City of Costa Mesa

Agenda Report

77 Fair Drive
Costa Mesa, CA 92626

Item #: 23-1311 **Meeting Date:** 7/26/2023

TITLE: FOLLOW-UP JOINT STUDY SESSION REGARDING A POTENTIAL INCLUSIONARY HOUSING PROGRAM

DEPARTMENT: ECONOMIC AND DEVELOPMENT SERVICES DEPARTMENT/PLANNING DIVISION

PRESENTED BY: JENNIFER LE, ECONOMIC AND DEVELOPMENT SERVICES DIRECTOR AND NANCY HUYNH, SENIOR PLANNER

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RECOMMENDATION:

Staff recommends the City Council and Planning Commission receive the staff presentation, provide feedback on staff's policy recommendations, and provide direction to regarding an inclusionary housing ordinance for potential Planning Commission and City Council consideration.

BACKGROUND:

The City Council is considering whether to move forward with preparation of an affordable housing program for Costa Mesa. An affordable housing program, also referred to as an inclusionary housing program, is a program by which a portion of new housing units built in the City would be required to be "affordable" and made available only to tenants or buyers who meet certain defined income limits (usually categorized as very low, low, or moderate-income households).

Summary of May 16, 2023 Joint Study Session

On May 16, 2023, the City Council and Planning Commission conducted a joint study session to review and discuss the major components of an inclusionary housing program, legal requirements, compliance options, policy considerations, and industry best practices.

A comprehensive overview was presented by the City's expert consultant Kathe Head with Keyser Marston Associates (KMA). The overview included the following topics:

- Income and affordability considerations;
- Program standards: threshold size, target affordability level, covenant periods, and alternative compliance options;
- Review of draft project prototypes for both rental and ownership housing;
- In-lieu fee payment considerations and other fulfillment options; and
- Overview of key policy decisions.

After the KMA presentation, City Council and Planning Commission provided comments which are summarized below:

- Establish policy goals for the inclusionary housing program;
- Focus on low and very low-income households for rental projects. Rental projects should have deeper affordability requirements compared to ownership housing;
- Focus on moderate income households for ownership housing types or allow an in-lieu fee by right for ownership housing projects rather than require on-site production. Also create a path for homeownership opportunities;
- Consider using a lower in-lieu fee option for smaller projects;
- Acquisition and rehabilitation of existing residential units is not a favorable alternative option to an onsite affordable housing requirement because of displacement concerns for existing tenants;
- Create incentives beyond the State's density bonus program to encourage the production of housing units such as reduced parking requirements; and
- Explore opportunities for deeper affordability requirements for specific areas in the City such as the Fairview Developmental Center site and properties north of the 405 Freeway.

Comments received from the community included concern with rising rental costs, the increasing need for affordable housing, balancing the need for affordable housing with the developer community's need to pursue profitable housing projects, apply incentives for land owners and developers to participate, and consider deeper affordability for the Fairview Developmental Center.

Following the discussion, City Council directed staff to complete the Financial Evaluation and incorporate rental and ownership housing prototypes based upon the candidate housing opportunity sites in the Housing Element and potential rezoning areas for housing located along the City's major commercial and industrial corridors. This analysis would determine the benefit of rezoning for housing on land values and help to calculate a supportable affordable housing "set aside" for those scenarios. City Council also requested a follow-up study session once the draft Financial Evaluation and policy recommendations were completed by KMA.

The May 16, 2023 study session agenda report and meeting video are included in the links below:

- May 16, 2023 Study Session Agenda Report: https://costamesa.legistar.com/View.ashx?M=F&ID=11974698&GUID=90360909-8600-4286-A076-E5B7F45794D4
- May 16, 2023 Study Session Meeting Video: https://costamesa.granicus.com/player/clip/3993?view_id=14&redirect=true&h=dc14b3b0c827980057c8fbbc40502a38

This follow-up study session will focus on an overview of the draft Financial Evaluation as well as the policy recommendations for each of the inclusionary housing program components. Staff is seeking feedback on the policy recommendations.

