

CITY OF LONG BEACH

AFFORDABLE HOUSING FEE STUDY



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EXECUTIVE SUMMARY

INTRODUCTION

Beginning in the 1970s and 80s, the price of housing in California has risen steeply. Although house prices have dropped somewhat in the recent market downturn, apartment rents have not declined, and there remains a large shortage of affordable housing in Long Beach. As housing costs have spiraled up, housing affordability has become a dominant local land use issue on the agenda of the State Legislature. The result has been the passage of landmark planning policies into law including:

- ◆ The General Plan Housing Element clause that requires that local housing needs be based on a locality's share of regional housing needs;
- ◆ The State Density Bonus Law that requires cities to provide 20 percent density bonuses for developments that provide 20 percent of the units for lower-income households, 10 percent for very low-income households, or 50 percent for senior citizens; and
- ◆ The Redevelopment Set-Aside that requires that 20 percent of the tax increment generated from redevelopment project areas is dedicated to affordable housing projects.

Cities have responded to the affordable housing crisis with a tiered approach that builds on the state mandates, as summarized below.

- ◆ **1st tier: State mandates.** Policies and programs required in general plan housing elements (e.g. density bonuses) and redevelopment project areas (e.g. housing set-asides). These mandates have a minimal impact on affordable housing unless the redevelopment program is significant.
- ◆ **2nd tier: Inclusionary zoning.** Residential development required to include a specified share of affordable housing units or pay in-lieu fee. Moderate impact if inclusionary zoning goals are set high enough and opportunities to evade requirements are limited.
- ◆ **3rd tier: Nonresidential linkage fee.** Impact fee on nonresidential development. Moderate impact because fees are discounted to avoid acting as a disincentive to economic development.
- ◆ **4th tier: Voter-approved tax increase.** Most common example is a general obligation bond funded by a voter-approved property tax increase. Significant impact because of revenue generating potential of broad-based tax.

Dedicated revenues realized from the above sources may be channeled through a **housing trust fund** for allocation to affordable housing projects.

The City of Long Beach is facing the same challenges as other cities in California. Housing demand is increasing faster than supply, causing overcrowding, excessive burdens on household incomes, and low home-ownership rates. The market has responded by producing approximately 2,900 new housing units in the City since 2000. This increased

supply has not been sufficient to moderate price increases, creating incentives to convert over 2,200 rental units to condominiums since 2000. Though the current downturn in the housing market has moderated these forces, long-term trends suggest that there will continue to be a shortage of affordable housing in the City.

The City has complied with the state mandates included in the first tier by adopting policies and goals as outlined in the Housing Element, adopted in 2001, and the Housing Action Plan (HAP) for fiscal years 2005-2009, adopted in June 2004. The City has also conducted studies to determine next steps, including the Housing Trust Fund Study conducted by David Paul Rosen & Associates in 2003 and more recent studies of the impacts of condominium conversion. These policies and studies led to the establishment of the Long Beach Housing Trust Fund in 2006.

PURPOSE OF THIS STUDY

The City of Long Beach is now considering alternatives for generating revenues for the Housing Trust Fund by implementing additional policies and programs in the second and third tiers listed above. MuniFinancial was engaged to update the economic analysis in the 2003 Housing Trust Fund Study and develop recommendations to increase resources for affordable housing. New resources are to come from the following three programs that would impose new obligations on development projects within the City:

- ◆ An inclusionary zoning policy and related in-lieu fee;
- ◆ A commercial linkage impact fee program; and
- ◆ A condominium conversion fee program.

The objective of this study is to identify the appropriate level of fees for each of these programs to increase resources for affordable housing while maintaining adequate incentives for private development within the City.

APPROACH

The first step in the analysis was to assemble the City's affordable housing policies and goals. The analysis compared documented policies and goals with the City's track record of producing affordable housing units.

The next step was the identification of development project prototypes. The selected development prototypes represent a range of typical rental and owner-occupied housing development within the City. The development project prototypes were used to evaluate alternative affordable housing policies.

The third step of the analysis included the calculation of the affordability gap, or the difference between the amount a household at a given income level can afford to pay for housing and the cost to develop housing in Long Beach. The amount of the affordability gap depends on the targeted household income level and the selected development prototypes.

Finally, we evaluated alternative affordable housing policies and associated revenue alternatives (inclusionary zoning in-lieu fee, commercial linkage fee, and condominium

conversion fee) using the development project prototypes. Policy alternatives were evaluated using the following four criteria:

1. Improve effectiveness of current programs;
2. Maximize affordable housing production;
3. Consider comparability with affordable housing programs adopted by other cities in California; and
4. Maintain adequate incentives for private development.

FINDINGS

Our review of existing affordable housing programs found that the City has been more successful in meeting housing production goals for the very low- and low-income categories than for the moderate-income category. At the same time, the market has exceeded regional housing needs for market-rate housing development. Consequently we recommend focusing the proposed programs on production of housing for low and moderate-income households.

To develop recommendations for fee levels we examined market data from mid-2007 and early 2008. This enabled us to test our recommendations against market conditions before and after the recent steep downturn in the housing market. The results of this analysis in terms of the impact on private development were fairly consistent. While housing values have declined since 2007, so have land values. Thus, the burden of the recommended fees on new development remained fairly consistent. These results provide confidence that the recommended fee levels will not place unreasonable disincentives for development in the City.

The recommended fee levels also considered the total impact fee burden in Long Beach relative to selected comparable cities. The fee burden in Long Beach is currently near the top of the range of the selected comparable cities for residential development, and in the middle of the range for office and retail development. With the proposed affordable housing fees, the fee burden in Long Beach would be higher than all comparable cities for residential development, and near the top of the range for nonresidential development.

RECOMMENDATIONS

In setting affordable housing fees, the City must balance the policy goal of generating revenue to provide affordable housing with the policy goal of setting the fees at a level where they will not discourage real estate investment in the City. Though this balance is of particular concern for the commercial linkage impact fee it is also a concern with regards to price pressures on market rate housing and the negative impact on housing affordability in the City.

For the in-lieu fee, it is critical to set the fee equivalent to the cost of providing the required affordable units in order to allow the City to realize the affordable housing goals of the inclusionary zoning requirements. Like new development, condominium conversions represent economic investment in residential neighborhoods. They do not, however,

represent a net addition of housing units. Therefore, the City has more latitude in establishing a fee without the concern that housing development will be stifled.

Based on the findings outlined above, we recommend an inclusionary zoning requirement and related in-lieu fee of five percent of new rental units affordable to lower-income households and ten percent of new owner-occupied units affordable to moderate-income households. We recommend that the same requirement for owner-occupied projects be applied to condominium conversions as well. Finally we recommend a \$4.00 per square foot linkage fee for office and hotel development, and a \$2.00 fee for retail development. We do not recommend a linkage fee for industrial development.

Table ES.1 summarizes our recommendations and provides a schedule of affordable housing fees.

Table ES.1: Proposed Fee Levels (2008\$)

<u>Residential Inclusionary Zoning</u>	<u>% of units</u>	<u>Affordable to</u>	<u>In-lieu Fee</u>
Rental Development	5%	Low Income Households	\$ 10.78 per square foot
Owner-Occupied Development	10%	Moderate Income Households	10.10 per square foot
<u>Condominium Conversions</u>			
Apply Inclusionary Zoning Policy	10%	Moderate Income Households	\$ 10.10 per square foot
<u>Commercial/Industrial Linkage Fee</u>			
Office	\$ 4.00	per square foot	
Retail	2.00	per square foot	
Hotel	4.00	per square foot	
Industrial	-	per square foot	

Sources: Tables 2.16 and 3.16; MuniFinancial.

In order to maintain adequate development feasibility, the proposed inclusionary housing requirements and fees are at the lower end of those found in affordable housing programs in other California cities. We also recommend a set of cost offsets and compliance alternatives to mitigate the impact of the proposed fee programs on development costs. Inclusionary zoning programs can maximize the creation of affordable housing and minimize impacts on the supply and price of market rate housing by providing appropriate cost offsets, developer incentives, and flexibility in how developers can meet inclusionary zoning requirements.

Recommended ways to offset the impact of the proposed affordable housing policies on development costs include:

- ◆ Density and/or height bonus;
- ◆ Expedited permitting;
- ◆ Housing Trust Fund could advance permit fees, to be repaid prior to issuance of Certificate of Occupancy; and
- ◆ Reduced parking requirements.

We recommend including compliance alternatives to provide flexibility in how developers can meet the inclusionary zoning requirements. Possible compliance alternatives include the following:

- ◆ Providing the required affordable on-site with market rate units;
- ◆ Paying an in-lieu fee;
- ◆ Providing the required affordable units at another site in the City;
- ◆ Providing financial assistance in an amount equal to or greater than the in-lieu fee to a non-profit affordable housing project;
- ◆ Donating environmentally clean land, developable for housing, with the land appraised at a value equal to or greater than the in-lieu fee; and
- ◆ Providing handicapped accessible affordable units. Fully accessible units would count as 1.5 units and visitable units would count as 1.25 units toward the required number of affordable units.

Finally, we recommend phasing the proposed inclusionary zoning requirements and affordable housing fees in over three years. This will allow the market to gradually adjust to the new policy. This will also provide time for the development market to recover from its current downturn before the full impact of the new requirements are in effect, preventing the policy from deterring new development during the market downturn and recovery. Based on the length of previous development downturns, the Long Beach development market should substantially recover within three years. **Table ES.2** shows a potential three-year phase in schedule for the proposed affordable housing fees.

Table ES.2: Phase-In Schedule for Proposed Affordable Housing Fees (2008\$)

	FY 2008-09	FY 2009-10	FY 2010-11
<u>Inclusionary Zoning</u>			
<u>Rental Units</u>			
Affordable Units	1%	3%	5%
In-Lieu Fee (per square foot)	\$ 2.16	\$ 6.47	\$ 10.78
<u>Owner-Occupied Units and Condo Conversions</u>			
Affordable Units	3%	6%	10%
In-Lieu Fee (per square foot)	\$ 3.03	\$ 6.06	\$ 10.10
<u>Commercial Linkage Fee (per square foot)</u>			
Office	\$ 1.33	\$ 2.67	\$ 4.00
Retail	0.67	1.33	2.00
Hotel	1.33	2.67	4.00
Industrial	-	-	-

Note: Fee amounts should be updated annually for changes in housing development costs. Fee amounts shown here are in 2008 dollars and do not include an inflation adjustment.

Sources: Tables 2.1, 2.16, and 3.16; MuniFinancial.

Table ES.3 contains a matrix summarizing our findings and recommendations.

Table ES.3: City of Long Beach Affordable Housing Findings and Recommendations

Criteria	Findings	Recommendations
Improve effectiveness of current programs	<ul style="list-style-type: none"> ◆ Achieving housing production goals for very low-income and low-income households. ◆ Not achieving goals for moderate-income households. 	<ul style="list-style-type: none"> ◆ Focus proposed affordable housing programs on production of units for low- and moderate-income households. ◆ Adopt inclusionary zoning requirements and associated in-lieu fees:
Maximize affordable housing production	<ul style="list-style-type: none"> ◆ Subsidy required for moderate-income households is \$115,000 per unit less than for very low-income households, and \$16,000 per unit less than for low-income households. 	<ul style="list-style-type: none"> - 10 percent moderate-income requirement for owner-occupied residential projects and condo conversions (or \$10.78 per sq. ft. in-lieu fee).
Consider comparability with programs adopted by other cities in California	<ul style="list-style-type: none"> ◆ Inclusionary zoning goals range from five to 20 percent ◆ Commercial linkage fees range from \$1 to \$15 per square foot. ◆ Little use of condo conversion fees. 	<ul style="list-style-type: none"> - 5 percent low-income requirement for rental residential projects (or \$10.10 per sq. ft. in-lieu fee). ◆ Adopt commercial/industrial linkage fees: <ul style="list-style-type: none"> - \$4 per sq. ft. on office and hotel development. - \$2 per sq. ft. on retail development. - No fee on industrial development.
Maintain adequate incentives for private development	<ul style="list-style-type: none"> ◆ Currently feasible residential project prototypes can sustain a modest inclusionary zoning in lieu fee. ◆ Office and hotel project prototypes can sustain a greater linkage fee burden compared to the retail project prototype. ◆ Two residential prototypes (owner-occupied townhomes and high-rise condos) and one nonresidential prototype (light manufacturing) not feasible under current market conditions. ◆ With proposed programs Long Beach fee burden is higher than comparable cities for residential development, and near the top of the range for nonresidential development. 	<ul style="list-style-type: none"> ◆ Adopt developer cost offsets for all projects subject to affordable housing fees: <ul style="list-style-type: none"> - Density and/or height bonus (residential projects only). - Expedited permitting. - Deferral of fees until certificate of occupancy. - Reduced parking requirements. ◆ Adopt developer incentive for handicapped accessible units. ◆ Phase fee amounts in over three years.

REVENUE ESTIMATES

Table ES.4 shows the estimated annual revenue that would be generated from the proposed new affordable housing fees. Revenue estimates are based on the average amount of development that has occurred in Long Beach over the past five years. While these figures provide a reasonable estimate of affordable housing revenue based on recent development, actual revenue will vary from these estimates based on actual development that occurs. In addition, if the City phases in the new fees, it will receive reduced revenue during the phase-in period. The estimated in-lieu fee revenue assumes that all residential development subject to the inclusionary zoning policy will comply by paying the in-lieu fee. In reality, it is likely that some development projects will pay the fee while others will provide affordable units on-site.

Table ES.4: Estimated Annual Fee Revenue

Inclusionary Zoning In-Lieu Fee - New Development	\$ 2,955,000
Inclusionary Zoning In-Lieu Fee - Condo Conversions	2,020,000
Commercial Linkage Fee	<u>600,000</u>
Total	\$ 5,575,000

Sources: Tables 6.1-6.3.

1 . INTRODUCTION

This report presents the technical analysis required to impose an affordable housing in-lieu fee, a commercial linkage fee, and a condominium conversion fee in the City of Long Beach. The analysis presented here also includes a review of the adequacy of the Redevelopment Agency Affordable Housing Set-Aside requirement and a discussion of the City's development fee burden in the context of comparable cities.

This introductory chapter describes the study approach and summarizes the affordability gap in Long Beach under the following sections:

- ◆ Background and Purpose;
- ◆ Policy Evaluation Criteria;
- ◆ Need for and Production of Affordable Housing in Long Beach;
- ◆ Methods and Data; and
- ◆ Organization of the Report.

BACKGROUND AND PURPOSE

The City is considering imposing inclusionary zoning requirements and the following affordable housing fees on residential and nonresidential development in Long Beach:

- ◆ Inclusionary Zoning In-Lieu Fee;
- ◆ Commercial Linkage Impact Fee; and
- ◆ Condominium Conversion Fee.

The primary purpose of imposing such policies is to increase the provision of affordable housing in new housing developments and to provide a dedicated funding source for the provision of affordable housing.

An inclusionary zoning policy requires the inclusion of housing units priced for low and moderate-income households with housing projects built privately in the marketplace. Developers are required to provide the affordable units within an otherwise market-priced development. Affordable housing units are built concurrently with market-rate housing.

The primary policy objective of inclusionary zoning is to provide housing for households that otherwise could not afford housing at market rates. By requiring that these affordable units be integrated into new development, an inclusionary zoning policy also provides opportunities for greater racial and economic integration within the housing stock.

Developers may pay a fee in lieu of providing affordable units on-site. Allowing developers to “buy-out” instead of requiring provision of units on-site is a delicate balancing act. When in-lieu fees are set below the level needed to actually fund new affordable housing construction, they can undermine program goals and lead to less affordable housing. For example, a jurisdiction with a 20 percent inclusionary requirement but an in-lieu fee that only captures 25 percent of the true cost to construct a unit might create less affordable housing than another with a 10 percent requirement and no alternative to constructing units on-site.

To meet policy goals, the required fee must be high enough to either dissuade developers from opting out of on-site construction or allow the jurisdiction to finance equivalent affordable units elsewhere. The in-lieu fee may also be applied to small developments where the inclusionary zoning policy would require a fractional number of affordable units.

A condominium conversion fee would require developers to pay a fee to mitigate for the loss of affordable housing units resulting from the removal of rental units from the market. The condominium conversion fee is designed to implement the same policy objectives as the inclusionary zoning policy. As with the inclusionary zoning requirements and in-lieu fee, a condominium conversion fee is invoked based on the City's land use regulatory authority.

A commercial linkage impact fee is assessed on commercial or industrial development. Commercial and industrial development usually results in new jobs, and additional jobs create the need for additional housing, including housing for lower-income wage earners. The purpose of the fee is to partially offset the impact of new nonresidential development on the need for affordable housing.

Fees charged to new development must meet several criteria. First, there must be a reasonable relationship between a fee's use and the type of development project on which the fee is imposed. There must also be a reasonable relationship between the need for the facility or program to be funded by the fee and the type of development on which the fee is imposed. Finally, there must be a reasonable relationship between the amount of the fee and the cost of the public facility or program attributable to the development on which the fee is imposed. The analysis contained Chapters 2, 3, and 4 of this report shows that the proposed fees meet those requirements.

NEED FOR AND PRODUCTION OF AFFORDABLE HOUSING IN LONG BEACH

As the City of Long Beach transitions from an industrial to a service economy, the cost of housing is rising faster than the incomes of residents. The City has documented its need for affordable housing in key policy documents, including the Housing Element, adopted in 2001, the Housing Action Plan (HAP) for fiscal years 2005-2009, adopted in June 2004, and the Housing Trust Fund Study conducted by David Paul Rosen & Associates in 2003. These documents identify housing issues including overcrowding, overpayment, and low home ownership.

Like many cities in California, Long Beach has been experiencing population and job growth, without a comparable increase in housing units. Long Beach is largely built out, but has areas transitioning from industrial to other uses and is also experiencing significant redevelopment.

The City's population is growing at a moderate rate. Between 1990 and 2005 Long Beach increased in population by over 60,000 people, from 429,321 to 489,528. The City reports that while the number of households increased from 158,975 to 163,088 between 1990 and 2000, only 1,271 housing units were added to the housing stock.

The Southern California Association of Governments (SCAG) projects that the population will continue to grow at a rate under one percent per year from 2005 to 2035, resulting in total population of over 560,000, a net increase of 72,000 people. SCAG has projected that

the number of jobs will grow at a faster rate than population and households. **Table 1.1** shows historic and projected population, households, and employment for Long Beach.

Table 1.1: Long Beach Population and Household Projections, 2000-2030

	2000	2005	2010	2020	2030	Growth 2005 - 2030	
						Amount	%
Population	463,406	489,528	503,450	533,590	561,694	72,166	16%
Households	163,088	166,144	171,723	184,906	198,040	31,896	20%
Employment	190,466	192,568	213,998	230,774	245,647	53,079	28%

Source: Southern California Association of Governments.

The scarcity of housing in Long Beach and surrounding areas and recent housing market trends led to a median housing price of over \$500,000 for a single-family residence in 2006. Such rising housing prices increase the need for affordable housing if household incomes do not increase as fast. Since 2006, there has been a decline in housing prices. The median price for a single-family home in the first two months of 2008 was approximately \$475,000.

HOUSING GOALS

The level of affordability to subsidize in housing programs is a policy decision for cities. Housing goals are also informed by regional housing need allocations. SCAG has prepared the Final Regional Housing Need Allocation Plan for the planning period January 1, 2006 to June 30, 2014 as part of the Regional Housing Needs Assessment (RHNA), as mandated by State law. The RHNA goals for Long Beach total 9,583 households, broken out as shown in **Table 1.2.**¹

Table 1.2: RHNA Allocation, 2006-2014

Income Level	RHNA Goals	Percent of Goals
<i>Affordable Units</i>		
Very Low	2,321	43%
Low	1,485	27%
Moderate	1,634	30%
Total - Affordable	5,440	100%
<i>Market</i>	4,143	
Total	9,583	

Source: SCAG.

¹ Final Regional Housing Need Allocation Plan - Planning Period (January 1, 2006 - June 30, 2014) for Jurisdictions within the Six-County SCAG Region, approved by the SCAG Regional Council on July 12, 2007.

In 2005, the City prepared the Housing Action Plan (HAP) to identify affordable housing needs, policies, and production goals for fiscal years 2005 through 2009. The HAP included a proposed allocation of anticipated affordable housing funding between very low-, low-, and moderate-income households. The proposed funding allocation for each income level was based on the percentage of units at each income level in the City's regional housing needs. Based on the funding allocation and the subsidy required per unit in the City's various affordable housing programs, the HAP also identified the number of units that could be anticipated to be produced at each income level.² The funding allocations identified in the HAP are shown in **Table 1.3**.

Table 1.3: Housing Action Plan: Housing Program Allocation, Fiscal Years 2005-2009

Target Population	New Construction		Acquisition/Rehabilitation		Homebuyer Assistance	Total		% of Total
	Units	Cost	Units	Cost		Units	Total Cost	
Very Low Ownership	0	-	40	\$ 1,725,000	-	40	\$ 1,725,000	6%
Very Low Rental	80	\$ 12,000,000	119	16,000,000	NA	199	28,000,000	29%
Subtotal Very Low	80	12,000,000	159	\$ 17,725,000	\$0	239	\$ 29,725,000	35%
Low Ownership	23	\$ 4,575,000	258	\$ 9,875,000	\$ 500,000	281	\$ 14,950,000	41%
Low Rental	35	5,250,000	9	1,250,000	NA	44	6,500,000	6%
Subtotal Low	58	\$ 9,825,000	267	\$ 11,125,000	\$ 500,000	325	\$ 21,450,000	47%
Moderate Ownership	53	\$ 10,675,000	72	\$ 2,650,000	\$ 4,500,000	125	\$ 17,825,000	18%
Moderate Rental	-	-	-	-	NA	-	-	0%
Subtotal Moderate	53	\$ 10,675,000	72	\$ 2,650,000	\$ 4,500,000	125	\$ 17,825,000	18%
Totals	191	\$ 32,500,000	498	\$ 31,500,000	\$ 5,000,000	689	\$ 69,000,000	100%

Source: City of Long Beach Housing Action Plan, p.34.

HOUSING RESOURCES AND PRODUCTION

In 2006, the City established the Housing Trust Fund to provide a dedicated fund for the production of affordable housing. Currently, the Housing Trust Fund has two primary funding sources:

- ◆ Tax increment revenue set-aside (as discussed in Appendix E of this report); and
- ◆ HOME funds from the Federal Department of Housing and Urban Development.

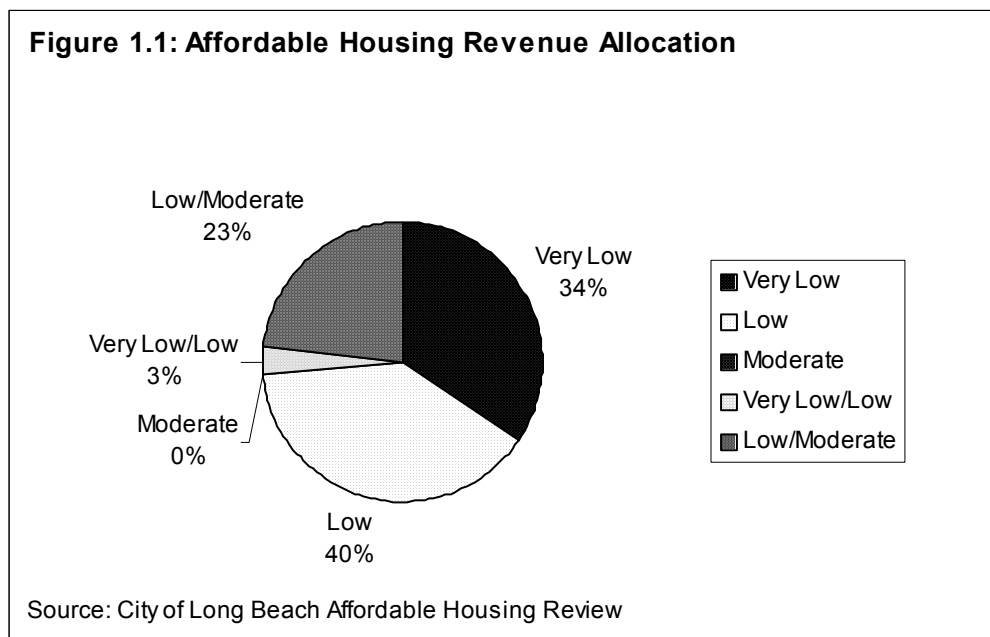
In addition, the Housing Trust Fund occasionally receives funding from several other programs. Many of these programs award funds on a competitive basis. These secondary funding sources include:

- ◆ Affordable Housing Program (AHP) grant funds awarded by the Federal Home Loan Bank;
- ◆ Building Equity and Growth in Neighborhoods (BEGIN) grants from the State of California Department of Housing and Community Development;

² The HAP was based in part on the Housing Element, which documents the City's housing goals, policies and programs, including regional needs adopted by SCAG. Since adoption of the HAP in 2004, SCAG has updated RHNA goals.

