THE IMPACT OF FEES:

Rethinking Local Revenues for More Multifamily Housing

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Executive Summary

Across California, local jurisdictions require home builders to pay development impact fees as a condition of approving new housing construction. The use of these fees, which vary in purpose and size, expanded widely in response to the loss of property tax revenues that followed the passage of Proposition 13 in 1978. Today, nearly all California localities charge some form of impact fee.

Impact fees, however, are not only used to generate revenue but can be a tool to stymie growth. This is an area of public policy that is overdue for reform. The United States Supreme Court ruled in April 2024 that California courts were reviewing development impact fee schedules too leniently to meet constitutional standards. The time is ripe for change to support multifamily housing growth.

In some instances, local governments use impact fees to assign costs of infrastructure maintenance to future residents, while allowing the increased property values of functioning infrastructure to accrue to current residents. In other cases, jurisdictions charge higher impact fees for multifamily homes than they do for single-unit homes on a per-square-foot basis, even though multifamily homes reduce infrastructure impact. In the worst cases, cities adjust impact fees upward until new housing construction is no longer feasible at all.

What are the various political and fiscal incentives that underpin development impact fees in California? How might impact fees be reformed to make them fairer and more predictable? Are impact fees the best tool for the job of generating necessary government revenues? And what might alternative revenue sources to impact fees look like?

Our key findings include:

1. **Property tax revenue declined by 53 percent immediately after Proposition 13 passed, falling from 58 percent of local revenue in 1972 to just 36 percent by 2012.**
2. **Impact fees only account for 2.6% of the average California cities' reported revenue.** However, reliance on revenue from impact fees varies greatly across jurisdictions, from as high as 16% to less than 0.5%.
3. **The average impact fee on a multifamily unit in California is $21,703, nearly triple the national average of $8,034.** Similarly, California's average single-family unit fee of $37,471 is triple the national average of $13,627.
4. **Developers transfer impact fee costs to homeowners and renters, increasing multifamily unit costs up to $60,000 and single-family unit costs up to $100,000.**
5. **Most jurisdictions charge higher fees per square foot on multifamily units compared to single-family homes, which disincentivizes multifamily housing construction.** In some cases, higher fees for multifamily homes result from overt efforts to block the construction of new apartment buildings.
6. **Many cities that had the lowest increases in impact fees had the greatest increases in multifamily housing.** Conversely, cities with the greatest increases in multifamily impact fees experienced the lowest growth in multifamily housing.

Remedies: Shift Revenue to Broad-Based Bonds and Fee Fairness

We review current policies, like AB 602, meant to reform impact fees through increased disclosures and guidance on how to properly calculate fees. Most jurisdictions are not complying with AB 602 mandates to disclose fee schedules, fiscal impact studies meant to justify those fee schedules, or actual fees charged to new development. In addition, we evaluate a sample of nexus studies - fiscal impact reports meant to justify impact fees. Most of these studies do not comply with AB 602 mandates and contain fees that likely overcharge new residents for their impacts on public capital. Overall, it appears current policies contain inadequate enforcement mechanisms to ensure compliance.

Following this review of current policy, we assess three policy options aimed at removing barriers to multifamily housing by reducing local governments' reliance on impact fees:

1. **eliminating impact fees altogether;**
2. **reducing barriers to challenging unjustified fees in court; and**
3. **capping impact fees.**

Policies such as ACA 1 - which would expand jurisdictions' capacity to raise revenue and spread the fiscal responsibility of paying for publicly-provided goods across the entire community - would go a long way toward solving local fiscal challenges while simultaneously minimizing per capita costs. Californians are set to vote on ACA 1 in November 2024.

Capping fees on a per-square-foot basis would also help streamline the administrative process, provide flexibility in the fee assessment timing, and incentivize smaller, more affordable units.

Given these findings, we recommend the following:

1. **Stronger enforcement of provisions in state law that require fees to be calculated on a per-square-foot basis, regardless of housing typology.**
2. **Stronger enforcement of provisions in state law that require consistency and transparency in how fees are determined, as well as streamlined sequencing.**
3. **Increasing private enforcement to discourage unjustified fees by providing an award of attorney's fees and costs, as well as punitive damages, to successful plaintiff home builders.**
4. **A cap on impact fees, on a per-square-foot basis, alongside efforts to replace lost municipal revenue streams, such as ACA 1.**

Building a home by Thayran Melo, used under the Unsplash License.

1. Introduction

This report considers how California can promote multifamily housing development by aligning local government funding streams to reduce their reliance on development impact fee revenue. On April 12, 2024, the United States Supreme Court heightened the standard under which California local governments can justify fees set by legislated schedules. This ruling has the effect of making it more difficult for local governments to raise revenues with impact fees and requires the legislature or courts to implement the Supreme Court decision by setting new rules. It provides an opportunity for the state to evaluate new policies around impact fees that better address California's continued and growing housing crisis.

Decades of inadequate housing development is widely recognized as the driving force behind California's housing crisis. Slow-growth and not-in-my-backyard (NIMBY) advocates steered state and local policies toward expensive, single-family homes and away from denser, multifamily development. While various policies hinder multifamily development, the passage of 1978's Proposition 13 – which drastically restricts local property tax revenue – motivated new local fiscal barriers to development. Before 1978, local governments funded infrastructure and public services needed to support new development primarily through property tax revenue. After Proposition 13, localities searched for alternative ways to generate revenue.

Many jurisdictions did so by increasing development impact fees intended to charge new development for their increased strain on public services and infrastructure. Today, nearly all California local jurisdictions impose impact fees, and they charge triple the national average.

While ostensibly charged to developers, fees are ultimately passed to new homeowners and renters in the form of higher home prices and rents. If the fees are too high, projects are rendered financially infeasible. Theory, empirical data, and anecdotal evidence suggest that NIMBY localities may impose excessive impact fees to obstruct development and exclude new residents from their community.

In this report, we draw on prior literature, interviews with eight stakeholders, and independent statistical analysis to investigate impact fees. First, we consider how California's housing crisis is uniquely situated within a fiscal structure where nearly all localities charge development impact fees. Although California's local governments charge fees that are well above the national average, we find that impact fees are, on average, a small portion of cities' total revenue or capital operating expenses. However, city staff we interviewed believe impact fees are an important funding source, particularly when voters have earmarked the bulk of other revenue sources for particular uses.

Second, we analyze the extent to which impact fees increase housing costs and slow housing production. Theoretically, impact fees may be an efficient way for cities to fund public services, as they force new residents to internalize their marginal impacts on public infrastructure. Consequently, impact fees may remove political opposition to new development from incumbent homeowners leading to development that might not otherwise occur. However, impact fees can also slow development by raising housing costs that disproportionately exclude poor households and people of color. Qualitative evidence also suggests that using fees for exclusionary purposes is common. The historical record shows that multifamily housing has long been vilified.

The Supreme Court in 1926 described apartments as “mere parasites” on the community. Contemporary affordable housing opponents parrot these views when they argue apartments will blight neighborhoods and destroy property values. City staff we interviewed noted that, while they do not agree with the views of NIMBY groups, NIMBY voices matter. Developers we interviewed cited multiple specific instances where NIMBY groups stymied affordable multifamily housing development. We also look at contemporary data supporting a bias against multifamily housing development. Impact fees are higher for multifamily than single-family development on a per-square-foot basis. Many statistical analyses also suggest impact fees increase the price of both existing and new multifamily development, and can reduce development. We conclude that impact fees raise housing costs and inequality.

Third, we survey recent policies meant to ensure the fair use of impact fees. We review federal and state law, with a particular focus on the impact of the recent United States Supreme Court decision in Sheetz v. County of El Dorado. That decision has heightened the legal standard for local agencies to justify fees set by schedules. Developers and homeowners will now be more likely to succeed in challenging fees. However, the United States Supreme Court provided little guidance on how its new ruling should be implemented in California – leading to uncertainty for both local jurisdictions and private developers.

We also evaluate the success of AB 602 (Grayson 2021), which reinforced fee disclosure requirements and sought to increase the quality of the fiscal analyses local governments use to justify impact fees – known as nexus studies. We review literature critiquing nexus studies, and the ways these studies may embed biases against multifamily housing development. Based on our survey of 60 cities, we find that the vast majority are not fully complying with AB 602’s fee and nexus study disclosure requirements. We conclude, based on reviewing a sample of recent nexus studies, that AB 602 has also not improved the quality of nexus studies.

Fourth, based on these findings, we consider three policy options aimed at promoting multifamily housing development by reducing the barriers posed by impact fees. We consider eliminating impact fees. We find this option to be politically infeasible as it would require residents to pay significantly higher taxes to finance infrastructure and services. We also consider expanding legal mechanisms to incentivize developers and homeowners to challenge unjustified impact fees. However, this option may not adequately ensure fees do not stymie multifamily development or provide local jurisdictions with replacement revenue. Finally, we consider capping impact fees based on the per-square-foot of development and replacing this revenue with alternative funding streams, such as that proposed by ACA 1. Ultimately, we recommend the final option as it directly limits impact fees’ negative effect on housing development, while providing jurisdictions with alternative funding.

A full description of our interview methodology can be found in **Appendix A**. A description of the datasets used to perform our statistical analysis is in **Appendix B**.

2. Background on California's Housing Crisis and the Rise of Impact Fees

California is in a housing deficit and must build millions of units to meet demand. California's unique fiscal system contributes to this deficit because localities cannot rely on property taxes to fund public capital projects. Instead, jurisdictions turn to other revenue sources, such as development impact fees, which nearly all California jurisdictions charge at rates well above the national average. Although these fees significantly burden development, they make up a small portion of total local revenue. Nonetheless, for jurisdictions where other revenue sources are earmarked for particular uses, impact fees are important.

2.1 California's Housing Crisis and Underdevelopment of Multifamily Housing

California faces a formidable housing crisis, continually failing to meet housing production mandates. As Figure 1 shows, housing development has not kept up with population growth. In 2020, the state had 40 million residents, yet only 14.35 million housing units (Henderson 2021). It is estimated that if housing production in California had kept pace with demand, current home prices would be 21 percent lower (Baron et al. 2022). The housing shortage and unaffordability have also exacerbated homelessness. Over 30 percent of the country's homeless population now resides in California (Paluch and Herrera 2023). Over 3.2 million Californians are currently rent-burdened, defined as spending at least 30 percent of their income on rent and utilities each month (McDonald 2023). Unaffordability increases inequality, particularly among younger generations: "Lack of supply and rising costs are compounding growing inequality and limiting advancement opportunities for younger Californians" (Department of Housing and Community Development 2018). As Figure 2 shows, housing production peaked in 1970 at 228,000 units per year but has plummeted since. Addressing potential barriers to housing development, such as impact fees, is essential to solving California's statewide housing shortage. It is estimated that the state must construct 3.5 million housing units to effectively resolve this issue (Woetzel 2016).

Figure 1

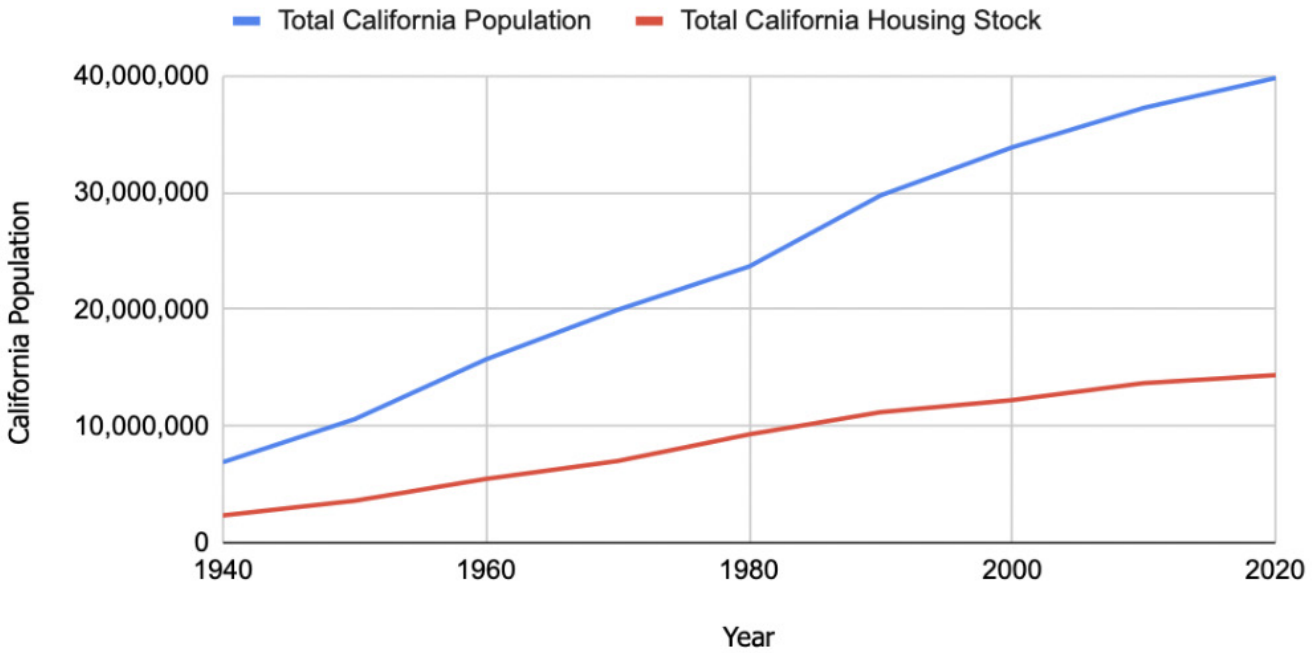
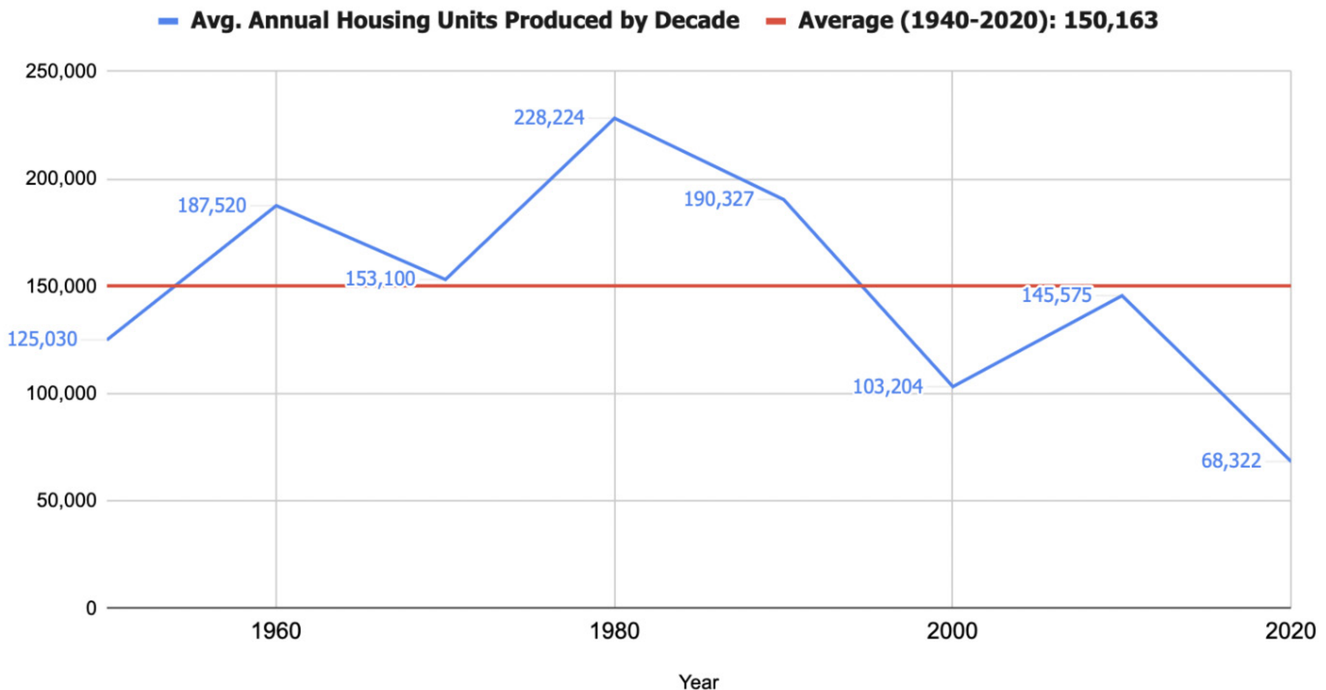


Figure 2



2.2 Local Revenue Sources are Limited

California's unique fiscal system contributes to its acute housing crisis. In 1978, the passage of Proposition 13 significantly reduced local property tax revenue. Specifically, it pegged the tax rate at one percent, capped increases in the tax base to two percent per year, and only allowed reevaluation of the tax base at the time of sale (Coleman 2022). Local governments also lost control of property tax revenue. The state now collects and redistributes property taxes, sharing it among schools and special districts. Additionally, if localities want to raise their own property taxes, Proposition 13 raised the voter approval threshold to 66.67 percent.

