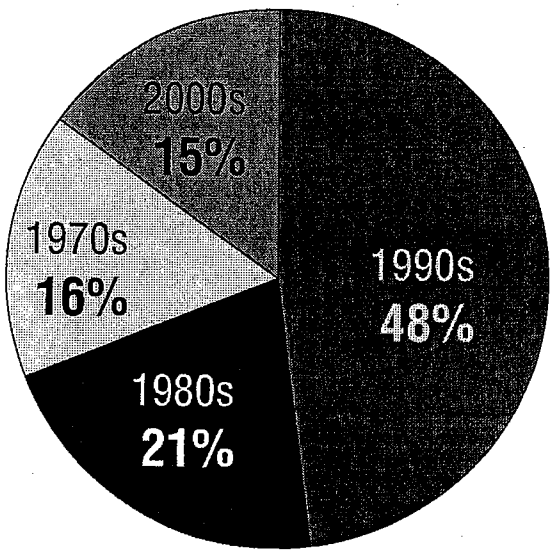
A. Number of Inclusionary Jurisdictions

As of March 2003, 107 California jurisdictions are known to use local inclusionary practices to provide affordable housing outside of the requirements of State redevelopment law. These include cities and counties that require affordable construction through an ordinance, general plan or permit approval process.[2] This list consists of 12 counties (21 percent of all counties) and 95 cities (20 percent of all cities).

The spread of inclusionary programs is most dramatic among cities, which represent 41 of the 43 new programs. As the map (see p. 11) clearly demonstrates, inclusionary housing is most prevalent in high-cost housing markets in the coastal counties. The most significant clusters are in the San Francisco Bay Area, metropolitan Sacramento, and San Diego County. At least two dozen other California jurisdictions are presently considering adopting inclusionary housing, including the largest city, Los Angeles.

Figure 1 shows the increasing popularity of inclusionary housing in the 1990s. Nearly half (48 percent) of all programs were adopted during that decade compared to about one-third (37 percent) in the 1970s and 1980s. The trend is continuing in the 2000s.

Figure 1: Year of Adoption



B. Measuring Effects on Affordable Housing Production

Although this report is primarily focused on providing a profile of inclusionary policies and ordinances, the survey also sought to gather data on affordable housing produced as a result of inclusionary housing practices. About one-third of known inclusionary jurisdictions reported production numbers accounting for over 34,000 units of affordable housing. In addition, 80 percent of all respondents believe that their inclusionary program has stimulated the production of affordable housing that would not have been built otherwise. For those jurisdictions that did not find inclusionary practices helpful in creating affordable housing, they generally agree that the principal barriers have been market stagnation or infrastructure limitations.

C. Forms of Inclusionary Policy

Inclusionary policies take the form of either a local ordinance, a General Plan policy, or a permit approval process that requires or rewards affordable projects. Seventy-eight percent of inclusionary programs are defined by a formal ordinance and 49 percent are prescribed in General Plans.[3] In many cases, the two are linked; General Plan policies often charge or commit local government to adopt an ordinance.

Three jurisdictions (three percent of respondents) report no ordinance or General Plan policy, but have permit approval procedures that promote affordable production. These jurisdictions are Contra Costa County, Morgan Hill and Huntington Beach. Critics argue that this form of inclusionary practice is inadequate since it is not explicitly required at the individual development or project level. Instead, annual permitting targets are set or preferences established within a competitive permitting approval process. This leaves open the possibility that the more difficult-to-develop, affordable units will be delayed and approved at the end of the permitting period, thereby undercutting the notions of mixed-income housing and simultaneity of development. All three jurisdictions, however, report that the permit process regulations have provided affordable units that would not otherwise have been built.

While adoption of an inclusionary ordinance or General Plan policy is often needed to establish a clear program mandate, which of the two is more effective in terms of actual production is difficult to say. Certainly, the passage of a formal ordinance tends to impose inclusionary requirements in a more permanent and universal way (applicable to all developments of a certain size), with more formal procedures and specificity for implementation than does a General Plan policy. However, there was no statistical correlation between the relative effectiveness of an inclusionary housing program and whether the policy itself is codified in ordinance or identified in the jurisdiction's General Plan or both.

D. Voluntary or Mandatory

Only six percent of jurisdictions responding report voluntary programs, which allow more flexibility for developers but compromise local ability to guarantee affordable housing production. Los Alamitos and Long Beach both specifically blame the voluntary nature of their programs for stagnant production despite a market-rate boom. In general, our research indicates that the voluntary programs do not cause market-rate developers to build or facilitate affordable units unless including affordable housing makes an application more competitive in the permit approval process.

E. Inclusionary Requirement and Project Size

Variation from jurisdiction to jurisdiction in the percentage of units required to be affordable is significant, ranging from four to 35 percent. The average requirement in rental developments is 13 percent, which is also the average requirement for ownership housing. The most commonly found inclusionary percentage is 10 percent. However, approximately half of all jurisdictions require at least 15 percent and one-quarter require 20 percent or more.

In many cases, the inclusionary percentage is only applied to projects over a certain size, commonly ranging from three to 10 units. As Figures 2 and 3 indicate, there is relatively little difference between the percentage requirements for rental versus ownership. For example, the City of San Anselmo reports that no inclusionary units have been built because the inclusionary requirement is only required of projects over 10 units and all developments in recent years fell below this threshold. In 20 percent of jurisdictions, the inclusionary requirement is applied to all developments, regardless of size. Typically, smaller projects are allowed to meet the inclusionary goals differently than larger projects (in 42 percent of jurisdictions), more often than not through the payment of in-lieu fees. Still others require different percentages based on project or parcel size, as is the case in the City of Davis, where rental developments of over 20 homes must provide 35 percent of the homes as affordable versus 25 percent for rental projects under 20 units.[4]

Figure 2: Percent Rental Required

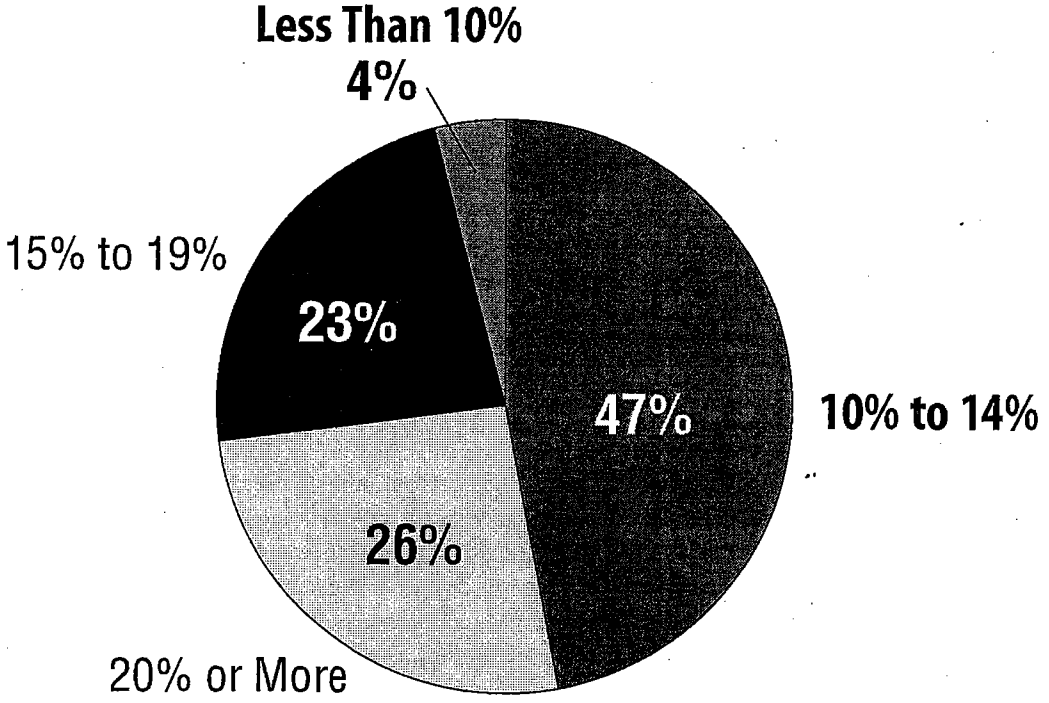
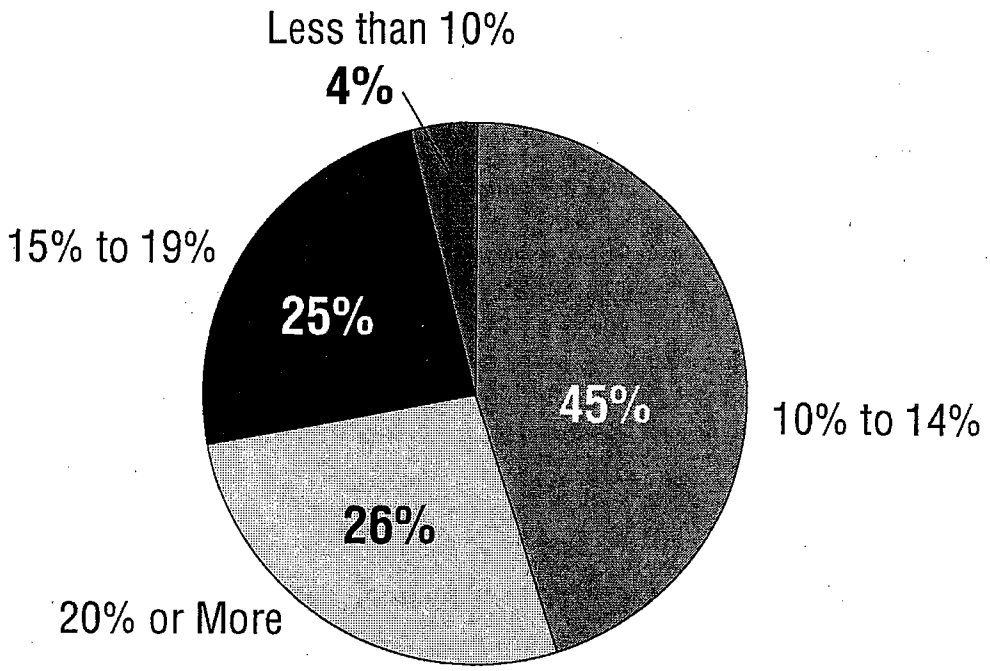


Figure 3: Percent Ownership Required



CASE STUDY

Morgan Hill

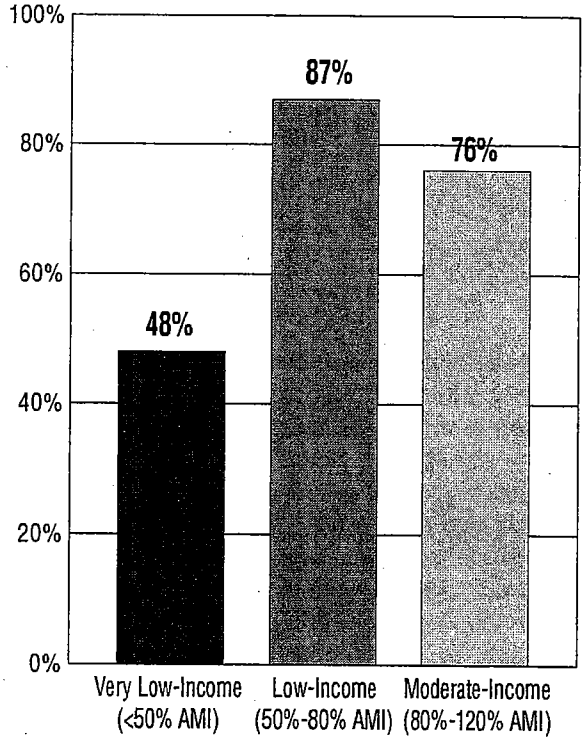
In general, jurisdictions with voluntary or incentive-only policies report that their policies did not produce the desired affordable housing. However, Morgan Hill in southern Santa Clara County is a notable exception. Morgan Hill accomplishes its inclusionary housing goals through its Residential Growth Management Policy, which limits the number of residential permits issued per year. The growth management policy is effectively a competition among potential projects. As part of the intense competition for permits, providing inclusionary affordable housing is worth as many as 13 points. In order to score high enough in the competition to get the permits for the overall development, builders must voluntarily choose from a set of inclusionary housing options. To date, the policy has created over 300 units of affordable housing.