Preliminary Findings Presented at May 16, 2023 Study Session

At the first study session, a draft Executive Summary from the Financial Evaluation that included preliminary findings was presented to the City Council and Planning Commission. These preliminary findings were based on a "traditional" approach to an inclusionary housing ordinance and assumed a vacant land scenario and therefore did not consider land value associated with a property already improved and operating as a commercial or industrial use. The analysis was also based on prototypes that only considered the current allowed density under the existing zoning code and not the rezoning envisioned in the adopted Housing Element. The preliminary findings were also based on a city-wide approach meaning the inclusionary housing requirement would be applicable to housing projects proposed anywhere in same City.

For rental housing projects anywhere in the City, KMA's supportable set-aside percentage was 10% for low income units and 7% for very low-income units; refer to Table 1 below.

Table 1
Supportable Set-Aside Requirements for Rental Housing Projects – City-Wide Approach

Supportable Inclusionary Housing Requirement Base Zoning Prototype	
Low Income	10%
OR	
Very Low Income	7%

For ownership housing projects anywhere in the City, KMA's supportable and recommended set-aside percentage ranged from 7% to 8% for moderate income units and 5% to 6% for low income units based on ownership housing product types; refer to Table 2 below.

Table 2
Supportable Set-Aside Requirements for Ownership Housing Projects – City-Wide Approach

Supportable Inclusionary Housing Requirement Ownership Housing Development Projects		
	Moderate Income	Low Income
Townhomes	8%	5%
Live / Work Units	7%	5%
Condominiums	8%	6%

Because the affordability gap (the difference between a market rate versus affordable sales price) is so large for ownership housing projects, KMA recommended that housing developers be allowed to pay an in-lieu fee by right instead of requiring on-site production of units for ownership projects.

Updated Financial Evaluation

The completed draft Financial Evaluation attached to this Agenda Report augments the one presented at the previous study session. The additional analysis included in the report is based on housing project prototypes in the City's adopted housing overlay/urban plan areas which generally correspond to the areas envisioned for rezoning by the City's adopted Housing Element. The City Council and Planning Commission can consider applying a potential inclusionary housing requirement for all housing projects throughout the City or apply the requirement only in specific areas of the City along commercial and industrial corridors where rezoning for housing is envisioned. A further discussion of the two approaches is included below in the Policy Recommendations section of this Agenda Report.

ANALYSIS:

Inclusionary Housing Program Guiding Principles

During the last study session, the Council expressed interest in identifying "guiding principles" or policy goals for a potential inclusionary housing program. These policy goals would help create a framework for City leaders and the community as it discusses and considers key elements of a potential inclusionary housing program.

The following are draft policy goals developed by staff for City Council and Planning Commission feedback and consideration. Should the City decide to move ahead, these policy goals would be incorporated into a draft inclusionary housing ordinance for adoption.

- Develop an inclusionary housing program that promotes the development of affordable housing without unduly constraining the creation of market rate housing.
- Balance the City's housing needs with the needs of property owners/developers, while also considering the added value enhancements from rezoning for housing required by State law and envisioned by the City's Housing Element.
- Balance the local and regional need for housing with consideration for protecting job-serving industrial and commercial uses.
- Adopt an inclusionary housing ordinance that is dynamic with the ability to be easily adjusted to respond to changing housing market demands.
- Commit the appropriate resources to successfully implement, monitor and evaluate the ordinance for effectiveness.
- Establish a Housing Trust Fund for collection of in-lieu fees to create housing loan programs for rehabilitation of existing housing, City-funded affordable housing projects, first-time homebuyers' program, or other similar programs to support the City's affordable housing goals.

Overview of Financial Evaluation

KMA completed a draft of the comprehensive Financial Evaluation to help the City assess potential financial impacts of an inclusionary housing requirement (refer to Attachment 2 for the Executive Summary and Attachment 3 for the full report). A Financial Evaluation is necessary prior to adopting an inclusionary housing ordinance because the California Supreme Court has ruled that the requirements included in a local ordinance can be neither "confiscatory" nor "deprive a property owner of a fair and reasonable return on investment". The Financial Evaluation compares the financial impacts of a market rate development project to a development project with an inclusionary housing requirement to ensure that the requirement would not be confiscatory or deprive a property owner of a fair return.

The Financial Evaluation analyzes both rental and ownership housing product types and at various density levels, which are representative of the candidate housing opportunity sites identified in the adopted Housing Element and properties located along the City's major commercial and industrial corridors envisioned for rezoning. Staff thoroughly reviewed these sites to determine representative site size, existing development, and allowable development under the existing zoning or urban plan overlay standards to develop the project prototypes.

