# Inclusionary Housing Ordinances and Housing Production

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Californians are facing the effects of a housing crisis that has been mounting for decades across the state. The California Housing Partnership estimates that increases in housing costs in California have outpaced wage growth by 32% since 2000. As a result, the majority of renters in California are burdened by the cost of housing, meaning they spend more than 30% of their monthly income on housing costs, according to the Public Policy Institute of California. The disparity between high housing costs and comparatively low wages in California has created an immense need for affordable housing. While developing housing is primarily the private sector's role, the state requires local governments to plan for the development of a number of housing units for people of different income levels. The number of units needed at very low, low, moderate, and above moderate-income levels in each of California's eighteen regions is determined by the California Department of Housing and Community Development (HCD) through the Regional Housing Needs Assessment (RHNA), for a period of eight years. The governing association for each region is responsible for allocating their RHNA among the municipalities in their jurisdiction. To complete their RHNA allocation of units, many municipalities in California implement policies meant to increase the production of affordable housing. One such policy is an inclusionary housing ordinance (IHO). An IHO is a city or countywide requirement for a certain percentage of new housing developments be made affordable. The specifics of IHOs vary, but most require that 10-15% of new housing units be made affordable, and many allow developers to pay an "in lieu fee" instead of building affordable housing. As the housing crisis in California continues to worsen, many municipalities are considering joining the hundreds in California already using IHOs.

Inclusionary housing ordinances first appeared in

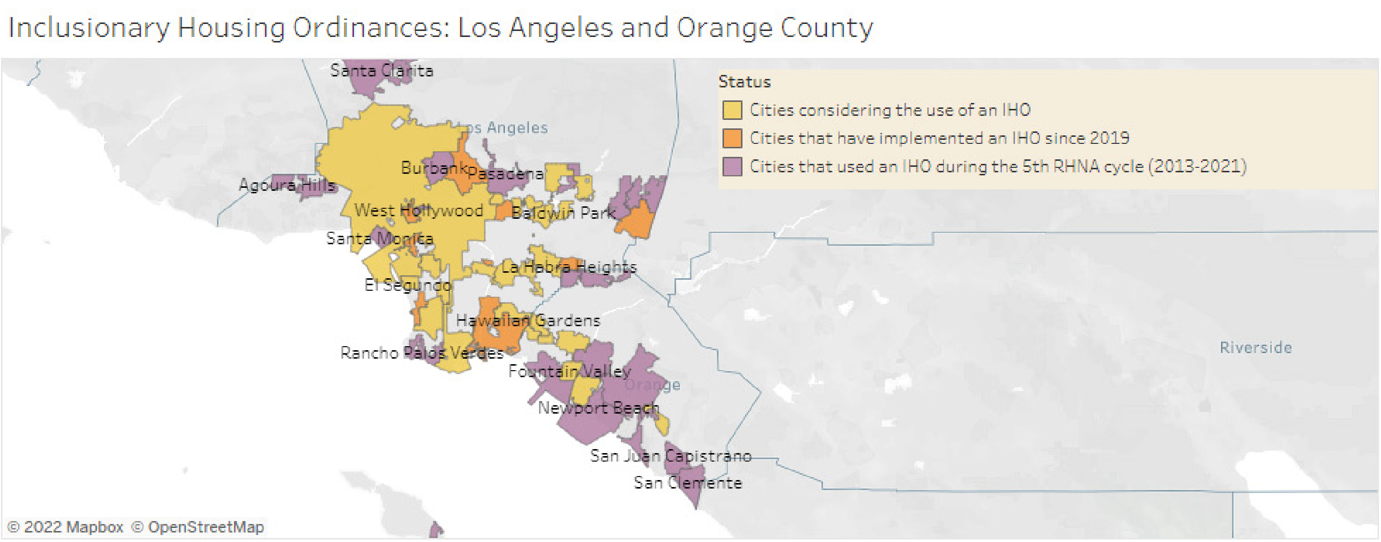
California in the early 1970s. The 1970s marked the start of an increasing disparity between housing prices and wages in California, and many municipalities began to look for ways to advance affordable housing. Orange County was among the first in California to adopt an IHO, in response to a growing need for affordable housing throughout the county. Orange County's IHO was later phased out, but throughout the following decade dozens of new IHOs were implemented in California. By the 1990s, a study by the California Coalition for Rural Housing showed that 64 California local governments were using IHOs. In 2003, a study by the Non-Profit Housing Coalition of Northern California (NPH) concluded that this number had nearly doubled to 107. The most recent statewide study on IHO programs, conducted in 2007 by NPH, shows that there are 170 jurisdictions using IHOs. Although there has not been a statewide study of IHOs conducted since 2007, the number of jurisdictions using IHOs has likely increased following new legal precedent and pressures from the state to increase the availability of affordable housing.