Consequently, property tax revenue declined by 53 percent immediately after Proposition 13 was passed (California Budget Project 1997). Property tax dropped from 58 percent of local revenue in 1972 to just 36 percent by 2012 (Raetz et al. 2019). As of 2015, schools received 38 percent of the state's total property taxes, counties received 24 percent, and cities received only 18 percent (Chu 2015).

While all cities experienced dramatic reductions in property tax revenues, the amount varies greatly. In 2016 in Los Angeles County, for example, Carson received 10 percent of property taxes collected within its borders while Long Beach received 26 percent (Chu 2016). Further, some cities receive little to no property tax revenue. This occurs because the state distributes property taxes to cities based in part on the amount the city collected and public services it provided before the passage of Proposition 13 (Chu 2016).

Not only have property tax revenues shrunk – so have other local revenue sources. In 2011, the California legislature dissolved redevelopment agencies (Chu 2015). These agencies previously allowed cities to redirect property tax revenue increases directly to infrastructure improvement that might increase real estate values in blighted areas. A principal planner of a California city noted in an interview that their city lost substantial affordable housing opportunities when the state eliminated redevelopment funding.

State and federal intergovernmental transfers have likewise declined. For example, although the federal government has recently approved increases in transfers to improve transportation and water infrastructure, federal funding is still well below its peak 60 years ago and insufficiently addresses the infrastructure debt incurred during that time (Banta and Yousofi 2023).

2.3 Local Governments Increasingly Rely on Impact Fees to Raise Funds

Proposition 13's property tax restrictions, as well as declines in other revenue sources, forced local governments to seek new funding sources (Altshuler & Gómez-Ibáñez 1993, 33). Although they initially hoped to balance budgets with state funds, local governments' strategy shifted during the economic recession of the early 1980s (Landis et al. 2021). Localities now raise revenue from regulations and land use development policies, engaging in a form of "competitive fiscal federalism" where jurisdictions compete to draw the wealthiest residents and most lucrative land uses to raise revenue (Paulsen 2014, 26; Altshuler & Gómez-Ibáñez 1993, 18-33). This is often referred to as the "fiscalization of land use" or "regulation for revenue" (Paulsen 2014, 26; Altshuler & Gómez-Ibáñez 1993). This approach has had two major impacts on development policy.

First, local governments changed zoning and permitting processes to discourage perceived high-cost, low-revenue land uses and encourage low-cost, high-revenue uses (Landis et al. 2021). Residential land use is viewed as high-cost because residents consume public services, like schools. For example, one city public works engineer told us, "We do promote land uses that are higher tax generators. We had undeveloped land that was originally planned for 1,100 homes, but we recognized that would be a burden, so we updated the general plan and changed the zoning to limited industrial."

As this civil public works engineer suggests, retail and industrial uses, like shopping centers and auto malls, are considered revenue generators as they can bring in sales tax income (Landis et al. 2021). The same public works engineer told us, "We don't give tax incentives, but we will speed up the process and be more developer-friendly when we can collect revenue from sales taxes." Between 1978 and 2015, inflation-adjusted sales, hotel, and utility tax revenue increased more than seven-fold, while property tax revenue only doubled (Taylor 2016).

Second, municipalities raised fees, including on new development. Municipalities charge developers numerous types of fees, such as processing fees for administrative services, specific fees negotiated in contracts, and charges for new development's impacts on local public goods and services. This report focuses on development impact fees, which nominally charge developers for the increased capital costs caused by new development (Raetz et al. 2019). For example, a local government might charge a development impact fee for increased policing services due to an influx of new residents. These fees should be calculated to cover the cost of additional capital improvements necessary to maintain the existing level of policing, such as building new facilities or purchasing police cars. Under California law, development impact fees cannot be used to cover non-capital costs, such as the salaries of new police officers.

A landmark 2001 survey of 89 local California jurisdictions found that the vast majority charged impact fees – 99 percent imposed development impact fees for school construction, 87 percent for parks, 80 percent for local traffic mitigation, 60 percent for storm drainage, and 55 percent for fire service (Landis et al. 2001). These statistics contrast with national averages. Only 60 percent of U.S. cities with more than 25,000 residents imposed any kind of impact fee (GAO 2000).

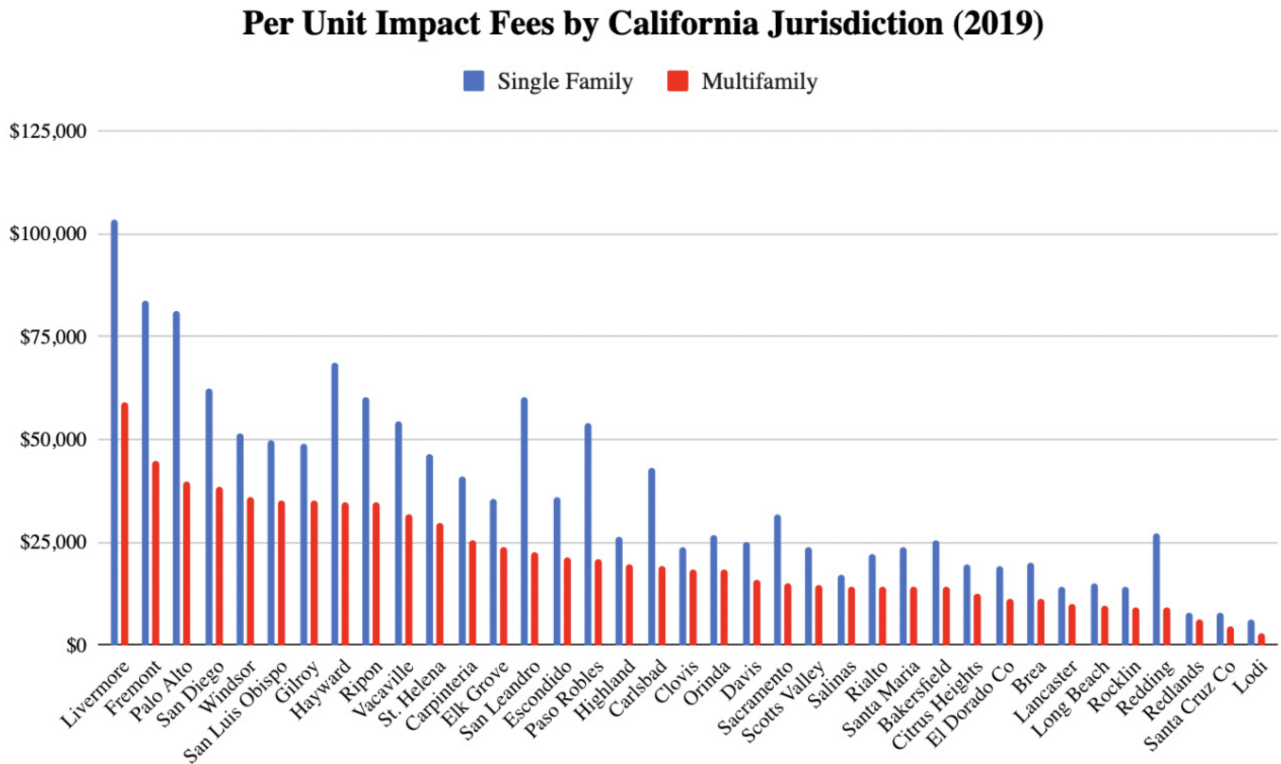
2.4 California's Impact Fees are Significantly Higher than the National Average

Not only do more local California governments charge impact fees than the national average - California local governments also charge the highest impact fees in the nation, according to a 2019 national impact fee survey of 270 jurisdictions (Mullen 2019a). The average impact fee on a multifamily unit in California is $21,703, nearly triple the national average of $8,034. Similarly, California's average single-family unit fee of $37,471 is triple the national average of $13,627 (Mullen 2019a).

All California localities charge fees, but they vary widely. Raetz and colleagues (2019) authored an overview of California impact fees for the Terner Center for Housing Innovation at UC Berkeley ("The Terner Center") (Raetz et al. 2019). They surveyed impact fees charged in ten California cities and found a large range in total fees. At the low end, Imperial charged $4,878 in total impact fees per multifamily unit. At the high end, Oakland charged almost five times more, or $24,000. Impact fees also vary by category. While Irvine charges no impact fees for parks,

Riverside charges around $500 per multifamily unit, and Fremont charges around $18,000. We reach similar results, finding that development impact fees vary widely among the 37 surveyed jurisdictions (Appendix B). Fees range from a total of $5,000 to over $100,000 per single-family home and from under $3,000 to $60,000 per multifamily unit *(Figure 3)*.

Figure 3



2.5 Impacts Fees are a Small, but Often Significant Portion of Revenue for Local Governments

Although California local jurisdictions charge the highest impact fees in the nation, there is little data quantifying the extent to which localities rely on impact fees as a source of revenue. The Terner Center evaluated five local governments' 2016 impact fee revenues as a proportion of their capital improvement budgets (Raetz et al. 2019). They found significant differences among jurisdictions: at the low end, Los Angeles' fees were three percent of the city's estimated capital improvement budget. On the high end, Fremont collected fees amounting to 66 percent of its capital improvement budget. The report concluded that larger cities rely less on impact fees and more on other revenue sources, like bonds, than suburbs do to fund infrastructure.

Following the Terner Center analysis, we compare reported development impact fees to all revenue sources for cities across California using State Controller data (Appendix B). We find that reported impact fees are not a significant income source for most cities. On average, impact fees amount to just 2.6 percent of total revenue for reporting jurisdictions in fiscal year 2022.

The average percent of total revenue coming from development fees has remained relatively constant each year since 2017. However, there is significant variance between different cities' development fees as a percentage of total revenue in the year 2022. Development fees range from one to 16 percent of cities' total revenue.

Further, development fee revenue is less than the revenue generated from other major sources. On average, reported property tax income contributes 9.6 percent to total revenue, and reported sales tax contributes 13.2 percent. As with development impact fees, there is significant variation by jurisdiction. Property taxes range from 0.01 to 54 percent of revenue. Sales tax revenues range from 0.16 to 75.8 percent of total revenues.

Figure 4

Top 10 Cities by Percentage of Revenue from Impact Fees	
City	**Percent**
Rancho Cordova	16.20%
Elk Grove	14.20%
Mountain View	13.20%
Marina	13.00%
South San Francisco	12.90%
Fowler	12.80%
Sunnyvale	12.30%
Gilroy	11.70%
Fillmore	11.20%
Waterford	11.20%

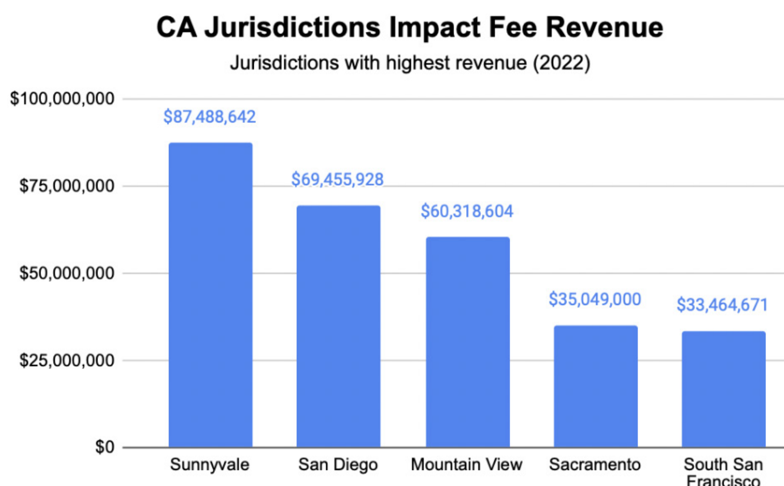
Bottom 10 Cities by Percentage of Revenue from Impact Fees	
City	**Percent**
Grover Beach	1.95%
San Jose	1.86%
Fresno	1.64%
Azusa	1.49%
Lancaster	1.40%
Hermosa Beach	1.39%
Santa Cruz	1.06%
Richmond	0.50%
Redwood City	0.38%
Buellton	0.07%

Although the Terner Center reported that larger cities rely less on impact fees than other jurisdictions, we do not find a similar pattern. We examined the top and bottom 10 cities ranked by percentage of revenue from impact fees (Figure 4). We compared median income, average rents, racial demographics, location, and rural/suburban/urban status, and did not find patterns to explain why certain jurisdictions rely on impact fee revenue more than others.

Our quantitative findings are consistent with our interviewee's experiences. A city manager noted that his city did not rely on impact fees as a continuous and significant funding source. Rather, the city saved the revenue generated from impact fees, and when enough was saved, the revenue was used to expand public facilities. Nonetheless, even this relatively small revenue source is critical for some cities, as voters have earmarked most other funds. One city planner stated that in his city, a large percentage of formerly discretionary revenue is now limited to expenditure on schools and policing. Similarly, a public works engineer told us that "a good portion of new facilities come from development impact fees" while very little is built with money from their general fund.

Although revenue from impact fees may constitute only a small share of most cities' total revenue, some cities' fee revenue in terms of actual dollars is high (Figure 5). The total reported development impact fees for California in fiscal year 2022 was $930,950,646. Sunnyvale alone took in nearly $90 million, or roughly 10 percent, of that sum. That is more impact fee revenue than is generated by the city of San Diego, whose population is over 1.3 million. Likewise, Mountain View, with a population of around 80,000, brought in impact fee revenue just below that of San Diego. On a per capita basis, Mountain View charged $722 and Sunnyvale charged $560 in impact fees, whereas San Diego and Sacramento, charged $51 and $68 respectively.

