



## CITY OF MILPITAS AGENDA REPORT (AR)

<b>Item Title:</b>	Milpitas Affordable Housing Ordinance Update
<b>Category:</b>	Community Development
<b>Meeting Date:</b>	1/18/2022
<b>Staff Contact:</b>	Sharon Goei, Building Safety and Housing Director, 408-586-3260
<b>Recommendation:</b>	Following the reading of the title by the City Attorney, move to waive the first reading beyond the title and introduce Ordinance No. 297.1 amending Milpitas Municipal Code Title XII, Chapter 1 (Affordable Housing Ordinance).

### **Executive Summary:**

In June 2018, the City Council adopted the current Affordable Housing Ordinance. In 2021, the City Council directed staff to find ways to ensure that residential developers would build more affordable units on-site, rather than paying in-lieu fees.

In this Affordable Housing Ordinance update, proposed amendments still provide developers with alternatives to building affordable units on-site because staff and legal counsel believe that providing alternative means of compliance is needed in order to comply with existing state law. However, staff has proposed substantial changes to the process for granting exceptions to building affordable units on-site for ownership housing, which include strengthening the City Council's required findings before allowing alternative means of compliance for ownership housing and incentivizing developers to build affordable units on-site.

For rental residential development, the proposed changes give developers the option to either build affordable rental units on-site or utilize any of the alternatives listed in the ordinance under certain conditions. While rental development would have a more flexible standard for compliance than ownership development, this flexibility is to ensure consistency and compliance with existing state law governing inclusionary housing as set forth in the Government Code.

Staff has also proposed additional changes to the Affordable Housing Ordinance relating to fractional units, design and distribution of affordable units, clarification of accessory dwelling units, allowing mixed tenure compliance, removing credit transfer option, extending ownership unit affordability from 45 to 55 years, broadening the criteria for preferences, among others. These proposed changes are for the most part consistent with the existing ordinance and are primarily intended to add clarity and consistency to the ordinance.

Community and stakeholder feedback on the proposed ordinance was overall positive and focused on having flexibility and a range of alternatives to meet the requirements of the Affordable Housing Ordinance.

Staff recommends that Council move forward with the steps toward adopting the proposed ordinance amendments.

### **Background:**

On June 19, 2018, the City Council adopted Affordable Housing Ordinance No. 297, which applies to any land use entitlement application not deemed complete by July 20, 2018. The purpose of this ordinance is to, "(a) Enhance the public welfare and assure that further housing development contributes to the attainment of the

City's housing goals by increasing the production of residential units affordable by households of very low, low and moderate income, and (b) Assure that the limited remaining developable land in the City's planning area is utilized in a manner consistent with the City's housing policies and needs.”

Under the Affordable Housing Ordinance, new residential development projects with 10 or more units must include 15% of very-low or low-income units for rental development and 15% of very-low, low, or moderate-income units for ownership development. These units must remain affordable for a minimum of 45 to 55 years. The ordinance allows several alternatives to building the required affordable housing on-site, including payment of in-lieu fees, building affordable housing off-site, dedicating land for affordable housing, and using credit transfers when a developer builds more affordable units than required.

On March 5, 2019, the City Council adopted Resolution No. 8852, which approved the affordable housing fee schedule for a residential in-lieu fee and a non-residential impact fee. The Resolution became effective on July 1, 2019. The affordable housing fee level is adjusted July every year for inflation using the Engineering News Record Building Cost Index. If granted an exception to pay in-lieu fees, a developer must pay the Affordable Housing Ordinance in-lieu fees prior to receiving a building permit.

On December 15, 2020, the City Council directed staff to explore changes to the in-lieu fee provisions in the ordinance. The City Council was interested in finding ways to ensure that developers would build more affordable units on-site, rather than paying in-lieu fees. Currently, the City needs to gather fee revenue for multiple years before it can support a new affordable housing project. On January 5, 2021, staff provided an [information memorandum](#) on the Affordable Housing Ordinance in-lieu fee options to the City Council. At the March 16, 2021 City Council meeting, Council directed staff to proceed with work on this item.

#### **Analysis:**

In alignment with Council direction, staff is proposing changes to the Affordable Housing Ordinance to encourage more on-site affordable housing production. Staff is also proposing changes to add clarity and consistency throughout the ordinance.

Staff has compiled a comprehensive summary of proposed changes to the Affordable Housing Ordinance along with the reason for the proposed changes. Please refer to Attachment 1 for the summary.

