

# **INCLUSIONARY HOUSING: A DISCUSSION OF POLICY ISSUES**

*Prepared for  
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## **Overview of Inclusionary Housing**

Inclusionary housing policies promote the production of affordable housing in a local jurisdiction either by requiring that all new housing developments include a percentage of affordable units or by providing incentives to developers for voluntary inclusion of affordable units.

Mandatory inclusionary housing policies usually provide compensating benefits to developers to mitigate the costs of providing affordable units, similar to the incentives provided under a voluntary program. The most common incentives or compensating benefits include density bonuses, expedited permitting, relaxed development requirements, and financial assistance for participating developers.

Inclusionary housing policies have two social objectives: to increase the local supply of affordable housing and to disperse affordable housing units throughout a community in order to avoid pockets of low-income units. At times, these objectives can conflict with each other. Maximum integration of affordable units into higher-income areas will likely result in the production of fewer affordable units; development costs for affordable units are higher in these areas due to increased land costs and possibly the need for higher-grade materials to fit the neighborhood. Conversely, creating the maximum number of affordable housing units possible would likely require scaling back their integration into higher-income areas, as larger affordable housing developments are better able to take advantage of economies of scale. A sound, workable inclusionary housing policy requires a balance between these two objectives.

In practice, inclusionary housing is a land use policy as much as it is an affordable housing regulatory policy. An inclusionary housing policy cannot work solely by expecting the private sector to produce its most common product—single-family, detached homes, often on large lots—at the lower price that low-income families can afford. Instead, requirements or incentives for the inclusion of affordable housing must be coupled with the flexibility to produce lower-cost housing types in conjunction with more traditional single-family homes. Land use policies can facilitate inclusionary housing development by allowing for more dense development with

smaller lot sizes, developments that combine attached and detached housing types, and the placing of accessory units with single-family homes.

The advantage of inclusionary housing as a policy is its flexibility. It can be applied locally and does not require significant state or federal intervention. Ideally, inclusionary housing policies also destigmatize low-income housing by integrating it fully within the surrounding community.

### **What Makes Inclusionary Housing Work?**

In order to produce a meaningful number of affordable housing units, inclusionary housing requires overall housing growth. Because inclusionary housing policies promote affordable housing in new developments, affordable units are produced only to the extent that overall development proceeds.

Inclusionary housing also requires private developer participation. If incentives for voluntary participation are not sufficient, most developers will not change their practices to include affordable units. Even in communities with mandatory inclusionary housing policies, developers may not participate if requirements are extremely stringent; they may choose to develop housing elsewhere instead.

The following conditions can maximize developer participation in inclusionary housing:

- *Meaningful incentives or compensatory benefits.* Participation in inclusionary housing is maximized when local governments provide strong financial incentives or compensatory benefits for participation. Ideally, the local government and the development community share the additional costs of creating affordable housing.

- *Strong local market.* The ideal community for an inclusionary housing policy is one in which developers compete to build and where new housing is assured to sell quickly. If such a community establishes a mandatory inclusionary zoning policy, developers will be more likely to build despite the mandates because the profit potential will remain significant. Incentive programs also are more effective in communities where market-rate units are high-priced and in high demand than in other communities, because incentives such as increased density and expedited permitting will allow developers to build more of these lucrative units more quickly.
- *Uniformity of regulations across the local housing market.* For mandatory inclusionary housing programs to work, nearby communities must share similar regulations. Otherwise, developers can easily escape requirements by building in a nearby jurisdiction, in effect producing the same product without the added costs associated with inclusionary housing.
- *An effective market for affordable units.* Even if a needs assessment reveals that a number of households in a community lack affordable housing, it is not necessarily true that those households can afford even the lower-cost units produced through an inclusionary housing program. Because it does not involve the deep subsidies typical of earlier federal housing programs, inclusionary housing tends to produce units affordable to the higher end of the low-income scale rather than housing for families in poverty. The local government must ensure that effective demand exists for the units that will be produced, either by identifying families with incomes that would allow them to purchase or rent the new affordable housing units or by providing additional financial assistance to allow lower-income families to afford the units.