- ◆ CalHome grants from the State of California Department of Housing and Community Development;
- ◆ Community Development Block Grant (CDBG) funds from the Federal Department of Housing and Urban Development;
- ◆ HELP funds from the California Housing Finance Agency (CalHFA);
- ◆ City of Industry set-aside funds allocated by the Los Angeles County Community Development Commission;
- ◆ Multi-Family Housing Program (MHP) funds from the State of California Department of Housing and Community Development;
- ◆ Mortgage Revenue Bond proceeds; and
- ◆ Low-Income Housing Tax Credits.

Figure 1.1 shows allocation of affordable housing revenues to affordability levels as presented in the City of Long Beach Affordable Housing Review.



Total affordable housing revenue in 2007 was \$189 million. As shown in the figure, about 77 percent of that revenue is designated for very low and low-income categories. Of the remaining 23 percent, almost all is designated for low and moderate-income categories jointly. Of the \$189 million, only \$125,000 is designated for the moderate-income category.

Affordable housing goals and revenue allocations demonstrate affordable housing policies. Actual housing production demonstrates how revenues are being expended to achieve those goals. Based on recent projects, the City is meeting goals outlined in the HAP for very low-income units. Of housing units currently under construction or in pre-construction or pre-

rehabilitation, 265, or 63% are intended for the very low-income category. **Table 1.4** shows the current pipeline for affordable housing construction through the City's programs.

Table 1.4: Current Housing Units in Development Compared to HAP Goals

Target Population	Units Under Construction	Pre-Construction Units	Total Current Units	HAP Goals
Very Low	106	159	265	239
Low	20	24	44	325
Moderate	32	48	80	125
Market Rate	26	-	26	NA
Manager Units	2	4	6	NA
Totals	186	235	421	689

Sources: *City of Long Beach Affordable Housing Review*; MuniFinancial Table 1.3.

When rehabilitated units are included in production totals, the City of Long Beach is achieving its goals for very low- and low-income units. The City has focused construction and rehabilitation on units for the very low- and low-income categories and will exceed the HAP goals for 2005-2009 when units currently in construction and pre-construction are completed. In contrast, only 80 units for the moderate-income category are currently under construction or in pre-construction and the City has not been attaining its RHNA allocation for moderate-income units.

This review finds that the City has been more successful in meeting housing production goals for the very low and low-income categories than for the moderate-income category. At the same time, the market has exceeded regional housing needs for market-rate housing development, allowing for the opportunity to impose an inclusionary zoning requirement on market rate developments.

REDEVELOPMENT AGENCY AFFORDABLE HOUSING SET-ASIDE

As required under state redevelopment law, the Long Beach Redevelopment Agency contributes 20 percent of the tax increment revenue in redevelopment areas to development of affordable housing target at very low-, low-, and moderate-income households. Appendix E of this report assesses the adequacy of the current Redevelopment Agency affordable housing set-aside. Our analysis of the Redevelopment Agency's budgets for 2008 through 2010 found that approximately 30 percent of redevelopment area tax increment will be used for debt payments and other financing costs during that time. The Agency is required to pass through approximately 16 percent of the anticipated tax increment revenue to the County of Los Angeles and other public agencies. Approximately 34 percent of tax increment revenue, or \$30 million annually, is available for uses other than affordable housing, debt service, and pass-throughs to other agencies.

The Redevelopment Agency also budgets for neighborhood revitalization, corridor revitalization, open space, public art, infrastructure and public improvements, and administration. With the budget information available, we were not able to determine if the Redevelopment Agency could designate a larger portion of tax increment revenue for affordable housing. However, given the ongoing debt service and revenue pass-through requirements, as well as the Agency's mission to remove blight, it is likely that expenditures will continue in the same proportion as budgeted for in fiscal years 2008-2010.

A significant portion of future development in the City is likely to occur in redevelopment areas. We recommend that the City impose the inclusionary zoning and affordable housing fee requirements Citywide, including in redevelopment areas. This will ensure that this development generates affordable housing units and fee revenue in addition to the required tax increment set-aside.

METHODS AND DATA

Our analysis incorporates the most recent data available from public and private data sources, including the following:

- ◆ DataQuick Information Systems land transaction data;
- ◆ *Dollars and Cents of Multifamily Housing: 2006*, published by the Urban Land Institute;
- ◆ RealFacts apartment market data;
- ◆ Colliers International Greater Los Angeles Multifamily Market Report;
- ◆ U.S. Census, 2000;
- ◆ Long Beach Redevelopment Agency reports and budget;
- ◆ American Community Survey, 2006, conducted by the U.S. Census Bureau; and
- ◆ California Employment Development Department employment and wage data.

In addition to these sources, we interviewed local professionals in the real estate, appraisal, and development community, and we looked at additional sources for data on specific conditions in the market and City of Long Beach policies. Our analysis describes the specific data sources and methods we used in more detail.

Preliminary research for this report was completed in the summer and fall of 2007. Since that time, the effects of the downturn in the housing market have become more apparent. For this report, additional research has been conducted so that the development cost and market value figures used in the report represent current market conditions in April 2008. One effect of the residential real estate decline has been a drop in land transactions and development activity, resulting in a lack of current comparable sales upon which to base our development cost and market value assumptions. To the extent they were available, recent sales data were used. We also relied on the informed opinions of professionals familiar with the Long Beach real estate market to guide our development cost and market valuation estimates.

Results from the earlier analysis are included in Appendix D of this report to allow comparison of the effects of the proposed policies near the peak of the housing market cycle

and after a significant decline in values for owner-occupied units. Finding that our proposed affordable housing policies meet the evaluation criteria outlined above (see “Background and Purpose”) at two different points in the development market cycle adds confidence in the recommendations. While we recommend phasing in the proposed inclusionary zoning requirements and fees to allow time for the market to recover from its current downturn, we find that the recommended policies are appropriate in a variety of market conditions.

POLICY EVALUATION CRITERIA

Alternative affordable housing policies and fees were evaluated based on the following policy goals:

1. Improve effectiveness of current Long Beach programs;
2. Maximize affordable housing production in Long Beach;
3. Consider comparability with affordable housing programs adopted by other cities in California; and
4. Maintain adequate incentives for private development in Long Beach.

ORGANIZATION OF THE REPORT

This report has six chapters and five appendices:

- ♦ **Chapter 1: Introduction** (this section) describes the purpose and organization of this report, and the methods and data we used to reach conclusions about affordable housing fees in Long Beach.
- ♦ **Chapter 2: Inclusionary Zoning In-Lieu Fee** summarizes the calculation of the affordability gap for housing in Long Beach and the calculation of the in-lieu fee.
- ♦ **Chapter 3: Commercial Linkage Fee** summarizes the calculation of the commercial linkage fee, including measuring the impact of nonresidential development on the need for affordable housing in Long Beach and findings from the Mitigation Fee Act.
- ♦ **Chapter 4: Condominium Conversion Fee** summarizes the calculation of a condominium conversion fee.
- ♦ **Chapter 5: Maintaining Development Feasibility** summarizes our recommendations for features to include in an affordable housing fee program to maintain the feasibility of private development in Long Beach.
- ♦ **Chapter 6: Fee Revenue Estimates** calculates potential fee revenues based on the current development pipeline and historic development patterns.
- ♦ **Appendix A: In-Lieu Fee Impact Analysis** presents an impact analysis of the proposed in-lieu fees based on residential development returns on cost.

- ◆ **Appendix B: Commercial Linkage Fee Impact Analysis** presents an impact analysis of the proposed linkage fees based on residual land value for non-residential development.
- ◆ **Appendix C: Fee Burden Analysis** presents a comparison of affordable housing and other impact fee burden in Long Beach and surrounding cities.
- ◆ **Appendix D: 2007 Inclusionary Zoning and In-Lieu Fee Analysis** presents the assumptions and results from the in-lieu fee analysis conducted in 2007. That analysis reflects a different point in the housing market cycle and allows for comparison with the findings presented in Chapter 2 and Appendix A, which are based on the most current development cost and market data available.
- ◆ **Appendix E: Redevelopment Agency Set-Aside** summarizes the evaluation of the adequacy of the set-aside.

2. INCLUSIONARY ZONING IN-LIEU FEE

An inclusionary zoning policy is a requirement for a given percentage of units in a residential development project to be made affordable to households at specific income levels. An inclusionary zoning in-lieu fee provides an alternative means for developers to comply with inclusionary zoning requirements by paying a fee to fund the development of affordable housing in lieu of providing affordable units on-site. This section provides proposed inclusionary zoning policy parameters for rental and owner-occupied development and calculates in-lieu fee amounts that would be equivalent to the cost of providing affordable units on-site.

INCLUSIONARY ZONING POLICY GOALS

We recommend an inclusionary zoning requirement of five percent of new rental affordable to lower income households and ten percent of new owner-occupied units affordable to moderate-income households. We arrived at the proposed inclusionary zoning requirements based on a review of the creation of housing units relative to city goals and policies (see Chapter 1) and by evaluating potential policy parameters against the following policy goals:

1. Improve effectiveness of current programs;
2. Maximize affordable housing production;
3. Consider comparability with affordable housing programs adopted by other cities in California; and
4. Maintain adequate incentives for private development.

The inclusionary zoning requirement for owner-occupied new development and conversions of existing rental housing to condominiums is targeted at moderate-income households. Compared with lower income households, moderate-income households have more income to spend on housing, and there is less of a gap between moderate-income households' affordable housing payments and market-rate housing costs. Thus, a higher required percentage of affordable units can be imposed on owner-occupied development without having an unacceptable impact on the feasibility of residential development. The inclusionary zoning policy parameters are shown in **Table 2.1**.

Table 2.1: Policy Parameters

	% of Units	Affordability Target
Rental Development	5%	Low Income
Owner-Occupied Development	10%	Moderate Income

Sources: City of Long Beach; MuniFinancial.

IN-LIEU FEE METHODOLOGY: FUNDING THE HOUSING AFFORDABILITY GAP

The in-lieu fee is a way to comply with the inclusionary zoning requirement as an alternative to constructing affordable housing on-site in a new development. The in-lieu fees calculated in this report are designed to be equivalent to the cost of providing affordable units on-site based on one of the development prototypes considered.

The amount of funding required to provide affordable units is less than the total development cost of those units because, even for affordable units, there will be some rental income or sales income available to partially cover the development costs. The difference between the development costs and the income available to support development costs is referred to as the “affordability gap.” The affordability gap depends on both the development costs and the income level of the households occupying the units.

Although the affordability gap depends on development costs and is different for each particular development, this report calculates the affordability gap for specific prototype developments that are representative of potential new housing developments in Long Beach. The affordability gap is calculated for a prototype rental townhome development and a prototype stacked flats apartment development. The affordability gap is also calculated for three prototype owner-occupied developments: townhomes, stacked flats condominiums, and high-rise condominiums.

The affordability gap is used in calculating both the in-lieu fee and the commercial linkage fee (see Chapter 3). The calculation of the maximum justified commercial linkage fee involves estimating the total affordability gap for the new households generated by non-residential development. The affordability gap estimated for owner-occupied stacked flats condominiums is used for moderate-income households in the linkage fee analysis. For lower income and very low-income households, the apartment affordability gap is used. For this reason, the apartment affordability gap for very low-income households is calculated in this section even though it does not factor into the in-lieu fee analysis.

The methodology for estimating in-lieu fee amounts that would be equivalent to the cost of providing affordable units on-site is slightly different for owner-occupied developments and rental developments. These specific differences will be explained in the respective sections below. The following general steps are used to calculate the in-lieu fees:

1. Estimate the development costs of prototype housing developments.
2. Estimate the amount of development costs that can be supported by income from the developments based on the inclusionary zoning affordability targets.
 - For rental units, this is the value of a mortgage that can be supported by the net operating income of the development. Net operating income is rental income less operating costs.
 - For owner-occupied units, this is the income from selling the units in the development at affordable prices. Affordable prices are based on the mortgage payment that can be supported with the household’s income, given the affordability target, plus a 10% down payment.

3. Calculate the affordability gap. This is the difference between the development costs and the amount calculated in step 2.
4. Based on the number of units in the prototype development, calculate the affordability gap per unit.
5. Based on the inclusionary zoning policy, calculate the percent of the affordability gap that should be paid in the in-lieu fee for each new unit developed. For example, if the inclusionary zoning policy requires that ten percent of new units are affordable, then each new housing unit is responsible for funding ten percent of one affordable unit. Thus, the in-lieu fee should be ten percent of the per-unit affordability gap.
6. Based on the in-lieu fee per unit calculated in step 5 and the estimated average square footage of new units, calculate the in-lieu fee per square foot.

RENTAL DEVELOPMENT AFFORDABILITY GAP

This section calculates the affordability gap for a prototype rental townhome development and a prototype apartment development based on estimated development costs and affordable rent payments.

RENTAL PROTOTYPE DEVELOPMENT COSTS

The prototype developments evaluated in this study are based on the prototypes used in the *City of Long Beach Housing Trust Fund Study* completed in 2003. Characteristics of the prototype rental developments are shown in **Table 2.2**. As shown, the townhome project would include twenty-two units with an average unit size of 1,011 square feet. The project would occupy 0.88 acres. The apartment project would be a five-story development with fifty units on 0.71 acres. The average unit size is 984 square feet.

Table 2.2: Prototype Rental Projects

	Rental Townhomes	Apartments
Total Unit Count	22	50
Zoning	R-3-T	R-4-R, R-4-N
FAR	0.64	1.77
Resident Population	Family	Family
Product Type	Townhomes, 2 stories	Stacked Flats, 5 stories
Construction Type	Type V	Type V
Density (DUs per Acre)	25	70
Land Area (Acres)	0.88	0.71
Number of Units		
1 Bedroom	4	7
2 Bedroom/1 Bath	3	8
2 Bedroom/2 Bath	11	25
3 Bedroom	4	10
Unit Size (Square Feet)		
1 Bedroom	900	800
2 Bedroom/1 Bath	950	950
2 Bedroom/2 Bath	1,000	1,000
3 Bedroom	1,200	1,100
Average	1,011	984
Building Square Feet		
Net Living Area	22,250	49,200
Ratio Net/Gross Square Feet	<u>90%</u>	<u>90%</u>
Gross Square Feet	24,722	54,667
Construction Period (months)	12	12
Lease-Up Period (months)	3	3

Sources: *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; MuniFinancial.

Table 2.3 shows estimated development costs for the two prototype rental developments. Development cost estimates come from a combination of recent market data, proformas for recent projects developed in Long Beach provided by the Long Beach Housing Services Bureau, consultation with developers and real estate professionals in Long Beach, and cost figures from the 2003 *Housing Trust Fund Study*. Figures based on the *Housing Trust Fund Study* were updated for inflation using the *Engineering News-Record* Building Cost Index or the Consumer Price Index for the Los Angeles metropolitan area published by the U.S. Bureau of Labor Statistics.

Table 2.3: Rental Unit Development Costs (2008\$)

	Rental Townhome Project		Apartment Project	
	Unit Cost	Total	Unit Cost	Total
<u>Land</u>	\$ 55.00 per sq. ft.	\$ 2,108,304	\$ 55.00 per sq. ft.	\$ 1,701,018
<u>Direct Costs</u>				
Construction	\$ 97.00 per sq. ft.	2,398,056	\$ 113.00 per sq. ft.	6,177,333
Site Improvements	\$ 7.60 per site sq. ft.	291,329	\$ 7.60 per site sq. ft.	235,050
Subtotal - Direct Costs		2,689,385		6,412,383
<u>Indirect Costs</u>				
Architecture and Engineering	5% direct costs	134,469	5% direct costs	320,619
Hard Cost Contingency	5% direct costs	134,469	5% direct costs	320,619
Permits & Impact Fees	\$ 18,200 per unit	400,400	\$ 18,200 per unit	910,000
Other Indirect Costs ¹	5% direct costs	134,469	5% direct costs	320,619
Subtotal - Indirect Costs		803,808		1,871,857
Subtotal - Land, Direct, and Indirect Costs		5,601,497		9,985,259
<u>Construction Loan Costs</u>				
Construction Loan as a % of				
Land, Direct, Indirect Costs	75% \$	4,201,122	75% \$	7,488,944
Fees, Title, and Closing	1.25% loan amount	52,514	1.25% loan amount	93,612
Average Loan Balance				
(Construction/Lease-Up)	60% \$	2,520,673	60% \$	4,493,366
Construction/Lease-Up Interest ²	7% per year	220,559	7% per year	393,170
<u>Marketing/Leasing/Startup Costs</u>				
Marketing/Leasing/Startup Costs	\$ 1,200 per unit	26,400	\$ 1,200 per unit	60,000
Market Study/Consulting	estimated project cost	29,600	estimated project cost	29,600
Subtotal - Development Costs		5,930,570		10,561,640
<u>Developer Overhead</u>				
	4% above costs	237,223	4% above costs	422,466
Development Cost		6,167,792		10,984,106
Developer Profit	12% dev. cost	740,135	12% dev. cost	1,318,093
Total Developer Cost and Profit		\$ 6,907,927		\$ 12,302,198
Cost per Unit		\$ 313,997		\$ 246,044

¹ Includes insurance and taxes during construction, legal, title, appraisal, soils testing, and environmental costs.

² Estimated construction loan term includes 12 month construction period and 3 month lease-up period, for a total of 15 months.

Sources: Table 2.2; DataQuick Information Systems; *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; Consumer Price Index for Los Angeles-Riverside-Orange County, CA, U.S. Bureau of Labor Statistics; Building Cost Index, *Engineering News-Record*; MuniFinancial.

Land costs account for a significant portion of the development costs. The estimated land value was estimated in mid-2007 based on the median price per square foot of vacant land sales with multifamily zoning over the past five years. Land transaction data were provided by DataQuick Information Services. Since mid-2007, the decline in the residential real estate market has reduced the value of land suitable for residential development; however, there has been little recent sales activity of vacant residential parcels upon which to base an updated land value. According to an appraiser familiar with the Long Beach market, residential land values have declined approximately 20 percent from their mid-2007 levels. The residential land value used in this study is based on a 20 percent reduction from the mid-2007 value. For comparison, we also considered trends in home sales prices documented by DataQuick Information Services. While changes in price varied between different areas in the City, the data indicated an overall average drop of approximately 10 percent.

Construction costs for these prototype developments are based on proformas for recent affordable apartment developments in Long Beach. Relative differences in construction costs for different types of construction are based on figures used in the *Housing Trust Fund Study*. Estimated site improvement costs are the *Housing Trust Fund Study* costs updated for inflation.

Architecture and engineering costs and a hard cost contingency are both estimated at five percent of construction and site improvement costs. Based on the development fee burden analysis conducted for this study, the estimated cost of permits and impact fees is approximately \$18,200 per unit. This includes the recently adopted public safety fees and recent increases in the parks and school fees. As shown in the table, other indirect costs are estimated to total five percent of construction and site improvement costs.

The development costs for the prototype projects include financing costs incurred during the development period. The financing scenario is based on the scenario used in the prototype developments in the *Housing Trust Fund Study*, based on input from the development community. A construction loan for 75 percent of the land, direct, and indirect costs, would be needed. Estimated total interest payments are based on an average loan balance of 60 percent and a seven percent annual interest rate. In addition, loan fees, title fees, and other closing costs total 1.25 percent of the total loan amount.

Marketing, leasing and startup costs are estimated at \$1,200 per unit, based on *Housing Trust Fund Study* figures, updated for inflation. A market study and consulting costs are estimated at \$29,600 per development, also based on the *Housing Trust Fund Study*.

Developer overhead costs are estimated at four percent of development costs (excluding profit), and developer profit is estimated at twelve percent of total development costs. Both of these figures are used in the *Housing Trust Fund Study*. A twelve percent profit was identified as the minimum profit necessary for a residential development to be feasible.

Based on the unit development costs outlined above, the total cost of the townhome prototype development is approximately \$6.9 million, or \$314,000 per unit. The apartment project prototype is estimated to cost approximately \$12.3 million, or \$246,000 per unit.

AFFORDABLE MONTHLY RENT

As explained above, the affordability gap for a housing unit is the difference between the development costs that can be supported by income from the unit and the actual cost of developing the unit. For rental developments, income comes from rent paid by the households occupying the units. Estimated rental income is based on the maximum affordable rent payments from households at the income level targeted by the inclusionary zoning policy. The income levels for each household size are calculated as a percentage of the area median income (AMI) for each household size, as reported by the California Department of Housing and Community Development. The percentages of AMI used as cutoffs for very low-, low-, and moderate-income households are those used for affordable housing projects funded by the Long Beach Redevelopment Agency, consistent with California Redevelopment Law. **Table 2.4** shows the affordable monthly rent payment for households at the very low-income and low-income levels.

For renter households, the maximum affordable housing cost is defined as thirty percent of gross income. The thirty percent affordability standard is used in federal housing programs

and state redevelopment law. A utility allowance is subtracted from the total affordable housing costs to yield the affordable monthly rent. The utility allowance is based on the utility allowance used in affordable rent calculations prepared by Keyser Marston Associates for the City of Long Beach.

Table 2.4: 2008 Income Standards and Affordable Monthly Rent (2008\$)

Household Size	2 Persons/ 1 Bedroom	3 Persons/ 2 Bedroom	4 Persons/ 3 Bedrooms
<i>Area Median Income</i>	\$ 47,800	\$ 53,800	\$ 59,800
<i>Very Low Income (50% AMI)</i>			
Annual Income	\$ 23,900	\$ 26,900	\$ 29,900
Affordable Annual Housing Costs (30% of Income)	7,170	8,070	8,970
Affordable Monthly Housing Costs	\$ 598	\$ 673	\$ 748
Utility Allowance	51	74	101
Affordable Monthly Rent	\$ 547	\$ 599	\$ 647
<i>Low Income (60% AMI)</i>			
Annual Income	\$ 28,680	\$ 32,280	\$ 35,880
Affordable Annual Housing Costs (30% of Income)	8,604	9,684	10,764
Affordable Monthly Housing Costs	\$ 717	\$ 807	\$ 897
Utility Allowance	51	74	101
Affordable Monthly Rent	\$ 666	\$ 733	\$ 796

Sources: California Department of Housing and Community Development; City of Long Beach; Keyser Marston Associates; MuniFinancial.

OPERATING COSTS

Annual operating costs for rental units must be subtracted from rental income to estimate the net operating income, which is used to determine the level of development costs the rental income can support. Property tax rates vary a small amount within Long Beach depending on the level of special assessments that are charged in a given area, but 1.1 percent is a representative rate assumed for these prototype developments. Per-unit management costs, insurance, and maintenance costs are based on survey data for properties with less than one hundred units in the Los Angeles area shown in the Urban Land Institute's *Dollars & Cents of Multifamily Housing, 2006*. An annual replacement reserve fund contribution of \$250 is included in the operating costs, consistent with the *Housing Trust Fund Study* and operating cost estimates shown in recent Long Beach affordable development proformas. **Table 2.5** shows estimated operating costs for the prototype rental developments.

Table 2.5: Rental Operating Costs (2008\$)

	Unit Cost	Number of Units	Total Cost
<i>Rental Townhomes</i>			
Taxes	1.10% of total dev. cost	\$ 6,907,927 dev. cost	\$ 75,987
Management Costs	\$ 900 per unit	22 units	19,800
Insurance	286 per unit	22 units	6,292
Maintenance	1,035 per unit	22 units	22,770
Replacement Reserve	250 per unit	22 units	5,500
Total Annual Operating Costs			\$ 130,349
<i>Apartments</i>			
Taxes	1.10% of total dev. cost	\$ 12,302,198 dev. cost	\$ 135,324
Management Costs	\$ 900 per unit	50 units	45,000
Insurance	286 per unit	50 units	14,300
Maintenance	1,035 per unit	50 units	51,750
Replacement Reserve	250 per unit	50 units	12,500
Total Annual Operating Costs			\$ 258,874

Sources: Los Angeles County Assessor; Table 3-271 Market Rent Properties in Los Angeles-Long Beach-Santa Ana, CA, MSA, Less than 100 Units, *Dollars and Cents of Multifamily Housing: 2006*, Urban Land Institute; *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; MuniFinancial.

NET OPERATING INCOME

Based on the affordable rent and the annual operating costs shown above, **Table 2.6** shows the annual net operating income for the prototype developments. A three percent annual loss to vacancy is assumed.

Table 2.6: Rental Net Operating Income (2008\$)

	Number of Units	Affordable Rent ¹	Monthly Income	Annual Income
<i>Townhome Project - Lower Income</i>				
1 Bedroom	4	\$ 666	\$ 2,664	\$ 31,968
2 Bedroom	14	733	10,262	123,144
3 Bedroom	4	796	3,184	38,208
Subtotal				\$ 193,320
Loss to Vacancy (3%)				(5,800)
Total Income				\$ 187,520
Operating Costs				130,349
Net Operating Income				\$ 57,171
<i>Apartment Project - Lower Income</i>				
1 Bedroom	7	\$ 666	\$ 4,662	\$ 55,944
2 Bedroom	33	733	24,189	290,268
3 Bedroom	10	796	7,960	95,520
Subtotal				\$ 441,732
Loss to Vacancy (3%)				(13,252)
Total Income				\$ 428,480
Operating Costs				258,874
Net Operating Income				\$ 169,606
<i>Apartment Project - Very Low Income</i>				
1 Bedroom	7	\$ 547	\$ 3,826	\$ 45,906
2 Bedroom	33	599	19,751	237,006
3 Bedroom	10	647	6,465	77,580
Subtotal				\$ 360,492
Loss to Vacancy (3%)				(10,815)
Total Income				\$ 349,677
Operating Costs				258,874
Net Operating Income				\$ 90,803

¹ Assumes two persons per bedroom.