F. Income Targeting

Most jurisdictions require that inclusionary homes be made affordable and offered to a predetermined income group, rather than providing developers with discretion or choices about whom to serve. Nonetheless, some jurisdictions do provide developers with options, such as providing a higher percentage of units to moderate-income households versus a lower percentage to very low-income households.[5] For example, the City of Richmond in the San Francisco Bay Area offers developers the option of providing 10 percent of the units to very low-income households, 15 percent of the units to low-income households, or 17 percent of the units to moderate-income households.

As demonstrated by Figure 4, most programs target some percentage of their inclusionary homes to low- and moderate-income households, 87 percent and 76 percent, respectively. Fewer than half of the programs (48 percent) target very low-income households. In 59 percent of jurisdictions, no distinction is made between income targeting for rental units versus units for ownership. Of the other 41 percent of cases, the income targeting is linked to form of tenure. In these instances, rental units are often targeted to low-income households and for-sale units to moderate-income households.

Figure 4: Income Targeting



Many inclusionary policies have been adopted in order to address the requirements of California Housing Element law. For example, Calavita and Grimes found that all eight of the San Diego County jurisdictions with inclusionary programs had adopted inclusionary housing in order to compensate for past under-production in particular income categories.[6] Because not all jurisdictions provided reliable data on the actual income limits of inclusionary units already produced, it is not possible to assess accurately who the actual beneficiaries of these policies are without more extensive and verifiable field research at the local community and project levels.

CALIFORNIA'S HOUSING ELEMENT LAW

In California, Housing Elements are state-mandated local plans for meeting housing needs, which are periodically required to be updated. The Housing Element is part of each locality's General Plan, its constitution for growth. Every Housing Element must show that the jurisdiction has adequate land zoned appropriately to accommodate its projected housing need for all income levels.

G. Alternatives to Construction On-Site

The most common alternatives to on-site construction are in-lieu fees and land dedications. In addition, developers are sometimes allowed to build the affordable housing off-site or receive credit for excess affordable units built in previous projects through credit transfers.

The flexibility with which policies and programs regulate developers varies greatly from jurisdiction to jurisdiction. The table below shows that the majority of jurisdictions allow in-lieu fees or off-site construction, 81 percent and 67 percent, respectively. Often, these two alternatives are offered within the same program; in 55 jurisdictions (54 percent), both strategies are allowed.

COMMON ALTERNATIVES TO ON-SITE CONSTRUCTION

In-Lieu Fees	Developer can pay a fee into a local fund instead of constructing the required affordable units. Often, fees are calculated per unit or per square foot for each unit not built.	Allowed by 81% of surveyed jurisdictions (N=102)
Land Dedications	Developer can substitute a gift of land that may accommodate an equivalent number of units in place of affordable unit construction.	Allowed by 43% of surveyed jurisdictions (N=93)
Credit Transfers	Developer can credit affordable units built beyond the inclusionary requirement in one project to satisfy the requirement in another.	Allowed by 20% of surveyed jurisdictions (N=93)
Off-Site Construction	Developer can build the affordable units at a different site than the market-rate units, sometimes conditioned on agreeing to increase the number of affordable units to be built.	Allowed by 67% of surveyed jurisdictions (N=96)

Interestingly, cities that allow the use of alternatives under specific conditions have been more successful than cities without those conditions. Monterey County's success is likely due to the use of: (1) restrictions on the use of the in-lieu fee option and (2) incentives for developers to construct more than the required number of affordable units (see Case Study, p. 20). In-lieu fees are only permitted under exceptional circumstances and are used specifically to buy land for affordable housing.

CASE STUDY
Carlsbad—The Benefits of Flexibility

A city of nearly 88,000 inhabitants in San Diego County, Carlsbad initiated its inclusionary program in 1993 during a period of fast residential growth. Impetus for the program came from a need to satisfy Housing Element requirements; before this time little affordable housing was produced. Despite effectively increasing the supply of affordable housing, the city still struggles to design adequate mechanisms to ensure continued affordability.

The ordinance requires 15 percent of all new residential development to be affordable to low-income residents, with an in-lieu fee option for projects of less than six units; larger developments are required to build. Land dedications are not regularly used, yet when the city joined a deal to finance a large affordable complex, some unassigned affordable units planned for construction were bought by small developers to satisfy their inclusionary requirements from other projects. Carlsbad's Housing and Redevelopment Agency, emphasizes the importance of (1) requiring construction instead of allowing in-lieu fees indiscriminately, (2) setting in-lieu fees high enough to encourage construction and fund development elsewhere and (3) mandating concurrent construction to reduce social resistance.

In-Lieu Fees

In-lieu fees are among the most controversial elements of inclusionary housing. While most jurisdictions offer in-lieu fees as a potential option, there is relatively little standardization in terms of calculating in-lieu fees or determining at whose discretion the in-lieu fee is an option. In-lieu fees can significantly affect levels of affordable construction, not only because they allow developers to pay instead of build, but also because the methods of calculation and uses of in-lieu fees can render them relatively ineffective. On the other hand, in-lieu fees can provide jurisdictions with the funds to subsidize affordable housing that serves people of even lower incomes or create supportive housing for people with special needs, such as mental health or substance abuse problems. In addition, in-lieu fees can be used in conjunction with other housing funds, such as the federal and state Low Income Housing Tax Credit or the State of California's Multi-Family Housing Program.

Jurisdictions vary greatly in terms of how they calculate in-lieu fees, often based on either construction costs or potential revenue. Typically, the dollar total of fees collected is not sufficient to produce the same number of units that would have been produced had developers opted to build the units themselves. For example, in fast-growing Patterson in San Joaquin County, the in-lieu fee per affordable unit required is a mere $7,340. Despite a 10 percent inclusionary requirement and growth of 750 units since the policy was enacted, the jurisdiction reports that its inclusionary program has created only five units of affordable housing since implementation. The County of Santa Cruz, on the other hand, has a $272,889 fee per affordable unit. A more typical case is Livermore in Alameda County, whose fee in 2002 was $122,720 per affordable unit-below what is actually needed to create the unit, but significantly increased from its previous level.

When in-lieu fees have been set below the level needed to actually fund new construction, they can undermine the program goals, as it is in the developer's clear financial interest to simply pay the fee. Therefore, a jurisdiction with a 20 percent inclusionary requirement but a low in-lieu fee might effectively create less affordable housing than a jurisdiction with a 10 percent requirement and fewer or less appealing alternatives to construction. To ensure that policies or ordinances produce results in keeping with their goals, the required fee should be high enough either to dissuade developers from opting out of construction or enable the city to finance construction of an equivalent number of affordable units elsewhere.

Some cities use in-lieu fees not for new construction, but for homeownership downpayment assistance or rental assistance programs, such as in the City of Coronado in southern California. While consumer subsidies are needed forms of housing assistance, they only indirectly affect production by increasing effective demand and do not ensure that supplies of affordable housing will increase.

In many cases, respondents credit a low in-lieu fee option with reducing the effectiveness of inclusionary mandates. According to the survey data, 80 percent of jurisdictions that reported numbers for affordable housing production allow in-lieu fees to be paid. Production numbers in these jurisdictions ranged from zero to levels commensurate with the outcomes anticipated by their policy goals. In other words, the in-lieu fee option may offer a way out for some developers who are not willing or able to construct affordable units themselves, but it does not necessarily impede affordable housing production in every case.

The freedom with which developers can choose fee payment also depends on policy design. In Davis, developers of smaller projects are allowed the in-lieu fee option only under circumstances of "unique hardship" as defined by the City Council. Many other jurisdictions allow the in-lieu fee option more freely, sometimes allowing developers to choose fee payment in all instances, or all developments below a certain size. In the case where an inclusionary formula obligates a developer to produce a fraction of an affordable unit, some jurisdictions require payment of in-lieu fees, instead of waiving the obligation entirely (see Case Study: Monterey County). Those jurisdictions that successfully produce affordable housing while using the in-lieu fee offer clues for effective policy design. The County of Monterey and Port Hueneme require that developers request permission to pay the in-lieu fee; projects are only allowed to use the in-lieu fee under certain circumstances defined on a case-by-case basis. This strategy avoids the overuse of the in-lieu fee alternative.

CASE STUDY

Making Every Unit Count in Monterey County — The Importance of In-Lieu Fees

In-lieu fees currently feed the engine driving Monterey County's inclusionary housing production. Since 1980, developers have constructed 448 units to directly satisfy inclusionary requirements, while 940 units have been created with assistance from in-lieu fees and other funds. In-lieu fees are an option for developers of small projects (seven units or less) and are based on the replacement cost of an affordable unit and the financing gap between affordable and market housing costs. For example, a project in the coastal zone of the County would pay an in-lieu fee of $339,636 per affordable unit required, which represents the difference between the average total development cost of $546,000 and the affordable sales price for a family of four at 100 percent of area median income, which is currently $206,364.

While other jurisdictions often waive requirements entirely in small projects, unincorporated Monterey County has greatly benefited from the in-lieu fees collected on each of these small projects, using funds for new construction and acquisition/rehabilitation projects. County planners note that, in the absence of an inclusionary policy, high land costs would prevent construction of affordable units. Monterey County requires permanent affordability for rental units, and imposes resale controls on homeowners who sell within 30 years. As of this writing, the County expects to amend its program by increasing inclusionary requirements to 20 percent (currently 15 percent), making the program mandatory for all developers, extending resale restrictions in perpetuity, eliminating the option for off-site construction, lowering the threshold for the in-lieu fee option to five units and crafting developer incentives.

Land Dedications

As noted above, 43 percent of jurisdictions responding allow land dedication instead of construction. This alternative faces similar challenges to in-lieu fees, in that the amount of land required to substitute for construction (similar to the amount of fees generated) must be large enough to ensure production of an equivalent number of units. Land dedications are most effective in areas where land is scarce and the cost is high; where the absence of land that is available for development and reasonably priced makes affordable housing development very difficult. In these environments, land dedications are most likely to yield significant resources for housing development.

A prerequisite for successful land dedication is that affordable units will be built on the dedicated land. Local governments must assume responsibility for this construction and often recruit nonprofit developers to complete the task. Typically, the land is deeded to the jurisdiction, which then deeds it to a community-based nonprofit on a competitive basis, or is deeded directly by the developer to a nonprofit organization. Edgewater Place in Larkspur in Marin County, for example, is a 50-unit development built by the Ecumenical Association for Housing on land dedicated by an adjacent condo developer. In this case, the land dedication allowed for double the number of units required under the policy by combining the land with funding from other sources.

Ensuring construction on dedicated land can be problematic. Portola Valley in the San Francisco Bay Area, for example, reports that the land dedication option may be revoked because the local government has been unable to advance development on four lots previously dedicated to it. Ideally, the land to be dedicated should be integrated into, or contiguous to, the proposed market-rate development. The construction of affordable units on isolated plots of land may undermine the economic and social integration that many inclusionary policies aim to create.

Ultimately, the success of land dedications depends on the quality of the land being dedicated: its size, shape and location; the existence of adequate sewer and water capacity and other infrastructure; environmental limitations; the capacity of local developers, especially nonprofit organizations, to undertake the development; the availability of financing to improve the land and build and operate the housing; and the level of public acceptance by the surrounding community.

Off-Site Construction

The allowance that affordable units may be built off-site also challenges the inclusive goals of inclusionary policy. Debate arises over whether programs should permit off-site development if that is the best way to maximize the number of affordable units that can be developed or, conversely, whether it is more important to insist on integrated development on-site even if such development yields fewer units.

As noted above, the location of affordable units on an isolated site restricts the extent to which new development can promote residential integration. In some cases, programs require that developers building off-site include more than the inclusionary allotment of affordable housing. This strategy attempts to justify the isolated construction by ensuring a greater number of affordable units, arguably the highest priority of inclusionary policy overall.

Off-site construction issues are particularly relevant when considering partnerships between for profit and nonprofit developers. In some cases, developers team up to satisfy

the inclusionary requirements; the for profit developer builds the market-rate units and the nonprofit builds the affordable units off-site on land it controls with funding support provided by the former. While this strategy allows each developer to exercise its expertise and appears to be a win-win proposition for all parties, the segregating effects should not be overlooked. In contrast to the land dedication option, however, where jurisdictions can be left with no means to develop the dedicated land, off-site construction requires the developer to be responsible for actual development.

