COMMERCIAL LINKAGE FEES IN NORTHERN VIRGINIA

A PRIMER

NORTHERN VIRGINIA AFFORDABLE HOUSING ALLIANCE

Dear Colleagues,

As a result of federal sequestration and diminished local revenue caused by the great recession, Northern Virginia jurisdictions increasingly struggle for resources to meet the housing needs for low- and moderate-income households. While jurisdictions have sought to maximize and leverage funding from state, federal and, in some instances, local appropriations dedicated to tackling this issue, affordable housing production continues to lose pace with both job and population growth. As a result, those contributions cannot be expected to meet the entirety of need. Moreover, we know from the past few years of local budget appropriations, that fewer and fewer resources are being allocated each year.

Local jurisdictions can address this growing challenge by considering and implementing a full range of tools available to them to support the production of affordable housing. Currently, a number of these tools, implemented in other areas around the country, are being used locally, but they are underutilized. The Northern Virginia Affordable Housing Alliance will spend the next year examining these tools, and offering a series of reports and special sessions to highlight our findings on strategies and best practices being undertaken to replace the loss of federal and local funding in many jurisdictions.

This first report focuses on commercial developer fees as an important potential source of revenue for local jurisdictions to support targeted affordable housing efforts. A substantive community conversation about commercial developer fees is timely, particularly as two jurisdictions — Alexandria and Fairfax County — consider expansions of their existing voluntary proffer policies.

Commercial Linkage Fees in Northern Virginia: A Primer suggests that both residents and elected officials need a better understanding of the relationship between jobs and housing for the economic sustainability of the region, the challenge of providing housing for our workforce, and the tools such as linkage fees/ proffers that can provide solutions to address housing needs.

With thousands of affordable units lost in our community over the past decade and a need for more than 400,000 affordable units to be developed over the next two decades, our region would be well-served by policies such as these that take advantage of the growth already happening in our communities, and share responsibility for mitigating the impacts of growth across a wider range of partners.

We gratefully acknowledge Angie Rodgers of Peoples Consulting who authored this report and we thank Klein Hornig for their valuable assistance on *Nollan Dolan* laws.

Sincerely,

Michelle Krocker
Executive Director
Northern Virginia Affordable Housing Alliance

Thank you to Citi for their generous support which made this report possible.

Introduction

A number of Northern Virginia jurisdictions have recently considered expansions of their proffer policies voluntary contributions made by commercial and/or residential real estate developers to support the development of affordable housing. These proffers provide a means of absorbing the impact their development would have on the supply of housing in their area in exchange for proposed rezoning. These fees are often an established amount (dollar per square foot) of the new development. Some policies give developers the choice of either paying the fee or providing actual affordable units.

As part of its housing master plan, the City of Alexandria is considering raising its recommended square footage fee, which has not increased since it was established in 2005, and indexing it to change with inflation for successive years. In 2010, when Fairfax County developed its proffer policy for workforce housing in the Tysons Corner redevelopment plan, the County's Board of Supervisors set an intention for future consideration of an expansion of the same or a similar policy for other transit station areas and business centers in the County. Those policy deliberations are taking place this fall. Arlington County, the only Northern Virginia jurisdiction allowed to have a mandatory fee — called a "linkage fee" when mandatory — imposed on development due to a special ordinance passed by the General Assembly, already indexes its fee to inflation.[1]

Linkage fees and proffers are an important element in the range of tools a jurisdiction can use to support its affordable housing efforts. They raise resources to provide a public benefit without imposing additional taxes and fees on individuals, and spread the overall cost of providing that benefit across a broader cast of stakeholders. It is important for businesses and citizens alike to understand the potential benefits of linkage fees and proffers, and also the components necessary to create a policy that will successfully contribute to creating a greater share of affordable housing in their locality. To that end, this primer explores the background, including the legal history of linkage fees, how those fees have been applied both locally and around the country, and the key issues that consideration of a linkage fee might trigger.