Sources: Tables 2.2, 2.4 and 2.5; MuniFinancial.

SUPPORTABLE MORTGAGE

Table 2.7 shows the mortgage amount that could be supported by the net operating income generated by the prototype developments. Consistent with the *Housing Trust Fund Study*, it is assumed that a 1.25 coverage ratio would be required, meaning the annual net operating income must be at least 1.25 times the annual mortgage payment. It is assumed that the developments would be financed with a thirty-year mortgage at a seven percent interest rate.

Table 2.7: Supportable Mortgage (2008\$)

	Rental Townhome Project - Lower Income	Apartment Project - Lower Income	Apartment Project - Very Low Income
Net Operating Income	\$ 57,171	\$ 169,606	\$ 90,803
Coverage Ratio	1.25	1.25	1.25
Supportable Annual Payment	\$ 45,737	\$ 135,685	\$ 72,642
Mortgage Term	30 years	30 years	30 years
Interest Rate	7%	7%	7%
Supportable Mortgage	\$ 572,884	\$ 1,699,536	\$ 909,892

Sources: Table 2.6; MuniFinancial.

RENTAL AFFORDABILITY GAP

Table 2.8 shows the affordability gap for the prototype development projects. The affordability gap is the difference between the total development costs and the development costs that could be supported by the project's income. The development costs that could be supported by the project's income are equal to the supportable mortgage, shown in the table above.

Table 2.8 also shows affordability gap per unit for each prototype development. This is the per-unit subsidy that would be required, in addition to the rental income, to make the development financially feasible at the target household income level.

Table 2.8: Affordability Gap on Rental Units (2008\$)

	Rental Townhome Project - Lower Income	Apartment Project - Lower Income	Apartment Project - Very Low Income
Development Costs	\$ 6,907,927	\$ 12,302,198	\$ 12,302,198
Supportable Mortgage	572,884	1,699,536	909,892
Affordability Gap	\$ 6,335,043	\$ 10,602,662	\$ 11,392,306
Number of Units	22	50	50
Affordability Gap per Unit	\$ 287,957	\$ 212,053	\$ 227,846

Sources: Tables 2.2, 2.3, and 2.7; MuniFinancial.

As shown in Table 2.1, the proposed inclusionary zoning policy would require that five percent of new rental units be made affordable to low-income households. The cost of providing a unit affordable to low-income households is equal to the affordability gap for low-income households. Thus, the cost of achieving the policy goal per new market rate unit is five percent of the per-unit affordability gap. An equivalent cost per square foot is calculated based on cost per unit and the average square footage of the prototype units. The in-lieu costs per unit and per square foot are shown in **Table 2.9**.

Table 2.9: Rental Housing Inclusionary Zoning In-Lieu Costs (2008\$)

	Rental Townhome Project	Apartment Project
Gap per Affordable Unit (Low Income Households)	\$ 287,957	\$ 212,053
Inclusionary Zoning Requirement	5%	5%
In-Lieu Cost per Market Rate Unit	\$ 14,398	\$ 10,603
Average Square Feet per Unit	1,011	984
In-Lieu Cost per Square Foot	\$ 14.24	\$ 10.78

Sources: Tables 2.1, 2.2 and 2.8; MuniFinancial.

OWNER-OCCUPIED HOUSING AFFORDABILITY GAP ANALYSIS

The following section describes a calculation of the affordability gap for three prototypes of owner-occupied residential developments: an owner-occupied town home development, a mid-rise stacked flats condominium development, and a high-rise condominium development. The affordability gap is then used to calculate an in-lieu fee for owner-occupied developments at a level equivalent to complying with the proposed inclusionary zoning policy by providing affordable units on-site. The process for calculating the in-lieu fee for owner-occupied developments is very similar to the methodology used to calculate the in-lieu fee for rental developments.

OWNER-OCCUPIED PROTOTYPE DEVELOPMENT COSTS

As with the rental development prototypes, the owner-occupied prototype developments evaluated in this study are based on the prototypes used in the *City of Long Beach Housing Trust Fund Study* completed in 2003. **Table 2.10** shows characteristics of the three owner-occupied prototype developments. As shown, the townhome project would include twenty-two units with an average unit size of 1,182 square feet. The project would occupy 0.88 acres. The apartment project would be a five-story development with fifty units on 0.71 acres. The average unit size is 1,118 square feet. Finally, the high-rise condo project prototype is a nine-story building with 100 units occupying one acre.

Table 2.10: Prototype Owner-Occupied Projects

	Owner-Occupied Townhome Project	Stacked Flats Condo Project	High-Rise Condo Project
Total Unit Count	22	50	100
Zoning	R-3-T	R-4-R, R-4-N	R-4-U
FAR	1	2	3
Resident Population	Family	Family	Family
Product Type	Townhomes, 2 stories	Stacked Flats, 5 stories	Stacked Flats, 9 stories
Construction Type	Type V	Type V	Type I
Density (DUs per Acre)	25	70	100
Land Area (Acres)	0.88	0.71	1.00
Number of Units			
Lofts	-	-	10
1 Bedroom	-	7	10
2 Bedroom	13	33	60
3 Bedroom	9	10	20
Unit Size (Square Feet)			
Lofts	-	-	800
1 Bedroom	-	800	800
2 Bedroom	1,100	1,100	1,100
3 Bedroom	1,300	1,400	1,400
Average	1,182	1,118	1,100
Building Square Feet			
Net Living Area	26,000	55,900	110,000
Ratio Net/Gross Square Feet	<u>90%</u>	<u>90%</u>	<u>85%</u>
Gross Square Feet	28,889	62,111	129,412
Construction Period (months)	15	18	18

Sources: *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; MuniFinancial.

Table 2.11 shows the estimated development costs for the owner-occupied prototype developments. Development cost estimates are similar to those used for the prototype rental developments, coming from a combination of recent market data, proformas for recent projects developed in Long Beach provided by the Long Beach Housing Services Bureau, consultation with developers and real estate professionals in Long Beach, and cost figures from the 2003 *Housing Trust Fund Study*. Figures based on the *Housing Trust Fund Study* were updated for inflation using the *Engineering News-Record* Building Cost Index or the Consumer Price Index for the Los Angeles metropolitan area published by the U.S. Bureau of Labor Statistics.

Compared with the same type of rental development, the owner-occupied prototype developments have higher construction costs because owner-occupied developments often have higher-quality materials and finishes than rental developments. Instead of the market

study and lease-up costs incurred in rental developments, owner-occupied developments pay sales commissions and other closing costs at the time the new units are sold. Estimates of these costs are based on those used in the 2003 *Housing Trust Fund Study*.

Based on the development cost estimates, the total development cost of the owner-occupied townhome prototype development is approximately \$8.5 million, or \$387,000 per unit. The stacked flat condo prototype has estimated development costs of \$15.6 million, or \$311,000 per unit. The high-rise condo development prototype has development costs of \$43.6 million, or \$436,000 per unit.

Table 2.11: Owner-Occupied Unit Development Costs (2008\$)

	Owner-Occupied Townhome Project		Stacked Flat Condo Project		High-Rise Condo Project	
	Unit Cost	Total	Unit Cost	Total	Unit Cost	Total
<u>Land</u>	\$ 55.00 per sq. ft.	\$ 2,108,304	\$ 55.00 per sq. ft.	\$ 1,701,018	\$ 55.00 per sq. ft.	\$ 2,395,800
<u>Direct Costs</u>						
Construction	\$ 102.00 per sq. ft.	2,946,667	\$ 118.00 per sq. ft.	7,329,111	\$ 191.00 per sq. ft.	24,717,647
Site Improvements	7.60 per site sq. ft.	<u>291,329</u>	7.60 per site sq. ft.	<u>235,050</u>	7.60 per site sq. ft.	<u>331,056</u>
Subtotal - Direct Costs		3,237,996		7,564,161		25,048,703
<u>Indirect Costs</u>						
Architecture and Engineering	5% direct costs	161,900	5% direct costs	378,208	5% direct costs	1,252,435
Hard Cost Contingency	5% direct costs	161,900	5% direct costs	378,208	5% direct costs	1,252,435
Permits & Impact Fees	\$ 18,200 per unit	400,400	\$ 18,200 per unit	910,000	\$ 18,200 per unit	1,820,000
Other Indirect Costs ¹	5% direct costs	<u>161,900</u>	5% direct costs	<u>378,208</u>	5% direct costs	<u>1,252,435</u>
Subtotal - Indirect Costs		886,099		2,044,624		5,577,305
Subtotal - Land, Direct, and Indirect Costs		6,232,399		11,309,803		33,021,809
<u>Construction Loan Costs</u>						
Construction Loan as a % of Land, Direct, Indirect Costs	85% \$	5,297,539	85% \$	9,613,333	85% \$	28,068,537
Fees, Title, and Closing	1.25% loan amount	66,219	1.25% loan amount	120,167	1.25% loan amount	350,857
Average Loan Balance (Construction/Sales Period)	60% \$	3,178,524	60% \$	5,768,000	60% \$	16,841,122
Construction/Sales Period Interest ²	7% per year	500,617	7% per year	1,009,400	7% per year	2,947,196
<u>Sales Costs</u>						
Commissions/Selling/Closing Costs	6% total dev. cost	<u>510,890</u>	6% total dev. cost	<u>934,686</u>	6% total dev. cost	<u>2,729,050</u>
Subtotal - Development Costs		7,310,126		13,374,056		39,048,912
<u>Developer Overhead</u>						
Developer Overhead	4% above costs	292,405	4% above costs	534,962	4% above costs	1,561,956
Development Cost		7,602,531		13,909,018		40,610,868
Developer Profit	12% dev. cost	<u>912,304</u>	12% dev. cost	<u>1,669,082</u>	12% dev. cost	<u>4,873,304</u>
Total - Developer Cost and Profit		\$ 8,514,835		\$ 15,578,100		\$ 45,484,173
Cost per Unit		\$ 387,038		\$ 311,562		\$ 454,842

¹ Includes insurance and taxes during construction, legal, title, appraisal, soils testing, and environmental costs.

² Construction loan interest based on 7% interest rate and construction/lease-up period shown in Table 2.10.

Sources: DataQuick Information Systems; *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; Consumer Price Index for Los Angeles-Riverside-Orange County, CA, U.S. Bureau of Labor Statistics; Building Cost Index, *Engineering News-Record*; MuniFinancial.

AFFORDABLE UNIT SALE PRICES

The affordability gap for an owner-occupied unit is the difference between the price that a household at the target income level can afford to pay for the unit and the actual development costs of the unit. The maximum affordable sale price is based on the size of mortgage affordable to a household at the target income level. The proposed inclusionary zoning policy would require ten percent of new owner-occupied units to be affordable to moderate-income households. For homeowner households, maximum housing costs are defined as 35 percent of gross income, based on typical lender requirements. Housing costs include mortgage principal and interest payments, property taxes, fire and casualty insurance, utilities, and homeowner association fees.

Table 2.12 shows the affordable monthly housing costs for moderate-income households in Long Beach. The income cutoff for moderate-income households is 110 percent of the area median income (AMI) published by the California Department of Housing and Community Development. This is the same standard used for moderate-income housing funded by the Long Beach Redevelopment Agency, consistent with California Redevelopment Law. Based on annual income, affordable total monthly housing costs are calculated. Property taxes, utility costs, maintenance expenses, insurance, and homeowner association fees are deducted from affordable monthly housing costs to estimate the moderate-income household's affordable mortgage payment. Property taxes and assessments are estimated at 1.1 percent annually in Long Beach. Estimated utility, maintenance, insurance, and homeowners association costs are based on affordable unit price estimates prepared for the City of Long Beach by Keyser Marston Associates, Inc.

Assuming a 6.5 percent interest rate and a thirty-year term, the mortgage amount that would have the maximum affordable monthly mortgage payment is shown in the table below. This mortgage amount, plus a five percent down payment, is estimated to be the maximum sale price that would be affordable to a household at the moderate-income level.

Table 2.12: 2008 Income Standards and Affordable Owner-Occupied Housing Target Prices (2008\$)

Household Size	1 person/ 0 bedrooms (loft)		2 persons/ 1 bedroom		3 persons/ 2 bedrooms		4 persons/ 3 bedrooms	
	Area Median Income	\$ 41,900	\$ 47,800	\$ 53,800	\$ 59,800			
Affordable Income Target (Moderate Income - 110% AMI)	46,090	52,580	59,180	65,780				
Affordable Annual Housing Costs (35% of Income)	16,132	18,403	20,713	23,023				
Affordable Monthly Housing Costs	1,344	1,534	1,726	1,919				
Property Taxes and Assessments ¹	\$ 143	\$ 163	\$ 181	\$ 199				
Utilities	68	78	109	142				
Maintenance/Insurance/HOA Dues	200	225	250	275				
Affordable Mortgage Payment	\$ 934	\$ 1,068	\$ 1,186	\$ 1,303				
Supportable Mortgage ²	\$ 147,729	\$ 168,906	\$ 187,642	\$ 206,103				
Down Payment (5%)	7,775	8,890	9,876	10,848				
Affordable Unit Price	\$ 155,504	\$ 177,796	\$ 197,518	\$ 216,951				

¹ Based on 1.1% estimated property tax rate and assessed value equal to affordable mortgage plus 5% downpayment.

² Based on 6.5% interest rate and 30 year term.

Sources: California Department of Housing and Community Development; Los Angeles County Assessor; Keyser Marston Associates; MuniFinancial.

Based on the affordable sale prices calculated above, **Table 2.13** shows the total revenue that would result from selling the units in the prototype developments at prices affordable to moderate-income households.

Table 2.13: Revenue on Owner-Occupied Developments (2008\$)

	Number of Units	Affordable Sale Price	Total Revenue
<i>Owner-Occupied Townhomes (Moderate Income)</i>			
Lofts	-	\$ 155,504	\$ -
1 Bedroom	-	177,796	-
2 Bedroom	13	197,518	2,567,733
3 Bedroom	9	216,951	1,952,556
Subtotal			\$ 4,520,289
<i>Stacked Flats Condos (Moderate Income)</i>			
Lofts	-	\$ 155,504	\$ -
1 Bedroom	7	177,796	1,244,574
2 Bedroom	33	197,518	6,518,091
3 Bedroom	10	216,951	2,169,507
Subtotal			\$ 9,932,172
<i>High-Rise Condos (Moderate Income)</i>			
Lofts	10	\$ 155,504	\$ 1,555,040
1 Bedroom	10	177,796	1,777,962
2 Bedroom	60	197,518	11,851,075
3 Bedroom	20	216,951	4,339,013
Subtotal			\$ 19,523,090

Sources: Tables 2.10 and 2.12; MuniFinancial.

OWNER-OCCUPIED DEVELOPMENT AFFORDABILITY GAP

Table 2.14 shows the total affordability gap if the all units in the prototype owner-occupied developments were sold at prices affordable to moderate-income households. The affordability gap is the difference between each project's development costs, as shown in Table 2.11, and the total revenue from selling units at affordable prices, as shown in Table 2.13 above.

Table 2.14: Affordability Gap on Owner-Occupied Units (2008\$)

	Owner-Occupied Townhome Project	Stacked Flats Condo Project	High-Rise Condo Project
Development Costs	\$ 8,514,835	\$ 15,578,100	\$ 45,484,173
Total Affordable Sales Price	<u>4,520,289</u>	<u>9,932,172</u>	<u>19,523,090</u>
Affordability Gap	\$ 3,994,546	\$ 5,645,928	\$ 25,961,082
Number of Units	<u>22</u>	<u>50</u>	<u>100</u>
Affordability Gap per Unit	\$ 181,570	\$ 112,919	\$ 259,611

Sources: Tables 2.10, 2.11 and 2.13; MuniFinancial.

Table 2.15 shows the in-lieu fee for owner-occupied units that would be equivalent to the cost of meeting the inclusionary zoning requirement by providing the required affordable units on-site. As shown in Table 2.1, the proposed inclusionary zoning policy would require that ten percent of new owner-occupied housing units are affordable to households at the moderate-income level. The cost of providing a unit affordable to households at the moderate-income level is equal to the affordability gap for that income level. Thus, the cost of achieving the policy goal per new market rate unit is ten percent of the per-unit affordability gap. An equivalent cost per square foot is calculated based on the cost per unit and the average square footage of the prototype units.

Table 2.15: Owner-Occupied Housing Inclusionary Zoning In-Lieu Costs (2008\$)

	Owner-Occupied Townhomes	Stacked Flats Condos	High-Rise Condos
Gap per Affordable Unit	\$ 181,570	\$ 112,919	\$ 259,611
Inclusionary Zoning Requirement	<u>10%</u>	<u>10%</u>	<u>10%</u>
In-Lieu Cost per Market Rate Unit	\$ 18,157	\$ 11,292	\$ 25,961
Average Square Feet per Unit	<u>1,182</u>	<u>1,118</u>	<u>1,100</u>
In-Lieu Cost per Square Foot	\$ 15.36	\$ 10.10	\$ 23.60

Sources: Table 2.1, 2.10 and 2.14; MuniFinancial.

These tables show the fees that are estimated to be financially equivalent to complying with the inclusionary zoning requirements by building affordable units on-site for the prototype developments. The cost of complying with the inclusionary zoning requirements depends on the cost of development; thus the equivalent in-lieu fee is different for the different prototype developments.

OWNER-OCCUPIED AND RENTAL AFFORDABILITY GAP COMPARISON

Comparing the results presented in Tables 2.8 and 2.14 shows that the affordability gap for moderate-income households in owner-occupied units is less than the affordability gap for very low- and low-income households in rental units. This is because moderate-income households can afford to spend more on housing and the housing costs affordable to a moderate-income household can support a higher amount of development costs, compared to a low- or very--low-income household.

Using the least expensive prototypes examined, namely the rental apartment project and the stacked flats condo project, the affordability gap for a moderate-income ownership household, approximately \$113,000, is just over half of the \$212,000 affordability gap for a low-income renter household. A very low-income household has an affordability gap of \$228,000, or approximately \$16,000 more than a low-income household. By targeting affordable owner-occupied housing to moderate-income households and rental housing to low-income households, the policy can require a higher percentage of affordable units in owner-occupied developments than rental developments while imposing a similar burden on each type of development.

IN-LIEU FEE SCHEDULE

Table 2.16 shows a proposed fee schedule for the inclusionary zoning in-lieu fee. The proposed in-lieu fee for owner-occupied developments is set at the level equivalent to the cost of complying with the proposed inclusionary zoning policy by providing on-site affordable units based on the stacked flat condo development prototype. The rental in-lieu fee is equivalent to the cost of providing the required affordable units on site for the apartment prototype. The actual cost of providing affordable units on-site for a particular development depends on the development costs specific to that project; however, for ease of implementation, a single in-lieu fee for all owner-occupied developments and a single fee for renter developments is proposed. These prototypes were selected as the basis for the in-lieu fee because they are the least costly of the prototype developments examined, thus imposing the lowest burden on housing developers while still allowing the City to realize the affordable housing goals of the inclusionary zoning requirements.

It is recommended that the City update the fees annually to account for changes in the cost of providing affordable housing units. This update could be based on the annual change in the *Engineering News-Record* Building Cost Index for Los Angeles.

Table 2.16: In-Lieu Fee Schedule (2008\$)

	\$/sq. ft.
Owner-Occupied Developments	\$ 10.10
Rental Developments	10.78

Sources: Tables 2.9 and 2.15.

The proposed in-lieu fees meet the general requirements for fees charged to new development:

- ◆ *There is a reasonable relationship between the fee's use and the type of development project on which the fee is imposed.* In-lieu fee revenues will be used to fund achievement of the proposed inclusionary zoning policy goals of including affordable housing with new housing development. The fee charged to owner-occupied development will be used to fund the development of owner-occupied housing affordable to moderate-income households and the fee charged to rental development will be used to fund rental housing affordable to lower-income households.
- ◆ *There is a reasonable relationship between the need for the facility or program to be funded by the fee and the type of development on which the fee is imposed.* As documented in the introduction to this report (Chapter 1), there is a need for increased affordable housing in Long Beach. Lower-income households are more likely to inhabit rental housing, compared with moderate-income households, and the proposed policy targets affordable owner-occupied housing for moderate-income households and rental housing for lower-income households. Paying an in-lieu fee gives housing developers a way of meeting the need for affordable housing units established by City policy for their specific type of development.
- ◆ There is a reasonable relationship between the amount of the fee and the cost of the public facility or program attributable to the development on which the fee is imposed. The above in-lieu fee analysis documents a reasonable relationship between the cost of providing the affordable units required by the inclusionary zoning policy and proposed per square foot in-lieu fees. Charging the in-lieu fee to development projects based on square footage ensures that there is a reasonable relationship between the total fee charged and affordable housing needs associated with each particular development project.

RETURN ON COST FEASIBILITY ANALYSIS

A return on cost analysis of the prototype developments was performed to evaluate the proposed inclusionary zoning policy parameters against the policy evaluation criteria of maintaining adequate incentives for private development. The return on cost analysis estimates the impacts of the proposed inclusionary zoning policy on the feasibility of residential development in Long Beach. Return on cost is a developer's profit margin, or the percentage by which sales revenues exceed or fall short of development costs. The estimated return on cost is compared to the hurdle rate necessary for a development to be financially

feasible. The minimum return on cost required for a development to be feasible is estimated at twelve to sixteen percent. This feasibility hurdle is based on input from the building industry collected for the *Housing Trust Fund Study* and industry standards.

The details of the analysis based on current market conditions are presented in Appendix A. The return on cost is also shown based on market conditions in mid-2007, prior to deterioration in the residential development market. The details of the mid-2007 return on cost analysis are shown in Appendix D. While several of the factors influencing development cost and revenues changed between the analysis conducted in the mid-2007 and the current analysis, the factors having the largest impact on return on cost were an estimated 20 percent drop in land cost and a 10 percent drop in condominium sales prices. Apartment rents showed a small increase from mid-2007 to the current analysis. Finding that the proposed inclusionary zoning requirements continue to meet the evaluation criteria of maintaining adequate incentives for private development at two different points in the market cycle and for a variety of different development prototypes increases confidence in the suitability of the recommendations.

RENTAL DEVELOPMENT RETURN ON COST

Tables 2.17a and 2.17b show the return on cost for this study's rental development prototypes under current market conditions and under mid-2007 market conditions. Under current market conditions, both rental prototypes are currently feasible and would remain feasible if the proposed inclusionary zoning policy were imposed. The proposed inclusionary zoning policy would reduce the developments' return on cost by four to five percentage points. The analysis conducted with mid-2007 market conditions found that rental townhome development would not be feasible, even without any inclusionary zoning requirement. Stacked flats apartments were found to be feasible with the proposed inclusionary zoning requirements.

From the mid-2007 market conditions to the current market, the analysis finds that rental development has become more feasible. This is primarily because with the drop in estimated land costs, development costs have decreased. Market rents have risen slightly over the same time period, increasing revenues from rental development. Market reports show that capitalization rates have decreased, reflecting a higher price per unit for a given amount of rental income.

Table 2.17a: Return on Cost, Rental Developments - Current Market Conditions

	Rental Townhome Project	Apartment Project
Operating Income-Market Rent	\$ 534,840	\$ 1,087,560
Operating Costs	<u>130,349</u>	<u>258,874</u>
Net Operating Income	\$ 404,491	\$ 828,686
Average Cap Rate	<u>5.1%</u>	<u>5.1%</u>
Project Market Value	\$ 7,931,192	\$ 16,248,742
Development Costs (Excluding Profit)	<u>6,167,792</u>	<u>10,984,106</u>
Developer Profit	\$ 1,763,400	\$ 5,264,636
Return on Cost, No In-Lieu Fee	29%	48%
In-Lieu Fee per Sq. Ft.	\$ 10.78	\$ 10.78
Return on Cost with In-Lieu Fee	24%	43%
Return on Cost Feasibility Threshold	12% to 16%	

Sources: Tables 2.3, 2.5, and A.1; Colliers International Greater Los Angeles Multifamily Market Report, Fall 2007; MuniFinancial.

Table 2.17b: Return on Cost, Rental Developments - 2007

	Rental Townhome Project	Apartment Project
Operating Income-Market Rent	\$ 525,600	\$ 1,069,200
Operating Costs	<u>135,695</u>	<u>259,751</u>
Net Operating Income	\$ 389,905	\$ 809,449
Average Cap Rate	<u>5.5%</u>	<u>5.5%</u>
Project Market Value	\$ 7,089,185	\$ 14,717,253
Development Costs (Excluding Profit)	<u>6,601,692</u>	<u>11,055,282</u>
Developer Profit	\$ 487,493	\$ 3,661,971
Return on Cost, No In-Lieu Fee	7%	33%
In-Lieu Fee per Sq. Ft.	\$ 11.13	\$ 11.13
Return on Cost with In-Lieu Fee	3%	28%
Return on Cost Feasibility Threshold	12% to 16%	

Sources: Tables D.1, D.3, and D.14; Colliers International Greater Los Angeles Multifamily Market Report, Spring 2007; MuniFinancial.

