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ARTICLES

THE IRONY OF "INCLUSIONARY" ZONING

ROBERT C. ELLICKSON*

Between 1973 and 1980, the average sale price of a single-family house in the five-county Los Angeles area rose from \$40,700 to \$115,000, or by 183%. This increase not only was twice the rate of increase in the Consumer Price Index for Southern California during the same period (92%), but also far outstripped the coincident increase in house prices in the nation as a whole (117%). In 1973, the average Los Angeles area house price was only 17% above the national average; by 1980, the

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A slightly different version of this Article will appear as a chapter in RESOLVING THE HOUSING CRISIS: GOVERNMENT POLICY, DECONTROL, AND THE PUBLIC INTEREST (M. Johnson ed. 1981), a book compiled by the Pacific Institute for Public Policy Research, and published by the Ballinger Publishing Company. I am grateful to David J. Theroux, President of the Pacific Institute, and the Ballinger Publishing Company for their permission to reprint material appearing here.

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^{1.} Federal Home Loan Bank Board, Office of Policy and Economic Research, Statistical Division, Mortgage Interest Rate Survey (Jan. 1980) (copy on file with Southern California Law Review). The survey is based on a sampling of sales of both new and used nonfarm houses financed with conventional mortgages originated by major lenders. The survey defines the greater Los Angeles area as including Los Angeles, Orange, Riverside, San Bernardino, and Ventura Counties; the San Diego area as consisting of San Diego County; and the San Francisco area, as including Alameda, Contra Costa, Marin, Napa, San Francisco, San Mateo, Santa Clara, and Solano Counties.

^{2.} Id.

gap had widened to 52%.³ In the San Diego and San Francisco metropolitan areas during the identical 1973 to 1980 period, the rate of house price inflation was slightly greater than in Los Angeles.⁴

There is growing evidence that the recent boom in California real estate prices is attributable in significant part to legal events of the 1970's. Several state enactments in the early part of the decade armed California environmentalists with powerful legal techniques for slowing or stopping new development. Moreover, a series of decisions by the California Supreme Court stripped away many previously perceived constitutional constraints on local land-use policies. These judicial decisions enabled the cities and counties of California to levy heavier taxes on new development and, by making local officials less fearful that their zoning restrictions would be declared unconstitutional, contributed to tighter and tighter local controls on the supply of housing.

The high housing costs in California seem to have discouraged households and firms from migrating to the state. During the period from 1970 to 1980, the population of California grew by a lower percentage than the population of any other Western state except Mon-

^{3.} Id., News Release from Statistical Division, Federal Home Loan Bank Board (Oct. 3, 1980) (copy on file with Southern California Law Review).

^{4.} News Release from Statistical Division, supra note 3.

^{5.} See, e.g., Frech, The California Coastal Commissions: Economic Impacts, in Resolving The Housing Crisis: Government Policy, Decontrol, and the Public Interest (M. Johnson ed. 1981); Mercer & Morgan, The Contribution of Residential Growth Controls to the Rise in House Prices: South Coast Santa Barbara County California, in Resolving the Housing Crisis: Government Policy, Decontrol, and the Public Interest (M. Johnson ed. 1981); S. Schwartz, The Effect of Growth Management on Housing Prices: Methodological Issues and a Case Study (Nov. 14, 1980) (unpublished paper presented at the Fourth Annual Lincoln Institute/USC Conference on Land Policy). "Our results generally support the hypothesis that growth management causes significantly higher house prices" Id. at 187.

^{6.} See, e.g., California Environmental Quality Act, Cal. Pub. Res. Code §§ 21000-21176 (West 1977 & Supp. 1981) (originally enacted in 1970); California Coastal Act of 1976, Cal. Pub. Res. Code §§ 30000-30900 (West 1977 & Supp. 1981) (replacing the California Coastal Zone Conservation Act of 1972, an initiative measure codified at Cal. Pub. Res. Code §§ 27000-27650 (West Supp. 1976)).

^{7.} See, e.g., Agins v. City of Tiburon, 24 Cal. 3d 266, 598 P.2d 25, 157 Cal. Rptr. 372 (1979), aff'd on other grounds, 447 U.S. 255 (1980) (landowner victimized by unconstitutional regulation has no remedy in damages); HFH, Ltd. v. Superior Court, 15 Cal. 3d 508, 542 P.2d 237, 125 Cal. Rptr. 365 (1975), cert. denied, 425 U.S. 904 (1976); Associated Home Builders v. City of Walnut Creek, 4 Cal. 3d 633, 484 P.2d 606, 94 Cal. Rptr. 630 (1971) (sustained exaction of in-lieu fees from developers for parks). See generally DiMento, Dozier, Emmons, Hagman, Kim, Greenfield-Sanders, Waldau & Woollacott, Land Development and Environmental Control in the California Supreme Court: The Deferential, the Preservationist, and the Preservationist-Erratic Eras, 27 U.C.L.A. L. Rev. 859 (1980).

tana.⁸ The price spiral has also produced political pressure for governmental adoption of rent controls and other programs popularly viewed as methods for alleviating high housing prices.

This Article analyzes "inclusionary" zoning, one of the most noteworthy of these governmental responses. Pioneered in 1971 by Fairfax County, Virginia, by 1980 inclusionary zoning was spreading rapidly in California and, to a lesser extent, in other states. In essence, an inclusionary ordinance requires the developer of new housing units to set aside a certain fraction of the units for occupancy at reduced prices by moderate-income and, less often, low-income families. Proponents of these programs describe them as "inclusionary" to contrast them with the "exclusionary" policies (such as large-lot zoning) that many suburbs adopt to hinder development of low cost housing.

By March 1981, inclusionary programs had been adopted by twenty-two California localities. ¹⁰ In addition, in January 1980, the California Coastal Commission adopted official guidelines which imposed an inclusionary requirement on housing built for sale within the coastal zone. ¹¹ Another state agency, the California Department of Housing and Community Development, has drafted and publicized a Model Inclusionary Zoning Ordinance. ¹² By early 1981, more than a thousand California families were already living in inclusionary units, and thousands more units were in the production pipeline. ¹³

^{8.} See Bureau of the Census, U.S. Dep't of Commerce, 1980 Census of Population (final apportionment counts).

^{9.} See generally N.Y. Times, Aug. 24, 1980, § 1, at 26, col. 1; Fox & Davis, Density Bonus Zoning to Provide Low and Moderate Cost Housing, 3 HASTINGS CONST. L.Q. 1015 (1976) (describing inclusionary programs in six states). See Kleven, Inclusionary Ordinances—Policy and Legal Issues in Requiring Private Developers to Build Low Cost Housing, 21 U.C.L.A. L. Rev. 1432, 1439 (1974).

^{10.} Memorandnm of Michael L. Fischer, Executive Director, California Coastal Commission 7 (Mar. 2, 1981) (transmitting the revised housing guidelines adopted by the Commission on May 5, 1981) [hereinafter cited as Revision of Coastal Commission Guidelines].

^{11.} California Coastal Commission, Interpretive Guidelines on New Construction of Housing (Jan. 22, 1980) [hereinafter cited as Coastal Commission Guidelines].

After considerable criticism, especially from the San Diego and South Coast Regional Commissions, the California Coastal Commission revised its guidelines in May 1981 to ease the inclusionary burdens on small developers. See Revision of Coastal Commission Guidelines, supra note 10, at 1.

^{12.} Legal Office, Cal. Dep't of Housing & Community Development, Model Inclusionary Zoning Ordinance (1978) [hereinafter cited as California Model Ordinance].

The inclusionary efforts of yet a third state agency, the State Water Quality Control Board, are described in note 28 infra.

^{13.} As of March 1981, the unincorporated areas of Orange County contained almost 500 occupied inclusionary units, and another 4000 more were beyond the approved-tentative-inap stage. Irvine also has hundreds of occupied inclusionary units. Telephone interview with F.W.

The thesis of this Article is that most "inclusionary" programs are ironically titled. These programs are essentially taxes on the production of new housing. The programs will usually increase general housing prices, a result which further limits the housing opportunities of moderate-income families. In short, despite the assertions of inclusionary zoning proponents, most inclusionary ordinances are just another form of exclusionary practice.

The Article's presentation is straightforward. Section one surveys the wide variety of inclusionary programs.¹⁴ Section two invokes economic analysis to examine the effects a typical inclusionary program would have on housing production, housing prices, and overall economic efficiency.¹⁵ Section three is essentially a political analysis that invokes the emerging literature on the theory of regulation to explore whether an inclusionary program is better perceived as being (1) an idealistic concept that has unexpectedly gone wrong; or (2) a conscious effort by owners of existing housing units to enrich themselves at the expense of others.¹⁶ Finally, section four briefly reviews the legal status of inclusionary zoning in California.¹⁷

THE STRUCTURE OF INCLUSIONARY PROGRAMS

Because the leading inclusionary programs have been described elsewhere, ¹⁸ this section simply highlights some of the more important program variations. Most of the references in the text are to five of the best known programs in California—those of the City of Irvine; the City of Palo Alto; Orange County (applicable only to its unincorporated areas); the California Coastal Commission; and the Model Ordinance drafted by the California Department of Housing and Community Development.

- 14. See notes 18-82 and accompanying text infra.
- 15. See notes 83-129 and accompanying text infra.
- 16. See notes 130-43 and accompanying text infra.
- 17. See notes 144-65 and accompanying text infra.

Olson, Manager, Information and Housing Development Office, Environmental Agency, County of Orange (Mar. 2, 1981).

A California Coastal Commission staff report in early 1981 calculated that the Commission's permit decisions had already produced 404 occupied inclusionary units, and had laid the groundwork for the provision of 4424 more. Revision of Coastal Commission Guidelines, *supra* note 10, at 5.

^{18.} See H. Franklin, D. Falk & A. Levin, In-Zoning: A Guide for Policy-Makers on Inclusionary Land Use Programs (1974); Fox & Davis, supra note 9, at 1036-67; Kleven, supra note 9, at 1439-48.

A. New Housing Projects Covered

Inclusionary programs apply only to new developments of a certain size and to certain types of new housing. Palo Alto, for example, only requires developers of ten or more units of multifamily housing, and subdividers of ten or more lots, to provide inclusionary units. 19 The Coastal Commission's guidelines, however, apply only to housing for sale. The Commission believes that the construction of rental units inherently makes a significant contribution to the supply of affordable housing, whereas the construction of housing for sale does not.²⁰ Like Palo Alto, the Commission is tougher on large developers than on small ones. Coastal subdividers who produce twenty-one or more forsale umits are generally required to set aside 25% of their units for occupancy by low- and moderate-income families.²¹ When dealing with projects consisting of ten to twenty for-sale units, however, the Commission may allow the developer to avoid provision of on-site inclusionary units if the developer will provide an equivalent number of offsite units; or it may allow the developer to pay a fee equal to 6% of the market price of the project. Any fee revenues go either to the state Coastal Conservancy, or to a local housing authority to be used to provide "affordable housing" in the neighborhood where the donating project is located.²² Moreover, the Commission totally exempts from its exclusionary policy subdivisions of nine or fewer for-sale units, because it asserts that the imposition of even a 6% fee on these small projects would be "neither feasible nor practical."23 Because the mathematics of multiplying a sales price by 6% seem eminently feasible in all situations, a more credible explanation is that the Commission foresees severe political risks in imposing high taxes on small developments—especially owner-built houses.

Inclusionary requirements typically apply only to developers of residential projects. The California Coastal Commission, however, has made some ad hoc efforts to extend the concept to commercial development. In 1979, the Commission awarded coastal permits to the general

^{19.} CITY OF PALO ALTO, CAL., COMPREHENSIVE PLAN, Housing Program 18 (adopted Nov. 29, 1976) [hereinafter cited as Housing Program 18]; DEPARTMENT OF PLANNING AND COMMUNITY ENVIRONMENT, CITY OF PALO ALTO, PALO ALTO'S BMR PROGRAM 2 (1980) [hereinafter cited as PALO ALTO'S BMR PROGRAM].

^{20.} Coastal Commission Guidelines, supra note 11, at 1, 8.

^{21.} Id. at 1, 8-9; Revision of Coastal Commission Guidelines, supra note 10, at 3.

^{22.} Revision of Coastal Commission Guidelines, supra note 10, at 3.

^{23.} Coastal Commission Guidelines, *supra* note 11, at 1 (exempting projects of four or fewer units); Revision of Coastal Commission Guidelines, *supra* note 10, at 3 (exempting projects of nine or fewer units).

partner of two partnerships seeking to build hotels on two lots in the Marina del Rey area of Los Angeles County, subject to the following three conditions:

- (1) That the waterside lot be used for a "moderate cost" motel of 200 rooms and a 50-bed hostel approved by the American Youth Hostel Association ("Moderate cost" was defined to mean, e.g., "no more than 60% of the published rate of the Holiday Inn chain.");
- (2) That the same waterside lot be equipped with a "moderate-cost coffee shop and fast food restaurant with window service"; and
- (3) That on weekends, 15% of the rooms in the market-rate hotel on the nonwaterside lot be made available at half price to moderate-income families.²⁴

The inclusionary model could be applied to still other sorts of uses. For example, developers of industrial parks might be required to include industrial facilities that provide job opportunities for unskilled laborers; and developers of shopping centers might be required to set aside low rent space for used-furniture stores and pawn shops.

Several cities in northern California have imposed ad hoc exactions on nonresidential developers to raise funds to finance city housing programs. For example, the Hewlett-Packard Corporation had to agree to donate \$215,000 in housing funds to the City of Palo Alto before receiving permission to build an office building in the city.²⁵ The San Francisco planning commission approved construction of a new twenty-seven story Holiday Inn only after the developer agreed to

Letter from Naphtali H. Knox, Director of Planning and Community Environment of the City of Palo Alto, to the author (Jan. 2, 1981) (copy on file with Southern California Law Review) [hereinafter cited as Knox Letter].

