

**TO:** Andrew P. Powers, City Manager

**FROM:** Kelvin Parker, Community Development Director

**DATE:** February 28, 2023

**SUBJECT:** Inclusionary Housing Program and Nonresidential Development Linkage Fee Update Policy

**RECOMMENDATION:**

1. Discuss the Inclusionary Housing Financial Evaluation and Nonresidential Development Linkage Fee Nexus Study results.
2. Provide direction on completing updates to the Inclusionary Housing Program and Nonresidential Development Linkage Fee ordinances.
3. Find that this action is not a Project as defined under the California Environmental Quality Act.

**FINANCIAL IMPACT:**

**No Additional Funding Requested.** Staff time required to prepare the report and \$206,000 is included in the Adopted FY 2022-23 General Fund Budget for the Inclusionary Housing Program and Nonresidential Development Linkage Fee Update consultant contract.

**BACKGROUND:**

Inclusionary housing describes a local government requirement that a specified percentage of new housing units be reserved for, and affordable to, lower- and moderate-income households. The goal of inclusionary housing programs is to increase the supply of affordable housing commensurate with new market-rate development in a jurisdiction. This can result in improved regional jobs-housing balance and foster greater economic diversity within a community.

Nonresidential development linkage fees provide a mechanism for producing housing affordable to extremely low-, very low-, low-, and moderate-income households by requiring applicable nonresidential development to pay an impact

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fee to be used for the production, preservation, or rehabilitation of affordable housing units.

On November 1, 2022, City Council discussed and provided initial direction for an update to the Inclusionary Housing Program Update Parameters and Policy (Attachment #1). After City Council received a presentation on the general framework and policy considerations, Keyser Marston and Associates (KMA) facilitated City Council's discussion and initial direction for an Inclusionary Housing Financial Evaluation (Attachment #2). During the meeting City Council considered the following:

1. What will be the minimum residential or mixed-use project sizes that will trigger the Inclusionary Housing requirements?
2. What target income and affordability standards are to be applied?
3. What are the allowable options for fulfilling the Inclusionary Housing requirements with at least one alternative other than on-site production of affordable housing?
  - a. Providing the Inclusionary Housing units within the market rate project that triggered the requirement.
  - b. Priority for production of Inclusionary Housing units within multi-family developments.
  - c. Production of the Inclusionary Housing units in an off-site location.
  - d. A payment to the City in-lieu of producing required Inclusionary Housing units.
  - e. Dedication of land to the City for the subsequent development of the required Inclusionary Housing units.
  - f. The acquisition and rehabilitation of existing apartment units to be Inclusionary Housing units.

City Council provided comments generally summarized as follows:

Apartment Projects

- Require on-site production of lower income categories in residential developments;
- Explore a minimum inclusionary requirement of 10 percent or greater of total units in a project;
- Explore applicability of inclusionary housing to projects of five units or more;
- Do not allow apartment developments the option for offsite production of affordable units;
- Explore allowing in-lieu fee as an option on a sliding scale;
- Explore acquisition/rehabilitation of existing units; and
- Do not allow land dedication as an option.

Ownership Housing Projects

- Explore preference for on-site production;
- Explore a minimum inclusionary requirement of 10 percent of total units in a project;
- Test the financial feasibility for both low- and moderate-income categories;
- Explore option for ownership housing project to include on-site parcel with apartment development;
- Explore option for off-site ownership or apartment development;
- Explore in-lieu fee payment on sliding scale based on project size and ownership type; and
- Do not allow land dedication as an option.

On January 25, 2022, City Council adopted the 2021-2029 Housing Element, which includes implementation actions for facilitating the development of affordable housing. Program 6 of the Housing Element contains an implementation objective that requires an update to the Inclusionary Housing Program and Nonresidential Development Linkage Fees ordinances.

Nonresidential Development Linkage Fees History

In 2008, the City adopted an ordinance creating affordable Housing Programs including the Housing Trust Fund, Inclusionary Housing Program, Nonresidential Linkage Fee Program, and Density Bonus Program. The Nonresidential Development Linkage Fee Program established fees applied to nonresidential development in order to mitigate the demand for affordable housing in the City caused by new employment resulting from development (TOMC Section 9-10.401 et seq). This ordinance required payment of fees for developments of 7,500 square feet or more of new gross floor area. The fees were initially set at the following rates:

- Commercial/ Retail - \$ 4.50/square foot building area (s. f.)
- Office - \$ 2.50/ s. f.
- Hotel/ Lodging - \$ 2.50/ s. f.
- Industrial - \$ 0.00/ s. f.
- Research & Development Flex Space - \$ 0.00/ s. f.

In 2009, City Council set the in-lieu and linkage fees at zero based on the market conditions at the time. Therefore, new residential projects were not required to provide a specified number of affordable units and nonresidential developments were not required to pay a linkage fee.

Before local agencies can adopt an inclusionary housing in-lieu fee, a market analysis and feasibility study are necessary to inform the decision-making body what the market can feasibly accommodate and the appropriate amount to incentivize construction of affordable housing. As a development impact fee, a

Linkage Fee may legally only be established when there is a demonstrated nexus (reasonable relationship) between the fee and the development's impacts. In this case, the employment growth of a commercial development will have an impact/reasonable relationship with the unmet housing needs in a community.

### **DISCUSSION/ANALYSIS:**

KMA completed a financial evaluation (Attachment #2) to identify the initial parameters for the update to the Inclusionary Housing Program. The report begins by explaining key legislation and the legal standards for Program considerations. Then the report presents the various parameters to be considered and explains the methodology to determine feasible levels of those parameters. KMA then conducted analyses on both ownership and rental developments to create prototypes representative of development types in Thousand Oaks to recommend parameter levels.