OWNER-OCCUPIED DEVELOPMENT RETURN ON COST

Table 2.18a shows the effects of the proposed inclusionary zoning policy on return on cost for the owner-occupied development prototypes under current market conditions. The analysis finds that, under the current market downturn, only the stacked flats condo prototype is feasible. This prototype would remain feasible under the proposed inclusionary zoning policy. As the residential real estate market recovers from the current downturn, the return on cost for owner-occupied residential development projects is likely to improve.

Table 2.18a: Return on Cost, Owner-Occupied Developments - Current Market Conditions

	Owner-Occupied Townhome Project	Stacked Flats Condos	High-Rise Condos
Sales Revenues	\$ 8,190,000	\$ 18,250,000	\$ 41,400,000
Development Costs (Excluding Profit)	7,602,531	13,909,018	40,610,868
Developer Profit	\$ 587,469	\$ 4,340,982	\$ 789,132
Return on Cost, No In-Lieu Fee	8%	31%	2%
In-Lieu Fee per Sq. Ft.	\$ 10.10	\$ 10.10	\$ 10.10
Return on Cost with In-Lieu Fee	4%	27%	-1%
Return on Cost Feasibility Threshold	12% to 16%		

Sources: Tables 2.11 and A.3; MuniFinancial.

As shown in **Table 2.18b**, all three owner-occupied development prototypes were found to be feasible with no inclusionary zoning policy under mid-2007 market conditions. The estimated ten percent reduction in prices of owner-occupied units has a large impact on the sales revenues from owner-occupied development, compared with conditions in mid-2007. Since mid-2007, land values have declined, but construction costs and permits and impact fees have increased. Total development costs have increased for the stacked flats and high-rise prototypes, but have decreased for the townhome prototype.

With the proposed inclusionary zoning policy, the stacked flats prototype provided a return on cost well above the feasibility threshold in mid-2007. The townhome and high-rise condo prototypes were found to be just above the feasibility threshold with no inclusionary zoning requirement and at the low end of the feasibility threshold range with the proposed inclusionary zoning policy. In both time periods the proposed inclusionary zoning requirements reduce return on cost by three to five percentage points.

Table 2.18b: Return on Cost, Owner-Occupied Developments - 2007

	Owner-Occupied Townhome	Stacked Flats Condos	High-Rise Condos
Sales Revenues	\$ 9,160,000	\$ 20,280,000	\$ 45,800,000
Development Costs (Excluding Profit)	<u>7,812,509</u>	<u>13,505,326</u>	<u>38,887,593</u>
Developer Profit	\$ 1,347,491	\$ 6,774,674	\$ 6,912,407
Return on Cost, No In-Lieu Fee	17%	50%	18%
In-Lieu Fee per Sq. Ft.	\$ 10.51	\$ 10.51	\$ 10.51
Return on Cost with In-Lieu Fee	13%	45%	14%
Return on Cost Feasibility Threshold	12% to 16%		

Sources: Tables D.8 and D.16; MuniFinancial.

ECONOMIC FEASIBILITY FINDINGS

This analysis estimated the return on cost for five residential development prototypes under Long Beach market conditions at two points in the market cycle, with and without the proposed inclusionary zoning in-lieu fees. The estimated return on cost for each prototype development was compared to a feasibility threshold of 12 to 16 percent.

Over all of the prototypes and at both points in time, the in-lieu fee reduced return on cost by three to five percentage points. Without in-lieu fees, several of the prototypes are well above the threshold; others are already below feasibility threshold. For these projects, the proposed fees are not likely to have an impact on the decision to move forward with development. Under current market conditions, we found that all of the prototype rental developments are feasible. Of the owner-occupied development prototypes, only the stacked flats condo prototype is currently feasible. Under current market conditions, the proposed in-lieu fee does not make any of the currently feasible prototypes become infeasible.

Mid-2007 market conditions were more favorable to owner-occupied development and less favorable to rental development, compared with current market conditions. All three of the owner-occupied development prototypes were above the feasibility threshold. The rental apartment prototype was feasible, but the rental townhome project was not. The proposed in-lieu fee would have moved the owner-occupied townhome prototype and high-rise condo prototype developments from just above the feasibility threshold to even with the feasibility threshold.

The inclusionary zoning policy should include cost offsets and compliance alternatives to reduce the impacts of the policy on residential development. Chapter 5, Maintaining Development Feasibility, details recommended offsets and compliance alternatives. In addition, the City should phase the inclusionary zoning requirements in over time to allow the market to gradually adjust to the new requirements. This will allow the market to recover from its current downturn before the new requirements are fully in effect.

The return on cost analysis suggests that a policy of this magnitude, accompanied with cost offsets and flexibility in how developers can comply with the policy, will not have a major impact on the feasibility of private residential development in Long Beach. Finding that the proposed inclusionary zoning requirements maintain adequate incentives for private development at two different points in the market cycle and for a variety of different development prototypes increases confidence in the suitability of the recommendations.

3. COMMERCIAL LINKAGE FEE

This chapter calculates a conservative estimate of the maximum justified commercial linkage fee for Long Beach and recommends a commercial linkage fee for Long Beach below the maximum justified fee amount.

LINK BETWEEN JOBS AND HOUSING

The commercial linkage fee is based on the impact of job creation on the need for additional housing to serve the new employees. The fee is designed to help address that need for workforce and affordable housing. To establish a nexus for the fee, the City of Long Beach must first demonstrate that there is a reasonable relationship between non-residential construction and the need for housing affordable for very low-, low- and moderate-income groups. In essence, the local government charging the fee must make findings showing that: (1) there is a reasonable relationship between the use of fee revenue and types of development subject to the fee; (2) there is a reasonable relationship between the need for facilities to be funded by the fee and the types of development paying the fee; and (3) the amount of the fee is reasonably related to the cost of facilities attributable to the development on which the fee is imposed.

HOUSING AFFORDABILITY GAP GENERATED BY NON-RESIDENTIAL DEVELOPMENT

A series of steps is used to estimate the number of households generated at different income levels for a given amount of new non-residential development. Affordable housing needs are estimated based on the number very low-, low-, and moderate-income households generated by 100,000 square feet of new non-residential development. A maximum justified commercial linkage fee is calculated based on the estimated affordable housing needs generated by new development. The City may adopt a fee at any level below this maximum justified fee.

Separate linkage fees are estimated for four different non-residential land uses: office, hotel, retail, and industrial. Data used in the analysis are specific to Long Beach where available. Data are largely from the U.S. Census and the California Employment Development Department (EDD). For some Census statistics, data are available from the 2006 U.S. Census American Community Survey (ACS). For others, the most recent data available are from 2000 Census.

The commercial linkage fee calculation involves the following steps:

1. Estimate the total number of employees generated by 100,000 square feet of new non-residential development.
2. Of the total number of employees, estimate the number who will live in Long Beach.

3. Based on the average number of employees per household in Long Beach, estimate the total number of new households that will be generated in Long Beach.
4. Based on the average distribution of occupation types for a given type of development, the distribution of wages for each occupation, and the household size distribution, estimate the number of very low-income, lower income, and moderate-income households that will be generated, assuming one worker per household.
5. Adjust the estimated number of households generated in each income category to take into account households with more than one worker.
6. Based on the affordability gap for very low, lower, and moderate-income households, estimate the total subsidy that would be required to provide affordable housing for the new households generated. This subsidy is equal to the maximum justified linkage fee.

To avoid overestimating the maximum justified linkage fee, conservative assumptions of the need for affordable housing created by non-residential development are employed in a number of places in the analysis.

EMPLOYMENT DENSITY

Table 3.1 shows average employee density for different land uses. Employment density is based on a survey conducted in 2001 by the Natelson Group for the Southern California Association of Governments. Survey results for Los Angeles County are used in this analysis.

Table 3.1: Employee Density by Land Use

Land Use	Sq. Ft. per Employee
Office	422
Hotel	762
Retail	495
Industrial	892

Sources: The Natelson Company, Inc., *Employment Density Study Summary Report*, October 31, 2001, pp. 15-23, results for Los Angeles County; MuniFinancial.

PERCENT OF NEW EMPLOYEES LIVING IN LONG BEACH

Non-residential development in Long Beach will employ workers who live in Long Beach and workers who commute to Long Beach from outside of the City. The maximum justified commercial linkage fee only attempts to recoup the difference between affordable housing costs and the actual cost of providing affordable units for new households residing in Long Beach. Table 3.2 shows the percentage of Long Beach employees living in Long Beach, as

of 2000. Total employment in Long Beach is based on EDD data from 2000, while the number of employees working in Long Beach who reside in the city comes from the 2000 Census. Based on these figures, it is assumed that only 29% of the employees of new non-residential development in Long Beach will live in Long Beach.

Table 3.2: Estimated Employees Living in Long Beach

Total Jobs in Long Beach	212,000
Long Beach Employees Living in Long Beach	<u>61,685</u>
Percent	29%

Sources: U.S. Census 2000 Summary File 3, Table P27, Long Beach; California Employment Development Department, LaborMarketInfo Data Library, 2000; MuniFinancial.

EMPLOYEES PER HOUSEHOLD

Table 3.3 shows the average number of employees per household in Long Beach, as reported in the 2000 Census. A large number of retirees live in Long Beach; therefore, this figure excludes households with a household head age 65 and older and employees age 65 and older to generate an employees per household figure more representative of the new households likely to be generated by new non-residential development. Based on these figures, it is estimated that one new household will be generated for every 1.34 new employees.

Table 3.3: Employees per Household

Employees in Long Beach	184,979
Households in Long Beach	<u>138,168</u>
Employees per Household	1.34

Note: Excludes employees 65 and older and households with household head 65 and older.

Sources: U.S. Census Bureau, Census 2000 SF 1 and SF 3; MuniFinancial.

Based on the employment density, percentage of employees living in Long Beach, and average employees per household, Table 3.4 shows the estimated number of new households in Long Beach generated per 100,000 square feet of development in each of the four land use categories.

Table 3.4: Household Generation per 100,000 sq. ft. Nonresidential Development

	Light			
	Office	Manufacturing	Retail	Hotel
Development Size (sq. ft.)	100,000	100,000	100,000	100,000
Square Feet per Employee	<u>422</u>	<u>892</u>	<u>495</u>	<u>762</u>
Total Employment	237	112	202	131
% Living in Long Beach	<u>29%</u>	<u>29%</u>	<u>29%</u>	<u>29%</u>
Employees in Long Beach	69	33	59	38
Avg. Emp. per Household	<u>1.34</u>	<u>1.34</u>	<u>1.34</u>	<u>1.34</u>
New Households in L.B.	52	24	44	29

Sources: Tables 3.1, 3.2, and 3.3; MuniFinancial.

OCCUPATION DISTRIBUTION OF NEW HOUSEHOLDS

Table 3.5 shows the percentage of employees in each occupation category for each type of land use analyzed in this study. The occupation distribution by industry is based on the 1990 U.S. Census Occupation by Industry Survey. This survey has not been repeated in subsequent Censuses, leaving the 1990 survey as the most recent source for this information.

Table 3.5: Occupation Distribution by Industry

	Light			
	Office	Manufacturing	Retail	Hotel
Managerial/Administrative	21%	9%	15%	6%
Professional/Technical	16%	8%	5%	3%
Service	5%	0%	0%	70%
Sales and Related	8%	0%	52%	0%
Clerical/Administrative Support	45%	23%	10%	15%
Production/Operating/Maintenance	<u>5%</u>	<u>60%</u>	<u>18%</u>	<u>6%</u>
Total	100%	100%	100%	100%

Source: Occupation by Industry Survey, U.S. Census, 1990, as cited in *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; MuniFinancial.

Based on the number of new workers generated by 100,000 square feet of nonresidential development calculated in Table 3.4 and the occupation distribution shown in Table 3.5, **Table 3.6** shows the estimated number of workers in each occupation category.

Table 3.6: Occupation Distribution of Households (HH) Generated per 100,000 sq. ft. Nonresidential Development

	Office		Light Manufacturing		Retail		Hotel	
	% ¹	Number of HH	% ¹	Number of HH	% ¹	Number of HH	% ¹	Number of HH
Total Households ¹	100%	52.00	100%	24.00	100%	44.00	100%	29.00
<i>Occupation Distribution</i> ²								
Managerial/Administrative	21%	10.92	9%	2.16	15%	6.60	6%	1.74
Professional/Technical	16%	8.32	8%	1.92	5%	2.20	3%	0.87
Service	5%	2.60	0%	-	0%	-	70%	20.30
Sales and Related	8%	4.16	0%	-	52%	22.88	0%	-
Clerical/Administrative Support	45%	23.40	23%	5.52	10%	4.40	15%	4.35
Production/Operating/Maintenance	5%	2.60	60%	14.40	18%	7.92	6%	1.74

¹ See Table 3.4.² See Table 3.5.

Sources: Tables 3.4 and 3.5; MuniFinancial.

INCOME DISTRIBUTION OF NEW HOUSEHOLDS

The next tables show data used to estimate income level of new employees and the number of very low-, low-, and moderate-income households generated by new non-residential development in Long Beach.

Table 3.7 shows the 25th percentile, median, and 75th percentile hourly wages in the Los Angeles area for the six occupation categories used in this analysis. Wage data are provided by the EDD for the Los Angeles County from the first quarter of 2007. This is the most recent data currently available as of May 2008.

Table 3.7: Average Wages by Occupation (First Quarter 2007)

SOC Codes	Occupational Category	Mean	Mean	25th	Median	75th
		Hourly Wage	Annual Wage	Percentile Hourly Wage	Hourly Wage	Percentile Hourly Wage
11	Management	\$ 50.45	\$ 104,946	\$ 31.12	\$ 45.39	\$ 64.50
13-29, 33	Professional, Paraprofessional and Technical	30.19	62,807	18.50	26.36	37.85
31, 35-39	Service	11.04	22,967	8.25	9.55	12.28
41	Sales and Related	18.15	37,761	8.88	12.83	21.83
43	Office and Administrative Support	16.21	33,719	11.09	14.93	20.21
47-53	Production, Construction, Operating, Maintenance, and Material Handling	16.01	33,301	10.10	13.67	19.85

Sources: Occupational Employment Statistics Survey, California Employment Development Department, Los Angeles-Long Beach-Glendale MD, First Quarter 2007.

For a given income level, categorization as very low-, low-, or moderate- income depends on household size. The household size distribution of households with the household head under age 65 for Long Beach is shown in **Table 3.8** below. Household size data are from the 2006 American Community Survey.³

Table 3.8: Long Beach Estimated Household Size Distribution, Householder Under 65

Household Size	Households	
	No.	%
1 Person	37,911	27%
2 Persons	39,578	28%
3 Persons	22,918	16%
4 Persons	19,761	14%
5 Persons	9,660	7%
6 Persons	5,446	4%
7 or More	4,014	3%
Total	139,288	100%

Sources: U.S. Census Bureau, 2006 American Community Survey, Tables B11016 and B25116; MuniFinancial.

Table 3.9 shows the maximum income for very low-income, low-income, and moderate-income households for each size household. Very low, low-, and moderate-income thresholds are calculated based on a percentage of the area median income established by the California Department of Housing and Community Development. The thresholds used in this analysis are those used in determining affordability levels for affordable housing funded by the Long Beach Redevelopment Agency. Based on the annual income thresholds, an equivalent wage is calculated assuming 2080 hours worked per year (52 weeks * 40 hours/week = 2080 hours).

³ The American Community Survey only subdivides households with a household head over age 65 into one-person households or two-or-more person households. The total number of over-65, two-or-more person households is distributed into specific household size categories according to the overall household size distribution. This likely overestimates the number of large households headed with a household head over 65 years old, because older households are more likely to have fewer members. This is a conservative assumption for this analysis because it underestimates the percentage of large households with an under 65-year-old householder. Larger households are classified as very low-, low-, or moderate-income at a higher income level than smaller households.

Table 3.9: Income Limits by Household Size (2008\$)

Household Size		1	2	3	4	5	6	7	8
Area Median Income (2008)		\$ 41,900	\$ 47,800	\$ 53,800	\$ 59,800	\$ 64,600	\$ 69,400	\$ 74,200	\$ 78,900
Very Low-Income (50% AMI)	Annual	\$ 20,950	\$ 23,900	\$ 26,900	\$ 29,900	\$ 32,300	\$ 34,700	\$ 37,100	\$ 39,450
	Hourly	10.07	11.49	12.93	14.38	15.53	16.68	17.84	18.97
Low-Income (60% AMI)	Annual	\$ 25,140	\$ 28,680	\$ 32,280	\$ 35,880	\$ 38,760	\$ 41,640	\$ 44,520	\$ 47,340
	Hourly	12.09	13.79	15.52	17.25	18.63	20.02	21.40	22.76
Moderate-Income (110% AMI)	Annual	46,090	52,580	59,180	65,780	71,060	76,340	81,620	86,790
	Hourly	22.16	25.28	28.45	31.63	34.16	36.70	39.24	41.73

Sources: California Department of Housing and Community Development; MuniFinancial.

Based on the income distributions shown in Table 3.7 above, the percent of employees whose salary is below each income cutoff is estimated. This is cross-tabulated with the household size information shown in Table 3.8 to estimate the percentage of very low-income, low-income, and moderate-income households in each occupation category, assuming only one worker per household. **Table 3.10** shows the estimated percentage of workers in each income category for each occupation type.

Table 3.10: Income Level by Occupation

Percent of Workers	Very Low Income	Lower Income	Moderate Income	> Moderate Income
Management	0%	0%	14%	86%
Professional, Paraprofessional and Technical	3%	7%	41%	49%
Service	76%	16%	8%	0%
Sales and Related	44%	10%	33%	12%
Office and Administrative Support	33%	15%	46%	6%
Production, Construction, Operating, Maintenance, and Material Handling	40%	13%	41%	6%

Sources: Tables 3.7, 3.8, and 3.9; MuniFinancial.

Table 3.11 shows the percentage of households in Long Beach with two or more workers, based on the 2006 American Community Survey (ACS). According to the ACS, 43 percent of households in Long Beach have two or more workers. This analysis removes 43 percent of households from the numbers of very low-, low-, and moderate-income households generated to account for multiple earners. Removing all multiple income households is a conservative assumption because, for example, a five-person household with two workers

working full time earning minimum wage (\$8.00 per hour) would still be a low-income household. Similarly, a four-person household with two workers earning \$15 per hour would still be a moderate-income household. However, data on the actual income distribution of multiple earner households is not available.

Table 3.11: Multiple Earner Household Adjustment

Households with Two or More Workers	52,410
Total Worker Households	<u>122,900</u>
Percent	43%

Source: U.S. Census Bureau, 2006 American Community Survey Table B8202.

Table 3.12 shows the estimated number of very low-, low-, and moderate-income households generated per 100,000 square feet of office, light manufacturing, retail, and hotel development. For each land use, the number of households generated in each occupation category, shown in Table 3.6, is distributed into income categories according to the income distribution shown in Table 3.10. Then the number of very low-, low-, and moderate-income households is totaled. Finally, multiple earner households are removed from the totals.

Table 3.12: Income Distribution of New Households (HH)

	Number of HH ¹	Very Low Inc.		Low Income		Moderate Inc.		Above Mod. Inc.	
		% ²	Number of HH	% ²	Number of HH	% ²	Number of HH	% ²	Number of HH
Office									
Managerial/Administrative	10.92	0%	-	0%	-	14%	1.57	86%	9.35
Professional/Technical	8.32	3%	0.27	7%	0.58	41%	3.42	49%	4.05
Service	2.60	76%	1.96	16%	0.43	8%	0.21	0%	-
Sales and Related	4.16	44%	1.85	10%	0.42	33%	1.38	12%	0.51
Clerical/Administrative Support	23.40	33%	7.80	15%	3.55	46%	10.67	6%	1.38
Production/Operating/Maintenance	2.60	40%	1.04	13%	0.35	41%	1.06	6%	0.15
Total Households	52.00		12.92		5.33		18.31		15.43
Multiple Earner Households ³		43%	5.51	43%	2.27	43%	7.81	43%	6.58
Adjusted Total			7.41		3.06		10.50		8.85
Light Manufacturing									
Managerial/Administrative	2.16	0%	-	0%	-	14%	0.31	86%	1.85
Professional/Technical	1.92	3%	0.06	7%	0.13	41%	0.79	49%	0.93
Service	-	76%	-	16%	-	8%	-	0%	-
Sales and Related	-	44%	-	10%	-	33%	-	12%	-
Clerical/Administrative Support	5.52	33%	1.84	15%	0.84	46%	2.52	6%	0.33
Production/Operating/Maintenance	14.40	40%	5.77	13%	1.94	41%	5.86	6%	0.82
Total Households	24.00		7.68		2.92		9.48		3.93
Multiple Earner Households ³		43%	3.27	43%	1.24	43%	4.04	43%	1.68
Adjusted Total			4.40		1.67		5.44		2.25
Retail									
Managerial/Administrative	6.60	0%	-	0%	-	14%	0.95	86%	5.65
Professional/Technical	2.20	3%	0.07	7%	0.15	41%	0.90	49%	1.07
Service	-	76%	-	16%	-	8%	-	0%	-
Sales and Related	22.88	44%	10.15	10%	2.32	33%	7.60	12%	2.81
Clerical/Administrative Support	4.40	33%	1.47	15%	0.67	46%	2.01	6%	0.26
Production/Operating/Maintenance	7.92	40%	3.18	13%	1.07	41%	3.22	6%	0.45
Total Households	44.00		14.87		4.21		14.68		10.24
Multiple Earner Households ³		43%	6.34	43%	1.80	43%	6.26	43%	4.37
Adjusted Total			8.53		2.41		8.42		5.87
Hotel									
Managerial/Administrative	1.74	0%	-	0%	-	14%	0.25	86%	1.49
Professional/Technical	0.87	3%	0.03	7%	0.06	41%	0.36	49%	0.42
Service	20.30	76%	15.33	16%	3.35	8%	1.62	0%	-
Sales and Related	-	44%	-	10%	-	33%	-	12%	-
Clerical/Administrative Support	4.35	33%	1.45	15%	0.66	46%	1.98	6%	0.26
Production/Operating/Maintenance	1.74	40%	0.70	13%	0.23	41%	0.71	6%	0.10
Total Households	29.00		17.51		4.30		4.92		2.27
Multiple Earner Households ³		43%	7.47	43%	1.84	43%	2.10	43%	0.97
Adjusted Total			10.04		2.47		2.82		1.30

¹ See Table 3.6.

² See Table 3.10.

³ See Table 3.11.

Sources: Tables 3.6, 3.10, and 3.11, MuniFinancial.

AFFORDABILITY GAP GENERATED BY NON-RESIDENTIAL DEVELOPMENT

The linkage fee is based on the number of new households generated by non-residential development and the affordability gap per household. The affordability gap for several prototype developments was calculated in the previous chapter. The commercial linkage fee is based on the affordability gap estimated for low- and very low-income households living in the rental apartment prototype, and for moderate-income households purchasing stacked flat condos. These are the least expensive renter and owner prototype developments modeled. These affordability gap calculations are for households with the maximum income for their income category. This is a conservative assumption because, for many households, the actual affordability gap would be larger than the estimate shown in the table. **Table 3.13** shows the affordability gap associated with 100,000 square feet of non-residential development, and the resulting maximum justified linkage fee.

Table 3.13: Affordability Gap per 100,000 Square Feet Development (2008\$)

	Light			
	Office	Manufacturing	Retail	Hotel
Very Low Income Households	7.41	4.40	8.53	10.04
Affordability Gap per Household	\$ 227,846	\$ 227,846	\$ 227,846	\$ 227,846
Total Affordability Gap - V.L.I. Households	\$ 1,688,950	\$ 1,003,280	\$ 1,942,815	\$ 2,288,056
Lower Income Households	3.06	1.67	2.41	2.47
Affordability Gap per Household	\$ 212,053	\$ 212,053	\$ 212,053	\$ 212,053
Total Affordability Gap - L.I. Households	\$ 648,840	\$ 354,620	\$ 511,945	\$ 523,541
Moderate Income Households	10.50	5.44	8.42	2.82
Affordability Gap per Household	\$ 112,919	\$ 112,919	\$ 112,919	\$ 112,919
Total Affordability Gap - M.I. Households	\$ 1,174,480	\$ 608,526	\$ 942,085	\$ 319,167
Total Affordability Gap	\$ 3,476,207	\$ 1,946,121	\$ 3,362,793	\$ 3,093,778
Affordability Gap per Square Foot	\$ 34.76	\$ 19.46	\$ 33.63	\$ 30.94

Sources: Tables 2.8, 2.14, 3.12; MuniFinancial.

LINKAGE FEE IMPACT ANALYSIS

While Table 3.13 above shows the maximum justified linkage fee amount, the City is free to set the actual fee at any level up to the maximum justified level. The City must balance the policy goal of generating revenue to provide affordable housing with the policy goal of setting the fee at a level where it will not have a significant effect of discouraging new non-residential development. This section presents a proposed linkage fee schedule based on considerations of total development fee burden, impacts on residual land value, and the fees charged in other cities in California.