Background

The concept of commercial impact fees is fairly simple: it is a fee applied to commercial development and used to provide a service or public good to absorb the impact of that commercial development. Hundreds of jurisdictions across the country have expectations that new developments — hotels, apartment complexes, office buildings, shopping malls, etc. — should contribute resources to cover infrastructure, facilities or other public amenities needed in the jurisdiction in general and/or in the area directly impacted by the proposed development. The developer may be asked to either provide the benefit directly, or to pay fees that will go toward providing the benefit. Typically, the benefit in question may be related to impacts on roads and transportation, schools, adequate utilities, storm-water or waste management.

When impact fees are dedicated to creating or preserving affordable housing in order to mitigate development pressures, they are called "commercial linkage fees." Many jurisdictions have policies that allow developers the option to provide either the housing unit or a fee that could be used to support development of a unit. If the fees are voluntary, they are referred to as proffers.

The developer typically gets some benefit in exchange: usually density bonus or use change, i.e. the right to build more (units, square footage, etc.) than would occur under by-right development. It is the application by the developer for this change in density or use that prompts the fee/proffer.

1 Note that Prince William County's policy is to negotiate affordable housing proffers (either units or monetary contributions) on a project-by-project basis. The County published a Monetary Contributions Report twice a year that details, among other things, the amounts negotiated on different projects for affordable housing. Similarly, Loudoun County negotiates project-by-project.

HISTORY AND LEGAL BACKGROUND

The two most important tenets of commercial impact and linkage fees come from two court cases — *Nollan v. California Coastal Commission*, 483 U.S. 825 (1987) and *Dolan v. City of Tigard*, 512 U.S. 374 (1994), referred to collectively as the *Nollan Dolan* laws. In *Nollan*, a private property owner who was seeking to demolish a bungalow on beachfront property and construct a 3-bedroom home instead, was required by the municipality to dedicate a portion of his beachfront property to public use in exchange for the coastal development permit needed to complete his project. The municipality argued that they had a legitimate public interest in preserving the public's ocean view. The Supreme Court ruled that the municipality's interests were not legitimate, and further that there was not a strong relationship between taking the owner's land to provide permanent public access to the beach and preserving the public's ocean view. The ruling in the case established that in order to condition the taking of private land for public use, the municipality must demonstrate a "nexus" between its legitimate public interest and the purpose of the requirement imposed on the private owner.

In *Dolan*, the need for more pedestrian and bicycle options to ease traffic congestion was used as an argument to compel a development to support the creation of a public greenway and walking/biking paths. In this case, the landowner applied for a permit to expand his store and pave a parking lot. The municipality required the owner to dedicate land to a public greenway and develop a pedestrian and bike path to relieve traffic congestion as a condition of receiving his permits. The Supreme Court ruled that even though the municipality's interests were legitimate, there was no relationship between its interest and the conditions imposed. The ruling further established that any government requirement must be related "in nature and extent" to the impact of the proposed development by the owner. Considering this ruling's application to the cause of linkage fees, a requirement to pay a linkage fee must be targeted to addressing housing service needs created by the new development, and not necessarily other, pre-existing housing or other public needs.

National Practices

Hundreds of linkage programs exist across the country, though they are most prevalent in California, Massachusetts and Washington (state).

BOSTON, MA. Boston has one of the oldest linkage programs, having been established in 1987. The city's fee is mandatory, gaining approval in a non-binding public referendum in 1983, and codified in a city ordinance later the same year. Under threat of legal action on the grounds that the City was not authorized by the state to collect a new tax, the City held contributions in escrow until authorizing legislation was passed by the state legislature allowing the City to adopt a revised ordinance. The city began with an original fee of $5.00 per square foot for housing and $1.00 per square foot for job training, payable over a seven-year period for downtown developments and a twelve-year period for the neighborhoods. The fee is now $7.18 per square foot for housing and $1.44 per square foot for job training. Boston is instructive for several reasons: (1) demonstrating the value created by a broad-based coalition, including both state and local groups that worked for four years to get the program established. This coalition continues today to ensure that program funding keeps pace with growth; and (2) permission from the state was needed for Boston to enact its policy and to approve increases in the future.

