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LAW ALERT

CALIFORNIA SUPREME COURT GREENLIGHTS AFFORDABLE HOUSING ORDINANCES

The California Supreme Court has held that local ordinances requiring a proportion of new housing to be affordable can be justified so long as they bear a reasonable relationship to the public welfare. The case is *California Building Industry Ass'n ("BIA") v. City of San Jose*, decided on June 15, 2015. In recognizing the state's critical housing needs, Chief Justice Tani Cantil-Sakauye, writing for the Court, stated, "[t]here is no reason why a municipality may not ...[require] new developments to set aside a percentage of its proposed units for sale at a price that is affordable."

The Court's unanimous decision will make it easier for cities and counties to adopt similar ordinances and more difficult for opponents to challenge them.

Background. In January 2010, the City of San Jose adopted an affordable housing ordinance that required 15 percent of new for-sale housing developments to be affordable to moderate-income households (earning 120 percent of median income or less). The BIA challenged the ordinance, contending that the affordable housing requirement was an "exaction" that could only be justified if it had a "reasonable relationship...to the deleterious public impact of the development" supported by evidence (usually provided through a "nexus study") demonstrating that new housing has a deleterious impact on the need for affordable housing.

The Supreme Court rejected the BIA's arguments and upheld the City's contention that the ordinance was a land use ordinance that did not require a nexus study.

Ruling. In rejecting the BIA's arguments, the Court reached these major conclusions:

Affordable Housing Ordinances Are Land Use Controls, Not Exactions. The Court concluded that affordable housing ordinances are simply price controls on new homes, which meet constitutional requirements so long as they have a reasonable relationship to the public welfare and are not confiscatory. A price control is not an "exaction" because it does not require conveyance of a property interest to a municipality. Consequently, it does not need to be justified by the "deleterious impact" of new housing on the need for affordable housing.

In-Lieu Fees Are Not Exactions. The Court held that where developers may *elect* to pay an in-lieu fee rather than provide affordable units, the fee does not need to be justified by the "deleterious impact" of the new housing. "No developer is required to pay the in-lieu fee and may always opt to satisfy the ordinance by providing on-site affordable units." The Court disapproved *Building Industry Ass'n v. City of Patterson*, concluding that *Patterson* was incorrect in finding an in-lieu fee to be invalid based on the "deleterious impact" test proposed by the BIA.

Some Practical Implications.

Adoption of Affordable Housing Ordinances. New and amended affordable housing ordinances do not need to be supported by a nexus study. They may be justified so long as they bear a reasonable relationship to the public welfare – a standard that most communities should be able to meet easily by making findings that incorporate the need for affordable housing demonstrated in their housing elements. The burden of proof is on the party challenging the ordinance.

Required Percentage of Affordable Housing. No nexus study is needed to justify the required percentage of affordable housing. However, under principles applicable to price controls, the requirement cannot be so high as to be confiscatory or constitute a regulatory taking. In adopting new ordinances or increasing the required amount of affordable housing, an economic feasibility study may be appropriate to demonstrate that the requirement is reasonable.

In-Lieu Fees for For-Sale Affordable Housing. A nexus study is not needed to support in-lieu fees as long as the developer has the option of constructing affordable homes on-site. If a fee is the only requirement, a nexus study is likely still needed.

Rental Housing. Rental housing fees should continue to be justified by a nexus study because affordable rental housing cannot be required on-site by ordinance, as determined by *Palmer/Sixth Street Props. LP v. City of Los Angeles*. The Court recognized that *Palmer* remains good law.

Commercial Linkage Fees. Commercial linkage fees (imposed on commercial development to provide affordable housing) should also continue to be justified by a nexus study, unless the local ordinance would otherwise require the affordable housing to be constructed on-site.

Recorded Restrictions. In dicta, the Court noted that requiring a developer to grant an *option* to local agency may be considered a requirement to provide a property interest, and hence an exaction, requiring greater justification. However, a recorded restriction simply requiring the homes to be sold at a reduced price would not grant a property interest.

Local agencies should review their policies regarding restrictions recorded against the *developer* to ensure that

they do not constitute the granting of a property interest. However, the Court stated that *homebuyers* who purchase units at a below-market price cannot plausibly consider similar restrictions to constitute a taking.

Ability to Protest Affordable Housing Requirements. In *Sterling Park LP v. City of Palo Alto*, the Court previously held that affordable housing in-lieu fees and the grant of an option from the developer were "exactions" for the purposes of the protest procedures under the Mitigation Fee Act (Gov't Code Section 66020). The Court has not decided whether on-site affordable housing requirements may also be protested under the State's Mitigation Fee Act.

Given this uncertainty, local agencies should provide notice of the right to protest at the time of project approval, or risk having their affordable housing requirements challenged years after approval.

Next Steps

News reports in the wake of the decision indicate that the Pacific Legal Foundation is considering filing a petition with the United States Supreme Court for a grant of certiorari to review the decision.

Legislation will also likely be introduced to permit agencies to apply affordable housing ordinances to rental housing. In vetoing a similar bill in October 2013, Governor Jerry Brown stated that he "would like the benefit of the Supreme Court's thinking" before acting. Now that the Court has acted, similar legislation may be successful.

Conclusion

As stated by the Court:

"The objectives of increasing the amount of affordable housing in the city to comply with the Housing Element Law and of locating such housing in economically diverse developments are unquestionably constitutionally permitted purposes."

Uncertainty regarding the applicable standard has made communities cautious about proceeding with affordable housing ordinances. *BIA v. City of San Jose* is a major victory for local government's efforts to assist in resolving the affordable housing crisis in California.

If you have any questions, please contact Barbara Kautz, Lynn Hutchins, Caroline Nasella, Eric Phillips, or any other attorney at Goldfarb & Lipman.