One way the impacts of the commercial linkage fee can be assessed is with a residual land value analysis. Residual land value analysis calculates the value of a development based on its net operating income and the current capitalization rate, and subtracts the development costs to estimate the underlying value of the land. A land residual analysis is commonly used

by real estate developers to evaluate the financial feasibility of a site and to select among alternative uses. This analysis identifies the change in residual land value with no impact fee and the reduction in residual land value resulting from possible linkage fee levels. Details of the residual land value calculations are shown in **Appendix B**.

Table 3.14 shows the residual land value for the prototype developments at various potential linkage fee levels. The residual land value is the difference between a development's market value and its development costs, excluding land. This difference is attributed to the value of the land. A proposed development is feasible if the actual land cost is less than the residual land value.

Table 3.14: Land Residual Value Analysis (2008\$)

	Class A Office	Community Retail	Hotel	Light Manufacturing
Gross SF Bldg Area	100,000	100,000	100,000	100,000
Floor Area Ratio	1.70	0.25	1.70	0.25
Net SF Site Area	58,824	400,000	58,824	400,000
Capitalized Value	\$ 42,959,136	\$ 35,535,938	\$ 36,133,662	\$ 11,895,246
Total Development Costs (Except Land)	\$ 28,136,508	\$ 18,028,883	\$ 24,575,348	\$ 14,095,186
Residual Land Value	\$ 14,822,628	\$ 17,507,054	\$ 11,558,313	\$ (2,199,940)
Residual Land Value per SF Site Area	251.98	43.77	196.49	(5.50)
<u>\$2.00/SF Linkage Fee</u>				
Total Linkage Fee	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000
Residual Land Value	14,622,628	17,307,054	11,358,313	(2,399,940)
Residual Land Value per SF Site Area	248.58	43.27	193.09	(6.00)
Pct. Reduction in Residual Land Value	1.3%	1.1%	1.7%	9.1%
<u>\$4.00/SF Linkage Fee</u>				
Total Linkage Fee	\$ 400,000	\$ 400,000	\$ 400,000	\$ 400,000
Residual Land Value	14,422,628	17,107,054	11,158,313	(2,599,940)
Residual Land Value per SF Site Area	245.18	42.77	189.69	(6.50)
Pct. Reduction in Residual Land Value	2.7%	2.3%	3.5%	18.2%

Sources: Tables B.2 and B.3; *Greater Los Angeles Basin Commercial Real Estate Market Outlook*, 2007, Colliers International; MuniFinancial.

As shown, the estimated residual land value for hotel and class A office space is over \$250 per square foot. Community retail development is estimated to have a residual land value of approximately \$44 per square foot with no linkage fee. Light manufacturing has a negative residual land value, suggesting that, even with no housing linkage fee, light manufacturing development is not financially feasible in Long Beach under current market conditions. The residual land value analysis conducted under mid-2007 market conditions found similar results to those shown here. Market reports suggest that nonresidential rents and development costs in Long Beach both increased modestly from mid-2007 to the current time.

The higher residual land value of class A office and hotel development is consistent with the locations where these land uses tend to be developed. Class A office space tends to be concentrated in high land value, downtown locations. Hotels are developed in a variety of areas, but are concentrated downtown. The higher residual land value of office and hotel uses suggests that these types of development can support a higher linkage fee than community retail while remaining feasible.

Table 3.15 shows the fee burden as a percentage of development value for fee levels of \$2.00 per square foot and \$4.00 per square foot. For the office, retail, and hotel developments modeled, a \$2.00 per square foot linkage fee would represent approximately 0.5 percent of market value, and the total fee burden is estimated at just over two percent of market value. The linkage fee would be a significantly higher portion of market value for the light manufacturing development, due to the lower estimated market value of this land use. A \$4.00 per square foot linkage fee is estimated to be approximately one percent of market value for office, retail, and hotel developments, and the total fee burden would be just under three percent.

Table 3.15: Total Fee Burden (2008\$)

	Class A Office	Community Retail	Hotel	Light Manufacturing
Development Value	\$ 42,959,136	\$ 35,535,938	\$ 36,133,662	\$ 11,895,246
<i><u>\$2.00/SF Linkage Fee</u></i>				
Total Linkage Fee	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000
Linkage Fee Percentage of Dev. Value	0.47%	0.56%	0.55%	1.68%
Other Development Fees	<u>1.80%</u>	<u>1.80%</u>	<u>1.80%</u>	<u>1.80%</u>
Total Fee Burden	2.27%	2.36%	2.35%	3.48%
<i><u>\$4.00/SF Linkage Fee</u></i>				
Total Linkage Fee	\$ 400,000	\$ 400,000	\$ 400,000	\$ 400,000
Linkage Fee Percentage of Dev. Value	0.93%	1.13%	1.11%	3.36%
Other Development Fees	<u>1.80%</u>	<u>1.80%</u>	<u>1.80%</u>	<u>1.80%</u>
Total Fee Burden	2.73%	2.93%	2.91%	5.16%

Sources: Tables B.1 and B.5; MuniFinancial.

PROPOSED LINKAGE FEE

The recommended linkage fee schedule is shown in **Table 3.16**. The recommended linkage fee is \$4.00 per square foot for office and hotel development and \$2.00 per square foot for retail. The schedule does not include a fee for light manufacturing land uses. These proposed fees are within the range of linkage fees charged in other cities in California, which charge fees between approximately \$1 and \$15 per square foot. These fees are not likely to have a large impact on the feasibility of commercial and industrial development in Long Beach. A higher fee is proposed for office and hotel development than for retail development based on the higher residual land value estimated for these land uses. Based on the assumptions

applied in the residual land value analysis, light manufacturing development is likely to be infeasible in Long Beach. No fee is proposed for light manufacturing developments to avoid negatively impacting projects that may be just marginally feasible.

It is recommended that the City update the fees annually to account for changes in the cost of providing affordable housing units. This update could be based on the annual change in the *Engineering News-Record* Building Cost Index for Los Angeles.

Table 3.16: Recommended Linkage Fee Schedule

	Office	Retail	Hotel	Industrial
Proposed Linkage Fee per Sq. Ft.	\$ 4.00	\$ 2.00	\$ 4.00	\$ -

Source: MuniFinancial.

The proposed in-lieu fees meet the general requirements for fees charged to new development:

- ◆ *There is a reasonable relationship between the fee’s use and the type of development project on which the fee is imposed.* The commercial linkage fees will be charged to office, retail, and hotel development to help meet the affordable housing needs generated by that development. The fee revenue will be used to fund affordable housing through the Long Beach Housing Trust Fund.
- ◆ *There is a reasonable relationship between the need for the facility or program to be funded by the fee and the type of development on which the fee is imposed.* Office, retail, and office development creates a need for affordable housing by employing lower- and moderate-income workers who cannot afford market-rate housing in Long Beach. Commercial linkage fees will be charged to these types of development to meet a portion of the affordable housing needs associated with that development.
- ◆ *There is a reasonable relationship between the amount of the fee and the cost of the public facility or program attributable to the development on which the fee is imposed.* The commercial linkage fee analysis estimates the average affordable housing need generated per square foot for four types of non-residential development. The proposed linkage fees are less than the affordable housing needs associated with each square foot of development.

The fee amount for a specific project is based on the project’s size. On average, larger new development projects employ more workers and generate more new households needing affordable housing. Since linkage fees are charged per square foot, larger projects will generate more fee revenue than smaller projects in the same land use classification. Thus, the fees ensure a reasonable relationship between a specific new development project and the cost of the affordable housing needs attributable to that project.

4. CONDOMINIUM CONVERSION FEE

This chapter analyzes condominium (condo) conversions in Long Beach and assesses the feasibility of applying the proposed inclusionary zoning requirement for owner-occupied developments to condo conversions.

LOSS OF AFFORDABILITY

As detailed in the *Nexus for Condominium Conversion Fee Ordinance*, conducted for Long Beach by Karen Warner in 2006, on average, rental units are affordable to households at a lower income level than condominium units. Thus, there is usually a loss of housing affordability when a unit is converted from an apartment to a condo. A condo conversion fee would shift some of the profit realized from a condo conversion from developers to the Housing Trust Fund, which would use it to fund affordable housing development. This would mitigate some of the loss of affordability resulting from the conversion.

Of the 172,000 housing units in Long Beach as of 2000, about 100,000, or 58 percent, were rental units. Since that time, the City of Long Beach has experienced a trend in condominium conversions that results in the removal of units from the rental market. Table 4.1 shows the number of conversion projects reviewed by the Planning Commission and the number of units to be converted from 2000 through mid-July 2007.

Table 4.1 Condominium Conversions in Long Beach, 2000-2007

Year	Projects Reviewed by Planning Commission	Units Impacted
2000	2	22
2001	5	60
2002	2	4
2003	4	18
2004	13	426
2005	30	262
2006	78	1,073
2007 ¹	18	350
Totals	152	2,215

¹ Projects and units for 2007 are through July 19, 2007.

Source: Long Beach Development Services Department.

The number of future conversions is difficult to predict. It will depend on real estate market factors including rental rates, condominium prices, and renovation costs. Builders involved

in condominium conversions interviewed for this analysis stated that conversions are likely to decline in the future due to a lack of available units to convert. City staff also report that it is increasingly difficult to find buildings suitable for conversion. The economic incentives for this type of real estate development are limited to the extent that some of the apartment building stock remaining is of substandard quality.

A decline in the number of conversions should not impact the policy decision regarding a condo conversion fee. Due to the cyclical nature of the real estate market, the trend in condominium conversions may decline and then pick up again in the future. A condo conversion fee ensures that projects provide mitigation for the loss in the City's affordable housing stock as units are converted regardless of market cycles.

CONDO CONVERSION PROTOTYPE PROJECT

The loss of affordability associated with a given condo conversion depends on the actual rent charged for the units as apartments and the sale prices of the converted units. The impacts of applying the proposed inclusionary zoning requirements to condo conversions are estimated for a prototype condo conversion project.

Details of the prototype condo conversion are shown in **Table 4.2**. The converted building prototype is based on the rental apartment prototype used in the in-lieu fee calculation. This fifty-unit prototype is in the size range of buildings that have been converted in Long Beach, although many conversions have been smaller buildings. The estimated market value of the converted units is based on 2006 and 2007 condo sales in Long Beach in the DataQuick Information Systems database and recent trends in the Long Beach condo market. The estimated market value of converted units is equivalent to the estimated market-rate value of new stacked flat condo units used elsewhere in this report. As shown, the estimated market value of the conversion project as condominiums is \$18.25 million.

Table 4.2: Condo Conversion Prototype (2008\$)

	Number of Units	Sq. Ft. per Unit	Total	Price per Unit (as Condo)	Market-Rate Sales Income
1 Bedroom	7	800	5,600	\$ 310,000	\$ 2,170,000
2 Bedroom/1 Bath	8	950	7,600	360,000	2,880,000
2 Bedroom/2 Bath	25	1,000	25,000	360,000	9,000,000
3 Bedroom	10	1,100	11,000	420,000	4,200,000
Total	50		49,200		\$ 18,250,000
Efficiency			90%		
Gross Square Feet			54,667		

Sources: Tables 2.2 and A.3; DataQuick Information Systems; MuniFinancial.

Table 4.3 shows estimated costs for the prototype condo conversion project. The estimated cost of the apartment building to the condo conversion developer is based on an average cost per unit of \$145,000. This is the average cost per unit for apartment buildings sold in

the Long Beach area in 2007, as reported by Colliers International. An estimate of condo conversion expenses is primarily based on the proforma for a recent apartment rehab project in Long Beach provided by the Housing Services Bureau. The cost of renovating and upgrading the building and units is estimated at \$70,000 per unit. Indirect costs, including architecture, engineering, taxes, and insurance, are estimated to be ten percent of the renovation costs. Permits, fees, and legal costs are estimated at \$10,000 per unit. (This is less than the estimated permit, fees and legal costs used for new construction in Chapter 2 because many of these costs, including building permits and impact fees are lower for building renovations than for new construction.) The estimate of financing costs assumes that the developer will finance 75 percent of the building value and conversion expenses. Sales costs and commissions are estimated at five percent of the project's sale value as condos. Due to the economies of scale that can be achieved with a large project, some of these costs would be higher per unit if a smaller building were being considered.

Table 4.3: Condo Conversion Costs (2008\$)

<u>Apartment Building Market Value</u>		\$ 6,900,000
<u>Condo Conversion Expenses</u>		
Renovation	\$ 70,000 per unit	\$ 3,500,000
Permits, Fees, and Legal	\$ 10,000 per unit	500,000
Other Indirect Costs ¹	10% of renovation costs	<u>350,000</u>
Subtotal - Building, Renovation, and Indirect Costs		\$ 4,350,000
<u>Financing</u>		
Percent of Building, Renovation, and Indirect Costs Financed	75% \$	8,437,500
Average Loan Balance	60%	5,062,500
Interest Rate ²	7%	354,375
<u>Sales Costs</u>	5% of condo value	<u>912,500</u>
Subtotal - Development Costs		\$ 12,516,875
<u>Developer Overhead</u>	4% Development Costs	<u>500,675</u>
Total Conversion Cost (Excluding Profit)		\$ 13,017,550

¹ Includes architecture, engineering, taxes and insurance.

² Assumes that loan period is twelve months, with an average loan balance over that period of 60 percent.

Sources: Table 4.2; Greater Los Angeles Multifamily Market Report, Colliers International, Fall 2007; Keyser Marston Associates, Inc.; MuniFinancial.

INCLUSIONARY ZONING POLICY APPLIED TO CONDO CONVERSIONS

The City must balance two policy goals in setting a condo conversion fee: mitigating the loss of affordability resulting from the conversion of rental units, and setting the fee at a level where it will not have a significant effect of discouraging new investment in residential neighborhoods. Condominium conversions involve economic investment in residential neighborhoods. They do not, however, create a net addition of housing units. The City can charge a condo conversion fee without constraining economic incentives to build new units. However, the City should avoid setting the fee at a level that would significantly discourage investments to upgrade existing units.

This study recommends applying the proposed inclusionary zoning requirements for new owner-occupied development to condominium conversions. This would apply a consistent policy across all types of owner-occupied development. While different types of development may be able to support different inclusionary zoning requirements, there is too much variation between individual development projects to tailor requirements and fees to every product type. Applying the inclusionary zoning policy to condo conversions would allow the City to achieve the same policy goals with condo conversions as with new development. Additional housing units would be available for moderate-income households and, if affordable units are provided on-site rather than through the payment of an in-lieu fee, there will be integration of affordable units with market rate units in the housing stock.

Chapter 2 recommends an inclusionary zoning requirement that ten percent of new owner-occupied units must be affordable to moderate-income households. As an alternative, developers may choose to pay an in-lieu fee of \$10.10 per square foot, which would allow the City to fund development of an equivalent number of affordable units. **Table 4.4** shows the estimated return on cost for the prototype condo conversion project under the inclusionary zoning policy, assuming the developer chooses to comply with the policy by paying the in-lieu fee. As shown, the proposed inclusionary zoning requirement would reduce return on cost for the prototype condo conversion project by approximately four percentage points. The prototype project would provide a return on cost above the feasibility threshold of 12 to 16 percent with the proposed inclusionary zoning requirements. (See Appendix A for more information on return on cost analysis.)

It is recommended that the City update the in-lieu fee annually to account for changes in the cost of providing affordable housing units. This update could be based on the annual change in the *Engineering News-Record* Building Cost Index for Los Angeles.

Table 4.4: Condo Conversion Fee Return on Cost (2008\$)

Sales Revenues		\$	18,250,000	
Development Costs (Excluding Profit)			<u>13,017,550</u>	
Developer Profit		\$	5,232,450	
				<u>Percent of Costs</u>
Return on Cost (Before Affordable Housing Fees)				40%
Project Gross Square Footage			54,667	
Owner-Occupied In-Lieu Fee per Sq. Ft.	\$		<u>10.10</u>	
In-Lieu Fee	\$		552,136	4%
Return on Cost (After Conversion Fee)				36%

Sources: Tables 4.2, 4.3, and 2.16; MuniFinancial.

The analysis conducted based on mid-2007 market data showed similar impacts from the proposed inclusionary zoning policy. With higher market prices for the converted units, return on cost was estimated to be higher both before and after the inclusionary zoning requirement was applied. As in the current analysis, the proposed in-lieu fee was found to be approximately four percent of development costs.

The proposed condominium conversion fees meet the general requirements for fees charged to new development:

- ◆ *There is a reasonable relationship between the fee's use and the type of development project on which the fee is imposed.* Condominium conversion fee revenues will be used to fund achievement of the proposed inclusionary zoning policy goals of including affordable housing with condominium conversions and offsetting the affordability loss usually associated with conversions of rental units. The fee will be used to fund affordable housing through the Long Beach Housing Trust Fund.
- ◆ *There is a reasonable relationship between the need for the facility or program to be funded by the fee and the type of development on which the fee is imposed.* As documented in the introduction to this report (Chapter 1), there is a need for increased affordable housing in Long Beach. In addition, conversions of rental units usually result in a decrease in housing affordability. If the City adopts an inclusionary zoning ordinance, City policy will require new residential development and condominium conversions to make a percentage of units affordable to low- and moderate-income households. Providing the option of paying a condominium conversion fee gives converters of rental units a way of meeting the need for affordable housing units established by City policy.
- ◆ *There is a reasonable relationship between the amount of the fee and the cost of the public facility or program attributable to the development on which the fee is imposed.* The in-lieu fee analysis (Chapter 2) documents a reasonable relationship between the cost of providing the affordable units required by the inclusionary zoning policy and the proposed per square foot in-lieu fee. Charging the in-lieu fee to condominium conversion projects

based on square footage ensures that there is a reasonable relationship between the total fee charged and affordable housing needs associated with each particular development project.

5. MAINTAINING DEVELOPMENT FEASIBILITY

This section provides additional recommendations for the inclusionary zoning policy and in-lieu fee, commercial linkage fee, and condominium conversion fee based on the findings of this study. These recommended measures would reduce the new policies' impacts on the feasibility of private development in Long Beach. We recommend that the City include cost offsets in the inclusionary zoning policy. The City should also offer a variety of means for development projects to comply with the inclusionary zoning policy. The City should phase in new affordable housing policies and fees to allow the market to gradually adjust to the new requirements.

These measures will also help to ensure that Long Beach is an attractive place for residential development when compared with surrounding cities. As shown in Appendix C, the proposed in-lieu fee would make Long Beach's total development fee burden higher than the burden in any of the comparable cities included in the analysis. While the recommendations in this chapter will not directly reduce the fee burden, they will help to offset the impacts of the fees on development feasibility in Long Beach.

COST OFFSETS

Inclusionary zoning policies often include developer cost offsets to mitigate the loss of profits that developers may incur from selling affordable units and reduce the possible impacts of the policy on the supply and price of market-rate housing. A study of inclusionary zoning policies in the Boston, San Francisco, and Washington D.C. areas conducted by the Furman Center for Real Estate & Urban Policy at New York University suggests that "policies that provide meaningful and achievable density bonuses or other benefits to offset the profits lost on affordable units should be less likely to impact adversely the price and supply of market-rate housing."⁴ Potential developer incentives include:

- ◆ **Density and/or height bonus:** Allow an increased number of dwelling units to be built on a given parcel than would be otherwise permitted. This can increase the profitability of a development project by allowing more market rate units to be developed on a given land parcel. To encourage developers to build affordable units on-site, the density bonus could be limited to developments that comply with the inclusionary zoning policy by providing affordable units on-site, rather than by paying an in-lieu fee.

As required by state law, Long Beach already has a density bonus in place for projects that choose to provide a minimum percentage of affordable units. A density bonus incorporated with the inclusionary zoning policy would dovetail with the existing density bonus. The inclusionary zoning policy would make it mandatory for new residential development projects to provide affordable units, and the density bonus would continue to provide an option to offset the reduced profitability associated with providing affordable units.

⁴ "The Effects of Inclusionary Zoning on Local Housing Markets: Lessons from the San Francisco, Washington DC and Suburban Boston Areas," Furman Center for Real Estate & Urban Policy, March 2008.

In some jurisdictions that nominally provide density bonuses, the bonuses are not effective in practice because of height restrictions or because of planning department or community opposition to higher densities.⁵ The City of Long Beach should ensure that developer incentives are achievable in practice to provide the desired cost offsets.

- ◆ **Expedited permitting:** The City can provide expedited permit processing to shorten the time required to complete a development project, potentially reducing carrying and financing costs. Providing expedited permitting would have cost impacts for the Development Services Department. The Development Services Department is currently calculating a fee to cover the cost of expedited permitting. That effort will provide the City with an estimate of the cost impacts of an expedited permitting cost offset for affordable housing.
- ◆ **Fee deferral:** The City could defer fees for residential development projects until issuance of the Certificate of Occupancy. This could reduce costs early in the development project, reducing financing costs. A fee deferral would have cost impacts on the Development Services Department.
- ◆ **Reduced parking requirements:** Reducing the parking requirements for projects providing affordable units would reduce the amount of land needed per unit, lowering development costs.

COMPLIANCE ALTERNATIVES AND EXEMPTIONS

The inclusionary zoning policy is based on a requirement for residential developers to make a given percentage of new units affordable at target income levels. In a joint policy statement, the Home Builders Associations of Northern California and the Non-Profit Housing Association of Northern California advocate flexibility in inclusionary zoning programs to maximize their effectiveness and efficiency.⁶ Offering a variety of ways to comply with the policy allows developers to select the alternative that is the least costly or otherwise most feasible for each specific development project, while still generating affordable housing.

Offering the following options for meeting the policy's requirements could enhance the efficiency of the inclusionary zoning policy and reduce its impacts on the feasibility of private development:

- ◆ Provide units on-site with market rate units;
- ◆ Pay an in-lieu fee;
- ◆ Provide the required affordable units at another site;
- ◆ Provide financial assistance in an amount equal to or greater than the in-lieu fee to a non-profit affordable housing project;

⁵ *Ibid.*

⁶ "On Common Ground: Joint Principles on Inclusionary Housing Policies," Home Builders Association of Northern California and Non-Profit Housing Association of Northern California, July 2005.

- ◆ Donate environmentally clean land, developable for housing, with land appraised at a value equal to or greater than the in-lieu fee.
- ◆ Provide a bonus toward meeting the required number of affordable units if inclusionary units are fully handicapped accessible or visitable. City staff has proposed counting fully accessible units as 1.5 units and visitable units as 1.25 units toward the required amount.

City staff has indicated that developers of single family homes and duplexes will be exempt from the inclusionary zoning requirements and in-lieu fee.

REQUIREMENT PHASE-IN

We recommend phasing the proposed inclusionary zoning requirements and affordable housing fees in over three years. To the extent that the new affordable housing requirements decrease the profitability of new development, land costs for new development may adjust as developers negotiate land prices necessary to maintain development feasibility. Phasing in the new requirements will allow markets to adjust gradually to accommodate the new requirements. Phasing in inclusionary zoning requirements and affordable housing fees fee levels will also reduce economic impacts on projects that are already committed to certain land and other development costs.

Phasing in the program will also give the development market time to recover from its current downturn before the full cost of the new affordable housing requirements is imposed, preventing the policy from deterring new development as the downturn continues and the market recovers. Based on the length of previous development downturns, the Long Beach development market should substantially recover within three years. **Table 5.1** shows a potential three-year phase in schedule for the proposed affordable housing fees.

Table 5.1: Phase-In Schedule for Proposed Affordable Housing Fees (2008\$)

	FY 2008-09	FY 2009-10	FY 2010-11
<u>Inclusionary Zoning</u>			
<u>Rental Units</u>			
Affordable Units	1%	3%	5%
In-Lieu Fee (per square foot)	\$ 2.16	\$ 6.47	\$ 10.78
<u>Owner-Occupied Units and Condo Conversions</u>			
Affordable Units	3%	6%	10%
In-Lieu Fee (per square foot)	\$ 3.03	\$ 6.06	\$ 10.10
<u>Commercial Linkage Fee (per square foot)</u>			
Office	\$ 1.33	\$ 2.67	\$ 4.00
Retail	0.67	1.33	2.00
Hotel	1.33	2.67	4.00
Industrial	-	-	-

Note: Fee amounts should be updated annually for changes in housing development costs. Fee amounts shown here are in 2008 dollars and do not include an inflation adjustment.

Sources: Tables 2.1, 2.16, and 3.16; MuniFinancial.

6. FEE REVENUE ESTIMATES

This section provides estimated annual fee revenues for the proposed inclusionary zoning in-lieu fee, the condo conversion fee, and the commercial linkage fee based on historic development trends in Long Beach.

IN-LIEU FEE REVENUE FROM RESIDENTIAL DEVELOPMENT

This analysis estimates annual in-lieu fee revenue based on the fee levels presented in this report and average residential development in Long Beach over the past five years. Data on the number of residential units developed in Long Beach over the past five years was provided by the Development Services Department. Only developments with three or more units were included in the historical development data because the City plans to exclude single family units and duplexes from inclusionary housing requirements.