Figure 5



These suburbs with the highest impact fee revenues have home values over double the state average of $765,000. Sunnyvale's average home value is over $2 million and Mountain View's is over $1.9 million. Likewise, both cities' average rent of around $3,150 is well above California's statewide average of $2,775 (Zillow 2024). Higher home values may support higher impact fees, but they also may reflect these communities' resistance to new affordable housing development.

Figure 6 shows the jurisdictions with the lowest reported impact fee revenue in 2022. As opposed to the top cities, which draw tens of millions in revenue, these cities report revenue in the thousands of dollars. These cities have small populations and low home values compared to the jurisdictions with the highest fee revenues. For example, Buellton's population is around 5,100 and Portola's is around 2,000. The average home value for these five cities is $523,836 – only one, Buellton, is above the state average (Zillow 2024). On average, these five cities charge 75 cents per person in impact fees. Buellton's particularly low impact fee revenue could be the result of the city reporting impact fees under other reporting categories.

Figure 6

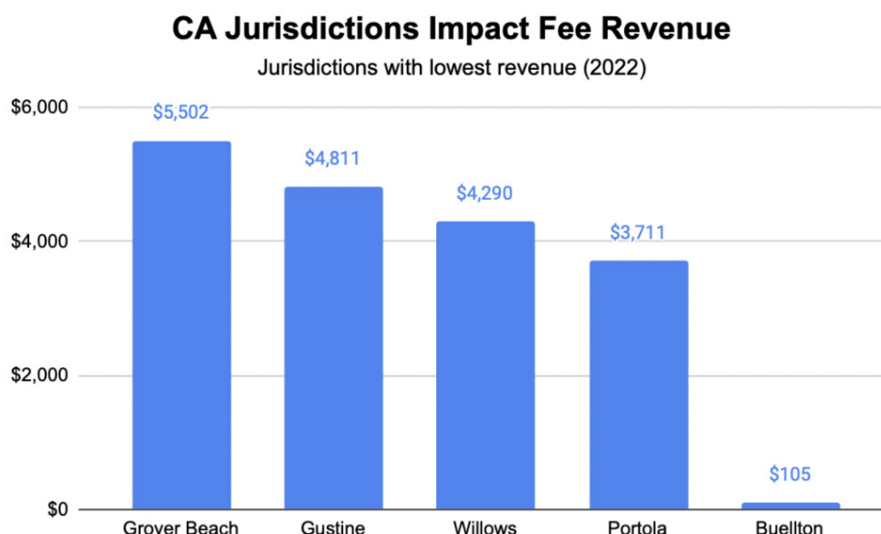
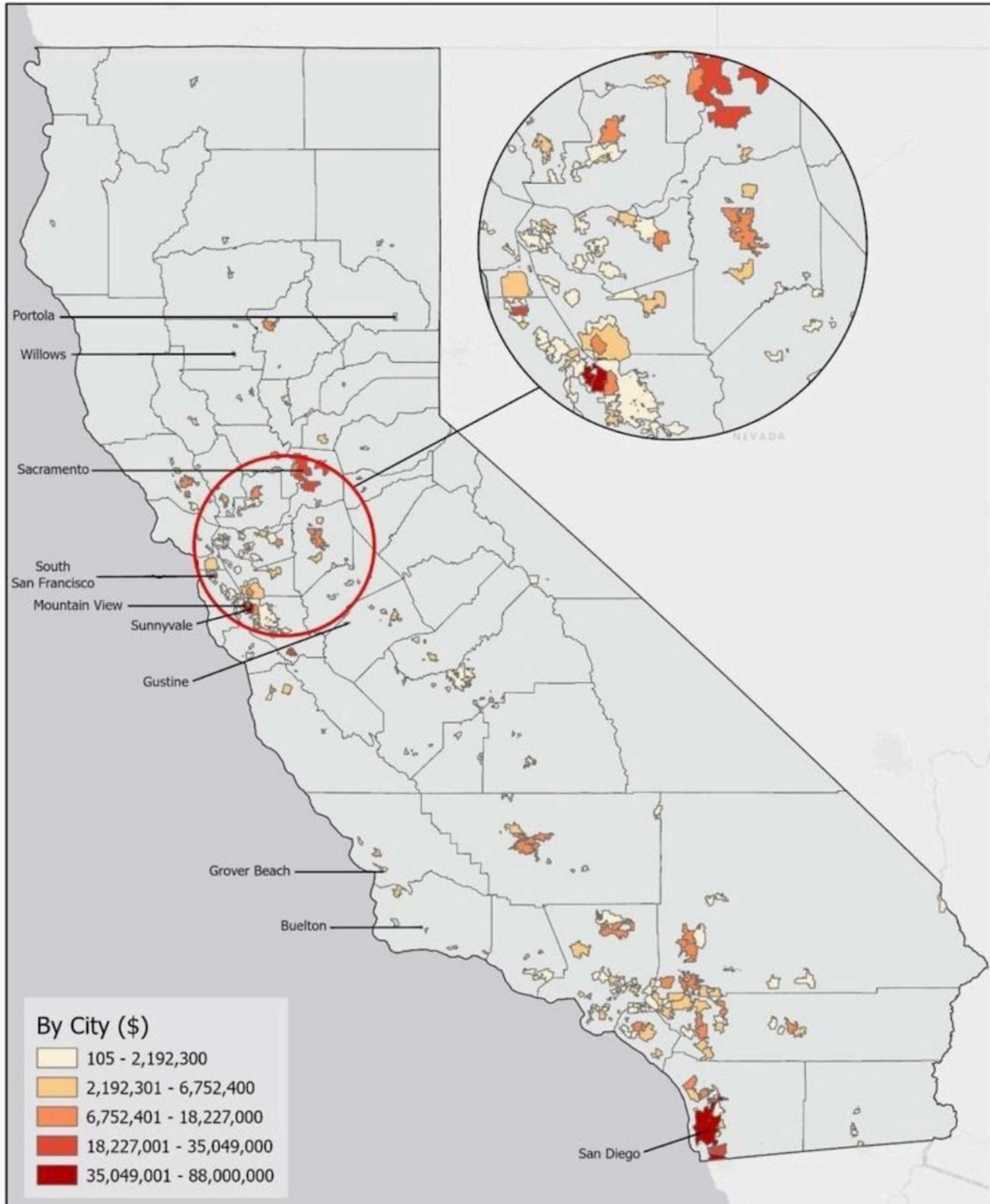


Figure 7 shows all reporting jurisdictions by the amount of impact fee revenue collected. Of the cities with the highest revenues in dollars from impact fees, four out of the five are clustered in and around the Bay area (Sunnyvale, Mountain View, Sacramento, and South San Francisco).

Figure 7



3. Analysis of Impact Fees' Effect on Multifamily Development

As discussed above, impact fees in California are much higher than the national average. These fees have theoretically opposing effects on housing development. Some economists argue that fees increase development by reducing political opposition, while others argue that fees raise overall housing costs contributing to inequality. Historic and contemporary views bias against apartment development, data suggests local jurisdictions charge multifamily developments more in impact fees on a per-square-foot basis, and statistical analyses generally show that impact fees raise housing costs and discourage affordable housing development. Ultimately, we conclude from this evidence that impact fees are more likely to raise housing costs, exclude residents, and exacerbate inequality.

3.1 Impact Fees May Have Opposing Effects on Housing Development

California's high impact fees may have conflicting effects on housing development. While impact fees increase the cost of development, they may induce more efficient infrastructure development and increase housing supply (Been 2005; Burge and Ihlanfeldt 2006). This can happen in two ways. First, these fees cause developers, homebuyers, and renters to internalize their marginal cost on local infrastructure, such as increased traffic congestion, noise, environmental impacts, or use of public facilities. Thus, impact fees can be more economically efficient than property taxes, which finance public infrastructure on an average cost basis (Mathur 2016; Been 2005). When average cost is used, households in higher-valued units often pay more than those in lower-valued units. Consequently, wealthier residents may pay more than their share for public services, and poorer residents may pay less. Impact fees reduce these externalities. Second, because developers and new residents pay impact fees to offset the cost of public infrastructure, incumbent residents may be less likely to oppose development. This may lead to increased housing development (Fischel 2015, 275).

On the other hand, impact fees can be used to exclude lower-income households (Burge & Ihlandfeldt 2006, 5). Existing residents can coordinate to pressure elected officials to increase impact fees (Fischel 2015, 274-280; Altshuler & Gómez-Ibáñez 1993, 10-15). To the extent developers pass on costs of development, impact fees increase housing costs. If market conditions do not allow developers to pass on these costs, development will not occur at all. Further, developers and prospective residents often lack the political power to oppose exclusionary impact fees. Residents moving into new development have no vote in local elections, and outside developers have little incentive to pressure local governments to reduce fees if they can pass costs to wealthier buyers.

Moreover, even if new residents can afford the increased housing costs because of fees, Mathur (2016) notes potential distributional equity concerns. If existing homeowners bought before the imposition of impact fees within a community, housing prices at that time did not internalize the full incremental cost of their impact on public facilities. Thus, new residents are forced to internalize their costs while existing residents are not.

Proposition 13 exacerbates this effect. California property values have been rising since 1975 (Federal Reserve Bank of St. Louis. n.d.). Proposition 13 assesses the tax base at the time of purchase. Consequently, an existing resident will likely pay property taxes on a lower tax base than a new resident. Not only do new residents pay impact fees to cover their marginal burden on public capital while existing residents may not, but new residents also pay more in property taxes than existing residents on the same market value unit.

These issues magnify California's racial and wealth disparities. Fees are likely to be regressive, such that poorer households pay a greater portion of income or home value than wealthier residents (Altshuler & Gómez-Ibáñez 1993, 106-110). In 2020, white Californians' homeownership rate was 72 percent while Black Californians' rate was only 41 percent (Goodman and Zhu 2021). Thus, impact fees perpetuate racial inequalities by favoring incumbent white, wealthy homeowners and by inhibiting marginalized households' mobility to areas with increased opportunity.

3.2 Evidence Suggests Impact Fees are Often Used to Exclude "Undesirable" Residents

While impact fees may have varied effects on housing production, historic and contemporary views of multifamily housing suggest fees are more likely used to block development. Modern zoning and land use decisions were driven by a desire to exclude "undesirable" residents from moving to desirable neighborhoods (Fischel 2015, 163-218). Altshuler & Gómez-Ibáñez (1993, 10-11) state: "[T]he use of land use regulatory power to keep out racial and ethnic minorities, low-income households of all types, and needed communal facilities that might disturb immediate neighbors…has been more commonplace than unusual" (see Fischel 2015, 163-218; Silver 1991).

H. L. Pollard, a Los Angeles land use attorney from the early 1900s, wrote: "[R]acial hatred played no small part in bringing to the front some of the early districting ordinances…." (quoted in Silver 1991, 191). Many of these ordinances focused on blocking multifamily housing – which was associated with working-class and non-white families. Berkeley, California in 1916 was the first United States city to adopt a zoning ordinance expressly limiting construction to single-family dwellings (Fischler 2007).

Early zoning proponent, Lawrence Veiller, illustrates early views on apartments. He contended they were an "evil." In a 1914 address to the Sixth National Conference on City Planning, he argued: "The multiple-dwelling is unquestionably a source of detriment to the development of any city and interferes greatly with proper social conditions and the development of true civic spirit. A city cannot be a city of homeowners where multiple-dwelling flourishes" (quoted in Fischler 2007, 175).

The United States Supreme Court echoed Veiller's anti-apartment views in 1926 when it ruled on the constitutionality of restrictive zoning. The Court characterized apartments as "mere parasites…destroying entire section[s] of private housing" by interfering with "free air circulation," "monopolizing the rays of the sun," "bringing…disturbing noises," and "depriving children of the privilege of quiet and open spaces to play" (Village of Euclid v. Amber Realty Co., 272 U.S. 365, 394-95 (1926)). These views continued in subsequent decades. During 1947 Senate hearings, proponents of single-family housing development linked public housing projects, rentals, and multifamily housing to stigmatize poverty and associate it with apartment dwelling (Larco 2010).

This bias against multifamily housing persists today. One principal planner we interviewed commented that there is still "a lot of NIMBYism." He explained that incumbent residents support affordable housing development, but want it built "somewhere else…. They equate density with affordability, and people are averse to change." McNee and Pojani (2022) also recorded comments from contemporary affordable housing opponents in the San Francisco Bay Area. Those comments sound similar to the Supreme Court's negative characterization of apartments made nearly 100 years ago. Multifamily development will be "unsightly," "will overburden the community," will "strain our already underfunded schools," "destroy" property values, and will increase crime rates.

City staff we interviewed said existing residents' opinions matter for land use decisions – even when city staff may not agree with them. Interviewed developers concurred: one developer emphasized that suburban homeowner activism from Parent Teacher Associations was critical in shutting down potential multifamily development. Even where political pressure does not stop construction, it raises housing costs (Altshuler & Gómez-Ibáñez 1993, 98). One developer stated: "[I]s the developer going to absorb this [increased cost]? No, this is just what a developer is going to add up and say…who around me can afford it." Another developer said, "The only projects that get built are financially feasible, so if assessing an impact fee makes it not pencil we don't do the project, or we will make it a luxury unit so we can collect higher rents."

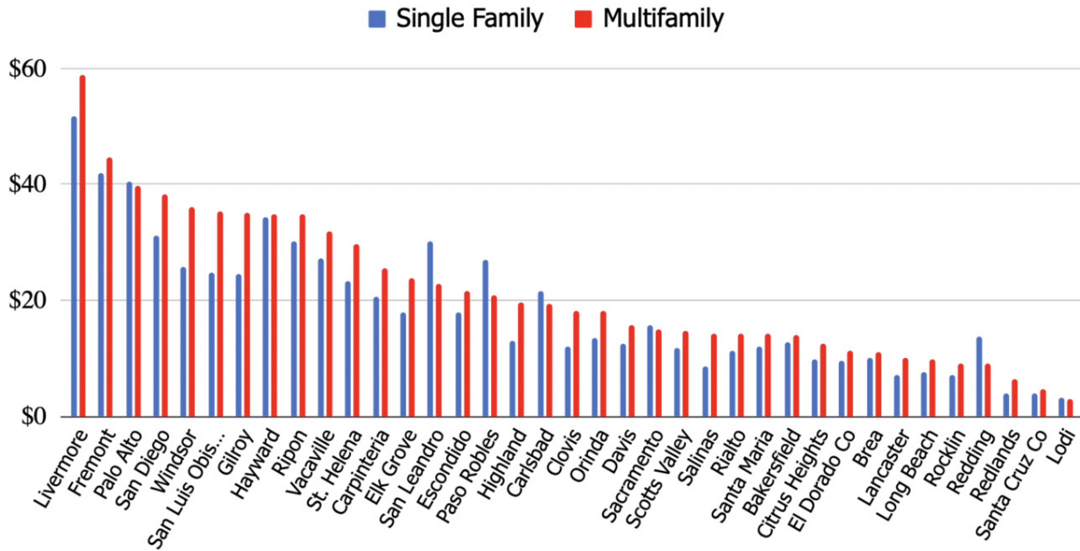
Hermosa Beach provides an example of impact fees likely intended to exclude. Hermosa Beach has no affordable housing and has failed, for years, to develop its state-mandated share (Asch 2024). It recently rezoned its commercial district for residential use to comply with Regional Housing Needs Allocation (RHNA) requirements but imposed a "land value recapture" fee of $104 per square foot on newly-developed market-rate apartments with five or more units. While revenue would nominally support affordable housing development, it means that a developer would pay an additional half million dollars to build five 1,000-square-foot apartments. Jon David, a local developer, states that the new fee will make projects infeasible, and Chris Elmendorf, a UC Davis law professor, states that the new fee will sabotage development (Asch 2024).