The Financial Evaluation also takes into consideration the potential financial benefits created by the future rezoning efforts and estimated density ranges as required by State law and as envisioned in the City's adopted Housing Element. Rezoning to allow for housing on a commercial or industrial site can potentially create value for a property owner, which can incentivize the property's sale and redevelopment for housing. In turn, a share of the added value can be leveraged to require that a portion of the housing units be designated as affordable units, while maintaining a reasonable level of profitability for the housing developer. This approach essentially creates an incentive "carrot-based" based program, whereby the incentive is the rezoning for housing at higher density ranges than are currently allowed by code.

The prototypes are reflective of these future rezoning efforts and include scenarios that assume that the apartment and ownership housing projects would be developed at the estimated density ranges envisioned in the adopted Housing Element. (In a few cases, modified development standards e.g. parking requirements shown in the Financial Evaluation are necessary to make a housing project financially feasible for that particular prototype scenario and are intended to spur discussion). The prototypes were then used to test the impacts associated with the following development characteristics: site size, achievable density, maximum allowable number of stories, parking requirements, and the value of the development site before and after rezoning and considering the value of existing onsite improvements.

<u>Methodology</u>

The methodology of the Financial Evaluation is generally described below:

1. *Market Surveys*: KMA conducted a market survey to compile development information related to land and sales value, common densities in apartments and ownership housing projects, typical unit mixes in apartments and ownership housing projects, and apartment rents and ownership housing sales prices;
2. *Develop Prototypes*: Staff worked with KMA to develop housing project prototypes. The prototypes are not actual projects but are based on projects that have been recently developed or proposed; and
3. *Pro Forma Analysis*: KMA used the created prototypes to prepare a pro forma analysis to determine the land value of a market rate apartment or ownership housing project, the value enhancement created by future rezoning efforts, and the share of the value enhancement that can reasonably be dedicated towards providing the inclusionary housing units in a proposed housing project. The results of the pro forma analyses were then used to identify the inclusionary

set-aside requirement that incentivizes the development of rental and ownership housing projects.

Pro Forma Analysis

The pro forma analysis of the prototypes is summarized below and is further detailed in the attached draft Financial Evaluation:

- *Estimated Construction Costs:* The pro forma first considers the estimated construction costs which includes direct, indirect, and financing costs. Direct costs are all the on-site improvements such as buildings, landscaping, and parking while indirect costs are staffing/consulting fees, development impact and permit fees, and legal/insurance fees. The cost of all three items are used to determine the total estimated construction cost of a proposed housing project.

- *Stabilized Net Operating Income (NOI) for Rentals/Projected Net Sales Revenue for Ownership:* The pro forma also considers an apartment developer's stabilized NOI which is the property's gross income that could be generated at full capacity. The stabilized NOI is estimated by taking the gross income from the rent generated by market rate units (with vacancy allowance so the gross income does consider that not all rental units would be occupied) minus the property's operating expenses. For ownership housing developers, the pro forma considers their projected net sales revenue which is the estimated total revenue from each for-sale unit minus the closing costs.

- *Residual Land Value:* The residual land value is the total value of the land after all costs of developing it, plus a market driven profit, have been subtracted. In other words, it is the estimated project value (stabilized NOI or net sales revenue) minus the estimated construction costs plus developer profit. The residual land value is then used to determine the added value enhancement of redeveloping the property from a non-residential use to a residential use at the density ranges envisioned in the adopted Housing Element.

- *Value Enhancement and Funds Available for Inclusionary Units:* The value enhancement is the land value difference between the residential use and existing use of the development site. The value enhancement is used to determine how much of the added project value could be reasonably shared or dedicated towards providing the inclusionary units while creating an incentive for developers to pursue residential development. KMA used the estimated funds available for inclusionary housing to then test the inclusionary requirement on the market rate projects to identify supportable set-aside percentages for rental and ownership housing projects.

