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REAL ESTATE
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AFFORDABLE HOUSING
ECONOMIC DEVELOPMENT

MEMORANDUM

To: Susan Georgino, Community Development Director
City of Burbank

From: Kathleen Head
Julie Romey

Date: September 14, 2003

Subject: Inclusionary Housing Ordinance – In-Lieu Fee Analysis

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In accordance with your request, Keyser Marston Associates, Inc. (KMA) reviewed the current housing market conditions in Burbank to assist in evaluating the impacts associated with the Inclusionary Housing Ordinance (Ordinance) proposed by the City of Burbank (City). The City is planning to include an option for projects that meet defined criteria to pay a fee in lieu of providing affordable housing units on site. The purpose of the KMA analysis is to determine the in-lieu fee payments that should be assessed by the City as part of the Inclusionary Housing Program (Program).

BACKGROUND

The City Council directed the City staff to create a Program for their consideration. To that end, the City staff, consultants and a stakeholders group comprised of developers, realtors and community members, are currently creating a preparing a draft Ordinance. The KMA role in this process is to provide the technical analysis that identifies the affordability gap associated with the proposed income and affordability restrictions, and to recommend the in-lieu fee amounts that should be included at the Program's inception.

INCLUSIONARY HOUSING ORDINANCE ASSUMPTIONS

The Ordinance will affect both ownership and rental projects built in the City. The KMA analysis is based on the following assumptions:

1. Income and affordability restrictions:
 - a. 15% of the units developed in a residential ownership project must be restricted to moderate income households; and

- b. 15% of the units developed in a residential rental project must be income-restricted:
 - i. 10% to low income households, and
 - ii. 5% to very low income households;
2. The income standards will be based on the following California Health and Safety Code definitions:
 - a. Low Income: Section 50079.5
 - b. Very-Low Income: Section 50105
3. The affordable housing cost calculations are based on California Health and Safety Code Section 50052.5 (Section 50052.5). The calculations are based on the following components:
 - a. Housing costs consist of mortgage debt service, homeowner association (HOA) dues, insurance, utility allowances, and property taxes.
 - b. The affordable housing costs for moderate income units are based on the following benchmark standards:
 - i. 110% of the Los Angeles County area median income (Median) for a household size equal to one more person than the number of bedrooms in the unit; and
 - ii. 35% of the defined household income.
4. The affordable housing cost for rental units are based on the California Health and Safety Code Section 50053 (Section 50053) standards. Affordable housing cost is calculated based on the following parameters:
 - a. Housing costs include rent plus utilities paid for by the tenants.
 - b. The affordable housing cost calculations are based on the following benchmark standards:
 - i. The household size is set at one person more than the number of bedrooms in the unit;
 - ii. The low income rent is calculated based on 60% of the Median and the very-low income rent is calculated based on 50% of the Median; and

- iii. Affordable housing cost is equal to 30% of the defined household income.
- 5. Small projects will be provided with the option to provide the inclusionary housing units, or to pay an in-lieu fee, which will be adjusted for project size.
- 6. Projects that apply more stringent affordability requirements than the basic Ordinance standards will be allowed to fulfill the inclusionary requirement with fewer than 15% of the units in the project.

INCOME STANDARDS

Based on the applicable California Health and Safety Code Sections, and the 2003 household income information published by HCD, the maximum incomes that can be earned by households renting or purchasing inclusionary housing units are currently:

Household Size	Very-Low Income	Low Income	Moderate Income
1	\$19,750	\$31,600	\$46,250
2	\$22,550	\$36,100	\$52,900
3	\$25,400	\$40,600	\$59,500
4	\$28,200	\$45,100	\$66,100
5	\$30,450	\$48,750	\$71,400
6	\$32,700	\$52,350	\$76,700
7	\$34,950	\$55,950	\$81,950
8	\$37,200	\$59,550	\$87,250

OWNERSHIP UNITS AFFORDABILITY GAP ANALYSIS

For the purposes of this analysis, KMA has assumed that the vast majority of new ownership housing projects will be attached townhome and condominium units. The methodology used in the KMA affordability gap analysis for ownership development projects can be described as follows:

- 1. KMA estimated the average market rate sales prices for two-, three- and four-bedroom units located in newly constructed subdivisions.¹
- 2. KMA calculated the maximum affordable home price for moderate income households based on household income statistics distributed by the State of California’s Housing and Community Development Department (HCD), and the affordability standards imposed by the Ordinance.