3.3 Data Suggest Impact Fees are Biased Against Multifamily Housing and Overburden New Residents

The above overview of historical and contemporary views on multifamily housing suggests impact fees are likely used to hamper multifamily development. The Terner Center found evidence of this bias when comparing impact fee rates. It compared impact fees imposed on prototypical single-family and multifamily housing development across ten California jurisdictions (Raetz et al. 2019). While many jurisdictions charged lower impact fees for multifamily housing per unit, every jurisdiction charged higher impact fees for multifamily development on a per-square-foot basis.

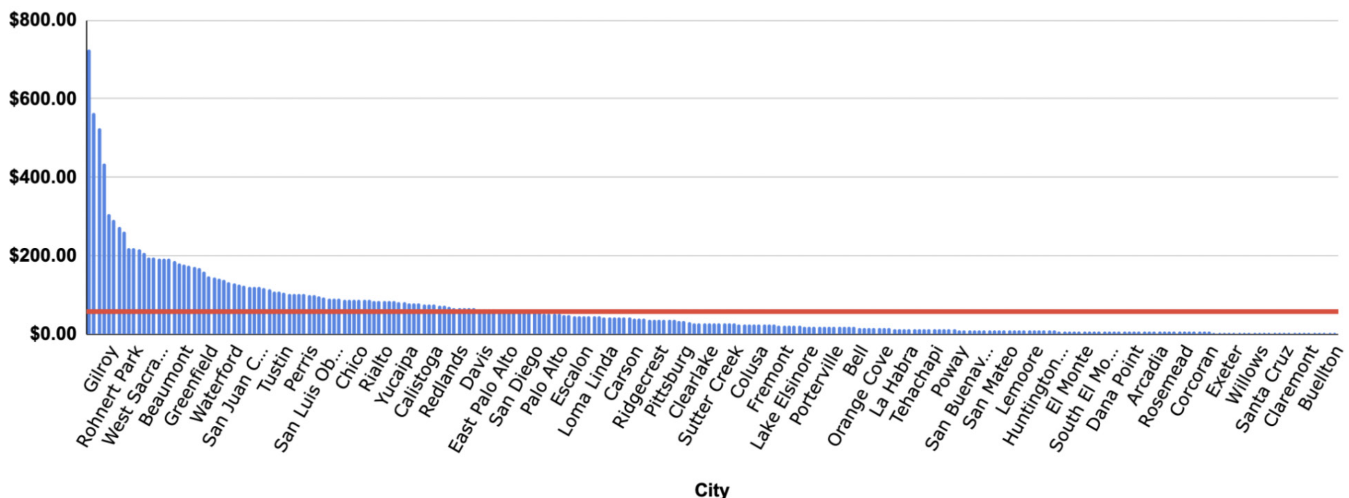
We find similar results. The dataset we used treated a typical multifamily unit as 1,000 square feet and a typical single-family unit as 2,000 square feet when reporting fees (Mullen 2019b). For all but a small handful of cities, multifamily homes are being charged more in impact fees than single-family homes on a per-square-foot basis (Figure 8).

Figure 8



Further, as discussed above, impact fees can burden new residents with higher costs than incumbent residents. We find that, generally, new residents in many communities are significantly burdened by impact fees. We consider how the costs to homeowners would differ in California if local jurisdictions financed public infrastructure and services through property taxes, rather than impact fees. By dividing the total revenue from development impact fees by the number of households in each jurisdiction, we can estimate the average household contribution needed to fund additional public facilities currently supported by these fees (Figure 9). While this figure does not directly correspond to a property tax assessment, it provides an indication of the approximate cost per household to finance new infrastructure.

Figure 9



Livermore, for example, imposes development fees exceeding $100,000 per single-family unit and over $60,000 per multifamily unit (Figure 8). A four-unit project would face fees totaling over $240,000, potentially rendering the project financially unviable. However, if Livermore distributed public costs evenly across the entire community of 84,793 households, each household share would amount to less than $42 annually. Here, we can see that, even assuming new residents are paying some portion of their own impacts on infrastructure, it is likely they are overpaying and instead subsidizing the public infrastructure of incumbent residents.

3.4 Statistical Analyses Suggest Impact Fees Raise Housing Costs

Additional research shows that housing prices overall increase as impact fees increase (Mathur 2016; Evans-Cowley et al. 2009; Ihlanfeldt and Shaughnessy 2004; Baden and Coursey 1999; Dresch and Sheffrin 1997). For example, Dresch and Sheffrin (1997) estimate that a $1 increase in impact fees increased the price of housing between $0.25 and $1.88 in parts of Contra Costa County, California. Similarly, Mathur (2007) estimates that a $1 increase in impact fees increased new house prices by $1.66 and existing house prices by $0.83 in King County, Washington. Evans-Cowley and co-authors (2009) find that new housing prices were 1.44 percent higher and existing housing prices were 6.5 percent higher in Texas cities imposing impact fees.

That said, some studies find effects differ by type of development fee. For example, Burge and Ihlanfeldt (2006) find that impact fees for water and sewage decreased multifamily construction in Florida while other "nonwater" impact fees increased production in inner suburbs and had no discernible effect in outer suburbs or central cities. Sewage and water fees do not offset existing homeowners' property taxes while other fees do. The authors hypothesize that homeowners may be less likely to oppose development that pays fees offsetting property taxes. It is unclear, however, whether these results are generalizable to California. Because California local governments have no control over property tax rates, impact fees cannot offset property taxes. Thus, one could infer from Burge and Ihlandfeldt's work that all impact fees in California would perform similarly to water and sewage fees in Florida, depressing multifamily construction.

We independently test whether increases in impact fees reduce multifamily housing production in California (Mullen 2019b; Appendix B). As shown in Figure 10, of the 33 cities with observations in both datasets, eight cities reduced impact fees between 2007 and 2019, whereas 25 increased their fees. Eleven of the cities that increased fees did so by over 100 percent. We compared these changes in impact fees to changes in multifamily housing stock. We find that almost all cities (30 out of 33) increased their multifamily housing stock, but to drastically different degrees. Many cities that had the lowest increases in impact fees had the greatest increases in multifamily housing stock. Those cities include Elk Grove, Ripon, Rocklin, and Orinda. Conversely, cities with the greatest increases in multifamily impact fees experienced the lowest growth in multifamily housing stock. This observational evidence could be consistent with a hypothesis that impact fees are negatively correlated with housing production in California.

Figure 10

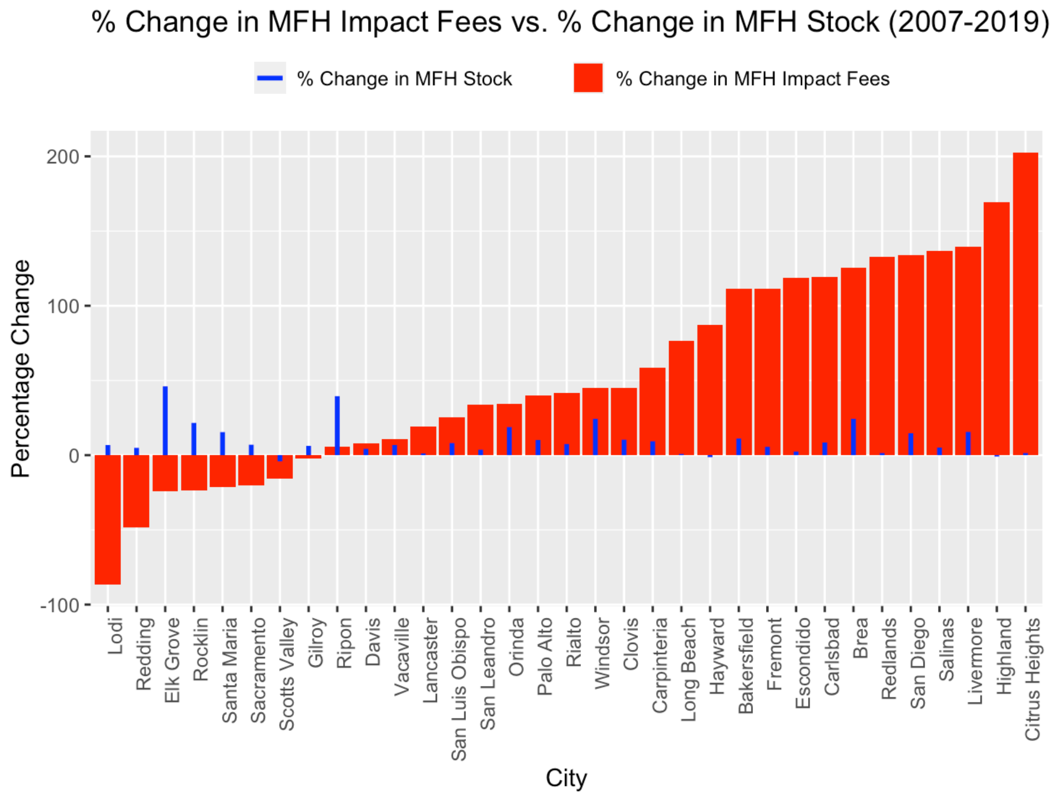


Figure 11

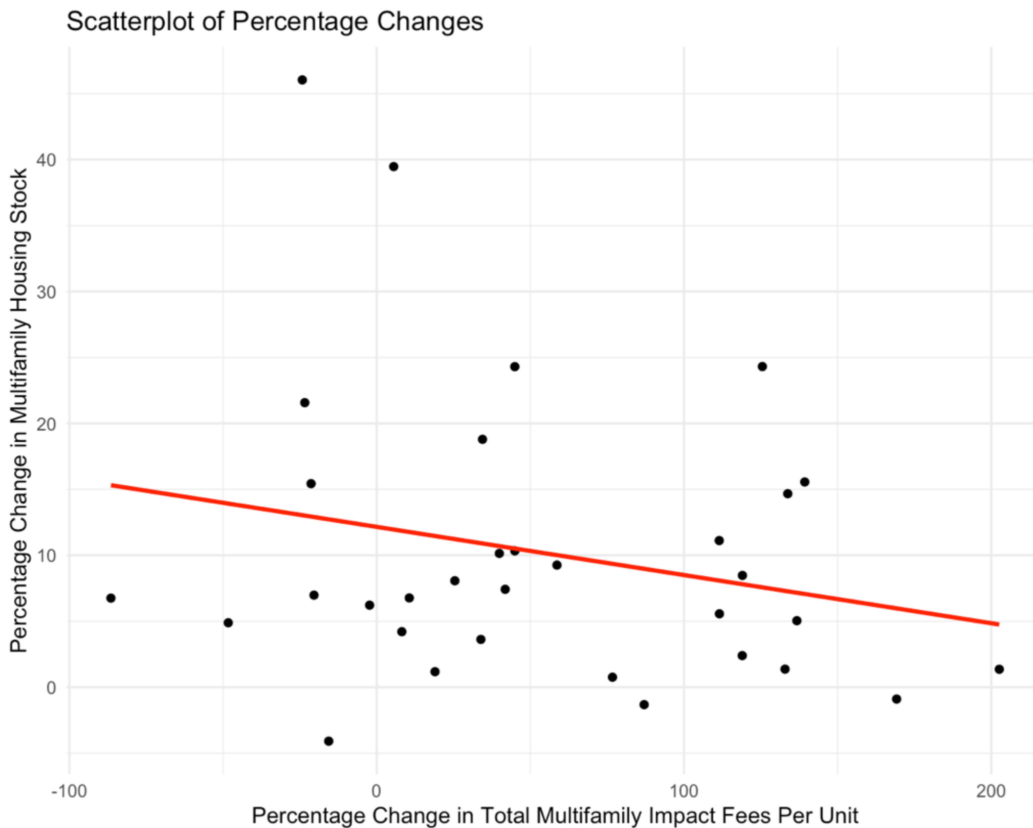


Figure 11 shows a line of best fit between the two variables. It shows a negative relationship between the percentage change in multifamily housing stock and the percentage change in multifamily impact fees per unit. Every one percent increase in impact fees per unit correlates with around a 0.04 percent reduction in housing stock. The correlation, however, is not statistically significant at conventional levels with a p-value of 0.197 (Appendix D).

We also test whether the amount of fees is correlated with multifamily housing production. The amount of impact fees may be a function of the housing values in a community. Therefore, we created a ratio of average 2015-2019 multifamily impact fees to average home prices in the middle of that period. This approximated how expensive each city's average impact fees were relative to housing prices. We compared that ratio to the percent change in multifamily housing stock over that same period. The results were inconclusive (Appendix D).

There are a few possible explanations for our failure to find statistically significant relationships between impact fees and multifamily housing development. First, as discussed above, cities may use impact fees for different purposes. Some may use fees to block housing production whereas others may seek to increase revenues from housing production. As discussed above, impact fees may increase efficiency by causing new residents to internalize costs and make development more politically feasible. This could explain Brea showing some of the highest increases in both multifamily impact fees and multifamily development. Other cities may be inhibiting overall development by raising impact fees, which would explain why the two cities with the highest increases in multifamily impact fees, Citrus Heights and Highland, experienced virtually no growth in multifamily housing stock. On average these heterogeneous effects may produce null results in our analysis.

Second, the sample consists of only 33 cities, and these cities were selected because of their consistency in impact fee reporting. Cities consistently reporting impact fees in compliance with state law may be less likely to use impact fees to outright block multifamily housing development. Thus, our results may be underestimating the negative effects of impact fees.

Third, the development of multifamily housing depends on many variables. For example, multifamily impact fees in Palo Alto and San Diego increased as multifamily housing development increased. Both of these markets were experiencing increased demand for housing during this period as their technology sectors were rapidly expanding. Our statistical tests did not control for changes in demand.

While our statistical tests do not provide additional evidence, the weight of evidence discussed in the report suggests impact fees do increase housing costs and slow housing development, particularly affordable multifamily housing. Existing empirical evidence supports this conclusion (Mathur 2016; Evans-Cowley et al. 2009; Ihlanfeldt and Shaughnessy 2004; Baden and Coursey 1999; Dresch and Sheffrin 1997). Further, Hermosa Beach provides an example of a city using development fees to exclude affordable housing. We also showed how Livermore's impact fees are far higher than the average cost associated with capital improvements. A developer specifically confirmed that those fees exclude development: "[I] never built a project in Livermore … but I looked out there plenty. I could never make the numbers work." Another stated, "I think out in the Danvilles and the Livermores of the world, one hundred percent they do" use impact fees to prevent development. Yet another developer told us generally, "If I'm assessed with an impact fee that I cannot recoup in the form of higher rent from my prospective tenants after I build it, I'm not able to deliver my investor an 80% IRR anymore. My investor says, 'Thanks, I like [it] a lot but I don't like [the return].'" Further, our current analysis of impact fees suggests

fees, generally, are higher on a per-square-foot basis for multifamily than single-family units – thus, favoring more expensive single-family development. More sophisticated data analysis may be necessary to show, statistically, that impact fees undermine multifamily development in California, but overall evidence supports that impact fees are contributing to California's multifamily housing crisis.