^{24.} California Coastal Commission Staff Recommendations on Appeals Nos. 49-79 and 207-79 (Aug. 15, 1979), as amended by Staff Recommendation on Appeal No. A-207-79 (Dec. 19, 1979).

^{25.} The Director of Planning and Community Environment, City of Palo Alto, wrote: [I]n Palo Alto, we have been receiving contributions for the City's housing programs from industrial and commercial developers. These began early in 1978 when Hewlett-Packard proposed to build a 478,000 square foot headquarters building, which, being the largest building built in Palo Alto in the 70's, required a full EIR [Environmental Impact Report]. The EIR determined that there would be impacts on the housing market, and, as a mitigation measure, Hewlett-Packard volunteered a contribution of \$215,000 to the City's housing programs. Between January, 1978, and February, 1980, Palo Alto approved nine additional projects ranging from 63,600 square feet in size to 193,000 square feet, where the environmental analysis determined that there would be some impact on the housing market. In each of those cases, "imitigated negative declarations" were prepared under CEQA [the California Environmental Quality Act] by the planning staff, and approved and signed by the applicant/developers. In total, some \$648,000 in housing mitigation monies are being contributed by these ten projects.

pay more than \$100,000 annually for low-income housing for a period of twenty years. 26

B. THE PERCENTAGE OF INCLUSIONARY DWELLING UNITS

Because the leading programs apply only to residential development, inclusionary requirements are usually stated as a percentage of new dwelling units produced. The required set-aside may range from 10% to 33% of those units.²⁷ Sometimes specific targets are established for different income categories. Orange County, for example, requires developers of both sales and rental projects (with certain exceptions) to set aside 10% of the units for families with incomes less than 80% of the county median; another 10% of the units for families having between 80% and 100% of median county income; and another 5% for families having between 100% and 120% of median county income.²⁸

C. ELIGIBLE FAMILIES

The housing subsidies made available through inclusionary programs are usually nominally directed at low- and moderate-income families. In fact, however, the beneficiaries are mostly households one would identify in ordinary language as middle class. This discrepancy arises from the definition of "moderate-income" used by professional housing advocates, and from the tendency of inclusionary programs to cater predominantly to the moderate-income group. Reflecting both federal and state housing statutes, inclusionary programs invariably define "moderate-income families" as those with incomes between 80% and 120% of the median income of families in the county in question.²⁹

^{26.} L.A. Times, Jan. 31, 1981, § 1, at 1, cols. 1, 2. After San Francisco made similar ad hoc demands on a number of other developers of highrise hotels and office buildings, the city's mayor proposed that the city switch to a more systematic program of taxing commercial developers to raise housing subsidy funds. L.A. Times, Apr. 11, 1981, § 1, at 1, col. 1.

^{27.} Revision of Coastal Commission Guidelines, supra note 10, at 8 (reporting the results of a survey of 22 inclusionary programs in California).

^{28.} If, after a good faith effort, a developer fails to secure housing subsidy funds, the 10% set-aside for families with incomes less than 80% of the county median is waived, but the developer must then provide 15% of the units to the 80-100% group, and 10% to the 100-120% group. F. Olson, Orange County's Inclusionary Housing Program 17-18 (Feb. 13, 1981) (paper presented at the Fourth Annual Lincoln Institute/USC Conference on Land Policy) (copy on file with Southern California Law Review) [hereinafter cited as F. Olson].

In the key coastal area of Orange County within the jurisdiction of the Aliso Water Management Agency, the State Water Quality Control Board has required that 35% of new dwelling units be "affordable." The State Board obtained the leverage to accomplish this first by restricting sewer inflows in the area for environmental reasons, and then by waiving the restriction only for developers who would agree to comply with its inclusionary guidelines. See id. at 13, 34.

^{29.} See, e.g., California Model Ordinance, supra note 12, § C9. Cf. Cal. Health &

(Some adjustments may be made for family size, family assets, and other factors.) Thus, the moderate-income group straddles the exact middle of the family income distribution. "Low-income" families are defined as all those with incomes below 80% of the county median. Together, the low- and moderate-income groups can be expected to constitute more than 60% of county population.

In Palo Alto, only moderate-income families have been eligible to receive inclusionary units.³⁰ Localities such as Irvine and Orange County do target some inclusionary units for low-income families, but both target considerably more for moderate-income families.³¹

Inclusionary governments may give priority to subcategories of families within the eligible income group. Irvine, for example, extends first priority to households with primary wage earners employed in Irvine.³² When Palo Alto began its program, first priority was extended to persons who had been residents of Palo Alto for two or more years; currently, however, eligibility is extended to any person who lives or works in Palo Alto.³³

D. DEPTH OF SUBSIDIES

Inclusionary governments (with the significant exception of Orange County) control the prices of inclusionary units to assure that the intended beneficiaries can afford to occupy them. Both the Coastal Commission guidelines and the California Model Ordinance generally limit the housing developer's sale price to two and one-half times the particular purchaser's annual income.³⁴ Irvine is less generous, and permits

SAFETY CODE § 50093 (West Supp. 1981) (statutory definition of "persons of low or moderate income" for purposes of housing and home finance legislation).

^{30.} Housing Program 18, supra note 19, reads: "In new multiple housing developments of 10 or more units, not less than 10 per cent of the units should be provided at below market rates to moderate- and middle-income families." Palo Alto's program has thus far served only moderate-income families, that is, those families with incomes between 80% and 120% of the median family income in Santa Clara County. The city, however, is considering broadening eligibility to include "middle-income" families, which it defines as those having incomes between 120% and 150% of the county median. Knox Letter, supra note 25.

^{31.} For the intended Orange County mix, see text accompanying note 28 supra. As of September 1980, over 80% of the inclusiouary units in Irvine were occupied by, or slated for, moderate-income families. Memorandum from Pamela Sheldon of the City of Irvine Department of Planning to Carolyn Burton 1 (Sept. 23, 1980) (copy on file with Southern California Law Review) [hereinafter cited as Sheldon Memorandum].

^{32.} Sheldon Memorandum, supra note 31, at 6.

^{33.} Knox Letter, supra note 25.

^{34.} Coastal Commission Guidelines, supra note 11, at 2, Exhibit 1; CALIFORNIA MODEL ORDINANCE, supra note 12, at § E2.

a multiple of three times annual income.³⁵ In the case of rental housing, the programs generally limit a tenant family's monthly rent to 25% (or perhaps 30%) of its gross monthly income.

Many California families spend more of their incomes on housing than these pricing formulas exact from included families. Moreover, inclusionary units tend to be of higher quality than the housing units program beneficiaries would otherwise occupy. These two factors combine to bring about rather deep subsidies to the chosen few. In Irvine, inclusionary units have been sold for roughly two-thirds of their market value.³⁶ Elsewhere, it has not been unusual for the discount to exceed 50%. For example, a dental receptionist in Palo Alto was enabled by that city's inclusionary program to purchase a new condominium unit worth over \$100,000 for only \$39,100.³⁷ The Coastal Commission has required an applicant for a condominium conversion project in Del Mar Heights to sell inclusionary units each having a market value of \$65,000 for between \$20,000 and \$40,000.³⁸

Some of the deepest subsidies go to inclusionary tenants who also receive federal rent subsidies under the Section 8 program.³⁹ The *Los Angeles Times* reported an instance in which the Coastal Commission compelled the developer of a seventeen unit apartment building in the Ocean Park district of Santa Monica to rent several units at only 10% to 20% of market value; Section 8 subsidies were to make up about two-thirds of the landlord's losses on the units in question.⁴⁰ Commission staff members have generally been so eager to "increase access to the coast" that they have taken pride in forcing the provision of inclusionary units at prices 80% to 90% below market value.⁴¹

Orange County's inclusionary program lacks mandatory controls on sale prices and thus, predictably, is the program most popular with builders. In Orange County, a unit counts as inclusionary if it sells below a specified price, or if its purchaser has a low or moderate income; the county, unlike other inclusionary governments, does not in-

^{35.} Sheldon Memorandum, supra note 31, at 4.

^{36.} Telephone Interview with Pamela Sheldon, City of Irvine Department of Planning (Sept. 12, 1980) (Author's notes on file with Southern California Law Review) [hereinafter cited as Sheldon Interview].

^{37.} Wall Street J., Jan. 25, 1980, at 1, col. 6.

^{38.} L.A. Times, Oct. 28, 1979, § 1, at 22, col. 2.

^{39. 42} U.S.C.A. § 1437(f) (West Supp. 1981).

^{40.} L.A. Times, Oct. 28, 1979, § 1, at 22, col. 1.

^{41.} Interview with Robert Sheppard, attorney formerly on the staff of the California Coastal Commission (Oct. 18, 1980) (author's notes on file with Southern California Law Review) [hereinafter cited as Sheppard Interview].

sist on both.⁴² Because there are no mandatory price controls and because the county gives developers of inclusionary units considerable freedom to avoid expensive design features (such as covered parking), Orange County developers have sometimes succeeded in selling their inclusionary units at market value.⁴³

E. NOMINAL SOURCE OF SUBSIDY

Local governments virtually never contribute their own funds to help defray the costs of including middle- and low-income families in new residential developments. The City of Los Angeles, in its 1974 inclusionary ordinance, specified that developers were to receive fair market value for their inclusionary units; the city, in effect, conditioned its program on the availability of federal subsidies.⁴⁴ The subsequent drying up of federal funds put the Los Angeles program in limbo.

Under most inclusionary ordinances, the costs of inclusion are nominally borne by the developer. As explained below, these costs may be partly offset by density bonuses. Moreover, as also will be explained, market conditions may enable the developer to shift the costs of inclusionary programs backward to land sellers, or forward to housing purchasers.

F. SELECTION OF PROGRAM BENEFICIARIES

The public announcement that inclusionary units are about to become available is likely to trigger an avalanche of applications, because over 60% of a county's households usually qualify as low- or moderate-income families. For example, a recent development of 392 inclusionary units in the El Toro section of Orange County attracted 12,000 moderate-income applicants.⁴⁵

Most inclusionary ordinances fail to specify how winners are to be selected from the surfeit of applicants. The critical variables in the design of a selection system are (1) who controls entry into the pool of eligible applicants; and (2) how the winners are selected from the pool.

^{42.} Memorandum from F.W. Olson, Manager, County of Orange Environmental Management Agency, Information and Housing Development Office, to H.G. Osborne, Director, County of Orange Environmental Management Agency (Mar. 27, 1980) (copy on file with Southern California Law Review).

^{43.} F. Olson, *supra* note 28, at 22; Letter to the author from Robert H. Rivinius, Executive Vice President, California Building Industry Association (Feb. 11, 1981) (on file with *Southern California Law Review*) [hereinafter cited as Rivinius Letter].

^{44.} See Fox & Davis, supra note 9, at 1041-44; Kleven, supra note 9, at 1446-48.

^{45.} L.A. Times, Sept. 21, 1980, § 7, at 1, col. 1.

In some places developers have had considerable control over entry into the pool. In Irvine, for example, the developer has been responsible for taking applications. In Orange County, builders of inclusionary units have been entitled to propose their own buyer-selection mechanisms for approval by the Board of Supervisors. A developer would obviously be tempted to allocate inclusionary units to persons with whom he had business relations. The director of Irvine's inclusionary program reports an instance where a developer sought the city's permission to reserve 20% of his inclusionary units for occupancy by his employees. The city refused because his employees were not otherwise eligible as they were not then employed in Irvine.

Because developers might abuse their selection powers by, for example, demanding kickbacks from applicants, most inclusionary governments have diminished developer influence over occupant selection. Irvine now requires that potential applicants be screened for eligibility by a nonprofit housing organization.⁴⁹ The Orange County Housing Authority has become increasingly involved in screening buyers.⁵⁰ Some jurisdictions have completely eliminated the developer from the screening and selection process. In Palo Alto, applications are taken and beneficiaries selected by the nonprofit Palo Alto Housing Corporation.⁵¹ In Montgomery County, Maryland, one of the pioneers of the inclusionary movement, the county itself maintains a county-wide eligibility hist.⁵²

Queues and lotteries are generally used to select the few beneficiaries from the many applicants who find their way into the pool of eligibles. Queues and lotteries are often encountered in situations where the imposition of price controls has prevented the price mechanism from equilibrating supply and demand. In Irvine and Orange County, inclusionary developers commonly conduct public lotteries to select the winning applicants.⁵³ These lotteries have often received

^{46.} Sheldon Interview, supra note 36.

^{47.} See F. Olson, supra note 28, at 20.

^{48.} Sheldon Interview, supra note 36.

^{49.} Id.

^{50.} F. Olson, supra note 28, at 30, 31, 33-34.

^{51.} PALO ALTO'S BMR PROGRAM, supra note 19, at 6.

^{52.} OFFICE OF HOUSING, MONTGOMERY COUNTY, MD., EVALUATION OF THE MODERATELY PRICED DWELLING UNIT PROGRAM 13 (1978), reprinted in State, Local and Environmental Affairs Dep't, Nat'l Ass'n of Homebuilders, Inclusionary Housing (1980) [hereinafter cited as Montgomery County Evaluation].

^{53.} Sheldon Interview, supra note 36.

great attention in the media. This may explain why developers of large, planned communities seem to favor the lottery system.

In other jurisdictions, the trend is toward allocation by queue. For example, after using lotteries for a few years, the Palo Alto Housing Corporation held a master drawing to rank the applicants in its pool. New applicants are now put at the bottom of the Corporation's list. The households most favored by a queue system are, of course, those who receive early notice that a queue is being formed.