SACRAMENTO, CA. Established in 1989, Sacramento's policy is almost as old as Boston's. Like Boston, the Sacramento supporters established a broad coalition of advocates that included realtors, builders, faith and business leaders, political groups, legal services, housing and homelessness advocates along with the city's Housing and Redevelopment Authority. This group formed the City's Housing Finance Task Force and recommended a policy that was approved by the City Council in 1989. It was soon challenged in court by a group of builders who claimed their constitutional rights were violated because the "nexus" between commercial development and the need for affordable housing did not exist. The Court sided with the City, upholding the principle that the connection did exist and that the fee was valid. Sacramento is instructive because: (1) the City used the equivalent of a nexus study to quantify the relationship between commercial development growth, jobs and the increase in need for

housing. This relationship was crucial to their defense once the policy was challenged; and (2) Sacramento pursued a linkage fee as a means to fund a housing trust fund that would support housing development across the city.

Local Practices

ARLINGTON COUNTY, VA. Arlington County is the only Northern Virginia jurisdiction with a mandatory commercial linkage fee that supports affordable housing. Arlington had a voluntary fee until 2003/2004, when rising prices in the housing market prompted the need for additional revenue to preserve affordability in rapidly growing areas (particularly around the County's metro stations) and to continue to develop enough affordable units to meet the needs of low-income households. Arlington attempted to raise their fee to meet their growing needs and was sued. The court ruled in *Kansas-Lincoln, L.C. v. Arlington County Board* with the plaintiff, finding that the County had no legislative authority to require either monetary contributions or units as part of a site plan approval process. Arlington chose not to appeal the ruling, but instead sought a negotiated settlement that was codified through passage of enabling legislation by the state's General Assembly.

The resulting policy, which allows developers to contribute either units or cash, was negotiated through an extensive community process with input from multiple stakeholders, and was codified into law in 2006. The ordinance as written applies exclusively to jurisdictions with a county manager form of government. Arlington is the only Virginia jurisdiction with a county manager form of government, and therefore the only jurisdiction to which the ordinance applies. Contributions go to the county's Affordable Housing Investment Fund (AHIF). The rate for 2013 is $1.77 per square foot of commercial development indexed to the CPI and adjusted annually. The per square foot rate is higher for projects seeking changes that affect the density on a particular site. In FY 2012, commercial contributions comprised about 12 percent of the funds that went into AHIF. The County collected $8.8M between FY 2008 and FY 2012, and they anticipate an additional $13.9M in fees between FY 2013 and FY 2016.

ALEXANDRIA, VA. The City of Alexandria has a voluntary proffer policy for commercial and residential developments, and referenced the decision in the Arlington case to reaffirm to the state legislature its intention to maintain a voluntary program. In a February 15, 2005 letter to the city's state delegation, Mayor William Euille affirmed, "the City will not require developers to make affordable housing contributions, but will only accept them if they are *voluntarily* offered." Like Arlington and other jurisdictions, though, the City arrived at its recommended contribution level — $1.50 per square foot of commercial development — after receiving extensive input from developers and other stakeholders. The rate has not changed however since 2005, and the City's recently proposed Housing Master Plan (released in 2012) assumes an increase to $1.82 per square foot to account for inflation, and adjusted annually in accordance with the CPI. The City collected $16.9M between FY 2006 and FY 2011, and it is anticipated that City Council will complete their deliberation of the Housing Master Plan by Fall/Winter 2013.

FAIRFAX COUNTY, VA. Fairfax County adopted a voluntary proffer policy in 2010 in response to the advent of the Silver line through Tysons and the planned redevelopment there. One of the guiding principles for the redevelopment of Tysons was to promote a more equitable jobs to housing ratio than exists currently (100,000 jobs to 17,000 residences), and to ensure that a portion of that housing serves the workforce. Given the scale of new development and the increase in the amount of residential density, the County adopted this new tool to support affordable housing development in the area. The policy calls for a $3 per square foot contribution for commercial development at Tysons, which may be made as a one-time contribution or at the rate of $0.25 per year over 16 years. For this reason, it may take a while for contributions to materialize, but the county is projecting $30.5M in collections based on developments approved as of June 2013.