CASE STUDY

Choosing Production Over Integration in Livermore

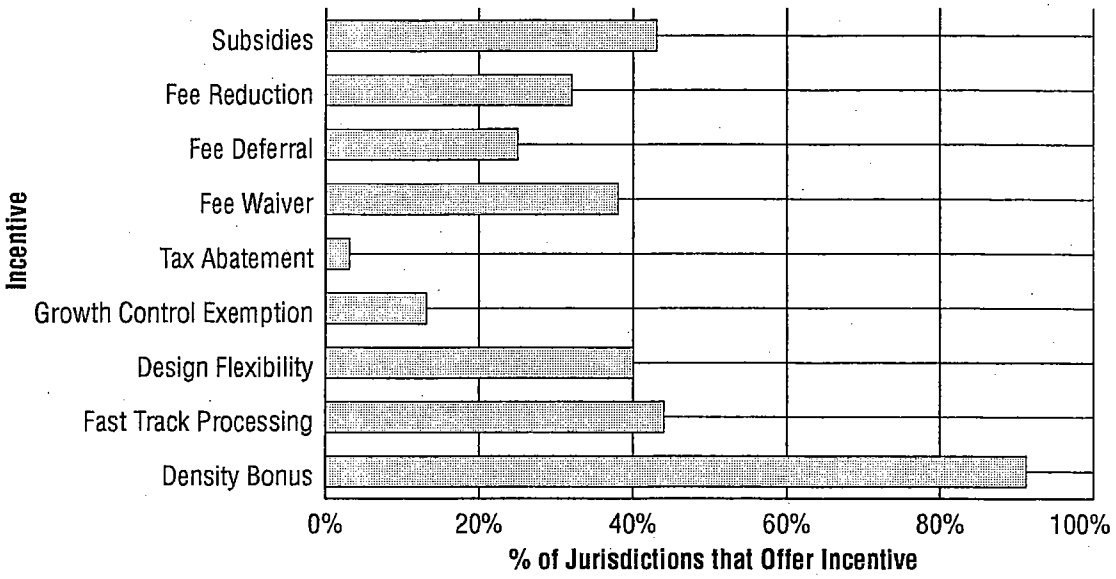
Livermore's inclusionary program is dedicated to boosting the affordable housing stock as the top priority, with secondary concern for integration. The program was first implemented in 1986 and has since become an integral part of the permit approval process. With a Residential Growth Management Policy as part of the General Plan, Livermore restricts residential development through a competitive permit selection process. Inclusionary requirements must be met as part of this review and project proposals that provide 35 to 50 percent affordable may bypass the selection process completely.

By discretion of the City Council, off-site construction, in-lieu fee payment or land dedications are considered and the City claims to be flexible wherever affordable construction can be maximized. Accordingly, Livermore reports that in-lieu fees have helped create some 600 affordable units. The City calculates the in-lieu fee as 10 percent of the difference between the cost of developing the market-rate unit and the maximum affordable purchase price for a unit of that size. As of 2002, that calculation resulted in a fee of over $120,000 per affordable unit. Fee collections finance Affordable Housing Fee Fund activities, including mortgage and rental subsidies, new construction and rehabilitation.

H. Developer Incentives

Various incentives are offered to developers to promote the construction of affordable housing. These incentives can be critical. Some jurisdictions stimulate significant numbers of affordable units by granting development benefits for those projects that either fulfill or exceed the inclusionary percentage. Some jurisdictions credit incentives for the success of their inclusionary program, claiming they have directly contributed to increases in actual affordable production (see Figure 5).

Figure 5: Developer Incentives



Density bonuses are by far the most popular incentive offered to developers to build affordable housing, reported by 91 percent of the respondents. There is some question, however, whether this density bonus can be used in some jurisdictions due to parking, setback and other requirements that effectively negate efforts to increase density. In some cases, developers may opt to build at less than the maximum allowable density in order to maximize the amount of nonresidential space for project facilities and open areas and minimize the density concerns of neighbors.

California's Density Bonus Law

Technically speaking, all jurisdictions in California are required to offer a density bonus per state law. Government Code Section 65915 provides that a local government shall grant a density bonus of at least 25 percent and an additional incentive or financially equivalent incentive(s), to a developer of a housing development agreeing to construct at least: a) 20 percent of the units for low-income households; or b) 10 percent of the units for very low-income households; or c) 50 percent of the units for senior citizens. Other incentives might include reduced parking requirements, reduced setbacks, fee waivers or other concessions identified by the developer or jurisdiction.

Design flexibility often means requiring identical or similar exteriors but allowing variations in internal features in order to facilitate financial feasibility for developers. While design differences between market- and below market-rate units might ease the burden for developers, jurisdictions struggle to avoid the neighborhood opposition and social stigma that can come with housing that stands out because of external design standards that are compromised or lowered to reduce costs.

The City of Livermore in Alameda County takes these issues into account by requiring "comparability of units" in its inclusionary program. This is defined in terms that reflect the goals of integration common in many communities: "From the street, the reserved units must not be distinguishable from other units in the project." Nonetheless, Livermore does allow for design flexibility in the interiors, focusing its attention on numbers of bedrooms and bathrooms and amenities such as air conditioning and laundry facilities.

The relatively high percentages of respondents providing subsidies, as well as various fee concessions as incentives, indicates that many jurisdictions are "paying" for inclusionary housing, either by direct cash assistance, foregone revenue or both. In other words, developers in these communities are not bearing 100 percent of the cost of earmarking a percentage of their units for affordable housing. Some jurisdictions release developers from the obligation to produce the affordable units when adequate subsidy is not available. Unlike direct housing subsidies, it is not clear whether fee concessions actually secure a specific public benefit, such as long-term affordability. Because the depth of subsidy was only reported by a few jurisdictions, future research in this area would be helpful.

CASE STUDY

Subsidizing Inclusionary Housing

Roseville, a rapidly growing suburb of Sacramento, adopted a General Plan policy in 1988 mandating housing affordability. Each plan area is required to meet a 10 percent inclusionary requirement, but the specific plan mandates different percentages on different parcels within each area. When City funding is not available to assist construction of below market-rate units, the requirement is waived entirely. The program has produced over 2,000 units of very low-, low-, and moderate-income housing since adoption of the policy. As required, 75 percent of affordable units constructed have been rental units.

I. Length of Affordability

Ensuring that new affordable units stay affordable is another problematic issue. Some jurisdictions report the loss of affordable housing stock because there were not adequate requirements or monitoring mechanisms in place to guarantee continued affordability. Affordable rents can easily be recalculated for subsequent renters and are typically offered by nonprofit and for profit ownership entities subject to long-term use agreements or deed restrictions that are conditions of the underlying financing. Restricting homeowners from reselling affordable units at market-rate prices or requiring equity sharing are much more difficult to regulate and require sustained and active monitoring by local officials.

One stunning example of the consequences of such policy failures is the City of Irvine in Orange County. Because the city had no system for resale control prior to 2001, almost all of the 1,610 ownership units created before that time are no longer part of the affordable housing stock, having now been resold at market-rate prices.[7] In contrast, the City of Palo Alto in the heart of Silicon Valley has a 59-year deed restriction on its inclusionary ownership units, which is reset each time a home is sold or refinanced, achieving something very close to permanent affordability. Palo Alto also retains the right to purchase the home upon resale and only assigns this right to a buyer from its waiting list.

While there is general agreement on the value and the mechanisms for ensuring long-term affordability of rental housing, for-sale housing is a more complicated picture. On the one hand is the desire to enable low- and moderate-income homebuyers to accumulate equity (wealth), which is one of the main benefits of homeownership in this country. On the other hand is the desire to ensure that public policy and investment assists more than just the one household that initially buys an affordable home.

Virtually all jurisdictions now report that they have formal mechanisms to maintain affordability over time. Deed restrictions, resale controls and rental contracts are the most common means by which affordability is ensured. These restrictions range from periods of 10 years to perpetuity with the median length for rental housing 42 years and for-sale housing 34 years. Permanent affordability is reported in 20 percent of programs for both rental and for-sale.

Over the last decade, a significant number of jurisdictions have chosen to amend their policies or ordinances to address deficiencies in affordability controls. In fact, nearly 50 percent of all jurisdictions have amended their ordinances at least once, many in the last five years. In doing so, jurisdictions have increased the term of affordability to 55 years or permanent affordability. Many have adopted new policies or mechanisms to address the particular challenge of monitoring and maintaining the affordability of for-sale units.

Nonetheless, monitoring units remains an area of obvious concern. Many jurisdictions declined to answer survey questions related to monitoring and overall tracking of inclusionary production. Among those that responded, most cities and counties report that they assume overall responsibility for monitoring long-term affordability, but it is unclear from discussions with local staff just how effectively those units are monitored. The high incidence of incomplete responses on monitoring leads the researchers to believe that greater emphasis in this area is needed.

J. Obstacles to Implementation

Local officials cite a number of factors that complicate or undercut successful implementation of inclusionary programs. The principal obstacle is scarcity of land for development, noted by 59 percent of jurisdictions, followed by developer opposition, noted by 39 percent. Lack of funding and community opposition are obstacles in 31 percent and 19 percent of jurisdictions, respectively. Other respondents cite high land prices and inadequate public works infrastructure as challenges to the development of new affordable housing.

Developer opposition arises from the perspective that inclusion of affordable housing in market-rate developments is financially prohibitive and/or unfairly shifts costs to moderate- and above moderate-income families via higher sales prices and rents. Moreover, profit motivated builders argue that they are unfairly forced to shoulder the financial onus for an affordable housing provision that should rightly be borne by the public sector in partnership with below market-rate developers in the business of developing and operating affordable housing.

In the face of enormous housing needs, expectations are shifting in the contemporary development scene. Accepting the task of building or supporting affordable housing will require for profit developers to adapt. While it is not surprising that there is resistance, the market arguments that inclusionary policies will stifle construction or dramatically increase market-rate real estate prices have yet gone unproved. During the 1990s, construction rates and permit valuations remained steady or rose in inclusionary jurisdictions, as they did statewide. Anecdotal reports confirm that developers continue to build and that more newly constructed units are affordable as the result of local inclusionary programs.

Conclusion

The rapid expansion of inclusionary housing in California over the last 30 years has aroused considerable debate. Advocates on both sides of the issue have raised questions about the impact of various kinds of inclusionary policies. In this section, we attempt to answer some of the critical questions pertaining to inclusionary implementation and make policy recommendations based on the experience of the 15 most successful programs as measured by sustained and significant production of affordable housing.

Although the data collected from the survey do not provide definitive answers, it is instructive to compare the 15 programs regularly producing affordable housing with the other 92 programs in the state, some of which have struggled to achieve consistent production.[8] We recognize that no simple statistical comparison can measure a program's success without understanding the particular local contexts involved. Likewise, it may very well be that the local variability of inclusionary programs is a key to their success.

A. Critical Questions in Inclusionary Implementation

Does a strong inclusionary policy discourage overall housing production?

Perhaps not surprisingly, it appears that the jurisdictions producing the most inclusionary units are those that have experienced rapid expansion. To be specific, the top-producing jurisdictions grew at an average rate of 25 percent compared to 14 percent in the other inclusionary jurisdictions from 1990 to 2000. These jurisdictions have managed to harness their exceptionally rapid population growth to stimulate affordable housing production. Respondents who offered comments on the subject believe their policy has not hindered overall housing production.

One of the key measurements of a policy's strength is the percentage of units required to be affordable. Interestingly, the more productive programs had similar percentage requirements to those of the other programs. This would seem to indicate that the results of a program depend heavily on other factors. One respondent commented that his jurisdiction had to reduce inclusionary requirements from 25 percent to 20 percent of all units produced to make the program effective, while four respondents recommended raising the percentage of units currently required to make their programs more effective.