The beneficiaries of inclusionary programs apparently include disproportionate numbers of both upwardly mobile young families and divorced women with children. A study of the applicants of Montgoinery County's eligibility hist, for example, revealed that the heads of households had a median age of 30.4 years and that 42% of the applicant households were headed by females.⁵⁴ Of the first forty households to occupy inclusionary units in Palo Alto, none was headed by a person over age sixty-two; only one was headed by a blue-collar worker; 45% were headed by women; and 22% consisted of a single individual. The average household size was 2.63 persons.⁵⁵ Approximately one-third of those benefited by the Palo Alto program are members of racial minorities (including Asians).⁵⁶

G. RESALE CONTROLS

In Irvine, the purchaser of an inclusionary unit typically is required to occupy the unit for one year. At the end of the year, the purchaser may sell the unit to whomever he pleases at whatever price he can obtain.⁵⁷ This system permits an Irvine purchaser to cash out his original good fortune of having been able to purchase the unit at tens of thousands of dollars below market value.

The officials who manage inclusionary programs generally favor imposition of resale controls to limit sale prices of inclusionary units. They see one of their major goals to be the provision of housing to

^{54.} Montgomery County Evaluation, supra note 52, at 3-4. See also California Building Industry Ass'n, The Implications of Inclusionary Housing Programs 81-82 (1979) (prepared by Connerly & Associates, Inc.) [hereinafter cited as Implications] (inclusionary units in the California cities of Davis and Petaluma went mainly to upwardly mobile young families, and thus brought about little mixing of different social classes).

^{55.} PALO ALTO HOUSING CORP., PROFILE OF PURCHASERS (1977) (copy on file with Southern California Law Review).

^{56.} Telephone Interview with Sylvia Seman, Palo Alto Housing Corporation (Dec. 2, 1980) (author's notes on file with Southern California Law Review).

^{57.} Sheldon Meinoranduin, supra note 31, at 9-10.

locally employed workers of modest income, and they deem price controls on resale necessary to accomplish this mission.⁵⁸ Resale controls are now required by the California Model Ordinance, Palo Alto, and most other inclusionary localities.⁵⁹ The California Coastal Commission also requires resale controls; its executive director believes inclusionary programs would be a "joke" without them.⁶⁰

A typical resale control calls first for the summation of the seller's original purchase price and the seller's costs of substantial improvements (less depreciation).⁶¹ This sum is then adjusted for inflation according to a specified imdex. The adjusted sum is the ceiling for the seller's proceeds on resale. This resale price formula is designed to prevent the original occupant from cashing out most of his prospective subsidy benefits when he moves.⁶² The usual resale control provision also prevents the original purchaser from controlling the identity of his successor. For example, in Palo Alto, the city (or its designee) has an option to repurchase at the controlled resale price; the city can thereby pick the subsequent occupant.⁶³ In the case of rental units, most inclusionary governments employ similar controls to prevent subleasing by tenants who enjoy below-market rents.⁶⁴

^{58.} See PALO ALTO'S BMR PROGRAM, supra note 19, at 1, 5; F. Olson, supra note 28, at 9-12, 20-21.

^{59.} California Model Ordinance, supra note 12, at § F3; Letter from Naphtali Knox, Director of Planning and Community Environment, City of Palo Alto, to the San Francisco Editor of the Wall Street Journal (Feb. 29, 1980) (unpublished) [hereinafter cited as Knox Letter to the Editor] (copy on file with Southern California Law Review); Revision of Coastal Commission Guidelines, supra note 10, at 8.

^{60.} L.A. Times, Sept. 21, 1980, § 7, at 1, col. 1.

^{61.} See, e.g., California Model Ordinance, supra note 12, at 2.

^{62.} William A. Fischel has observed that a poorly drafted resale-control formula will create perverse incentives for controlled owners:

[[]R]esale controls discourage everyday maintenance such as painting and cleaning. At first I thought that this would be [deterred] by the price index, but let me give an example to show why it is not so. If the market price of a unit is \$100,000, and the controlled price is \$60,000, assume that all housing prices rise in five years by 50%. The controlled house now can be sold for \$90,000, for a tidy tax free gain of \$30,000. But why should the lucky "moderate income" family settle for only a \$30,000 gain? Suppose that ordinary maintenance in the five year period would have cost \$5000. Forgoing the maintenance causes the house to depreciate by \$10,000. But what does the controlled price owner care? All that happens to him is that the "true" value of the house is now only \$140,000 (\$150,000 mimus \$10,000). But since he cannot get more than \$90,000, he has no incentive to maintain the house. In fact, in this situation he has some incentive to cannibalize the house, selling good features and replacing them with cheap (or no) features.

Letter from William A. Fischel, Department of Economics, Dartmouth College, to the author (June 9, 1981) (copy on file with the Southern California Law Review).

^{63.} Palo Alto uses deed covenants to establish the city's option to repurchase. See CALIFORNIA MODEL ORDINANCE, supra note 12, exhibit A (a copy of one of the Palo Alto covenants).
64. Id.

H. DENSITY BONUSES

Most inclusionary ordinances entitle an inclusionary developer to build more dwelling units than the applicable zoning restrictions would otherwise allow. In other words, the inclusionary units may be, in whole or in part, add-on units that the developer would not have been able to build in the absence of the inclusionary program. By coupling a density bonus to its inclusionary requirements, a government can reduce the construction industry's political opposition to the inclusionary program, and can help rebut a developer's contention that an inclusionary requirement is an unconstitutional taking of property.

Density bonus provisions vary widely. The California Coastal Commission is unable to guarantee any form of density bonus because in coastal areas local governments continue to control densities through zoning. The Commission does advocate, "particularly on smaller projects, [use of] a density increase, reduced parking standards, or other offsetting techniques." Of course, the Commission is able to lower its own development standards, and may volunteer to help persuade local governments to lower theirs.

The California Model Ordinance provides for one bonus unit for every two required inclusionary units.⁶⁶ Most local ordinances are more generous, offering at least one bonus unit for every inclusionary unit.⁶⁷ As others have noted, "It is bewildering from a planning perspective, however, to understand how a locality can justify relaxing standards as a quid pro quo for participating in an inclusionary housing program and yet insist that the standards are essential to protect the public's health and safety in noninclusionary circumstances."⁶⁸

Without question, a density bonus can reduce (or conceivably eliminate) the net tax that an inclusionary program imposes on a developer. The extent of the reduction depends on many variables including: (1) the ratio of bonus units to inclusionary units; (2) the developer's savings in cost-of-land-improvements per lot resulting from the additional density; (3) the reductions in consumer valuations of

^{65.} Coastal Commission Guidelines, supra note 11, at 8.

^{66.} CALIFORNIA MODEL ORDINANCE, supra note 12, § H.

^{67.} CALIFORNIA BUILDING INDUSTRY ASS'N, THE FEASIBILITY OF THE DENSITY BONUS IN RELATION TO INCLUSIONARY HOUSING PROGRAMS 25 (1980) (prepared by Connerly & Associates, Inc.) [hereinafter referred to as FEASIBILITY]. But of. F. Olson, supra note 28, at 36-38 (although Orange County formulas provide for at least one, and sometimes more than two, bonus units per inclusionary unit, during the eighteen-month period after February 1979, inclusionary developers actually received only one-half bonus unit per inclusionary unit).

^{68.} FEASIBILITY, supra note 67, at 101.

project units resulting from both the increased project density and the presence of inclusionary units; (4) scale efficiencies (or inefficiencies) resulting from the construction of more dwelling units; and (5) whether the developer is permitted to downgrade the designs, floor areas, and lot areas of inclusionary units.

The most ambitious inquiry into density bonuses is a study by Connerly & Associates for the California Building Industry Association. These consultants assumed one bonus unit for every inclusionary unit, and used actual data from a project in the San Gabriel Valley to estimate the developer's net costs under a mix of inclusionary program variations. Under all variations, the study concluded that the developer's losses from having to provide inclusionary units would exceed the developer's benefits from the density bonus. The basic reason for this result was that developer's costs of merely building the inclusionary units was likely to exceed the revenues to the developer from selling the inclusionary units at their controlled prices. In short, even if one were to assume that sites for inclusionary units have a zero cost, a developer would still usually lose money on those units.

However, the construction of inclusionary housing in Orange County has sometimes proved profitable. There, mainly because of the absence of sale price controls, a developer may gain more from the density bonus than he loses from having to comply with the inclusionary requirements.

I. BUILDER-INITIATED INCLUSIONARY HOUSING

In 1979, the California Legislature enacted a statute that gave builders who volunteer to provide inclusionary units some leverage to exact special concessions from a local government—even when that government has not adopted an inclusionary ordinance. The statute provides that when a developer agrees to build 25% of his units for low- and moderate-income families, the local government must provide either: (1) a density bonus of 25%; or (2) two other concessions, such as an exemption from park fees (or other cost-inflating ordinances) and local provision of off-site improvements.⁷²

^{69.} Id.

^{70.} Id. at 53-103.

^{71.} See also Construction Industry Research Board, Review and Comments on Proposed Affordable Housing Zone of the Draft Housing Element, Riverside County (July 28, 1980) (prepared for the Riverside County Chapter, Building Industry Association of Southern California).

^{72.} CAL. GOV'T CODE §§ 65915-65918 (West Supp. 1981), interpreted in 63 Op. Att'y Gen. Cal. 478 (1980).

This statute, which applies to charter cities as well as unchartered ones, strengthens the bargaining power of developers who want to build inclusionary units. However, a local government eager to resist a proposed inclusionary project should not find it particularly difficult to cope with the statute. The reluctant government can simply choose to offer the developer two rather minor concessions (not including a density bonus). The value of these concessions to the developer is apt to be outweighed by the developer's costs of having to deal with an antagonistic government. Moreover, if the occupants of the inclusionary units would not receive housing subsidies from the state or federal government, the developer's gain from the concessions would probably be less than the developer's loss from providing units affordable by moderate-income families.

J. LOCATION AND DESIGN OF INCLUSIONARY UNITS

In Irvine and Orange County, inclusionary units are usually physically separate from market-rate units. Irvine has decreed that each new planning area of the city must contain between 10% and 26% inclusionary units. However, it has permitted the Irvine Company to apply this percentage in the aggregate to each planning area. The Company has chosen to cluster its inclusionary units in separate projects, no doubt both to reduce production costs and to increase the consumer appeal of the market-rate units. The first inclusionary units for sale in Irvine were townhouses; more recently they have been condominium units in two- or three-story garden apartments.⁷³

Other inclusionary governments have chosen to pursue economic integration at the block or building level. The California Model Ordinance, for example, requires that inclusionary units be "reasonably dispersed" throughout the affected development, and that they have, on average, the same number of bedrooms as the market-rate units. ⁷⁴ Members of the Coastal Commission staff often strive to make their inclusionary units identical to abutting market-rate units, perhaps in the belief that this will help foster social contact between families of

^{73.} Sheldon Memorandum, *supra* note 31; Telephone Interview with Pamela Sheldon, City of Irvine, Department of Planning (Sept. 8, 1980) (author's notes on file with *Southern California Law Review*).

The Orange County "program explicitly states that it is not the County's intention to achieve small scale socio-economic integration e.g., by insisting that every individual development include affordable housing." F. Olson, *supra* note 28, at 19. The County therefore permits the transfer of inclusionary-unit credits from site to site and even from developer to developer.

^{74.} CALIFORNIA MODEL ORDINANCE, supra note 12, § F1.

different income groups.⁷⁵ Palo Alto officials also generally seek to make their inclusionary units indistinguishable from market-rate units; when the exteriors of the inclusionary units will be similar to the exteriors of market-rate units, however, Palo Alto has authorized developers to reduce the floor areas and amenities (such as luxurious carpeting) of the inclusionary units to bring down costs.⁷⁶ In most jurisdictions these issues of design seem to be decided on an ad hoc basis.

K. In-Lieu Fees and Dedications

Projects containing just a few housing units or consisting entirely of luxury single-family houses are typically regarded as inappropriate sites for the provision of in-kind subsidized housing. Most inclusionary programs, therefore, specify situations where developers are to pay fees in lieu of providing actual inclusionary units.⁷⁷ Fee revenues are usually placed in a fund earmarked to finance inclusionary housing in the same neighborhood as the development. In Palo Alto, where all developers are given the option of paying an in-lieu fee, the fee in October 1980 was \$3556 per market-rate unit built, with this figure indexed to rise with inflation.⁷⁸ The Coastal Commission's guidelines sometimes call for a developer of a for-sale project of between ten and twenty units to pay an in-lieu fee equal to 6% of project value.79 Thus, in a case involving a proposed project of \$500,000 houses on one-acre lots in San Diego County, the Commission was prepared to charge the developer inclusionary fees equal to \$30,000 per house.80 There is, as yet, little evidence on how inclusionary governments actually spend their revenues from in-heu fees.

A government could conceivably use an inclusionary requirement

^{75.} Sheppard Interview, supra note 41.

^{76.} Knox Letter, *supra* note 25. Inclusionary units in Palo Alto, however, often approach luxury standards. The memorandum advertising a one-bedroom, one-bath condominium unit reports that: "Features include carpets, range, self-cleaning oven, dishwasher, disposal, gas-burning fireplace, personal storage room on same floor as living unit, use of the swimming pool, spa, lounge, and all common areas." Palo Alto Housing Corp., Application Form and Instructions for Prospective Buyers of Unit for Resale at Four Ten Sheridan Avenue (Oct. 12, 1979).

^{77.} Orange County does not permit payment of in-lieu fees, but does allow a developer to purchase inclusionary-unit credits from other developers. See F. Olson, supra note 28, at 18-19.

^{78.} Knox Letter, *supra* note 25. Palo Alto has successfully insisted on the payment of even greater sums. City officials assert that they would rather receive inclusionary units than in-lieu fees. See id.

^{79.} Coastal Commission Guidelines, *supra* note 11, at 1, 10-11; Revision of Coastal Commission Guidelines, *supra* note 10, at 3.