#### **Key Proposed Changes to Milpitas Municipal Code Title XII (Housing), Chapter 1 (Affordable Housing Ordinance)**

This section describes and highlights key proposed changes to the Affordable Housing Ordinance.

- **Section 2: Definitions**

Eight definitions are proposed to be added or modified to provide clarity. The proposed changes are intended to make the definitions more explicit and to remove ambiguity. The changes are staying consistent with the current ordinance.

- **Section 3.00: 15 percent affordability requirement**

Sometimes the 15% calculation of required affordable housing results in a fraction. The current ordinance provides that in-lieu fees are paid for all fractional units and there is no rounding. In Section 3.00, the proposed changes state that if the 15% calculation results in a fractional unit that is less than 0.5, the developer may pay an in-lieu fee for that fractional unit. If the 15% calculation results in a fractional unit that is equal to or greater than 0.5, the requirement is rounded up to the next whole number, resulting in one more unit.

Another proposed change in Section 3.00 adds language to clarify that accessory dwelling units shall not be included in the calculation of the total number of units subject to the on-site 15% inclusionary requirement. This is in concert with the proposed change in Section 2 that clarifies that accessory dwelling units cannot be used to meet inclusionary requirements.

- **Section 3.02: Conditions of approval**

The proposed changes clarify that the ordinance applies to mixed-use projects. A list of data and information that needs to be submitted is also delineated in order to clarify the documents that must be provided for staff to review the project.

- **Section 3.03: Concurrent construction of affordable units**

Proposed language is added to explain how construction of affordable units must be carried out for phased developments and to further clarify that affordable units must be constructed in advance of, or concurrently with, market rate units within each phase.

- **Section 3.04: Design and distribution of affordable units**

More specific language is added on how the design and distribution of affordable units should be ensured and to clarify how the quality of affordable units must be reasonably consistent with the market rate units.

- **Section 4: Exceptions to on-site development of 15% affordable units**

- **Section 4A: Ownership projects**

For ownership projects, substantial changes are proposed to the process for granting exceptions to building affordable units on-site. The changes encourage building affordable ownership units on-site by providing more stringent standards for ownership projects to use alternative means of compliance such as in-lieu fees, off-site units, or land dedication.

In the proposed ordinance, a developer must construct on-site affordable ownership units unless the City Council makes findings that allowing the developer to use one of the listed alternatives will

1. further the City's low and moderate income housing goals; *and*
2. *either* (i) result in a greater amount of affordable housing or deeper affordability by meeting at least two of four listed criteria in the ordinance; *or* (ii) provide other community benefits that exceed the benefit of constructing on-site affordable units.

Consistent with Council direction to incentivize on-site affordable housing construction, the proposed ordinance requires that for an ownership project to not construct affordable units on-site and to use one of the alternative means of compliance, the City Council must make the above findings. In other words, if a developer intends to use one of the alternatives for an ownership project, the developer would need to provide a greater contribution to affordable housing or other greater community benefit, as compared to building the units on-site.

From a legal perspective, it is recommended that the City retain alternatives for ownership projects as part of the ordinance, rather than requiring all affordable units on-site. The key court case that upheld cities' authority to require inclusionary housing is the California Supreme Court case of California Building Industry Association v. City of San Jose (2009). In that case, the California Supreme Court found that a city could require the development of affordable housing as part of a market rate development, but also indicated that it was important to provide a menu of alternatives to developers to provide flexibility in the event that on-site development is infeasible. The court did indicate that the alternatives could require a larger contribution to affordable housing in order to incentivize on-site construction. Therefore, in the proposed ordinance, the City can require the additional findings outlined above before allowing developers to use an alternative in ownership projects.

In alignment with Council direction, the proposed ordinance clarifies and strengthens the findings required for City Council to approve exceptions to building affordable units on-site, thereby encouraging more on-site affordable housing construction. This sets a higher standard that must be met in order for developers to use any of the alternatives. The proposed ordinance gives the City Council more control in determining when and if to accept ownership development proposals that do not include on-site affordable housing units.

- **Section 4B: Rental projects**

The proposed changes clarify that the City may allow an exception to the requirement to construct on-site affordable units for a residential rental project if requested by the applicant, provided that applicant shall be required to contribute to the City's affordable housing needs through one of the alternative means of compliance (i.e., paying in-lieu fees, constructing units off-site, or making a land dedication).