The legality of inclusionary housing ordinances has long been contested in California. Throughout the early 2000s, a number of lawsuits were brought against cities using IHOs. In 2001, the City of Napa had its IHO upheld by the courts in *Home Builders Association of Northern California v. City of Napa*. Similar decisions in favor of IHOs were reached in *Action Apartments Assn v. City of Santa Monica* in 2008, and in *California Building Industry Assn. v. City of San Jose* in 2013. These cases primarily established the right of cities to use IHOs to compel developers to sell a percentage of units at an affordable rate. They did not raise the issue of cities requiring developers to set rent at an affordable rate. In 2009, IHOs relating to rent were challenged in *Palmer/Sixth Street Properties, L.P v. City of Los Angeles*, and were declared invalid under the Costa-Hawkins Act of 1995, which greatly limited rent control in the state. After the decision in *Palmer v. City of Los Angeles*, many municipalities suspended their IHOs, or modified them to allow for developers to opt out by paying a fee instead of producing affordable housing. Nearly a decade passed with IHOs in a largely unenforceable limbo, until the passing of California Assembly Bill 1505 in 2017. AB1505 authorized any city or county in California to adopt ordinances requiring new developments in their jurisdiction to include a percentage of affordable housing for moderate-income, low-income, very low-income, or extremely low-income households. It also included a provision to allow the Department of Housing and Community Development to require cities to implement IHOs, but this provision does not take effect until 2027.

With the legality of IHOs in California now established by AB 1505, the question remains as to whether IHOs are an effective tool to produce affordable housing. A 2004 study of IHOs in Los Angeles County and Orange County by the Reason Foundation found that IHOs had an adverse effect on the price and production of housing in cities where they were used. By analyzing the production of affordable housing in thirteen cities with IHOs, the Reason Foundation study concluded that IHOs only resulted in the production of 34 affordable units each year on average. In addition to this relatively low production of affordable housing, the study found that each inclusionary housing unit came at a cost of over $570,000, by comparing a hypothetical affordable price to the average market rate cost for housing in each city. The results of the Reason Foundation study are supported by a more recent study conducted by university researchers in 2009 titled "Market Effects of Inclusionary Zoning." This study analyzed housing prices in California from 1988-2005 and determined that jurisdictions using IHOs experienced an increase in the cost of single-family homes.

Other studies challenge the conclusion that IHOs can have negative effects on the housing market. One, "Can Inclusionary Zoning Be an Effective and Efficient Housing Policy? Evidence from Los Angeles and Orange Counties," was conducted by academic researchers and the housing non-profit organization Adobe Communities in 2010. It studied the effectiveness of IHOs in Los Angeles and Orange Counties by comparing them to other affordable housing policies and analyzing the impact of IHOs on housing markets. This study determined that there is little evidence to support an adverse effect of IHOs on housing supply in Los Angele County or Orange County. The main difference in methodology between the 2010 study and other studies which drew contrary conclusions, such as the Reason Foundation's 2004 study on IHOs, was the 2010 study's recognition that many cities use incentives to offsets costs to developers in tandem with their IHOs.

Most California municipalities with IHOs use a variety of methods to reduce the cost of building affordable housing for developers, including density bonuses, fee reductions, and subsidies. These developer incentives help to prevent developers from pushing costs incurred by IHOs onto the housing market. By recognizing these incentives in its research, the 2010 study determined that IHOs with density bonuses result in an overall increase in the supply of housing. A more recent study of IHOs in Southern California conducted in 2015 by a researcher at the University of California Irvine supported the findings of the 2010 study. Using a survey sent out to Los Angeles, Orange, Riverside, San Bernardino, and Ventura counties, the 2015 study showed that over 80% of cities using IHOs in Southern California also offer density bonuses and other incentives to developers as a means of encouraging the production of affordable housing. By analyzing the production of affordable housing in those five counties, the study concluded that cities using both IHOs and several incentive programs were more likely to produce affordable housing.