^{80.} The Commission eventually decided to disapprove this particular subdivision because of risks posed to the ecology of a nearby lagoon. L.A. Tunes, Aug. 25, 1980, § 2, at 1, col. 1 (San Diego ed.).

as a bargaining chip that it would relinquish in return for developer concessions unrelated to the goal of affordable housing. For example, the Coastal Commission's paramount goal seems to be to increase government ownership of coastal lands. The Commission recognizes that it can use its inclusionary requirements as leverage for achieving that unrelated goal. The Commission's guidelines state that a developer who dedicates an unusual amount of parkland will generally be relieved of some inclusionary burdens.⁸¹ In one instance the Commission is known to have offered to waive a 20% inclusionary requirement otherwise applicable to the developer of a 368-unit coastal project if the developer would agree to dedicate six acres of land to the public.⁸²

II. ECONOMIC EVALUATION OF INCLUSIONARY ZONING

Stripped to its essentials, inclusionary zoning consists of three key policies:

- (a) The taxation of new housing construction to raise revenue for local social programs;
- (b) The provision of deep housing subsidies to a tiny fraction of eligible middle-income (occasionally lower-income) families to enable those families to reside in *new* housing projects; and
- (c) The spending at step (b) of the revenues raised at step (a) without the legislative oversights (such as budget reviews) that typically constrain government spending programs.

This section employs simple tools of economic analysis to explore the merits of the first two policies. The third policy is examined in the next section, which analyzes the political factors that have shaped inclusionary zoning programs. The major conclusions reached are that the latter two policies are unwise in all situations, and that the first policy—the taxation of new housing construction—while conceivably defensible in some situations, is likely to be undesirable in the markets in which inclusionary programs have actually come into being.

A. THE FILTERING MECHANISM IN HOUSING MARKETS

Historically, new housing in the United States has tended to be first occupied by families in the upper part of the income distribution. Less wealthy families have tended to find their dwellings in the stock of used

^{81.} Coastal Commission Guidelines, supra note 11, at 8.

^{82.} Cal. Coastal Comm'n Appeal No. 87-78 (W & B Builders), noted in Coastal Commission Guidelines, supra note 11, at 3.

housing. As time passes, any individual housing unit tends to filter downward in relative quality as its components depreciate, and as its layout and equipment become obsolete. The central point about filtering is this: low- and moderate-income families benefit from the construction of housing at all levels of quality, including the highest quality units that they could not conceivably afford to buy. The infusion of new housing units into a regional market sets off a chain of moves that eventually tends to increase vacancy rates (or reduce prices) in the housing stock within the means of low- and moderate-income families. Consequently, an excellent way-perhaps even the best way-to improve the housing conditions of low- and moderate-income families is to increase the production of housing priced beyond their reach.83 Although this trickle-down process does not occur instantaneously or without some friction, most housing economists agree that it does work in due time,84 and that it has produced in the United States a housing stock that is the envy of the world.85

Many officials who draft and administer inclusionary programs appear to lack a sophisticated economic understanding of housing production, the workings of housing markets, and public finance. This causes them to underestimate (or wholly ignore) the filtering mechanism at work in the housing market. For example, Palo Alto's Planning Director has described Palo Alto's inclusionary program as "an example of local government doing its small part to see that some housing is produced in the price ranges needed."86 This statement assumes housing needs must primarily be met with new housing. Yet most moderate-income housing has always been "produced" through filtering. Palo Alto has severely curtailed that more important source of

^{83. &}quot;[Investigators have found] less low-quality housing in areas where there is a high rate of private new housing construction, relative to household formation, even though the private new units are occupied by relatively high-income households who certainly did not live in substandard housing before moving in." J. WEICHER, HOUSING: FEDERAL POLICIES AND PROGRAMS 25-26 (1980).

[&]quot;[T]he filter down process provides higher quality housing for the poor than can be provided by construction of new houses for them." E. MILLS, URBAN ECONOMICS 123 (2d ed. 1980) (emphasis in original).

^{84.} See generally W. GRIGSBY, HOUSING MARKETS AND PUBLIC POLICY (1963); J. LANSING, C. CLIFTON & J. MORGAN, NEW HOMES AND POOR PEOPLE (1969) [hereinafter cited as J. LANSING]; Ohls, Public Policy Toward Low Income Housing and Filtering in Housing Markets, 2 J. URB. ECON. 144 (1975); Sweeney, A Commodity Hierarchy Model of the Rental Housing Market, 1 J. URB. ECON. 188 (1974); White, Multipliers, Vacancy Chains, and Filtering in Housing, 37 J. AM. INST. PLANNERS 88 (1971).

^{85.} See J. WEICHER, supra note 83, at 12-15, 157-58.

^{86.} Knox Letter to the Editor, supra note 59.

supply by adopting a wide variety of antigrowth measures.⁸⁷ Repeal of those measures would do far more than any inclusionary program to increase the "production" of moderate-income housing in Palo Alto.

A lack of appreciation of the dynamics of housing markets is also evident in the "Findings" section of the California Model Inclusionary Zoning Ordinance, which reads in part:

The city finds that the high cost of housing in new developments has exacerbated and will continue to exacerbate the low and moderate income housing shortage by reducing the supply of developable land that is needed to satisfy the total community need for housing for all income levels.⁸⁸

According to this view, if all vacant land were to be built up with luxury housing, that construction would actually do injury to less wealthy families. In fact, however, the filtering effects would be beneficial to the less wealthy.

Moreover, in the long run, these filtering benefits would tend to equal the benefits the less wealthy would receive from new construction of moderate-income housing. Suppose that market forces at work in a city are leading to the production of luxury housing on the city's few remaining vacant tracts. Nevertheless, the city arranges for the construction of subsidized housing units on those sites. This might result in some short-run benefits for moderate-income families. In the long run, however, the city's provision of these low- and moderate-income units would tend to reduce the number of similar units produced through the filtering process. Owners of existing houses and apartments would tend to upgrade (or halt the downward filtering of) their buildings in hight of (1) the increased demand for luxury units arising from the city's frustration of new luxury development; and (2) the decreased demand for their buildings among low- and moderate-income families resulting from the construction of the new, subsidized units. In

^{87.} Under the Palo Alto Comprehensive Plan approved by the City Council on November 29, 1976, the city's large undeveloped bayfront and foothills areas are designated conservation and open-space districts that allow development only at very low densities. Palo Alto has sought for years to prevent housing development in the foothills. This history is recounted in Arastra Ltd. Partnership v. City of Palo Alto, 401 F. Supp. 962, 963-76 (N.D. Cal. 1975), vacated, 417 F. Supp. 1125 (N.D. Cal. 1976). Palo Alto's BMR Program reports that "[n]o non-subsidized apartment developments have been built in Palo Alto since at least 1972." PALO ALTO'S BMR PROGRAM, supra note 19, at 2. Between 1970 and 1980, the population of Palo Alto fell by 1229 persons, making it the only municipality in Santa Clara County to show a population decline during that period. Bureau of the Census, U.S. Dep't of Commerce, 1980 Census of Population, Pre-Liminary Counts.

^{88.} CALIFORNIA MODEL ORDINANCE, supra note 12, § A.

sum, as empirical studies have shown, whatever steps government takes to shape the quality mix of new housing will tend to be offset in the long run by opposite changes in the stock of used housing.⁸⁹

Inclusionists also seem to overlook the presence of filtering in non-residential markets. As noted earlier, for several years the Coastal Commission has held up the construction of two luxury hotels at Marina del Rey in order to assure that at least one of them is redesigned to be in the low budget price range. This effort to increase access to the coast may well have been counterproductive. First, the construction delay would tend to increase hotel rates in the local hotel market in the interim, perhaps more than cancelling out any subsequent short-term access benefits emanating from construction of the hotels. Moreover, like dwelling units, hotels tend to filter downward as they age. The Commission's success in injecting a modest quality hotel into the market would thus tend to slow the downward filtering of other nearby hotels and motels, and therefore, in the long run, might not produce a net increase in the number of modestly priced hotel rooms.

B. THE ECONOMICS OF CONSTRUCTION TAXES

The inclusiomists' lack of economic sophistication has disabled them from making serious assessments of the consequences of the first policy prong of an inclusionary measure—its operation as a tax on the construction of new housing. Inclusionists, of course, are not completely blind to the possibility that the heaping of more and more financial burdens on developers might lead to an increase in housing prices and thus injure consumers. However, they voice optimism that this will rarely occur because they predict that the inclusionary burden will usually simply reduce the developer's profits. 90 Spokesmen for the build-

^{89.} J. WEICHER, supra note 83, at 26:

Of particular interest for housing policy is a finding that government production of subsidized housing for low- and moderate-income households directly has only a short-run effect on the incidence of substandard housing. In the first years after it is built, the subsidized unit appears to generate an improvement in housing quality, but after ten years, the effect disappears.

^{90.} See Coastal Commission Guidelines, supra note 11, at 10; Knox Letter to the Editor, supra note 59; California Model Ordinance, supra note 12, at 2.

The Coastal Commission Guidelines and the Knox Letter to the Editor respectively estimate developer "profits" at 12% and 25% of gross sales. These estimates are highly implausible. Economic theory predicts that, in the long run, the average profits in a competitive industry will be zero, leaving firms just enough revenue to hire the necessary factors of production. See, e.g., J. Hirshleifer, Price Theory and Applications 262-63 (1976); P. Samuelson, Economics 594-95 (8th ed. 1970). If greater profits were available, price cutting firms would enter the market, and compete those profits away. The housing industry is one of the more competitive industries in the American economy. See, e.g., J. Herzog, The Dynamics of Large-Scale Housebullding

ing industry who oppose inclusionary requirements predictably argue that any additional financial burdens on developers will be entirely or mostly passed on to housing consumers.⁹¹ This debate over the incidence of inclusionary burdens has usually proceeded without the aid of economic analysis. Economic analysis, however, as will be shown, indicates that a third group—the owners of undeveloped land—will often bear most of the costs of inclusion.⁹²

Inclusionary requirements are essentially excise taxes on the activity of homebuilding. A tax is imposed both when the developer pays cash as an in-heu fee, and when he is forced to provide inclusionary umits at a financial loss. The amount of the inclusionary tax is reduced to the extent that a developer's losses are offset by a density bonus that would not otherwise be forthcoming to him. The following analysis rests on the assumption that the usual density bonus does not completely offset the tax. The analysis is not applicable to situations in which developers receive net benefits from an inclusionary policy, as is apparently sometimes the case in Orange County.

1. The Relevance of Elasticity of Demand

The basic effects of an excise tax are illustrated by the partial-equilibrium graphs in figures 1 and 2. Because more sophisticated graphic treatments are available elsewhere in the literature, the two figures have been kept as simple as possible.⁹³ In both figures, the net inclusionary tax per unit of new housing is represented by the vertical distance between the pre-tax and post-tax supply curves for housing.⁹⁴

The figures portray hypothetical housing markets in two different

^{(1963).} The rapid escalation of California land prices in recent years has undoubtedly brought large "profits" to many developers who already owned land. This temporary phenomenon should not obscure what seasoned developers know only too well—that homebuilding historically has been an unusually risky type of business endeavor, and that it has recently become even riskier as the regulatory web has become more elaborate.

^{91.} See, e.g., FEASIBILITY, supra note 67, at 12-13; California's Latest Gimnick: Inclusionary Zoning, REAL EST. TODAY, Oct. 1979, at 32.

^{92.} See text accompanying notes 93-95 infra.

^{93.} For a more complete economic and legal analysis of construction taxes, see Ellickson, Suburban Growth Controls: An Economic and Legal Analysis, 86 YALE L.J. 385, 392-403, 450-89 (1977) [hereinafter cited as Suburban Growth Controls].

^{94.} The supply curves in both figures reflect the following assumptions about the applicable market:

⁽¹⁾ The factors other than land that are employed to produce liousing are infinitely elastically supplied; and

⁽²⁾ The supply of land for housing is neither infinitely elastic (because sites are limited), nor infinitely inelastic (because landowners can use their land for farming or other nonhousing uses).

cities. The city portrayed in figure 1 has no unique attributes which would make this city more attractive than neighboring cities to housing consumers. Because housing consumers will perceive the city as having perfect substitutes, they will not be willing to pay a housing price above

Figure 1

The Incidence of a Construction Tax Imposed By a City

With Perfect Substitutes

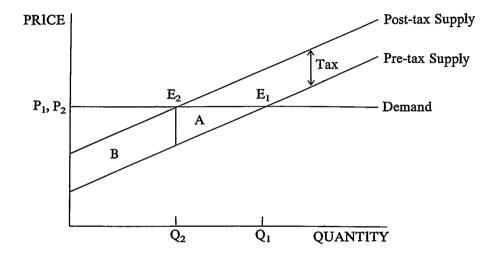
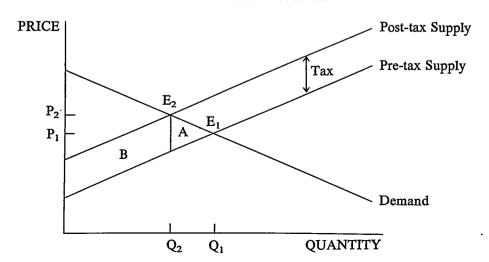


Figure 2

The Incidence of a Construction Tax Imposed By a City

Without Perfect Substitutes



the price prevailing in the regional housing market to live in that city. This means that demand for housing in that city is infinitely elastic, i.e., completely responsive to changes in price. This condition of infinite elasticity is represented in figure 1 by a horizontal demand curve.

The city portrayed in figure 2, by contrast, has unique features (such as location near a university, or an exceptional park system) that are not completely matched in other nearby communities. Some housing consumers would, therefore, be willing to pay more than the prevailing regional price for housing to live in this unique city. This consumer preference results in a demand curve which is somewhat sloped. The consumers who value the special attributes of the community most highly are represented in figure 2 by the uppermost (leftmost) points on the demand curve.

