



**Sacramento
Housing &
Redevelopment
Agency**

REPORT TO COUNCIL
City of Sacramento
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Staff Report
March 18, 2008

**Honorable Mayor and
 Members of the City Council**

Title: Economic Analysis of the Mixed Income Housing Ordinance

Location/Council District: Citywide

Recommendation: Review the purpose, scope, and timing of an economic impact analysis of the City's Mixed Income Housing Ordinance and comment on the methodology, including prototype developments, public input process, and expectations.

Contact: Cindy Cavanaugh, Assistant Director, 440-1317, Emily Halcon, Management Analyst, 440-1399, ext. 1420

Presenters: Cindy Cavanaugh, Assistant Director, Emily Halcon, Management Analyst, Matt Kowta, Bay Area Economics (BAE)

Department: Sacramento Housing and Redevelopment Agency

Description/Analysis

Issue: In May 2007, staff from the Sacramento Housing and Redevelopment Agency (SHRA) presented a comprehensive assessment of the Mixed Income Housing Ordinance (commonly known as the inclusionary program) to the City Council. Adopted in June 2000, the inclusionary program has achieved a high level of housing production and the intended depth of affordability. Outcomes for homeownership units have been mixed with approximately 24 percent of inclusionary units built or approved as ownership units. For a variety of reasons, the majority of large planned unit developments (PUDs) were fulfilling their inclusionary obligation through the construction of affordable rental apartments. Smaller single family developments and condominiums, on the other hand, almost always provided their inclusionary units as owner-occupied units.

To improve homeownership outcomes, Council confirmed that SHRA should pursue modifications to the Ordinance by adjusting income targets upward for inclusionary homeownership units. The intention of these changes is to encourage developers, especially those of large PUDs, to incorporate affordable ownership units within their overall project. Choosing an appropriate income target requires weighing market, economic, and equity factors; therefore SHRA contracted with Bay Area Economics (BAE) to conduct an economic impact analysis to perform this calibration.

Economic Analysis of the Mixed Income Ordinance

BAE has convened an advisory panel of local developers and housing industry professionals to provide continual input and feedback on the analysis. Throughout the process, the panel members will meet with BAE collectively and individually to guide the analysis, more specifically confirming the characteristics and cost of the development prototypes. In general, the analysis determines the financial feasibility of these prototypical developments, using both return on investment and residual land value as measurements. Inclusionary obligations are then applied to the prototypes to quantify the financial impact or "cost" of inclusionary housing and how that cost adjusts as the inclusionary obligation changes and/or development incentives are added. The analysis recognizes that development conditions are fluid and calculates impacts notwithstanding market fluctuations. More details on the five proposed prototype developments to be tested as well as the process and advisory panel for the analysis are included in Attachment 1, and Attachment 2 outlines the purpose of and expectations for the analysis.

In addition to the proposed homeownership income target adjustment, the analysis will provide useful information in regards to several other policy issues. Specifically, by including prototypes that are typically located in more urban settings, the analysis will provide background for future discussions on expansion of the Ordinance to non new growth areas. BAE is also calculating the fee equivalent of building inclusionary units relevant to any future consideration of an in-lieu fee option.

BAE will also evaluate how to restructure the existing equity share provisions in the Ordinance that severely restrict the ability of the homeowner to share in any equity appreciation. The deep income targeting of the current ordinance, combined with the equity share approach, limits the pool of eligible buyers able to purchase a home. Changes to the re-sale restrictions and equity sharing will be made once income levels for ownership units are determined. Different levels of affordability may suggest different approaches to equity sharing.

Policy Considerations: The City Council has expressed an interest in modifying the Ordinance to encourage affordable homeownership. Should more developers, especially those of larger PUDs, choose to incorporate homeownership units as part of their inclusionary obligation, another outcome will be more dispersal of affordable units and more integration into the market rate units, one of the objectives of the Ordinance. In addition, the City is promoting modest income homeownership as a theme for the 2008-2013 Housing Element. Without a new funding source, the Ordinance may be one of the best vehicles for promoting homeownership for those households currently priced out of the market.