The breakdown of recent residential development between rental units and owner occupied units was not available; however, market reports state that most market rate residential development in Long Beach has been owner-occupied development over the past several years. This revenue estimate is based on an assumption that 90 percent of new residential development is owner-occupied. The proposed in-lieu amount is similar for rental and owner-occupied development, so a different mix of rental and owner-occupied development would not have a large impact on in-lieu fee revenue.

Table 6.1 shows the average number of residential units developed on an annual basis and estimated fee revenue at the proposed fee levels.

Table 6.1: Estimated Annual In-Lieu Fee Revenue (2008\$)

Average Residential Units per Year (FY 2003-04 through 2007-08) ¹	A	266	
Estimated Average Square Feet per Owner-Occupied Unit	B	1,100	
In-Lieu Fee per Square Foot (Owner-Occupied)	C	\$ 10.10	
In-Lieu Fee Revenue per Unit	$D = B * C$	\$ 11,110	
Owner-Occupied Units per Year (90% of total)	$E = 90\% * A$	239	
Owner-Occupied In-Lieu Fee Revenue per Year	$F = D * E$		\$ 2,660,000
Estimated Average Square Feet per Rental Unit	G	1,000	
In-Lieu Fee per Square Foot (Rental)	H	\$ 10.78	
In-Lieu Fee Revenue per Unit	$I = G * H$	\$ 10,775	
Rental Units per Year (10%)	$J = 10\% * A$	27	
Rental In-Lieu Fee Revenue per Year	$K = I * J$		\$ 287,000
Total Annual In-Lieu Fee Revenue	$L = K + F$		\$ 2,947,000

¹ Includes only units in buildings of three or more units. Includes FY 2007-2008 development through March 31, 2008.

Sources: City of Long Beach Development Services Department; MuniFinancial.

This revenue estimate is based on the proposed in-lieu fee and an estimated average of 1,100 square feet per owner-occupied unit and 1,000 square feet for rental units. These average sizes are consistent with the prototypes used in the in-lieu fee analysis (see Tables 2.2 and 2.10).

This estimate assumes that all new development will comply with the inclusionary zoning policy by paying the in-lieu fee, rather than by constructing affordable units. In reality, it is likely that a mix of both approaches will be used to comply with the policy. Either means of complying with the policy should result in creation of approximately the same number of affordable units. If all developers complied with the inclusionary zoning requirement by developing on-site affordable housing units, the estimated 239 owner-occupied units developed per year would result in approximately 24 affordable moderate-income units. The estimated 27 rental units developed annually would result in approximately one affordable lower-income unit.

IN-LIEU FEE REVENUE FROM CONDO CONVERSIONS

For condo conversions, the Planning Commission reviewed 152 projects with a total of 2,215 impacted units between 2000 and mid-2007 as shown in Table 4.1 in a prior section of this report. According to the Development Services Department, some of the projects applied for were not pursued due to changes in market conditions. The historical conversion data does not show a clear trend of annual condo conversions. Thus, the condo conversion fee revenue estimate is based on a reasonable estimate of 200 conversions per year.⁷

Table 6.2 shows the estimated annual in-lieu fee revenue from condo conversions if the proposed inclusionary zoning requirements for owner-occupied development are applied to condo conversions. This estimate assumes that all condo conversions will comply with the inclusionary zoning policy by paying the in-lieu fee, rather than by constructing affordable units. In reality, it is likely that a mix of both approaches will be used to comply with the policy. The average square footage of converted units is estimated at 1,000 square feet, consistent with the prototype condo project (see Table 4.2). Annual in-lieu fee revenue is estimated to be \$2.0 million.

⁷ A June 15, 2006 Department of Planning & Building staff report estimated a condo conversion rate of 300 units annually. Because of recent market conditions and uncertainty, we use a more conservative estimate of 200 units annually. (The name of the Department of Planning & Building has changed to the Development Services Department since this staff report was prepared.)

Table 6.2: Potential In-Lieu Fee Revenue from Condo Conversions (2008\$)

Average Square Footage		1,000
In-Lieu Fee per Square Foot	\$	10.10
Fee Revenue Per Unit	\$	10,100
Conversions per Year		200
Annual In-Lieu Fee Revenue	\$	2,020,000

Sources: Table 2.16; MuniFinancial.

COMMERCIAL LINKAGE FEE REVENUE

Table 6.3 presents estimated linkage fee revenue based on the proposed fee levels and the average amount of office, retail, and hotel development that occurred in Long Beach over the past five years. Average development figures are based on data provided by the Long Beach Development Services Department. Both new buildings and additions to existing buildings are included in the average development figures. Fee revenue from all three land uses is estimated to total approximately \$600,000 per year.

Table 6.3: Estimated Annual Commercial Linkage Fee Revenue (2008\$)

	Office	Retail	Hotel ²	Total
Average Development per Year (FY 2004-2008) ¹	37,000	152,000	37,000	
Proposed Fee per Square Foot	\$ 4.00	\$ 2.00	\$ 4.00	
Linkage Fee Revenue per Year	\$ 148,000	\$ 304,000	\$ 148,000	\$ 600,000

¹ Includes FY 2007-2008 development through March 31, 2008.² Hotel square footage estimate based on average of 350 square feet per room, per Long Beach Development Services Department.

Sources: City of Long Beach Development Services Department; MuniFinancial.

APPENDIX A: IN-LIEU FEE IMPACT ANALYSIS

This appendix presents an analysis of the impacts of the proposed in-lieu fees on the feasibility of residential development. Inclusionary zoning impacts are assessed by estimating the change in developers' return on cost for the prototype developments resulting from the imposition of the proposed in-lieu fee.

The impacts of the inclusionary zoning policy and the in-lieu fee on the return on cost will likely be greatest over the short run. Real estate economics suggests that, over time, land values are likely to adjust to accommodate development in response to the inclusionary zoning policy.

RETURN ON COST

The return on cost for the prototype developments is used to estimate the impact of the proposed affordable housing policies on development feasibility. Return on cost, the ratio of net revenue (profit) to total development costs, is one measure used by developers, lenders, and equity investors to evaluate the feasibility and attractiveness of potential development projects. For a project to be feasible, it must provide a large enough return to attract investors and developers to compensate them for the efforts, equity investment, and financial risk. The return on cost percentage covers the entire development period and is not a measure of annual return.

The minimum return on cost required for a development to be feasible is estimated at twelve to sixteen percent. This feasibility hurdle is based on input from the building industry collected for the *Housing Trust Fund Study* and industry standards. As the development period and the perceived risk of a project increase, the minimum feasible return on cost is also likely to increase. For a riskier project, investors and developers will need a higher expected return on cost to make the investment attractive. With a longer development period, equity is tied up for a longer period of time, and a higher total return is needed to attract investment.

Return on cost estimates for the prototype residential developments used in this study are based on the development cost estimates developed in Chapter 2 and market sale price estimates based on recent real estate transactions in Long Beach.

RENTAL PROTOTYPE DEVELOPMENTS

The market value of the rental prototype developments is based on the estimated capitalization rates and net operating income for apartment developments in Long Beach. Net operating income is rental income, less operating costs. Market rents are based on data from RealFacts, which conducts a survey of rents at apartment buildings in Long Beach. The RealFacts data were compared with rents currently advertised on the internet to generate reasonable estimates of rents for new apartments. **Table A.1** shows estimated market rent for the rental development prototypes.

Table A.1: Revenue on Market-Rate Rental Developments (2008\$)

	Number of Units	Market Monthly Rent	Total Annual Revenue
<i>Rental Townhome Project</i>			
1 BR	4	\$ 1,420	\$ 68,160
2 BR/1 BA	3	1,930	69,480
2 BR/2 BA	11	2,140	282,480
3 BR	4	2,390	114,720
Subtotal			\$ 534,840
<i>Apartment Project</i>			
1 BR	7	\$ 1,370	\$ 115,080
2 BR/1 BA	8	1,580	151,680
2 BR/2 BA	25	1,880	564,000
3 BR	10	2,140	256,800
Subtotal			\$ 1,087,560

Sources: Table 2.2; RealFacts Long Beach Market Overview; Craigslist.org; Rent of Primary Residence series, Los Angeles-Riverside-Orange County, Bureau of Labor Statistics; MuniFinancial.

Table A.2 shows the estimated return on cost for the prototype developments, based on the estimated market value and development costs. The market value of the prototype developments is based on estimated net operating income and the current average capitalization rate for apartments in Long Beach. Net operating income consists of rental income less operating costs. Annual operating costs for rental prototype developments are calculated in Table 2.5 in Chapter 2, and capitalization rates are based on figures for Long Beach in the Fall 2007 Colliers International Greater Los Angeles Multifamily Market Report. Based on the return on cost feasibility threshold of twelve to sixteen percent, both rental development prototypes would be feasible with the proposed inclusionary zoning policy.

Table A.2: Return on Cost, Rental Developments - Current Market Conditions

	Rental Townhome Project	Apartment Project
<i>No In-Lieu Fee</i>		
Operating Income-Market Rent	\$ 534,840	\$ 1,087,560
Operating Costs	<u>130,349</u>	<u>258,874</u>
Net Operating Income	\$ 404,491	\$ 828,686
Average Cap Rate	<u>5.1%</u>	<u>5.1%</u>
Project Market Value	\$ 7,931,192	\$ 16,248,742
Development Costs (Excluding Profit)	<u>6,167,792</u>	<u>10,984,106</u>
Developer Profit	\$ 1,763,400	\$ 5,264,636
Return on Cost	29%	48%
<i>In-Lieu Fee per Sq. Ft. of:</i>		
\$	10.78	24%
		43%

Sources: Tables 2.3, 2.5, and A.1; Colliers International Greater Los Angeles Multifamily Market Report, Fall 2007; MuniFinancial.

OWNER PROTOTYPE DEVELOPMENTS

For owner-occupied developments, market value is the total sale value of the condo units in the development. Market value estimates are based in condo sales in 2006 and the first half of 2007 in Long Beach in the DataQuick Information Systems database, combined with DataQuick reports documenting trends in condo prices over the past year. Values shown are based on the median price per square foot for each number of bedrooms, multiplied by the square footage of the prototype units. The high-rise condo prototype represents a premium condo development. Estimated prices for the high-rise units are based on the 75th percentile price per square foot for the given number of bedrooms. The trends documented by DataQuick lead to an estimated ten percent drop in market condo prices since the initial estimates were prepared in mid-2007. **Table A.3** shows estimated revenue for each of the owner-occupied prototype developments.

Table A.3: Revenue on Owner-Occupied Developments (2008\$)

	Number of Units	Market Sale Price	Total Revenue
<i>Owner-Occupied Townhomes</i>			
Loft	-	N/A	N/A
1 BR	-	N/A	N/A
2 BR	13	\$ 360,000	\$ 4,680,000
3 BR	9	390,000	3,510,000
Subtotal			\$ 8,190,000
<i>Stacked Flats Condos</i>			
Loft	-	N/A	N/A
1 BR	7	\$ 310,000	\$ 2,170,000
2 BR	33	360,000	11,880,000
3 BR	10	420,000	4,200,000
Subtotal			\$ 18,250,000
<i>High-Rise Condos</i>			
Loft	10	\$ 340,000	\$ 3,400,000
1 BR	10	340,000	3,400,000
2 BR	60	400,000	24,000,000
3 BR	20	530,000	10,600,000
Subtotal			\$ 41,400,000

Sources: Table 2.10; DataQuick Information Systems; MuniFinancial.

Table A.4 shows the estimated return on cost for the owner-occupied prototype developments, based on the estimated revenue shown above and the development costs shown in Table 2.11. As shown, the stacked flats condo prototype development provides a return on cost above the feasibility threshold with the proposed in-lieu fee. The townhome

and the high-rise condo prototype developments are not feasible under current market conditions, even without an inclusionary zoning requirement. At the proposed fee level, the in-lieu fee results in a three to four percentage point reduction in return on cost for the three prototype developments.

Table A.4: Return on Cost, Owner-Occupied Developments - Current Market Conditions

	Owner-Occupied Townhome Project	Stacked Flats Condos	High-Rise Condos
<i>No In-Lieu Fee</i>			
Sales Revenues	\$ 8,190,000	\$ 18,250,000	\$ 41,400,000
Development Costs (Excluding Profit)	<u>7,602,531</u>	<u>13,909,018</u>	<u>40,610,868</u>
Developer Profit	\$ 587,469	\$ 4,340,982	\$ 789,132
Return on Cost	8%	31%	2%
<i>In-Lieu Fee per Sq. Ft. of:</i>			
\$ 10.10	4%	27%	-1%

Sources: Tables 2.11 and A.3; MuniFinancial.

APPENDIX B: LINKAGE FEE IMPACT ANALYSIS

This Appendix provides details of the impacts of the proposed commercial linkage fees on the feasibility of nonresidential development. Residual land value analysis calculates the value of a development based on its net operating income and the current capitalization rate, and subtracts the development costs to estimate the underlying value of the land. A land residual analysis is commonly used by real estate developers to evaluate the financial feasibility of a site and to select among alternative uses.

Assumptions on development costs, income, and operating expenses are shown in **Table B.1**. These assumptions generally follow and update the assumptions used in the 2003 *Housing Trust Fund Study*. Construction costs are updated for inflation from the 2003 study using the *Engineering News-Record* Building Cost Index (BCI). Other costs are adjusted for inflation based on the Consumer Price Index. Market rent (annual gross income) figures are based on current market reports for the Los Angeles-Long Beach area. Existing development fees are estimated to be 1.8 percent of the development's market value based on the fee burden analysis conducted as a part of this study.

Table B.1: Nonresidential Development Unit Costs (2008\$)

Cost/Income by Land Use	Unit of Measure	Community			
		Class A Office	Retail	Hotel	Light Manufacturing
Hard Construction Costs	Gross SF	\$ 137	\$ 107	\$ 140	\$ 101
Development Fees	% Capitalized Value	1.8%	1.8%	1.8%	1.8%
Tenant Improvement Allowance/FF&E	Net Rentable SF	\$ 45	\$ 45	\$ 45	\$ 19
Annual Gross Income	Net Rentable SF	\$ 28.68	\$ 27.00	\$ 110.00	\$ 8.04
Other Income	% of Gross Income	0%	0%	33%	0%
Operating Expenses	% of Gross Income	5%	5%	75%	5%
Efficiency	%	90%	87.5%	75%	95%
Gross SF/Room	Gross SF			750	
Occupancy Rate	%	95%	95%	70%	100%
Parking Income	\$/Space/Month	\$ 89	0%	0%	0%
Parking Expense	% of Gross Income	20%	0%	0%	0%
<u>Parking Requirements</u>					
Parking Spaces		2.4	5	1.2	2
Per		1000	1000	1	1000
Unit		Gross SF	Gross SF	Room	Gross SF
<u>Parking Costs</u>					
Above-Grade Structured Parking	\$ 31.75 per SF @		400 SF/Space or	\$ 12,700 /Space	
Underground Parking	\$ 63.75 per SF @		400 SF/Space or	\$ 25,500 /Space	
Surface Parking	\$ 3.14 per SF @		350 SF/Space or	\$ 1,100 /Space	
<u>Parking</u>					
Development					
Gross Building SF		100,000	100,000	100,000	100,000
# of Hotel Rooms				133	
Total Parking Spaces Required		240	500	160	200
Parking Allocation					
Above-Grade Parking Spaces		0%	0%	0%	0%
Underground Parking Spaces		100%	0%	85%	0%
Surface Parking Spaces		0%	100%	15%	100%
Total Parking Spaces					
Above-Grade Parking Spaces		-	-	-	-
Underground Parking Spaces		240	-	136	-
Surface Parking Spaces		-	500	24	200
Contingencies		3.0% Percent of Total Hard Costs			
<u>Construction Financing</u>					
Construction Interest		7.0% Assumes 12 month development period and 60% average loan balance			
Loan Origination Fees		1.5%			
<u>Soft Costs</u>					
Planning/Design		0% Included in Hard Costs			
Taxes/Insurance/Legal/Accounting		2% Percent of Hard Costs plus Tenant Improvements			
Marketing/Leasing		2% Percent of Hard Costs plus Tenant Improvements			
Development/Management		3% Percent of Hard Costs plus Tenant Improvements			
Total Soft Costs		7% Percent of Hard Costs plus Tenant Improvements			

Sources: City of Long Beach Housing Trust Fund Study, David Paul Rosen & Associates, 2003; Building Cost Index, Engineering News-Record; Office Market Trends Los Angeles, Fourth Quarter 2007, Grubb and Ellis; Retail Market Trends Los Angeles County, First Quarter 2007, Grubb and Ellis; South Bay Industrial Market Report, Fourth Quarter 2007, Colliers International; MuniFinancial.

Based on the unit development costs shown above, **Table B.2** shows the development costs for the 100,000 square foot prototype developments included in the residual land value analysis.

Table B.2: Development Costs (2008\$)

	Class A Office	Community Retail	Hotel	Light Manufacturing
Building Square Feet	100,000	100,000	100,000	100,000
<i>Construction Costs (thousands)</i>				
Shell and Core Costs	\$ 13,700,000	\$ 10,700,000	\$ 14,000,000	\$ 10,100,000
Parking Costs	6,120,000	550,000	3,494,400	220,000
Permits and Fees	773,264	639,647	650,406	214,114
Total Hard Costs	\$ 20,593,264	\$ 11,889,647	\$ 18,144,806	\$ 10,534,114
Contingencies	\$ 617,798	\$ 356,689	\$ 544,344	\$ 316,023
Tenant Improvements/FF&E	4,050,000	3,937,500	3,375,000	1,805,000
Soft Costs	1,725,029	1,107,900	1,506,386	863,738
Subtotal - All Construction Costs	\$ 26,986,091	\$ 17,291,737	\$ 23,570,537	\$ 13,518,876
<i>Financing Costs</i>	\$ 1,150,417	\$ 737,147	\$ 1,004,812	\$ 576,310
Total Development Costs (Excluding Land)	\$ 28,136,508	\$ 18,028,883	\$ 24,575,348	\$ 14,095,186
Total Costs per SF	\$ 281	\$ 180	\$ 246	\$ 141

Sources: Table B.1, MuniFinancial.

Table B.3 shows the net operating income for the non-residential prototype developments.

Table B.3: Net Operating Income (2008\$)

	Class A Office	Community Retail	Hotel	Light Manufacturing
<i>Net (Operating) Income (thousands)</i>				
Gross Income by Use	\$ 2,452,140	\$ 2,244,375	\$ 3,737,965	\$ 763,800
Other Income	-	-	1,233,528	-
Parking Income	256,320	-	-	-
Total Income	\$ 2,708,460	\$ 2,244,375	\$ 4,971,493	\$ 763,800
Operating Expense	173,871	112,219	2,803,474	38,190
Net (Operating) Income	\$ 2,534,589	\$ 2,132,156	\$ 2,168,020	\$ 725,610
Net (Operating) Income per SF	\$ 25.35	\$ 21.32	\$ 21.68	\$ 7.26

Sources: Tables B.1 and B.2; MuniFinancial.

Table B.4 shows the residual land value for the prototype developments at various potential linkage fee levels. The residual land value is the difference between a development's market value and its development costs, excluding land. This difference is attributed to the value of the land. A proposed development is feasible if the actual land cost is less than the residual land value. The market value of the prototype developments is based on the net operating

income estimated above and current capitalization (cap) rates for Long Beach.⁸ Cap rate data was not available for hotels, so the average cap rate for the other development types is used.

Table B.4: Land Residual Value Analysis (2008\$)

	Class A Office	Community Retail	Hotel	Light Manufacturing
Gross SF Bldg Area	100,000	100,000	100,000	100,000
Floor Area Ratio	1.70	0.25	1.70	0.25
Net SF Site Area	58,824	400,000	58,824	400,000
Annual Net Operating Income	\$ 2,534,589	\$ 2,132,156	\$ 2,168,020	\$ 725,610
Assumed Capitalization Rate	5.9%	6.0%	6.0%	6.1%
Capitalized Value	\$ 42,959,136	\$ 35,535,938	\$ 36,133,662	\$ 11,895,246
Total Development Costs (Except Land)	\$ 28,136,508	\$ 18,028,883	\$ 24,575,348	\$ 14,095,186
Residual Land Value	\$ 14,822,628	\$ 17,507,054	\$ 11,558,313	\$ (2,199,940)
Residual Land Value per SF Site Area	251.98	43.77	196.49	(5.50)
<u>\$2.00/SF Linkage Fee</u>				
Total Linkage Fee	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000
Residual Land Value	14,622,628	17,307,054	11,358,313	(2,399,940)
Residual Land Value per SF Site Area	248.58	43.27	193.09	(6.00)
Pct. Reduction in Residual Land Value	1.3%	1.1%	1.7%	9.1%
<u>\$4.00/SF Linkage Fee</u>				
Total Linkage Fee	\$ 400,000	\$ 400,000	\$ 400,000	\$ 400,000
Residual Land Value	14,422,628	17,107,054	11,158,313	(2,599,940)
Residual Land Value per SF Site Area	245.18	42.77	189.69	(6.50)
Pct. Reduction in Residual Land Value	2.7%	2.3%	3.5%	18.2%

Sources: Tables B.2 and B.3; *Greater Los Angeles Basin Commercial Real Estate Market Outlook, 2007*, Colliers International; MuniFinancial.

⁸ The cap rate is a measure used in real estate analysis to compare the price of a property to the income it generates. The cap rate is the net operating income divided by the sales price.

APPENDIX C: FEE BURDEN ANALYSIS

Appendix C presents an analysis of the overall fee burden on development in the City of Long Beach and six comparable cities in California. This involves analyzing the aggregate impact of plan check fees, permit fees, and development impact fees on several typical types of development. Specific attention is given to affordable housing fees charged in the cities included in the survey. The affordable housing fee survey included in-lieu fees, commercial linkage fees, and condominium conversion fees that are charged to benefit an affordable housing trust fund. The analysis presented here updates a study conducted by MuniFinancial in January 2007.

While a comparative analysis should not be used as a tool to determine fee amounts, it does provide a reference point indicating how the fees charged in a given city compare to those in neighboring or similar communities. Studies show that inclusionary zoning requirements and in-lieu fees have had little to no impact on the production of market-rate housing in jurisdictions where they have been adopted.^{9,10} Although the fees charged to new development are not typically large enough to have a tangible affect on real estate markets, substantial differences in the fee burden between two otherwise similar cities could potentially impact the location patterns of development over time.

The development project prototypes used in this analysis are shown in **Table C.1**. These development scenarios constitute hypothetical rather than actual projects. These projects were determined based on market research and input from City of Long Beach staff. A key objective of the project selection was to provide a diverse range of development types that vary across land use, building size, and market value. Because this study is based on a variety of development types, it is possible to apply the conclusions of the fee burden analysis to most types of development likely to occur within the City.

The market values shown in the table below are for the City of Long Beach only. Alternative market values for the target cities are shown in Table C.2.

⁹ “The Effects of Inclusionary Zoning on Local Housing Markets: Lessons from the San Francisco, Washington DC and Suburban Boston Areas,” Furman Center for Real Estate & Urban Policy, March 2008.

¹⁰ “Inclusionary Housing and its Impact on Housing and Land Markets,” *Inclusionary Zoning: The California Experience*, NHC Affordable Housing Policy Review, February 2004.

Table C.1: Typical Developments by Type (2008\$)

	Multi-Family Dwelling Unit	Office Development	Retail Development
Average Size (square feet)	1,518	7,671	6,600
Market Value per Square Foot	\$ 366	\$ 420	\$ 420
Total Market Value	\$ 555,463	\$ 3,221,820	\$ 2,772,000

Sources: DataQuick Information Services, SoCal MLS Database; City of Long Beach; MuniFinancial.

Table C.2 presents a summary of the fee burdens by city and development scenario in greater detail. Market values for each of the three development prototypes are shown for each city. The fee burden includes affordable housing fees, plan check fees, permit fees, and development impact fees. The overall fee burden is shown as a percent of market value. The most significant differences in the amounts charged by the cities included in the burden analysis are in the amount of development impact fees charged to capture the cost of infrastructure and public facilities, and whether the city charges affordable housing fees.

The development impact fees for Long Beach include school fees approved by the School Board on September 25, 2007. The school fee increased to \$3.28 per square foot. The \$0.42 per square foot school fee for nonresidential development did not change. The development impact fees also include recently adopted parks and public safety fees.