In other words, the proposed ordinance allows rental project developers to either build affordable units on-site, or satisfy their obligations through utilizing any of the alternative means of compliance listed in the ordinance. Therefore, for rental projects, the proposed ordinance provides a more flexible standard than ownership projects. This flexibility is provided for rental development to ensure compliance with existing state law governing inclusionary housing as set forth in the Government Code. The legal background is described below.

In 2009, in a California Court of Appeals decision in the case of *Palmer/Sixth Street Properties v. City of Los Angeles*, the court held that a city inclusionary requirement to include affordable housing (or pay a fee in lieu of doing so) violated the Costa-Hawkins Rental Housing Act. As a result of the *Palmer* decision, cities could not require developers to construct on-site affordable housing as part of a private development until 2018, when AB 1505 was enacted. Intended to allow for inclusionary rental housing, AB 1505 amended Government Code Section 65850 to authorize cities to adopt inclusionary housing ordinances for residential rental projects and indicated that any ordinance must include alternative means of compliance, such as payment of an in-lieu fee, land dedication, off-site construction, or the like.

In light of the current state law and the explicit statutory requirement from AB 1505 to provide alternatives for residential rental development, the proposed ordinance provides alternatives for rental projects in order to ensure compliance with AB 1505. The proposed ordinance allows developers to utilize any of the listed alternative means of compliance. Developers will still be incentivized to build on-site units based on potential density bonus benefits (waivers, incentives, and increased density).

For policy discussion, staff has evaluated a different set of options for rental projects to encourage on-site affordable housing construction while providing flexibility for developers. This set of options is as follows:

- (A) Developer may construct 50% of required units on-site, and pay 50% of requirement in-lieu fees without City Council findings;
- (B) Developer may pay 100% in in-lieu fees if the City Council makes the same findings required for ownership alternatives (i.e., fees will further the City's low and moderate income housing goals, and result in a greater amount of affordable housing or deeper affordability or will provide other community benefits that are greater than constructing on-site units);
- (C) Developer may meet the requirement through land dedication or off-site construction, provided that the standards in the Affordable Housing Ordinance are met.

This approach still provides developers with alternatives to on-site construction, but limits a developer's ability to meet the full requirement through in-lieu fee payment. This approach still likely complies with existing state law governing inclusionary housing ordinances, but is not as straightforward as the proposed language.

- **Section 4.00: Payment of fees in lieu of creation of affordable units**

Proposed language is added to clarify that calculation of in-lieu fees must be based on the total gross square footage of all dwelling units developed as part of the project, including any accessory dwelling units.

- **Section 4.01: Off-site projects**

Proposed language is added to clarify that off-site projects must be located within the City of Milpitas. New language is also proposed that would allow developers flexibility to build off-site affordable units with a different tenure from the market rate units. The proposed change would require more square footage of affordable units off-site at an equivalent or lower income category. These proposed changes provide flexibility so developers can creatively develop more market rate and affordable housing while encouraging on-site construction.

- **Section 4.02: Land dedication**

Proposed language is added to clarify that dedicated land must be located within City limits and be zoned and usable for the required amount of housing. Dedicating non-residentially zoned land is unacceptable, as it would require the conversion of employment lands.

- **Sections 4.03, 4.04, and 7: Credit transfers**

Under the existing ordinance, upon request of the applicant, the City Council may permit an applicant to apply for affordable unit credits for units constructed in excess of the number required in one project and use those

credits to satisfy the requirements for another project in the City. The proposed changes delete credit transfers as an alternative means of compliance. To date, this alternative has not been used and it would be very staff intensive to administer.

- **Sections 6.00 and 6.02: Ownership affordability term**

The proposed updates change the affordability covenant for ownership units from 45 to 55 years to be consistent with rental unit affordability and to gain a longer-term affordability. This change would apply 55 years to all affordable units created under the Affordable Housing Ordinance.

- **Section 6.03: Selection criteria**

The current ordinance states that the City shall endeavor to make housing available for Milpitas residents and employees. Proposed language is added to broaden the criteria for preferences under the ordinance to add displaced former Milpitas residents and households with children enrolled in the Milpitas Unified School District that have inadequate housing as defined under the federal McKinney-Vento Homeless Assistance Act. Language is also added to clarify the need to conform with state and federal fair housing laws.

#### Stakeholder and Community Outreach

On December 8, 2021, the City posted the proposed amendments to the Affordable Housing Ordinance on the City's website. The packet of materials included a cover letter to the community and developers, policy discussion on rental inclusionary alternatives, summary of proposed changes, redlined version of proposed changes, and clean version of proposed changes.

