



Agenda Report

Item #: 24-011

Meeting Date: 01/16/2024

TITLE: AN ORDINANCE AMENDING TITLE 13 (PLANNING, ZONING AND DEVELOPMENT) OF THE COSTA MESA MUNICIPAL CODE TO ESTABLISH AFFORDABLE HOUSING REQUIREMENTS FOR NEW RESIDENTIAL DEVELOPMENT PROJECTS

DEPARTMENT: ECONOMIC AND DEVELOPMENT SERVICES DEPARTMENT/PLANNING DIVISION

PRESENTED BY: NANCY HUYNH, PRINCIPAL PLANNER

CONTACT INFORMATION: NANCY HUYNH, PRINCIPAL PLANNER, (714) 754-5609

RECOMMENDATION:

Staff recommends the City Council:

1. Find that the adoption of Ordinance No. 2024-XX is exempt from the California Environmental Quality Act (CEQA) per CEQA Guidelines Section 15061(b)(3), General Rule in that the affordable housing ordinance will not have a significant impact on the environment.
2. Give first reading to Ordinance No. 2024-XX (PCTY-23-0001) modifying Title 13 (Planning, Zoning, and Development) of the Costa Mesa Municipal Code (CMMC) to establish affordable housing requirements for new residential developments.

BACKGROUND:

In 2021, the City Council adopted a Strategic Plan identifying five key goals to address specific community issues and needs which included to **“diversify, stabilize, and increase housing to reflect community needs.”** To address this goal, the City Council also identified several objectives and priorities. One of the Council’s identified priorities included considering a draft inclusionary housing ordinance (also referred to as an affordable housing ordinance).

In addition, pursuant to State housing requirements, the City is required to plan for its Regional Housing Needs Assessment (RHNA) allocation of 11,760 units. Approximately 40% of its RHNA allocation falls into moderate, low, and very low-income housing. In response, the City’s Housing Element identifies 47 programs that work together to support and incentivize housing and affordable housing. Program 2A of the City’s 2021-2029 adopted Housing Element calls for the City to adopt an affordable housing ordinance which would generally require new housing projects in the City to provide a certain percentage of its housing units as affordable units to moderate, low, and/or very low-income households. Housing Element Program 2A states:

“As of adoption of the 6th Cycle Housing Element, the City of Costa Mesa is analyzing the market impacts and potential affordability requirements for an inclusionary housing requirement for specific projects. The City has hired a consultant to evaluate and make recommendations regarding the

structure of a potential inclusionary housing ordinance, including the affordability percentage requirement, potential for an in-lieu fee option, and other factors. As part of this effort, the City will consider the applicability of establishing a local preference policy.

Objectives: Adopt an inclusionary housing ordinance.”

Financial Evaluation

In order to identify a supportable affordable housing percentage and other policy recommendations, the City retained an expert housing consultant, Keyser Marston Associates Inc. (KMA). KMA prepared a draft Financial Evaluation (FE) report in July 2023, which was supplemented in November 2023. The Financial Evaluation is an analysis that determines the financial impact of applying an affordable housing requirement on a housing development project. Based on that potential financial impact, the FE determines the supportable affordable housing requirement that the City could impose on new residential developments without being “confiscatory”.

The completed FE and supplemental analysis were made available online on the City’s Affordable Housing Ordinance webpage and the links are included below. Staff and KMA’s recommendations are discussed in detail in the Analysis section of this report.

- KMA Financial Evaluation (July 11, 2023):
https://www.costamesaca.gov/home/showpublisheddocument/54969/638253773_340200000
- KMA Supplemental Analysis (November 6, 2023):
<https://www.costamesaca.gov/home/showpublisheddocument/55858/638351433427070000>

City Council and Planning Commission Joint Study Sessions

On May 16, 2023 and subsequently on July 26, 2023, City Council and Planning Commission held two joint study sessions to discuss an affordable housing ordinance for Costa Mesa. The first study session provided a general overview of affordable housing program best practices while the second study session focused on the preliminary findings of KMA’s draft FE. City Council and Planning Commission also received public comments at both study sessions as well as provided feedback regarding KMA’s policy recommendations to be incorporated in a draft ordinance.