Economic Analysis of the Mixed Income Ordinance

Environmental Considerations: No action required and therefore not a project as defined by the California Environmental Quality Act (CEQA) [CEQA Section 21065 and CEQA Guidelines Section 15378 (b)(4)].

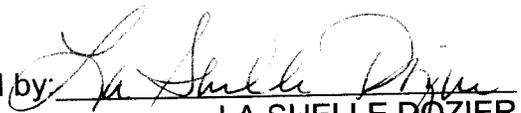
Committee/Commission Action: Staff presented this report to the Sacramento Housing and Redevelopment Commission on February 20, 2008 and will present it to the City of Sacramento Planning Commission on March 20, 2008. In addition, staff has notified the members of the City Development Oversight Commission of this workshop and has invited them to attend the Planning Commission or Council workshop for this item.

Rationale for Recommendation: The Mixed Income Ordinance has been successfully implemented in the new growth areas of the City. While the ordinance has been largely successful, modest ordinance modifications could enhance homeowner outcomes and improve options for smaller developments and condominium developments. Using an economic impact analysis to study these proposed modifications allows for an objective, impartial discussion about the true economic benefits and effects of inclusionary housing.

Financial Considerations: There are no financial impacts associated with the assessment of the Ordinance.

M/WBE Considerations: The items discussed in this report have no M/WBE impact; therefore, M/WBE considerations do not apply.

Respectfully Submitted by:



LA SHELLE DOZIER
Interim Executive Director

Recommendation Approved:

for 
RAY KERRIDGE
City Manager

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Advisory Panel Information

Purpose: Provide feedback on economic impact analysis process and product and confirm that appropriate assumptions are used in the development prototypes. Advisory panel members are expected to understand and bring relevant development experience to the discussion of the prototype developments. The panel will also review the final report before dissemination to the public and their comments will be shared with the Council along with the final report and recommendations.

Timing: The advisory panel will meet three times during the preparation of the economic impact analysis as follows:

1. To discuss the methodology, purpose and expectations for the analysis and to review the five prototype development characteristics.
2. To review the five prototypes cost assumptions and the six alternative inclusionary obligations to be tested. The methodology for calculating the in-lieu fee alternative will also be discussed.
3. To review and provide comments on the draft analysis and findings prior to public dissemination.

Members: The advisory panel consists of thirteen members representing building and housing interest groups, non-profit developers, for-profit affordable housing developers, and market rate developers. Most panel members have in the past or currently are working on projects subject to the Mixed Income Ordinance and have developed different product types throughout the City.

Prototypes: The analysis will test the economic impact of six alternative inclusionary obligations on five different prototypes. The advisory panel members will help provide the costs for each of the recommended prototypes as follows:

- Suburban detached single family home in a small development (< 30 units)
- Suburban detached single family home in a mid-sized development (\approx 150 units)
- Suburban cluster, small lot single family home
- Suburban low rise condominium
- Urban mid rise condominium



MEMORANDUM

Date: November 29, 2007

To: Mayor Heather Fargo
Councilmember Ray Tretheway Councilmember Lauren Hammond
Councilmember Sandy Sheedy Councilmember Kevin McCarty
Councilmember Steve Cohn Councilmember Robbie Waters
Councilmember Robert King Fong Councilmember Bonnie Pannell

From: Cindy Cavanaugh, Assistant Director, Housing and Community Development

SUBJECT: Report back to Council re: Improving Homeownership Outcomes in Mixed Income Ordinance

This memo follows up the May 1, 2007 City Council workshop on the Mixed Income Ordinance (“Ordinance”) and summarizes Sacramento Housing and Redevelopment Agency (SHRA) work, including the use of an economic analysis, intended to improve homeownership outcomes. We are working closely with the City’s Long Range Planning Department and Development Services to determine appropriate homeownership income targets in the Ordinance. Key milestones and the timeframe for delivery of recommendations are contained in Attachment I.

Background

On May 1, 2007, SHRA presented to the City Council an assessment of the Mixed Income Housing Ordinance (Ordinance) adopted in 2000. The assessment highlighted progress in achieving overall high production, with 1,552 inclusionary units constructed or approved, and an additional 1,447 pipeline units. The assessment also measured the depth of affordability achieved under the Ordinance: nearly 2,000 units planned or approved for very low income families making no more than 50 percent of area median income.