¹ The market rate prices are based on a Meyers Group sales survey.

3. KMA compared the estimated market price to the defined affordable price to identify the financial gaps that would be incurred by a developer if they chose to fulfill their inclusionary housing obligation on-site.
4. KMA calculated the in-lieu fee that would have to be charged to provide the City with adequate funds to produce the inclusionary units in an off-site location.

The tables that detail the analysis are located in Appendix A, and are organized as follows:

Appendix A:
Ownership In-Lieu Fee Analysis

Table 1	Market Rate Sales Price Comparables by Project
Table 2	Affordability Gap Calculations (Moderate Income Households)
Table 3	Ownership In-Lieu Fee Calculation

Market Sales Comparables

As shown in Appendix A – Table 1, KMA found two projects that are currently selling new attached residential units in the City. The following summarizes the current average market prices for the units being marketed:

Two-Bedroom Units	\$311,500
Three-Bedroom Units	\$347,400
Four-Bedroom Units	\$419,000

Affordable Housing Price Calculation

The affordable housing cost calculations, are shown in Appendix A – Table 2, and are based on the following assumptions:

1. The housing related costs have been estimated as follows:
 - a. The HOA dues, assuming that insurance is included in the dues, are estimated at \$150 per month for two-bedroom units, \$175 per month for three-bedroom units, and \$200 per month for four-bedroom units.
 - b. The utility allowances are estimated at \$104 per month for two-bedroom units, \$115 per month for three-bedroom units, and \$142 per month for four-bedroom units.
 - c. The property tax cost is estimated at 1% of the projected unrestricted market rate price for the units. These prices were estimated based on the survey presented in Appendix A – Table 1.

2. The mortgage amount that can be supported is based on a 30-year fully amortizing mortgage at a 6.50% interest rate (7.58% mortgage constant).
3. It is assumed that the homebuyers will be required to contribute a down payment equal to 5% of the home's market value.

The following summarizes the resulting maximum affordable prices:

Two-Bedroom Units	\$195,600
Three-Bedroom Units	\$216,100
Four-Bedroom Units	\$229,300

Affordability Gap Calculations

The results of the affordability gap analysis for moderate income households are presented in Appendix A – Table 3. When the maximum affordable prices are compared to the average market rate prices, the resulting affordability gaps are calculated as follows:

	Two- Bedrooms	Three- Bedrooms	Four- Bedrooms
Average Market Price	\$311,500	\$347,400	\$419,000
(Less) Maximum Affordable Price	<u>(195,600)</u>	<u>(216,100)</u>	<u>(229,300)</u>
Affordability Gap	\$115,900	\$131,300	\$189,700

As can be seen in the table above, the affordability gap ranges from \$115,900 to \$189,700. The weighted average affordability gap per moderate income unit is estimated at \$131,800.

Inclusionary Housing Obligation Cost

The draft Ordinance requires developers to allocate 15% of the units in a residential project to moderate income households. If the City wishes to adopt an in-lieu fee that would allow the inclusionary housing units to be developed in an off-site location, with no City financial assistance, the fee would have to be based on the weighted average affordability gap of \$131,800 per restricted unit. The resulting in-lieu fee amount would have to be set at \$19,800 per unit being developed in a market rate project.² Assuming that the average unit size is +/- 1,570 square feet of gross living area (GLA), the in-lieu fee would total approximately \$12.60 per square foot of GLA.

² The in-lieu fee amount per total unit in the project is calculated by multiplying \$131,800 times 15%.

RENTAL UNITS AFFORDABILITY GAP ANALYSIS

The KMA affordability gap analysis for apartment developments can be described as follows:

1. KMA compiled rental data for one- and two-bedroom apartment units in Burbank to estimate the achievable rents for new developments.
2. KMA calculated the maximum affordable rents for low and very-low income households based on household income statistics distributed by HCD, and the affordability standards established in the Ordinance and Section 50053.
3. KMA compared the resulting project value for a prototype 40-unit market rate project, to the value supported at low, and very-low income rents. This was done to identify the financial gaps that would be incurred by a developer if they chose to fulfill the proposed inclusionary housing obligations on-site.