The May 16, 2023 study session agenda report, meeting video, and public comments 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

- May 16, 2023 Study Session Public Comments:
<https://costamesa.legistar.com/View.ashx?M=E3&ID=1103184&GUID=F4CDF38E-2EEE-4D0C-8B90-ADB54899FEF6>

The July 26, 2023 study session agenda report, meeting video, and public comments are included in the links below:

- July 26, 2023 Study Session Agenda Report:
<https://costamesa.legistar.com/View.ashx?M=F&ID=12177354&GUID=A49D2109-3609-4770-A7CE-76223D45F377>
- July 26, 2023 Study Session Meeting Video:
https://costamesa.granicus.com/player/clip/4019?view_id=14&redirect=true&h=a7972baf3ae0c1909cbb73e6a43d05fe
- July 26, 2023 Study Session Public Comments:
<https://costamesa.legistar.com/View.ashx?M=E3&ID=1113344&GUID=50122EA8-6A28-42B3-BB2F-5D5434897623>

Planning Commission Public Hearings

Following the joint study sessions, staff prepared a draft ordinance for Planning Commission review and recommendation to City Council. The Planning Commission held two public hearings on November 13, 2023 and December 11, 2023 to discuss the draft ordinance.

At the first public hearing, staff presented the draft content intended to be included in the proposed affordable housing ordinance. The Planning Commission received staff's presentation as well as public comments, discussed the item, and voted 4-0 (Chair Ereth, Commissioner Rojas, and Commissioner Klepack absent) to continue the item to December 11, 2023.

The November 13, 2023 Planning Commission agenda report, meeting video, and public comments are included in the links below:

- November 13, 2023 Planning Commission Agenda Report:
<https://costamesa.legistar.com/LegislationDetail.aspx?ID=6413792&GUID=4C906E13-F94B-49E9-AD3E-73B588C6EB6E>
- November 13, 2023 Planning Commission Meeting Video:
https://costamesa.granicus.com/player/clip/4063?view_id=14&redirect=true&h=f22a251337c41beb55301395ff67cc2
- November 13, 2023 Planning Commission Public Comments:
<https://costamesa.legistar.com/View.ashx?M=E3&ID=1135455&GUID=7ECD4C06-87E5-4283-8149-4BFF97215AA2>

At the subsequent Planning Commission meeting, staff presented the final draft affordable housing ordinance for recommendation to City Council. The Planning Commission recommended changes to the draft ordinance and voted 5-2 (Commissioner Zich and Commissioner Andrade voting no) to recommend the City Council give first reading of the ordinance. The Planning Commission's recommended changes are detailed further in the Analysis section of this Agenda Report.

The December 11, 2023 Planning Commission agenda report, meeting video, and public comments are included in the links below:

- December 11, 2023 Planning Commission Agenda Report:
<https://costamesa.legistar.com/LegislationDetail.aspx?ID=6448847&GUID=F06836A7-2485-4993-A2B9-7413119EBE05>
- December 11, 2023 Planning Commission Meeting Video:
https://costamesa.granicus.com/player/clip/4071?view_id=14&redirect=true&h=3afc5737bffd6e2094027c9beb28f56c
- December 11, 2023 Planning Commission Public Comments:
<https://costamesa.legistar.com/View.ashx?M=E3&ID=1145138&GUID=D27058F5-3E1C-458F-BC71-819FE295D4F8>

Stakeholders Meetings

In addition to the joint study sessions, KMA's FE and policy recommendations, and staff's research, the process of drafting the affordable housing ordinance also involved a total of 17 stakeholder meetings with local affordable housing advocate groups and local housing developers with expertise in land development and affordable housing. The meetings were conducted both in person at City Hall and virtually through Zoom.

The meetings included residents from the Costa Mesa community and representatives from the following organizations: Affordable Housing Coalition, The Irvine Company, Sakioka Company, Legacy Partners, City Ventures, The Olson Company, Red Oak Investments, Kennedy Commission, People for Housing, OC Resilience, and the Building Industry Association. In addition, staff and/or KMA have had conversations with the cities of Huntington Beach, Irvine, Santa Ana and several other cities about their experiences with adopting and managing an affordable housing program. Staff and KMA also met one-on-one with developers that have specific experience in developing housing projects in Costa Mesa who were willing to discuss their development and construction cost projections to ensure that the FE's projections were reflective of actual residential project costs. The proposed draft ordinance is reflective of the stakeholders' input which included the importance of focusing policy on very-low income households (in addition to low-income), requiring onsite production of affordable units, setting affordable housing percentages at a level that would not disincentivize housing projects, and providing incentives such as flexible parking requirements and concurrent processing of entitlement application(s) with plan check review to further encourage housing production.