The assessment found that homeownership outcomes were mixed. Approximately 23 percent of all the constructed and approved inclusionary units were homeownership, mostly in small single family developments or condominiums.

Several factors contribute to developers choosing to meet their affordable obligation through rental rather than ownership housing, including:

- Aggressive income targets within the Ordinance (generally, targeting 10 percent at very low income and 5 percent at low income);
- Availability of multifamily land within the market development coupled with available public financing for affordable rental housing; and
- Lack of financial incentives for affordable homeownership developments.

In addition, Ordinance restrictions on the equity appreciation allowed for participating homebuyers makes it harder to find qualified interested buyers.

In May, Council directed staff to follow through with “Tier One” Ordinance modifications intended to improve homeownership outcomes:

- 1) Adjust the income targets upward when homeownership is selected; and
- 2) Modify the resale provisions to allow the homeowner to share in the market appreciation.

Staff also recommended in May that two broader policy issues be addressed through the Housing Element update process and within a context larger than the Ordinance (e.g., one that considers the full complement of strategies within the affordable housing “toolkit”). These issues were: providing housing for extremely low income households and increasing affordable housing production on a citywide level. At the workshop, some City Council members expressed interest in considering options for a citywide inclusionary approach.

Staff agreed to report back on Tier One in the fall of 2007 and to include the broader policy issues in the Housing Element process, scheduled to be complete by June 2008 (referenced as Tier Two in the assessment.)

Work to Date

Selecting the appropriate income target for homeownership has been more difficult than anticipated. In June, staff met with market rate builders to understand what regulatory and financial barriers were discouraging them from building their inclusionary obligation in ownership products. Our goal was to hear from developers what changes to the Ordinance might make inclusionary ownership a more viable option. Developers provided good feedback in regards to homebuyer processing and best practices, but did not have specific recommendations on Ordinance income target modifications.

Staff also researched for-sale inclusionary requirements in other jurisdictions in California (Attachment 2). This inquiry looked only at for-sale requirements, including depth and term of affordability and resale provisions. As is seen in the attached matrix, the variety of ordinances is wide, with no obvious “best practice” model, but with great variation reflecting the local economic as well as political landscape. Staff intends to expand this research to include actual production under each of the Ordinances. Also underway is a staff analysis of various equity sharing approaches used in other jurisdictions.

Economic Analysis

To determine appropriate income targets for homeownership, staff has selected a consultant to evaluate viable homeownership income targets. Similar analysis has been widely used by jurisdictions contemplating inclusionary strategies (e.g., Oakland, San Jose, and Los Angeles). Using a 'return on investment' or 'residual land value' approach, the inclusionary obligation is applied with varying percentages and income targets to a variety of market products (e.g., single family, mid rise, high rise, etc.). Reflecting variation by development type and location, the analysis shows the maximum obligation that developments can absorb and still be economically viable.

To be useful and worth the effort of time and money, it is important that all stakeholders understand and support this approach. Toward this end, staff has met and received conditional support from representatives of both affordable housing advocates and the building industry. Staff will work with the consultant to identify a representative stakeholder group for regular check-in while the study is underway.

Timeline

Key milestones are listed in Attachment 1. The economic analysis will take about six months. A significant amount of this time is required to develop real-world housing prototypes with input and assistance from the development professionals in the community. Agreement on development costs from the local development community is paramount because the financial effects of inclusionary housing must be tested against true development scenarios.

We anticipate having two presentations with the Council in 2008: one to discuss the preliminary affordability scenarios and the second to present final recommendations on ordinance changes. Based on the outcome of those presentations changes to the ordinance would be made by the City attorney for Council approval and adoption in late 2008.