The incidence of an inclusionary tax is different in the two cities. Developers in a city like the one portrayed in figure 1 would be utterly unable to pass on the burden of a construction tax to their consumers. Any developer who did try to raise his price would make no sales because his potential consumers could buy housing at the former price in nearby cities (assumed to be perfect substitutes). In more formal terms, in figure 1 the market price at the post-tax equilibrium (E_2) remains the same as at the pre-tax equilibrium (E_1), i.e., $P_1 = P_2$. On the other hand, once the tax was in effect (or fully anticipated) developers would not bear the tax either. Rather, when bidding for land in a city with an inclusionary program, they would bid less because they would take into account the tax they would later have to pay when they built. The burden would thus be passed backwards to the persons who, at the time the tax became fully anticipated, owned land suitable for residential development.

The situation in figure 2 is more complex. Because some consumers regard the city portrayed in that figure as unique, they can be induced to pay higher housing prices to live there. As a result, in these cities, developers attempting to raise their prices to pass on the costs of an inclusionary tax will meet with some success. In more formal terms, the inclusionary tax in figure 2 would raise the price of housing from P_1 to P_2 , and to that extent the tax would be passed on to consumers. However, the price increase (P_2 minus P_1) is less than the amount of the tax (the vertical distance between the pre-tax and post-tax supply curves). As explained in the discussion of figure 1, the part of the tax

that would not be passed on to consumers would be passed backward to sellers of land suitable for residential development.

The foregoing analysis helps explain why construction taxes are extremely popular with local officials. Future housing consumers and owners of undeveloped land often are not current residents of a city; if they are not residents, then they are not entitled to vote in local elections. Construction taxes thus are less likely than other taxes to antagonize the voters. Moreover, as I have explained in another article, construction taxes imposed on a market like the one portrayed in figure 2 will raise the price not only of new housing, but of used housing as well.95 The price of existing housing would rise because used housing is a perfect substitute for new housing, and owners selling used housing would face less competition from homebuilders. Any increase in usedhousing prices resulting from a tax on new construction would obviously benefit owners of existing residential units, especially those who plan to rent or sell their units in the not too distant future. Homeowners, who constitute a potent political force in many localities, are thus apt to be genuinely enthusiastic about construction taxes.

2. Distributive Justice

To summarize, in the long run, the owners of underdeveloped land bear all of the burden of unusual construction taxes imposed by fungible cities, and part of the burden when the taxing city is unique. The fairness of taxing the site value of selected parcels of land is a matter of some controversy. Those who perceive this consequence of inclusionary programs as fair would emphasize the unusually generous development rights the siteowner may have been given by local zoning officials, the (probably) progressive nature of the tax, and, á la Henry George, the fact that the tax would not discourage any form of productive activity. Those who perceive the burden on landowners as unfair would emphasize that only some (generally voteless) landowners are subjected to site-value taxation, and that the beneficiaries of the tax would be other landowners—the homeowners who would gain both from any increase in the local government's revenue and from any increase in housing prices. Critics of the equity of a construction tax have their strongest case when the landowner has not been granted unusually generous development rights and, therefore, the tax cannot be viewed as a means for recouping zoning windfalls.⁹⁶

^{95.} Suburban Growth Controls, supra note 93, at 392-403.

^{96.} See id. at 438-40 (discussing these arguments in greater detail).

The fairness of construction taxes becomes highly doubtful when the taxing city is unique (as many inclusionary governments seem to be).⁹⁷ Housing consumers unrepresented in the local political process would then be bearing part of the burden of the inclusionary tax.

3. Efficiency

Construction taxes can distort the efficiency of resource allocation. In figure 2, the tax would reduce the amount of new housing produced from Q_1 to Q_2 , and produce a deadweight loss of welfare equal to the triangle marked A. (The revenue produced by the tax, collection costs aside, is indicated by the parallelogram marked B.) Virtually all taxes, however—whether on income, sales, value-added, or whatever—discourage some form of productive activity. Whether a construction tax would create a greater misallocation of resources than some other local tax is thus highly dependent on particularized facts.

In sum, construction taxes are not invariably inefficient. Neither are they invariably inequitable; they become inequitable only when they fall partially on voteless consumers, or on landowners who have not received zoning windfalls. Thus, the first policy prong of inclusionary zoning—the tax on new construction—cannot be condemned out of hand. Unfortunately, inclusionary policies have been most often applied to housing markets (such as that in the coastal zone) that are characterized by downwardly sloped demand curves. In these markets, construction taxes are likely to be less efficient and fair than other available taxes.

C. THE ECONOMICS OF IN-KIND HOUSING SUBSIDIES

The spending prong of an inclusionary zoning policy dispenses in-kind housing subsidies to selected low- and moderate-income families to enable them to live in new housing developments. This spending prong is even more vulnerable to criticism than is the taxation prong.

1. Distributive Justice

a. Vertical equity: As a method of inproving the distribution of wealth, inclusionary zoning must be given low marks. As noted earlier, over 60% of a metropolitan area's households will typically be defined as having either low or moderate incomes. Moreover, most inclusionary programs (such as those in Irvine, Palo Alto, and Orange County)

^{97.} See text following note 132 infra.

^{98.} See text accompanying notes 29-31 supra.

deliver either all or a large majority of their subsidized units to moderate-income families. These families have between 80% and 120% of the county's median family income; at first blush, one might therefore expect incomes of moderate-income beneficiaries to average out at 100% of the county median. Certain features of the selection process, however, increase the probability that these beneficiaries will be clustered toward the top end of the 80% to 120% range. The developer's sale price for an inclusionary unit is typically set at some multiple of the recipient family's annual income. Therefore, to the extent that a developer can control the identity of his occupants, he has a strong incentive to serve the wealthiest portion of the eligible group. This bias is likely to be reinforced by the developer's desire to minimize the degree of economic integration in order to avoid jeopardizing the sale of his unsubsidized units.

Even ambitious agencies such as the Coastal Commission rarely require that more than one-half of inclusionary units be occupied by low-income families. Again, for the reasons just given, developers have strong incentives to serve the low-income families whose incomes are just below 80% of the county median.

Data from Palo Alto support the assertion that inclusionary units tend to be occupied by families with incomes close to the ceiling for eligibility. Twenty-seven of the first forty families to receive inclusionary units in Palo Alto had incomes within 20% of the maximum permitted. Administrators of other inclusionary programs in California have not released statistical profiles of program beneficiaries. Nevertheless, there can be no doubt that the great majority of the California families who have received inclusionary units have had incomes in the middle third of the state's income distribution.

To defend the distribution of massive welfare benefits to the middle class, a proponent of inclusionary zoning might invoke trickledown arguments. The proponent might contend that a somewhat shorter chain of moves links the moderate-income and low-income housing markets, than links the high-income and low-income markets. If so, when moderate-income households move from their prior dwelling units into inclusionary units, the freeing up of their old units con-

^{99.} Palo Alto Housing Corporation, Profile of Purchasers at viii (1977). A city official attributes this pattern to the fact that only families with incomes near the limit of 120% of county median income can both afford the monthly payments and also qualify for loans. Telephone Interview with Glenn Miller, Planning Department, City of Palo Alto (Dec. 2, 1980). Palo Alto is considering raising its income ceiling to 150% of the county median. See note 30 supra.

fers more immediate benefits on low-income families than those families would receive from the construction of housing for high-income families.

Although this argument may have some validity, it lacks force for two reasons. First, poor families that benefit from accelerated filtering still have to pay the full market price to move into the units freed by filtering. ¹⁰⁰ If the overriding purpose of inclusionary programs is to help *poor* people, government is ill advised to subsidize the housing outlays of only non-poor families. Second, proponents of inclusionary zoning enter dangerous terrain when they recognize that filtering takes place in the housing market. The better filtering works, the more suspect the entire idea of inclusionary zoning becomes. All chains of moves caused by new housing construction eventually tend to free units at the bottom end of the market. Even when luxury units start the chain, the chain is likely to be complete in a year or two. ¹⁰¹ Can one justify the expenditure of tens of thousands of dollars per chain just to shorten the length of the chain by a matter of months?

b. Horizontal equity: Even if one could be persuaded of the virtues of subsidizing members of the middle-class, one might remain doubtful about the justness of a program that confers benefits on only a tiny fraction of the eligible population. For example, in seven years of operation (from 1973 to 1980), Palo Alto's inclusionary program produced a total of fifty-seven inclusionary units, all for moderate-income families.¹⁰² In 1969, the latest year for which census data on incomes are available, the incomes of Palo Alto families were distributed as follows:¹⁰³

^{100.} These families would benefit to whatever extent the accelerated filtering reduced the market price of the housing they consumed.

^{101.} The chains of moves triggered by sales of new houses average 3.5 moves. J. LANSING, supra note 84, at 12-16. Typically, the chain takes a year or two to complete. Id. at 98.

^{102.} Knox Letter, supra note 25. As of January 1981 seven more units were under construction. Id.

^{103.} Data from Bureau of the Census, U.S. Dep't of Commerce, 1970 Census of the Population [heremafter cited as 1970 Census].

Income Range	Number of Families	Percent
Below \$5,000	1,186	8.4
\$5,000- \$9,999	2,775	19.6
*\$10,000-\$14,999	3,088	21.8
\$15,000-\$24,999	4,909	34.7
\$25,000 and over	2,175	<u>15.4</u>
	14,133	100.0%

In 1969, the median family income in Palo Alto's county (Santa Clara) was \$12,456. The moderate-income (80% to 120%) range around this figure would be \$9965 to \$14,947, or approximately the range in the asterisked line in the table. Thus, if the income distribution of Palo Alto families did not change during the 1970's, roughly 3088 resident families were eligible for Palo Alto's fifty-seven units for moderate-income families. Hence, less than one eligible family in fifty received the benefits of Palo Alto's subsidy, which, in some instances, was an entitlement to purchase a housing unit for \$60,000 below market value. 104

Palo Alto's penetration rate of less than 2% in seven years is not unexpected for a largely developed city which has only a modest amount of new housing construction to tax. In a developing area, there is more construction and the penetration rate might be considerably higher. Nevertheless, as the number of applications for Orange County projects shows, it is inconceivable that any inclusionary government could come close to serving all its eligible families in the foreseeable future.

A low penetration rate has plagued all types of in-kind housing subsidy programs from the New Deal public housing program onward. This problem is not cured by the passage of time because, even if one heroically assumes that all eligible families will eventually be served, some families will have been served decades earlier than others. Unless the last served receive truly luxurious units, the first served will have received benefits of much greater present value.

There is no satisfactory solution to this dilemma. Lotteries are the

^{104.} The discussion in the text actually exaggerates Palo Alto's penetration rate in two ways. First, the table only shows numbers of "families," that is, households of two or more persons related by blood, marriage, or adoption. Close to one-quarter of Palo Alto's inclusionary umits have been occupied by one-person households. Palo Alto Housing Corporation, Profile of Purchasers at vii (1977). Census data indicate that at least another 1000 "unrelated individuals" in Palo Alto would qualify as being of "inoderate income." Second, nonresidents who work in Palo Alto are also eligible for the city's inclusionary units. In fact, 13 of the first 40 beneficiaries were nonresidents. Id. For these two reasons, Palo Alto's actual penetration rate among eligible resident families may be as little as one-half the rate indicated in the text.

least corruptible system for allocating the scarce units among the pool of eligible families, but the use of lotteries publicizes the randomness of the benefit distribution. Allocation by queue is less visible, but is subject to manipulation by whoever controls the hist of eligibles. For example, developers might conceivably leak word of a forthcoming project to their employees; officials of nonprofit housing organizations might tip off their most loyal members; politicians might reward their campaign volunteers and contributors; and civil servants might sell out to whoever offers the largest kickback. The beneficiary selection processes used by inclusionary governments could be fertile ground for investigative reporters.

2. Efficiency

The spending prong of an ambitious inclusionary zoning program has three features. It distributes (1) in-kind housing subsidies (2) to achieve economic integration (3) in (mainly) new buildings and subdivisions. This subsection shows that each of these three features is of doubtful value when judged by the goal of efficiency in resource allocation.

a. The presumptive inefficiency of in-kind housing subsidies: The im-kind housing subsidy programs that have dominated United States housing policy since the 1930's are increasingly viewed as inferior to housing allowances (or other cash subsidies) that would assist program beneficiaries in procuring their own accommodations through the private housing market. Because the in-kind programs require the services of government employees to pair particular families with particular units, administrative costs are typically higher for in-kind programs than for cash distribution programs. Moreover, when subsidized units are readily distinguishable from private market units (as is only sometimes the case with inclusionary units) the program beneficiaries are publicly stigmatized as they would not be if they received cash. Most important of all, in-kind housing subsidies are, by definition, not transferable by program beneficiaries. A beneficiary who became entitled to purchase a \$100,000 inarket-value condominium for \$40,000, for exam-

^{105.} See, e.g., H. AARON, SHELTER AND SUBSIDIES 44-47, 159-73 (1972); R. MUTH, PUBLIC HOUSING: AN ECONOMIC EVALUATION 2-3 (1973): R. STRUYK & M. BENDICK, JR., HOUSING VOUCHERS FOR THE POOR: LESSONS FROM A NATIONAL EXPERIMENT (1981); AARON & VON FURSTEINBURG, The Inefficiency of Transfers in Kind: The Case of Housing Assistance, 9 W. ECON. J. 184 (1971); Frieden, Housing Allowances: An Experiment That Worked, Pub. Interest, Spring 1980, at 15. See also President's Committee on Urban Housing 71-72 (1968) (Kaiser Committee Report) (urging federal experiment with housing allowances).

ple, might value the condominium at some intermediate figure—say \$75,000. The prohibition on transfer would create a deadweight loss of \$25,000—the gain the beneficiary would have realized (ostensibly to no one's detriment) if he could have cashed out the in-kind subsidy by selling the unit at market value. ¹⁰⁶ In other words, if the beneficiary had originally received \$60,000 in cash rather than the \$60,000 discount on the condominium, the beneficiary would never have chosen to purchase that particular condominium, but would have spent the money in other ways which would have brought him more personal satisfaction. In short, whenever government dispenses nontransferable in-kind subsidies, it is either (1) acting paternalistically on the assumption that the beneficiaries are incapable of spending wisely, or (2) seeking to achieve some goal *other* than the maximization of beneficiary welfare.