ANALYSIS:**Costa Mesa Community Profile**

Approximately 47-percent of the Costa Mesa community earn a lower income and approximately 29-percent of the community qualify for very low or extremely low-income housing. However, lower income households in Costa Mesa cannot afford to own or rent in Costa Mesa without experiencing overpayment. Per State guidance, a household should generally spend no more than 30-percent of gross income on housing expenses including utilities. The current average rent for a market rate one-bedroom apartment unit in Costa Mesa is approximately \$2,700 yet nearly half of renters in Costa Mesa experience housing cost burdens that exceed 30-percent of gross income and over a quarter of renters experience severe housing cost burdens that exceed 50-percent of gross income. Recent average for sale home prices in Costa Mesa are over \$1 million yet the home price that a moderate-income level household could afford for a three-bedroom house is approximately \$500,000. This data indicates a general mismatch in incomes versus housing expenses and a lack of affordable housing units to meet the community's current and future housing needs

Unfortunately, affordable housing options including deed restricted units are very limited in Costa Mesa. Without an affordable housing requirement or redevelopment-based funding programs, newer housing projects have produced market rate housing units. In addition, deed restricted affordable housing units that were constructed in the 1980s and 1990s have since expired and reverted to market rate. As such, production of and access to affordable housing options for lower income households is limited and is unlikely to be remedied by the market or additional housing supply alone. One of the tools that many cities throughout the state and country have utilized to help make progress toward affordable housing goals is an affordable housing ordinance (also referred to as inclusionary housing).

Policy Context

Inclusionary housing programs are not new and in fact, have been used to address affordable housing issues since the 1970s. Since then there have been over 700 other cities across 31 states with an adopted affordable housing ordinance. In California, there are more than 170 jurisdictions with an adopted ordinance including eight from Orange County with some that have existed and produced affordable units within their community for over 30 years. For example, Santa Ana has been able to produce nearly 3,500 affordable rental units and Huntington Beach has produced over 2,500 affordable rental units as part of their inclusionary housing program. These two cities have also collected in-lieu fees and accumulated a sufficient amount to subsidize 100% affordable housing projects and other programs aimed at promoting entry into the ownership housing such as providing down payment assistance for first-time homebuyers.

While an affordable housing ordinance is one tool to address housing affordability, it is not anticipated to produce all of the affordable units that the City is mandated to plan for pursuant to the RHNA allocation. The affordable housing ordinance is one of many housing programs in the City that complement each other to address housing and affordability issues. Existing programs include tenant eviction protection, rental assistance programs, accessory dwelling unit programs, and the City's Bridge Shelter. Programs also underway include the corridor visioning and rezoning effort and development standards update intended to promote new ownership and rental housing opportunities overall in compatible areas of the City.

Although these programs are starting to address the issue, these programs alone do not produce new affordable units or require housing developers to do so. An affordable housing ordinance would help the City meet this specific need by requiring new housing projects to set aside a percentage of new units as affordable and maintain those units as affordable for a specific timeframe (as proposed in the ordinance – 45 years for ownership and 55 years for rental units). Collected in-lieu fees as part of the affordable housing program requirement would also assist the City by creating a Housing Trust Fund that could be used to fund affordable housing projects and new programs.

Furthermore, adoption of the ordinance would help the City maintain compliance with State housing laws since the affordable housing program is listed in the City's adopted Housing Element. The City is required to implement this program within one year of the Housing Element adoption in order for the City to remain consistent with its Housing Element. If the City does not adopt one, the State could find the City out of compliance with State law requirements making it more vulnerable to legal challenges which could ultimately result in the loss of local control over land use and permitting decisions.

An Incentive-Based Program

The City's proposed Affordable Housing Program has been structured as an "incentive-based program" that uses the City's rezoning along commercial/industrial corridors for housing to create value and incentivize housing production overall, while coupling the creation of that value with a requirement to provide a portion of the project's units as affordable housing. This program structure is in effect a local density bonus program.

To implement the affordable housing program, the City would implement its rezoning program described in the City's approved Housing Element – which would rezone non-residentially zoned properties located along major commercial and industrial corridors to allow for housing where housing does not currently exist and at increased densities with reduced parking requirements. The rezone and increase in density creates opportunities for new homes that presently do not exist because of the lack of available properties that allow residential uses and the historically low maximum allowable density in Costa Mesa (maximum of 20 units per acre pursuant to the City's General Plan). Rezoning would create value and thus, incentivizing land owners to sell commercial and industrial properties to housing developers and incentivize housing developers to build. In doing so, the City would require a portion of the added value to be used to provide the required affordable units under the City's Affordable Housing Program.

The affordable housing program consists of four main components:

- 1) Project threshold size (minimum number of housing units subject to the ordinance);
- 2) Required percentages of affordable units;
- 3) Required income levels for affordable units; and
- 4) Covenant period (required length of time that units must remain affordable).

