

Date of Hearing: April 17, 2024

ASSEMBLY COMMITTEE ON LOCAL GOVERNMENT

Juan Carrillo, Chair

AB 2909 (Santiago) – As Introduced February 15, 2024

SUBJECT: Historical property contracts: qualified historical property: adaptive reuse

SUMMARY: Allows adaptive reuse properties that are at least 30 years old on or after January 1, 2026 to make use of the Mills Act until January 1, 2036. Specifically, **this bill:**

- 1) Adds, until January 1, 2036, properties that meet all of the following to the definition of “qualified historic properties” in the Mills Act:
 - a) The privately owned property is not exempt from property tax.
 - b) The property is on an infill site that satisfies the site requirements of AB 2011(Wicks), Chapter 647, Statutes of 2023.
 - c) The property was constructed at least 30 years prior to the property owner and legislative body entering in to a contract, under this bill.
 - d) The legislative body and property owner entered into a contract between January 1, 2026 and January 1, 2036.
- 2) Specifies that a contract entered into to restrict the use of qualified historical property described in 1) above, shall require adaptive reuse, as defined, of the qualified historical property. This provision shall become operative on January 1, 2026, and shall remain effect only until January 1, 2036, and as of that date is repealed.
- 3) Updates a reference to federal law relating to the National Register of Historic Places.

EXISTING LAW:

- 1) Allows, pursuant to AB 2011(Wicks), Chapter 647, Statutes of 2023, a housing development project to be subject to a streamlined, ministerial approval process if it located on a site that satisfies all of the following:
 - a) The project is located in a zone where office, retail, or parking are a principally permitted use.
 - b) It a legal parcel that is within a city or an unincorporated area within an urbanized area or urban cluster.
 - c) At least 75% of the perimeter adjoins parcels with urban uses.
 - d) It is not a site where more than one third of the square footage is dedicated to industrial use, as specified.
 - e) The parcel is not located on prime farmland, wetlands, very high fire hazard severity zones, a hazardous waste site, an earthquake fault zone, a special flood hazard area,

floodway, land for conservation, habitat for protect species, or lands under conservation easement.

- f) The site is not an existing parcel of land or site that is under the Mobile Home Residency Law, Recreation Vehicle Park Occupancy Law, Mobilehome Parks Act, or Special Occupancy Parks Act.
- g) For sites that are within a neighborhood plan, the site must meet the following:
 - i) As of January 1, 2022, there was a neighborhood plan applicable to the site that permitted multifamily housing development on the site.
 - ii) As of January 1, 2024, there was a neighborhood plan applicable to the site that permitted multifamily housing development on the site and all of the following occurred:
 - 1. A notice of preparation for the neighborhood plan was issued before January 1, 2022, as specified.
 - 2. The neighborhood plan was adopted on or after January 1, 2022, and before January 1, 2024.
 - 3. The environmental review for the neighborhood plan was completed before January 1, 2024.
- h) For vacant sites, the site meets both of the following:
 - i) The site does not contain tribal cultural resources, as specified.
 - ii) It is not within a very high fire hazard severity zone, as specified. (GOV § 65912.111)
- 2) Allows, pursuant to the Mills Act, a city, county, or city and county to contract with the owner or the agent of the owner of the qualified historical property to restrict the use of a qualified historical property, as specified. (GOV § 50280)
- 3) Defines “qualified historical property” to mean a privately owned property which is not exempt from property taxation which is listed in the National Register of Historic Places, or is located in a registered historic district, as defined, or is listed in any state, city, county, or city and county official register of historical or architecturally significant sites, places, or landmarks. (GOV § 50280.1)
- 4) Requires any contract entered into under the Mills Act to restrict the use of a qualified historical property to contain all the following:
 - a) The term of the contract shall be for a minimum period of 10 years.
 - b) Where applicable, the contract shall provide the following:
 - i) For the preservation of the qualified historical property and, when necessary, to restore and rehabilitate the property to conform to the rules and regulations Office of Historic

Preservation of the Department of Parks and Recreation, the United States Secretary of the Interior's Standards for Rehabilitation, and the State Historical Building Code.