Rental Housing Prototypes

The draft Financial Evaluation created seven rental housing project prototypes which are shown below:

- North Costa Mesa:
  - Site area – 4 acres, Total units – 240, Density – 60 units/acre

- Harbor Mixed Use:
    - Site area – 2.4 acres, Total units – 96, Density – 40 units/acre
- Mesa West:
    - Site area – 4.3 acres, Total units – 172, Density – 40 units/acre
- 19 West:
    - Site area – 2 acres, Total units – 80, Density – 40 units/acre
- SoBECA:
    - Site area – 2.4 acres, Total units – 120, Density – 50 units/acre
- Major Corridors:
    - Site area – 3.15 acres, Total units – 189, Density – 60 units/acre

KMA used each of the rental project scenarios to test an inclusionary requirement at the low-income very-low income, and a blend of income (low and very-low) affordability levels. In addition, KMA tested the rental prototype scenarios applying the State density bonus incentive (since it is possible that developers will use the State's density bonus program once they are already required to provide affordable units by the City's local inclusionary program).

<u>Ownership Housing Prototypes</u>

The draft Financial Evaluation also created six ownership housing project prototypes shown below:

- North Costa Mesa:
    - Site area – 3.4 acres, Total units – 85, Density – 25 units/acre
- Harbor Mixed Use:
    - Site area – 0.53 acres, Total units – 8, Density – 15 units/acre
- Mesa West:
    - Site area – 1.18 acres, Total units – 20, Density – 17 units/acre
- 19 West:
    - Site area – 2 acres, Total units – 40, Density – 20 units/acre
- SoBECA:
    - Site area – 0.67 acres, Total units – 11, Density – 16 units/acre
- Major Corridors:
    - Site area – 0.63 acres, Total units – 10, Density – 16 units/acre

KMA used each of the ownership housing development scenarios to test an inclusionary requirement at the moderate-income level. Many other inclusionary housing programs target the moderate-income for ownership housing. This is reflective of the fact that the moderate-income households are likely to have more discretionary income for sufficient down payment and to devote to the ongoing costs associated with homeownership than that of lower income households.

<u>Policy Recommendations</u>

Based on the findings of the Financial Evaluation, KMA prepared policy recommendations for each of the inclusionary housing program components for the City's consideration. These recommendations are included in the memorandum attached to this Agenda Report (Attachment 1). Below is a summary of the policy recommendations.

Threshold Size

The threshold size is the minimum project size that would be subject to the inclusionary housing requirements. KMA's recommended threshold size is five (5) units meaning that any housing project (rental or ownership) that proposes five or more housing units would be required to comply with the ordinance (and projects under five units would be exempt). Under the State's density bonus law, a proposed housing project of at least five units is eligible to utilize the density bonus incentives if the project also includes affordable housing units. Any housing project under five units would not be eligible for the State's density bonus law. Since it is likely that developers may use the State's density bonus to balance the cost associated with providing the affordable units scenario, KMA recommends setting the threshold at five units.

The majority of housing projects approved in the City from 2014 to 2021 were one or two units and were infill projects on residentially zoned sites located within existing residential neighborhoods. Of the other housing projects (located in the City's urban plan areas or along major commercial or industrial corridors), all were more than 5 units. Therefore, setting the threshold at 5 units allows for smaller infill housing development within existing residential neighborhoods to move forward while the inclusionary ordinance is applied to housing projects with more than 5 units which are more financially capable of absorbing the costs of building affordable housing.

If the threshold is set too low, it could discourage smaller housing projects in the City because it may become financially infeasible to construct a profitable smaller project along with the inclusionary requirements. If it is too high, then fewer development projects could trigger the inclusionary housing requirement and therefore not produce affordable units, frustrating the goal of the ordinance. Given the data on past housing projects in the City, staff concurs with KMA's recommended threshold size of five units for both rental and ownership housing projects. However, ultimately this is a policy decision for the Planning Commission or City Council.

Set-Aside Requirement and Affordability Level

The set-aside requirement is the percentage of units required to be "set aside" as affordable housing. The percentage requirement is applied to the number of housing units allowed by the base zoning (exclusive of any additional units granted through the State's density bonus). The affordability level refers to the target income level for which the affordable units would be set at e.g. low, very-low, moderate income. The recommended set-aside requirement and affordability level are different for rental versus ownership projects.

Rental Housing in Rezoning Areas

For rental projects, KMA's supportable and recommended set-aside percentage provides three different options for consideration: focusing the affordable housing requirement on low-income units, very-low income units, or blended income requirement which requires housing to be provided at both the low and very-low income levels. The percentages vary depending on a housing project's estimated density. Refer to Table 3 below from KMA's draft Financial Evaluation.