PERCENTAGE OF NEW UNITS REQUIRED TO BE AFFORDABLE

% REQUIREMENT	15 MOST PRODUCTIVE PROGRAMS		OTHER PROGRAMS	
	RENTAL	OWNERSHIP	RENTAL	OWNERSHIP
Less than 10%	7%	13%	4%	3%
10-14%	40%	33%	45%	43%
15-19%	33%	27%	23%	21%
20% or more	20%	20%	22%	22%

In contrast, comparison shows that deep income targeting is a feature of many policies that produce a significant number of units. In fact, the most productive programs are more likely to target low- and very low-income households and less likely to target moderate-income households. On the surface, this would seem counterintuitive; programs with relaxed or higher targeting would seem more likely to produce greater numbers of units than programs with more stringent targeting. What this analysis suggests is that deeper targeting does not, in and of itself, discourage production and, perhaps, coupled with staff commitment, funding resources and other local factors can create an environment for success.

INCOME GROUPS TARGETED BY INCLUSIONARY PROGRAMS		
INCOME-TARGETING	**15 MOST PRODUCTIVE PROGRAMS**	**OTHER PROGRAMS**
Very Low-Income	60%	42%
Low-Income	87%	71%
Median-Income	53%	65%

Can a voluntary program be as effective as a mandatory program?

Only six jurisdictions responding to the survey identified their policy as voluntary. None of these jurisdictions was among the most productive and three reported no production of inclusionary units at all. Programs classified as "mandatory with exceptions" because they allow developers to avoid inclusionary requirements under certain conditions, such as small project size or lack of funding, appeared in both groups. Although truly voluntary programs are generally unsuccessful in producing affordable units, mandatory programs with exceptions are not necessarily less effective simply because they permit exceptions.

Do alternatives to construction promote the production of affordable housing or merely provide a loophole for developers who want to avoid inclusionary requirements?

The highly productive programs are more likely to permit most alternatives to construction than other programs. In-lieu fees are permitted by a high percentage of all programs, although somewhat less often by the most successful programs. The success or failure of an in-lieu fee option is likely to depend on the way the fee is calculated, as well as the ways in which collected funds are used. This correlation suggests that flexibility is not inimical to program success, provided it is accompanied by appropriate controls to ensure that units are still produced.

ALTERNATIVES TO CONSTRUCTION ALLOWED BY INCLUSIONARY PROGRAMS		
ALTERNATIVES TO CONSTRUCTION	**15 MOST PRODUCTIVE PROGRAMS**	**OTHER PROGRAMS**
Off-Site Allowance	86%	64%
Land Dedication Allowance	60%	39%
In-Lieu Fees	73%	80%
Developer Credit Transfer	33%	17%

Should jurisdictions allow owners to "opt out" of inclusionary requirements altogether, based on small project size or infeasibility?

Of the most productive programs, none allow exemptions to inclusionary requirements based on infeasibility. The most productive programs are also slightly less likely than other programs to allow exemptions based on small project size.

EXEMPTIONS PERMITTED BY INCLUSIONARY PROGRAMS		
EXEMPTIONS	**15 MOST PRODUCTIVE PROGRAMS**	**OTHER PROGRAMS**
Small project size	67%	82%
Infeasibility	0%	15%

What incentives help developers produce affordable units?

The most productive programs were much more likely than the other programs to subsidize the construction of affordable units (71 percent versus 38 percent). The substantial difference suggests that funding is an important facet of a successful inclusionary program. There was little difference between productive programs and less productive programs with respect to other incentives offered.

What prevents inclusionary programs from being successful?

Respondents identified a number of obstacles to the production of inclusionary units. Among the most productive programs, lack of funding was the most commonly cited concern, listed by 67 percent of these respondents compared to only 24 percent of the others. On the other hand, scarcity of land was much more likely to be identified as an obstacle by the less productive programs (64 percent versus 33 percent). Respondents from both groups frequently mentioned developer opposition as a significant obstacle to construction of affordable units.

Several considerations help explain why jurisdictions producing more units perceive the obstacles to inclusionary production differently. Since land is a prerequisite for all new construction, jurisdictions with a limited supply of land are much more likely to find themselves producing fewer units each year than other jurisdictions. In other words, programs producing fewer units may be more restricted in terms of their available land. The more productive jurisdictions' greater concern about funding is probably due to a couple of factors. One is that these jurisdictions were also more likely to report that subsidies were provided for inclusionary units, implying that limited funding would truly harm these programs' ability to produce. Also, jurisdictions might be less likely to single out limited funding as a problem when other barriers frequently prevent a project from moving to the funding stage.

Although many respondents in both groups identified developer opposition as an obstacle, one respondent commented that most developers in California are "resigned" to inclusionary policies, given the number of jurisdictions in the state that have such requirements. Another respondent observed that market-rate housing developers may not like inclusionary programs, but choose to produce affordable units rather than stop developing altogether.

OBSTACLES TO SUCCESS OF INCLUSIONARY PROGRAMS

OBSTACLES TO IMPLEMENTING POLICY	15 MOST PRODUCTIVE PROGRAMS	OTHER PROGRAMS
Community opposition	8%	22%
Developer opposition	42%	38%
Local government processes	0%	5%
Lack of funding	67%	24%
Scarcity of land	33%	64%
Other	33%	27%

What other factors tend to increase the number of units produced?

The most productive programs were adopted earlier, but amended more recently, than the others. It is not surprising that the jurisdictions that have had a sustained commitment and continued to fine tune and update their programs, would be the ones that have achieved the most production of affordable units.

B. Policy Recommendations for Local Governments

There is a great deal of variation in the success of local inclusionary programs, as judged from the production of affordable units. The following policy recommendations for local governments are drawn largely from the characteristics of those programs that have produced the most affordable units since their inception. Since the most productive programs are often older, the recommendations below also include successful elements

of newer programs, as well as program elements contained in recently updated inclusionary policies. While each jurisdiction has unique circumstances and needs, cities and counties developing a new inclusionary program (or revising an existing program) can learn from what is working well elsewhere.

Inclusionary Percentage

Aim high in the percentage of units required to be affordable; 15 percent is realistic in most communities. Design incentives and program flexibility can mitigate the burden developers face in meeting inclusionary requirements, as described below.

Income Targeting

Unless financially infeasible, require housing for very low-income, low-income, and moderate-income households to be included. Section 8 vouchers can provide deeper affordability. Income categories can and should be adjusted based on local needs; for example, programs can target moderate-income units to a maximum of 100 percent of median, instead of 120 percent. The relative need of income groups as identified in the locality's Housing Element should guide inclusionary program design, with the inclusionary housing complementing other housing programs, such as new construction of assisted housing.

Rental and Ownership

Adopt inclusionary requirements for rental and for-sale housing that are similar enough so that developers continue to provide an appropriate mix of both housing types. Creating too great a difference between the targeting of inclusionary rental units versus for-sale units could create an unintended financial incentive for developers to produce only for-sale housing.

Alternatives to Construction On-Site

Offer some flexibility, such as in-lieu fees, land dedication or off-site development, but subject to local government determination that the alternative meets the need for affordable housing at least as well as traditional on-site inclusionary units.

Where in-lieu fees are an option, set the fee level as high as the cost to the locality of making the units affordable without other public subsidy. In other words, a decision to build units or pay fees should be revenue neutral, and the locality collecting the fees should be able to fund as many units as would have been required. In-lieu fee levels should be tied to the cost of construction and adjusted regularly. Allow in-lieu fees at the discretion of local government or in specific circumstances, such as when fractional units are required, or when a developer can prove that providing affordable units on-site is financially infeasible.

Developer Incentives

Provide incentives that local developers want and can use. Consult with developers during program design to find out how to structure density bonuses, reduced parking requirements, expedited permit review, design differences, growth control exemptions, etc., so that they are meaningful incentives.

Length of Affordability

Require units to be kept affordable permanently or for at least 55 years for rental homes. For homeownership units, programs should allow for reasonable amounts of equity to accrue to owners while still ensuring the long-term affordability of the home. Design effective mechanisms to track long-term affordability, such as restrictions recorded against the property.

Endnotes

[1]Various jurisdictions listed on the California Planners Information Network (www.calpin.ca.gov) self-report having some kind of inclusionary housing. Our research confirmed that many of these jurisdictions only have formal inclusionary programs as required or governed by State Redevelopment Law or the Coastal Act.

[2]Jurisdictions enforcing inclusionary requirements as part of Redevelopment Agency practices or State Density Bonus Law, but with no local policy, were not included.

[3]It seems likely that more jurisdictions with inclusionary ordinances also have policies in their General Plans since local laws are required to be consistent with General Plans.

[4]For the purposes of the charts comparing inclusionary practices in California, the authors have classified those policies in terms of the minimum percentage required for a project.

[5]Figure 4 provides detail on those variations, but for the income targeting charts in this section, the authors have classified multiple choice policies in terms of the highest income target allowed at the developer's discretion.

[6]Calavita and Grimes, p. 160-5.

[7]Calavita and Grimes, p. 155.

[8]Several factors determine the relative "strength" of an inclusionary policy. A multivariate statistical analysis to correlate overall housing production with the relative strength of a locality's inclusionary program, controlling for other factors, would not be possible based on the data collected. However, we have made simple correlations that may explain, at least in part, the success experienced by the top 15 programs in terms of annual production relative to the other 92 programs, and dispel some of the negatives associated with different inclusionary program features. These jurisdictions produce at least 35 affordable units per year.

Avoiding Constitutional Challenges to Inclusionary Zoning

By Deborah Collins and Michael Rawson

Given the vibrant legal debate on property rights issues nationally, it should come as no surprise that inclusionary housing is a highly controversial topic. This article addresses attacks based on the United States Constitution.[1] Constitutional attacks on local land use actions generally allege violation of one or more of three provisions: 1) the Fifth Amendment prohibition against taking without just compensation; 2) the substantive and procedural protections of the due process clauses of the Fourteenth Amendment; and 3) the equal protection clauses of the Fourteenth Amendment. A recent California decision upheld the constitutionality of the City of Napa's inclusionary zoning ordinance and provides significant guidance on all of these issues.[2]

Stepping back, the authority for local governments to adopt zoning and land use regulations such as inclusionary zoning stems from their "police power." This power emanates from the Tenth Amendment to the United States Constitution, and entitles communities to adopt laws protecting the public's health, safety and welfare, including the broad discretion to determine the use and development of a finite supply of land within their borders.[3] Any controls or regulations that are not unreasonable and bear some relationship to the general welfare of the community are permissible unless proscribed by preemptive state or federal laws or by the federal or state constitution. This article addresses attacks based on the United States Constitution.[4]

Based on its findings related to the critical need for affordable housing and a diminishing supply of land to accommodate those needs, the Napa inclusionary zoning ordinance requires developers to set aside ten percent of all new residential units as affordable housing. Developers have the opportunity to provide "equivalent alternatives," including land dedication, off-site construction or in-lieu payments. The ordinance also provides several concessions and incentives to developers in exchange for the inclusionary requirement, including expedited processing, waiver of development standards, loans and grants, and density bonuses. The ordinance also provides an opportunity for developers to appeal for an adjustment or waiver of the inclusionary requirement "based on the absence of any reasonable relationship or nexus" between the development's impact and the inclusionary requirement.[5]

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[1]Readers are encouraged to also review the constitution, statutes and case law addressing land use regulation in their states.

[2]Homebuilders of Northern California v. City of Napa, 90 Cal.App. 4th 188 (2001); review denied 2001 Cal. LEXIS 6166 (2001) and cert. den. 535 U.S. 954 (2002).

[3]*See Euclid v. Amber Realty Company*, 272 U.S. 365, 387 (1926); *Agins v. City of Tiburon*, 447 U.S. 255, 260-63 (1980); and *Penn Central Transp. Co. v. New York City*, 438 U.S. 104, 124 (1978).

[4]Readers are encouraged to also review the constitution, statutes, and case law addressing land use regulation in their states.

[5]*See* City of Napa, California Mun. Code 15.94.050 (1999), available at http://www.cityofnapa.org/municipal-code.