## Elements of an Inclusionary Housing Ordinance

An inclusionary housing ordinance must include the following<sup>1</sup>:

- *Conditions under which the ordinance applies.* A local government has a number of options in determining the mandatory or voluntary nature of an inclusionary housing ordinance. First, at one end of the spectrum, it may make inclusionary housing requirements mandatory in new developments in all parts of its jurisdiction. Second, it may require a percentage of affordable units only in areas of the jurisdiction with little such housing, with the ordinance not applicable in other areas. Third, it may require the affordable units in areas with little low-cost housing and offer similar incentives, but not mandates, for the inclusion of affordable housing in developments in other parts of the jurisdiction that already have a supply of affordable units. Fourth, it may make the program entirely voluntary and offer incentives for inclusion of affordable units in developments throughout the jurisdiction. Finally, it may offer a voluntary program with incentives applicable to developments located only in areas with little existing affordable housing.

The ordinance also should specify the minimum size of developments that will be subject to mandates or incentives, expressed as the minimum number of dwelling units in the development. It is reasonable to exclude very small developments from the ordinance. For example, in the most extreme case, an individual building one house should not be required to create an accessory affordable unit to comply with an inclusionary housing ordinance. However, if the inclusionary housing program is mandatory, the minimum development size should be relatively low so that the program does not simply encourage the building of slightly smaller developments. For example, setting the minimum development size at 75 units could result in a spate of 74-unit developments that do not include affordable units.

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<sup>1</sup> A similar list is included in Marc T. Smith, Charles J. Delaney, and Thomas Liou. "Inclusionary Housing Programs: Issues and Outcomes." *Real Estate Law Journal*, Vol. 25, No. 155 (1996), p. 156.

- *Requirements for new developments (mandatory program) or triggers for incentives (voluntary program).* The ordinance must include a clear definition of the “affordable” units whose inclusion in a development will meet ordinance requirements or trigger the availability of incentives. First, the ordinance should specify the household income levels for which units must be affordable. Typically, inclusionary housing programs target families at the very low (50 percent of the area median income) and low (80 percent of the area median) income levels; some programs also include units for families with moderate incomes (120 percent of the area median). Housing would be considered affordable at one of these income levels if it cost no more than 30 percent of the family’s income for rent or mortgage costs.

The ordinance also should specify the minimum percentage of affordable units in each new development. Usually the minimum percentage ranges from 10 to 20 percent of the units.

To reduce the stigma attached to affordable housing units further, some inclusionary housing ordinances also require some measure of comparability between market-rate and affordable units in the same development. An ordinance might require comparable location of each type of units, with affordable units required to be on the same site as market-rate units or even to be scattered throughout the development. The ordinance might require comparable appearance, with affordable units required to contain similar exterior materials and design elements where feasible. Finally, the ordinance might require comparable timing, with affordable units required to be phased in throughout a development to ensure their timely completion.

These requirements for comparability between market-rate and affordable units are not absolutely necessary for a successful inclusionary housing ordinance. Their advantage is that they encourage more complete integration of affordable units into market-rate developments. However, by placing these requirements in the ordinance, the jurisdiction restricts its flexibility to accommodate projects whose developers wish to fulfill the affordability requirements in a different way.

- *Compensatory benefits (mandatory program) or incentives (voluntary program)*. Offering benefits to developers who participate in a mandatory inclusionary housing program or incentives for developers to participate in a voluntary program helps to mitigate the costs of producing housing for below-market purchase price or rent.