4. Analysis of Current Law Governing Impact Fees

Existing legal regulations seek to curb the potential exclusionary effects of impact fees. The United States Supreme Court has just clarified that these rules apply to fees both set by an individualized assessment of a particular property's impacts on public capital and fees set through legislated schedules applying to general categories of development. Despite this change, the legally required fiscal analyses used to justify fees, known as nexus studies, may embed bias against multifamily construction even though results appear mathematically precise. Recent legislation, AB 602 (Grayson 2021), sought to improve the quality of nexus studies and reinforce disclosure requirements of impact fee schedules and nexus studies. However, our survey of compliance suggests AB 602 is not meeting its goal. Most cities are not disclosing complete and up-to-date fee schedules, nexus studies, and fees charged on completed development projects as mandated by AB 602. Further, recent nexus studies also do not appear to comply with AB 602's mandate that fees be calculated on a proportionate per-square-foot basis. Those studies further suffer from flaws undermining their reliability that impact fees are only charged for direct impacts of new development.

4.1 Legal Constraints on Impact Fees Seek to Fairly Distribute Public Burdens

Recognizing that impact fees can be used to burden new developments with the cost of public improvements that benefit the entire community, federal and state laws limit local governments' discretion to condition issuance of development permits on developers' donating land or paying fees (Sheetz v. County of El Dorado, No. 22-1074, slip op. at 5-6 (Apr. 12, 2024); Koontz v. St. John's River Water Management District, 570 U.S. 595, 615-617 (2013); Ehrlich v. City of Culver City, 12 Cal. 4th 854, 876 (1996)). The Takings Clause of the United States Constitution "bar[s] government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole" (Dolan v. City of Tigard, 512 U.S. 374, 384 (1994)). Governments can demand the property owner pay for the "social costs" of new development, including "internaliz[ing] the negative externalities of their conduct," but they are "forbid[den]… from engaging in out-and-out…extortion" (Koontz, 570 U.S. at 605).

To meet Constitutional requirements controlling impact fees, a government agency must demonstrate two things. First, it must establish an "essential nexus" – a reasonable relationship – between a fee and the development's negative impact on public facilities (Nollan v. California Coastal

Commission, 483 U.S. 825 (1987); Dolan, 512 U.S. 374). Second, the agency must prove that the amount of the fee is "roughly proportionate" to the development's impact (Dolan, 512 U.S. 374, 388-395). These requirements, collectively, are referred to as the Nollan/Dolan test.[10]

At the state level, California enacted the Mitigation Fee Act[11] in 1987 in response to the growing public burden of impact fees.[12] Under this act, a local agency must also show a reasonable relationship between the fee imposed and the new development's impact on public facilities. Impact fees may only be used to pay for the portion of capital improvements attributed to new development. The California Supreme Court has ruled that the standards set out in the Mitigation Fee Act are the same as those under the Takings Clause (Ehrlich, 12 Cal. 4th 859, 860 (1996).

When applying the Takings Clause or Mitigation Fee Act, California courts make a distinction based on how fees are imposed. Impact fees may be imposed on a particular property based on an individualized assessment, known as "ad hoc" fees, or through a generalized fee schedule on various categories of development, known as "legislated fees." (Sheetz v. County of El Dorado, 84 Cal. App. 5th at 415). California courts strictly review ad hoc fees under the Nollan/Dolan test. On the other hand, California courts do not apply the Nollan/Dolan test to legislated fees. While a reasonable relationship must be shown, legislated fees must not be "so close or so thoroughly established" as ad hoc fees (San Remo Hotel L.P. v. City and County of San Francisco, 27 Cal. 4th 643, 686-87 (2002)). In California, fee schedules are valid under the Takings Clause and Mitigation Fee Act as long as they are not arbitrary (San Remo Hotel L.P. v. City and County of San Francisco, 27 Cal. 4th at 687 (2002)).

4.2 The United States Supreme Court's Ruling Means Fee Schedules will be Scrutinized More Closely

Not all states distinguish between ad hoc and legislated fees. Some states apply the Nollan/Dolan test strictly to both types of fees. The United States Supreme Court considered whether California's distinction is valid. The Court just ruled it is not (Sheetz, No. 22-1074, slip op. at 1 (Apr. 12, 2024)). In that case, the plaintiff homeowner sought to build a prefabricated home and was assessed an over $23,000 fee for traffic impacts as determined by a fee schedule. The plaintiff argued that the fee was disproportionately high and that the county made no individualized determination that the fee charged related to road use from his particular property.

A California appellate court considering the issue ruled that the fee was valid under the Takings Clause, declining to apply the Nollan/Dolan test because the fee was set in a schedule. On appeal, the United States Supreme Court reversed the California court. It ruled that all permits conditioned on payment of an impact fee – whether individually-determined or set in a fee schedule – must be strictly reviewed under the Nollan/Dolan test.

10 For a comprehensive overview of federal Takings Clause jurisprudence, please see Andrew Klemm. (2024). "Impact Fees in Flux." Case Western Law Review Note. Unpublished. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4799786

11 Cal. Govt. Code §§ 66000 et seq.

12 Certain types of development impact fees are governed by more specific statutes, including fees levied by school districts and in-lieu fees for the dedication of parklands. However, these additional statutes typically also require a showing of a reasonable relationship between the fee and the intended use.

Significantly, however, the United States Supreme Court did not comment on how California courts should apply the Nollan/Dolan test to legislated fees. California courts have only previously applied the "essential nexus" and "rough proportionality" tests to fees where the local agency individually evaluated impacts from a specific property. Yet, fees set by a general schedule to a category of properties will always be less precisely related to the impacts of a new development than fees specifically determined for a particular property. The California courts or legislature will need to determine the appropriate standard.

Other states may provide guidance although they apply the Nollan/Dolan test with differing levels of rigor. For example, the Illinois Supreme Court requires fees be "specifically and uniquely attributable to the new development" whereas the Ohio Supreme Court requires fees only be reasonably related to the new development – a standard it considers more lenient than that in Illinois. (Northern Illinois Home Builders Association v. County of Du Page, 165 Ill. 2d 25, 33 (1995); Home Builders Association of Dayton and Miami Valley v. Beavercreek, 89 Ohio St. 3d 121, 128 (2000); see Sheetz, slip op. at 4 n.3).

Under any of these standards, however, fees set by schedules begin to look more like individually-determined fees. For example, the fees statute found valid in Home Builders Assn. of Dayton and Miami Valley separately determined traffic impacts from residential, office, and commercial development; subtracted traffic impacts not related to new development; subtracted funding from other sources; exempted specific properties including smaller residential units; created a system of credits if developers dedicated land; and ensured all impact fees would be used for projects within the impact fee district (89 Ohio St. 3d 121, 123-24 (2000)). Further, the court in Northern Illinois Home Builders Association invalidated an implementing statute simply because it failed to require fees be used only on road improvements that directly and materially benefitted the specific new development on which the fee was imposed (165 Ill. 2nd at 34).

Unless the legislature acts, California courts will need to determine which legal standard to apply to fee schedules and which fee schedules meet those standards. The process of creating a clear precedent could take years. No matter what standard is used, however, fees set by a schedule will begin to look more like individually-determined fees.

4.3 Regardless of the Legal Standard, Nexus Studies Embed Assumptions Undermining Their Reliability in Calculating Impacts from New Development

California local agencies conduct "nexus studies" to justify impact fees under the Takings Clause and Mitigation Fee Act. These analyses are meant to determine the maximum impact fees permitted by law. Regardless of the legal standards against which they are judged, these studies rest on opaque assumptions that present reliability problems.

Generally, nexus studies provide a rationale for charging the fee, including how the fee relates to the burden placed on infrastructure by new development, satisfying the "essential nexus" requirement. To satisfy the "rough proportionality" requirement, analyses assess future infrastructure needs and then seek to fairly apportion those costs incurred by the new development. To do so, nexus studies often consider the existing level of service (LOS), which refers to outputs or outcomes of infrastructure investment, like a certain level of traffic congestion or parkland acres per resident. Tying fees to LOS should avoid charging new residents for the repair of existing service level

deficiencies or increased service levels that benefit the whole community.

Nexus studies often appear mathematically precise. However, commentators note that fiscal analyses do not prevent local governments from using fees in an exclusionary manner (Clapp et al. 2017; Paulsen 2014). A key problem is that these fiscal analyses rest on “strong assumptions” that can embed problematic bias (Paulsen 2014).

One example involves the attribution of costs and revenues (Paulsen 2014). Thirty years ago, Altshuler & Gómez-Ibáñez (1993, 33) noted that the conventional wisdom that commercial development is more profitable than residential owes simply to how costs and revenues are allocated. For example, sales tax revenue is typically assigned to retail uses because it is assumed retail generates this revenue. However, one could easily justify attributing some sales tax revenue to residential uses, as residents purchase retail goods and services. More recently, researchers have shown that one popular type of fiscal analysis biases toward agricultural uses despite econometric evidence showing that retail, industrial, and residential land uses all have similar revenue and cost impacts (Clapp et al. 2014).

Assumptions around the LOS approach in nexus studies can also lead to imprecision and embed bias (Paulsen 2014). The level of service is often not an output, like building a new highway lane, but instead an outcome, like maintaining a set level of roadway congestion. However, government expenditure alone does not determine outcomes. Outcomes are also based on community behavior (Paulsen 2014; Altshuler & Gómez-Ibáñez 1993, 87). For example, a local government can build a new highway lane, but congestion may not be reduced if the local population starts driving more. In fact, some experts argue that increasing traffic capacity induces more congestion (Speck 2012, 80).

When LOS is an outcome, prejudiced assumptions may result in the exclusion of new residents unfairly perceived as undermining a purportedly objective “outcome.” For example, “peer group” or “neighborhood effects” research suggests individual outcomes are determined, in part, by group association (Paulsen 2014; Calabrese et al. 2006; Hanushek et al. 2001). Existing homeowners who control fiscal decisions frequently make assumptions about peer group effects on public education or neighborhood effects on public safety. This may lead to the exclusion of lower-income households from their neighborhoods.

Older economic models reinforce the stigma of poverty by assuming multifamily residents disproportionately burden schools and other public resources. This assumption seeks to justify exclusionary practices as “efficient.” Economists claimed that in communities with residents of differing income levels, poorer residents living in apartments will freeride off wealthier residents living in single-family homes (Gallagher 2016; Hamilton 1975; Tiebout 1956). Their solution was to use exclusionary zoning and impact fees to create homogenous communities through land use regulation; in such communities, all residents would pay the same average property taxes, eliminating freeriding. Setting aside significant equity concerns with this theory, several recent analyses simply disprove that multifamily residents freeride off single-family residents.

Goodman (2005) finds that multifamily households in California metropolitan areas actually paid a higher effective tax rate than single-family households. Ives-Dewey (2007) finds similar results, showing a negative relationship between apartment value and tax burden: on average a $1,000 increase in assessed apartment value lowers the overall tax burden by $11.90. Additionally, Gallagher (2016) finds a consistent negative relationship between property tax burden and share of apartments in a locality although not all relationships were significant at conventional

levels. Commenting on the overall results, he concludes that "[t]ogether, these observations cast considerable doubt on earlier hypotheses regarding the fiscal externalities of multifamily housing" (Gallagher 2016, 255).

Moreover, Ihlanfeldt and Yang (2022) directly uncover bias against multifamily housing in the results they reported. Consistent with prior research, they find that multifamily households do not freeride off single-family households. However, they find that an increasing share of average-quality apartments increased the tax price of public services. Significantly, however, the authors reported that tax assessors are overestimating apartments' negative spillover effects on the taxable value of other properties. In other words, tax assessors' bias against apartments may be driving the result that apartments increase the cost of public services.

Thus, nexus studies and other fiscal analyses, while appearing precise, can embed unfounded bias within the assumptions they make. James and Windsor (1976) assess the relationship between actual fiscal incentives and land use decisions across 175 U.S. municipalities. They concluded: "Either the residents, community leaders, or both are ignorant of the fiscal consequences of apartment development, or fiscal arguments are used as a smokescreen to conceal actual motives for opposing apartment development. In either case, these findings do not inspire confidence in which land use controls…take account of actual fiscal forces" (James & Windsor 1976, 133).

4.4 AB 602 Seeks to Improve Nexus Studies

The California legislature has attempted to increase the quality of nexus studies recognizing their potential to hide anti-development biases. They passed AB 602 (Grayson 2021). AB 602 first mandates new substantive requirements for nexus studies. Prior to the law, many jurisdictions imposed impact fees without conducting nexus studies. AB 602 reinforces the Mitigation Fee Act by mandating that local agencies adopt nexus studies to justify the fees charged and update that nexus study every eight years.

Second, it requires nexus studies to:

1. **Disclose existing levels of service of public infrastructure;**
2. **Justify any new level of service claimed necessary by the addition of new residents; and**
3. **Justify increases in existing impact fees.**[13]

These changes were meant to make the assumptions underlying nexus studies more explicit.

Third, AB 602 mandates that local jurisdictions calculate fees on a per-square-foot basis unless the municipality:

1. **Explains why per-square-foot is not appropriate;**
2. **Describes why an alternative is better; and**
3. **Adopts policies that do not disproportionately charge smaller developments more.**

13 Government Code 66016.5.

As the Terner Center and our own analysis above show, impact fees calculated on a per-unit basis can obfuscate that certain local governments charge higher impact fees on multifamily than single-family development.

AB 602 also requires large jurisdictions to adopt capital improvement plans as part of nexus studies. Those plans project community needs and the specific infrastructure to address those needs. AB 602 further required that the California Department of Housing and Community Development (HCD) develop a nexus study template to assist local jurisdictions,[14] which it did in December 2023 (HCD 2023).

4.5 AB 602 Has Not Led to Substantive Reform of Nexus Studies

We reviewed recent nexus studies to determine whether they have improved since AB 602 went into effect in January 2022. We also reviewed the HCD template. The nexus studies include:

1. **May 5, 2022 AB 602 Supplemental Analysis of a 2020 Tri-Valley Transportation Council nexus study;**[15]
2. **September 2022 Update to Elk Grove Roadway Fee Program Draft Nexus Study;**
3. **July 6, 2023 Development Impact Fee Calculation and Nexus Report for the City of Highland, California; and**
4. **January 18, 2024 Fire and Dispatch Facilities Development Impact Fee Study for City of Brea.**

Before AB 602 became law, the Terner Center reviewed nexus studies from eight localities, including Elk Grove, Fremont, Fresno, Irvine, Riverside County, Roseville, Santa Cruz, and Truckee (Terner Center 2020). The report found that some nexus studies did not disclose the current level of service, which could allow local jurisdictions to impose impact fees on new residents to fund improvements that benefit all residents. It also found that some local jurisdictions overestimated the facility cost increases brought on by new residents. Overall, the report found that localities did not spend enough time considering the impact of total fees and exactions on development.

We find many of the same issues still exist in recent reports. First, we find that many of the reports do not impose fees on a proportionate per-square-foot basis. Second, we find that most reports disclose an existing level of service. However, that disclosure does not ensure new residents are only charged for their impacts on public capital. The studies, instead, seem to calculate fees closer to an average cost than a marginal cost basis. Third, most reports are not likely to meet the new legal requirements set out in Sheetz.