Table 3
Recommended Set-Aside Requirements for Rental Housing Projects

Recommended Inclusionary Housing Production Options Apartment Development					
Density Range	Low Income Units	+	Very Low Income Units	=	Total Obligation
0 to 39 Units Per Acre	6%	+	0%	=	6%
40 to 59 Units Per Acre					
Low Income Only	11%	+	0%	=	11%
Very Low Income Only	0%	+	7%	=	7%
Low & Very Low Income	6%	+	3%	=	9%
60+ Units Per Acre					
Low Income Only	19%	+	0%	=	19%
Very Low Income Only	0%	+	12%	=	12%
Low & Very Low Income	11%	+	5%	=	16%

Focusing the “set aside” percentage on the low-income level would allow for a higher set aside percentage and therefore a greater number of affordable units compared to the very-low income and blended income approaches. However, setting the required affordability level to target only the low-income level may mean fewer very-low income units would be developed. However, if a developer uses the State’s density bonus incentive, the City would likely still receive very-low income units (despite not requiring it) since it is more cost efficient for housing developers given the rent structures applied by the State density bonus.

Based on their analysis, KMA provided the above menu of options from which developers can elect to fulfill the inclusionary housing requirement for rental housing projects. Staff concurs with KMA’s recommendation to include all three set-aside options for rental housing projects in a potential inclusionary housing ordinance to allow developers the flexibility to choose. Depending on the residential building type e.g. wrap (housing units are wrapped around the parking) versus podium (housing units are located on top of a parking structure), developers may find one set-aside requirement option more economically feasible than the other options.

Whether to focus on low income units, very low income units or allow the developer to choose from the options listed above is a policy decision for the Planning Commission or City Council.

Ownership Housing in Future Rezoning Areas

For ownership projects, the supportable set-aside percentage varied for each prototype area studied. The supportable percentages ranged from 1.7% to 9.8% percent as shown in Table 4 below.

Table 4
Supportable Set-Aside Requirements for Ownership Housing Projects – Rezoning Areas

Supportable Inclusionary Housing Requirements Ownership Housing Development	
Area	Moderate Income Units
North Costa Mesa	9.8%
Harbor Mixed Use	2.5%
Mesa West	6.1%
19 West	1.7%
SoBECA	3.5%
Corridors	N/A

The draft Financial Evaluation results found that the affordability gap (difference between the market rate unit sales price and affordable inclusionary unit sales price) for ownership housing projects is so wide (between $557,000 to $745,000) that it limited the supportable percentage of units that could feasibly be required to be sold to moderate-income households.

Given that finding, it is recommended by KMA to allow ownership housing projects of any size could provide the affordable units onsite or pay an in-lieu fee. This would mean that ownership projects could pay the in-lieu fee "by right" and not as an alternative compliance option. The revenue generated by the in-lieu fee could be placed into a Housing Trust Fund to create programs that support the City's housing goals such as first-time homebuyer assistance, funding affordable housing projects, or City-led projects for the rehabilitation of existing housing units.

If the City were to require on-site production and not allow a by-right in-lieu fee for ownership housing projects, the City could potentially see less ownership housing projects proposed due to the economic constraints of building and providing the affordable units on-site. While creating affordable homeownership is a goal identified in the Housing Element, progress toward that goal could be achieved by encouraging new housing stock. More housing supply could give more opportunities for residents to transition from a rental unit to ownership housing and in turn could make more rental units available for other residents who may wish to relocate to a larger rental unit and/or live more independently. Furthermore, the in-lieu fees could be used to create opportunities for homeownership. For example, a first-time homebuyer program would provide financial assistance (e.g. down payment) to a resident wishing to transition from a rental unit to their first home. Even though the recommended inclusionary requirement for ownership housing may not result in on-site production of affordable ownership units, the by-right in-lieu fee requirement would still create opportunities for homeownership in the City.

Covenant Periods

The covenant period is the minimum required length of time for which the units must remain affordable. There are different covenant periods for rental versus ownership housing projects. KMA's recommended covenant period for rental housing projects is a minimum of 55 years. That means the affordable rental units must remain affordable for 55 years and will continue to remain as affordable beyond 55 years until the property is rezoned and the land use changed to a non-residential use. In other words, the affordable rental units would be required to be affordable for the life of the residential development on the site

For ownership housing projects, KMA's recommended covenant period is 45 years which is very typical in other inclusionary housing programs for ownership housing projects. Within the 45-year period, the ownership inclusionary unit must be sold and resold to moderate income households at the affordable sales price.

