STROOCK

REAL ESTATE

SPECIAL BULLETIN

Housing New York:

A Quick Look at Mandatory Inclusionary Housing Programs (and Legal Issues under Federal Takings Law)

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Background: New York's Inclusionary Housing Program (and How it Might Change)

As Mayor Bill de Blasio highlighted in his recent State of the City Address, New York City is poised to launch a mandatory inclusionary housing program. It appears likely that under the mandatory program, the City would rezone certain manufacturing districts – such as those along Atlantic Avenue in East New York, Brooklyn – allowing developers to build residential buildings if they provide affordable housing through the inclusionary housing program.[1]

Under New York's existing voluntary program, a developer may either build an entirely market-rate residential building or may build a slightly larger building if the developer also provides affordable housing through the inclusionary housing program. Unlike in the existing voluntary program, Mayor de Blasio's likely proposal would prohibit developers from building residential buildings in these districts if they did not provide affordable housing.

This Stroock Real Estate Special Bulletin reviews the provisions of inclusionary housing programs in other cities and analyzes some of the issues that are raised by mandatory inclusionary housing in the context of federal takings law.

Inclusionary Housing Programs in Other Cities

In voluntary inclusionary housing programs, private developers build affordable housing in return for cost offsets, such as floor area bonuses and tax incentives.

[1] East New York Community Plan – Zoning Proposal, NEW YORK CITY DEPARTMENT OF CITY PLANNING, http://www.nyc.gov/html/dcp/pdf/east_new_york/zoning_proposal_presentation.pdf (last visited Feb. 8, 2015).

Inclusionary housing programs exist in more than 400 cities and towns nationwide, and many of these programs are mandatory.[2] In San Francisco, for example, the mandatory inclusionary housing program applies to all new residential buildings containing 10 or more units.[3] To comply, developers must either (1) pay a fee based on the number of total units, (2) designate 12% of the on-site units as affordable, or (3) provide 20% of the total units built as off-site affordable housing within a mile of the new development.[4] Similarly, in Cambridge, Massachusetts, all new residential buildings containing 10 or more units or more than 10,000 square feet of residential area must provide affordable housing of at least 15% of the base units in the building.[5]

Mandatory Inclusionary Housing Programs and the Law of "Takings"

Among the potential legal issues raised by mandatory inclusionary housing programs are whether they constitute unconstitutional "takings" by the government. Under the United States and New York State Constitutions, the government may not take private property for public use without paying the property owner just compensation.[6] Takings may be of two types: (1) physical takings and (2) regulatory takings. Land use regulation, including exactions like inclusionary housing, may be unconstitutional if it amounts to a taking.

Physical Takings

In a permissible physical taking, the government takes private property for public use, paying the owner just compensation. For example, the government may use eminent domain to take a privately owned building in order to devote the land to public use, such as a park, so long as the government pays the property owner just compensation. The physical occupation need not be by the government itself, but may also be a third party under government authority.[7] A physical taking may also occur where a government regulation forces the existence of a landlord-tenant relationship.[8]

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[2] ROBERT HICKEY, AFTER THE DOWNTURN: NEW CHALLENGES AND OPPORTUNITIES FOR INCLUSIONARY HOUSING 2 (National Housing Conference, Center for Housing Policy, Feb. 2013), available at www.nhc.org/media/files/InclusionaryReport201302.pdf (last visited Feb. 8, 2015).

[3] Inclusionary Housing Program, CITY & COUNTY OF SAN FRANCISCO, MAYOR'S OFFICE OF HOUSING AND COMMUNITY DEVELOPMENT, http://sf-moh.org/index.aspx?page=263 (last visited Feb. 8, 2015).

[4] *Id.*; San Francisco, Cal., Planning Code, §§ 415.1 - 415.11 (2013).

[5] Inclusionary Housing Program for Developers, CITY OF CAMBRIDGE, MASSACHUSETTS, COMMUNITY DEVELOPMENT DEPARTMENT, www.cambridgema.gov/CDD/housing/fordevelopersandpropmanagers/inclusionarydevelopers.aspx (last visited Feb. 8, 2015).

[6] U.S. CONST. amend. V ("[N]or shall private property be taken for public use, without just compensation…"); N.Y. CONST. art. 1, § 7 ("Private property shall not be taken for public use without just compensation.").

[7] *Seawall Assoc. v. City of N.Y.*, 74 N.Y.2d 92, 103 (1989) ("Moreover, to constitute a physical taking, the occupation need not be by the government itself, but may be by third parties under its authority[.]") (internal citations omitted)).

[8] *See id.* at 106 (finding municipal law to constitute physical taking because it "compels owners to be residential landlords; it requires owners to rehabilitate and offer their properties for rent, as SRO units, to persons with whom they have no existing landlord-tenant relationship."); *see also Manocherian v. Lenox Hill Hosp.*, 84 N.Y.2d 385 (1994) (finding local ordinance a physical taking where an apartment building was forced to rent space to hospital employees rather than remain vacant).

Regulatory Takings

Although zoning and other forms of land use regulation may reduce the value of real estate, government regulation of private property is not a taking unless the regulation is "so onerous that its effect is tantamount to a direct appropriation or ouster."[9] A regulatory taking indeed occurs where the regulation has the effect of depriving a landowner of all economically viable use of the land.[10] This notion of "total takings" typically requires the landowner to be unable to realize any profit from the land.[11]

In the alternative, if the landowner is only deprived of some economic use of the property, a regulatory taking may still occur if the regulation goes "too far." To determine whether a particular regulation goes "too far" requires a fact-based inquiry into (1) the economic impact on the landowner; (2) "the extent to which the regulation has interfered with distinct investment-backed expectations"; and (3) "the character" of the regulation.[12] Although the character of the regulation is only one factor, in New York, affordable housing has been deemed a legitimate government interest and courts have viewed rent regulations favorably.[13] Therefore, in an examination of a regulatory taking, the fact-based inquiry will turn on the relationship between the regulation and the landowner.