Table C.2: Fee Burden Comparison Survey (2008\$)

Square Footage	Multi-Family Residence (8 unit condo)			Office Development	Retail Development
	12,144	7,671	6,600		
<u>Long Beach (existing fees)</u>					
Market Value	\$ 4,443,708	\$ 3,221,820	\$ 2,772,000		
Plan Check Fees	18,394	14,524	7,050		
Permit Fees	27,225	15,341	8,262		
Development Impact Fees	103,042	27,836	29,220		
Total Fees	\$ 148,661	\$ 57,700	\$ 44,532		
Fees as a % of Value	3.35%	1.79%	1.61%		
<u>Long Beach (proposed fees)</u>					
Market Value	\$ 4,443,708	\$ 3,221,820	\$ 2,772,000		
Affordable Housing Fees ¹	122,655	30,684	13,200		
Plan Check Fees	18,394	14,524	7,050		
Permit Fees	27,225	15,341	8,262		
Development Impact Fees	103,042	27,836	29,220		
Total Fees	\$ 271,316	\$ 88,384	\$ 57,732		
Fees as a % of Value	6.11%	2.74%	2.08%		
<u>Anaheim</u>					
Market Value	\$ 3,746,800	\$ 3,506,500	\$ 3,016,900		
Plan Check Fees	8,993	6,095	4,363		
Permit Fees	13,479	14,749	16,726		
Development Impact Fees	99,054	42,097	51,247		
Total Fees	\$ 121,525	\$ 62,942	\$ 72,336		
Fees as a % of Value	3.24%	1.80%	2.40%		
<u>Santa Ana</u>					
Market Value	\$ 4,170,100	\$ 3,390,000	\$ 2,916,700		
Plan Check Fees	23,971	10,392	10,399		
Permit Fees	11,178	5,412	3,390		
Development Impact Fees	103,019	50,614	45,219		
Total Fees	\$ 138,168	\$ 66,418	\$ 59,009		
Fees as a % of Value	3.31%	1.96%	2.02%		

Table C.2 continues on the next page.

Table C.2: Fee Burden Comparison Survey (cont.) (2008\$)

Square Footage	Multi-Family Residence (8 unit condo)		Office Development	Retail Development		
	12,144		7,000	6,600		
<u>Los Angeles</u> ²						
Market Value	\$	5,310,953	\$	3,815,900	\$	3,283,200
Plan Check Fees		5,142		3,586		2,683
Permit Fees		9,402		5,863		4,499
Development Impact Fees		44,375		11,370		4,396
Total Fees	\$	58,919	\$	20,819	\$	11,577
Fees as a % of Value		1.11%		0.55%		0.35%
<u>Huntington Beach</u>						
Market Value	\$	4,869,300	\$	3,545,300	\$	3,050,300
Plan Check Fees		6,760		4,003		2,738
Permit Fees		4,708		2,828		1,922
Development Impact Fees		43,069		6,162		5,544
Total Fees	\$	54,537	\$	12,993	\$	10,204
Fees as a % of Value		1.12%		0.37%		0.33%
<u>San Diego</u>						
Market Value	\$	4,019,200	\$	3,597,100	\$	3,094,800
Affordable Housing Fees ³		38,375		8,131		4,224
Plan Check Fees		10,702		6,780		5,750
Permit Fees		272		2,514		2,461
Development Impact Fees		26,251		3,222		2,772
Total Fees	\$	75,600	\$	20,647	\$	15,207
Fees as a % of Value		1.88%		0.57%		0.49%
<u>San Jose</u> ⁴						
Market Value	\$	5,039,200	\$	3,855,800	\$	3,317,500
Plan Check Fees		14,087		2,093		2,093
Permit Fees ⁵		1,647		534		534
Development Impact Fees		122,674		23,856		15,893
Total Fees	\$	138,408	\$	26,483	\$	18,520
Fees as a % of Value		2.75%		0.69%		0.56%

¹ Proposed affordable housing fees for the City of Long Beach include a \$10.10 per square foot fee for owner-occupied residential development, a \$4.00 per square foot fee for office developments, and a \$2.00 per square foot fee for retail developments.

² The City of Los Angeles only charges affordable housing fees for the area covered by the Central City West Specific Plan. Currently, no citywide affordable housing fees exist.

³ Affordable housing fees for the City of San Diego include an in-lieu fee of \$3.16 per square foot on residential developments of 9 or fewer units. Commercial linkage fees are \$1.06 per square foot for office developments, and \$0.64 per square foot for retail developments.

⁴ The City of San Jose charges a \$17 per square foot affordable housing fee on residential developments for a redevelopment area only. Currently, no citywide affordable housing fees exist.

⁵ Includes construction taxes.

Sources: City of Long Beach; City of Anaheim; City of Santa Ana; City of Los Angeles; City of Huntington Beach; City of San Diego; City of San Jose; MuniFinancial.

Table C.3 below summarizes the results of the survey in terms of fee burden as a percent of market value. The burden on new multi-family residential development in the comparison cities included in the burden analysis ranges from a high of 3.31 percent in Santa Ana to a low of 1.11 percent for a development in Los Angeles. The current fee burden in Long Beach is estimated at 3.35 percent, which is close to, but slightly higher than, the fee burden estimated in Anaheim and Santa Ana. The proposed affordable housing fees are estimated to be approximately 2.29 percent of market value for the prototype multi-family residential development. If the proposed affordable housing fees are adopted, the total fee burden in Long Beach would be approximately 6.11 percent of market value, which is almost three percentage points higher than the fee burden charged in the comparison cities with the next highest fee burden.

Long Beach's existing fee burden on office development is in the middle of the range of cities surveyed, with fees ranging from approximately 0.37 percent of market value in Huntington Beach to 1.96 percent in Santa Ana. The proposed affordable housing linkage fee for office development would raise the fee burden to 2.74 percent, which is higher than the burden imposed in any of the comparison cities.

Like the office fee burden, Long Beach's current retail fee burden is in the middle of the range of comparison cities. The burden on retail development ranges from 0.33 percent in Huntington Beach to 2.40 percent in Anaheim. Long Beach's current fee burden on the retail development prototype is estimated at 1.61 percent. The proposed affordable housing fees would raise the fee burden on retail development to approximately 2.08 percent.

Only one of the cities surveyed in the burden analysis currently charges affordable housing fees. The fee burden of San Diego's affordable housing fees is shown in Table C.3 as a portion of the overall burden. The burden attributable to affordable housing fees on an eight unit multi-family residential development is 0.95 percent of market value. San Diego's affordable housing fees on nonresidential development create a burden of 0.23 percent of market value on office development and 0.14 percent on retail development.

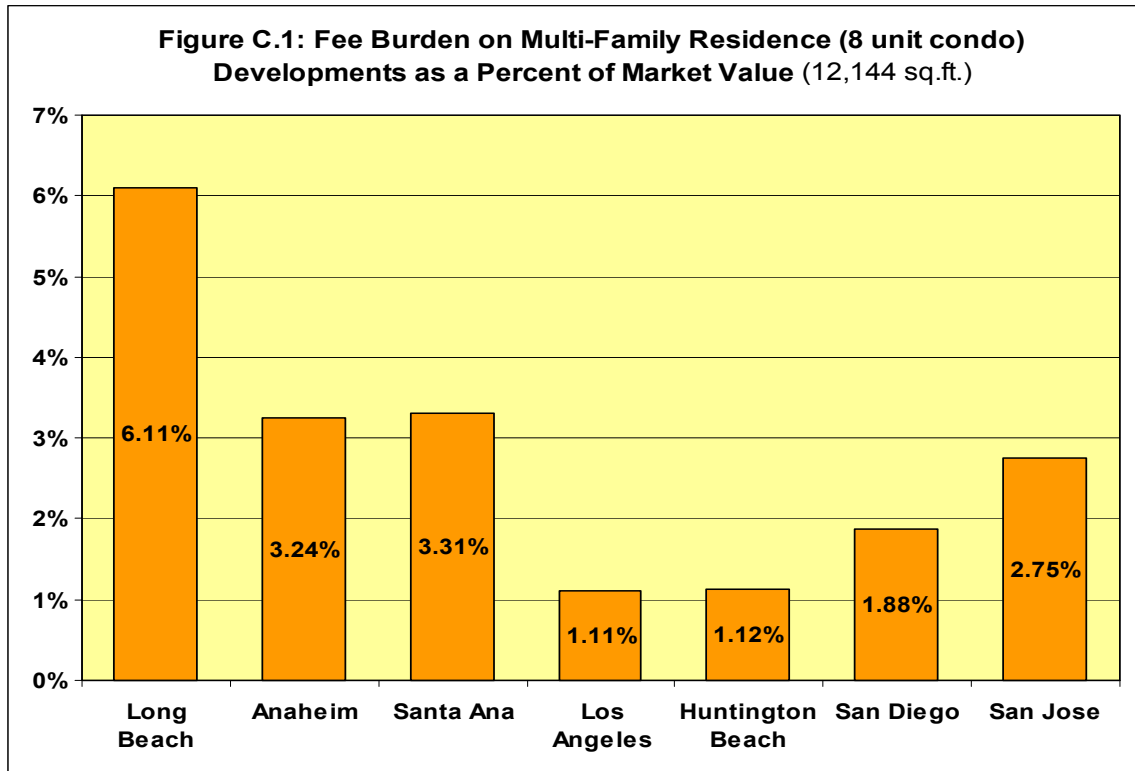
We recommend including cost offsets and a variety of options for complying with the inclusionary zoning requirements to reduce the policy's impacts on the feasibility of development in Long Beach. (See Chapter 5, Maintaining Development Feasibility.) While not directly reducing the fee burden, these measures would help to offset the impact of the new requirements on development feasibility.

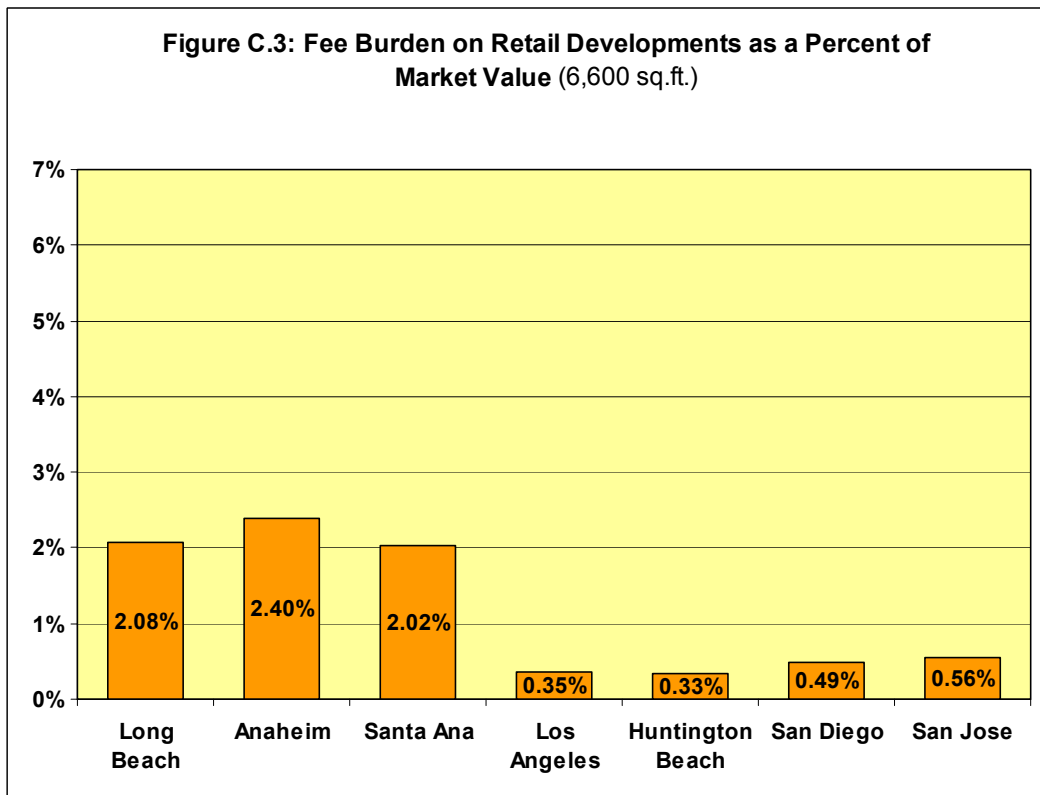
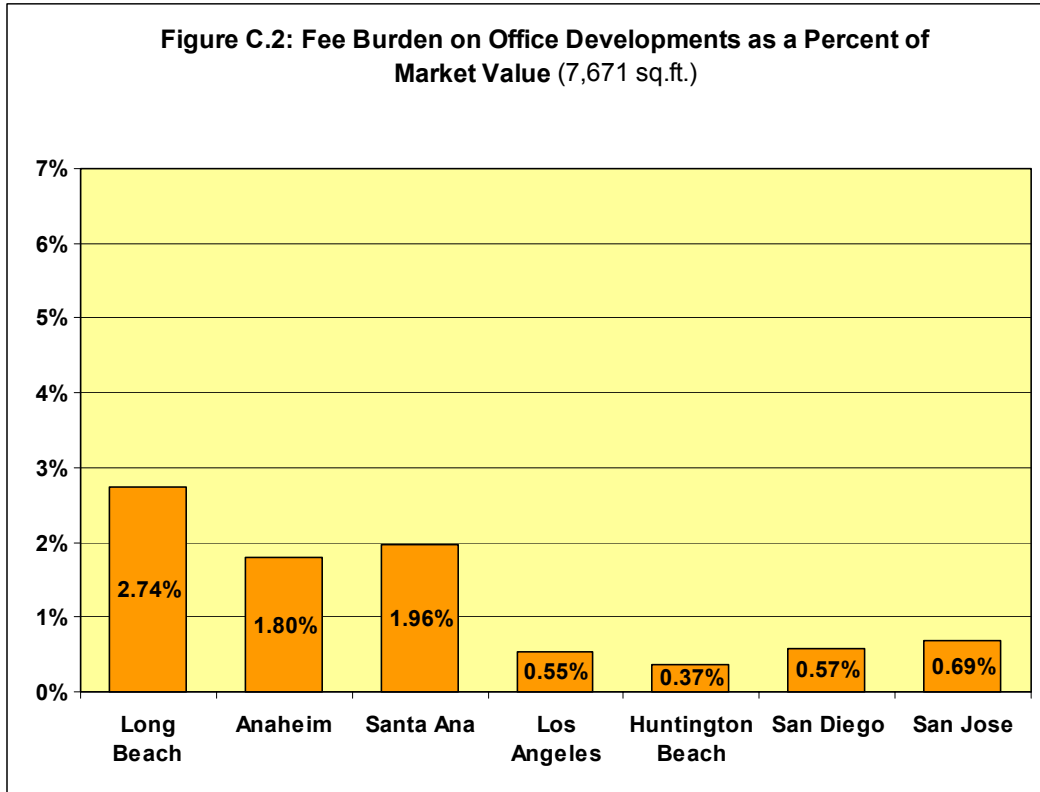
Table C.3: Fee Burden Comparison Survey Results (Fee Burden as a Percentage of Total Market Value)

	Multi-Family Residence (8 unit condo)	Office Development	Retail Development
Square Footage	12,144	7,671	6,600
Long Beach			
Existing Burden	3.35%	1.79%	1.61%
Proposed Affordable Housing Fees	2.76%	0.95%	0.48%
Total Potential Burden	6.11%	2.74%	2.08%
Anaheim	3.24%	1.80%	2.40%
Santa Ana	3.31%	1.96%	2.02%
Los Angeles	1.11%	0.55%	0.35%
Huntington Beach	1.12%	0.37%	0.33%
San Diego	1.88%	0.57%	0.49%
<i>Affordable Housing Fees</i>	0.95%	0.23%	0.14%
San Jose	2.75%	0.69%	0.56%

Sources: City of Long Beach; City of Anaheim; City of Santa Ana; City of Los Angeles; City of Huntington Beach; City of San Diego; City of San Jose; MuniFinancial.

Figures C.1 through C.3 below present a summary of fee burdens by city and development type.





APPENDIX D: 2007 INCLUSIONARY ZONING ANALYSIS

This section presents the tables used in the affordability gap and inclusionary zoning impact analysis based on development cost and market price data collected in mid-2007. A full description of each table is provided where it appears in the analysis based on current data in Chapter 2 or Appendix A.

RENTAL AFFORDABILITY GAP AND INCLUSIONARY ZONING COST

Table D.1 shows the estimated development costs for the rental prototypes. See Table 2.3 in Chapter 2 for development cost estimates based on current market data.

Table D.1: Rental Unit Development Costs - 2007

	Rental Townhome Project		Apartment Project	
	Unit Cost	Total	Unit Cost	Total
<u>Land</u>	\$ 69.00 per sq. ft.	\$ 2,644,963	\$ 69.00 per sq. ft.	\$ 2,134,004
<u>Direct Costs</u>				
Construction	\$ 95.00 per sq. ft.	2,348,611	\$ 110.00 per sq. ft.	6,013,333
Site Improvements	\$ 7.50 per site sq. ft.	287,496	\$ 7.50 per site sq. ft.	231,957
Subtotal - Direct Costs		2,636,107		6,245,290
<u>Indirect Costs</u>				
Architecture and Engineering	5% direct costs	131,805	5% direct costs	312,265
Hard Cost Contingency	5% direct costs	131,805	5% direct costs	312,265
Permits & Impact Fees	\$ 14,700 per unit	323,400	\$ 14,700 per unit	735,000
Other Indirect Costs ¹	5% direct costs	131,805	5% direct costs	312,265
Subtotal - Indirect Costs		718,816		1,671,794
Subtotal - Land, Direct, and Indirect Costs		5,999,886		10,051,088
<u>Construction Loan Costs</u>				
Construction Loan as a % of				
Land, Direct, Indirect Costs	75% \$	4,499,915	75% \$	7,538,316
Fees, Title, and Closing	1.25% loan amount	56,249	1.25% loan amount	94,229
Average Loan Balance				
(Construction/Lease-Up)	60% \$	2,699,949	60% \$	4,522,990
Construction/Lease-Up Interest ²	7% per year	236,246	7% per year	395,762
<u>Marketing/Leasing/Startup Costs</u>				
Marketing/Leasing/Startup Costs	\$ 1,200 per unit	26,400	\$ 1,200 per unit	60,000
Market Study/Consulting	estimated project cost	29,000	estimated project cost	29,000
Subtotal - Development Costs		6,347,781		10,630,079
<u>Developer Overhead</u>				
	4% above costs	253,911	4% above costs	425,203
Development Cost		6,601,692		11,055,282
Developer Profit	12% dev. cost	792,203	12% dev. cost	1,326,634
Total Developer Cost and Profit		\$ 7,393,895		\$ 12,381,916
Cost per Unit		\$ 336,086		\$ 247,638

¹ Includes insurance and taxes during construction, legal, title, appraisal, soils testing, and environmental costs.

² Estimated construction loan term includes 12 month construction period and 3 month lease-up period, for a total of 15 months.

Sources: Table 2.2; DataQuick Information Systems; *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; Consumer Price Index for Los Angeles-Riverside-Orange County, CA, U.S. Bureau of Labor Statistics; Building Cost Index, *Engineering News-Record*; MuniFinancial.

Table D.2 shows the affordable rent for very low- and low-income households based on the 2007 AMI. (Compare with Table 2.4.)

Table D.2: 2007 Income Standards and Affordable Monthly Rent

Household Size	2 Persons/ 1 Bedroom	3 Persons/ 2 Bedroom	4 Persons/ 3 Bedrooms
<u>Area Median Income</u>	\$ 45,200	\$ 50,900	\$ 56,500
<u>Very Low Income (50% AMI)</u>			
Annual Income	\$ 22,600	\$ 25,450	\$ 28,250
Affordable Annual Housing Costs (30% of Income)	6,780	7,635	8,475
Affordable Monthly Housing Costs	\$ 565	\$ 636	\$ 706
Utility Allowance	51	74	101
Affordable Monthly Rent	\$ 514	\$ 562	\$ 605
<u>Low Income (60% AMI)</u>			
Annual Income	\$ 27,120	\$ 30,540	\$ 33,900
Affordable Annual Housing Costs (30% of Income)	8,136	9,162	10,170
Affordable Monthly Housing Costs	\$ 678	\$ 764	\$ 848
Utility Allowance	51	74	101
Affordable Monthly Rent	\$ 627	\$ 690	\$ 747

Sources: California Department of Housing and Community Development; Keyser Marston Associates; MuniFinancial.

Table D.3 shows the estimated operating costs used in the 2007 analysis. (Compare with Table 2.5.)

Table D.3: Rental Operating Costs - 2007

	Unit Cost	Number of Units	Total Cost
<u>Rental Townhomes</u>			
Taxes	1.10% of total dev. cost	\$ 7,393,895 dev. cost	\$ 81,333
Management Costs	\$ 900 per unit	22 units	19,800
Insurance	286 per unit	22 units	6,292
Maintenance	1,035 per unit	22 units	22,770
Replacement Reserve	250 per unit	22 units	5,500
Total Annual Operating Costs			\$ 135,695
<u>Apartments</u>			
Taxes	1.10% of total dev. cost	\$ 12,381,916 dev. cost	\$ 136,201
Management Costs	\$ 900 per unit	50 units	45,000
Insurance	286 per unit	50 units	14,300
Maintenance	1,035 per unit	50 units	51,750
Replacement Reserve	250 per unit	50 units	12,500
Total Annual Operating Costs			\$ 259,751

Sources: Los Angeles County Assessor; Table 3-271 Market Rent Properties in Los Angeles-Long Beach-Santa Ana, CA, MSA, Less than 100 Units, *Dollars and Cents of Multifamily Housing: 2006*, Urban Land Institute; *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; MuniFinancial.

Table D.4 shows the estimated net operating income for the rental development prototypes based on the 2007 affordable rents and operating costs. (Compare with Table 2.6.)

Table D.4: Rental Net Operating Income - 2007

	Number of Units	Affordable Rent ¹	Monthly Income	Annual Income
<i><u>Townhome Project - Lower Income</u></i>				
1 Bedroom	4	\$ 627	\$ 2,508	\$ 30,096
2 Bedroom	14	690	9,653	115,836
3 Bedroom	4	747	2,986	35,832
Subtotal				\$ 181,764
Loss to Vacancy (3%)				(5,453)
Total Income				\$ 176,311
Operating Costs				135,695
Net Operating Income				\$ 40,616
<i><u>Apartment Project - Lower Income</u></i>				
1 Bedroom	7	\$ 627	\$ 4,389	\$ 52,668
2 Bedroom	33	690	22,754	273,042
3 Bedroom	10	747	7,465	89,580
Subtotal				\$ 415,290
Loss to Vacancy (3%)				(12,459)
Total Income				\$ 402,831
Operating Costs				259,751
Net Operating Income				\$ 143,080
<i><u>Apartment Project - Very Low Income</u></i>				
1 Bedroom	7	\$ 514	\$ 3,598	\$ 43,176
2 Bedroom	33	562	18,546	222,552
3 Bedroom	10	605	6,050	72,600
Subtotal				\$ 338,328
Loss to Vacancy (3%)				(10,150)
Total Income				\$ 328,178
Operating Costs				259,751
Net Operating Income				\$ 68,427

¹ Assumes two persons per bedroom.

Sources: Tables 2.2, D.2 and D.3; MuniFinancial.

Table D.5 shows the mortgage that would be supportable by the net operating income generated by the prototype developments, based on 2007 affordable rents. (Compare with Table 2.7.)

Table D.5: Supportable Mortgage - 2007

		Rental Townhome Project - Lower Income		Apartment Project - Lower Income		Apartment Project - Very Low Income
Net Operating Income	\$	40,616	\$	143,080	\$	68,427
Coverage Ratio		1.25		1.25		1.25
Supportable Annual Payment	\$	32,493	\$	114,464	\$	54,742
Mortgage Term		30 years		30 years		30 years
Interest Rate		7%		7%		7%
Supportable Mortgage	\$	406,995	\$	1,433,736	\$	685,674

Sources: Table D.4; MuniFinancial

Table D.6 shows the affordability gap for rental units based on 2007 assumptions. (Compare with Table 2.8.)

Table D.6: Affordability Gap on Rental Units - 2007

		Rental Townhome Project - Lower Income		Apartment Project - Lower Income		Apartment Project - Very Low Income
Development Costs	\$	7,393,895	\$	12,381,916	\$	12,381,916
Supportable Mortgage		406,995		1,433,736		685,674
Affordability Gap	\$	6,986,900	\$	10,948,180	\$	11,696,242
Number of Units		22		50		50
Affordability Gap per Unit	\$	317,586	\$	218,964	\$	233,925

Sources: Tables 2.2, D.1, and D.5; MuniFinancial.

Table D.7 shows the cost per square foot equivalent to meeting the inclusionary zoning policy affordability requirement by providing the required affordable units on-site. (Compare with Table 2.9.)

Table D.7: Rental Housing Inclusionary Zoning In-Lieu Costs - 2007

	Rental Townhome Project	Apartment Project
Gap per Affordable Unit (Low Income Households)	\$ 317,586	\$ 218,964
Inclusionary Zoning Requirement	<u>5%</u>	<u>5%</u>
In-Lieu Cost per Market Rate Unit	\$ 15,879	\$ 10,948
Average Square Feet per Unit	<u>1,011</u>	<u>984</u>
In-Lieu Cost per Square Foot	\$ 15.71	\$ 11.13

Sources: Tables 2.1, 2.2 and D.6; MuniFinancial.

OWNER-OCCUPIED AFFORDABILITY GAP AND INCLUSIONARY ZONING COST

Table D.8 shows the estimated development costs for the owner-occupied prototype developments. (Compare with Table 2.11.)