If the Mayor, Councilmembers or your staff have any questions, SHRA and City Planning staff would be glad to meet with you. Please contact Cindy Cavanaugh at 916-440-1317 or at ccavanaugh@shra.org if you wish to schedule a briefing.

cc. SHRA Commission
Planning Commission
John Dangberg, Assistant City Manager
Carol Shearly, Director, Planning Department
Bill Thomas, Director, Development Services Department

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Attachment 1: Key Milestones and Timeline
Attachment 2: California For-Sale Inclusionary Provisions

ATTACHMENT 1
Key Milestones and Timeline

Task	Status	Date
Research inclusionary requirements for homeownership in other jurisdictions	X	June 2007
Developer Focus Group: Incentivizing Homeownership	X	June 2007
Economic Analysis, including Equity Share work <ul style="list-style-type: none"> • Solicit key Stakeholder Support • Select Consultant • Stakeholder meetings with Consultant 	X X	November 2007 November 2007 January/February 2008
Council Workshop: Economic Analysis methodology and approach		February 2008
Final Report to City Council with recommendation for Ordinance changes (through SHRA Commission and Planning Commission)		June 2008
Adopt Ordinance changes through the City Attorney's office		August 2008

X = Completed

ATTACHMENT 1 Key Milestones and Timeline

JURISDICTION	INCOME TARGET Percent	INCOME TARGET Income	AFFORDABILITY TERM	RESALE/RECAPTURE	EQUITY SHARE	OTHER
"TOP TEN" CITIES						
San Diego (Citywide Ordinance)	10%	100%	None	<input type="checkbox"/> Resale only <input checked="" type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	15% equity first year, increasing to 100% by 15 th year	Exemption for "naturally affordable" projects – 100% at 150% AMI
San Francisco	12% – 20%	120%	50 years	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Equity only from increase in affordable sales price, plus improvements and sales fees	Percentage based on location and density of development
LOCAL JURISDICTIONS						
Davis	25%	80% - 120%	On-going through right of 1 st refusal	<input type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input checked="" type="checkbox"/> Resale & Recapture	3.75% compounding appreciation annually	
West Sacramento	10% 5%	120% 80%	45 years	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Equity only from increase in affordable sales price	
Folsom	10% 5%	50% 80%	30 years	<input type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input checked="" type="checkbox"/> Resale & Recapture	Equity only from increase in affordable sales price	Up to 50% of the IH units may be built as granny flats
Woodland	10%	80%	10 years, renewable	<input type="checkbox"/> Resale only <input checked="" type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	City receives proportionate share of appreciation based on silent second	
Sacramento County	15%	80%	30 years	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	County receives initial subsidy; seller receives 1/30 th market equity per year	
OTHER CALIFORNIA JURISDICTIONS						
Santa Barbara	15%	120% - 160%	45 years, renewable	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Equity only from increase in affordable sales price	
Contra Costa County	12% 3%	120% 80%	3 years	<input type="checkbox"/> Resale only <input checked="" type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	County receives initial subsidy plus proportionate share of market equity	
Santa Cruz County	15%	120%	In perpetuity	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Equity only from increase in affordable sales price	

ATTACHMENT 1

Key Milestones and Timeline

JURISDICTION	INCOME TARGET		AFFORDABILITY TERM	RESALE/RECAPTURE	EQUITY SHARE	OTHER
	Percent	Income				
Marin County	20%	60%	In perpetuity	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Equity only from increase in affordable sales price	
Walnut Creek	10% OR 6% OR 4.5%	120% 80%	45 years	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Equity only from increase in affordable sales price	While Ordinance income limits do not limit for sale to 120% AMI, all for sale documentation assumes for-sale inclusionary at 120% AMI.
Sunnyvale	12.5%	80%	30 years	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	1/3 of percent increase in CPI during occupancy	
San Rafael	10% - 20%	1/2 - 120% 1/2 - 80%	In perpetuity	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Equity only from increase in affordable sales price	
Fremont	15%	110%	30 years, renewable	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Equity lesser of increase in affordable sales price or % increase in CPI	
Emeryville	20%	80% - 120%	45 years	<input checked="" type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture	Resale at new moderate income level	
Concord	10% OR 6%	120% 80%	45 years	<input type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input type="checkbox"/> Resale & Recapture		
Carlsbad	15%	"lower income"	30 years	<input type="checkbox"/> Resale only <input type="checkbox"/> Recapture only <input checked="" type="checkbox"/> Resale & Recapture	Resale – appreciation based on increase in affordable price Recapture – City receives proportionate share of market equity	