As part of its 2010 adoption of the Tysons redevelopment plan, the Fairfax County Board of Supervisors instructed County staff to draft similar policy language for other designated transit areas

or business centers in the County. A subcommittee comprised of members of the County's Planning Commission, Redevelopment and Housing Authority and Affordable Housing Advisory Committee has considered and proposed a draft policy that is scheduled to be taken up by the Board by early 2014. The subcommittee has proposed a tiered approach, where a $3 per square foot contribution would apply to commercial developments in "Transit-Oriented Development (TOD)" areas that are within a quarter mile of a transit station area; $2 per square foot would apply in areas between a quarter and half mile of any transit station area, and $1 per square foot would apply outside of the half mile and in all other designated areas of the County. The tiered system is meant to take advantage of planned high intensity activity around the County's transit nodes — areas in Herndon, Reston, Franconia-Springfield and Huntington as well as Tysons — while placing fewer requirements in areas of the County where development activity has been less robust (Annandale or Baileys Crossroads). The County has not projected anticipated contributions county-wide in this proposal phase, but has projected developer fee revenue based on anticipated development within ¾ of a mile around the Reston transit station area. Under the tiered proposal, this area alone could generate some $33.7M based on known planned growth.

Key Issues

MANDATORY VS. VOLUNTARY

The terms "commercial impact" and "commercial linkage" refer to mandatory fees. In Virginia, commercial impact fees are codified in state law allowing jurisdictions with populations in excess of 90,000 to require fees of all development projects. Eligible uses for the fees include road construction and public infrastructure.[2]

There is only one commercial linkage fee (i.e. mandatory impact fee for housing) in Virginia. Arlington County, whose ordinance is detailed in the previous section, is the only jurisdiction with a commercial linkage fee. All other Virginia jurisdictions collecting fees to support affordable housing are collecting voluntary contributions, or "proffers" from developers.

As stated, voluntary contributions are always negotiated. However, some jurisdictions establish a per square foot rate to provide a baseline expectation of the fee, and some predictability of costs for developers. This also gives jurisdictions an estimate of revenue to be provided for their affordable housing programs. Remember that these fees are requested when developers seek zoning changes to support either additional density, or a change in allowable use beyond what they can do by-right on their parcel of land. Project by project negotiation of fees and other benefits can often result in variations. Setting an expected rate allows negotiations to at least begin at the same place for each project. Moreover, experience shows that the collaborative process of establishing a per square foot rate that includes a broad range of stakeholders results in a higher level of acceptance by developers, who absorb the resulting fee as a cost of doing business.

As an example, the City of Alexandria first set its rate some eight years ago and has only had one instance of non-compliance in that time. Fairfax County set the Tysons Corner rate three years ago and, in the period of rapid development since, has had no issues with the policy. Further, although Arlington's first attempt to mandate a fee resulted in a lawsuit, the negotiated settlement that ensued and led to their mandatory fee included input from the County's development community. Whether jurisdictions have voluntary fees or mandatory fees, most follow the same process of community engagement and negotiation to set their per square foot rate.

IS IT A "TAKING"?

Voluntary fees cannot, by definition, constitute a taking — in this case an exaction of money or other benefits mandated by a jurisdiction that violates the developers constitutional right to ownership, value and use of his/her own property. Even when the rate is pre-set, voluntary fees are part of a negotiated process with the developer.

2 Cited in VA 15.2-2317 and VA 15.2-2328 respectively.

When a jurisdiction imposes a mandatory impact or linkage fee without meeting the two tests established by *Nollan Dolan*, their actions can be considered a taking. (1) *Nollan* established that a jurisdiction must demonstrate a strong relationship, or "nexus" between their (public) interest and the requirement that an owner use his/her private property to advance their interest without being compensated to do so. (2) *Dolan* further established that any requirement that an owner use his/her property to advance a jurisdiction's public interest must be related "in nature and extent" to the impact of the development proposed by the owner.