A. Takings Issues After *Napa*— A Sound Ordinance Is Not A Taking

The Fifth Amendment prohibits the taking of private property for public use without just compensation. The courts have established a two step analysis for determining whether a local regulation is a taking: 1) whether it substantially advances a legitimate state interest[6] or 2) whether it denies the property owner all economically viable use of the property.[7] Generally, in applying this analysis to local land use regulations, the courts will give great deference to the local government's decision, recognizing that the community adopts these regulations under the broad authority of the police power.[8]

1. Inclusionary Requirements Substantially Advance Legitimate State Interests

The *Homebuilders of Northern California v. City of Napa* court had no doubt that the City had a *legitimate interest* in requiring the provision of affordable housing. The "assistance of moderate-income households with their housing needs is recognized in this state as a legitimate governmental purpose."[9] The court also referred to state legislation mandating that development of sufficient housing for all Californians is a matter of statewide concern and that local governments have "a responsibility to use powers vested in them to facilitate improvement and development of housing to make adequate provision for the housing needs of *all economic segments of the community.*"[10]

The *Napa* court also found it "beyond question" that the City's inclusionary ordinance will *substantially advance* these important affordable housing interests. When determining whether a land use requirement, condition or fee substantially advances a legitimate state interest, a court is essentially deciding whether there is a "nexus" between the interest advanced and the requirement (*i.e.*, whether there is a sufficient relationship between the two). Generally, a court will defer to the local government's assessment of that relationship and will not second guess the locality. Recently, however, the United States and California Supreme Courts have applied a "heightened scrutiny" test when reviewing *land dedication requirements or exaction fees* imposed on an *ad hoc* basis as a condition for approval of particular

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[6]Due process focuses on whether the government regulation is *related to* the government interest, while the takings analysis is slightly stricter-whether the regulation *substantially advances* the interest. *See Erblich v. City of Culver City*, 12 Cal. 4th 854, and fn 7 (1996).

[7]*Agins v. City of Tiburon*, 447 U.S. 255 (1980).

[8]See Euclid at 387; Penn Central Transp. Co. v. New York City, 438 U.S. 104, 124; Village of Belle Terre v. Boraas, 416 U.S. 1, 4-6 (1974).

[9]Homebuilders v. Napa, 90 Cal.App. 4th 188 at 195, *quoting Santa Monica Beach, Ltd. v. Superior Court*, 19 Cal.4th 952, 970.

[10]*Id., quoting* Cal. Govt. Code §65580(d).Mandating the inclusion of affordable housing also can help counteract the effect of past exclusionary zoning practices and further the goals of state and federal fair housing laws. *See* Roisman, *Opening the Suburbs to Racial Integration: Lessons for the 21st Century*, 23 W. New Eng. L. Rev. 65.

developments.[11] The *Napa* court found that the "heightened scrutiny" test did *not* apply to its review of Napa's inclusionary zoning ordinance because it was a broad-based ordinance rather than an ad hoc response (*Napa* at 196).

A local ordinance or regulation that, on its face, substantially advances a legitimate state interest-as does the *Napa* ordinance-can nonetheless violate the takings clause if it is *applied* to a particular development in a way that fails to advance the interest. In other words, if the regulation does not include clear implementation standards and procedures, an inclusionary requirement could conceivably be applied in an arbitrary or discriminatory manner to a particular development and consequently be found to lack the essential nexus to the interest.

Napa involved a challenge to the City's ordinance, only "on its face" (not "as applied" to a particular development). However, the court's reasoning provides clear guidance on how an inclusionary zoning ordinance also can survive a taking challenge to a particular development.[12] In *Napa*, the inclusionary ordinance provides significant benefits to the developer-expedited processing, fee deferrals, loans or grants and density bonuses-which balance the regulatory burden. "More critically, the ordinance permits a developer to appeal for a reduction, adjustment or *complete waiver* of the ordinance's requirements. Since the City has the ability to waive the requirements imposed by the ordinance, the ordinance cannot and does not, on its face, result in a taking."[13]

Thus, to ensure an inclusionary ordinance can avoid unconstitutional *application*, the ordinance should provide standards and procedures for reducing, waiving or mitigating the requirements. Clearly, what was most important to the *Napa* court was the possibility of complete waiver of the requirements. However, the court also emphasized that an ordinance that provides significant benefits to developers may offset the impact of the inclusionary obligations. Accordingly, the appeals process provided in an ordinance should first require a developer to show that the benefits afforded by the ordinance do not fully compensate for the alleged impermissible hardship, before making reductions, alternative compliance or waiver available.

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[11] In *Nollan v. California Coastal Commission*, 483 U.S. 825 (1987), the U. S. Supreme Court held that there must be an "essential nexus" between an ad hoc dedication imposed as a condition of development and the impacts of the development. Id. at 837. Then, in *Dolan v. City of Tigard*, 512 U.S. 374 (1994) the Court found that the degree of the nexus between the impact and the dedication must be one of "rough proportionality" as assessed by an "individualized determination" with some "quantification." *Id.* at 391. The California Supreme Court considered this "*Nollan/Dolan* heightened scrutiny test" in *Erhlich v. City of Culver City*, 12 Cal.4th 854 (1996) and held that the test applies to fees as well as to dedications, ***but only to those imposed "on an individual and discretionary basis.***" (Emphasis added.)

[12] "'A claim that a regulation is invalid *on its face* is only tenable if the terms of the regulation will not permit those who administer it to avoid an unconstitutional *application* to the complaining parties.'" 90 Cal.4th at 194 (Citations omitted).

[13] *Napa* at 194 (emphasis in original).

2. Inclusionary Requirements Do Not Deprive Owners of All Economically Viable Use of the Property

Another potential challenge to the application of an inclusionary zoning requirement is that the financial impact of the regulation on a particular development is so drastic that the effect should be deemed a taking. Inclusionary ordinances do not *preclude* development; they merely require a reasonable percentage of the development to be affordable. It is highly unlikely that an inclusionary requirement would have so substantial an impact as to deprive an owner of all economically viable use of the property. Moreover, even local regulations that have diminished property values by as much as 87.5 percent have been upheld by the courts.[14] Accordingly, it is doubtful that an attack on this basis could succeed.

B. Substantive Due Process Issues After *Napa*— Availability of Appeal, Waiver and Alternatives Important

The Fourteenth Amendment's guarantee of due process of law has been interpreted to prevent governments from "enacting legislation that is 'arbitrary' or 'discriminatory' or lacks 'a reasonable relation to a proper legislative purpose.'"[15] This is known as the "reasonable relationship test."

Opponents to inclusionary zoning argue that such laws fail the reasonable relationship test because they amount to price or rent controls that lack procedures to ensure that developers will receive a "fair return" on their investments.[16]

The first hurdle for a "fair return" argument to overcome is whether a due process analysis is even applicable to a land use regulation such as an inclusionary zoning ordinance. In *Armendariz v. Penman*,[17] the Ninth Circuit recognized that "the use of substantive due process to extend constitutional protection to economic and property rights have been largely discredited," because the takings clause provides sufficient constitutional protection.[18] Since the takings clause has been found to relate more directly to land use regulation than substantive due process,[19] a substantive due process claim challenging an inclusionary zoning ordinance should be precluded.

Nevertheless, inclusionary requirements, including in the *Napa* case, have been attacked as price controls that violate the due process clause. The court in *Napa* stopped short of holding that the "fair return" standard did not apply in inclusionary zoning cases because it could find the Napa ordinance was valid on its face on other grounds. However, it indicated that it is unlikely that a developer is entitled to a "fair return" under the due process clause, noting that the "fair return" standard developed in evaluating restrictions placed on regulated industries such as railroads and public utilities.[20]

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[14] *See, e.g., Penn Central Transp. Co. v. New York City*, 438 U.S. 104 (1978) upholding a landmark historic preservation regulation and establishing a three-factor test for determining the financial impact of a regulation.

[15] *Kavanau v. Santa Monica Rent Control Bd.*, 16 Cal.4th 761, 771 (1997) (*citing Nebbia v. New York* (1934) 291 U.S. 502, 537).

[16] *See* discussion in *Home Builders Assn. v. City of Napa*, 90 Cal.App.4th 188 at 198.

[17] *Armendariz v. Penman*, 75 E3d 1331, 1318-1319 (9th Cir. 1996).

[18] *Id.* at p. 1318-1319, 1324.

[19] *See e.g. Agins v. Tiburon* (1980) 447 U.S. 225.

[20] *Napa* at 198.

Although it has since been used in assessing rent control ordinances, the *Napa* court doubted that it would apply to inclusionary zoning ordinances (*Id*). The court further noted that although the ordinance may not have specifically given the administrative agency authority to make adjustments to guarantee a fair return, this ability was "present by implication" in light of the administrative appeal available under the ordinance.[21]

Thus, a constitutionally defendable inclusionary zoning ordinance should contain provisions which allow a developer to seek administrative relief and provide sufficient flexibility to provide that relief. When an ordinance contains provisions which allow for administrative relief, the court reviewing the ordinance must presume that the administrative body will exercise its authority in conformity with the Constitution.[22]

Adequate administrative standards and procedures for relief also protect against application of inclusionary requirements in arbitrary or discriminatory ways to individual developers. Fair application of clear standards will lessen the likelihood that the requirement *as applied* to a particular developer will be found to be arbitrary *or* a denial of a fair return.

C. Equal Protection Issues— A Sound Ordinance Will Avoid Problems

The equal protection clauses of the Constitution prohibit state and local governments from depriving persons of equal protection of the laws (U.S. Constitution, Fourteenth Amendment). On the surface, all land use and planning laws and practices would seem to violate this principle because their purpose is to treat property owners differently-permitting uses on some property and prohibiting them on other property. However, courts will generally uphold a local land use regulation as a lawful exercise of the police power if it bears a *rational relationship* to a legitimate governmental interest.[23] Consequently, an inclusionary requirement that satisfies the takings and due process mandates, will also pass muster under the equal protection strictures.

Inclusionary requirements are more likely to be challenged as unconstitutional under the takings clause or the substantive due process clause. Both of those relate more directly to the specific offenses usually raised by challengers-lack of sufficient nexus (takings) and arbitrary price control (due process). The plaintiffs in *Napa* attacked the constitutionality of the City's ordinance on takings, substantive due process and other state law, not equal protection. Almost all successful equal protection challenges of land use actions have been when the local government *applies* local regulations to landowners in an unequal, discriminatory manner.[24] Therefore, if an inclusionary

[21] *Id., citing City of Berkeley v. City of Berkeley Rent Stabilization Bd.* 27 Cal.App.4th 951, 962 (1994).
[22] *Napa* 90 Cal.App.4th at p. 199 (citing *Fisher v. City of Berkeley*, 37 Cal.3d 644, 684 (1984)).
[23] Like the test under the due process clause, the "rational relationship test" is virtually identical to that employed in substantive due process cases. It is also akin to the "furtherance of a legitimate government purpose" test for takings claims. If a land use regulation intentionally discriminates against a "suspect class" of persons (e.g. racial or ethnic minorities), however, or denies someone a "fundamental right" (e.g. the right to live as a family), it will be held to a much tougher "strict scrutiny" test, requiring the local government to show that the regulation serves a "compelling governmental interest." *See Construction Industry Association of Sonoma County v. City of Petaluma*, 522 F.2d 897, 906 (9th Cir. 1975), *cert. denied*, 424 U.S. 934.
[24] See, e.g., Longtin's California Land Use, 2002 Update at §1.32[3], pp. 27-29.

requirement is attacked on equal protections grounds it will probably be in a case where challengers allege *unequal application* of the requirement to a specific development.

Accordingly, inclusionary requirements should be based on established facts and sound analysis of the need for affordable housing and adopted and implemented so as to apply uniformly and across the board to all similarly situated developers. And, all exemptions, exemption procedures and categories of alternative performance should have a clear basis and clear standards for eligibility.

Inclusionary Housing and its Impact on Housing and Land Markets

By David Rosen

What Effect Has Inclusionary Housing Had on Housing Production in California Cities?

To determine if inclusionary housing programs are associated with a decline in housing production, the author compiled data on annual housing starts over a 20-year period in California. For the period 1981 through 2001, annual new construction residential building permit figures for 28 cities-with and without inclusionary housing programs-located in Los Angeles, Orange, San Diego, San Francisco and Sacramento counties were reviewed. The author also analyzed housing start data for the State of California for the same period. The analysis includes separate tabulations for single family and multifamily housing starts.

The annual housing start data were then compared to passage of the 1986 Tax Reform Act (which significantly reduced favorable tax treatment for the construction of market-rate investment property) and key economic indicators: the prime rate, the 30-year mortgage rate, the unemployment rate and area median home price.

