

Date of Hearing: May 4, 2022

ASSEMBLY COMMITTEE ON LOCAL GOVERNMENT

Cecilia Aguiar-Curry, Chair

AB 2536 (Grayson) – As Amended April 26, 2022

**SUBJECT:** Development fees: impact fee nexus studies: connection fees and capacity charges.

**SUMMARY:** Requires local agencies to meet specified standards and disclosure requirements for evaluations prepared in connection with the adoption of a new fee or capacity charge, and excludes school districts and other public agencies from certain nexus study requirements.

Specifically, **this bill:**

- 1) Requires that, prior to levying a new fee or capacity charge, a local agency must evaluate the amount of the fee or capacity charge. Specifies that the evaluation must include evidence to support that the fee or charge does not exceed the estimated reasonable cost of providing service as required by law.
- 2) Requires local agencies to make all information constituting the evaluation publicly available at least 14 days prior to holding a public meeting related to the approval of the fee or charge.
- 3) Incorporates the following definitions from Section 66013 of the Government Code by reference:
  - a) “Capacity charge” means a charge for public facilities in existence at the time a charge is imposed or charges for new public facilities to be acquired or constructed in the future that are of proportional benefit to the person or property being charged, including supply or capacity contracts for rights or entitlements, real property interests, and entitlements and other rights of the local agency involving capital expense relating to its use of existing or new public facilities. A “capacity charge” does not include a commodity charge.
  - b) “Fee” means a fee for the physical facilities necessary to make a water connection or sewer connection, including, but not limited to, meters, meter boxes, and pipelines from the structure or project to a water distribution line or sewer main, and the estimated reasonable cost of labor and materials for installation of those facilities bears a fair or reasonable relationship to the payor’s burdens on, or benefits received from, the water connection or sewer connection.
  - c) “Local Agency” means a county, city, whether general law or chartered, city and county, school district, special district, authority, agency, any other municipal public corporation or district, or other political subdivision of the state.
- 4) Declares that nothing in the bill shall be construed to relieve a local agency of existing requirements related to the calculation of a fee or charge, as specified.
- 5) Amends a drafting error in AB 602 (Grayson), Chapter 347, Statutes of 2021, to narrow that measure’s requirements to cities, counties, and special districts.

**EXISTING LAW:**

- 1) Establishes the Mitigation Fee Act specific to local agency fees for development projects.
- 2) Defines “housing development projects” to mean a use consisting of any of the following:
  - a) Residential units only.
  - b) Mixed-use developments consisting of residential and nonresidential uses with at least two-thirds of the square footage designated for residential use.
  - c) Transitional housing or supportive housing.

**FISCAL EFFECT:** None.

**COMMENTS:**

- 1) **Author’s Statement.** According to the author, “Local jurisdictions levy development fees to pay for the services needed to support new housing and to offset the impacts of growth on a community. These fees can make up a substantial portion of the cost to build new housing in California. While impact fees are regulated by the Mitigation Fee Act (MFA), connection and capacity fees (such as water or sewer connection fees) are governed by a different body of law. While connection and capacity fees must abide by certain provisions of the MFA, including covering only the reasonable cost of services, they are excluded from the Act’s findings and accounting requirements. AB 2536 will establish important new accountability standards for the studies that local governments use to calculate the fees that they impose on new housing development.”
- 2) **Constitutional Limits on Local Government Revenues.** Local governments have seen their tax revenues decline on a per-capita basis since Proposition 13 (1978) capped property tax rates at 1% of assessed value (which only changes when ownership changes), limited the growth in assessed value to 2% per year, and required 2/3 voter approval for special taxes. As a result, local governments turned to general taxes to avoid the higher voter threshold. When Proposition 62 (1986) required majority voter approval of general taxes, local governments turned to assessments that were more closely tied to the benefit that an individual property owner receives. Subsequently, Proposition 218 (1996) required voter approval of parcel taxes and created a landowner-voter process for approving assessments and property-related fees.

As a result of these limitations, the revenue that local governments in California receive from taxes has declined on a per-capita basis. A 2018 report on Proposition 13 by the Legislative Analyst’s Office notes that, “adjusted for inflation, cities and counties received roughly \$790 per person in 1977-78, but only about \$640 per person in 2014-15.” Local governments made up for this shortfall by imposing other types of fees and assessments. Overall, local revenues per capita have increased in California since the passage of Proposition 13, but less so than has occurred for local governments in other parts of the United States.

3) **Legal Framework for Impact Fees.** When approving development projects, counties and cities can require the developers to mitigate the project's effects by paying impact fees. Impact fees stem from a straightforward principle: new developments should pay for the impacts that they have on the community and the burden they impose on public services. When establishing, increasing, or imposing a fee as a condition of approving a development project, the Mitigation Fee Act requires local officials to:

- a) Identify the fee's purpose.
- b) Identify the fee's use, including the public facilities to be financed.
- c) Determine a reasonable relationship between the fee's use and the development.
- d) Determine a reasonable relationship between the public facility's need and the development.

In its 1987 *Nollan* decision, the U.S. Supreme Court said that there must be an "essential nexus" between a project's impacts and the conditions for approval, which is similar to the "reasonable relationship" requirement under the Mitigation Fee Act. In the 1994 *Dolan* decision, the U.S. Supreme Court said that conditions on development must have a "rough proportionality" to a project's impacts.

In the 1996 *Ehrlich* decision, the California Supreme Court distinguished between "legislatively enacted" conditions that apply to all projects and "ad hoc" conditions imposed on a project-by-project basis. Ehrlich applied the "essential nexus" test from *Nollan* and the "rough proportionality" test from *Dolan* to "ad hoc" conditions. The Court did not apply the *Nollan* and *Dolan* tests to the conditions that were "legislatively enacted." In other words, local officials face greater scrutiny when they impose conditions on a project-by-project basis, but local officials have more leeway when setting fees that apply broadly to all projects in a given category.