The most common inclusionary housing benefit or incentive is a *density bonus*, which allows a developer to create more units on a parcel of land than otherwise allowed. In some cases, the density bonus may be equal to the number of affordable units required. For example, if a developer normally would be allowed to place 90 dwelling units on a parcel, he/she would be allowed to place 100 units on that parcel as long as 10 were affordable units. In effect, this allows the construction of extra affordable units without the purchase of additional land for them. In other cases, the density bonus may exceed the number of affordable units required. Thus, in return for the provision of affordable units, the developer would be allowed to build both the additional affordable units and additional market-rate units without requiring additional land.

Another common inclusionary housing benefit or incentive is the relaxation of development requirements for developments that include affordable housing units. The ordinance might allow for reduced requirements, such as reductions in road paving and rights of way. It also might provide more flexible standards that would result in lower costs, such as allowing odd lot shapes or a mix of housing unit types.

A third benefit or incentive is expedited permitting and reduction or waiver of permit fees for developments including affordable units. If the policy does not require all developments to be inclusionary, either because participation is voluntary or because requirements apply only to certain areas, then the local government can move developments that do include affordable units to the top of the list for permits. Moreover, the jurisdiction can waive or reduce fees such as PUD application and land use change fees in order to reduce the cost of development.

Finally, the local government may offer financial assistance to developments to offset the costs of producing affordable units. For example, in Florida, local governments may use SHIP funds to fund some of the development costs of affordable for-sale units.

While these benefits or incentives are vital to ensuring developer participation in inclusionary housing programs, local governments must be sure that they can afford to make these concessions on a widespread basis, particularly if the inclusionary housing policy will be mandatory. If most new developments are expected to include affordable units, then the increased density, relaxed development requirements, reduced permit fees, and expected financial assistance will constitute a new development regime that will apply to a significant portion of the jurisdiction's future development.

- *Alternative methods of compliance.* In some cases, it may not be feasible to include a percentage of affordable units in the same development as market-rate units. Most mandatory inclusionary housing ordinances offer alternative methods of compliance to address these cases. In practice, these methods of compliance usually call for a greater commitment to producing affordable housing units at the expense of the dispersal of this housing throughout higher-income developments.

One alternative method of compliance is payment of a fee in lieu of including affordable units. The fee would capitalize a housing trust fund that could be used for financial assistance to future inclusionary housing developments or for direct assistance to families needing housing. Because payment of the fee does not fulfill the objective of integrating affordable units into market-rate developments, the fee should not be so low as to give all developers the incentive to pay it rather than to include affordable units in developments. Moreover, since fees in lieu tend to be a popular option, the jurisdiction must have a concrete plan in place to spend the funds collected and must devote adequate staff time to oversee their expenditure. Without this planning and staff commitment in place, some communities with inclusionary housing ordinances have amassed large trust funds without spending them to create affordable housing.

Another alternative method of compliance is the creation of a larger number of affordable units in less dispersed locations. The ordinance may allow developers to bank “credits” for producing extra affordable housing units at some locations or to rehabilitate existing affordable housing units in another area.

Finally, the ordinance may allow developers to donate land for the development of affordable units in areas with an insufficient supply of affordable housing. Unlike other alternative compliance means, this would contribute to the dispersal of affordable housing throughout the jurisdiction.

- *Assurance of continued affordability.* Unless the jurisdiction places explicit restrictions on the future rental or sale of affordable units, it could lose the affordable units as they are sold or rented to new owners and tenants. The ordinance may require units to remain affordable in perpetuity, or it may specify a period of years during which units must remain affordable. The ordinance also may specify that affordable units must continue to be available only to income-qualified buyers and renters.