Proponents of in-kind housing subsidization may argue that housing is a "merit good" and that governments should encourage citizens to consume more housing than they would otherwise choose to consume. ¹⁰⁷ This argument, however, lacks force in the context of inclusionary zoning because most program beneficiaries are typical middle-class households whose consumption decisions are not normally second guessed. Moreover, eligibility for program benefits is not restricted to particular subcategories of the target population (such as families with many children) that might arguably be especially likely to make "incorrect" consumption decisions.

Nor can in-kind housing subsidies be persuasively justified on the ground that the improvement in a household's housing conditions benefits the household's neighbors by reducing risks of disease, crime, or other social pathologies. This facially plausible justification, once used to support the early federal public housing programs, has since proved lacking in empirical support. Better housing does not, in itself, seem to generate measurable external benefits. Even if it did, the main thrust of inclusionary zoning—moving middle-income households from average-quality units to superior-quality units—would not remedy the social pathologies emanating from the circumstances of slum housing.

Some economists have argued that in-kind subsidies may provide

^{106.} As William Fischel has perceptively noted, a poorly drafted resale-control formula will not only create the deadweight loss mentioned in the text, but also invite the beneficiary to undermaintain his unit. See note 62 supra.

^{107.} The concept of a merit good is critically examined in R. Musgrave & P. Musgrave, Public Finance in Theory and Practice 65-66 (2d ed. 1976).

^{108.} See J. WEICHER, supra note 83, at 5-8.

more satisfaction to donors than would distribution of the same amount of cash subsidies. For example, Salvation Army workers may get more satisfaction from giving hot soup, rather than the cash equivalent, to skid row bums. Indeed, officials who administer inclusionary programs seem to be extraordinarily proud of the subsidies they have dispensed. Being able to point to a specific building as a monument to one's munificence apparently makes one happier than being able to point to a cancelled check. A similar bricks-and-mortar mentality is often encountered by university fundraisers. Thus, the main advantage of in-kind housing subsidies over cash housing subsidies may be that in-kind subsidies make housing officials happier.

b. The uneasy case for the economic integration of neighborhoods: The second noteworthy feature of the spending prong of the most ambitious inclusionary efforts, such as the Palo Alto and Coastal Commission programs, is that the in-kind housing subsidies are allocated to achieve the residential mixing of different income groups, not only within neighborhoods, but also within specific subdivisions and buildings. 110 Avid inclusionists perceive economic integration to be efficiency enhancing. They seem to believe that the injection of hillbillies into Beverly Hills will reduce interclass tensions, enhance the human understanding of all concerned, and help reduce social pathologies that may arise when different income groups are spatially separate. The view that economic integration is desirable is apparently shared by the Kerner Commission, Anthony Downs, and many other prestigious commentators. 111 These commentators, however, have usually been most concerned about the residential isolation of the very poor (and particularly black) families whose members might suffer from lack of access both to jobs and to schools dominated by a middle-class ethos. Because inclusionary zoning as practiced in California serves a largely middle-class and (apparently) mostly white clientele, it will do little to remedy these most basic concerns.

More significantly, it is hardly clear that there are, in fact, net social benefits from the residential integration of different income

^{109.} See A. Alchian & W. Allen, University Economics 148-50 (3d ed. 1972).

^{110.} Irvine and Orange County do not attempt to achieve the integration of different income groups at the block level. See text accompanying notes 73-76 supra.

^{111.} See, e.g., A. Downs, Opening Up the Suburbs (1973); C. Haar & D. Iatridis, Housing the Poor in Suburbia 14-17 (1974); Report of the National Advisory Commission on Civil Disorders 263 (1968) (the Kerner Commission Report); L. Rubinowitz, Low-Income Housing: Suburban Strategies 9-25 (1974).

groups.¹¹² In 1973, a panel of experts assembled by the National Academy of Sciences concluded that:

At present, the desirability of intervention to foster socioeconomic mixing in residential areas is uncertain. In question are not only the possible benefits, but untested assumptions concerning the amount and kind of present interaction across socioeconomic lines.

There is no evidence from field studies that socioeconomic mixing is feasible. The trend in the movements of urban populations is toward increasing separation of socioeconomic categories—a tendency manifested among blacks as well as among whites. 113

This trend is a clue that upper-income groups disvalue the proximity of lower-income groups more than lower-income groups value the proximity of upper-income groups.¹¹⁴ If the opposite were true, then one would sometimes find developers voluntarily choosing to integrate different income groups within the same project. For example, an apartment builder might then find he could maximize profits by sprinkling a few cheaply finished, lower-rent apartment units in each of his buildings. These units would command higher rents than similar units in more modest buildings because lower-income groups would pay a premium to be able to live with those more affluent. If economic integration were efficient, the added profits from the cheaply finished units would exceed any drop in the rental revenue from the high quality units.

The actual practices of developers and other real estate operatives strongly suggest that economic integration is generally not efficient. Homebuilders seem to have learned from experience that their eco-

^{112.} Hawley & Rock, *Introduction* to SEGREGATION IN RESIDENTIAL AREAS 20 (A. Hawley & V. Rock eds. 1973); Mannett, *Social Stratification in Urban Areas*, in SEGREGATION IN RESIDENTIAL AREAS 172-88 (A. Hawley & V. Rock eds. 1973).

^{113.} Hawley & Rock, supra note 112, at 20. See also Mark, Boehm & Leven, A Probability Model for Analyzing Interneighborhood Mobility, in THE ECONOMICS OF NEIGHBORHOOD 43, 50 (D. Segal ed. 1979) (The more a family's income exceeds mean neighborhood income, the more likely the family will move out of the neighborhood.).

^{114.} Cf. R. MUTH, CITIES AND HOUSING 106-12 (1969) (hypothesizing that the preferences of whites to live apart from blacks are stronger than the preferences of blacks to live close to whites).

The earliest students of urban spatial structure observed that different income groups tend to live in different neighborhoods. They developed competing models of this fundamental residential pattern. See The City 48-62 (R. Parks & E. Burgess eds. 1925) (different income groups cluster in separate concentric zones); H. Hoyt, The Structure and Growth of Residential Neighborhoods in American Cities (1939) (different income groups cluster in separate pieshaped sectors). See generally A. Speare, S. Goldstein, & W. Frey, Residential Mobility, Migration, and Metropolitan Change (1975); Hoyt, Where the Rich and the Poor People Live, 5 Urb. Land Inst. Tech. Bull. No. 551 (1966).

nomic survival requires them to target each of their projects at a rather narrow stratum of the housing market. For example, when Levitt & Sons decided in the 1960's to offer a somewhat higher priced line of single-family houses at its massive ongoing development at Willingboro, New Jersey, it situated those houses in a separate area that it named "Country Club Ridge." Similarly, real estate brokers who work in established neighborhoods know that a house that is much superior to adjacent houses will tend to sell for less than it should; therefore, they caution homeowners against overimproving. Apparently, the Joneses not only want to keep up with their neighbors, but the Joneses want their neighbors to keep up with them.

The fact that market forces tend to produce economically stratified neighborhoods creates a prima facie case that this stratification is efficient. Efficiency, in this context, means that if residency rights were fully transferable, richer residents would generally be willing to pay enough to persuade poorer residents to move to other neighborhoods. To overcome the prima facie evidence of efficiency, an inclusionist would first have to identify significant benefits from economic integration of a project that would accrue to persons living *outside* the immediate project, and, second, would have to show that a Levitt & Sons (for example) would be likely to ignore those benefits when it chose to stratify its subdivisions. The conceivable external benefits of economic integration—perhaps greater interclass harmony or the destruction of the critical masses necessary for the survival of lower-class cultures—would, of course, be extremely difficult to quantify.

Significantly, many social scientists doubt that there are net benefits from economic integration. Some of the most ardent proponents of "opening up the suburbs" are also quite skeptical of the feasibility (and desirability) of economic integration at the block level. For example, Anthony Downs has been mainly concerned with giving poor households better access to jobs and to schools dominated by a middle-class ethos. He therefore would prefer that the neighborhood serving any particular elementary school be economically integrated. For several reasons, however, he is extremely cautious about pushing economic integration at the block level where there would be daily per-

^{115.} This is the Kaldor-Hicks test for efficiency. Cf. Lewis v. Gollner, 14 N.Y.S. 362 (Brooklyn City Ct.), rev'd, 129 N.Y. 227, 29 N.E. 1 (1891) (homeowners in a fashionable area of Brooklyn bought off a developer who planned to build tenements in their neighborhood).

^{116.} See W. GRIGSBY & L. ROSENBERG, URBAN HOUSING POLICY 113-27 (1975); notes 112-13 and accompanying text supra.

^{117.} A. Downs, supra note 111, at 87-102, 166-67.

sonal interaction among households.¹¹⁸ First, he fears that the higher-income families would flee unless they were confident that their group was dominant. Second, he suspects that most poor families prefer being immediately surrounded by families in their own income group rather than by richer families.¹¹⁹ If Downs' second suspicion is correct, inclusion-ary programs that aim at economic integration at the block level could produce block populations that would please neither the subsidized families nor the unsubsidized families.

The eminent sociologist Herbert Gans, after an empirical study in 1960-1961 of Willingboro, New Jersey, made prescriptions similar to Downs'. 120 He speculated that "the optimum solution, at least in communities of homeowners who are raising small children, is selective homogeneity at the block level and heterogeneity at the community level." 121

Downs and Gans would honor consumer preferences for economic separation at the block level, but would overrule them at the neighborhood level. At the extreme, all neighborhoods in a Downs-Gans world would have similar population profiles—each with a mixture of some rich and some poor, some old and some young, some black and some white, and so on. Government would see to it that more homogeneous neighborhoods did not evolve. Ultimately, there would be no Chinatowns, no retirement communities, and no gay neighborhoods. As a result, consumers would have considerably fewer choices among neighborhoods than they currently do.

All major American cities contain some economically integrated neighborhoods: for example, Manhattan's West Side, Chicago's Hyde Park, Washington's Capitol Hill, Los Angeles' Venice. Households, rich or poor, with a strong preference for living in these neighborhoods, can do so today. Or, if they prefer, they can seek out a more homogeneous neighborhood. Plaimers should be hesitant to deprive households of their current rich menu of neighborhoods for the uncertain, perhaps nonexistent, benefits of universal economic integration.

^{118.} Id. at 109-11.

^{119.} Id. at 110. Cf. W. GRIGSBY & L. ROSENBERG, supra note 116, at 100. The authors report survey results indicating that most low-income families prefer living in neighborhoods containing large numbers of low-income families. The survey showed that enough low-income families had a suburban preference for Grigsby and Rosenberg to recommend "consideration of limited provision of low-income accommodations in the suburbs." Id. at 102. But see id. at 113-27.

^{120.} H. Gans, The Levittowners 165-74 (1967).

^{121.} Id. at 173 (emphasis in original).

Moreover, even if the goal of neighborhood heterogeneity espoused by Downs and Gans were worthy of pursuit, the typical inclusionary zoning program may do precious little to achieve it. The distribution of family incomes in the suburban city of Palo Alto is already remarkably wide. 122 This pattern results in part because a household's income in a particular year may vary widely from its "normal income,"123 and because of differences in household wealth. The large numbers of "low- and moderate-income families" already living in Palo Alto are probably headed mostly by middle-class persons who are elderly, divorced, currently unemployed, or studying at Stanford University. There is evidence that young families and families headed by females tend to be overrepresented among the beneficiaries of inclusionary programs. 124 Downs and Gans are interested in the residential integration of truly different socioeconomic classes. Because inclusionary ordinances define eligibility according to annual income, an often unreliable indicator of class status, even a facially ambitious ordinance may produce little true socioeconomic integration.

c. Should new buildings and subdivisions bear the brunt of economic integration?: The third salient feature of the Palo Alto and Coastal Commission programs is that they primarily seek economic integration of new subdivisions and buildings. This feature is not inevitable. For example, the revenues raised from taxing new construction could readily be spent by an inclusionary government to enable low-and moderate-income families to purchase existing housing units in older subdivisions or buildings. For obvious political reasons, however, an inclusionary government eager to pursue real class integration will almost invariably decide that unidentified future residents of new housing projects, rather than current homeowners and tenants, should have the consciousness raising experience of economic integration at the block level.

Recall that even social reformers such as Downs and Gans have recognized that heterogeneity at the block level is disfavored by most consumers. The fact that inclusionists mainly seek to integrate new subdivisions and buildings suggests that they are actually motivated by exclusionary purposes. The inclusionists first tax new development

^{122.} See note 104 and accompanying text supra.

^{123.} See M. REID, HOUSING AND INCOME 826 (1962). Cf. Creedy, Income Averaging and Progressive Taxation, 12 J. Pub. Econ. 387 (1979) (suggesting a scheme for the assessment of income tax based on income averaging).

^{124.} See notes 54-56 and accompanying text supra.

through the revenue raising prong by putting heavy financial burdens on developers, and then they tax new development a second time through the spending prong by making new subdivisions and buildings relatively less appealing to consumers. (The severity of the second tax is of course lessened when the inclusionary government adheres to the usual practice of allocating most inclusionary units to moderate-income families.) This double tax on new construction will almost invariably reduce the quantity of new housing produced. Moreover, when an inclusionary community lacks perfect substitutes, the double tax can significantly raise the price of existing housing units, partly because homebuyers will tend to bid more for units that are not burdened by what they regard as an undesirable social environment. Viewed most cynically, inclusionary zoning appears to be a clever double tax on new construction that existing homeowners and landlords have devised largely in order to augment their own wealth.