Planning Commission's Recommendation

The Planning Commission discussed each proposed affordable housing program component. Table 1 below provides a summary of staff's recommendations and the Planning Commission's recommended changes:

TABLE 1 – SUMMARY OF AFFORDABLE HOUSING PROGRAM COMPONENTS		
PROGRAM COMPONENT	PLANNING COMMISSION RECOMMENDATIONS	FINANCIAL EVALUATION/STAFF RECOMMENDATIONS
Project Threshold*	<ul style="list-style-type: none"> 60+ dwelling units per acre; two-acre minimum (Effectively a 120 unit threshold) 	<ul style="list-style-type: none"> 10 units
Number of Affordable Units/Required Income – Rental*	<ul style="list-style-type: none"> 10% at low-income or 5% at very-low income 	<ul style="list-style-type: none"> 60+ du: 11% at low-income or 7% at very-low income Under 60 du: 6% at low-income or 4% at very-low income
Number of Affordable Units/Required Income – Ownership*	Exempt ownership projects	<ul style="list-style-type: none"> 8% at moderate-income if providing onsite affordable units, or payment of in-lieu fee by right
Covenant Period – Rental	At least 55 years	At least 55 years
Covenant Period – Ownership	N/A	45 years (if producing affordable units onsite)
Affordable Unit Minimum Size	No more than 15% smaller than average market rate unit	No more than 15% smaller than average market rate unit
Affordable Unit Bedroom Mix	Proportional to market rate units	Proportional to market rate units
Affordable Unit Location	Evenly distributed/dispersed throughout residential project	Evenly distributed/dispersed throughout residential project
Alternatives for Compliance	<ul style="list-style-type: none"> Land dedication Offsite construction of affordable units Payment of in-lieu fees Onsite construction of rental units (ownership only) 	<ul style="list-style-type: none"> Land dedication Offsite construction of affordable units Payment of in-lieu fees Onsite construction of rental units (ownership only)
Incentives	<ul style="list-style-type: none"> Allow residential uses in commercial/industrial corridors Increased densities Allow low income rents to be charge based on 80% AMI vs 60% AMI (required by State density bonus) Reduced parking requirements Concurrent processing 	<ul style="list-style-type: none"> Allow residential uses in commercial/industrial corridors Increased densities Allow low income rents to be charge based on 80% AMI vs 60% AMI (required by State density bonus) Reduced parking requirements Concurrent processing
<p>* These program components are the main differences between Planning Commission and the Financial Evaluation/staff's recommendations.</p>		

Based on the Planning Commission’s recommendation, staff updated the draft affordable housing ordinance for City Council’s review. The Planning Commission recommended changes are described below in further detail and shown as strikethrough and underline text in Attachment 2:

• **Project Threshold – Ordinance Section 13-38.1 and 13-330(a)**

Staff recommended a project threshold size of ten units based on the size of housing projects typically experienced in Costa Mesa. At ten units, the ordinance would not apply to the majority of infill projects on small lots, while projects at ten or more units would be required to provide onsite affordable units or to pay an in-lieu fee. Locally in Orange County, the threshold size ranges from zero, meaning requirements apply to any housing project (City of Irvine) to 20 units (City of Brea).

The Planning Commission recommended the minimum project threshold be higher and based on a housing project's proposed density (60+ dwelling units per acre) and/or project site size (two-acre minimum site size). This would mean any new housing projects under 60 dwelling units per acre and/or any projects under two-acres (even if over 60 dwelling units per acre) would be exempt from the ordinance's requirements and would not provide onsite affordable units or pay housing in lieu fees. Compared to staff's recommendation, and assuming a two-acre site at 60 dwelling units per acre, this would mean projects with 120 units and under would not be subject to the ordinance.

It should be noted that approximately 30% of the "housing opportunity sites" listed in the Housing Element and shown in Attachment 5, Corridors Map, are two or more acres. (Refer to Page 26 of [Appendix B of the Housing Element](#) for a complete list of the housing opportunity sites.) Thus, increasing the threshold would reduce the number of affordable units (or their related housing in lieu fees) that would result from the ordinance.

- **Required Number/Percentage of Affordable Units – Section 13-330(b)(1a)**

Staff and KMA recommended requiring 11% of a housing project's units be provided at the low-income level, or 7% at the very-low income level which is the supportable recommendation based on the FE's "improved land" scenarios. KMA's financial analysis is based on a conservative approach that balances the City's need for affordable housing while not discouraging the development of housing in general. In addition, the analysis is unique to each city's real estate market conditions since it is based on actual land value and sales data from that area. If adopted, the affordable housing ordinance would be re-evaluated on a continued basis to ensure the requirements reflect current market conditions which has been similarly done on several occasions by Santa Ana and Huntington Beach.