- ii) For an inspection of the interior and exterior of the premises by the city, county, or city and county prior to a new agreement, and every five years thereafter, to determine the owner's compliance with the contract.
 - iii) For it to be binding upon, and inure to the benefit of, all successors in interest of the owner. A successor in interest shall have the same rights and obligations under the contract as the original owner who entered into the contract. (GOV § 50281)
- 5) Specifies that each contract shall provide that on the anniversary date of the contract, or other annual date specified in the contract, a year shall be automatically added to the initial term of the contract unless notice of nonrenewal is given. If the property owner or the legislative body desires in any year not to renew the contract, that party shall serve written notice of nonrenewal of the contract on the other party before the annual renewal date of the contract. Unless the notice of nonrenewal is served by the owner 90 days prior or the legislative body at least 60 days prior to the renewal date, one year shall automatically be added to the term of the contract. (GOV § 50282)
- 6) If the legislative body or the owner serves notice of intent in any year not to renew the contract, the existing contract shall remain in effect for the balance of the period remaining since the original execution or the last renewal of the contract. (GOV § 50282)
- 7) Defines "adaptive reuse" to mean the repurposing of building structures for residential purposes, such as former office use, commercial use, or business parks. When referring to building structures, adaptive reuse means retrofitting and repurposing of existing buildings that create new residential rental units, and expressly excludes a project that involves rehabilitation of any construction affecting existing residential units that are, or have been, recently occupied. [Health and Safety Code (HSC) §53559.1]
- 8) Provides that when a county assessor is valuing an enforceably restricted historical property, the county assessor shall not consider sales data on similar property, whether or not enforceably restricted, and shall value historical property by the capitalization of income method, as defined. [Revenue and Taxation Code (RTC) § 439.2]
- 9) Defines how a county assessor will value that restricted historical property when a city, a county, or the owner of a restricted historical property subject to a contract has served a notice of nonrenewal. (RTC § 439.3)

FISCAL EFFECT: This bill is keyed fiscal.

COMMENTS:

- 1) **Bill Summary and Author's Statement.** This bill allows adaptive reuse projects to use property tax benefits provided by the Mills Act if the property was constructed at least 30 years from the date the owner of the property and the legislative body of a city, county, or city and county enter into a contract restricting the use of the property. The property must be located on a site that meets the requirement of AB 2011 (Wicks), Chapter 647, Statutes of 2023. The Central City Association of Los Angeles is the sponsor of this bill.

According to the Author, "Shifts in current and projected office demand have led to declining commercial office building valuations, which threaten local governments' budgets that rely heavily on property taxes on commercial real estate to provide public goods and services. Adaptive reuse of underutilized commercial buildings has the potential to provide quality, infill residential units, offering a potential solution to meeting both housing supply and environmental sustainability goals. AB 2909 will empower local governments to make adaptive reuse a viable tool for tackling our housing crisis while sparking economic recovery for downtowns."

- 2) **The Mills Act.** Enacted in 1972, the Mills Act is a state enabled, but locally administered, historic preservation incentive that results in the reduction of property taxes for qualified historical properties under a Mills Act contract. A qualified historical property includes properties that are: listed in the National Register of Historic Places, designated as a historic property by the state of California; is located in a historic district; or listed in a city or county's official register of historical or architecturally significant sites, places, or landmarks. Under the Mills Act, a city or county enters into a contract with a property owner of a qualified historical property and provides the owner with a property tax benefit. In exchange for the property tax benefit, the owner of the property commits to restoring, rehabilitating, and maintaining the property, as specified in the contract.

The initial Mills Act contract term is for a minimum of ten years, with an additional year added to the contract annually on the anniversary date. The contract remains in effect in perpetuity until either party provides notice to stop renewing the agreement.

Under the Mills Act, the city or county will use the capitalization of income method to assess the property tax. For properties that are rented, the income of the property is based off of the actual rental income or the fair market rent of similar properties with similar uses in the same area, not including allowed expenditures or expenses. When there is not enough rental information, the income is based off of what the property is expected to yield under prudent management and subject to the restrictions imposed by its contract with the city or county. Comparable rental data may be obtained from county assessor offices or, in some cases, real estate broker and rental agencies.

Cities and counties are the sole administrators of the Mills Act. Although the definition of qualified historical properties includes properties identified in state and national registers, local governments have the discretion to choose to adopt a program that limits Mills Act contracts to properties that are locally designated.

- 3) **California's Housing Crisis.** California faces a severe housing shortage. A variety of factors have contributed to the lack of housing production. The Statewide Housing Plan

adopted by the Department of Housing and Community Development in 2022 found California needs approximately 2.5 million units of housing, including one million units affordable to lower income households, to address this mismatch over the next eight years. That would require production of over 300,000 units a year, including over 120,000 units a year of housing affordable to lower income households. However, production in the past decade has lagged at under 100,000 units per year – including less than 10,000 units of affordable housing per year.