3. Net Effects on the Welfare of Moderate-Income Families

Households that actually receive inclusionary units are unquestionably helped by inclusionary zoning. However, the fact that these households gain does not necessarily mean that inclusionary zoning improves the welfare of low- and moderate- income families in the aggregate. The eligible class unmistakably gains as a whole only when the inclusionary government has perfect substitutes (that is, the price elasticity of demand for housing is infinite). In such communities inclusionary zoning will not raise housing prices to the detriment of nonbeneficiaries; rather, the program will essentially transfer wealth from owners of underdeveloped land to the households lucky enough to be chosen from the long eligibility list. 127

By contrast, when an inclusionary government faces a downwardly sloped demand curve for housing, the members of the eligible class who do not receive units are hurt by the program. In these communities, the double tax on new housing construction enables owners of existing units to raise their prices and rents because competition from builders marketing new units has been stifled. The inclusionary pro-

^{125.} Saddling new housing with special environmental burdens causes the demand curve for new housing to shift downward and to the left. This shift produces results similar to the consequences of a direct tax on housing production. The shift reduces local housing production, impairs the welfare of local housing suppliers; and, sometimes, impairs the welfare of consumers.

^{126.} Recipients would typically be even better off if given an equivalent amount of cash. See text accompanying notes 105-07 supra.

^{127.} See text accompanying notes 93-95 supra.

grain of the California Coastal Commission has probably increased the price of existing modest-quality housing located in the coastal zone. Therefore, it is possible for an inclusionary program to reduce the aggregate wealth of the members of the eligible class; the dollar losses sustained by the nonbeneficiaries may outweigh the dollar gains received by the beneficiaries.

This important conclusion can be illustrated by example: Suppose that an inclusionary program burdens new housing construction with a tax that is so high that new construction is completely snuffed out. 128 There would then be no program revenues and no moderate-income families would ever receive inclusionary units. If the community were unique, however, the cessation of new housing construction would raise the price of existing housing units, thereby harming many moderateincome families. On balance, moderate-income housing consumers would have been made worse off by a program that had nominally been designed for their benefit. Similarly, if Palo Alto is regarded as a unique city by consumers, the benefits received by that city's fifty-seven inclusionary families may have been outweighed by the costs inflicted on moderate-income families in Palo Alto who are not beneficiaries. Only a careful econometric study of the Palo Alto housing market could determine whether the moderate-income group gained in the aggregate. The matter is sufficiently clouded for the California Department of Housing and Community Development to reconsider its current blanket assertion that "the adoption of [an inclusionary] ordinance represents a substantial local effort toward solving the housing crisis."129

III. POLITICAL EXPLANATIONS FOR THE EMERGENCE OF INCLUSIONARY ZONING

The leading inclusionary municipalities—Irvine, Palo Alto, Davis, and Del Mar—are hardly a random sample of California cities. First, the permanent residents of these cities are relatively prosperous.¹³⁰ Sec-

^{128.} New construction may already have been brought to a standstill in some places in California:

[[]W]e have examples in which our members have indicated their abandonment of projects which had been planned, but which are no longer feasible because of inclusionary requirements and other government exactions. Not only are individual projects being abandoned, but there is evidence that entire jurisdictions are boycotted by the development industry because of their requirements.

Rivinius Letter, supra note 43.

^{129.} CALIFORNIA MODEL ORDINANCE, supra note 12, at 2.

^{130.} According to the 1970 Census of Populatiou, in 1969 the median family income in California was \$10,732. 1970 Census, *supra* note 103. The comparable figure for Davis was \$11,858;

ond, the list contains an overrepresentation of university towns, and, relatedly, of centers of environmentalist and antigrowth sentiment. These common characteristics may reveal something about the political conditions that are conducive to the emergence of inclusionary zoning.

Professor Frank Michelman has recently identified two polar conceptions of local government behavior. The first, the "public interest" model, views local officials as selflessly seeking to define and achieve community ideals. The second, the "self interest" model, regards all the persons on the political stage—voters, bureaucrats, and elected officials—as self-serving actors seeking to maximize their own welfare, even at the expense of others.

A. THE PUBLIC INTEREST MODEL

It is difficult, but not impossible, to square the emergence of inclusionary zoning with the public interest model. The task is easiest in Orange County, where local politicians have used the rallying cry of "affordable housing" as their justification for loosening inefficient zoning restrictions that might otherwise have proved politically impossible to amend. Unlike the other inclusionary programs discussed, Orange County's program does not necessarily constitute a tax on new housing construction because the sale prices of inclusionary units are not invariably controlled, and because the County does not pursue economic integration at the block level.

In the other jurisdictions discussed (where inclusionary programs do operate as a tax) the chief piece of positive evidence supporting the public interest model is the unquestionable idealism of many of the persons who advocate and administer the programs. They appear to be well-motivated people who are in fact trying to move toward a more just society. Many advocates of inclusionary programs see themselves essentially as Robin Hoods who are snatching away outrageously large developer profits for distribution to the deserving. Most of them display great confidence that their efforts represent an important solution to the so-called housing crisis.

If the analysis in this Article is correct, however, the inclusionists outside Orange County are, at best, wasting taxpayer money, and, at worst, acting in a manner counterproductive to their own purposes.

for Del Mar, \$13,378; and for Palo Alto, \$15,036. *Id*. (Irvine was not yet incorporated as a city in 1970.)

^{131.} Michelman, Political Markets and Community Self-Determination: Competing Judicial Models of Local Government Legitimacy, 53 Ind. L.J. 145 (1978).

Consequently, true adherents of the public interest model would be compelled to describe the inclusionists' endeavors as honest mistakes in judgment. The public interest model would optimistically predict that as soon as the inclusionists recognize the error of their ways, the inclusionary programs would be repealed, just as Congress has recently started to dismantle mistaken regulatory programs governing airlines, lending institutions, and broadcasters. 132

B. THE SELF-INTEREST MODEL

The self-interest model, by contrast, would attribute the emergence of inclusionary zoning to the benefits it confers on the most influential political actors in inclusionary jurisdictions. This alternative model would predict that an inclusionary program would continue, even if it were not in the public interest, so long as it served the narrow interests of the politically powerful.

Many features of inclusionary zoning square nicely with the self-interest model. Irvine, Palo Alto, Davis, and the other inclusionary governments tend to be communities without perfect substitutes. The three cities just listed, for example, are all university towns—the natural homes for partially captive university employees. Del Mar, a small elite city on the coast, can understandably aspire to become another Carmel or Newport Beach and, like the other inclusionary cities, may also face a downward sloping demand curve for housing. In communities like these, inclusionary zoning's double tax on housing construction can be expected to raise the value of existing houses. The inclusionary programs are, therefore, in the narrow self-interest of the homeowners who constitute a major, if not the major, interest group in these cities.

The burdens of inclusionary efforts, by contrast, fall largely on potential homebuyers and on owners of undeveloped land. The consumer group is inchoate and impossible to organize. Landowners also have little or no voting strength in local elections. Although landowners can obtain some political influence via campaigu contributions, in California political contributions must be publicized and candidates in antigrowth communities tend to fear being identified with land developers. Only in large and diverse local arenas, such as Orange County, is it possible for landowners to become a dominant political force. In

^{132.} Cf. Levine, Revisionism Revised? Airline Deregulation and the Public Interest, 44 L. & CONTEMP. PROB. 179 (1981) (suggests a modified public interest model of regulation in which public officials do try to enhance the general welfare, but are sometimes co-opted by special interests).

most small municipalities, the losers from inclusionary zoning are virtually certain to lose more than the winners gain, but the losers tend to be politically weaker than the winners.

Other scraps of evidence support the cynical view that inclusionary zoning is usually an exclusionary tactic designed to enrich current homeowners. Fairfax County, Virginia, the first locality to experiment with inclusionary zoning, was, at that time, dominated by antidevelopment politicians who were pursuing a wide range of antigrowth policies. The fact that inclusionary zoning programs seek to integrate mainly new buildings and subdivisions is a persuasive clue that the programs have been framed with the interests of current homeowners principally in mind.

Although current homeowners unquestionably gain from the imposition of charges on developers, it is not obvious why the homeowners' self-interest would lead them to squander the revenues generated by these charges on massive housing subsidies to selected middle-income families. In other words, the spending prong of inclusionary zoning is harder to square with the self-interest model than is the revenue raising prong. Apart from whatever satisfaction they may derive from being charitable, or relieving guilt, however, the homeowners do gain in two ways from the spending prong. First, as shown above, the imposition of inclusionary requirements on new subdivisions and buildings can operate as a second tax on new housing construction by making the new construction less appealing to consumers. 134

Second, homeowners and their representatives may be attracted to inclusionary zoning because it promises to be one of the exclusionary techniques least vulnerable to legal attack. In the past some judges have been fooled into thinking that all self-proclaimed inclusionary programs are, in fact, inclusionary. The chief example of this judicial naiveté is Construction Industry Association v. City of Petaluma, 135 the Ninth Circuit's well-publicized decision that rejected various constitutional challenges to the so-called Petaluma Plan. The Plan established an annual quota on the aggregate number of new housing units that developers could build in Petaluma each year. In allocating the quota among developers, the Petaluma Plan gave plus-points to proposed developments which would include units for low- and moderate-income families. This feature probably discouraged developers from applying

^{133.} See M. Danielson, The Politics of Exclusion 65-66, 68-69 (1976).

^{134.} See text accompanying note 125 supra.

^{135. 522} F.2d 897 (9th Cir. 1975).

to build in Petaluma, and may help explain why, in most years, Petaluma failed to achieve the Plan's quota of housing production. Petaluma failed to achieve the Plan's quota of housing production. Nevertheless, the Ninth Circuit was blind both to the negative repercussions the inclusionary element might have on the supply of new housing in Petaluma, and to the ultimate effect of the inclusionary element on the supply of used housing through filtering. The court thought that the inclusionary element ensured that the Petaluma Plan would be an unqualified boon for low- and moderate-income families. The court stated that the Plan stood in "stark contrast" to the exclusionary programs characteristic of so many suburbs. In short, inclusionary zoning promises to be useful to homeowners as a legal cover for their exclusionary practices.

As listed above, the third fundamental structural feature of an inclusionary zoning program is the direct linkage between the revenue raising prong and the spending prong—that is, the bypassing of normal legislative oversight over the appropriation of the revenues raised. This direct linkage prong can also be seen as serving the self-interest of influential participants. First, as just noted, the pairing of a "suspect" revenue raising program with a "benign" spending program may help persuade courts to sustain the legality of the suspect feature.

Second, a small but influential interest group greatly benefits from this shortcircuiting of the local legislative body. This group consists of those who may be called professional housers. These persons, many of them trained in law or urban planning, have the self-defined mission of improving housing conditions by intervening in various ways in private housing markets. They may be employed by local planning departments, nonprofit housing groups, or development corporations which produce subsidized housing. The skills of professional housers lie in securing the bureaucratic approvals needed for construction and occupancy of subsidized housing units. The significant fact about professional housers is that their place in the sun depends on the continued appropriation of in-kind housing subsidies for low- and moderate-income families. By the late 1970's the natural sources of these subsidies seemed to be drying up. In 1973, after disappointing results in the early 1970's, the federal government placed a moratorium on its major hous-

^{136.} See Schnidman, Continued Development in an Atmosphere of Growth Management, ENVT'L COM., Aug. 1977, at 12-13.

^{137. 522} F.2d at 905.

^{138.} Id. at 908 n.16.

ing subsidy programs.¹³⁹ Thereafter, Congress funded the main successor program, Section 8, at less ample levels than before.¹⁴⁰ Moreover, voter approval of Proposition 13, in 1978, ultimately left California and its municipalities with little discretionary revenue to spend. These political events were understandably threatening to professional housers, who may have glimpsed some measure of relief in inclusionary zoning. It is the professional housers who now draft proposed inclusionary ordinances, and attend public conferences to discuss the fine points of their programs.

Professional housers have a strong interest in bypassing a local legislature's review of appropriations for housing subsidies. The Palo Alto City Council, for example, might balk at spending \$60,000 to help one moderate-income household buy one condominium; the Council might instead choose to use the \$60,000 to buy three police cars or three thousand library books. By drafting inclusionary ordinances to preclude subsequent city council review of spending on subsized housing, professional housers, like the highway builders¹⁴¹ and the landmark preservationists, have devised a politically insulated financing system that helps them achieve their personal objectives. 143

Which model, public interest or self-interest, better explains the phenomenon of inclusionary zoning (at least as practiced outside Orange County)? Neither explanation is completely satisfying. However, the telling fact that inclusionary programs have tended to flourish in otherwise exclusive communities, where the program's effects are likely to be exclusionary, seems most consistent with the self-interest model. One would expect mere mistakes in policy to happen more randomly.

^{139.} See Pennsylvania v. Lynn, 501 F.2d 848 (D.C. Cir. 1974) (sustaining administrative moratorium on housing subsidy programs); J. WEICHER, supra note 83, at 44-48.

^{140.} See J. WEICHER, supra note 83, at 43-44, 66-67.

^{141.} See Schwartz, Urban Freeways and the Interstate System, 49 S. CAL. L. REV. 406 (1976) (discussing the evolution of highway trust funds that automatically channel revenues raised from the taxation of gasoline sales into expenditures on highway construction and maintenance).

^{142.} See F. JAMES & D. GALE, ZONING FOR SALE 31-34 (1977) (analyzing transferable-development-rights plans as schemes to establish trust funds for historic preservation or other purposes).

^{143.} The interests of professional housers provide the best self-interest-model explanation for the receut actions by the cities of Palo Alto and San Francisco to tax nonresidential construction to raise housing subsidy funds. See notes 25-26 and accompanying text supra. The taxation of commercial and industrial development does not directly stifle residential construction. These taxes are thus less advantageous to current homeowners than taxes on new housing construction. Professional housers, however, if they were interested in maximizing the money they had to spend, would be as eager to tax nonresidential development as to tax residential development.