Map: Daniela Corona'23

While current research suggests that IHOs paired with developer incentives can increase the supply of affordable housing, potential differences in the efficacy of IHOs in coastal and inland municipalities have not been adequately examined. Existing studies on IHOs in California have focused primarily on densely populated coastal communities, such as Orange County and Los Angeles County, leaving a significant gap in research concerning the use of IHOs in inland municipalities. Inland cities in California are typically less built out than urbanized coastal cities, and they have considerably different housing markets as a result. The lack of research on IHOs in inland California is an impediment to many local governments' abilities to make informed housing policy decisions. It is especially important that information on IHOs in inland California be available in the near future, as many municipalities are restructuring their housing policies for the 6th cycle of RHNA and Housing Elements.

This article aims to address the current shortcomings of research on IHOs in California by comparing the use of IHOs in Riverside County and San Bernardino County to Los Angeles County and Orange County. It focuses on the questions: Do cities in inland Southern California counties use IHOs on a similar scale to those in coastal counties, and are IHOs in either area effective at accomplishing RHNA requirements for affordable housing? We analyze this question by comparing the progress made by cities with and without IHOs in each county on completing their 5th cycle RHNA housing allocations, which spanned 2013-2021. Production of affordable housing was estimated by the number of permits for housing units approved at very low and low-income levels during the 5th cycle. Production levels were then compared between cities in Los Angeles County, Orange County, Riverside County and San Bernardino County to identify any differences in the effectiveness of IHOs in inland and coastal areas of California that previous studies may have overlooked. This study builds upon previous research concerning the efficacy of IHOs, but its results were more representative of the diversity of housing markets in cities across California.

To analyze the use and efficacy of IHOs in Los Angeles County, Orange County, Riverside County and San Bernardino County, we studied the Housing Element and municipal code of each city in these counties to determine where IHOs are used. Only IHOs used in the 5th cycle of Housing Elements and RHNA allocations, from 2013-2021, were considered. IHOs which were not in use for more than three years, meaning they were either implemented and quickly repealed or implemented after 2019, were not considered to have significantly influenced housing production during the 5th cycle, but were noted in the study. In inland counties, six cities with IHOs were identified. These were Chino Hills, Fontana, Highland, Montclair and Yucaipa in San Bernardino County, and Calimesa in Riverside County. In coastal counties, twenty-three cities with IHOs were identified. These cities were Brea, Huntington Beach, Irvine, Laguna Beach, Laguna Woods, La Habra, Newport Beach, San Clemente, San Juan Capistrano, and Santa Ana in Orange County, and Agoura Hills, Avalon, Burbank, Calabasas, Claremont, Duarte, La Verne, Pasadena, Rancho Palos Verdes, San Dimas, Santa Clarita, Santa Monica and West Hollywood in Los Angeles County.

We then utilized the Annual Progress Report (APR) data published by HCD to determine each city's prog-