A range of other cases, both favorable and unfavorable, have affirmed that the *Nollan Dolan* rulings, indeed, extend to linkage fees.[3] Together these rulings state that in order to impose a linkage fee, jurisdictions must successfully demonstrate that an owner's proposed development will negatively impact the availability of affordable housing, and as a result the owner can be compelled to provide resources to close the gap in availability created by the proposed development. The owner can only be required to provide enough resources to fill the gap, however, and no more. An owner cannot be compelled to provide resources to address a general lack of affordable housing in the jurisdiction although notably, proffers often do this very thing. Violation of the tests established by the *Nollan Dolan* rulings constitute a "taking," which can be challenged by the developer. Although *Nollan* was unclear on the issue, *Dolan* clarified that burden of proof lies with the government to demonstrate both nexus and impact in the instance of a challenge.

FOR VA JURISDICTIONS — DILLON RULE IMPLICATIONS

Virginia is a "Dillon Rule" state which means that local governments derive their power from the state, and localities cannot exercise powers not expressly granted to them by the state, implied by powers expressly granted, or indispensible to the locality. In this case, Virginia law does not provide for the collection of linkage fees (mandatory fees for housing). As a result, jurisdictions are only allowed to negotiate proffers with developers in order to support affordable housing efforts. The lone exception is Arlington County.

HOW LINKAGE FEES ARE CALCULATED

Because *Nollan Dolan* requires a rather narrow tailoring of proposed development activity to impact, linkage fees are calculated by (1) calculating the housing demand to be stimulated by a development, and (2) multiplying that demand by the amount of money it will take to make those units affordable. Fees are most often calculated on a dollar per square foot basis, and rates are around $1 per square foot. Rates in Northern Virginia range from $1.82 per square foot in the city of Alexandria (voluntary) to as much as $9.00 for some development types in Arlington County (mandatory).

Often this calculation is further adjusted to accommodate the economic or political realities of the jurisdiction. Localities are careful to avoid setting a fee so high that it stifles commercial development or invites a challenge. Organizations like the Urban Institute, Brookings Institute and Policy Link provide technical assistance to communities to build their formulas. Jurisdictions with successful policies have also built strong community coalitions to vet and support the fee.

FOCUS ON HOUSING VS. OTHER PUBLIC BENEFITS

As discussed, while impact fees focus on other public benefits (transportation, utility and infrastructure needs, public facilities, etc.), linkage fees focus explicitly on affordable housing. Impact fees have been in existence since the 1940s, and are used more widely than linkage fees. According to a national survey, 26 states authorize impact fees in their local jurisdictions, and 60 percent of large cities along with 40 percent of metropolitan counties use the fees. Linkage fees are less common, and are more likely to appear as

3 In *Commercial Builders of N. Cal. V. Sacramento*, the Ninth Circuit upheld a fee linking a new commercial development anticipated to generate jobs with a requirement to provide a relevant amount of workforce housing. In *San Remo Hotel L.P. v. City & County of San Francisco,* the California Supreme Court struck down a fee using *Nollan Dolan* and citing the defendant's inability to demonstrate a relationship between the fee and the development's impact.

voluntary “proffers.” Since (mandatory) linkage fees are prohibited in Virginia (except in Arlington), local policies always reference (voluntary) proffers.

HALLMARKS OF TYPICAL CHALLENGES TO LINKAGE FEES

Linkage fees and proffers have faced three kinds of challenges:

POLITICAL – These challenges typically come first and perhaps at a jurisdiction’s first mention that it intends to consider an impact fee or proffer policy. Arguments here often focus on (1) the probability that more fees will deter development when added to an already expensive development process; (2) the potential illegality of such fees; and (3) the unfairness of potential fees that may target some developers, types of developments, geographical areas, etc. and not others.

NONCOMPLIANCE – This issue arises later, once a policy is in place. For voluntary policies, noncompliance can be an ever-present concern, although smart practices where a jurisdiction develops its policy through a community process can mitigate this. A more likely scenario is that jurisdictions will fall behind their revenue projections for affordable housing programs because development projects take longer to complete than anticipated, rather than projects not complying at all.

LEGAL – Noncompliance with mandatory policies can lead to a legal challenge, which most often centers on the issue of whether the policy violates one or more of the *Nollan Dolan* tests and, in states like Virginia, whether the local government has the power to tax.