IV. POSSIBLE LEGAL CHALLENGES TO INCLUSIONARY ZONING

Legal journals already contain a number of detailed analyses of the legality of inclusionary programs. 144 The principal legal issues are (1) whether a local government has the power to adopt such a program; and (2) whether the spending and revenue raising prongs in combination constitute an unconstitutional taking of a developer's property without just compensation. In California there is an important third issue: whether Proposition 13 requires voter approval of inclusionary "taxes" on developers. These three issues are briefly discussed below.

A. MUNICIPAL POWER

In Board of Supervisors v. DeGroff Enterprises, 145 the Virginia Supreme Court struck down Fairfax County's pioneering inclusionary program on the ground, among others, that the Virginia legislature had not authorized its local governments to regulate the identity of housing occupants (as opposed to the physical characteristics of buildings). No state supreme court in the United States is more restrictive in interpreting local government powers, and more expansive in interpreting landowner rights, than the Supreme Court of Virginia. Although DeGroff remains the best known reported decision on inclusionary zoning, one must be wary of exaggerating its relevance in other states. Nonetheless, in two decisions not precisely on point, the state supreme courts of Massachusetts and New Jersey expressed concern about whether their local governments were empowered to initiate inclusionary zoning programs. However, in the most recent decision on the issue, Uxbridge Associates v. Township of Cherry Hill, 147 a trial court in New Jersey decided the power issue in favor of the inclusionary mumicipality.

In California, inclusionary governments should currently have little problem prevailing on the power issue. The California Constitution grants broad powers to both chartered and general law cities to adopt

^{144.} See Kleven, supra note 9. See also Fox & Davis, supra note 9; Pazar, Constitutional Barriers to the Enactment of Moderately Priced Dwelling Unit Ordinances in New Jersey, 10 Rut.-Cam. L. Rev. 253 (1979).

^{145. 214} Va. 235, 198 S.E.2d 600 (1973).

^{146.} Middlesex & Boston St. Ry. v. Board of Aldermen, 371 Mass. 849, 359 N.E.2d 1279 (1977); Oakwood at Madison, Inc. v. Township of Madison, 72 N.J. 481, 371 A.2d 1192 (1977).

^{147.} No. L47371-77, (N.J. Super. Ct. Camden County March 17, 1980), summarized in [1980] HOUS. & DEV. REP. (BNA) 979.

local measures not in conflict with state law.¹⁴⁸ Moreover, a California statute requires every local government to include in the housing element of its general plan a program to "assist in the development of adequate housing to meet the needs of low- and moderate-income households."¹⁴⁹ This statutory provision could be construed as empowering local governments to adopt inclusionary programs.¹⁵⁰ If the California legislature were to enact legislation restricting the powers of all local governments to adopt inclusionary measures, however, that disenabling legislation would almost certainly be held constitutional.¹⁵¹

B. THE TAKING ISSUE

Inclusionary zoning requirements are just one of many types of exactions that local governments impose on landowners as a precondition to granting permission to develop. Landowner challenges to the legality of exactions have traditionally been conceptualized as posing a taking issue. Instead of applying standard taking doctrine in exaction cases, however, the state courts have worked out special constitutional rules. The strictest of these rules, the Illinois Supreme Court's much maligned *Pioneer Trust* test, permits an exaction only when the need for the exaction is uniquely and specifically attributable to the development in controversy. ¹⁵² The typical inclusionary ordinance could not survive this constitutional test because the problem allegedly being addressed—a community wide shortage of low- and moderate-income housing—caimot be uniquely laid at the doorstep of any particular new development.

Most state courts, however, have backed away from the strict Pio-

^{148.} See Cal. Const., art. 11, §§ 5(a), 7; Birkenfeld v. City of Berkeley, 17 Cal. 3d 129, 550 P.2d 1001, 130 Cal. Rptr. 465 (1976).

^{149.} CAL. GOV'T CODE § 65583(c)(2) (West Supp. 1981).

^{150.} But see CAL. GOV'T CODE § 65589(c) (West Supp. 1981).

^{151.} The legal issue would be whether the statute wrongfully invaded the autonomy of chartered cities to control their municipal affairs. See Cal. Const., art. 11, § 5(a). Because the state could demonstrate that a city's inclusionary measures would be likely to raise the housing prices that outsiders would have to pay, the statute should be upheld as dealing with a matter of statewide concern. See CEEED v. California Coastal Zone Conservation Comm'n, 43 Cal. App. 3d 306, 118 Cal. Rptr. 315 (1974); Sato, "Municipal Affairs" in California, 60 Calif. L. Rev. 1055 (1972). See generally Weekes v. City of Oakland, 21 Cal. 3d 386, 579 P.2d 449, 146 Cal. Rptr. 558 (1978) (Richardson, J., concurring).

Although it would be constitutional, a statute of this sort would do little by itself to dampen the exclusionary tendencies of local governments in California. To achieve that broader result, the legislature would have to adopt limitations on all forms of exclusionary practices. See generally Suburban Growth Controls, supra note 93.

^{152.} Pioneer Trust & Sav. Bank v. Village of Mount Prospect, 22 Ill. 2d 375, 176 N.E.2d 799 (1961).

neer Trust approach, and require only that there be a "rational nexus" between the construction of a development and the need for the exaction. Proponents of inclusionary zoning seem to think that this test would be satisfied by a showing that a new subdivision of luxury houses (for example) would add new consumers to a community, that these consumers would want to shop at nearby stores, and that those stores would thus have to hire more low- and moderate-income workers. This nexus, however, is almost nonexistent. As shown earlier, even in a wealthy city like Palo Alto, one-half of all families have either "low" or "moderate" incomes; bringing in a few more house-holds with income in the middle third of the state's income distribution therefore could not possibly have a significant effect on the Palo Alto labor market. More importantly, because most workers are willing to commute, storekeepers in suburban shopping centers have succeeded in staffing their stores without the aid of inclusionary zoning.

Even if a nexus between new housing construction and local labor shortages could be shown, inclusionary zoning is seldom a rational way to cure the problem. When labor shortages do crop up in suburban areas, the villain is usually municipal regulations that require large lot sizes, prohibit use of mobile homes, and so on. The straightforward solution to the labor shortage would be the repeal of these prohibitions on low cost housing. "Inclusionary" communities, however, not only allow these exclusionary measures to stand, but also saddle all new residential development with a double tax that may aggravate the housing plight of most moderate-income workers.

Additionally, the rational nexus test is unsound. In my opinion, it is fair to place special taxes on a new subdivision to finance a particular service benefitting that subdivision only when either (1) the subdivider has been granted above normal development rights; or (2) prior subdividers have rather consistently been forced to pay for that same type of service through special taxes. The first prong of this test suggests that a landowner who has been granted unusually generous zoning (e.g., for multifamily development) should not normally be able to use the taking clause to defeat inclusionary requirements. Palo Alto, for

^{153.} See, e.g., Longridge Builders, Inc. v. Planning Bd., 52 N.J. 348, 245 A.2d 336 (1967) (per curiam).

^{154.} See, e.g., Kleven, supra note 9, at 1495.

^{155.} See table at text accompanying note 103 supra. The table only shows figures for "families." In 1970 Palo Alto's population included an additional 7267 "unrelated individuals" with incomes below \$10,000. See 1970 CENSUS, supra note 103.

^{156.} See Suburban Growth Controls, supra note 93, at 450-67, 477-89.

example, should usually be deemed not to have violated the taking clause when it imposes inclusionary requirements to recoup a land-owner's windfall from having had his land placed in a multifamily zone. Neither prong of the proposed test, however, is satisfied by the Coastal Commission's program, which taxes the construction of normal types of single family housing in order to finance inclusionary units. Why should the subdivider/residents of a typical coastal housing tract be forced to subsidize housing for store employees when subdividers/residents of preexisting coastal subdivisions have never had to?

This analysis suggests that some inclusionary requirements should be held to violate the taking clause. But inclusionists can take heart; the foregoing analysis is unlikely to win judicial acceptance in California. The California Supreme Court's landmark opinion in Associated Home Builders v. City of Walnut Creek 157 adopted a policy of extreme judicial deference to all types of governmental charges on developers. Prospects for developer success on the taking issue in California are so weak that there appear to have been no constitutional challenges to California inclusionary programs despite their popularity in the state. California's courts are at the other ideological extreme from Virginia's, and almost never treat landowners' constitutional claims with any sympathy. A consultant's report for a California builder's group correctly concludes that there is "little hope" that the California courts will declare an inclusionary zoning measure to be unconstitutional. 158

Outside California, the resolution of the taking issue posed by inclusionary ordinances is harder to predict. In *DeGroff*, the Virginia Supreme Court not only found inclusionary zoning to be beyond a local government's authority, but also held that Fairfax County's 15% inclusionary requirement constituted a taking of the developer's land. ¹⁵⁹ By contrast, in *Uxbridge Associates*, the New Jersey trial court rejected the taking claim of a condominium developer who had been forced to set aside 5% of its units for low- and moderate-income families. The court emphasized that the developer had never applied for federal housing subsidies to cushion its financial loss on the inclusionary units and, thus, that the developer was responsible for much of its own hardship. ¹⁶⁰ These decisions, as well as the logic of the *Pioneer*

^{157. 4} Cal. 3d 633, 484 P.2d 606, 94 Cal. Rptr. 630 (1971) (upholding legality of city's in-lieu fees for parks).

^{158.} IMPLICATIONS, supra note 54, at 94.

^{159. 214} Va. at 238, 198 S.E.2d at 602.

^{160.} No. L47371-77, (N.J. Super. Ct. Camden County March 17, 1980), summarized in [1980] Hous. & Dev. Rep. (BNA) 979.

Trust and the "rational nexus" tests, have prodded most commentators to advise local governments to defuse landowners' taking claims by extending generous density bonuses to offset the burdens of inclusionary requirements. 161

C. Proposition 13

A third legal challenge to inclusionary zoning in California would rest on the provisions of section 4 of article XIIIA of the California Constitution. This section, approved by the voters in 1978 when passing Proposition 13, reads in part: "Cities, counties and special districts, by a two-thirds vote of the qualified electors of such district, may impose special taxes on such districts" The County Counsel of Santa Cruz County sought the California Attorney General's opinion on whether this language prevented the County, without the requisite voter approval, from imposing cash exactions on new residential construction to fund low- and moderate-income housing on sites near the new construction. In a 1979 opinion, the Attorney General's office ruled that voter approval was indeed required. 162 After long discussion and a review of the history of Proposition 13, the opinion stated: "It is our conclusion... that 'special taxes' as used in section 4 refers to any new or increased exactions imposed [by local governments] for revenue purposes."163

This opinion is not as important as it might imitially appear. First, the reasoning of the Attorney General's opinion has been rejected in a poorly crafted Court of Appeal decision, *Trent Meredith, Inc. v. City of Oxnard*, ¹⁶⁴ a case sustaining cash exactions imposed on developers to relieve school crowding.

In addition, the Attorney General's opimion did not discuss the legality, under section 4, of the most common form of inclusionary zoning ordinance—one that requires developers to set aside specific inclusionary units. Local governments might argue that they receive no "revenue" in this situation because the revenue raising and spending prongs are directly linked, thereby depriving the local legislature of any discretion. Acceptance of this argument, however, would create a major loophole in section 4, because a local government could then easily

^{161.} See, e.g., Kleven, supra note 9, at 1524-28.

^{162. 62} Op. Att'y Gen. Cal. 673 (1979).

^{163.} Id. at 686.

^{164. 114} Cal. App. 3d 317, 170 Cal. Rptr. 685 (1981). Cf. Mills v. County of Trinity, 108 Cal. App. 3d 656, 166 Cal. Rptr. 674 (1980) (fees charged in conjunction with regulatory activities are not "special taxes" which require voter approval).

avoid the "tax" label by pairing a compulsory spending program with any new revenue raising program. The Attorney General's opinion discusses the difference between special assessments (and other user charges) and general taxes, and concludes that only the latter are subject to section 4.165 If this distinction is the operative one for section 4's coverage, the logic of the opinion would also doom the usual form of inclusionary exaction because, to borrow from the language of special-assessment law, inclusionary units confer "general," not "local," benefits on the community, and thus inclusionary exactions cannot be viewed as a form of user charge.

SUMMARY

Inclusionary zoning, as usually practiced, is a misguided undertaking that is likely to aggravate the housing crisis it has ostensibly been designed to help solve. As a program of income redistribution, inclusionary zoning makes no sense. Although nominally aimed at benefiting low- and moderate-income families, almost all inclusionary units have in fact been bestowed on families in the middle third of the state's income distribution. Because only a small percentage (at most) of the members of the class of eligibles can hope soon to obtain units, inclusionists must resort to lotteries and queues to select the few lucky beneficiaries of handsome housing grants.

Government distribution of massive subsidies to a few arbitrarily designated members of the middle class might be defensible if this redistribution produced important benefits to the larger society. The only possible social gains from inclusionary zoning are the intangible benefits flowing from the economic integration of new buildings and subdivisions. Yet even the social critics who have pushed most strongly for greater residential mobility doubt that economic integration at the block and building level is in the interest of the members of any income group. Moreover, inclusionary zoning as currently practiced will have only a trivial effect on the amount of economic integration in residential neighborhoods.

The costs of inclusionary zoning, by contrast, are large and tangible. Inclusionary zoning involves in-kind housing subsidies, a method increasingly viewed as one of the most inefficient forms of income redistribution. Inclusionary zoning can also constitute a double tax on new housing construction—first, through the burden of its exactions; and second, through the "undesirable" social environment it may force on new housing projects. In the sorts of housing markets in which inclusionary zoning has been practiced, this double tax is likely to push up housing prices across the board, often to the net injury of the moderate-income households inclusionary zoning was supposed to help. The irony of inclusionary zoning is thus that, in the places where it has proven most likely to be adopted, its net effects are apt to be the opposite of the ones advertised.