Other requirements in the Mitigation Fee Act ensure that development fees are appropriately levied and spent, including that a local agency must:

- a) Hold at least one open and public meeting prior to levying a new fee or increasing an existing one.
  - b) Deposit and spend the fees within five years of collecting them.
  - c) Refund fees or make specific findings on when and how the fees will be spent for construction, if the fees are not spent within five years of collection.
- 4) **Uses of Impact Fees.** To ensure that any proposed impact fees meet all legal requirements, including the essential nexus test and the reasonable relationship test, local governments must conduct a nexus study prior to imposing a new impact fee or increasing a fee above the level of fees allowed by the previous nexus study. These nexus studies often identify the new demand for services from development, usually on a per-unit or per-capita basis, an expected level of service provision, and a maximum level of impact fees needed to fund the facilities to meet that level of service provision. Some nexus studies also consider the feasibility of different levels of fees and their effects on local housing production. Local

governments must spend the revenues generated by impact fees on capital projects and cannot use them to support ongoing operations and maintenance. These fees can be used to improve existing facilities, but can't be spent to remedy existing service deficiencies.

Impact fees support a wide range of community services and benefits, including:

- a) Public safety infrastructure, including fire stations, police stations, and correctional facilities.
- b) Transportation infrastructure, including roads, traffic improvements, public transportation systems, and sidewalks.
- c) Affordable housing.
- d) Environmental mitigation (such as habitat conservation).
- e) Libraries.
- f) Parks and open space.
- g) Flood control.
- h) Public art requirements.

In addition, local agencies that provide public utility services, including water, wastewater, and electricity, impose fees on new developments for any needed infrastructure and capacity increases, and school districts impose fees to construct school facilities needed to serve new students. While these are broadly defined as impact fees, they are governed by different statutory rules than those that apply to other types of impact fees, which contain more specific limitations on rates that can be charged.

Not all local governments impose fees on new developments for all of the purposes noted above—instead, they reflect the jurisdiction's priorities for service delivery.

- 5) **Other Development Costs.** Local governments also impose other costs on developers that are not strictly impact fees. These include:
- a) Fees to recover the costs of processing permits, reviewing plans, or performing inspections.
  - b) Dedications of parkland or fees charged in lieu of this dedication imposed pursuant to the Quimby Act (these dedications may be combined with other park impact fees).
  - c) Dedications of property for public infrastructure, such as streets and roads, and utility easement.
  - d) Conditions that a developer and a city or county agree to in a development agreement.
  - e) Mello-Roos Taxes, in which a special tax is assessed on properties that benefit from the construction of public facilities.

- f) Mitigation requirements under other statutes, such as the Subdivision Map Act or the California Environmental Quality Act.
  - g) Construction excise taxes.
  - h) Inclusionary housing requirements that mandate a percentage of units in a development be rented or sold at a price that is affordable to lower-income households.
- 6) **AB 602 Nexus Fee Requirements.** Last year the Governor signed AB 602 (Grayson), which required a city, county, or special district to conduct a nexus study prior to the adoption of an impact fee. This bill amended the law to require the preparation of nexus studies to follow certain standards and practices including:
- a) When applicable, identify the existing level of service and proposed new level of service, explain the metric being used, and include an explanation of why the new level of service is necessary.
  - b) In calculating the fee, it must be proportionate to the square footage of the proposed units, unless the local agency makes a finding that another standard is more appropriate. Local agencies can still establish different fees for different types of developments.
  - c) Adopt a capital improvement plan in jurisdictions located in counties with over 250,000 residents.
  - d) Studies must be adopted at a public hearing with at least 30 days' notice, which must be provided to members of the public that request it.
  - e) Calculate fees using standards that comply with existing law, including, but not limited to, vehicle miles traveled.
  - f) Studies must be updated every eight years, from the period beginning on January 1, 2022.
- Additionally, AB 602 was inadvertently amended in the Senate to apply the bills provisions to "local agencies," which includes school districts. This amendment was made in error.
- 7) **Bill Summary.** This bill will require local agencies to evaluate the amount of a fee or capacity charge prior to adopting fees for water connections or sewer connections, or imposing capacity charges to determine if those fees or charges are reasonable. This bill additionally requires the information constituting the evaluation to be made publicly available at least 14 days prior to a meeting associated with the approval of these fees or charges. Finally, this bill modifies the scope of AB 602 so that it's provisions apply only to cities, counties, and special districts.
- 8) **Related Legislation.** AB 2186 (Grayson) creates the Housing Cost Reduction Incentive Program to reimburse cities and counties for development impact fees that are reduced or deferred for affordable housing developments. AB 2186 is pending in the Assembly Appropriations Committee.

9) **Previous Legislation.** AB 602 (Grayson) Chapter 347, Statutes of 2021, added new requirements to impact fee nexus studies, required local agencies to request certain information from development proponents and required the Department of Housing and Community Development to develop a nexus study template.

10) **Arguments in Support.** None on file.

11) **Arguments in Opposition.** The Orange County Sanitation District wrote in opposition to a previous version of the bill, “This measure would impose new standards and practices for determining the reasonable cost of providing sewer and water service. However, it is already an industry standard to conduct a fee study, which gathers information that is critical to making decisions, before adopting or increasing connection fees or capacity charges. Specifically, the OC San Board of Directors uses this information, as well as the proposed impacts on customers, to make informed decisions on increasing or adopting new fees.”

**REGISTERED SUPPORT / OPPOSITION:**

**Support**

None on file.

**Opposition**

Orange County Sanitation District (prior version)

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