Exactions

Exactions are a form of land use regulation where "developers [must] provide, or pay for, some public facility or other amenity as a condition for receiving permission for a land use that the local government could otherwise prohibit."[14] In theory, exactions exist to internalize the negative externalities caused by a development – *i.e.*, to offset the increased burdens on public services that the development imposes. For example, a

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[9] *Consumers Union of U.S., Inc. v. State*, 5 N.Y.3d 327, 357 (2005) (quoting *Lingle v. Chevron U.S.A., Inc.*, 544 U.S. 528, 537 (2005)).

[10] *Seawall Assoc.*, 74 N.Y.2d at 107 ("[A] burden-shifting regulation of the use of private property will, without more, constitute a taking: (1) if it denies an owner economically viable use of his property, or (2) if it does not substantially advance legitimate State interests.").

[11] *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1019 (1992) ("When the owner of real property has been called upon to sacrifice all economically beneficial uses in the name of the common good, that is, to leave his property economically idle, he has suffered a taking."); *Park Ave. Tower Assoc's v. City of New York*, 746 F.2d 135, 139-40 (2d Cir.1984) (defining the standard "as whether the owner was precluded from realizing any profit whatsoever." (internal citations and quotations omitted)); *see also Sadowsky v. City of New York*, 732 F.2d 312, 317–18 & n. 3 (2d Cir. 1984) (finding that "unmarketability" is equated with no economically viable use); *Dean Tarry Corp. v. Friedlander,* 650 F.Supp. 1544, 1550 (S.D.N.Y. 1987) ("[L]andowner must demonstrate that he has been deprived of all reasonable uses of his land…."), *aff'd* 826 F.2d 210 (2d Cir.1987).

[12] *Lingle*, 544 U.S. at 538-39 (citing *Penn Cent. Transp. Co v. City of New York*, 438 U.S. 104, 124 (1978)).

[13] *Rent Stabilization Ass'n of N.Y.C. v. Higgins*, 83 N.Y.2d 156, 174 (1993) ("The question before us, however, is not the general wisdom or desirability of present rent regulation…to address the State's housing situation—that is a question for the legislature."); *Israel v. City Rent and Rehab. Admin. of City of N.Y.*, 285 F.Supp. 908 (S.D.N.Y. 1968) (holding that New York rent control statutes do not violate due process or equal protection and do not constitute taking of property without compensation or impairment of contract rights).

[14] Vicki Been, *"Exit" as a Constraint on Land Use Exactions: Rethinking the Unconstitutional Conditions Doctrine*, 91 COLUM. L. REV. 473, 474-83 (1991), *quoted in* ROBERT C. ELLICKSON & VICKI L. BEEN, LAND USE CONTROLS: CASES AND MATERIALS 635 (6th ed. 2005).

developer may be required to build public space in return for receiving permission to build a residential building along the Brooklyn waterfront. Similarly, mandatory inclusionary housing can be considered a form of an exaction because the developer must provide the public amenity of affordable housing as a condition to receiving permission to build a residential building.

An exaction will not be deemed to be a taking, and therefore will be permissible as a form of land use regulation, if (1) an essential nexus exists between the costs imposed by the development on the public and the costs imposed by the exaction on the developer and (2) the costs imposed by the exaction are roughly proportional to the costs imposed on the public. An essential nexus exists where the exaction "further[s] the end advanced as the justification" for the regulation.[15] An exaction is roughly proportional if there is "some sort of individualized determination that the required dedication is related both in nature and extent to the impact of the proposed development."[16] This individualized determination does not require a "precise mathematical calculation."[17]

For example, the required open space along the Brooklyn waterfront may fulfill the essential nexus requirement because new developments may generate more demand for open space, and the required open space may offset that demand. In addition, the City can make an individualized determination that the amount of open space required is roughly proportional to the increased demand generated by the development.

[15] *Nollan v. Cal. Coastal Comm'n*, 483 U.S. 825, 837 (1987).
[16] *Dolan v. City of Tigard*, 512 U.S. 374, 391 (1994).
[17] *Id.*

Mandatory Inclusionary Housing Programs

In the context of mandatory inclusionary housing, one could argue that redevelopment increases property values, thereby displacing lower-income residents and increasing the demand for affordable housing. An essential nexus between development and mandatory inclusionary housing could exist because mandatory inclusionary housing advances the legitimate government interest of meeting the increased demand for affordable housing that the development creates.

In addition, a rough proportionality analysis may find that mandatory inclusionary housing places no economic burden on the developer because a manufacturing-to-residential rezoning would likely increase property values substantially, and the amount of that increase would likely be greater than the cost to the developer of providing affordable housing.

Conclusion

If mandatory inclusionary housing is ever subjected to a constitutional exactions analysis, the City may have to demonstrate that (1) an essential nexus exists between the burden imposed on the public by new housing and the burden imposed on the developer by the mandatory inclusionary component, and (2) the required inclusionary component is roughly proportional to this burden. Stroock & Stroock & Lavan LLP will continue to watch this issue as it develops.

Although this **Stroock Real Estate Practice Group Special Bulletin** highlights some of the key issues regarding mandatory inclusionary housing programs, it is not intended as an exhaustive analysis of all of potential issues and you are encouraged to consult an expert. We will

continue to provide updates regarding significant developments.

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