HALLMARKS OF SUCCESSFUL POLICIES

With hundreds of linkage fees in place around the country, a body of best practices has begun to emerge detailing how to successfully implement such policies. Jurisdictions should:

1. Illustrate in a detailed study the effect that the existing supply of affordable housing has on the jurisdiction and its employers and the need for additional affordable housing units.
2. Due to established case law, jurisdictions considering mandatory policies must demonstrate the relationship between the development impact and the resulting fee in a nexus study, and also be able to quantify the amount of housing demand by income level that would be generated by the development.
3. Provide consistent and meaningful returns to developers (density bonuses, expedited permitting, etc.).
4. Build community consensus for the policy through an advisory body of residents, government staff, and private sector employers.

Conclusion

Several Northern Virginia jurisdictions are considering changes to their proffer policies, and others continue to grapple with how to provide adequate resources to ensure all residents have decent, safe affordable housing. To that end, some examination of what communities should be considering about new funding sources for affordable housing is timely.

- **What does a successful linkage fee or proffer policy look like? What should it aim to achieve?**
  Proffers are a good tool as part of a jurisdiction’s overall plan to fund affordable housing or secure units. What can jurisdictions aim for and anticipate, though, in terms of volume and impact? How strong a role can proffers play in meeting the community’s housing needs?
- **What effect does the voluntary status of a jurisdiction’s policy have on their ability to do long term planning, and on their ability to keep pace with commercial growth?**
  For both voluntary and mandatory policies it can be difficult to determine when funds will come in or when units will come online. Market forces are a significant factor and each development has its own timelines, making consistency an elusive concept. Monetary contributions can also trickle in over a long period of time, depending on how many options are provided to developers. For

the redevelopment of Tysons in Fairfax County, developers can pay the $3.00/square foot flat rate, or they can spread it out over 16 years, paying 25 cents per square foot per year over that time. Officials in the City of Alexandria have also found over the eight years of their program that contributions can take twice as long to come in as predicted.

- **How are employers and residents alike affected by the existing supply of affordable housing?**
  Recent analyses from George Mason University's Center for Regional Analysis indicate that the region will need over 700K net new housing units over the next 20 years, and more than half of those will need to be affordable to low- and moderate-income households. The numbers are no less stark looking jurisdiction by jurisdiction, particularly when also considering the number of affordable units that have been lost to the market over the past decade. Policymakers are starting to embrace the concept of using a broad range of housing creation/preservation tools (include zoning changes and impact fees/proffers) because absorbing the impact of the region's anticipated growth will require multiple strategies.
- **How can an effective coalition (with residents, advocates, employers and government staff) be built to craft and support successful policies (like adequate linkage fees/proffers) that support the preservation and creation of affordable housing?**
  A common best practice from jurisdictions around the country that have successfully implemented these types of fees has been the ability to build a broad-based coalition that supports proposition of a policy, but also continues to support their locality through long-term implementation.

SELECT RESOURCES

INTERNET RESOURCES

- PolicyLink, *Equitable Development Toolkit*
- ImpactFees.com

PRESENTATIONS

- Melissa Bondi, *Commercial Impact and Linkage Fees*, January 2013 to the NVAHA
- Eric Keeler/City of Alexandria Office of Housing, *Alexandria's Voluntary Contribution*, January 2013 to the NVAHA
- David Cristeal/Arlington County Housing Division, *Commercial Contributions & Affordable Housing – Arlington's Experience*, January 2013 to the NVAHA
- Fairfax County AHAC Special Subcommittee, *Countywide Policy for Affordable Housing Contributions by Non-Residential Developers – Concept for Consideration*, September 2013 to the Fairfax County RHA, Planning/Zoning and AHAC

REPORTS AND PAPERS

- David L. Callies/University of Hawaii School of Law, *Mandatory Set-Asides as Land Development Conditions for Affordable/Workforce Housing*, 2010
- Andrew Knudtsen/Economic & Planning Systems, *The Economics of Commercial Linkage and Inclusionary Zoning: Community Case Studies and Impacts to Project Viability*, 2006

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