

Assessing the City of San José's Proposed Affordable Housing Impact Fee: Do Post-Palmer and Patterson Residential Nexus Studies Satisfy Applicable Constitutional and Statutory Requirements?

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October 2014

Executive Summary

In response to recent judicial decisions (*Palmer*, *Patterson*, *Sterling Park*, and the California Supreme Court's grant of review in *CBLA v. City of San José*), California local governments have hired consulting firms to prepare "residential nexus studies" purporting to demonstrate the legally required nexus between new market rate housing and the need for affordable housing. Local governments have relied on these studies to adopt ordinances imposing development impact fees or other exactions on new residential development to fund affordable housing.

This analysis focuses on the legal validity of the methodology underlying these nexus studies fees—such as the fees on new rental housing currently under consideration by the City of San José. The fees purportedly justified by the methodology are staggering. A study prepared for Hayward purports to justify a fee of \$81,900 per market rate unit for single-family detached units (\$40.98/sq. ft.) and \$82,800 (\$44.73/sq. ft.) per market rate unit for townhomes/condominiums. The San José study purports to justify a fee of \$28.28 per/sq. ft. on new rental housing (\$28,000 per market rate unit). A similar methodology has also been used in the context of nonresidential development. A study prepared for Mountain View purports to justify a fee of \$243.61/sq. ft. on commercial/retail/entertainment uses and \$59.31/sq. ft. on office/tech/industrial uses. A study prepared for Emeryville purports to justify a fee of \$142.60/sq. ft. for office development.

Under the California Supreme Court's decision in *San Remo Hotel, L.P. v. City and County of San Francisco*, 27 Cal.4th 643 (2002), legislatively imposed exactions must, as "a matter of both statutory and constitutional law,... bear a reasonable relationship, in both intended use and amount, to the deleterious public impact of the development." To satisfy the constitutional and legislative standards embodied in *San Remo's* reasonable relationship test, the local agency imposing the exaction must produce evidence showing that: "(1) there is a cause-and-effect relationship between a property owner's proposed use of the property and the social evil that the exaction seeks to remedy, and (2) the exaction is reasonably related in both intended use and amount to that social evil." *Id.* at 687 (Baxter, J. concurring and dissenting). In other words, an ordinance establishing a legislatively imposed development exaction can only be sustained if

both its purpose and extent are reasonably related to some negative public impact proximately caused by the projects on which the exaction would be imposed.

A description of the methodology employed in the affordable housing nexus studies appears in Keyser Marston's report for the City of San José:

At its most simplified level, the underlying nexus concept is that the newly constructed units represent net new income in San José that will consume goods and services, either through purchases of goods and services or 'consumption' of governmental services. New consumption translates to jobs; a portion of those jobs are at lower compensation levels; low compensation jobs relate to lower income households that cannot afford market rate units in San José and therefore need affordable housing.

Close review of the methodology reveals it comprises a 13-step chain-of-events and no fewer than 60 underlying assumptions covering such disparate data inputs as federal, state, and local tax rates, the prevalence of online shopping and the household marginal propensity to save vs. consume.

City of San José and Keyser Marston written responses to questions posed by BIA of the Bay Area indicate that the methodology: (1) has not been validated or endorsed in any academic or professional journals; (2) was developed specifically for the purpose of supporting affordable housing impact fees on new residential development; (3) has not been used in contexts other than affordable housing; (4) cannot adequately distinguish between purported housing needs generated by residential development and overlapping housing needs projected by the same methodology when applied to nonresidential development; and (5) has never been empirically validated (only that it purportedly "aligns with accepted economic principles that households demand goods and services and that the businesses and institutions that provide those goods and services need employees."). Keyser Marston was also unable to provide the methodology's cumulative margin of error for the final results.

In response to the question—"Is it your professional opinion that the Study establishes a causal relationship between building market rate housing and a quantifiable need for affordable housing or rather a correlative one?"—Keyser Marston refused to provide such an opinion and instead offered a legal conclusion: "The City's Consultant prepared the nexus analysis to meet the reasonable relationship standard under the Mitigation Fee Act, and in the Consultant's opinion, the analysis meets that standard."

This paper concludes that the "new generation" of nexus studies, with their lengthy series of untested (and ultimately unverifiable) assumptions, neither establish the required causal connection between new housing development and affordable housing needs nor show why it is fair and reasonable to require development applicants—rather than the general public—to shoulder the burden of providing affordable housing. They do not establish that new residential development proximately "causes" or even contributes to the need for affordable housing. The lack of affordable housing has been a problem for California for decades. Scores of government

and academic studies, supported by a wealth of research and economic data, have demonstrated that the need for affordable housing has been created over an extended period by a complex amalgam of factors, including restrictive zoning and growth controls leading to a massive and chronic undersupply of new market rate housing, California local governments' pursuit of jobs and other types of development over new housing, high impact fees, complex environmental regulations, outdated building codes, multifamily housing restrictions, and NIMBYism. None of these studies has demonstrated or even postulated any causal relationship between building additional market rate housing and affordable housing needs, and the residential nexus studies fail to show the existence of such a relationship.