To begin, three of the four reports do not impose fees on a proportionate per-square-foot basis despite AB 602's mandate. Only Brea's report does. In contrast, Highland calculates fees on a dwelling unit basis, charging different fees for attached units, detached units, and mobile homes. It argues that calculating fees on a dwelling unit basis has advantages over calculating on a land acreage basis. Highland, however, does not explain why calculating fees on a per-square-foot

14 Health and Safety Code Sec. 50466.5.

15 The Tri-Valley Transportations Council is a joint authority of the County of Alameda, the County of Contra Costa, the City of Livermore, the City of Pleasanton, the City of San Ramon, the City of Dublin, and the Town of Danville.

basis is not appropriate, why the alternative of dwelling units is better, or what steps are being taken to ensure fees do not impact smaller developments, all requirements under AB 602.

Similarly, the supplemental analysis to the Tri-Valley Transportation Council imposed fees on a dwelling unit basis. The study acknowledges that AB 602 requires that fees be assessed on a proportional per-square-foot basis, but provides no explanation to justify its alternative fee basis.

Elk Grove imposes different residential development fees based on seven square-footage categories. This approach does not result in fees being charged proportionally. The lowest category includes residential units “up to 1,200 sq. ft,” and the highest includes units “greater than 3,400 sq. ft.” The “up to 1,200 sq ft” fee is $3,860.99. The next category is “greater than 1,200 to 1,400 sq. ft.” A residential unit, thus, may increase by one square foot, and yet the fee more than doubles to $7,345.

Moreover, Elk Grove’s analysis assigns Institute of Transportation Engineers (ITE) land use codes to each category. The lowest square footage category is coded as “mid-rise multifamily housing.” All other categories are coded as “single-family unit residential-detached.” Elk Grove appears to have chosen its square-footage categories to reflect unit type.

The HCD template says that a “nexus study should analyze and determine estimates for residential square feet” (HCD 2023, 7). It does not explain that the fee must be calculated on a proportionate per-square-foot basis. Most of the remainder of the template recommends conducting analyses on bases other than square footage. For example, number of bedrooms is suggested as a proxy to calculate the service population. In some steps of analysis, the template suggests using residential type, rather than square footage, to ensure fees are proportionate. This makes the calculation of fees confusing, and, as we see above, localities struggle with providing fee schedules on a proportionate per-square-foot basis.

Second, all reports make some attempt to disclose existing levels of service. For example, when calculating fees supporting law enforcement facilities, Highland determines the total average calls for police services by dwelling unit type over the prior 12-month period. The Tri-Valley Transportation Council study includes details on each type of planned transportation improvement, using existing or desired traffic density, delay, or crash rates.

These disclosures, however, do not ensure that new residents only pay for the marginal burden they put on public facilities. For example, the Tri-Valley Transportation Council study includes 100 percent of roadway technology enhancement in its fee calculations. These improvements purport to leverage new technology, like connected autonomous vehicles, to increase safety and mobility. The report notes that these improvements are meant to offset the impacts of future development. It is, however, also arguable that these improvements increase the level of service and benefit the entire community. Thus, the Tri-Valley Transportation Council study may be overestimating impacts from new residents despite identifying an existing level of service in compliance with AB 602.

All studies used an “existing inventory” or “planned facilities” method of calculating impacts. These approaches, which are also found in the HCD template, use an average cost rather than a marginal cost basis. For example, under the “Existing Inventory Method,” the template states that localities should value existing infrastructure and then divide by the current population (or a similar cost unit of demand) (HCD 2023, 10). Similarly, it instructs that under the “Planned Facility Method,” localities estimate the new facilities’ value and divide by demand units per

new development. But an average cost basis undermines a key advantage of impact fees. As discussed above, new residents should internalize their marginal, not average cost, on public infrastructure (Altshuler & Gómez-Ibáñez 1993, 87).

Further, the methodologies in the reviewed reports are using both outcome and output bases for determining the level of service. Average calls for police service is an output, whereas traffic density and crash rates are an outcome (Paulsen 2014). As noted above, outcome-based LOS is more susceptible to biasing (Paulsen 2014). The HCD template provides a detailed discussion of the existing level of service but does not discuss the costs and benefits of each modality.

Third, as noted above, the Sheetz decision changes the legal standard under which fee schedules will be reviewed. It appears that fee schedules in states that are already consistent with Sheetz are more particularized than those in California. The HCD template already recommends some particularized tailoring, for example, determining fees based on the type of development, subtracting impacts from other developments, and exempting certain properties from fees. This particularization, however, is not mandated. For example, of the nexus studies reviewed above, only the Elk Grove study and implementing ordinance appears to contain all the elements found in the Ohio statute considered in Home Builders Association of Dayton and Maimi Valley (89 Ohio St. 3d 121, 123-24 (2000).[16]

Overall, three of the four reviewed studies did not appear to calculate fees on a proportionate per-square-foot basis or explain the advantage of the chosen alternative. Further, while they disclosed existing levels of service, this disclosure does not appear to ensure that developers and new residents are only paying their marginal burden on public facilities. These were issues the Terner Center identified in its 2020 survey of nexus studies, and AB 602 does not seem to have remedied them. It is unclear whether these fee schedules will meet Sheetz legal requirements.

4.6 More Local Jurisdictions are Disclosing Impact Fees, but not Nexus Studies, After AB 602

AB 602 also imposes disclosure requirements to increase transparency and certainty around development impact fees. Beginning with the Mitigation Fee Act, the California legislature sought to use disclosures to control impact fees. That statute requires a local jurisdiction to disclose an annual report showing the:

1. **Purpose of the fees collected and the balance from prior years;**
2. **Specific amounts collected in that fiscal year;**
3. **Public improvements on which fees were expended; and**
4. **Approximate date by which further construction will begin.**[17]

Within five years after collecting fees, a local jurisdiction must identify the purpose of the fees still in an account; again demonstrate a reasonable relationship between the fee and the purpose

16 That statute: (1) separately determined traffic impacts from residential, office, and commercial development; (2) subtracted traffic impacts not related to new development; (3) subtracted funding from other sources; (4) exempted specific properties including smaller residential units; (5) created a system of credits if developers dedicated land; and (6) ensured all impact fees would be used for projects within the impact fee district

17 Cal. Govt Code §66006(c).

for which it was charged; and identify sources to fund incomplete public capital projects. To the extent a local jurisdiction does not make these findings, it must immediately refund the money collected (Cal. Govt. Code 66001(d)(2); Walker v. City of San Clemente, 239 Cal. App. 4th 1350 (2015)). SB 1202 (Stone 2018) added further strength to Mitigation Fee Act disclosures. If a local agency fails to file an annual report for three years, the municipality must bear the cost of any requested fee audits. SB 319 (Melendez 2021) goes further, requiring a city to pay for audits for each additional year they are out of compliance.

Other recent bills have focused on disclosure requirements meant to provide certainty to developers. A developer summed up issues they face: "[T]he biggest problem will be you'd have to go look in various places for different impact fees." Another echoed: impact fees are "notoriously hard to figure out." To remedy this problem, AB 1483 (Grayson 2019) required localities to post fee schedules and archives of nexus studies on their websites. Further, SB 330 (Skinner 2019) prohibits localities from charging additional impact fees, except for annual inflationary adjustments, after the developer submits a preliminary application. AB 1820 (Schiavo 2024), which was just re-referred to the Committee on Housing and Community Development in late February 2024, would shorten the time in which localities would have to provide initial fee estimates to developers. AB 3012 (Grayson 2024), which was also re-referred to the Committee on Housing and Community Development on April 22, 2024, would expand disclosure requirements for development fees. It requires local jurisdictions to provide a tool on their website allowing developers to estimate fees for constructing housing. It also would require the HCD to develop a fee schedule template and outline best practices in presenting fees.

However, there are few enforcement mechanisms associated with these bills, and local jurisdictions do not consistently comply. In 2021, SPUR reported that fewer than half of surveyed localities posted comprehensive fee schedules in compliance with AB 1483 (SPUR 2021). Further, SPUR found that 78 percent of jurisdictions failed to post nexus studies. Following this finding, the legislature added disclosure requirements in AB 602 to reinforce AB 1483. Localities must:

- **Post a direct website link to fee schedules;**
- **Publish nexus studies adopted since January 1, 2018; and**
- **Disclose total fees imposed for any development after issuance of certificates of occupancy or final inspection.**

Local governments must update these disclosures on a regular basis, but no less than twice a year.

We visited the same 60 jurisdictions' websites reviewed by SPUR (see Appendix C) to assess current compliance with AB 602. We search for: (1) impact fee schedules, (2) nexus studies since 2018, and (3) actual fees charged to developers. First, we find impact fee disclosure to be relatively high – 76 percent of the surveyed jurisdictions disclosed impact fee schedules. However, 30 percent were not immediately available and took significant effort to locate (Figure 13). Moreover, some cities posted fee schedules that were quite old. For example, Davis' fee schedule was from 2009, Newman's from 2014, and Upland's from 2015.

Figure 12

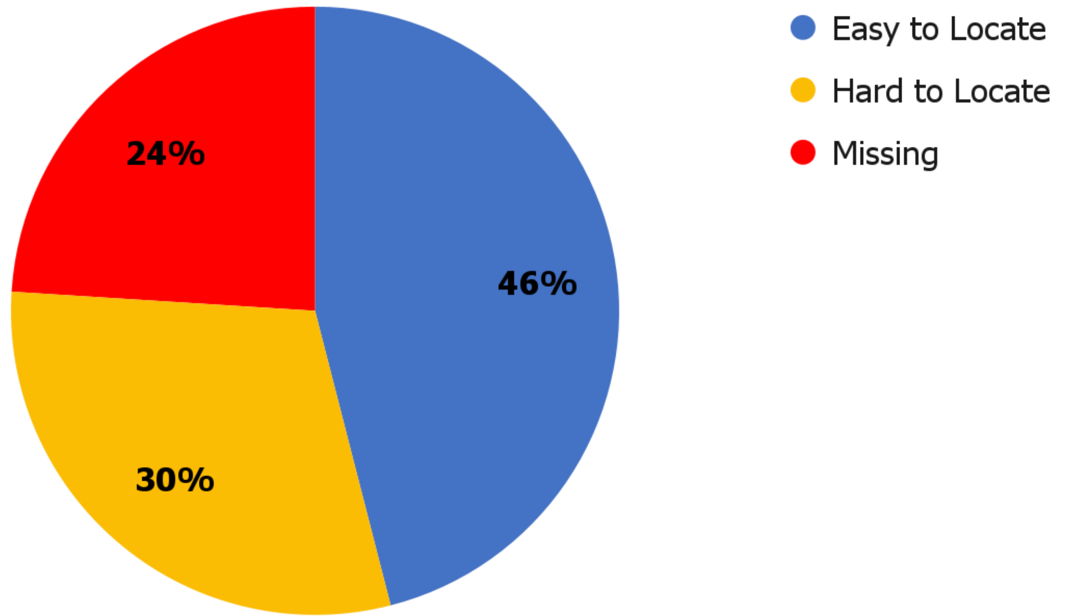
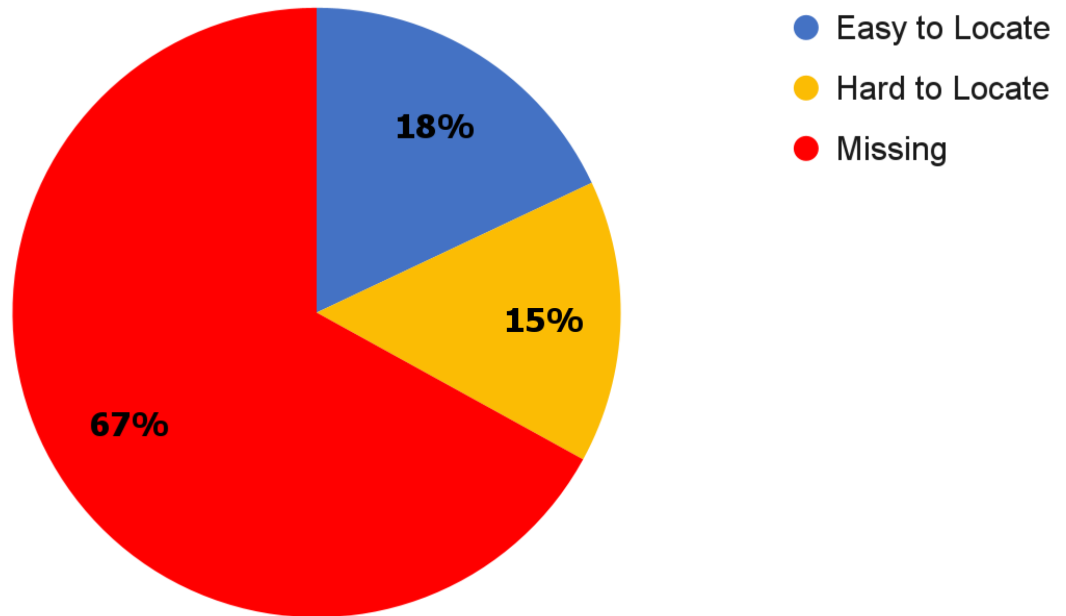


Figure 13



Only 33 percent of surveyed jurisdictions posted their nexus studies at all or indicated that they had no nexus studies from 2018 onward (Figure 14). While AB 602 only requires that nexus studies after 2018 be posted, we located nexus studies from as early as 2004.

We also found that no local jurisdiction posted actual fees charged to developers after final inspection or certificates of occupancy were issued. This is a new requirement that was not present in AB 1483. One city planner noted that there has been a lot of state-level regulation of impact fees in recent years, and it is difficult to keep up; he stated that he is still working to ensure his city is complying with regulations that were chaptered three years ago. It is possible compliance will increase with time.

4.7 Reforms Limiting Impact Fees Meet Political Resistance

The legislature may focus on disclosure efforts because reforms intended to cap impact fees meet strong political resistance from California cities and counties. El Dorado County in Sheetz argued that limiting impact fees "would disrupt if not destroy [local government's] ability to fund the capital-intensive infrastructure necessary to serve new development" (Christopher 2024). One reason for political resistance is that proposed legislation limiting fees does not provide a means to replace lost revenue (Neuburger and Gallager 2020). Doing so may reduce political opposition.

5. Policy Options

Considering current evidence, the legislative landscape, and the Sheetz decision, we evaluate three policy options: eliminating, capping, or disincentivizing impact fees while providing alternative local revenue sources. These policy options are meant to remove impact fees as a barrier to multifamily housing development while replacing lost local revenue. Sheetz will require a reevaluation of the way in which California local jurisdictions justify and evaluate fees set in a schedule. It provides an excellent opportunity to consider new impact fee policies. Overall, our analysis suggests that current reforms tied to increasing disclosure or improving nexus study quality have not been successful. Thus, we suggest three more direct ways of regulating impact fees.

5.1 Eliminate Impact Fees & Replace Local Revenue Stream

One option to increase multifamily housing development is to eliminate impact fees entirely. Eliminating local impact fees would cut developers' upfront costs, reducing the cost of housing. The removal of impact fees would also reduce the administrative burden cities face when mandated to justify, disclose, and collect impact fees. Therefore, the removal of impact fees would get rid of a significant barrier to development, reduce local administrative burden, and make more projects financially viable.