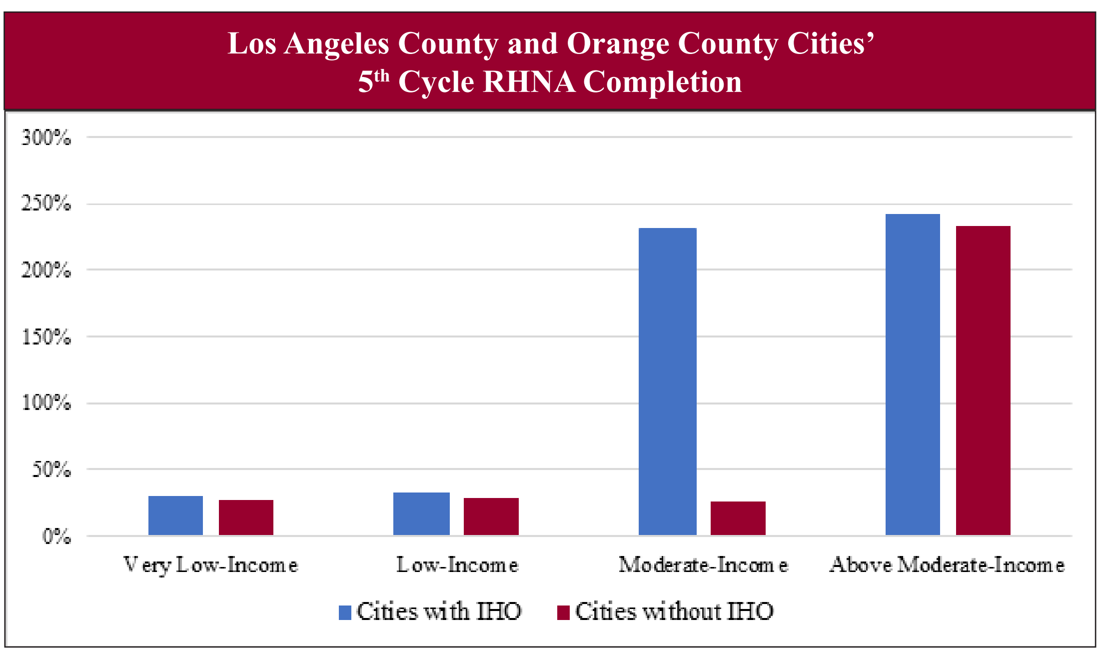



**Figure 1**: Comparison of 5th cycle RHNA completion of cities in Los Angeles County and Orange County based on their use of IHOs

ress towards completing their 5th cycle RHNA allocation for very low, low, moderate, and above moderate-income housing units. Data for very low and low-income units was used to estimate the amount of affordable housing developed in each city. Data for moderate and above moderate units was included to test whether cities with IHOs experienced a decrease in housing development at higher income levels. We also included the total RHNA allocation to each city for the 5th cycle to measure each city's progress towards completion. We collected data for each city in Los Angeles County, Orange County, Riverside County and San Bernardino County, divided it between inland and coastal regions, and split it into categories for cities with IHOs and cities without IHOs.

In the two coastal counties, cities with IHOs completed a greater percentage of their RHNA allocation for affordable units than cities without IHOs. Cities with IHOs completed 31% of their RHNA allocation, with 4,476 permits approved for very low and low-income units. Cities without IHOs approved 16,463 permits, which represents a greater number of units overall, but only a 27% RHNA completion rate. Cities with IHOs in coastal counties also completed a greater percentage of their RHNA allocation for moderate and above moderate-income housing than those without, with 51,266 permits approved for a 239% RHNA completion rate. In cities without IHOs, permits were approved for 156,008 moderate and above moderate-income units for a RHNA completion rate of 175%. These findings indicate that cities with IHOs in coastal counties did not experience a decrease in the production of housing in other sectors. In fact, as shown in Figure 1, cities with IHOs in coastal counties completed a greater percentage of their RHNA allocation in every income category than cities without IHOs.

In the two Inland Empire counties, IHOs had a similarly positive effect on the production of affordable housing. In cities with IHOs, permits were approved for 504 very low and low-income units during the 5th cycle, which represents a 10% RHNA completion rate. In cities without IHOs, permits were approved for 2,231 very low and low-income units for a 5% RHNA completion rate. For moderate and above moderate-income housing, cities in inland counties with IHOs approved permits for 6,835 units for an 88% RHNA completion rate. In cities without IHOs, permits were approved for 44,273 units at these income levels for a 66% RHNA completion rate. As

