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Commercial Development and COAH A Bad Mix?

Affordable housing is not just the residential builder's obligation

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The Council on Affordable Housing (COAH), created to administer New Jersey's innovative affordable housing program resulting from the *Mount Laurel* doctrine (*Southern Burlington County NAACP v. Twp of Mount Laurel*, 92 NJ 158 (1983)), has faced numerous challenges since it was established by the Fair Housing Act (N.J.S.A. § 52:27 D-301 et seq.). In an effort to stem criticism from municipalities that its previous rules fostered inappropriate growth, COAH proposed new rules in December 2004. What are called "the third-round rules" are based on a concept called "growth share," in which COAH no longer tells a town what its affordable housing obligation is, but rather, provides every municipality the opportunity to plan for affordable housing. Under these "third-round" rules, growth that takes place in a town creates an affordable housing obligation in a ratio set forth by these rules. For

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example, eight market-rate houses creates the obligation for one affordable housing unit.

The state's housing developers have become used to the affordable housing issue, and while the New Jersey Builder's Association did sue COAH for the third-round rules, it was because the builders thought the new rules would create an incentive for towns to downzone, eliminating both market-rate and affordable housing. Under the builder's reasoning, if towns could regulate their growth so as to avoid an affordable housing obligation, there would be fewer opportunities to build market-rate housing. If "down-zoning" became the norm, affordable housing would become an illusion.

The state's commercial and industrial developers, largely immune to the *Mount Laurel* obligation (other than financial contributors) before the third-round rules, had not thought that affordable housing would impact them. Most commercial developers were largely unaware of the concept of growth share and paid little attention to COAH or the affordable housing regulations. However, COAH, in an effort to treat

all sources of growth equitably, incorporated industrial and commercial development in the third-round rules. For every 25 jobs created, the towns had to come up with one affordable housing unit — an obligation that has created some significant problems for the commercial developers.

Imagine, for example, that you are a developer of office buildings. Despite the fact that New Jersey has had a formidable vacancy rate for Class A office buildings, you have been able to get a commitment from a Fortune 100 client for a 300,000 square foot office building. You've penciled out the pro-forma, and have had discussions with the town, which is eager to get a new tax ratable. However, in your last meeting with the mayor, he has told you that there is now an affordable housing issue. The town planner says that under COAH rules, for every 1,000 square feet of development, there is anticipated to be one worker; so for your project, the town will anticipate that there will be 300 workers; and since each 25 workers generate one housing unit of affordable housing, you now are creating a 12-unit affordable housing obligation. From the town's perspective, this is your problem, not theirs, and you will be expected to provide the housing. Your first question, after learning that the town expected you to deal with this obligation, is "How much will this cost?" And the answer, as you will find, can be "Plenty!"

What started out as an effort to make

the process equitable and fair to both residential and commercial developers has now turned out to be a lot more problematic, and has impelled NAIOP, the trade organization representing the state's leading office and industrial developers, to file an amicus brief in the current lawsuit challenging the third-round rules. The reasons why the commercial developers have challenged these rules provides a cautionary tale for both lawyers and policy makers.

As it turns out, in its eagerness to encourage municipal compliance with the third-round rules, COAH left an enormous amount of discretion to the towns. Each town must calculate its own growth prospects and is free to do planning and zoning as it sees fit. If a town wants to be in compliance with COAH, it must project what its total job creation and housing growth will be by the year 2014, and file a plan to meet the affordable housing need created by the growth. For example, assume that a town figures it will add another 480 housing units between 2004 and 2014. That creates an affordable housing requirement of 60 housing units. Assume that the town plans to add enough retail, commercial and industrial projects to add 1,000 jobs to the town's economic base. That creates a need for 40 housing units. Somehow, the town has to come up with 100 additional housing units by 2014.

COAH rules permit towns to "export" 50 percent of their new construction obligation to other municipalities, as has been the case since the enactment of the Fair Housing Act. Those "exported" units, under COAH rules, will cost at least \$35,000; which means that those 50 units will cost \$1.75 million. The remaining 50 units will have to be built in town. While the typical mechanism under the earlier rules was to have the residential builders provide the housing, under the new rules the municipalities are free to impose the obligation on the commercial/industrial developers. Thus, it is conceivable that a project with 300,000 square feet of office space will have its approval to build conditioned on the developer providing 12 affordable housing units on site. If you are an office/industrial developer, you may not welcome the

opportunity to learn how to build affordable housing and integrate it into your site plans.

Moreover, COAH's concern is with municipal compliance, not necessarily equity of impact on various segments of the economy. In its publication, Third Round Quick Facts (www.state.nj.us/dca/coah), COAH suggests that if the town has experienced growth since 2004 (when the obligation was to be calculated) and has not created a mechanism to capture affordable housing contributions, the town is free to require more affordable housing from future developers. Since there is no linkage between planning, zoning and COAH compliance, it is possible for a town to simply require a developer to contribute affordable housing, in excess of the suggested rate, without creating more value for the developer. So a developer who has escaped the requirement to contribute enjoys an economic advantage that another developer does not. Does an "equal protection" issue arise? Quite likely.

The inequities can become quite significant. The rules permit, but do not require, a town to negotiate options with the developers. The town can exempt some districts from having any affordable housing, can mandate that the housing be located on specific tracts, can permit developers to pay money "in lieu" of constructing the affordable housing, or can tell a developer that option is not available and that the developer, like it or not, must construct affordable housing on his site if he wants to build the office building, shopping mall, movie theatre or warehouse for which he has a customer.

The third-round rules are largely standardless. NAIOP sees the potential for mischief as municipalities allocate the affordable housing obligation, and in particular, NAIOP is concerned about the "in lieu" fee process. So far, a number of municipalities have adopted these "in lieu" fee ordinances, and the numbers are widely variable. In Town A, the planners have computed the cost of land, building and administration for affordable housing and have concluded that that an affordable housing unit will cost the developer \$200,000 each. In Town B, the equivalent number is \$450,000. Because the rules have

no standards, there is no theoretical upward limit. So if you are the developer of that 300,000 square foot project, your 12 units could cost you either what it would cost you to build them on site and integrate them into your project, or the in-lieu fee, which could be \$5.4 million if you were building in town "B" or "only" \$2.4 million if you were in town "A."

NAIOP objects to the potential abuse, the lack of standards and the poor planning it believes these rules will engender, and makes the point that unlike the early rules, there is neither choice available for a developer nor a calculation of the economic impact on the developer. NAIOP argues that under the earlier rules, the affordable housing fees, while significant, were not "deal breakers," while under the third-round rules, the possibility of mandated inclusionary housing without any concomitant benefits may well make the project impossible.

NAIOP's challenge to the rules is important, not just to the office/industrial park developers, but also to those who are shaping development policy for the state as well as to the legal community. If NAIOP is right and the imposition of an expensive affordable housing obligation on office/commercial developers may mean that specific projects may not be built in New Jersey — after all, the New York-New Jersey-Pennsylvania market is highly competitive — Governor Corzine's hope to cure our current fiscal problems by economic growth is at risk.

For lawyers, affordable housing obligations have to become far more salient. If a developer is aware of the obligation before he purchases property, he can make the sale contingent on the seller taking care of the obligation; if the seller is aware of the implications of the obligation, he can work with the town officials to assure that the obligation is fair and bearable. It's now part of the lawyer's obligation to advise clients that affordable housing is not just the residential builder's obligation, but could be part of any development project in New Jersey. ■