



KEYSER MARSTON ASSOCIATES  
ADVISORS IN PUBLIC/PRIVATE REAL ESTATE DEVELOPMENT

## MEMORANDUM

ADVISORS IN:  
Real Estate  
Affordable Housing  
Economic Development

**To:** Kirk Pelser, Deputy City Manager  
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**Date:** September 9, 2020

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**Subject:** Inclusionary Housing: Policy Recommendations

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Keyser Marston Associates, Inc. (KMA) was engaged by the City of Pomona (City) to assist in creating an Inclusionary Housing program. As the first step in this process, KMA prepared the accompanying *Inclusionary Housing: Financial Evaluation* (Financial Evaluation). Based on the results of the Financial Evaluation, KMA created Inclusionary Housing policy recommendations, which are presented in the following memorandum.

This memorandum is organized as follows:

1. The findings of the Financial Evaluation are summarized.
2. The components of the recommended policies are identified.
3. The recommended implementation package is described.
4. Case studies are presented to compare the Inclusionary Housing options that could potentially be applied to hypothetical projects.

## FINANCIAL EVALUATION FINDINGS

Based on the results of the Financial Evaluation, KMA reached the following key findings:

1. The on-site Inclusionary Housing requirements identified in the Financial Evaluation are:
  - a. Ownership housing projects:
    - i. A 7% moderate income requirement for single family home projects; and
    - ii. A 10% moderate income requirement for townhome and condominium projects.
  - b. An 8.2% moderate income requirement is supported for apartment projects.
2. The in-lieu fee amounts identified in the Financial Evaluation are:

Maximum Financially Feasible In-Lieu Fees		
	Per Inclusionary Unit	Per Sq. Ft. of Saleable / Leasable Area
Single Family Homes	\$320,000	\$11.40
Townhomes / Condominiums	\$132,000	\$9.30
Apartments	\$99,000	\$9.20

## POLICY RECOMMENDATIONS

The Inclusionary Housing policy recommendations cover the following topics:

1. The minimum residential project size that will trigger an Inclusionary Housing obligation.
2. The income and affordability requirements that will be applied to ownership housing projects and apartment projects.

3. The covenant periods under which the income and affordability standards should be imposed for ownership housing projects and apartment projects.
4. Fulfillment options need to be provided that are tailored to the type of housing being developed in order to mitigate the financial impacts created by the imposition of Inclusionary Housing requirements. The following options are proposed to be offered under specified circumstances:
  - a. On-site production;
  - b. Off-site production;
  - c. In-Lieu Fee Payment;
  - d. Land Dedication; and
  - e. Acquisition and rehabilitation of existing apartment units.
5. Implementation activities that should be undertaken by the City are identified.

### THRESHOLD PROJECT SIZE

The majority of Inclusionary Housing programs in California include a threshold project size below which projects are not subject to the affordable housing production requirements. Common thresholds fall between three and 10 units. Following guidance from the City Council and the Planning Commission, the threshold project size will be set at three units.

### INCOME AND AFFORDABILITY STANDARDS

An Inclusionary Housing program's income and affordability standards should be set at levels that do not constrain the opportunities for residential development. The Financial Evaluation provides context for the on-site production requirements that can be imposed within that standard. However, the results of the Financial Evaluation are only meant to serve as a tool to assist the City in establishing the Inclusionary Housing requirements that will be imposed.

City Council members have expressed a goal to set some of the Inclusionary Housing requirements at higher percentages than were identified in the Financial Evaluation. To that end, KMA explored opportunities for increasing the requirements to some extent without creating a constraint to development. The results are described in the following sections of this memorandum.

## **Ownership Housing**

### **Affordable Sales Price Calculation Methodology**

KMA recommends that the City apply the California Health and Safety Code (H&SC) Section 50052.5 methodology to the calculation of Affordable Sales Prices. In addition, the following specific calculation metrics are being recommended by KMA.

### **Benchmark Mortgage Interest Rate**

The assumption used in setting the benchmark mortgage interest rate that is applied in the calculations creates a significant impact on the Affordable Sales Price. In establishing a benchmark interest rate it is important to understand the following issues that are commonly faced by moderate income first time home buyers:

1. Credit history and scores that do not fall within the exceptional level required to obtain the lowest interest rate available in the marketplace;
2. Back-end ratios that are often higher than the typical ratios applied in conventional lenders' underwriting standards for the lowest interest rate mortgages; and
3. There is a limited pool of mortgage lenders that are willing to provide loans on homes that are subject to income and affordability covenants. These lenders do not generally offer the lowest interest rates available in the marketplace.

Given that mortgage interest rates can be expected to fluctuate over time, KMA recommends that the City apply the following conservative methodology in setting the benchmark interest rate used in the Affordable Sales Price calculations:

1. KMA recommends that the benchmark mortgage interest rate be set on the first day of each calendar quarter.

2. In setting the benchmark interest rate, KMA typically uses the Bankrate sitewide average annual percentage rate (APR) for 30-year fixed interest rate mortgages. Other sources that provide the same type of information are also acceptable.