Table D.8: Owner-Occupied Unit Development Costs - 2007

	Owner-Occupied Townhome Project		Stacked Flat Condo Project		High-Rise Condo Project	
	Unit Cost	Total	Unit Cost	Total	Unit Cost	Total
<u>Land</u>	\$ 69.00 per sq. ft.	\$ 2,644,963	\$ 69.00 per sq. ft.	\$ 2,134,004	\$ 69.00 per sq. ft.	\$ 3,005,640
<u>Direct Costs</u>						
Construction	\$ 100.00 per sq. ft.	2,888,889	\$ 115.00 per sq. ft.	7,142,778	\$ 187.00 per sq. ft.	24,200,000
Site Improvements	\$ 7.50 per site sq. ft.	287,496	7.50 per site sq. ft.	231,957	7.50 per site sq. ft.	326,700
Subtotal - Direct Costs		3,176,385		7,374,735		24,526,700
<u>Indirect Costs</u>						
Architecture and Engineering	5% direct costs	158,819	5% direct costs	368,737	5% direct costs	1,226,335
Hard Cost Contingency	5% direct costs	158,819	5% direct costs	368,737	5% direct costs	1,226,335
Permits & Impact Fees	\$ 14,700 per unit	323,400	\$ 14,700 per unit	735,000	\$ 14,700 per unit	1,470,000
Other Indirect Costs ¹	5% direct costs	158,819	5% direct costs	368,737	5% direct costs	1,226,335
Subtotal - Indirect Costs		799,858		1,841,210		5,149,005
Subtotal - Land, Direct, and Indirect Costs		6,621,206		11,349,949		32,681,345
<u>Construction Loan Costs</u>						
Construction Loan as a % of Land, Direct, Indirect Costs	85% \$	5,628,025	85% \$	9,647,457	85% \$	27,779,143
Fees, Title, and Closing	1.25% loan amount	70,350	1.25% loan amount	120,593	1.25% loan amount	347,239
Average Loan Balance (Construction/Lease-Up)	60% \$	3,376,815	60% \$	5,788,474	60% \$	16,667,486
Construction/Lease-Up Interest ²	7% per year	295,471	7% per year	607,790	7% per year	1,750,086
<u>Sales Costs</u>						
Commissions/Selling/Closing Costs	6% total dev. cost	525,001	6% total dev. cost	907,558	6% total dev. cost	2,613,246
Subtotal - Development Costs		7,512,028		12,985,890		37,391,917
<u>Developer Overhead</u>						
	4% above costs	300,481	4% above costs	519,436	4% above costs	1,495,677
Development Cost		\$ 7,812,509		\$ 13,505,326		\$ 38,887,593
Developer Profit	12% dev. cost	937,501	12% dev. cost	1,620,639	12% dev. cost	4,666,511
Total - Developer Cost and Profit		8,750,010		15,125,965		43,554,104
Cost per Unit		\$ 397,728		\$ 302,519		\$ 435,541

¹ Includes insurance and taxes during construction, legal, title, appraisal, soils testing, and environmental costs.

² Construction loan interest based on 7% interest rate and construction period shown in Table 2.10.

Sources: DataQuick Information Systems; *City of Long Beach Housing Trust Fund Study*, David Paul Rosen & Associates, 2003; Consumer Price Index for Los Angeles-Riverside-Orange County, CA, U.S. Bureau of Labor Statistics; Building Cost Index, *Engineering News-Record*; MuniFinancial.

Table D.9 shows the affordable sales prices for owner-occupied units at the moderate-income cutoff of 110 percent of AMI, based on the 2007 AMI. (Compare with Table 2.12.)

Table D.9: 2007 Income Standards and Affordable Owner-Occupied Housing Target Prices

Household Size	1 person/ 0 bedrooms (loft)	2 persons/ 1 bedroom	3 persons/ 2 bedrooms	4 persons/ 3 bedrooms
Affordable Income Target (Moderate Income - 110% AMI)	\$ 43,560	\$ 49,720	\$ 55,990	\$ 62,150
Affordable Annual Housing Costs (35% of Income)	15,246	17,402	19,597	21,753
Affordable Monthly Housing Costs	1,271	1,450	1,633	1,813
Property Taxes and Assessments ¹	\$ 133	\$ 152	\$ 169	\$ 185
Utilities	68	78	109	142
Maintenance/Insurance/HOA Dues	200	225	250	275
Affordable Mortgage Payment	\$ 870	\$ 995	\$ 1,105	\$ 1,211
Supportable Mortgage ²	\$ 137,600	\$ 157,457	\$ 174,871	\$ 191,571
Down Payment (5%)	7,242	8,287	9,204	10,083
Affordable Unit Price	\$ 144,842	\$ 165,744	\$ 184,075	\$ 201,654

¹ Based on 1.1% estimated property tax rate and assessed value equal to affordable mortgage plus 5% downpayment.

² Based on 6.5% interest rate and 30 year term.

Sources: California Department of Housing and Community Development; Los Angeles County Assessor; Keyser Marston Associates; MuniFinancial.

Table D.10 shows the revenue that would be generated by selling the prototype owner-occupied prototype developments at affordable prices. (Compare to Table 2.13.)

Table D.10: Revenue on Owner-Occupied Developments - 2007

	Affordable Sale		
	Number of Units	Price	Total Revenue
<i>Owner-Occupied Townhomes (Moderate Income)</i>			
Lofts	-	\$ 144,842	\$ -
1 Bedroom	-	165,744	-
2 Bedroom	13	184,075	2,392,977
3 Bedroom	9	201,654	1,814,883
Subtotal			\$ 4,207,860
<i>Stacked Flats Condos (Moderate Income)</i>			
Lofts	-	\$ 144,842	\$ -
1 Bedroom	7	165,744	1,160,209
2 Bedroom	33	184,075	6,074,480
3 Bedroom	10	201,654	2,016,537
Subtotal			\$ 9,251,225
<i>High-Rise Condos (Moderate Income)</i>			
Lofts	10	\$ 144,842	\$ 1,448,425
1 Bedroom	10	165,744	1,657,441
2 Bedroom	60	184,075	11,044,509
3 Bedroom	20	201,654	4,033,074
Subtotal			\$ 18,183,448

Sources: Tables 2.10 and D.9; MuniFinancial.

Table D.11 shows the affordability gap for the owner-occupied units based on 2007 income levels and the 2007 development cost estimates. (Compare with Table 2.14.)

Table D.11: Affordability Gap on Owner-Occupied Units - 2007

	Owner-Occupied Townhome Project	Stacked Flats Condo Project	High-Rise Condo Project
Development Costs	\$ 8,750,010	\$ 15,125,965	\$ 43,554,104
Total Affordable Sales Price	4,207,860	9,251,225	18,183,448
Affordability Gap	\$ 4,542,150	\$ 5,874,740	\$ 25,370,656
Number of Units	22	50	100
Affordability Gap per Unit	\$ 206,461	\$ 117,495	\$ 253,707

Sources: Tables 2.10, D.8 and D.10; MuniFinancial.

Table D.12 shows the cost per square foot equivalent to complying with the inclusionary zoning policy by providing the required affordable units on-site. (Compare with Table 2.15.)

Table D.12: Owner-Occupied Housing Inclusionary Zoning In-Lieu Costs - 2007

	Owner-Occupied Townhomes		Stacked Flats Condos		High-Rise Condos
Gap per Affordable Unit	\$	206,461	\$	117,495	\$ 253,707
Inclusionary Zoning Requirement		<u>10%</u>		<u>10%</u>	<u>10%</u>
In-Lieu Cost per Market Rate Unit	\$	20,646	\$	11,749	\$ 25,371
Average Square Feet per Unit		<u>1,182</u>		<u>1,118</u>	<u>1,100</u>
In-Lieu Cost per Square Foot	\$	17.47	\$	10.51	\$ 23.06

Sources: Table 2.1, 2.10 and D.11; MuniFinancial.

Table D.13 shows the in-lieu fee schedule that would have been proposed based on the 2007 development cost estimates. (Compare to Table 2.16.)

Table D.13: In-Lieu Fee Schedule

	\$/sq. ft.
Owner-Occupied Developments	\$ 10.51
Rental Developments	11.13

Sources: Tables D.7 and D.12.

RETURN ON COST ANALYSIS

Table D.14 shows the estimated revenue that the rental development prototypes would generate at market rental rates, as of mid-2007. (Compare with Table A.1.)

Table D.14: Revenue on Market-Rate Rental Developments - 2007

	Number of Units	Market Monthly Rent	Total Annual Revenue
<i>Rental Townhome Project</i>			
1 BR	4	\$ 1,400	\$ 67,200
2 BR/1 BA	3	1,900	68,400
2 BR/2 BA	11	2,100	277,200
3 BR	4	2,350	112,800
Subtotal			\$ 525,600
<i>Apartment Project</i>			
1 BR	7	\$ 1,350	\$ 113,400
2 BR/1 BA	8	1,550	148,800
2 BR/2 BA	25	1,850	555,000
3 BR	10	2,100	252,000
Subtotal			\$ 1,069,200

Sources: Table 2.2; RealFacts Long Beach Market Overview; Craigslist.org; MuniFinancial.

Table D.15 shows the estimated impacts of the proposed inclusionary zoning policy on return on cost, based on 2007 development costs and market rents. (Compare with Table A.2.)

Table D.15: Return on Cost, Rental Developments - 2007

	Rental	
	Townhome Project	Apartment Project
Operating Income-Market Rent	\$ 525,600	\$ 1,069,200
Operating Costs	<u>135,695</u>	<u>259,751</u>
Net Operating Income	\$ 389,905	\$ 809,449
Average Cap Rate	<u>5.5%</u>	<u>5.5%</u>
Project Market Value	\$ 7,089,185	\$ 14,717,253
Development Costs (Excluding Profit)	<u>6,601,692</u>	<u>11,055,282</u>
Developer Profit	\$ 487,493	\$ 3,661,971
Return on Cost, No In-Lieu Fee	7%	33%
In-Lieu Fee per Sq. Ft.	\$ 11.13	\$ 11.13
Return on Cost with In-Lieu Fee	3%	28%
Return on Cost Feasibility Threshold	12% to 16%	

Sources: Tables D.1, D.3, and D.14; Colliers International Greater Los Angeles Multifamily Market Report, Spring 2007; MuniFinancial.

Table D.16 shows the estimated revenue that the owner-occupied development prototypes would generate at market sales prices, as of mid-2007. (Compare with Table A.3.)

Table D.16: Revenue on Owner-Occupied Developments - 2007

	Number of Units	Market Sale Price	Total Revenue
<u>Owner-Occupied Townhomes</u>			
Loft	-	N/A	N/A
1 BR	-	N/A	N/A
2 BR	13	\$ 400,000	\$ 5,200,000
3 BR	9	440,000	<u>3,960,000</u>
Subtotal			\$ 9,160,000
<u>Stacked Flats Condos</u>			
Loft	-	N/A	N/A
1 BR	7	\$ 340,000	\$ 2,380,000
2 BR	33	400,000	13,200,000
3 BR	10	470,000	<u>4,700,000</u>
Subtotal			\$20,280,000
<u>High-Rise Condos</u>			
Loft	10	\$ 380,000	\$ 3,800,000
1 BR	10	380,000	3,800,000
2 BR	60	440,000	26,400,000
3 BR	20	590,000	<u>11,800,000</u>
Subtotal			\$45,800,000

Sources: Table 2.10; DataQuick Information Systems; MuniFinancial.

Table D.17 shows the estimated impacts of the proposed inclusionary zoning policy on return on cost, based on mid-2007 development costs and market sales prices. (Compare with Table A.4.)

Table D.17: Return on Cost, Owner-Occupied Developments - 2007

	Owner-Occupied Townhome	Stacked Flats Condos	High-Rise Condos
Sales Revenues	\$ 9,160,000	\$ 20,280,000	\$ 45,800,000
Development Costs (Excluding Profit)	7,812,509	13,505,326	38,887,593
Developer Profit	\$ 1,347,491	\$ 6,774,674	\$ 6,912,407
Return on Cost, No In-Lieu Fee	17%	50%	18%
In-Lieu Fee per Sq. Ft.	\$ 10.51	\$ 10.51	\$ 10.51
Return on Cost with In-Lieu Fee	13%	45%	14%
Return on Cost Feasibility Threshold	12% to 16%		

Sources: Tables D.8 and D.16; MuniFinancial.

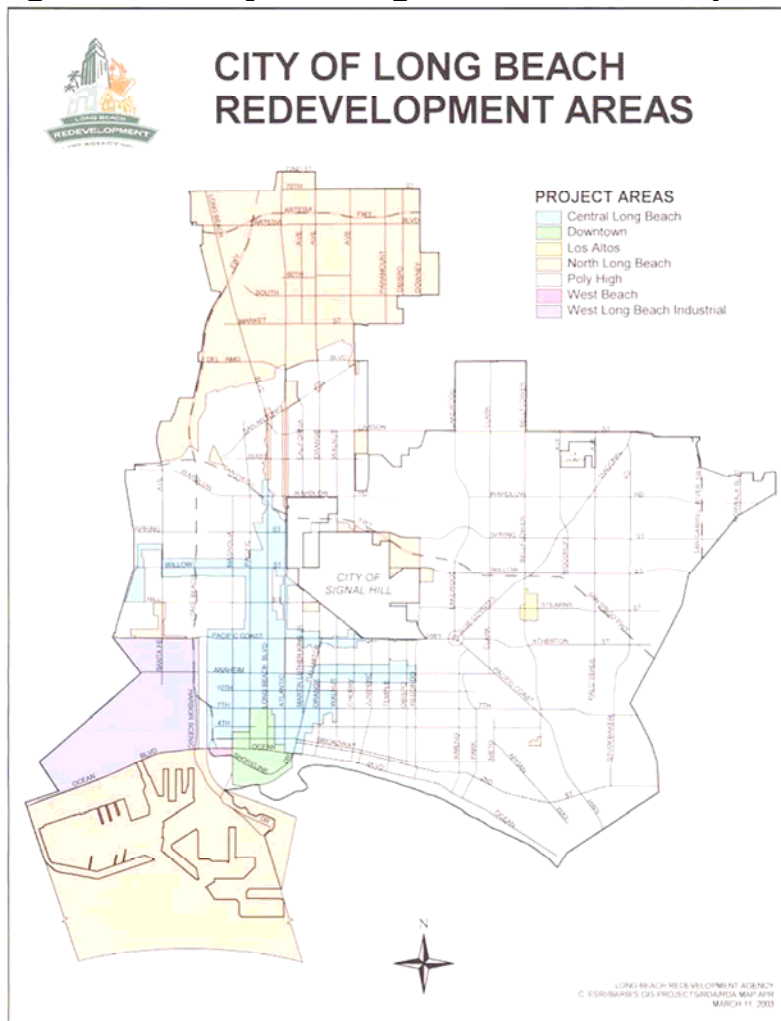
APPENDIX E. REDEVELOPMENT AGENCY SET-ASIDE

California Community Redevelopment Law requires redevelopment agencies to put at least 20 percent of tax increment revenue into a housing fund to be used for low- and moderate-income housing. This chapter evaluates the adequacy of the required Long Beach Redevelopment Agency “set-aside” for the attainment of affordable housing goals in Long Beach. The purpose of this evaluation is to determine if a higher set-aside is justified and/or feasible.

LONG BEACH REDEVELOPMENT AGENCY

The Long Beach Redevelopment Agency was formed in 1961. **Figure E.1** shows the seven redevelopment project areas in Long Beach.

Figure E.1: City of Long Beach Redevelopment Areas



The project areas encompass different land uses and redevelopment goals as summarized in the following project descriptions:

- ◆ Central Redevelopment Project - The Central Long Beach Redevelopment Plan was originally adopted in 1993, readopted in 2001, and terminates in 2032. The project area includes about 2,619 acres of urbanized land. The primary goal of the redevelopment effort is to concentrate commercial facilities in significant centers, in order to preserve existing neighborhoods.
- ◆ Downtown Redevelopment Project - The Downtown Redevelopment Plan was adopted in 1975 and terminates in 2017. The project area contains about 421 acres including commercial and residential uses.
- ◆ Los Altos Redevelopment Project - The Los Altos Redevelopment Plan was adopted in 1991 and terminates in 2032. It includes about 45 acres with two shopping centers and other commercial uses. There are no residential units within the project area.
- ◆ North Long Beach Redevelopment Project - The North Long Beach Redevelopment Plan was adopted in 1996 and terminates in 2027. The project area includes 10 non-contiguous land areas totaling about 7,540 acres of land and 4,967 acres of harbor waterfront. The primary goals of the North Long Beach Redevelopment Plan are to improve the commercial corridors through the North Long Beach area and halt negative impacts of deteriorating conditions on the surrounding residential areas.
- ◆ Poly High Redevelopment Project - The Poly High Redevelopment Plan was adopted on in 1973 and terminates in 2014. It includes about 87 acres. The primary goals of the Poly High Redevelopment Plan were to enlarge Polytechnic High School and to rehabilitate its surrounding residential neighborhood.
- ◆ West Beach Redevelopment Project - The West Beach Redevelopment Plan was adopted in 1964 and terminates in 2012. The project area covers about 21 acres in downtown and contains no residential units.
- ◆ West Long Beach Industrial Redevelopment Project - The West Long Beach Industrial Redevelopment Plan was adopted in 1975 and terminates in 2015. It contains about 1,368 acres north of Anaheim Street within the Long Beach Harbor District. The goals of the West Long Beach Industrial Redevelopment Plan are to expand industrial uses by removing non-conforming residential uses and improving public infrastructure.

The seven redevelopment project areas account for a significant portion of Long Beach, particularly in the Downtown, Central, and North Long Beach areas. The Downtown and Central areas account for much of the recent housing production in Long Beach.

AFFORDABLE HOUSING REQUIREMENTS UNDER REDEVELOPMENT

In addition to the 20 percent set-aside for affordable housing, the California Community Redevelopment Law contains inclusionary housing requirements. At least 30 percent of all new or rehabilitated dwelling units developed by the Redevelopment Agency must be

affordable to households in the very low-, low-, and moderate-income categories. Of those units, at least 50 percent must be affordable to households of very low-income.¹¹

For new housing developed or substantially rehabilitated within a project area by persons or entities other than the Redevelopment Agency, at least 15 percent must be affordable to households in the very low, low, or moderate-income categories. Of such units, at least 40 percent must be affordable to very low-income households.

Recent legislation has placed more stringent requirements on the use of the redevelopment set-aside than was the case in the past. Now, affordable housing developed with the set-aside is required to remain affordable to the targeted income group for at least 55 years for rentals and 45 years for ownership housing.

Under the Redevelopment Law it is the Redevelopment Agency's responsibility to provide inclusionary units. There is no requirement that the private-sector developers contribute to the provision of affordable housing units or that affordable housing units are provided within market-rate developments. If the affordable housing units are provided outside of the project area, twice as many units are required.

Under State law, redevelopment projects adopted prior to 1976 are not subject to the inclusionary housing requirement. In the City of Long Beach, this excludes the Downtown, Poly High, West Beach, and West Long Beach Industrial project areas, because they were adopted before 1976. Of the remaining project areas, Los Altos has non-residential development only and will therefore not produce any affordable housing. Therefore, the inclusionary housing requirement only applies to the Central and North project areas.

In 2002, State law was changed such that only those rehabilitated housing projects that are completed with agency assistance must meet the inclusionary housing requirements. The Redevelopment Agency has not assisted with the rehabilitation of housing units. Therefore the inclusionary housing requirements have not been invoked for any rehabilitation projects.¹²

In addition to the inclusionary housing requirements, agencies must replace affordable housing units removed from the housing stock as a result of redevelopment activities. This requirement is intended to prevent the net loss of affordable units within the project areas. Units are considered affordable if they are occupied, or would be expected to be occupied, by a household with an income of 120 percent of median income or less. The replacement units must be affordable to households in the same or a lower income category as those in the destroyed or removed housing units. In addition, replacement units must have at least the same number of bedrooms as the eliminated units.

ADEQUACY OF THE SET-ASIDE

The Redevelopment Agency has budgeted for the 20 percent set-aside in the budgets available through fiscal year 2010, which is the duration of the Agency's current budget outlook. The redevelopment set-aside is estimated to be about \$17.5 million for fiscal year 2008. That amount is estimated to increase to about \$18.5 million in 2010. City policy is that

¹¹ Section 33413 of the Health and Safety Code.

¹² Housing Program Compliance Plan, Redevelopment Agency of the City of Long Beach Five-Year Implementation Plan Period from October 1, 2004, through September 30, 2009.

the redevelopment set-aside will be divided equally between home ownership and rental programs. Three neighborhood focus areas are targeted to receive 65 percent of the resources for the five-year period covered in the Housing Action Plan. Two of the areas are in the Central Redevelopment Project Area and the third is in the North Redevelopment Project Area.

Table E.1 shows the Redevelopment Agency's revenues and expenditures as budgeted for fiscal years 2008 through 2010.

Table E.1: Redevelopment Agency Budgeted Revenue Sources, FY 2008-2010

	2008	2009	2010
Beginning Fund Balance	54,627,315	24,402,159	20,787,915
Revenue Source			
Gross Tax Increment	87,367,000	89,856,000	92,339,000
Housing Set Aside	(17,486,000)	(17,985,000)	(18,488,200)
Tax Increment Sharing and County Charges	(13,945,000)	(14,605,000)	(15,276,000)
Net Tax Increment	55,936,000	57,266,000	58,574,800
Program Revenues	13,351,820	23,314,660	6,667,474
Restricted Revenues	705,000	195,000	0
Total Revenues	69,992,820	80,775,660	65,242,274
Expenditures and Commitments			
Financing Costs	25,762,844	25,811,837	25,862,021
Neighborhood Revitalization	17,870,250	12,975,250	12,760,250
Corridor Revitalization	15,742,000	7,377,000	5,127,000
Open Space/Public Art	4,118,000	5,538,000	5,653,000
Infrastructure/Public Improvements	29,010,000	23,635,000	10,235,000
Housing	0	1,500,000	1,000,000
Administration	7,714,882	7,552,817	7,645,604
Total Expenses	100,217,976	84,389,904	68,282,875
Ending Fund Balance	24,402,159	20,787,915	17,747,314
Less Voluntary Reserves ¹	23,804,015	23,810,478	23,819,980
Amount Above (Below) Voluntary Reserves	598,144	(3,022,563)	(6,072,666)

¹ It is Redevelopment Agency policy to reserve revenues in an amount equal to one year's debt service.

Source: Long Beach Redevelopment Agency.

In addition to the set-aside requirement, the Redevelopment Agency is also required to share tax increment revenue with the County of Los Angeles and other public agencies. Redevelopment areas established in 1994 or later are required to pass-through 20 percent of the gross tax increment. Prior to 1994, pass-through rates varied. For all of the project areas together, the Redevelopment Agency budgets for pass-throughs equal to about 16 percent of total annual tax increment revenues.

The Redevelopment Agency also anticipates spending an amount equal to about 30 percent of tax increment revenues for debt payments and other financing costs. Together, the affordable housing set-aside, increment sharing, and debt service are equal to about 66

percent of tax increment revenues through fiscal year 2010, leaving about 34 percent of tax increment revenue, an amount equal to about \$30 million annually, for other uses.

As shown in Table E.1, the Redevelopment Agency also budgets for:

- ◆ Neighborhood Revitalization, which provides for neighborhood enhancements and blight removal, including residential facade improvements;
- ◆ Corridor Revitalization, which provides for blight removal in commercial corridors or major thoroughfares;
- ◆ Open Space/Public Art, which provides for park development in historically underserved areas and provides arts programming in conjunction with the one percent for art requirements;
- ◆ Infrastructure/Public Improvements, which provides for public facilities expansion, replacement, and improvements;
- ◆ Housing, which provides for property acquisition, site assembly, and other development costs for affordable housing projects that the Agency and Long Beach Housing Development Company work on together; and
- ◆ Administration, which provides for the management and administration of the Redevelopment Agency.

The Redevelopment Agency has not prepared comprehensive budgeting information for years after 2010 and was unable to provide descriptions of planned capital improvement projects for fiscal years 2008-2010, making it difficult to evaluate if the Redevelopment Agency could designate a larger portion of tax increment revenue for affordable housing in those years or beyond. Given the demands on the Agency's finances and its mission to remove blight, it is likely expenditures will continue in the same proportion as budgeted for in fiscal years 2008-2010. To evaluate whether or not the Agency could increase its contributions to affordable housing programs would necessitate the review of capital improvement project lists and the economic impacts of forgoing enhancement projects within the project areas.

OPTIONS FOR AFFORDABLE HOUSING REVENUE

To increase available revenue for affordable housing in the Redevelopment areas there are at least three options:

- ◆ Increase the affordable housing set-aside from its current rate of 20 percent of gross tax increment, which will divert tax increment revenue from other redevelopment projects;
- ◆ Impose inclusionary zoning and affordable housing fee requirements on residential and non-residential developments City-wide, which would require developers to participate in the provision of affordable housing within the redevelopment project areas, unless they are Agency-assisted projects; and
- ◆ Do a combination of both.

At this time we recommend that the City impose the inclusionary zoning and affordable housing fee requirements City-wide, including in the seven redevelopment project areas

already in place and in any future project areas, unless development projects are completed with the assistance of the Redevelopment Agency. Much of the recent development in Long Beach has occurred within redevelopment areas. It is reasonable to assume that a significant portion of future development will also occur in the project areas. If the City chooses to not impose the inclusionary zoning and affordable housing fees in the redevelopment project areas, it will forego a significant portion of available fee revenue.