An analysis of these data shows that for the jurisdictions surveyed, adoption of an inclusionary housing program is not associated with a negative effect on housing production. In fact, in most jurisdictions as diverse as San Diego, Carlsbad and Sacramento, the reverse is true. Housing production increased, sometimes dramatically, after passage of local inclusionary housing ordinances.

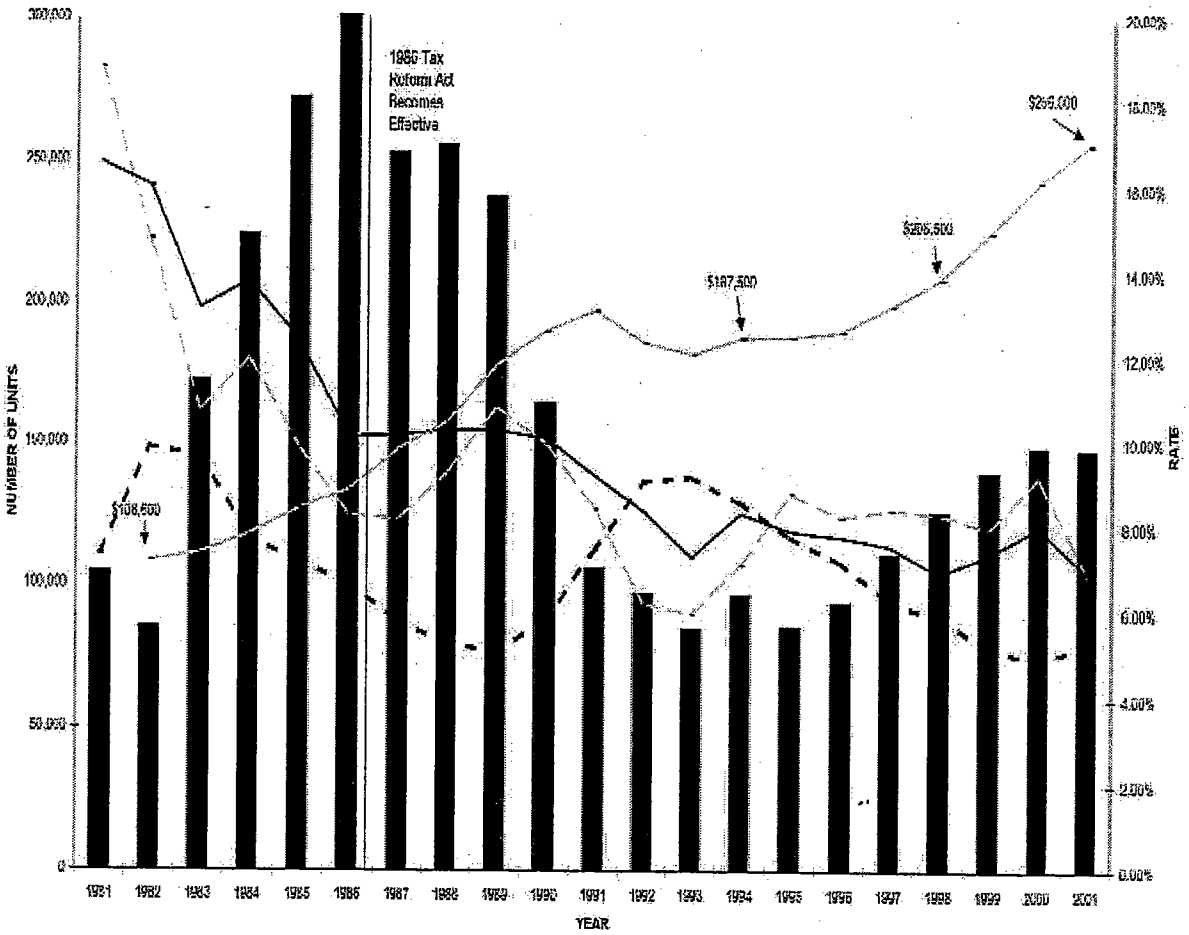
In only one of the cities surveyed, Oceanside, did residential building permit activity drop immediately after passage of inclusionary zoning (from 1,430 units in 1991 to 536 units in 1992). Although the inclusionary housing ordinance adopted in 1991 may have had some effect, other factors may have had a more important impact on housing production. The Gulf War (1990-91) dramatically increased vacancy rates in Oceanside, which is located next to United States Marine Corps Camp Pendleton. According to Margery Pierce, Director of Housing and Neighborhood Services for Oceanside, the vacancy rate increased to approximately 17 percent during that war. Second, the San Diego County unemployment rate increased steadily beginning in 1990 through 1993. In fact, housing starts were down during the same years for other cities in San Diego County: Escondido, Carlsbad, Chula Vista and San Diego itself.

A review of the data indicates that the one factor that most clearly tracks housing production is the unemployment rate. For most jurisdictions, there is an inverse relationship between the county unemployment rate and housing production. In Los Angeles, housing production figures have an inverse relationship with the Los Angeles County unemployment rate. For example, beginning in 1989 and through 1993, the increase in the Los Angeles County unemployment rate tracks the dramatic decrease in new housing production. Modest increases in new housing production did not occur until the late 1990s. Unemployment steadily dropped beginning in 1994 and continued to drop through 2000. The unemployment rates in Orange, San Diego, San Francisco and Sacramento Counties as well as the state follow similar patterns.

The passage of the 1986 Tax Reform Act is associated with a sharp drop in new housing production.The act ended favorable tax treatment of market-rate rental housing, which effectively subsidized that housing. In almost all jurisdictions surveyed, housing production figures dropped significantly after 1986. In Los Angeles, the highest number of residential units (as measured by building permits) was developed in 1986.After 1986, housing production figures dropped dramatically until a small upward trend in production beginning in the mid to late 1990s. Carlsbad is another example of a city that experienced a dramatic drop in housing production in 1987. In most instances, the drop in housing production after 1986 was not immediate.Therefore, it may be a combination of the recessionary period beginning in the early 1990s and the 1986 Tax Reform Act that dampened production of housing.

Chart 1 summarizes residential building permit figures over time for the State of California.

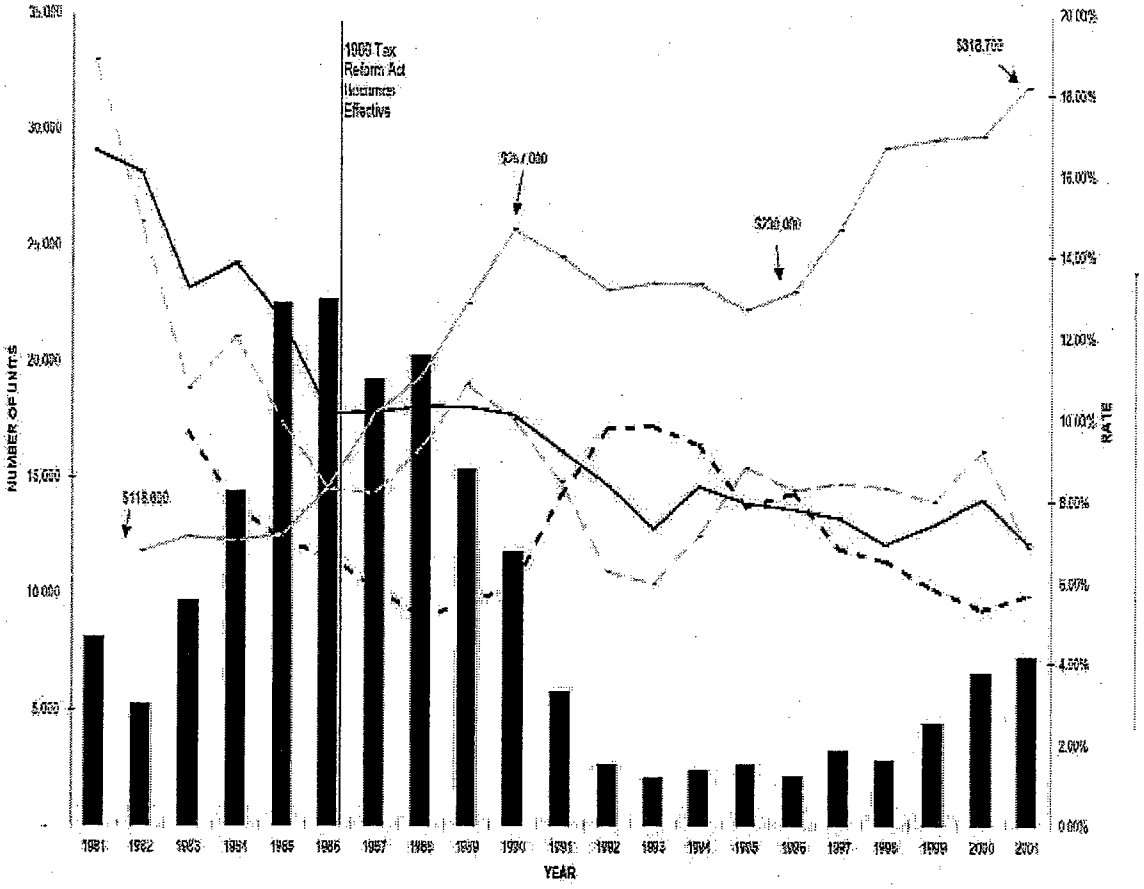
Chart 1: STATE OF CALIFORNIA TOTAL RESIDENTIAL BUILDING PERMIT ACTIVITY, 1981-2001



Sources: David Paul Rosen & Associates, Oakland, California
Residential Permit Data - Construction Industry Research Board
Unemployment Rate - Employment Development Department, Labor Market Information
Prime Rate - Federal Reserve Board
30 Year Mortgage Rate - Federal Home Loan Mortgage Corporation (FHLMC) Survey of Major Lenders
Median New Home Price - Construction Industry Research Board

Chart 2 shows the residential building permit figures for the City of Los Angeles.

Chart 2: CITY OF LOS ANGELES TOTAL RESIDENTIAL BUILDING PERMIT ACTIVITY, 1981-2001

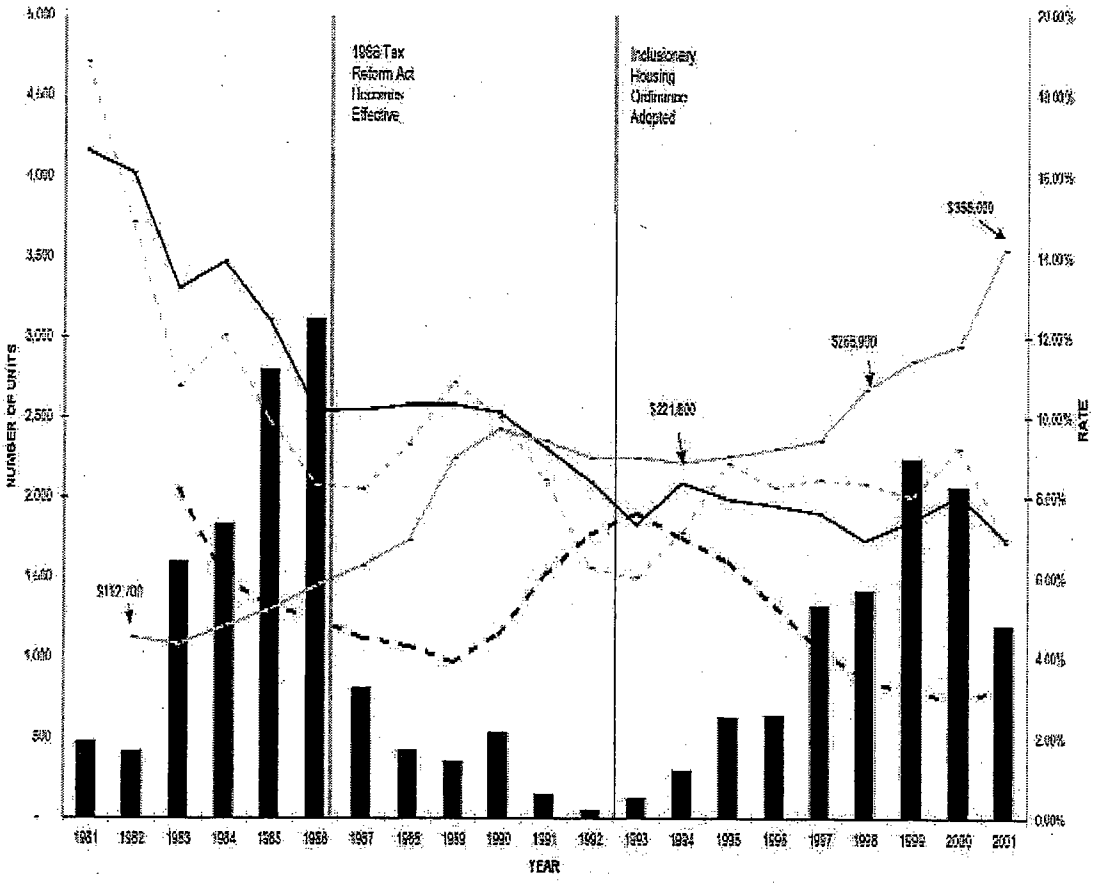


Sources: David Paul Rosen & Associates, Oakland, California
Residential Permit Data - Construction Industry Research Board
Unemployment Rate (seasonally adjusted) - Employment Development Department, Labor Market Information
Prime Rate - Federal Reserve Board
30 Year Mortgage Rate - Federal Home Loan Mortgage Corporation (FHLMC) Survey of Major Lenders
Median New Home Price - Construction Industry Research Board (CIRB provides data by county, not city)

Chart 3 displays trends in the City of Carlsbad (one city in San Diego County with inclusionary housing).