The tables that detail the analysis are located in Appendix B, and are organized as follows:

Appendix B Rental In-Lieu Fee Analysis

Table 1	Apartment Rent Comparables by Project
Table 2	Affordable Rents for Low and Very-Low Income Households
Table 3A	Net Operating Income – 100% Market Rate Rents
Table 3B	Net Operating Income – 100% Low Income Rents
Table 3C	Net Operating Income – 100% Very-Low Income Rents
Table 4	Rental In-Lieu Fee Calculation

Market Rent Rates

As shown in Appendix B – Table 1, KMA surveyed 12 apartment projects that are currently renting units in Burbank. The following summarizes the current weighted average market rents per unit being achieved in Burbank:

One-Bedroom Units	\$1,213
Two-Bedroom Units	\$1,550

Maximum Affordable Rents

The draft Ordinance requires 10% of the units to be set-aside for low income units and 5% of the units to be set-aside for very-low income households. The affordable rent calculations are detailed in Appendix B – Table 2. The calculations are based on the Section 50053 standards, and monthly utilities allowances of \$77 per month for one-bedroom units and \$91 per month for two-bedroom units. The maximum allowable rents under the income categories are as follows:

	Low Income	Very-Low Income
One-Bedroom Units	\$585	\$474
Two-Bedroom Units	\$653	\$529

Affordability Gap Calculations

To estimate the affordability gap between a market rate apartment project and one subject to the Ordinance’s restrictions, KMA created a prototypical apartment project comprised of 20 one-bedroom units and 20 two-bedroom units, totaling 40 units. This conceptual analysis was prepared to identify the financial gap associated with including low and very-low income rental units in a market rate project.

The components included in the project value comparisons, as calculated in Appendix B - Tables 3A - 3C, are:

1. The difference between the market rate and income restricted rents is calculated.
2. The income analysis for both market rate and income restricted projects include \$8 per unit per month in miscellaneous income and a standard 5% vacancy and collection allowance.
3. The property tax expense estimates vary between the market rate and income restricted apartment projects. The difference is calculated by comparing the value supported by the various scenarios.
4. The balance of the operating expenses and reserve for capital repairs are assumed to remain constant among market rate, low and very-low income units. These expenses are estimated at \$2,950 per unit per year.
5. The net operating income for both the market rate and income restricted units was capitalized at an 8% rate to estimate the relative values supported by market rate, low and very-low income units.

As illustrated in Appendix B – Table 4, the estimated value per unit of a typical apartment project in Burbank is as follows:

	Value/Unit
Market Rate Units	\$143,400
Low Income Units	\$46,600
Very-Low Income Units	\$31,900

Appendix B – Table 4 also calculates the affordability gaps per unit, which are estimated as follows:

	Affordability Gap/Unit
Low Income Units	\$96,900
Very-Low Income Units	\$111,600

To determine the overall affordability gap, it is necessary to take the weighted average gap exhibited at each income level. Given that the obligation is split to require 2/3 of the affordable units to be low income, and 1/3 of the affordable units to be very-low income, the effective affordability gap equals \$101,800 per unit.

Inclusionary Housing Obligation Cost

The Ordinance requires developers to allocate 10% of the units in a rental project to low income households, and 5% of the units to very-low income households. Alternatively, the developer can pay an in-lieu fee that is assessed on 100% of the units in the residential project. If the in-lieu fee is set equal to the affordability gaps calculated in this analysis, the supportable fee totals \$15,300 per unit being developed in a market rate rental project.³ Assuming the units average 1,000 square feet of GLA, the in-lieu fee would equal \$15.30 per square foot of GLA.

IN-LIEU FEE COMPARISON ANALYSIS

To assist the City in setting a new in-lieu fee payment amount, KMA compiled information from other jurisdictions that have inclusionary housing requirements, and that allow in-lieu fees to be paid. It is important to note, that most cities allow for an in-lieu fee option, but that the vast majority of cities set the fee on a case-by-case basis. For the surveyed cities that have stated in-lieu fees, the fee is calculated on one of the following bases:

1. Per total unit constructed in the project;
2. Per square foot of GLA included in the project; or
3. As a percentage of project or construction valuation.

³ The in-lieu fee amount per total unit in the project is calculated by multiplying \$101,800 times 15%.