### **Range of Allowable Home Buyer Down Payments**

An Inclusionary Housing program is intended to target home buyers that could otherwise not afford to purchase a home in Pomona. To achieve that goal while minimizing the risk of defaults, KMA recommends that the following down payment requirements be imposed:

1. The minimum home buyer down payment amount should be set at 5% of the Affordable Sales Price.
  - a. At least 1% of this down payment amount must be provided from the home buyer's own funds.
  - b. Gifts funds may be obtained by the home buyer to fulfill the balance of the 5% requirement.
2. The maximum down payment amount should be set at 35% of the Affordable Sales Price:
  - a. Gift funds of up to \$75,000 may be used for the down payment amount that falls between 1% and 35% of the Affordable Sales Price.
  - b. Mortgage Assistance Program (MAP) funds may be used by low income households. These funds will not be counted against the 35% down payment cap.

### **Income and Affordability Standards**

The results of the KMA Financial Evaluation indicate that a low income home ownership requirement cannot be imposed without creating a financial impact that deprives a property owner or developer of a fair and reasonable return on their investment. As such, KMA recommends that the City designate moderate income units as the affordable housing type for ownership housing projects.

Based on the results of the Financial Evaluation KMA recommended that the City impose the following Inclusionary Housing requirements on ownership housing development:

Single Family Homes	7%
Townhomes and Condominiums	10%

It is our understanding that the City Council would like to increase the Inclusionary Housing obligation for townhomes and condominiums above the 10% requirement that was supported by the Financial Evaluation. It is KMA's opinion that there is a +/- 10% buffer in the results of the Financial Evaluation. If that buffer is applied, the Inclusionary Housing obligation for townhome units could potentially be increased to 11%.

#### Low Income Option

The City would also like to provide opportunities for low income households to purchase Inclusionary Units. To achieve this goal KMA recommends that the City to allow low income households to purchase Inclusionary Units at the designated Affordable Sales Prices for moderate income units. This can be allowed on a financially feasible basis for the following reasons:

1. In 2020, the top end of the low income category equates to 117% of the area median income (AMI). Households with incomes that fall within the upper range of the low income category will likely be able to afford a home at the designated Affordable Sales Price.
2. The City currently offers the MAP Program that is funded with HOME Program funds provided by the United States Department of Housing and Urban Development (HUD):
  - a. The City allocated \$1.09 million to the program In fiscal year 2020/21.
  - b. At the \$100,000 per unit cap that is applied by the program, the City could assist 10 low income home buyers with down payment and/or closing costs.

## Apartments

### Affordable Rent Calculation Methodology

KMA recommends that the City apply the California Health and Safety Code (H&SC) Section 50053 methodology to the calculation of Affordable Rents.

### Income and Affordability Standards

Based on the results of the Financial Evaluation KMA recommended that the City apply the following Inclusionary Housing requirements on apartment development:

Income Category	Moderate Income
Inclusionary Housing Requirement	8.2%

The City Council has indicated a desire to apply an Inclusionary Housing obligation that exceeds the 8.2% requirement identified in the Financial Evaluation. To justify an increase, the City look to the benefits created by the use of the density bonus provided by California Government Code Sections 65915-65918 (Section 65915) density bonus.

Developers commonly use the Section 65915 density bonus to mitigate the impacts created by the imposition of Inclusionary Housing requirements. For example, the density bonus projects analyzed in the Financial Evaluation supported an Inclusionary Housing requirement in the range of 10.6% to 12.7% of the total number of units developed in an apartment project.

It is KMA's recommendation that the City set the requirement at the lower end of the range. For the purposes of this analysis KMA assumed that the City Council would set the Inclusionary Housing requirement at 11%.

### Use of Apartment Units to Fulfill Inclusionary Housing Obligations

It is KMA's recommendation that apartment units be allowed to fulfill the Inclusionary Housing requirements under the following circumstances:

1. The on-site fulfillment of the Inclusionary Housing obligation that is imposed on a market rate apartment project;

2. The creation of a parcel within an ownership housing development site in which affordable apartment units are produced to fulfill the ownership housing project's Inclusionary Housing requirements; and
3. The off-site production of apartment units to fulfill the Inclusionary Housing obligation associated with both market rate ownership housing projects and apartment projects.

The recommended income and affordability standards for the three options are presented in the following table:

Recommended Income and Affordability Standards Apartment Units Used to Fulfill Inclusionary Housing Requirements <sup>1</sup>		
	% of Total Units	Income Category
On-site production within a market rate apartment project	11%	Moderate
On-site production to fulfill the requirements imposed on a market rate home ownership project	15%	Low
Off-site production to fulfill the requirement for an ownership housing or an apartment project	15%	Low

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<sup>1</sup> At a developer's sole discretion, very low or low income units should be allowed to fulfill the City's Inclusionary Housing obligations.