- 4) **Adaptive Reuse Projects.** Adaptive reuse projects convert office, commercial, and business properties to residential units. By converting underutilized commercial and office buildings in urban centers, critical housing units are positioned in high-resource areas close to job centers and transit services. The City of Los Angeles (City) has boasted the success of its adaptive reuse program which has brought 12,000 units to Downtown Los Angeles since its adoption in 1999. When initially adopted, the City’s adaptive reuse program targeted buildings constructed prior to 1974 as part of an effort to revitalize the City’s Downtown. As part of its updated Housing Element, Los Angeles proposed to expand its Adaptive Reuse Ordinance to allow for a faster approval process and has expanded eligibility to structures that are at least 15 years old across the entire city. This effort is part of six core strategies to provide more affordable housing near jobs and transit.

Project Homekey is another example of a prominent adaptive reuse program. As a response to the COVID-19 pandemic, Project Homekey converted hotels and motels into housing for Californians experiencing homelessness. These uses are already divided into quarters designed for short-term human habitation and can readily be converted to housing with the addition of kitchens. As of February, 2024, the Legislative Analyst’s Office reported that Project Homekey has created 15,319 units of housing with an expenditure of \$3.35 billion. The cost of converting a unit under Project Homekey, at \$218,683 per unit, is substantially less than the current cost of constructing a new multifamily unit which averages at a little under \$600,000 a unit as calculated by a recent report from the UC Berkeley’s Turner Center for Housing Innovation, *Making it Pencil: the Math of Housing Development-2023*. This report found that for a multifamily mixed use project with five stories of residential and a nonresidential ground floor, the average cost per unit in the Bay Area is \$637,000 in the East Bay and \$623,000 in the South Bay, \$594,000 in Los Angeles, and \$508,000 in Sacramento.

The success of an adaptive reuse project is highly dependent on the type of building and its initial use. The cost of converting a hotel or motel, which is already used for short-term human habitation, will be significantly less than converting an office building or big box retail, which would very likely need to be completely reconstituted to provide the necessary plumbing and meet light and air quality standards for residential units. These types of projects run the risk of being more expensive than new construction, especially when unexpected expenses are taken into account.

Older buildings, particularly those built prior to the 1980’s, are more likely to require more intensive upgrades to align with modern public health and safety standards, seismic retrofitting, fire safety, or environmental remediation. In November 2021, the Turner Center reported that commercial conversions are relatively rare and are more likely to entail demolition and new construction than the adaptive reuse of any existing structure. Over five years (2014-2019), less than one percent of all commercial zoned parcels were converted to

residential use across California’s four metro regions (*Adaptive Reuse Challenges and Opportunities in California*).

- 5) **Updated Housing Element and the Regional Housing Needs Assessment.** One important tool in addressing the state's housing crisis is to ensure that all of the state's cities and counties appropriately plan for new housing. Such planning is required through the housing element of each community's General Plan, which outlines a long-term plan for meeting the community's existing and projected housing needs. Cities and counties are required to update their housing elements every eight years in most of the high population parts of the state, and five years in areas with smaller populations

Most jurisdictions across the state are entering, or have entered, the sixth regional housing needs assessment (RHNA) cycle. To ease the Department of Housing and Community Development’s (HCD) workload, regions have staggered start dates for RHNA cycles. For example, the sixth cycle for the Southern California Association of Governments (SCAG), the Sacramento Area Council of Governments (SACOG), and the San Diego Association of Governments (SANDAG) is 2021-2029, while the San Luis Obispo Council of Governments’ (SLOCOG) sixth cycle is 2020-2028 and the Association of Bay Area Governments’ (ABAG) sixth cycle is 2023-2031. Due to the combination of recent RHNA reforms and the fact most areas of the state are suffering from a severe shortage of housing due to decades of underbuilding, most regions are receiving a sixth cycle RHNA allocation that is vastly larger than their fifth cycle allocation.

Data from the 5th RHNA cycle shows that many key cities and counties have been under-producing units that are affordable to lower and moderate incomes. At the same time, these cities has gone above and beyond their allocation of above moderate income housing. The charts below show the needs of the 6th RHNA cycle and the number of units built under the 5th cycle compared to the identified need in the 5th cycle.

