Housing and Homelessness Committee Memorandum

City of Arts & Innovation

TO: HOUSING AND HOMELESSNESS COMMITTEE MEMBERS **DATE: MAY 23, 2022**

FROM: OFFICE OF HOMELESS SOLUTIONS **WARDS: ALL**

SUBJECT: UPDATE ON CITY OF RIVERSIDE INCLUSIONARY HOUSING PROGRAM FEASIBILITY STUDY

ISSUE:

Receive an update related to the City of Riverside Inclusionary Housing Program study and preliminary recommendations for elements of a potential inclusionary housing ordinance.

RECOMMENDATIONS:

That the Housing and Homelessness Committee:

1. Receive an update on the Inclusionary Housing Program Study for the City of Riverside, including preliminary recommendations on elements of a potential inclusionary housing ordinance; and

2. Provide direction on the recommendations listed in Attachment 4 to be included in an Inclusionary Housing Ordinance to be considered by the City Council.

BACKGROUND:

In recent years, the State of California has identified the shortage of housing, particularly affordable housing, as a legislative priority. A housing shortage impacts the State's economy, contributes to homelessness, and results in long commutes, increasing production of greenhouse gas emissions, air pollution, and poor public health. Affordable housing is defined as rent/utilities or mortgage/taxes/insurance/utilities that cost 30% or less of the gross household income and are available to persons who earn at or below 80% of the Area Median Income (or $63,200 for a family of four in 2021). The State further delineates affordability levels for “low-income” households, earning between 50% and 80% of the Area Median Income; and for “very-low income” households, earning between 30% and 50% of the Area Median Income. The State also defines households earning “moderate incomes,” between 80% and 120% of Area Median Income.

Facing a rise in local rents and housing costs, a steady rise in homelessness, and a decrease in homeownership associated with the high cost of housing, on May 18, 2021, the City Council and Housing Authority Board authorized the award of an Agreement with Economic & Planning

Systems, Inc., (EPS) to explore the possibility of implementing an inclusionary housing policy in the City of Riverside.

By definition, inclusionary housing policies are local policies that could require developers to sell or rent a percentage of new residential units to lower-income residents or pay an in-lieu fee to support the development of such units. To offset the cost of providing affordable housing in all new projects, an Inclusionary Housing Program can offer incentives to developers in the form of zoning concessions such as reduced parking, density bonuses, or tax abatements. Developers can also be given an option to choose an alternative to providing the affordable units in the form of in-lieu fees or providing affordable units at an alternate location. Inclusionary Housing Programs can include both for-sale and rental units and are often implemented through the jurisdiction' s zoning code.

On September 28, 2021, City staff and EPS presented to the Housing and Homelessness Committee the initial analysis of the development feasibility impacts of a range of inclusionary policy alternatives on new market-rate residential development. At that meeting, the Committee directed Housing Authority staff and EPS to proceed with the next steps of the study, including stakeholder and community outreach.

On February 28, 2022, City staff and EPS presented to the Housing and Homelessness Committee on refined analysis of development feasibility impacts of a range of inclusionary policy alternatives on new market-rate residential development, as well as stakeholder outreach undertaken as part of the study effort. City staff and EPS provided the Housing and Homelessness Committee with recommendations for a potential inclusionary housing requirement for the City. At the meeting, the Committee provided guidance on several elements of a potential inclusionary housing program and directed City staff and EPS to develop a draft inclusionary housing policy for Committee consideration and discussion.

DISCUSSION:

Nexus Study

At the City’s request, EPS has prepared a nexus study that illustrates the impact that new market-rate housing can have on the need for affordable housing. The relationship is based on the idea that the occupants of new housing units in Riverside will require goods and services, and the number of employees needed to provide those goods and services can be expected to grow accordingly. Based on the typical incomes of workers in the retail and service industries, many workers will qualify for housing at moderate- or lower-income pricing. The scale of this increased demand will be affected by the incomes of the occupants of the new market-rate housing units, because higher-income households tend to spend more, creating more service industry jobs than available workers.

Using prevailing market-rate pricing for apartments, single-family attached homes (or townhomes), and single-family detached homes in Riverside, EPS estimated the incomes required to rent or purchase such units, and then applied consumer expenditure survey data to those income levels to estimate the new household spending and therefore revenues that would be expected in different types of businesses. EPS then used established industry-specific ratios of revenues to wages to estimate the number of employees that would be added in the local economy.

Not every employee will form a unique household, as many will live with another working adult and others at younger ages may be expected to still live with their parents, so the number of new households attributed to this new spending is well below the number of new employees. The estimated incomes of those new employee-based households determine the proportion of affordable housing demand that can be attributed to new market-rate housing growth.