However, as noted above, local jurisdictions rely on impact fees as a revenue source. Although impact fees typically constitute only a small portion of total local revenue, certain jurisdictions

depend heavily on them to finance public infrastructure and services. As gleaned from interviews with city managers, impact fees may be one of the only means of funding infrastructure, particularly in local jurisdictions that do not have discretion over other revenue streams. The California Association of Counties states that they “will oppose any arbitrary limitations or waivers on impact fees that do not backfill local costs to provide necessary infrastructure and public facility needs” (Neuburger and Gallager 2020).

Therefore, any revenue loss resulting from the elimination or capping of impact fees must be adequately supplemented by alternative funding sources, such as that proposed by ACA 1 (Aguiar-Curry 2023). This legislation, already approved by the California State Assembly, is slated for a vote by Californians in 2024.

ACA 1 allows jurisdictions to increase property taxes, lowers the voting threshold from 65 percent to 55 percent to assess property taxes, and raises the level of debt allowed to fund public infrastructure, affordable housing, and other related community development costs. Crucially, no taxes could be levied without the direct endorsement of the jurisdiction’s electorate (Appendix C). By eliminating impact fees and replacing the lost revenue with property taxes and bonds, the fiscal responsibility is distributed evenly across the entire community. ACA 1, therefore, provides an alternative to impact fees and backfilling lost revenue.

5.2 Cap Impact Fees & Replace Local Revenue Stream

Eliminating impact fees in their entirety may not be politically viable, as replacing all lost revenue might be difficult. Capping impact fees will lessen barriers to development while still allowing cities to collect revenue from fees. One developer explains: “Whatever you can do on the fee side to eliminate [or limit] them would help housing without question, and it’s really just as simple as that.” Limiting the wide variance in impact fees through a cap can help remove barriers to development. Three potential methods for implementing a cap include:

Cap impact fees as a percentage of market value

Introducing a flat percentage fee based on the market value of development serves to cap the upper limit of assessed fees. This approach does not address the tension between localities and developers surrounding the timing of fee collection. Local governments often prefer to collect fees early, typically at permit issuance, which can be years before project completion. Front-loaded fee payment heightens the risk for developers, who would prefer to pay fees closer to project completion. The timing of market value assessment can also be contentious. Assessing market value at permit issuance becomes challenging due to fluctuating market conditions. Developers have an incentive to underestimate the projected market value to pay lower fees, while jurisdictions may be inclined to overestimate and assess higher fees. While it is optimal to collect fees upon occupancy to align with revenue generation and ensure accurate market value assessment, the prevailing tendency of governments to collect fees early suggests that enforcing occupancy-based fees may be challenging.

Cap impact fees as a percentage of construction costs

Charging fees based on construction costs presents challenges. Relying on developers to disclose their construction costs introduces transparency issues and potential conflicts. Developers could be incentivized to misrepresent their true costs. Since final construction costs are not known until the completion of a project, this option leaves developers uncertain about the fee amount they will be charged. Additionally, calculating fees for each project based on costs is administratively cumbersome. Many jurisdictions already struggle with compliance regarding impact fee standards, making it unlikely that they have the capacity to assess every development's costs individually.

Cap impact fees as a flat fee per square foot

Assessing impact fees per square foot would allow developers to know their charges upfront without discouraging the construction of smaller units. For instance, if fees were set at $10 per square foot, a 500 sq. ft. studio would incur a $5,000 impact fee, while a 1,250 sq. ft. three-bedroom unit would incur a $12,500 fee. Capping impact fees per square foot resolves issues such as administrative burden and leaves flexibility around when fees can be assessed. Both our analysis and the Terner Center analysis show that charging fees other than on a per-square-foot basis obfuscates that multifamily development is charged more than single-family development. Finally, this recommendation is consistent with current legislation, like AB 602, which seeks to calculate residential development fees on a proportionate per-square-foot basis.

Overall, we favor capping fees on a per-square-foot basis. Capping fees on a per-square-foot basis streamlines the administrative process, provides flexibility in the fee assessment timing, and incentivizes smaller, more affordable units. This proposal would also include efforts to replace lost revenue from other sources like ACA 1. Capping fees and replacing revenue prevents the misuse of impact fees to exclude, makes new development less expensive, and provides broader revenue sources for jurisdictions.

5.3 Reduce Barriers for Developers and New Homeowners to Challenge Unjustified Impact Fees

The state could also consider increasing private enforcement of the Mitigation Fee Act to disincentivize localities from imposing excessive impact fees and ensure that, when they do impose fees, they are fully justified.

As discussed above, many disclosure and other requirements lack enforcement mechanisms. Other policy analysts have called for state agencies to further monitor and enforce recent legislation (Terner Center 2020). However, these agencies are already overburdened.

An alternative is to amend the Mitigation Fee Act to incentivize private enforcement. This approach is already used to enforce the state's antitrust and labor laws, where government enforcement is supplemented by "private attorneys general" bringing private actions. These amendments could reduce the use of impact fees for exclusionary purposes while not burdening state agencies with the costs of enforcement. We consider the following changes:

Align substantive legal standards with development goals

There is no doubt that the legal standard matters. An analysis of Takings Clause cases from 1979 to 2012 revealed that plaintiffs won around 10 percent of the time under the lenient standard California courts previously used to evaluate fee schedules (Krier & Sterk 2016, 59). However, three times as many plaintiffs – just under 30 percent – succeeded in challenging exactions under the Nollan/Dolan standard now imposed by the United States Supreme Court. While increased litigation success may disincentivize local governments from charging unjustifiable fees, there are potential downsides. As discussed above, in states that apply the Nollan/Dolan test, fees set by schedules look a lot more like ad hoc fees. Individualized assessments may slow permit processing time, increase developer uncertainty, and unfairly favor developers with more economic and political power. Moreover, states that apply the Nollan/Dolan test to fee schedules use different legal standards. The California legislature could evaluate the pros and cons of these standards and amend the Mitigation Fee Act to provide courts with guidance. This may more quickly provide needed certainty to both local agencies and developers than waiting for courts to establish rules by setting precedent.

Mandate detailed nexus study methodologies

As shown above, AB 602 and the HCD template seem ineffective in improving the quality of nexus studies. AB 602 does not have an enforcement mechanism, and the template states it simply sets out "typical" ways of conducting nexus studies. Legislation could mandate that local governments use certain methods that are more likely to support development and less likely to shackle new residents with more than their share of public facility costs. Mandated guidance would also reinforce standards in compliance with Sheetz. To the extent those mandated methodologies are not followed, this would be evidence that a local jurisdiction has failed to show a reasonable relationship between its fees and the impacts of new development on public facilities.

Introduce fee- and cost-shifting provisions

Bringing private legal challenges is expensive. Currently, successful plaintiffs are only entitled to damages amounting to the unjustified fees they previously paid plus interest. Yet, attorneys' fees and costs will significantly cut into that damage award. Therefore, the legislature could mitigate cost barriers by amending the Mitigation Fee Act to allow successful plaintiffs to recover attorney fees and costs from localities with unjustified fees.

Allow punitive or automatically multiplied damages

Legislation could amend the Mitigation Fee Act to provide plaintiff developers a larger upside and defendant localities a greater downside, by allowing for recovery of punitive damages in egregious cases or automatically trebled damages – as already allowed for antitrust claims.[18] This would encourage private suits and disincentivize localities from imposing unjustified fees.

18 This means that damages would be automatically multiplied by three.

6. Method of Evaluation: Multi-Criteria Decision Analysis

We assess our three policy alternatives according to the following criteria:

Pro-multifamily Housing Development

We center policy options that encourage and facilitate the development of multifamily housing across California. We evaluate the extent to which the adoption of this policy either removes barriers to or motivates housing development, especially multifamily housing.

Political Feasibility

We evaluate the proposed policies based on their propensity for enactment and anticipate the political challenges policy options may face. We seek to understand the supporting and opposing arguments of each option and the level at which this policy will be implemented. We seek to recommend the option with the highest political viability.

Raises or Maintains Adequate Revenue for Jurisdictions

While hindering new development, impact fees provide a critical revenue source for local governments to finance public services, facilities, and improvements. Our policy recommendation must work to adequately establish alternative revenue sources for localities. Each policy option is evaluated on its ability to create or maintain a revenue stream for jurisdictions to continue operations that are currently funded through impact fee enforcement.

Centers Distributional Equity

The development of multifamily housing is central to overcoming California's housing and homelessness crises, both of which disproportionately harm communities of color and low-income individuals. Our policy recommendation must ensure that alongside promoting housing development, the benefits are distributed equitably across communities. As discussed above, there is reason to believe that new residents are paying more than existing residents for the costs of public facilities. Our evaluation of each policy option's commitment to equity is predicated on fees, exactions, or taxes being progressive. Additionally, we consider how each policy option manages to safeguard existing communities from displacement and gentrification while allowing for mobility and a fair fiscal burden for new residents.

Increases Transparency Around Development Decisions

The lack of transparency and accessibility around impact fees, including how jurisdictions calculate and justify them, are significant factors preventing development. We evaluate each policy option on its capacity to make fiscal housing development requirements more transparent, as well as its ability to limit the role of municipal discretion in the development process.

7. Analysis of Policy Options

The following evaluation matrix outlines our process of ranking the three policy options:

1. **Eliminate impact fees and replace this revenue stream**
2. **Cap fees and replace this revenue stream**
3. **Increase private enforcement mechanisms to challenge excessive or unjustified fees.**

We scored each of our policy options one through five on each of our decision criteria. A score of one signifies flaws in the policy option's design or efficacy that prevent it from adequately addressing that criterion, while a score of five indicates that the policy option fully addresses the criterion. The scores from all criteria were then totaled. "Eliminate and replace" had the lowest total score of 18, followed by "enforcement" with 19. The policy option that received the highest score of 22 out of 25 was capping impact fees and replacing this revenue stream. Figure 14 and the following explanation details the scoring rationale.

	1	2	3	4	5
Pro-multifamily Housing Development			Enforcement	Cap & Replace	Eliminate & Replace
Political Feasibility	Eliminate & Repalce			Cap & Replace	Enforcement
Raise or Maintain Adequate Revenue for Jurisdictions		Enforcement		Eliminate & Replace	Cap & Replace
Centers Equity			Eliminate & Replace	Enforcement	Cap & Replace
Increases Transparency around Development Decisions				Cap & Replace	Eliminate & Replace/ Enforcement

Total Scores	
Eliminate Fees	18
Enforcement	19
Cap & Replace	22

7.1 Eliminate Impact Fees & Replace Local Revenue Stream (18)

Eliminating impact fees and replacing them with new revenue streams had the lowest score of the three policy options. Eliminating and replacing impact fee revenue received a score of five for its ability to promote multifamily housing development and its capacity to improve transparency around the development process; without the burden of impact fees, developers would face reduced and more precise costs associated with a project, potentially spurring development. This option received a score of four for its ability to generate an adequate local revenue stream because it proposes legislation – ACA 1 – to fund necessary infrastructure and publicly provided goods. While eliminating impact fees would likely appease developers by reducing upfront costs and local governments by providing an alternative source of revenue, this option still received a score of one for its political feasibility. In order to replace the funds previously generated through impact fee exactions, residents would face increasingly high property taxes, which voters, particularly incumbent residents, would be reluctant to pass. Lastly, this policy option received a score of three for equity concerns. Eliminating impact fees, while encouraging housing development where it may have been previously blocked, could create equity issues by stripping localities of their ability to finance needed services if ACA 1 does not pass.

7.2 Increase Private Enforcement Around Challenging Fees (19)

Increasing private enforcement mechanisms to challenge impact fees received the next highest score of 19. Because it does not directly remove fiscal barriers to development, this option received a score of three for the pro-multifamily housing criterion. However, it is more politically feasible than the other two options, as it does not directly remove or cap impact fees as a revenue source for local jurisdictions. Most stakeholders can agree that impact fee processes and compliance mechanisms are flawed and would support legislation aimed at its reform. This option received a score of two for maintaining local revenue sources. While it should allow for the continued use of justified fees, it may generally disincentivize the use of fees altogether because of the increased risk of litigation. Finally, this option scores very high for increasing transparency because lawsuits brought by developers and other private parties will force increased disclosure and the improvement of nexus studies to justify fees. While this option outlines clearer ways for developers to challenge and punish cities that enact unjustifiable fees, jurisdictions needing revenue may find a way to rationalize excessive fees. Thus, the propensity for this option to increase housing development is low.

7.3 Cap Impact Fees & Replace Revenue Stream with ACA 1 (22)

The policy option that received the highest total score is capping impact fees and replacing this revenue stream. The cap and replace option scored a four out of five for its capacity to promote multifamily housing development since reduced fees would result in additional fiscally viable development projects. As denoted by a score of four, capping impact fees would also significantly increase transparency and reduce municipal discretion around development fees. Ultimately, the reason for this policy option's high total score comes down to its ability to generate an adequate revenue stream for localities, while still mitigating the consequences of excessive impact fees on development projects. Local governments are now obliged to rely on impact fees to pay for public facilities, as property tax revenue has been severely reduced. Local jurisdictions heavily influence the state legislature, such as CalCities, who urge their members to "think creatively

about the use of development impact fees in your community," as a way to finance all types of city projects (Brown and Lyons 2003). Further, a legislative advocate for the California State Association of Counties stated, "Unless you want a dirt road and like, you know, bandits out there because we don't have a sheriff, we need to have some level of an assessment done" – emphasizing local jurisdictions' reluctance to alter impact fees (Christopher 2024). By offering a method of replacing the revenue caused by capping fees, both local jurisdictions and developers are more likely to support this option, giving it a score of four for both its political feasibility and its generation of jurisdictional revenue. Lastly, this option was deemed the most equitable because it is most likely to ensure development can occur without jurisdictions having to reduce vital public services for residents.

8. Policy Recommendation

Given this report's findings, we recommend statewide legislation that enforces jurisdictional compliance with a cap on development impact fees on a per-square-foot basis, and simultaneously support advocacy efforts for ACA 1 or other legislation that works to replace lost municipal revenue streams.

9. Conclusion

This report considers development impact fees. We find that on average, impact fees are a small portion of local jurisdictions' revenue. However, interviews with city planners and managers suggest that in jurisdictions where voters have earmarked other revenue sources for specific uses, impact fees provide an important means of funding infrastructure improvements. Additionally, we find that while impact fees may have positive effects within communities, evidence ultimately suggests that impact fees discourage multifamily housing development and increase the cost of housing. We also find that past legislative reforms aimed at improving the quality of nexus studies and fee disclosure have not been successful, in part because fiscal analyses are inherently based on strong assumptions that embed historic and contemporary bias against multifamily housing development. Finally, the Sheetz ruling – which invalidated California's standard for reviewing fee schedules – provides an opportunity to enact clear legislation around fees. We consider three policy options and conclude that capping fees on a per-square-foot basis and simultaneously supporting reforms to replace lost revenue would effectively balance the need to increase housing development and preserve localities' revenue.

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Appendix A

Interview Methodology

A total of eight stakeholders interviews were conducted with city staff and developers, including two city managers, two principal planners, three public works engineers, and three developers. We initially reached out over email and phone to city staff of fourteen different cities in California. We were put in contact with three developers over email through the California YIMBY Education Fund. Interviews lasted for thirty minutes to an hour. Interview questions were provided ahead of time upon request.

We wrote four sets of interview questions for the four different sets of stakeholders. Please see below for the specific questions. Interviews were conducted with two members of the research team present on almost all of the interviews with both members taking notes on the interview question document.