Alternative Compliance Options

Because on-site production of affordable units may not always be economically feasible, the City is required by law to provide for alternative ways a developer could fulfill the inclusionary housing requirements. KMA's recommended alternative option for rental housing projects is an in-lieu fee but only for projects with less than 100 rental units. For projects with more than 100 units, on-site production is required unless at the City finds that on-site production would create an extreme financial hardship.

KMA's recommended alternative for ownership housing projects is the ability to fulfill the inclusionary requirement with the on-site production of rental units. Those units should be required to be within the ownership housing project site either interspersed throughout the project or on a separate parcel within the development site as well as constructed concurrently with the market rate units.

While other jurisdictions' inclusionary housing ordinances include other compliance options such as acquisition and rehabilitation of existing property or land dedication, these options are not recommended for Costa Mesa. Acquisition and rehabilitation of an existing property would not result in the creation of new housing units and therefore, could not be counted towards the City's allocated Regional Housing Needs Allocation (RHNA). There are also tenant displacement concerns with this alternative option. Another alternative compliance option also commonly included in other inclusionary housing programs is land dedication. However, it is unlikely a developer would choose this alternative option due to the additional cost of acquiring land especially in a market with high land value.

Should the Council decide to move ahead, KMA will analyze and recommend an in-lieu fee structure for projects of all scales. The recommended in-lieu fee amount would be presented as a resolution along with the draft ordinance pending City Council direction.

Parking Requirements

For all rental housing protypes, KMA found that lowering the City's residential parking requirements would be necessary in order to make an affordable housing requirement financially feasible.

Considering a typical bedroom count distribution for a housing project in Costa Mesa, on average the City requires 2.8 parking spaces per housing unit (inclusive of guest parking). Studies from credible sources have shown that a lower parking requirement is feasible while still providing adequate parking based on actual demand. The City has approved the use of lower parking standards for multiple past projects in the City based on project specific parking demand studies that supported the lower requirement. Without lowering parking requirements, the Financial Evaluation concludes that inclusionary requirement would not be feasible for all rental housing product types and scenarios.

Parking requirements are important in this context because they affect the financial feasibility of a housing project. Higher parking requirements mean that there is less land on any given housing site to devote to housing units, resulting in lower unit counts and higher project costs. However, parking requirements that are too low run the risk of making the units less marketable to renters or buyers who expect adequate on-site parking. Therefore, it is important that residential projects provide enough parking to meet demand but not overpark projects such that scarce land resources are being used inefficiently. It is important to understand these dynamics and tradeoffs to make informed decisions.

As such, and because the City's overall parking requirements have not been studied or substantively updated for many years. staff recommends the City Council direct staff to prepare a residential parking standards analysis to determine the appropriate number of parking spaces necessary to address demand for housing projects and product types commonly built in Costa Mesa. The result of this study would provide on-the-ground demand data to confirm whether staff's parking recommendations used in the Financial Evaluation are appropriate. It should be noted that a study of residential parking standards is already called for in the City's adopted Housing Element and could be used to inform future parking code updates as well.

Requirement Applicability – Citywide or Rezoning Areas

The analyses in the draft Financial Evaluation analyzed a potential inclusionary housing requirement city-wide as well as in areas where rezoning is envisioned to provide a comprehensive analysis and policy choice for the City Council.

Applying the inclusionary requirement city-wide would disperse the affordable units throughout the City so that they are not located only along commercial or industrial corridors envisioned for rezoning. However, this approach would produce less affordable units since the supportable set-aside percentages for the city-wide approach are less than the percentages for the rezoning areas.

Staff recommends that the inclusionary housing requirement be applied both city-wide and in the urban plan areas. KMA's draft Financial Evaluation has identified separate supportable set-aside requirements for both approaches. Any housing projects within the rezoning areas would be subject to those set-aside requirements (refer to Tables 3 and 4 above) and housing projects not within the rezoning areas would be subject to the city-wide set-aside requirement (refer to Tables 1 and 2 above). This means the inclusionary housing requirement would be applicable to all areas of the City but have different set-aside requirements depending on the specific area and housing type. By doing this, it would ensure the City would receive affordable units regardless of where a housing project is proposed.