For rental units, restricting income levels and rents is relatively simple; as in other affordable housing programs, the jurisdiction can specify rent limits and can require certification of new tenants’ incomes as they move into the development. Assuring continued affordability of for-sale units is more complex, since the home sellers are made up of a number of individual lower-income families. The ordinance may allow these families to sell to any buyer and to realize the full appreciation of the cost of their units at the expense of future affordability, or it may require them to sell their units to income-qualified buyers at a price that incorporates inflation and the cost of home improvements but remains restricted to the affordable level. One compromise is to allow home owners to sell to any buyer but require them to place “windfall” profits over the cost of inflation and improvements in an affordable housing trust fund. The jurisdiction loses that particular affordable unit, but it gains some resources to create new affordable housing, and the home seller is relieved of the burden of finding income-qualified buyers. If the ordinance does require home owners to sell to income-

qualified buyers, the jurisdiction may wish to assign staff to create a waiting list of eligible buyers.

- *Compliance monitoring and enforcement.* The ordinance should specify the method by which the jurisdiction will monitor compliance with any mandated inclusionary housing policy. Some inclusionary housing ordinances require a written declaration of home price or rent and income ranges as a condition for granting a construction permit. The ordinance might also require initial or ongoing certification of home buyer and tenant income levels.

While this may not be part of the ordinance itself, it is important that jurisdictions assign adequate staff to monitor compliance with inclusionary housing requirements.

### **Applicability to Alachua County**

Alachua County's strong housing market and continued growth offer opportunities to create affordable housing through inclusionary housing. The major challenge in implementing an inclusionary housing policy will be the creation of a meaningful set of incentives or compensating benefits to bring about developer participation. Density bonuses—the primary means by which communities have encouraged inclusionary housing—may not be very meaningful in an area where development already often does not reach allowable densities. Moreover, while the County may reduce or waive permitting costs, the impact of such reductions may be modest in comparison to development costs. The County also must consider carefully whether it can support the loss of revenue caused by permit fee reductions or waivers.

While strongly opposed to a mandatory inclusionary housing policy, developers have offered some suggestions for incentives that might encourage the voluntary inclusion of affordable units:

- Forgiveness of capital facilities charges;
- Relaxation of zoning standards to allow mixed lot sizes, combinations of multi-family and single-family housing types, and accessory units;

- Simplification of the PUD approval and amendment process;
- Relaxation of street width and drainage requirements.

If the County introduces an inclusionary housing policy, it can take several steps to maximize the policy's chances of success. First, if the County implements a mandatory inclusionary housing policy, it should negotiate with surrounding communities, particularly Gainesville, to create a similar set of regulations for their jurisdictions. Otherwise, mandates will be easily escapable through development elsewhere and annexation.

Second, the County must ensure that a real demand exists for the product that it is encouraging or requiring. The market studies envisioned in the Housing Element of the updated Comprehensive Plan can ensure that there are families in the county with incomes low enough to qualify them for inclusionary housing benefits but adequate to afford the payments or rent for new units produced. If necessary, the County should identify sources of financial assistance to assist lower-income families in meeting the costs of the new units.<sup>2</sup>

Third, the County must display the commitment to flexibility in land use policy that will make mixed-income developments feasible. Developers should not be encouraged or required to create an affordable product on the one hand and forced to fight for the mixed housing types and flexibility in lot sizes that make affordable housing possible on the other.

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<sup>2</sup> Alachua County's SHIP allocation is the natural source of funds for financial assistance to families for home purchases or rentals in inclusionary developments. However, as SHIP assistance programs such as down payment assistance are already utilized fully, their application to inclusionary housing developments will represent a shifting of existing assistance rather than the creation of new affordable housing opportunities. If the County uses fees in lieu of compliance to create a housing trust fund, that fund eventually can serve as source of housing assistance for families. Initially, however, the County may need to identify additional sources of housing assistance funds.

Finally, the County should ensure that adequate staff resources are devoted to the long-term implementation and monitoring required for a successful inclusionary housing policy. The County can maximize the policy's chances for success by devoting significant staff time for negotiating inclusionary housing agreements with developers; certifying incomes, rents, and housing prices associated with new affordable units; planning for the use of the housing trust fund generated by fees in lieu of participation; and administering the trust fund and other financial incentives.

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