6th Cycle Regional Housing Needs Assessment

	<i>Los Angeles (2021-2029)</i>	<i>Sacramento (2021-2029)</i>	<i>San Diego (2021-2029)</i>	<i>San Francisco (2023-2031)</i>
Extremely Low (<30% AMI)	-	-	12,380 units	-
Very Low (< 50% AMI)	115,978 units	10,436 units	15,169 units	20,867
Low (51%-80% AMI)	67,873 units	6,306 units	17,311 units	12,014
Moderate (80%-120% AMI)	75,091 units	8,545 units	19,319 units	13,717
Above Moderate (>120% AMI)	196,831 units	20,266	43,837 units	35,471
Total	456,643 units	45,580 units	108,036 units	82,069 units

5th Cycle Regional Housing Needs Assessment

Income Level	<i>Los Angeles (2013-2021)</i>	<i>Sacramento (2013-2021)</i>	<i>San Diego* (2013-2021)</i>	<i>San Francisco (2015-2023)</i>
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Needed-Very Low	20,426 units	4,944 units	10,989 units	6,234 units
Built-Very Low	7,012 units (34%)	255 units (5%)	-	2,688 units (43%)
Needed-Low	12,435 units	3,467 units	16,703 units	4,639 units
Built-Low	3,727 units (30%)	486 units (14%)	-	2,500 units (54%)
Needed-Moderate	13,728 units	4,482 units	15,462 units	5,460 units
Built-Moderate	827 units (6%)	5,808 units (129%)	-	2,847 units (52%)
Needed-Above Moderate	35,412 units	11,208 units	33,954 units	12,536 units
Built-Above Moderate	105,522 units (298%)	11,692 units (104%)	-	18,826 units (151%)

*San Diego reported in its 6th Cycle Housing Element that the City had only constructed 42,275 units of the 88,000 schedule of which a majority were affordable to households with incomes more than 120% AMI.

6) **Policy Considerations.** The Committee may wish to consider the following:

- a) **RHNA Allocations and Affordability Requirements.** AB 2909 authorizes a city or county to provide property tax benefits under the Mills Act to adaptive reuse projects that convert buildings that are at least 30 years old into housing or mixed-used development. The bill targets infill projects in urban centers. As highlighted in the Turner Center Report, *Adaptive Reuse Challenges in California*, the cost of converting nonresidential units to residential varies highly on the type of building and its original use. In order to make these types of projects profitable, the cost per unit may be out of reach for lower and moderate income Californians. Considering that major cities in California have not met their lower and moderate income housing allocations while exceeding above-moderate income housing allocation, the Committee may wish to consider if a percentage of the residential units should be affordable for properties seeking to use the Mills Act under this bill.
- b) **Commercial vs. Residential.** Adaptive reuse projects can be mixed-use developments. AB 2909 does not require that a percentage of the square footage be dedicated to residential uses or prescribe a minimum number of units to be built. The Committee may wish to consider if a minimum percentage of the total square footage be dedicated to residential uses for properties seeking to use the Mills Act under this bill.
- c) **Technical Considerations.** Lastly, if the bill was signed into law, the bill allows local governments to enter into a contract beginning January 1, 2025, even though only contracts entered into after January 1, 2026 are deemed valid. The Committee may wish to consider if adding a sunrise date of January 1, 2026 will create consistency and provide clarity on how the bill will be implemented.

- 7) **Committee Amendments.** In order to address the policy consideration outlined above, the committee may wish to amend the bill as follows:
- a) Limit the bill to the City of Los Angeles.
 - b) Require that, at minimum, 80% of the project's square footage is dedicated to residential uses.
 - c) Require that any adaptive reuse project converting hotels, motels, short-term rental buildings, or other structures previously used for human habitation into housing must include the affordability levels prescribed in AB 2011.
 - d) Require projects to provide open-space for recreation, community centers, or daycare for the community to use.
 - e) Require each project to include a minimum of 3 artist lofts.
 - f) Require the developer to work with the City to provide and accommodate for active-transportation infrastructure.

Due to timing constraints, these amendments should be adopted in the Housing and Community Development Committee.

8) **Related Legislation.**

AB 2910 (Santiago) authorizes cities and counties to adopt alternative building regulation for the conversion of commercial and industrial buildings to residential uses. This bill is currently in the Assembly Committee on Housing and Community Development.

AB 3068 (Haney) deems an adaptive reuse project a use by right in all zones, regardless of the zoning of the site, and subject to a streamlined ministerial review process if the project meets specified requirements. This bill is currently in Assembly Committee on Housing and Community Development.