On December 16, 2021, the City hosted a Community Development Roundtable to gather input from developers and real estate professionals on the proposed changes to the Affordable Housing Ordinance. Eleven stakeholders attended this meeting. The Building Industry Association commented that they do not want policy changes that would discourage market rate projects or discourage development overall, and encouraged the City to adopt policy changes that help achieve the City's upcoming Regional Housing Needs Allocation goals. Questions were addressed to clarify how accessory dwelling are considered in the ordinance. Questions were also addressed regarding how current projects meet the existing ordinance. Developers commented that flexibility is important and the ability to pay in-lieu fees where Council deems appropriate is important, and that the City can utilize the fees collected to support potential projects.

On December 17, 2021, the City hosted a virtual community meeting to gather input from the broader community and residents on the proposed changes to the Affordable Housing Ordinance. Nine stakeholders attended this meeting, including SV@Home, residents, Commissioners, and Homelessness Task Force members. Attendees were very engaged with staff in active discussions and question and answer session. Comments were overall positive with discussions around income levels, providing a range of options, balancing between fee level versus building units, different policy for ownership and rental projects, among others. The robust discussions at this meeting also helped to inform and educate about some details of the Affordable Housing Ordinance. Please refer to Attachment 4 for SV@Home's comment letter.

#### Residential Development

Since the Affordable Housing Ordinance took effect, six residential development projects subject to the Affordable Housing Ordinance have received approval from the City. The six residential projects consist of three rental and three ownership developments. Five of these six projects are building affordable units on-site and not using any alternative means of compliance. The sixth project, which is an ownership development, is building almost all of the required affordable units on-site but is paying a fee in-lieu of building one unit and a fractional unit. Therefore, all six residential projects developed since the Affordable Housing Ordinance was adopted in 2018 are meeting almost all of their inclusionary housing obligations by incorporating affordable units on-site within the development.

With the proposed amendments to the ordinance, the City will further encourage more on-site affordable housing construction.

#### Action Steps

To achieve Council intent to encourage more on-site affordable housing production, and to add clarity and consistency to the Affordable Housing Ordinance, staff recommends that Council move forward with the first reading and introduce the ordinance on January 18, 2022.

The second reading and ordinance adoption is scheduled to take place at the February 1, 2022 Council meeting.

**Policy Alternative:**

**Alternative:** Do not amend the Affordable Housing Ordinance.

Pros: The current Affordable Housing Ordinance would remain without additional staff time.

Cons: The current Affordable Housing Ordinance would not have the benefit of the amendments for added clarity and consistency and encouraging on-site affordable housing construction.

Reason not recommended: The proposed amendments to the Affordable Housing Ordinance would achieve Council intent to encourage on-site affordable units and add clarity and consistency throughout the ordinance.

**Fiscal Impact:**

Many of the proposed changes would facilitate administration of the Affordable Housing Ordinance and save staff time. Limiting developers' ability to pay in-lieu fees may slow the growth of the City's Affordable Housing Fund, but it may result in more on-site affordable units. These proposed changes have no immediate fiscal impact.

**California Environmental Quality Act:**

The introduction and adoption of this Ordinance is (1) not a Project under the California Environmental Quality Act (CEQA) and is therefore exempt, pursuant to Title 14 of the California Code of Regulations, Section 15378(b)(4)4, that adoption of this ordinance is exempt from the requirements of the California Environmental Quality Act (CEQA) because it constitutes a governmental fiscal activity that does not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment; (2) statutorily exempt pursuant to CEQA Guidelines section 15267 (Financial Assistance to Low or Moderate Income Housing); (3) not intended to apply to specifically identified affordable housing projects and as such it is speculative to evaluate any such future project now and, moreover, they will be subject to appropriate environmental review at such time as approvals for those affordable housing project are considered; and/or (4) not intended to, nor does it, provide CEQA clearance for future development-related projects by mere establishment or payment of the fees. Each of the foregoing provides a separate and independent basis for CEQA compliance and, when viewed collectively, provides an overall basis for CEQA compliance.

**Recommendation:**

Following the reading of the title by the City Attorney, move to waive the first reading beyond the title and introduce Ordinance No. 297.1 amending Milpitas Municipal Code Title XII, Chapter 1 (Affordable Housing Ordinance).

**Attachments:**

1. Summary of proposed changes to the Affordable Housing Ordinance
2. Ordinance No. 297.1 for introduction
3. Redline comparison showing changes to the Affordable Housing Ordinance
4. SV@Home comment letter