In conclusion, after reviewing 20 years of building permit history for both multifamily and single family housing in 28 California jurisdictions plus the state itself, no correlation whatsoever was found between a city's adoption of inclusionary housing and a reduction in housing development activity.

Chart 3: CITY OF CARLSBAD TOTAL RESIDENTIAL BUILDING PERMIT ACTIVITY, 1981-2001



Sources: David Paul Rosen & Associates, Oakland, California
Residential Permit Data - Construction Industry Research Board
Unemployment Rate - Employment Development Department, Labor Market Information
Prime Rate - Federal Reserve Board
30 Year Mortgage Rate - Federal Home Loan Mortgage Corporation (FHLMC) Survey of Major Lenders
Median New Home Price - Construction Industry Research Board

Measuring the Cost and Feasibility of Inclusionary Housing

In order to assess the potential impact of alternative inclusionary housing requirements and incentives, one needs to start with basic information on how housing actually gets built in a city today. Using information from developers, one can establish the economic assumptions, development prototypes and incentives to be used in the analysis.

The approach takes care to quantify the cost of imposing an inclusionary obligation on housing developers. The approach also measures the economic value of various incentives and alternative compliance options a city may provide to offset this cost.

Inclusionary housing imposes a prospective cost on development which can be partially to completely offset with economic incentives and alternative compliance options. We determine whether and to what extent the cost of alternative inclusionary requirements can be offset by the value of incentive "packages."

This analysis assists policymakers in making informed decisions about inclusionary housing for their communities. A land residual value analysis is used to measure these effects.

Some policymakers and developers concerned with the adoption of inclusionary housing assert that it will drive up the price of apartments and homes. This assertion is belied by the fundamentals of real estate market supply and demand. The price of housing is not a function of its development cost. Rather, housing price, be it rents or sale prices, are solely a function of market demand. For example, a developer may experience an increase in construction interest from that contained in his or her development pro forma. That developer can no more pass along the "cost increase" of higher than projected interest rates to renters or homebuyers than could be done for a "cost increase" associated with inclusionary housing. Similarly, if the price of lumber or steel experiences a sharp increase during a project's construction, it too cannot be passed on in the form of higher rents or home prices. Conversely, no one expects a developer enjoying lower than projected interest costs to lower rents or home prices accordingly.

Why Was a Land Residual Approach Used?

Land residual analysis is commonly used by real estate developers, lenders and investors to evaluate development financial feasibility and select among alternative uses for a piece of property. The land residual methodology calculates the value of a development based on its income potential and subtracts the costs of development and developer profit to yield the underlying value of the land. An alternative land use that generates a negative land value is not financially feasible. Similarly, an alternative use which generates a land value lower than the land seller is willing to accept is infeasible. Recent land sales ("market comparables") provide an indication of the range of land prices sellers may accept for different types of land.

Land residual analysis is the most realistic way to view the potential impact of inclusionary requirements on residential development. Developers and landlords already charge the maximum rents and sales prices the market will bear. Therefore, any increase in development costs resulting from government regulation or other factors, will ultimately impact the price of land and/or profits to developers and owners, and cannot

be passed on to the consumer. A reduction in developer profit margins does not necessarily render a project infeasible. Developers typically have "threshold" profit and overhead requirements. When developers reach their maximum profit thresholds, the price they will pay for a given land parcel will be reduced.

In some market climates, developers are willing to build and lenders and investors are willing to finance a development based on a "future value." One example of such "speculative" development is constructing apartments which may later be sold as condominiums.

What Are the Low, Middle and High Rent/ Land Value Scenarios?

In large cities, residential land sales prices vary widely in different locations. The land prices are tied to the market rents and/or sales prices in different market areas of a city. For the Los Angeles analysis, the author analyzed actual land sales prices for 79 residential developments receiving building permits in the City of Los Angeles in 2001.

The market land sales comparables were divided into thirds based on price per square foot of site area to represent *low, middle* and *high* land price ranges in the City. For the rental land residual analysis, the author used *low, middle* and *high* average rent data from 45,000 rental units (*RealFacts*, 2002) to calculate rents for the three (low, middle and high) rent/land values scenarios.

Prototype: Los Angeles

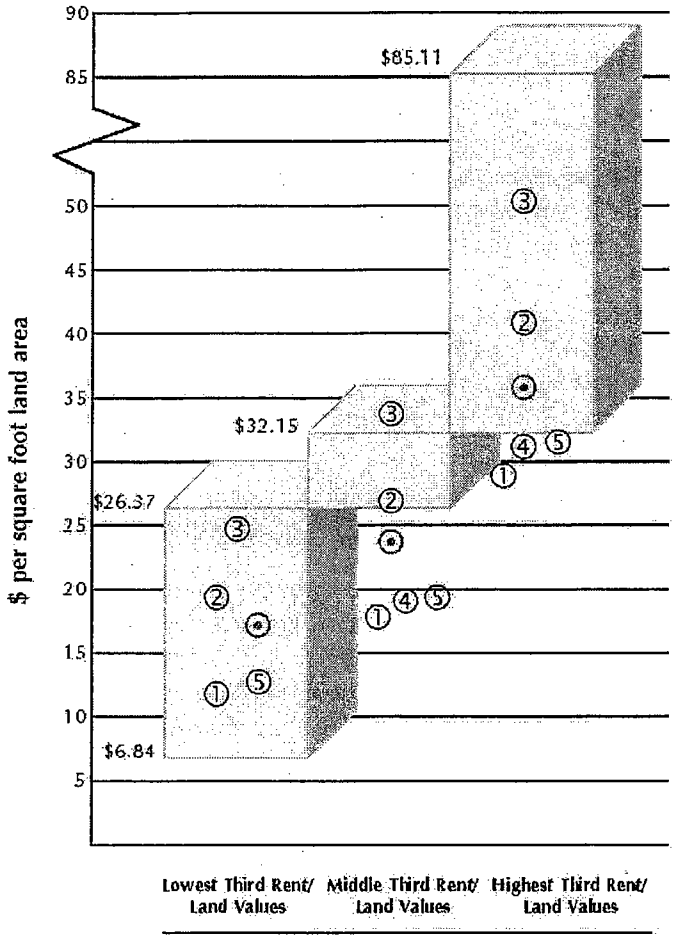
Chart 4 illustrates one set of land residual value findings applying this methodology to the City of Los Angeles. A rental residential development prototype is shown in this chart: a 30-unit infill project of stacked flats at 25 units to the acre with covered parking at grade. In this case, the market-rate prototype in the lowest third of land comparable values and rents for Los Angeles yields a residual land value of approximately $17 a square foot. Setting aside 10 percent of the units affordable to families at 45 percent of the 2003 area median income (approximately $25,000) yields a residual land value of $12 a square foot, with no offsets. A 25 percent density bonus, as required by California state law, yields a residual land value higher than the market-rate prototype: $20 a square foot. For middle-tier rents and land values, the market-rate prototype yields a land value slightly below land comparables, and suggests that a developer/buyer and land seller may not come to terms on land price for this project. However with the affordable set-aside of inclusionary housing and a 25 percent bonus, land value increases above that for the market-rate project to competitive prices ($27 a square foot).

For the Los Angeles analysis, most of the 10 prototypes analyzed yielded market comparable land values. Exceptions were adaptive reuse of existing commercial buildings, where no density bonus or parking concessions could reasonably be applied, and high-rise steel frame construction where luxury rents and home prices where not modeled. Los Angeles has seen no high-rise steel frame construction housing in recent years, with the exception of Marina Del Rey, a luxury oceanfront location.

Los Angeles Inclusionary Housing Economic Impact Analysis
Land Residual Values Based on Alternative Incentive/Compliance Options

Chart 4

Renter Prototype:
Type V Low Density Construction



KEY: Incentive/ Compliance Options *

① No offsets

② 25% density bonus; fee deferrals; affordable unit modifications

③ 50% density bonus; fee deferrals; affordable unit modifications

④ Off-site compliance; fee deferrals; affordable unit modifications

⑤ Multifamily acquisition/ rehabilitation compliance; fee deferrals

⊙ Market-rate prototype

The $6.84-$85.11 represents actual land sale comparables in Los Angeles for residential projects permitted in 2001.

* All options require 10% of total units to be affordable to households at 45% of the area median income; approximately $25,000 for a household of four in Los Angeles, 2002.

Chart prepared for the Los Angeles Housing Department.

DAVID PAUL ROSEN & ASSOCIATES

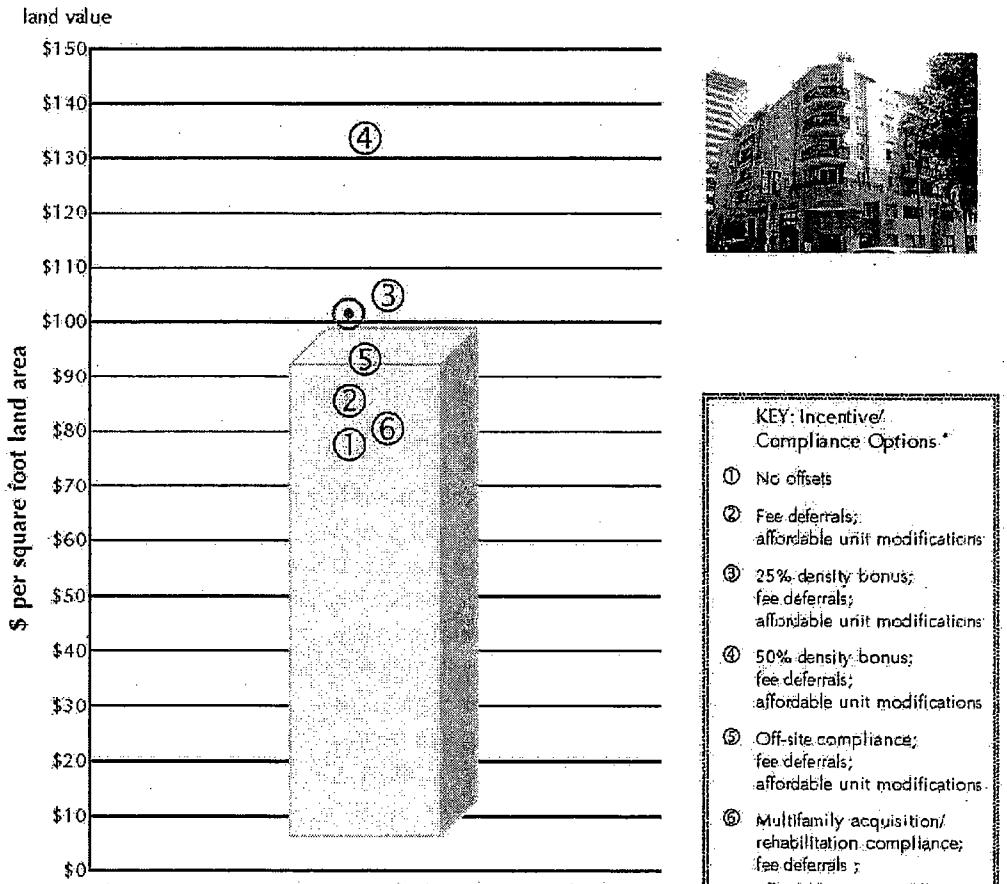
Prototype: Long Beach

Similar results were found for a comparable study in the City of Long Beach. **Chart 5** shows an owner condominium prototype of Type V stack flat condominium construction at 70 units to the acre with one level of subterranean parking. Here, the affordability set-aside is 15 percent of the units at 90 percent of the area median income, or $50,000 for a family of four in Long Beach in 2003. The market-rate prototype, without inclusionary requirements, yields a land value of $100 a square foot, slightly above the top of the range of recent land sales in the City. The set-aside requirement, with no offsets, reduces land value to approximately $78 a square foot, still near the top of the range of land sale comparables in Long Beach. When incentives and/or offsets are added, land values approach, and exceed, the market-rate prototypes' land value.