For example, a household buying a typical new single-family detached home in Riverside is likely to earn about $129,000 based on the average home price of $625,000. That same household can be expected to spend about $6,600 annually eating at restaurants ("food away from home"), so 1,000 such households (scaled up to make the math more understandable) would spend about $6.6 million in that category. That spending would support roughly 95.4 workers in "food services and drinking places," and those workers can be expected to form roughly 41.7 households that would qualify as "low income." Similar relationships in other spending categories determine the aggregate impact that the typical new homebuying households are likely to have on demand for affordable housing in Riverside.

The inclusionary housing nexus study supports the following inclusionary requirements:

- *Multifamily*: 12.6% total, including 8.0% of units affordable to low-income households and 4.6% of units affordable to moderate-income households

- *High-Density/Attached Single Family (e.g., Townhomes)*: 10.6% total (rounded), including 6.4% of units affordable to low-income households and 4.3% of units affordable to moderate-income households

- *Low-Density/Detached Single Family*: – 14.4% total, including 9.1% of units affordable to low-income households and 5.3% of units affordable to moderate-income households

The nexus study further details and informs discussions regarding the appropriate proportions and income levels for the inclusionary housing ordinance.

If the City moves forward with an Inclusionary Housing Ordinance, these inclusionary requirements would be codified in Title 19 – Zoning. However, there is no legal obligation for the City to constrain itself to the results of the nexus study, as inclusionary housing ordinances have not been subject to the requirements of the Mitigation Fee Act and are authorized and recognized by State and case law as an allowable expression of the City's "police powers" to regulate development in the public interest.

Inclusionary Housing Ordinance Elements

EPS and City staff have been collaborating on a draft inclusionary housing ordinance for consideration by the Planning Commission and City Council. There are several elements of the ordinance that require additional decisions by the Committee, as detailed below:

1. Inclusionary Requirements

Decision Point: What will be the inclusionary requirements (percentage of unit, affordability level) be for different residential development types?

Options: EPS's feasibility analysis looked at four types of residential products: low-density single-family, high-density single-family (aka townhomes), mid-density multifamily, and high-density multifamily. The feasibility analysis was conducted at a variety of inclusionary percentage and affordability levels (see Attachment 1, Figures 1-3), which indicated that multifamily rental and higher-density single-family attached projects (e.g., townhomes) are more likely to be able to support inclusionary units than are lower-density single-family detached projects

EPS also looked at the inclusionary requirements of other cities in and around the Inland Empire, as illustrated in Attachment 2, Figures 4 and 5.

The City can adopt any mix of percentages and levels desired, including those not analyzed by EPS, but the ordinance may be subject to review by the California Department of Housing and Community Development (HCD) if the inclusionary standards exceed 15% of units at low income.

Recommendation: Based on EPS's market and development feasibility analysis, the following recommended inclusionary requirements were provided at the February 28, 2022 Housing and Homelessness Committee Meeting:

Development Type	% of Units	Affordability Level
Multifamily	10%	Low-income 70% of Area Median Income (AMI)
High-Density Single Family (e.g., Townhome)	10%	Low-income 70% of AMI
Low-Density Single-Family	5%	Moderate-income 110% of AMI

**These requirements would automatically qualify projects for use of State density bonus*

These suggested levels are also within the demand-based parameters established through the nexus study. At these levels, Riverside's inclusionary standards would generally fall within the range of other Southern California jurisdictions surveyed but would be on the lower/less aggressive end of that range.

2. Exemptions to Inclusionary Housing Requirement

Decision Point: Should there be projects that are exempt from the inclusionary housing requirement?

Options: Many cities exempt new residential projects under a certain unit size from inclusionary housing requirements. For example, in the City of Pomona, projects with fewer than three (3) dwelling units are exempt from inclusionary housing requirements. Other cities exempt projects with fewer than six units, or fewer than ten units. Depending on the adopted inclusionary housing percentage, smaller projects may only be required to provide a fraction of a unit; in this case, many cities allow the project to pay an in-lieu fee on the fractional unit required.

It is also common to exempt projects that are at a certain stage in the development process at the time of adoption of the inclusionary housing ordinance, in recognition that the developer was not able to factor the requirement into their financial considerations before submittal. For example, the City may exempt any project that has submitted a complete application by the time of adoption or other effective date, and only any new application after that time would be subject to the requirement.

Recommendations:

1. Exempt residential projects with fewer than three units from the inclusionary housing requirement.
2. Exempt residential projects that have submitted a complete application (i.e., the project is ready to be considered by the approval authority) by the effective date of the inclusionary housing ordinance.

3. Affordability Term

Decision Point: What is the minimum term (in years) of affordability for affordable units?