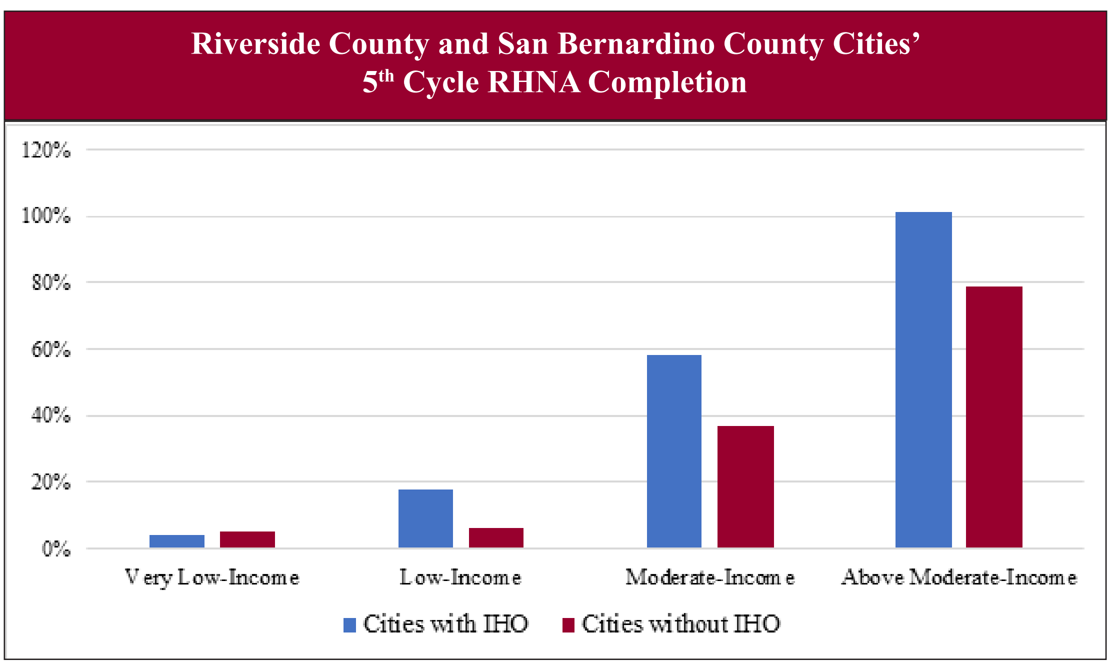
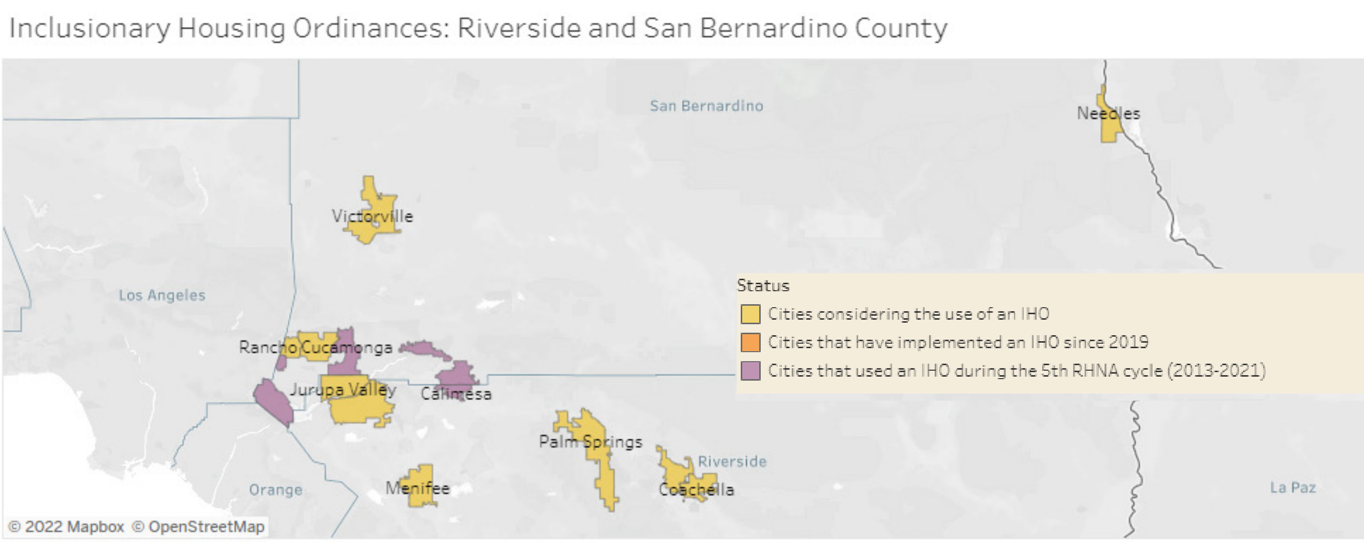



**Figure 2:** Comparison of 5th cycle RHNA completion of cities in Riverside County and San Bernardino County based on their use of IHOs

shown in Figure 2, cities with IHOs in inland counties completed a slightly smaller percentage of their very low-income housing RHNA allocation than cities without IHOs, but they achieved a greater percentage of their allocations in every other income category.