The in-lieu fees charged in the surveyed cities are presented in the following table:

Jurisdiction	Fee/Unit in a Market Rate Project	Fee/Square Foot of GLA	Fee as % of Construction/Project Valuation
Fee Basis: Per Unit in a Market Rate Project ⁴			
Laguna Beach ⁵	\$7,047	\$4.40 - \$7.05 (est)	N.A.
Carlsbad ⁶	\$4,515	\$2.82 - \$4.52 (est)	N.A.
Coronado	\$7,000	\$4.38 - \$7.00 (est)	N.A.
Del Mar	\$16,000	\$10.00 - \$16.00 (est)	N.A.
Fee Basis: Per Square Foot of GLA ⁷			
Pasadena ⁸	\$10,400 - \$10,500 (est)	\$6.50 - \$10.50	N.A.
San Diego ⁹	\$500 - \$1,600 (est)	\$0.50 - \$1.00	N.A.
Palos Verdes	\$1,000 - \$1,600 (est)	\$1.00	N.A.
Santa Monica ¹⁰	\$6,140 - \$17,616 (est)	\$6.14 - \$11.01	N.A.
West Hollywood ¹¹	\$6,700 - \$21,440 (est)	\$6.70 - \$13.40	N.A.
Fee Basis: Percentage of Project/Construction Valuation ¹²			
San Clemente	\$1,430 - \$3,420 (est)	\$1.43 - \$2.14 (est)	\$1,430-\$3,420
San Juan Capistrano	\$1,430 - \$3,420 (est)	\$1.43 - \$2.14 (est)	\$1,430-\$3,420

⁴ To translate the fee per unit into a fee per square foot of GLA, the unit size is set at 1,000 square feet for rental units and 1,600 square feet for ownership units.

⁵ The fee is set at \$46,978 per affordable lot or unit. 15% of the units are required to be affordable, which equates to \$7,047 per total unit in a market rate project..

⁶ Applies only to residential projects with six or fewer dwelling units.

⁷ To translate the fee per square foot of GLA to a fee per market rate unit, the unit size is set at 1,000 square feet for rental units and 1,600 square feet for ownership units

⁸ Projects with fewer than 10 units are currently exempt from the ordinance. The fee varies by subarea; the low is typical for ownership; the high is typical for rental. The fees are currently being re-evaluated.

⁹ The lower fee is charged for projects with fewer than 10 units. These fees are for the first year that the ordinance is in effect. By the third year, the fees will be \$1.25 to \$2.50 per square foot of GLA.

¹⁰ The low is the fee for rental units, while the high is applied to ownership projects.

¹¹ The in-lieu fee is set at \$6.70 per square foot of GLA for projects with one- to two-units, increasing to \$13.40 per square foot of GLA for projects with nine to 20 units. The in-lieu fee option is not provided by right for projects with 20 or more units.

¹² To translate the fee as a percentage of value into a fee per market rate unit, the value is set at \$143,000 for rental units and \$342,000 for ownership units. To translate the fee into a fee per square foot of GLA, the unit size is set at 1,000 square feet for rental units and 1,600 square feet for ownership units.

SUMMARY

Ownership In-Lieu Fee

To allow for the City to attract comparable ownership units in off-site locations, the in-lieu fees would have to be set as follows:

	In-Lieu Fee
Per Affordable Unit	\$132,000
Per Total Unit	\$19,800
Per Square Foot of GLA	\$12.60

Rental In-Lieu Fee

To attract affordable rental development to off-site locations, the in-lieu fees would have to be set as follows:

	In-Lieu Fee
Per Affordable Unit	\$101,800
Per Total Unit	\$15,300
Per Square Foot of GLA	\$15.30

In-Lieu Fee Comparison

The KMA in-lieu fee survey indicates that the fees that would have to be charged to allow the City to produce affordable housing units in off-site locations are at the upper-end of the fee range being charged in other jurisdictions. However, it is a fundamental assumption of the KMA analysis that the City wishes to encourage developers to produce the inclusionary housing units within their market rate projects. If that is the case, it is advisable to set the in-lieu fee at the full cost recovery rate, and to provide development incentives that encourage developers to produce the inclusionary housing units on site.

APPENDIX A
OWNERSHIP UNITS

APPENDIX B
RENTAL UNITS