Options: Most inclusionary programs set a minimum amount of time that affordable units must stay affordable. Some options for these terms include:

- For rental units, a typical affordability term is 55 years including in State density bonus law, although some cities have longer terms.
- For for-sale units, there are several options:
    - The City can set an affordability term – for example, 45 years, which is the standard in State density bonus law – and limit the re-sale of the unit to income-qualified households for the duration of that term
    - The City can set the affordability term to renew each time the unit is sold.
    - The City can decline to set an affordability term, but rather require an "equity sharing agreement" on the unit. This would allow the income-qualified buyer to sell the unit at market rate. However, the City would recoup some portion of the sale price, which could be reinvested into new affordable housing. The benefit of this approach is that it allows lower-income households to benefit from building equity in the unit. The drawback is that once the unit is sold, it is no longer part of the City's affordable housing stock and the City's share of the equity from the unit's resale may be inadequate to subsidize that unit's replacement.

Recommendation: Set an affordability term of 55 years for rental units and 45 years for for-sale units. This approach aligns with State density bonus law.

4. Size of Affordable Housing Units

Decision Point: Can required affordable housing units be smaller than market-rate units?

Options: The Housing and Homelessness Committee provided direction that inclusionary housing affordable units should be similar to market-rate units in terms of finishes, features, and access to amenities. Many cities have similar requirements but do allow for developers to build affordable units that are slightly smaller (e.g., 10 percent smaller) than the average market-rate unit. For example, this flexibility is allowed in the inclusionary housing ordinances in the cities of Pomona and South Pasadena.

Recommendation: For multifamily rental projects, require on-site or off-site affordable units to reflect the mix of market-rate units (e.g., same proportion of one-bedrooms, two-bedrooms, etc.) and have net leasable areas of at least 90 percent of the average size of the market-rate units of similar bedroom counts.

5. For-Sale Projects Meeting Requirement with Affordable Housing Rental Units

Decision Point: Can for-sale projects meet their inclusionary housing requirement by developing affordable housing rental units?

Options: Under the premise that rental multifamily units may be the most cost-effective format for providing affordable housing, some cities allow developers of for-sale single-family residential projects to meet their inclusionary requirement by building affordable rental units, either on the same site as the market-rate project or elsewhere in the City. Both the cities of South Pasadena and Pomona provide this option.

If this option is used, the City can require that the number of affordable rental units is equal to the number of affordable for-sale units that the developer would have been required to build; or they can require that the number of affordable rental bedrooms is equal to the numbers of affordable for-sale bedrooms that the developer would have been required to build if they had built units similar to the market-rate units. For example, if a for-sale project includes 100 four-bedroom homes, and the inclusionary requirement is 10%, the project would be required to provide 10 affordable units. If they are built as four-bedroom homes, that would equal 40 affordable bedrooms. If the developer built affordable rental units instead, they could be required to build 40 affordable bedrooms in any configuration (e.g., 20 two-bedroom rental units or 40 one-bedroom units), rather than 10 affordable four-bedroom rental units.

Recommendation: Allow for-sale projects to meet their inclusionary requirement by building affordable rental units on the same site as the market-rate project or elsewhere in the City within reasonable proximity of the primary project (see below). Allow the requirement to be met by providing the required number of affordable bedrooms in any configuration, rather than the required number of units similar in size to the market-rate units.

6. Off-Site Affordable Housing Units

Decision Point: Can residential projects meet their inclusionary housing requirement by providing affordable housing units off-site?

Options: Some cities allow developers to meet their inclusionary requirement by building affordable units elsewhere in the City, rather than as part of the market-rate project. In some cases, the inclusionary requirement is higher if the units are built off-site. For instance, the City of Pomona requires that 13 percent of units are affordable to moderate-income households if built as part of the market-rate project, but if the affordable units are built off-site, the number of affordable units must be equivalent to 15 percent of the market-rate units and must be affordable to low-income households.

Some cities also require that the off-site affordable units be within a maximum distance from the market-rate project (e.g., within two miles), and that the off-site affordable units cannot be built in an area with an "overconcentration" of existing affordable units. For example, the City of Pomona's inclusionary housing ordinance specifies that "The inclusionary units shall not create an overconcentration of deed restricted affordable housing units in any specific neighborhood. For purposes of this section, "overconcentration" is defined as more than 50 deed restricted very low or low-income dwelling units within ¼ mile of the site of the proposed inclusionary units, or more than 200 of such units within ½ mile of the site of the proposed inclusionary units.

Recommendation: Allow developers to meet their inclusionary housing requirement by providing affordable housing units off-site. Require that the number of off-site affordable housing units be equivalent to a higher proportion of the market-rate units than if the inclusionary requirement is met on-site. Define a maximum distance from the market-rate project site for the off-site affordable units. Develop a definition of overconcentration and restrict the development of off-site affordable units to prevent overconcentration of these units.