The Planning Commission recommended the required number or percentages of affordable units be lower to be consistent with the surrounding Orange County cities such as Santa Ana (15% at low-income, 10% at very-low income, or 5% at extremely-low income) and Huntington Beach (10% at low-income or 5% at very-low income); refer to Attachment 3 for a comparison table. The Planning Commission recommended that the required affordable percentages should be 10% at the low-income level and 5% at the very-low income level.

- **Exempt Ownership Housing Projects – Section 13-328**

Staff and KMA recommended requiring 8% of an ownership housing project's units to be provided onsite at the moderate income level, or to allow a developer to fulfill the requirement with payment of in-lieu fees for any size ownership project. (For rental projects 100 units or less, the ordinance allows payment of in-lieu fees, but any rental project over 100 units is required to provide affordable units onsite).

The in-lieu fees collected would be used to fund housing projects and programs that could include 100% affordable projects or financial assistance for a first-time homebuyer. New ownership units incentivized through the City's rezoning program would help improve the ownership to renter ratio in the City while in homebuyer programs create an easier path to those homeownership opportunities.

The Planning Commission recommended that applying the affordable housing requirements (even just in lieu fees) could be a barrier that could discourage ownership housing projects. As such, they recommended to exempt any ownership housing projects from the affordable housing ordinance's requirements.

Exempting ownership projects from the affordable requirements altogether would mean all new ownership housing units would likely be market rate and in addition, such projects would not contribute funds (through in-lieu fees) to programs that could promote affordable ownership projects or otherwise support homebuyers. It should be noted that KMA's FE did support applying the requirements to ownership projects and determined that doing so would not cause an undue constraint and would allow a developer a fair return.

Staff Resources

The Department is already restructuring its existing entitlement staff to create a housing-focused team as part of its overall program to improve efficiencies and customer service and promote housing opportunities in Costa Mesa. The vacant Planning and Sustainable Development Manager and Senior Planner positions are being filled and, along with existing planning staff, will continue to more efficiently review and process housing projects.

If an inclusionary ordinance is adopted, it would create a new housing program that would require additional staff and consultant resources to implement, manage, monitor, and enforce the ordinance. Such tasks would include but are not limited to the collection and management of in-lieu fees, preparation of requests for proposals for housing projects funded by in-lieu fees, agenda reports for the allocation of in-lieu housing funds, development of community development partnerships, preparation and monitoring of affordable housing agreements for each inclusionary project, annual rent certifications to ensure required units are rented to households at the appropriate income levels, and appropriate tracking and reporting of units to the State annually.

Initially, these responsibilities could be absorbed by the Department's existing Housing and Community Development team, particularly when the program is in its infancy and in lieu fees are still being collected. However, as the program matures and as affordable housing projects develop, a manager position will likely be necessary to lead and administer this program. The City Manager's Office and the Department will continue to evaluate Department staffing and bring a recommendation to the City Council concurrently with its mid-year or annual budget.

In addition, initially staff will utilize the Department's existing consulting budget and third-party plan check contract services to process concurrent plan checks for housing projects, when in house staff resources are at maximum utilization. Annual budget and contract amounts for plan check services will be reviewed and adjusted if necessary as part of the annual budget process.

Next Steps

If the City Council approves the first reading, staff will return at the next meeting for second reading. If approved, the Ordinance becomes effective 30 days after second reading. In addition, KMA will immediately complete an in-lieu fee study which will be presented to the Council for adoption by Resolution, concurrently with the effective date of the Ordinance. Staff in consultation with KMA will also prepare Affordable Housing Program procedures and templates concurrently with the effective date of the Ordinance. KMA's efforts would require a contract amendment but would be funded within the existing Department budget.

ALTERNATIVES:

The City Council could modify the ordinance and direct staff to return with an update to the draft for an additional first reading. City Council could also not approve the Ordinance, which may subject the City to litigation and/or other State enforcement actions.

FISCAL REVIEW:

Fiscal impacts of the ordinance include 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 agenda report and draft Ordinance has been reviewed and approved as to form by the City Attorney's Office.

CITY COUNCIL GOALS AND PRIORITIES:

This item supports the following City Council Goal:

- Diversify, Stabilize and Increase Housing to Reflect Community Needs

CONCLUSION:

The adoption of the proposed Affordable Housing Ordinance would require new residential development projects that meet the minimum threshold size to set aside a portion of its new units as "affordable units" for a 45- to 55-year timeframe. Its adoption would fulfill the objective of Program 2A of the 2021-2029 General Plan Housing Element and help achieve City Council's goal to "diversify, stabilize and increase housing to reflect community needs".