<u>Stakeholders Feedback</u>

As part of staff's on-going analysis and research on inclusionary housing, staff held additional meetings after the first study session with local affordable housing advocate groups and housing developers with expertise in land development to seek input on the proposed policy recommendations. Staff conducted a total of four separate meetings via Zoom.

Below is a summary of the feedback from these meetings. This feedback was considered and incorporated into the draft Financial Evaluation and staff's recommendations presented in this report.

- **In-Lieu Fees:** Housing developers encouraged the City to adopt in-lieu fees that have the ability to be responsive to market conditions and can be updated frequently. Developers suggested that the City also review other jurisdictions in-lieu fee amounts to ensure feasibility.
- **Incentivize Workforce Housing:** Housing developers encouraged the City to incorporate incentives into the program that will result in providing more workforce housing projects. Workforce housing in this discussion referred to households that fall between the moderate and above moderate-income definitions.
- **State's Density Bonus:** Housing developers that use the State's density bonus will be entitled to lower "by right" parking standards defined by the State. Housing advocates, however, pointed out that if the estimated density ranges in the adopted Housing Elements were to be implemented then there may not be a need or desire to use the State's density bonus – which then may not produce very-low units for the City unless specifically required as part of the City's program.
- **Off-site Production Alternative:** Consider a program that offers flexibility for something akin to a transfer of development rights for the offsite development alternative.
- **Covenant Periods:** Housing developers were concerned that extended covenant periods may conflict with requirements from institutional investors.
- **Set-Aside Percentage:** Housing developers indicated that the proposed densities and affordability percentages should take into consideration what are feasible product construction types. Housing advocates were concerned with the low set-aside percentage at the lower density range.
- **Fairview Developmental Center (FDC):** Both groups agreed that FDC was a unique site with a unique opportunity to support a higher affordability requirement. Staff agreed and shared that a site-specific affordable housing requirement for FDC could be as part of the Specific Plan. Such a requirement can leverage the fact that the site is State-owned and therefore, there is potential flexibility in the site's sale price as a means of supporting high levels of affordable housing at the property.

Next Steps

Following the second joint study session, staff and KMA will finalize the Financial Evaluation (incorporating Planning Commission and City Council direction). KMA will then analyze and recommend an in-lieu fee structure for the program. In addition, staff would further study the City's existing residential parking standards especially for multi-family residential projects to either amend in the Zoning Code or include as special parking standards under the inclusionary housing ordinance.

Staff in coordination with the City Attorney's Office would then prepare an ordinance and in-lieu fee resolution, followed by implementing guidelines. The ordinance would be reviewed and recommended by the City's Planning Commission. Following Planning Commission's recommendation, the first reading of the draft ordinance would be presented to City Council for consideration. If the first reading is approved, the second reading would be scheduled for the next meeting. If the second reading is approved, then the ordinance becomes effective 30 days thereafter.

Subsequent evaluation of staff/consultant resources necessary to implement the new inclusionary housing program would be presented at a later date.

ALTERNATIVES:

The City Council could request an additional study session if additional information or analysis is needed to provide staff with further feedback and direction prior to drafting an ordinance.

FISCAL REVIEW:

There is no impact to the City's General Fund from a policy discussion pertaining to inclusionary housing. However, if the Council directs staff to move forward with preparation of a draft ordinance, staff will evaluate the fiscal impacts of such an ordinance, including the potential for revenue in the form of housing in-lieu fees and the potential for additional staff or consultant resources necessary to manage an affordable housing program over time.

LEGAL REVIEW:

The City Attorney's Office has reviewed and approved this report as to form.

CITY COUNCIL GOALS AND PRIORITIES:

This item supports the following City Council Goal:

- Diversify, Stabilize and Increase Housing to Reflect Community Needs

CONCLUSION:

Consideration of an inclusionary housing ordinance has been included in the City's Housing Element as part of an overall strategy to promote the creation of additional housing supply that is affordable to all segments of the Costa Mesa community. Furthermore, the inclusionary housing ordinance is included as a strategic plan objective and priority to accomplish the City Council's goal to "*diversify, stabilize and increase housing to reflect the community needs".*

Staff is seeking feedback from the City Council and Planning Commission regarding the findings of the draft Financial Evaluation, the policy recommendations, and any other policy considerations the Planning Commission or City Council would like to consider. Ultimately staff is seeking direction as to whether or not the Council would like staff to draft an inclusionary housing ordinance for consideration.