Long Beach Inclusionary Housing Economic Impact Analysis
Land Residual Values Based on Alternative Incentive/Compliance Options

Chart 5

Owner Prototype:
Type V Stacked Flat Condos



KEY: Incentive/ Compliance Options *

① No offsets

② Fee deferrals; affordable unit modifications

③ 25% density bonus; fee deferrals; affordable unit modifications

④ 50% density bonus; fee deferrals; affordable unit modifications

⑤ Off-site compliance; fee deferrals; affordable unit modifications

⑥ Multifamily acquisition/ rehabilitation compliance; fee deferrals ; affordable unit modifications

⑦ 100% Market-Rate Units

The bar represents actual recent residential and planned development land sales comparables and appraised values in Long Beach between 1998 and 2003 ranging between $13 to $99 per square foot. When the bulls-eye and numbered dots fall within the bar areas, the residual land values generated by the prototype and "package" option are within the range of recent land sales comparables in Long Beach, and should generally be reviewed as financially feasible.

* All options require 15% of total units to be affordable to households at 90% (45% for package 6) of the area median income; approximately $50,000 for a household of four in Long Beach, 2003.

Chart prepared for the Long Beach Housing Services Bureau.

In both the Los Angeles and Long Beach analyses, it is important to note that conservative (i.e., high) assumptions regarding developer profit, overhead and interest rates were used. Developer profit and overhead was modeled at 16 percent; construction and permanent interest rates were modeled at 8.5 percent and eight percent respectively. Developer profit is often acceptable as low as eight percent and market interest rates as of this writing are more than two points lower than that modeled. Thus, land residual values are understated, as is the economic feasibility of the inclusionary housing set-asides shown.

Furthermore, holding developer profit constant in this illustration has the effect of assuring an acceptable profit margin. In the real world of land sellers (land owners) and land buyers (developers), land price is a delicate negotiation between the two parties, each seeking to maximize their own profit. If development costs, be they associated with construction interest rates, the price of lumber or steel or the projected costs of inclusionary obligations, are excessive, land buyers and sellers may agree to part company without concluding a sale. We have shown an approach to balance the cost of inclusionary housing obligations against the economic value of a variety of incentives, offsets and alternative compliance provisions. When the combined effect of such costs and incentives does not reduce current comparable land values by more than 10 to 20 percent, the policy package may be deemed economically feasible in a given jurisdiction. Land prices, with no public sector intervention whatsoever through the zoning or regulatory process, readily fluctuate 10 to 20 percent in any given rolling 12-month period. Thus, a projected effect of 10 to 20 percent on land values may be seen as operating within the normal limits of real estate land values within relatively short business cycles.

The land residual value methodology applied to inclusionary housing economic analysis helps policymakers and stakeholders craft inclusionary housing set-aside requirements which maximize the yield of affordable units without unduly restricting land value or developer profit.

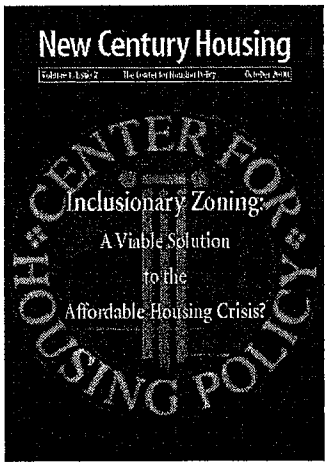
Real estate development is a customized process. No project is the same. Thus, citywide analysis may only be properly modeled through prototypes fully representative of the range of housing product developed in that jurisdiction. Political constraints may also restrict the application of various incentives or alternative compliance provisions for an inclusionary housing program. For example, while a density bonus may be offered, if limits on height, floor area ratio or set backs render such a density bonus unusable, it will prove of little value to developers. Similarly, if neighborhood or political opposition forces developers to scale back or eliminate their projects, then prototypical analysis becomes an academic exercise. Development, like politics, is the art of the possible.

Nevertheless, empirical analysis uncovers no chilling effect of inclusionary housing on California jurisdictions which have adopted the program. More importantly, the land residual economic methodology shows that policymakers can craft inclusionary programs which fall within the range of economic feasibility.

Long-term, perhaps no other single local housing policy is more valuable in the production of affordable housing. For the period 1981 through 2001, approximately 190,000 units were built in Los Angeles. If the City had a 15 percent set-aside requirement, throughout that time, 28,500 units of affordable housing would have been constructed.

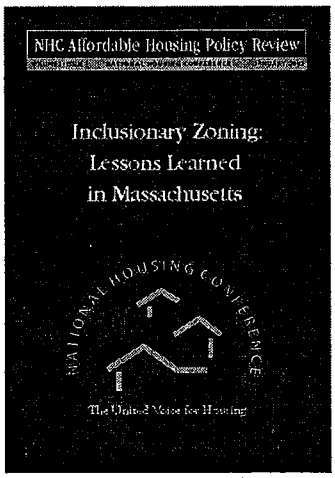
Additional National Housing Conference Inclusionary Zoning Publications

The following reports are available online at *www.nhc.org.*



Inclusionary Zoning: A Viable Solution to the Affordable Housing Crisis?

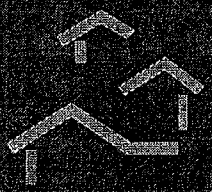
This issue of *New Century Housing* focuses on inclusionary zoning as a tool that could be applied at the state or local level to address affordable housing needs and highlights the steps taken to implement inclusionary zoning policies in Montgomery County, Maryland.



Inclusionary Zoning: Lessons Learned in Massachusetts

This issue of *NHC Affordable Housing Policy Review*, a collaborative effort between the National Housing Conference and the Massachusetts Housing Partnership Fund, explores the issue of inclusionary zoning by reviewing the experiences of select cities and towns in Massachusetts where inclusionary zoning has been used to produce affordable housing.

The contributing authors of both publications represent some of the best minds on the topic of inclusionary zoning. They include academics, local program administrators, as well as housing developers. Their differing perspectives help to provide a balanced view of the strengths, weaknesses, successes and limitations of this approach.



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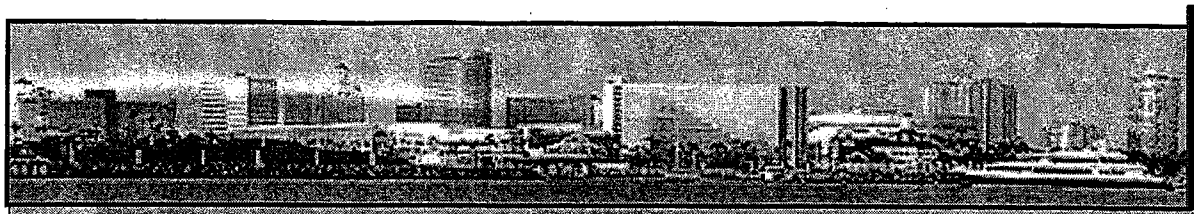
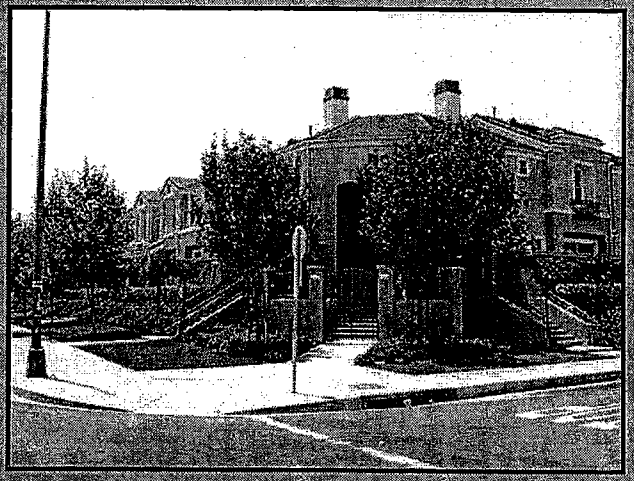
P.U. Union Bug

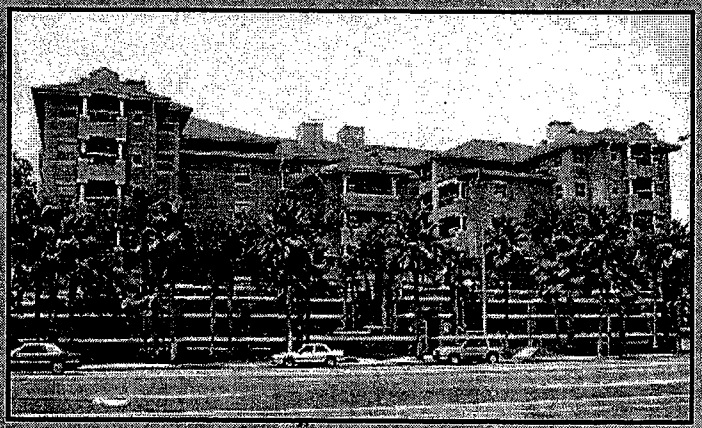




CITY OF LONG BEACH
HOUSING ACTION PLAN

FY 2005-2009

ADOPTED JUNE 2004



CITY OF LONG BEACH
DEPARTMENT OF COMMUNITY DEVELOPMENT
HOUSING SERVICES BUREAU
110 PINE AVENUE, SUITE 1200
LONG BEACH, CA 90802

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I. INTRODUCTION

A. DIRECTOR'S MESSAGE

Over the last several years, the City of Long Beach has invested millions of dollars in its neighborhoods, especially in our lower-income neighborhoods. Because of that investment, many of our citizens enjoy a better quality of life. The City's Single-Family and Multifamily Rehabilitation Loan Programs have been responsible for the rehabilitation of about 5,000 housing units in Long Beach. Using federal and redevelopment funds, over 200 new affordable units have been developed, 75 units acquired and rehabilitated, and 2,030 households assisted in becoming new homeowners over the past decade. The City also continues to invest in infrastructure improvements and social service programs. But in spite of these investments, it is apparent that the quality of some of our neighborhoods has been in decline. Many would say that certain of our neighborhoods are deteriorating, and that this deterioration may expand to impact our more stable neighborhoods.

Many residents do not understand the severity of the affordable housing crisis in Long Beach. Many think that if we provide affordable housing, the poor people would come. The reality is that there are many poor people who are already here in Long Beach. In fact, Long Beach ranks 10th in the nation in terms of the percentage of our population earning less than the poverty level. On the other hand, many think that if we do not build it, the poor people would go away and find a place somewhere else. However, if nothing is done to address the housing crisis, the problems we face will get worse – housing units will be more overcrowded and neighborhoods will deteriorate much faster. It is our responsibility to assist in providing safe, decent and affordable housing to this population. Otherwise, the effects of not doing so will be evident in our neighborhoods.

The City must adopt a strategy to reverse this trend. Such a strategy will require addressing the needs of a large percentage of our population that is very low-income and living in crowded substandard conditions, and at the same time, supporting our strong middle-class neighborhoods.

The City has very limited resources to tackle a seemingly insurmountable task. But if our resources are utilized in a carefully planned and focused fashion, real change can be expected over a period of time. And that's the reason we developed a Housing Action Plan, a plan that can serve as the framework for the allocation of scarce housing resources, with the end in view of maximizing the utilization of these resources to benefit as many of our residents who have the