All interviews were conducted over Zoom video calls and recorded with the use of Otter.ai. We informed interviewees that the interview would be recorded in the initial email, and reiterated the request and received permission before the Zoom call recording began. We then downloaded the audio recording and transcript of each interview to a hard drive and uploaded to the shared Google drive of the research team.

Each interviewee was informed at the beginning of each interview prior to recording that they would be identified in the report under a vague title such as, “a California City Manager,” a different preferred title, or completely anonymously based on their level of comfort. Additionally, interviewees were informed that if they were to be directly quoted in the report with their name, they would be emailed and asked for permission.

The stakeholders were asked the following questions:

City Manager Interview Questions

1. Tell us about yourself, your role, how long you’ve been with the city, etc.
2. Development Impact Fees:
   a. What types of fees is the city charging on multifamily development?
   b. How do you identify impact fee amounts?
   c. Are there specific projects in the city that have been funded by impact fees?
   d. How much of your city’s budget comes from these types of fees? Does the city rely on these fees?
   e. At what point is the city assessing these fees?
   f. If the city was unable to use impact fees, what ways would you look to make up for the lost revenue?
3. Fiscal Zoning:
   a. When considering types of development, is the city considering local tax outcomes of that development?
   b. Do you generally know what properties lead to fiscal surpluses v fiscal deficits? What are the ones leading to surplus? What are the ones leading to deficits?

4. Challenges:
    a. Why do you think California is in a housing crisis?
5. Incentives:
    a. What do you think the solutions are?
    b. Are there any state or federal incentives the city receives when building housing?

City Planner Interview Questions

1. Tell us about yourself, your role, how long you've been with the city, etc.
2. Fiscal Zoning:
    a. When considering types of development, is the city considering local tax outcomes? What scale are you considering this? Broad development patterns? Or per development basis and land use adjustments?
    b. Are you utilizing Fiscal Impact Analysis tools? Is there a specific tool/model or workbook you are using? What methodologies do you use? (E.g Per Capita Multipliers, Cost of Community Services Case studies etc.)
        i. Do you see any flaws in the FIA results?
    c. Is the result of the analysis the primary decision-making factor? If not, what else is taken into account? Who are the results shared with - staff, the public, or developers?
        i. If so, what types of development do you aim for?
            1. Does the city benefit more from SFH vs MFH?
    d. Do you generally know what properties lead to fiscal surpluses v fiscal deficits? What are the ones leading to surplus? What are the ones leading to deficits? Why? How did you come to these general conclusions? Experience? Education?
3. Fees and Exactions:
    a. Does the city enforce impact fees on developments?
        i. How do you identify fee and exaction amounts?
        ii. What impact fees or exactions are imposed on housing development?
        iii. Where does the tax and fee revenue go when a new building is built?
        iv. Do you think the impact fees affect the speed or scale of development?
4. Challenges:
    a. Why do you think California is in a housing crisis?
    b. What are the biggest challenges the city faces when getting more housing built?
        i. Regulation? Finances? NIMBY Pressure?
    c. What are developers' complaints/hurdles they face at the municipal level?
5. Incentives:
    a. What do you think the solutions are?
    b. What fiscally incentivizes a city's shift to develop more housing? Or are there other kinds of incentives?
    c. Are there any state or federal incentives the city receives when building housing?

Public Works Interview Questions

1. Tell us about yourself, your role, how long you've been with the city, etc.
2. Impact Fees and Exactions:
    a. What types of impact fees does the city enforce on housing development?
        i. How do you identify fee amounts? Nexus studies?
    b. If using nexus studies, how often are you updating the study?
        i. How accurate do you feel the nexus study is to the actual burden on infrastructure, etc.?
    c. Are there certain fees that you have seen grow more significantly than others?
    d. Where does the tax and fee revenue go when a new building is built?
        i. Do you think the impact fees affect the speed or scale of development?
    e. When are these fees being assessed?
3. Challenges:
    a. Why do you think California is in a housing crisis?
4. Incentives:
    a. What do you think the solutions are?

Developers Interview Questions

1. Tell us about yourself, your role, how long you've been with the organization and in the field, etc.
2. Impact/Development Fees:
    a. Begin with a general question - as a developer, do you consider Impact Fees and Development Fees as one in the same?
    b. Is the process to identify the fee amount which you will be assessed transparent?
        i. Is it something you can plan ahead for?
    c. At what point of the development process are you considering a city's development fees? When do these fees need to be paid?
    d. How much of these fees are passed down to the final consumer VS eaten up in the profit? Does this change either the number of units you are building or the type of unit being built? (luxury unit VS affordable)
    e. Do you believe these fees are being used as a tool to stop development?
    f. How much of the burden of these fees do you think falls on developers, and how is this affected by supply and demand or current economic conditions?
    g. Have you seen these fees increase over time?
    h. If fees remain, do you have a preference if they are charged on a per-unit basis or a sq. ft. basis?
    i. How effective would limiting these fees based on the percentage of development cost or sale price be? Would an alternative measurement be more effective?
    j. If a city was unable to use impact fees to pay for necessary infrastructure development, would you have any suggestions on ways they could offset the loss of revenue?

3. Fiscalization:
    a. From your perspective, are cities considering the projected tax revenue from certain types of development? Given their tax revenue goals, are they more willing to approve other developments over multifamily?
4. Challenges:
    a. Why do you think California is in a housing crisis?
    b. What are the biggest challenges you face when building housing?
        i. Regulation? Finances? NIMBY Pressure?
5. Incentives:
    a. What incentives could a city provide to a developer to increase shift multifamily housing development?
    b. What do you think the solutions are?

Appendix B

Data Summary

Three main databases were used for this project. The databases were joined based on city name and year, where applicable. The three databases are: E-5 Population and Housing Estimates for Cities, Counties, and the State, 2007-2023[10], impactfees.com data for select California cities in 2007, 2011, 2015 and 2019,[11] and California State Controller's Office: "Cities by the Numbers" data. [12]

E-5 Population and Housing Estimates for Cities was used to collect information about total housing stock and total multifamily housing stock for cities between 2007-2023. Data manipulation performed on the original dataset included cleaning and combining datasets from 2007 to 2023 in order to create panel data. To account for a different column naming system and different unit size breakdown of housing units between 2007-2009 and 2010-2023, multifamily columns were aggregated for 2010-2023. The final dataset covered the years 2007-2023, with one observation per city per year, plus one observation summing across all unincorporated areas per county per year.

Some important notes on E-5 data include that the City of Eastvale (Riverside County) was incorporated in 2010 and does not appear in the dataset before 2010; the City of Jurupa (Riverside County) was incorporated in 2011 and does not appear in the dataset before 2011. All other cities, and all counties, have entries for each year between 2007-2023.

Impact fee data can be obtained from the "survey" section of the impactfees.com website. Data across four time periods was compiled for the impactfee.com team upon our request. Cover sheets for each survey year include a discussion of survey methodology as well as caveats, mostly related to the fact that the surveys were completed voluntarily. The cover sheets also include the author's qualifications for considering any given fee as a development fee. Further cleaning upon receipt of the compiled dataset included filtering data for entries in California. This joined dataset covers 33 cities in California across four surveyed years: 2007, 2011, 2015, and 2019, for a total of 132 observations.

California State Controller's Office information was used to gather city revenue in 2022 as well as city revenue from development fees, city revenue from sales, and city revenue from property taxes in 2022. Development fees specifically were obtained from sheet #23 in the excel download, titled "23 CI_REV_MISC_REV_GRANDTOT," from the column titled "Development Impact Fees_Total Revenues_Miscellaneous Revenues. There was one observation for each city in California for the year 2022. These data are reported from each locality to the state at the end of the fiscal year.

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10 State of California, Department of Finance, E-5 Population and Housing Estimates for Cities, Counties and the State — January 1, 2007-2023. Sacramento, California, May 2023.

11 Mullen, C. (2019). National impact fee surveys: 2007, 2011, 2015, 2019. Retrieved from https://www.impactfees.com

12 California State Controller's Office. (2022). Cities by the Numbers [Data set]. Retrieved from https://cities.bythenumbers.sco.ca.gov/#!/year/2022/revenue/0/entity_name

Data provided by the State Controller provides a specific reporting category for "Development Impact Fees" as described above. However, some cities appear to be reporting impact fees in other accounting categories that are intermingled with revenue from sources other than impact fees. Our data only reflects those cities separately reporting development impact fees.

Appendix C

List of Jurisdictions Surveyed for Fee and Nexus Study Disclosure

1. Anaheim
2. Auburn
3. Bakersfield
4. Berkeley
5. Bishop
6. Calexico
7. Campbell
8. Clovis
9. Coronado
10. Dana Point
11. Delano
12. El Cajon
13. Eureka
14. Foster City
15. Fresno
16. Hemet
17. Humboldt County
18. Huron
19. La Palma
20. Larkspur
21. Lathrop
22. Livermore
23. Los Gatos
24. Mammoth Lakes
25. Modesto
26. Mono County
27. Montebello
28. National City
29. Newark
30. Newman
31. Oceanside
32. Orange County
33. Oxnard
34. Palm Springs
35. Palmdale
36. Pismo Beach
37. Redding
38. Riverside
39. Sacramento
40.San Bernardino County
41. San Diego
42. San Francisco
43. San Joaquin County
44. San Jose
45. San Juan Capistrano
46.San Luis Obispo County
47. San Mateo County
48. Santa Ana
49. Santa Barbara County
50. Santa Clarita
51. Santa Rosa
52. Solano County
53. Sonoma County
54. South Lake Tahoe
55. South San Francisco
56. Stockton
57. Torrance
58. Turlock
59. Upland
60. Yuba City

Appendix D

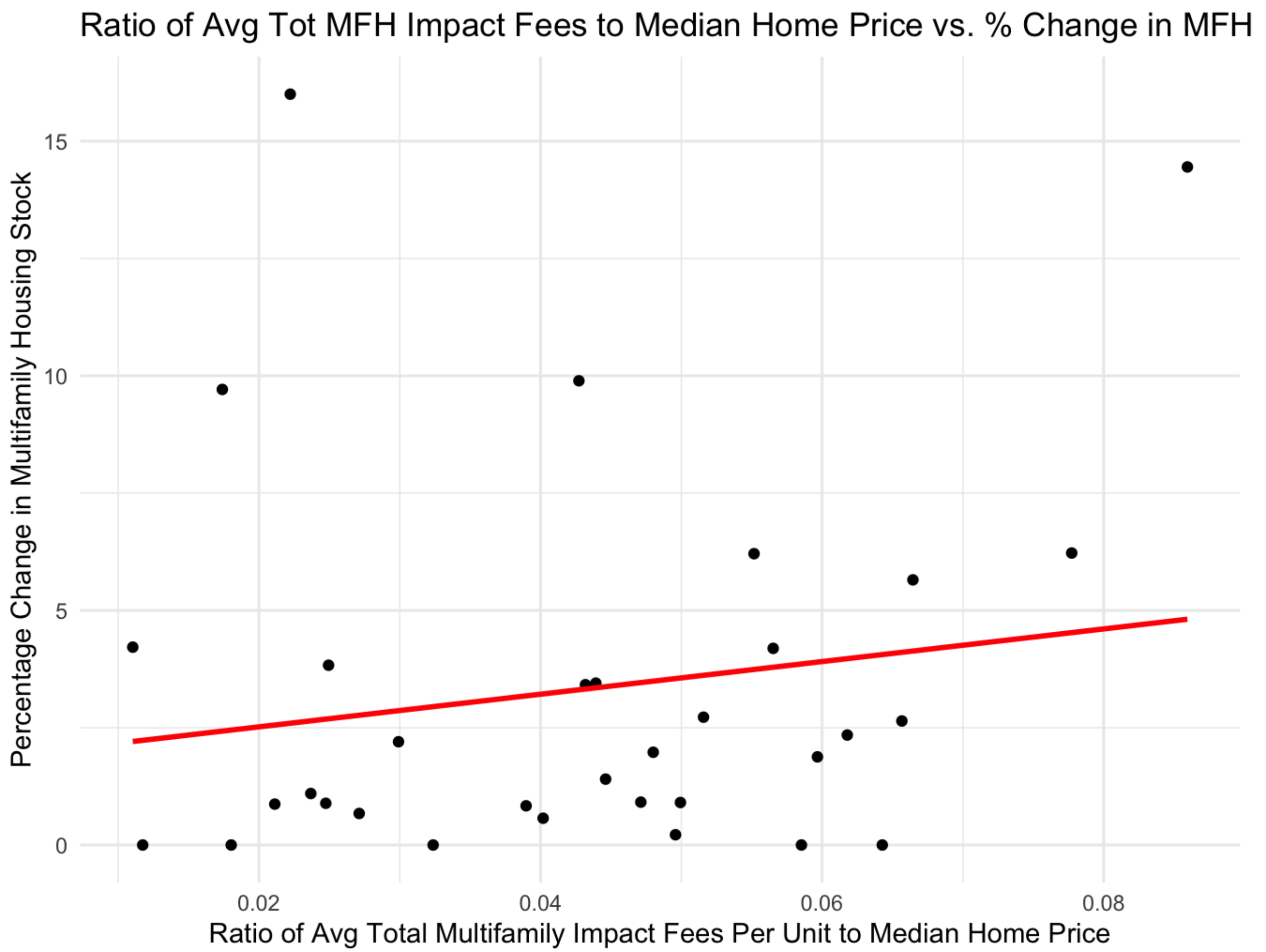
Further Examinations of Relationship Between Impact Fees and Housing Stock

Regression of Percentage Change in Multifamily Home Impact Fees vs. Percentage Change in MFH Stock [2007-2019]:

```
regression_change_mfh_fees_change_mfh_stock_07_19 <- lm(percentage_change_mfh_housing
~ percentage_change, merged_2007_2019)

===============================================================
                 Dependent variable:
              -----------------------------
              % Change Multifamily Housing Stock
-----------------------------------------------
% Change MFH Impact Fees      -0.037
                                (0.028)

Constant                 12.158***
                                (2.419)

-----------------------------------------------
Observations                  33
R2                       0.053
Adjusted R2                   0.023
Residual Std. Error      10.899 (df = 31)
F Statistic              1.742 (df = 1; 31)
===============================================
Note:          *p<0.1; **p<0.05; ***p<0.01
```

Percentage_change
Df: 1
Sum: 206.9
Sq Mean: 206.95
Sq F value: 1.7423
Pr(>F): 0.1965

Scatterplot Of Average Total Multifamily Home Impact Fees / Median Home Price Vs. % Change In Mfh Stock [2015-2019]:



Regression Of Average Total Multifamily Home Impact Fees / Median Home Price Vs. % Change In Mfh Stock [2015-2019]:

```
=============================================================
                     Dependent variable:
                   ---------------------------
                  % Change Multifamily Housing Stock
-------------------------------------------------------------
Average MFH Impact Fees
To Median Home Price               34.788
                                  (37.148)

Constant                           1.822
                                  (1.741)

-------------------------------------------------------------
Observations                        33
R2                              0.028
Adjusted R2                        -0.004
Residual Std. Error                 4.029 (df = 31)
F Statistic                     0.877 (df = 1; 31)
=============================================================
Note:                     *p<0.1; **p<0.05; ***p<0.01
```

An unfinished home by Avel Chukla, used under the [Unsplash](https://unsplash.com) License.