7. In-Lieu Fee

Decision Point: Are there any limitations on when a project can pay an in-lieu fee instead of providing on-site or off-site affordable housing units?

Options: The City is required to provide alternative means of compliance with the inclusionary housing requirement. An in-lieu fee is a common alternative means, and EPS has calculated the in-lieu fees that would be aligned with the recommended inclusionary requirements (and can re-calculate depending on the requirements adopted). While some cities allow for any residential market-rate project to pay an in-lieu fee instead of providing affordable units, others place limitations on when an in-lieu fee can be paid. Some common limitations include:

- In-lieu fee can only be paid on fractional required affordable units (e.g., a 12-unit project with a 10% requirement would build one affordable unit and pay the in-lieu fee on the additional 0.2 required units).
- In-lieu fee can only be paid by projects of a particular size (e.g., smaller than certain number of units) or particular type (e.g., only for-sale projects or only rental projects)

The City also has the discretion to set the in-lieu fee at a level that would incentivize the development of affordable units rather than payment of the fee. For example, the on-site inclusionary requirement could be 10% of units at low income, but the off-site requirement and in-lieu fee could be calculated to reflect 12% of units at low income.

During the stakeholder outreach with market-rate and affordable housing developers alike, there was significant interest in allowing in-lieu fees liberally. The market-rate developers believed that fee payments would be less financially onerous, and affordable housing developers indicated that such fees could provide much-needed local matching funds to support their overall financing efforts. However, the City would need to weigh this interest in fee generation with the trade-offs of not having affordable units built at the same time and in the same locations as the market-rate units paying the fees.

Recommendation: Allow payment of an in-lieu fee only for fractional units required for multifamily and townhome projects but allow in-lieu fees for all inclusionary housing units required for single-family detached projects of any size.

8. Other Alternative Means of Compliance

Decision Point: What other alternative means of compliance will the City allow?

Options: In addition to the in-lieu fee, other common alternative means of compliance include:

- Land dedication, often within a certain distance of the market-rate project;
- Acquisition and rehabilitation of existing units to be rented or sold at affordable levels; and/or
- Extension of affordability covenants on existing affordable units.

These alternative means are often allowed on a discretionary basis, to be determined by the City Council or other body. The deliberation to accept or reject such alternative means frequently involves both qualitative and quantitative considerations, ultimately resulting in a determination that the alternative means equals or exceeds the “value” of the standard inclusionary requirement. In this case, the perceived “value” can be based on the number of affordable units, their income levels, the ability to provide affordable units for underserved populations or neighborhoods, the challenges of replacing existing lower-priced units, etc. However, as a discretionary action rather than a prescribed formula, it can be difficult for developers to predict what alternatives will and will not be accepted, introducing risk and uncertainty as well as the potential perception of arbitrary decision-making.

Recommendation
Allow developers to propose an alternative means of compliance, subject to Council findings that the alternative provides equal or greater value relative to the standard inclusionary requirements.

STRATEGIC PLAN ALIGNMENT:

This item contributes to **Strategic Priority 2: Community Well-Being** and **Goal No. 2.1** - Facilitate the development of a quality and diverse housing supply that is available and affordable to a wide range of income levels.

This item aligns with each of the five Cross -Cutting Threads as follows:

1. **Community Trust** — The initiative to explore an inclusionary policy merges best practices in policy development with intensive outreach and communication with both the development community and public to be transparent and make decisions based on sound policy, and inclusive community engagement based on timely and reliable information.

2. **Equity** — Inclusionary Housing promotes the integration of affordable housing into the City's market rate stock which allows people of different races, backgrounds, and economic circumstances to live throughout Riverside, lessening the concentration of poverty and broadening the experiences of those who live in affordable/ market mixed units.

3. **Fiscal Responsibility** — By tapping local development resources to ensure a balanced housing market, Riverside is a prudent steward of public funds and ensures responsible management of the City' s financial resources while providing quality of life to all residents.

4. **Innovation** — Exploring inclusionary housing potentially creates a development tool to address changing needs and prepares for the future through collaborative partnerships and adaptive processes in consultation with the public and development community.

5. **Sustainability & Resiliency** — By creating a balanced housing market, Riverside is ensuring a balanced economy that serves all income levels of city residents but does not sacrifice growth.

FISCAL IMPACT:

There is no fiscal impact associated with the report.

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Attachments:

1. Feasibility Analysis

2. Sample of Inclusionary Housing Standards
3. Nexus Study
4. Committee Recommendation
5. Presentation