Several conclusions regarding the use of IHOs and the production of housing in inland and coastal counties in Southern California can be drawn from the Rose Institute study. Nearly one in every four cities in coastal counties uses an IHO while only one in seven cities in inland counties does. This difference may be a result of increased concerns in inland cities that IHOs will deter housing developers, whereas coastal cities typically have higher levels of developer interest regardless of additional taxes or fees. Nonetheless, cities with IHOs in both inland and coastal counties collectively completed a greater percentage of nearly every 5th cycle RHNA allocation category. The one exception to this is the very low-income category for the inland counties, but here the difference between housing production for cities with and without IHOs was only 1%. These findings not only demonstrate that cities with IHOs usually complete a greater percentage of their affordable housing RHNA allocations, they also show that IHOs do not seem to have a negative effect on housing production in other sectors of the housing market.

Although this study's findings indicate that IHOs can increase housing production without reducing production at other income levels, there are several limitations to the study. First, determinations about which cities in Los Angeles County, Orange County, Riverside County and San Bernardino County use IHOs were based solely on an analysis of city information available online, which is not always up to date. Second, this study had a relatively small sample size of only 29 cities with IHOs and 143 cities without. This allowed outlier cities such as Irvine, which alone produced more housing than all other Los Angeles County and Orange County cities with IHOs combined, to potentially skew the results. Third, in-lieu fees that allow developers to opt out of IHO requirements were not adequately addressed in this study. Nearly every city with an IHO in all four counties uses a form of an in-lieu fee, and many developers choose to pay this fee instead of building affordable housing. These fees are often set aside and used to subsidize future affordable housing developments, but such funds are not reflected in the RHNA data used in this study. Finally, higher levels of housing production in cities with IHOs may be a result of a third variable such as a city government's willingness to encourage and approve housing development – rather than the direct result of IHOs.



Map: Daniela Corona'23

The Rose Institute study can also be used to analyze differences in the overall production of housing in inland and coastal counties. Cities in Los Angeles County and Orange County collectively approved more permits and completed a greater percentage of their RHNA allocations at every income level compared to cities in Riverside County and San Bernardino County. With a growing population of over 7 million people, compared to Riverside County and San Bernardino County's combined population of 4.6 million, it is to be expected that cities in Los Angeles County and Orange County would receive a larger RHNA allocation and approve more permits as a result. In fact, they received a 5th cycle RHNA allocation roughly one and a half times larger, which is nearly equal to their current population difference.

This proportionality did not hold up during the 5th RHNA cycle, however, as coastal cities approved permits for over four times the amount of housing as inland cities. In other words, cities in Riverside County and San Bernardino County only completed 43% of their total 5th cycle RHNA allocation with permits approved for 53,038 units. Cities in Los Angeles County and Orange County, in comparison, completed 123% of their total RHNA allocation with permits approved for 228,213 units. The stark contrast between housing production in coastal and inland cities during the 5th RHNA cycle demonstrates a conflict between RHNA allocations and the housing market in Southern California. The Southern California Association of Governments (SCAG), which allocated the RHNA requirements from HCD to the four counties, appears to want more housing built inland, whereas housing developers still greatly favor the coast.

Coastal cities approved a greater number of permits than required by their RHNA allocation, but the vast majority of these permits were for above moderate-income units. In Los Angeles and Orange County, cities collectively completed 235% of their collective RHNA allocation for above moderate-income units, approving permits for 186,987 units during the 5th RHNA cycle. Similarly, in Riverside and San Bernardino County, 81% of the RHNA allocation for above-moderate income units was completed with 41,377 permits approved. Above moderate units represented the largest share of permits collectively approved by cities in all four counties. At the same time, few cities came close to completing their very low, low, and moderate-income RHNA allocations. Riverside County and San Bernardino County cities collectively only completed 5% of their very low, 7% of their low and 40% of their moderate-income RHNA allocations. Los Angeles County and Orange County cities came closer, but fell short at 27% completion of very low-income, 30% of low-income and 65% of moderate-income RHNA allocations. Several individual cities in the counties studied such as Santa Ana, West Hollywood and Westminster were able to complete their RHNA allocations at these income levels. This was not the case for the majority of cities.

This study noted that twenty-seven cities in Los Angeles County, six cities in Orange County, six cities in Riverside County and four cities in San Bernardino County have recently started to consider the use of an IHO, or have implemented an IHO since 2019. With the availability and affordability of housing in California on the line, it is imperative that local governments are well informed when choosing whether to implement IHOs, and in all of their housing policy decisions. ◆

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