KMA performed initial community outreach with stakeholders from the residential, business, and development community on Inclusionary Housing and Nonresidential Development Linkage Fees. While there was general support for the application of Inclusionary Housing requirements applied to new residential development, the feedback on the possibility of reintroducing a linkage fee for nonresidential development was generally not supported by the business community.

### **Inclusionary Housing Analysis and Recommendations**

Based on the financial evaluation, KMA considered City Council's initial parameter direction when performing the evaluation of those parameters in prototype scenarios. The recommendations for income and affordability standards are the following:

#### **Applicability**

- Apartment and Ownership projects consisting of 10 or more units

#### **Apartment Housing Development**

- Affordable Housing Percentage Requirement
  - Require 10 percent of a project to be dedicated for Low-Income Households
- Fulfillment Options
  - Allow an In-lieu fee payment for projects with 20 or fewer units
  - Allow the discretionary imposition of an In-lieu fee based on extreme hardship for apartments of more than 20 units
  - No off-site production
- Require affordability covenants for 55 years or more, as long as property

was residential use

#### Ownership Housing Development

- Affordable Housing Percentage Requirement
  - Require townhomes (Ownership) to provide 10 percent of the project to be affordable at a Moderate Income level
  - Require Detached Single Family Home Projects to provide 5 percent of the project to be affordable at a Moderate Income level
- Fulfillment Options
  - Allow an In-lieu fee by right for ownership development of any size
  - Allow an option for ownership projects to meet their affordability requirement by providing affordable apartment housing production in an off-site project
  - Allow an option for ownership projects to provide on-site parcels that require concurrent construction of affordable apartment units
- Require an affordability covenant for a 45-year cumulative period

#### Nonresidential Development Linkage Fee Analysis and Recommendation

KMA prepared two analyses for purposes of analyzing linkages between nonresidential development and the demand for additional affordable housing. To provide a recommendation regarding the Nonresidential Linkage Fee, the Nexus Study (Attachment # 3) identifies the maximum legally supportable amount for a linkage fee, and the Financial Feasibility Report provides a maximum financially supportable fee amount (Attachment # 4). KMA prepared pro forma analyses for five nonresidential development prototypes that might be developed in Thousand Oaks: retail/commercial; office; industrial; research and development; and hotel/lodging. These prototypes test the affordability gaps associated with providing housing at various income levels. The “affordability gap” measures the differences between what affordable households can afford to pay for housing and the cost of building rental and ownership housing.

Cities with linkage fees often establish them at an amount below the maximum justifiable level as a matter of policy to remain competitive in their marketplace and reduce the risk of legal challenges.

The Nexus Study identifies the reasonable relationship between the impact of a project and proposed fee which provides a legal basis for establishing a linkage fee for new nonresidential development. The Study identifies the legally supportable maximum fees range from \$60 per square foot for industrial to \$162 per square foot for office which would represent the full cost for creating the needed affordable housing. This fee analysis does not consider the impact on the financial feasibility of new development. However, in order to establish balance between

the policy objectives to produce affordable housing and the economic impact experienced by developers, a financial feasibility analysis assesses the impact of the proposed impact fee.

As part of the conclusions of the financial feasibility analyses, the industrial prototype was the only nonresidential development scenario that resulted in a financially feasible estimated return on investment with a linkage fee of \$1 - \$5 per square foot (Attachment #4). However, it is important to note that based on threshold return requirements established by KMA, the retail/commercial, office, research and development, and hotel prototypes did not demonstrate an ability to realize a return on investment even without the application of a linkage fee (Attachment #4 pages 2-4 Financial Feasibility Nonresidential Development Linkage Fees section).

KMA examined fees of neighboring jurisdictions and cities in California with similar business compositions in terms of fee amounts and the fees' relative cost burden on new nonresidential development. When considering the real estate market and policy objectives towards producing affordable housing, KMA studied a possible fee range of \$0 to \$5 per square foot for each of the five nonresidential building types. However, staff recommends City Council apply the fee only to Industrial uses at this time due to the infeasible rate of return for the other use types.

### Recommendation Summary

Staff recommends that City Council move forward with all recommendations in the analysis and recommendations sections above to update the Inclusionary Housing Program and Nonresidential Development Linkage Fee based on the following general applicability:

- Apartment and ownership projects consisting of 10 or more units
- Industrial projects

### Next Steps

Based on City Council direction for implementation of the Inclusionary Housing Program and Nonresidential Development Linkage Fee, staff will return with a proposed ordinance for City Council's consideration at a future meeting.

### **COUNCIL GOAL COMPLIANCE:**

Meets the following City Council goals:

A. Create a more equitable, accessible, safe, welcoming, and inclusive government and community regardless of race, color, ethnicity, religion, sex, physical or mental ability, sexual orientation, gender identity and expression, age,

language, education, and/or socio-economic status.

B. Provide municipal government leadership which is open and responsive to residents, and is characterized by ethical behavior, stability, promoting public trust, transparency, confidence in the future, and cooperative interaction among civic leaders, residents, business representatives, and staff, while recognizing and respecting legitimate differences of opinion on critical issues facing the City.

J. Implement high quality revitalization projects within Thousand Oaks Boulevard and Newbury Road Areas; Develop a pedestrian-oriented, viable, and self-sustaining "Downtown;" and, continue to support production of long-term affordable housing.

**PREPARED BY:** Iain Holt, Senior Planner

**Attachments:**

Attachment #1 – November 1, 2022, City Council Staff Report and Presentation

Attachment #2 – Inclusionary Housing Financial Evaluation

Attachment #3 – Nonresidential Development Linkage Fee Nexus Study

Attachment #4 – Financial Feasibility Analysis of Nonresidential Development Linkage Fees