9) **Previous Legislation.**

AB 529 (Gabriel), Chapter 743, Statutes of 2023, required the Department of Housing and Community Development (HCD) to convene a working group to identify challenges to and opportunities to promote adaptive reuse residential projects. The bill requires HCD and other state agencies in the working group to propose adaptive reuse building standards for adoption by the Building Standards Commission.

AB 1490 (Lee), Chapter 764, Statutes of 2023, required local governments to approve adaptive reuse projects where 100% of the units are affordable to lower income households and at least half of the units were dedicated to very-low income households.

AB 2592 (McCarty), Chapter 439, Statutes of 2022 required the Department of General Services (DGS) to report to the Legislature a plan to transition underutilized multistory state building to affordable housing and adaptive reuse opportunities.

AB 1695 (Santiago), Chapter 639, Statutes of 2022, requires that any notice of funding availability issued by HCD for an affordable multifamily housing loan program states that adaptive reuse of a property for affordable housing purposes is an eligible activity.

SB 1369 (Wieckowski) of 2022 would have required an adaptive reuse project to be a use by right in all areas regardless of zoning, and that an adaptive reuse project would not constitute a “project” for the California Environmental Quality Act (CEQA). SB 1369 would have prohibited a city or a county from imposing certain requirements on an adaptive reuse project and would have required the California Building Standards Commission to update building standards to consider and apply to adaptive reuse projects. SB 1369 was never heard in Senate Governance and Finance Committee.

AB 1068 (Santiago) of 2021 would have required DGS to solicit and consider proposals for adaptive reuse projects that result in at least 50% of units being affordable to persons who are extremely low and very low income for surplus state real property. This bill was never heard by the Assembly Committee on Housing and Community Development.

AB 654 (Hueso), Chapter 278, Statutes of 2011 required historical properties subject to Mills Act contracts, which restricts the use of the property in exchange for lower tax assessment values, to be inspected prior to a new agreement and every five years thereafter; required that any fee charged by the local agency to administer the program not exceed the reasonable cost of providing the services for which the fee is charged; and, required local agencies to take actions to enforce the contracts.

AB 601 (Cedillo) of 1999 would have required HCD to appropriate \$6,000,000 from the General Fund for the preparation and adoption of an urban adaptive reuse program. The bill was vetoed by the Governor.

- 10) **Arguments in Support.** The Central City Association of Los Angeles states, “While adaptive reuse projects provide many benefits, they are complex and face financial feasibility challenges. Recognizing this barrier, cities across North America have developed various financial incentive programs and tools to support conversion projects, including Calgary, New York City, Atlanta, Chicago, Boston and Washington DC. California too must act in the wake of the pandemic to catalyze adaptive reuse in its cities and it can leverage an established financing mechanism to do so – the Mills Act.

“Since 1972, the Mills Act has offered a unique tool for local governments to incentivize – through a property tax abatement – significant investment in historic preservation. The Mills Act empowers participating local governments to enter into contracts with owners of ‘qualified historic properties’ who actively participate in the restoration and maintenance of their historic properties while receiving property tax relief. The Mills Act Program has already demonstrated the ability to facilitate adaptive reuse projects in the City of Los Angeles and has the potential to spur commercial to residential conversions across California.

“AB 2909 would, beginning January 1, 2026, expand the definition of ‘qualified historic properties’ to include buildings that are at least 30 years old and located in commercial zones, making these properties eligible for Mills Act contracts. Contracts pertaining to this expanded definition require that property tax savings be reinvested in retrofitting and

repurposing existing buildings to create new residential rental units and participating governments would continue to retain significant local control over their Mills Act programs to address unique, local needs. This would be a thoughtful, targeted expansion of a program that has been proven to be successful and is beloved in California communities and it can be instrumental in unlocking the benefits of adaptive reuse.”

11) **Arguments in Opposition.** None on file.

12) **Double-Referral.** This bill is double-referred to the Assembly Committee on Housing and Community Development.

REGISTERED SUPPORT / OPPOSITION:

Support

Central City Association (Sponsor)

AARP

Abundant Housing LA

Axis/GFA

Boma California

California Apartment Association

California Business Properties Association

California Downtown Association

Housing Action Coalition

Institute of Real Estate Management (IREM)

International Interior Design Association Northern California Chapter

International Interior Design Association Southern California Chapter

Miyamoto International, INC.

NAIOP California

One individual.

Opposition

None on file.

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