## COVENANT PERIODS

### Ownership Housing

KMA recommends that the covenant period for affordable ownership housing units be set at one cumulative 45-year period. Within that one 45-year period the home must be sold and resold to moderate income households at the then current Affordable Sales Price.

### Apartments

KMA recommends that the covenants for the Inclusionary Housing apartment units should remain in place for as long as the property is developed with a residential use, but for not less than 55 years. Following the 55-year term, the covenant should only be removed if at some point the property is rezoned and subsequently put to a non-residential use.

## INCLUSIONARY HOUSING FULFILLMENT OPTIONS

### On-Site Production of Inclusionary Units

By right, developers should be allowed to fulfill a project's Inclusionary Housing obligations on site within a proposed market rate project. The recommended options for fulfilling the Inclusionary Housing requirements on site are described in the following sections of this memorandum.

### Ownership Housing Projects

#### **Development of Affordable Ownership Housing Units**

The following standards should be imposed on affordable ownership units that are built within a market rate ownership housing project:

1. The income and affordability standard is set at the moderate income level. The recommended Inclusionary Housing obligations are set as follows:
  - a. In single family home projects the Inclusionary Housing obligation is set at 7% of the units in the project.

- b. In townhome and condominium projects the Inclusionary Housing obligation is set at 11% of the units in the project.
- 2. The Inclusionary Units must be required to be dispersed throughout the project.
- 3. The affordable housing units must be built concurrently with the market rate project. The Inclusionary Units can be constructed in phases if the market rate project is being developed in phases.
- 4. The affordable housing units must comply with the following development scope requirements:
  - a. The bedroom mix for the Inclusionary Units must be proportional to the bedroom mix of the market rate units. However, the Inclusionary Units may be smaller in square footage than the market rate units.
  - b. The exterior improvements for the Inclusionary Units must be comparable to the exterior improvements for the market rate units.
  - c. The interior improvements for the Inclusionary Units must meet the following standards:
    - i. The interior finished must be comparable to the base level interior finishes provided in the market rate units; and
    - ii. The appliance packages must be the same as the packages provided in the base level market rate units.

#### **Development of Affordable Apartments within an Ownership Housing Project**

If the developer of an ownership housing project wishes to fulfill the project's Inclusionary Housing requirements with apartment units, KMA recommends that the following requirements be applied:

- 1. The developer should be allowed to create a separate affordable housing parcel within their development site to fulfill the project's Inclusionary Housing obligations.

2. If the following criteria are met, the developer of the market rate project can enter into an agreement with an affordable housing developer to construct, own and operate the affordable housing units:
  - a. The affordable housing developer must have relevant recent experience, and must be approved by the City.
  - b. The affordable housing developer may not request any financial assistance from the City.
3. The Inclusionary Housing obligation should be required to be fulfilled with apartment units that meet the following criteria:
  - a. The set aside should be set at 15% multiplied times the total number of ownership housing and apartment units being developed on the site.
  - b. The income standard should be set at the low income level. However, at the developer's sole discretion the requirement should be allowed to be fulfilled with very low income units.
4. The bedroom mix should not be required to match the unit mix provided in the market rate ownership housing project. However, the following requirements should be applied:
  - a. The percentage of studio units should be capped at 15%;
  - b. At least 40% of the units must include two or more bedrooms; and
  - c. The remaining units must include one or more bedrooms.

#### Apartment Projects

KMA recommends that the following standards be applied to the on-site production of Inclusionary Units within market rate apartment projects:

1. An 11% moderate income requirement should be imposed on market rate apartment projects that choose to fulfill the Inclusionary Housing obligations on site.

2. The affordable housing units should be required to be constructed concurrently with the market rate project, and they must be dispersed throughout the project.
3. The affordable housing units should be required to comply with the following development scope requirements:
  - a. The bedroom mix for the Inclusionary Units must be proportional to the bedroom mix of the market rate units. However, the Inclusionary Units may be smaller in square footage than the market rate units.
  - b. The interior improvements of the Inclusionary Units must comport with defined quality standards such as those applied by the Low Income Housing Tax Credit (Tax Credit) program. The market rate units in the project can include enhanced interior improvements.

### Off-Site Production of Inclusionary Units

For both ownership housing projects and apartment projects, KMA recommends that the Inclusionary Housing program allow a developer to fulfill the Inclusionary Housing obligations in an off-site location under the following conditions:

1. Irrespective of the market rate project's tenure, the Inclusionary Housing obligation must be fulfilled with apartment units.
2. The development parcel must be located within one mile of the market rate project that is subject to the Inclusionary Housing obligations.
3. The development must not create an over concentration of deed restricted affordable housing units in any specific neighborhood.<sup>2</sup>
4. The following income and affordability standards will be applied:
  - a. The inclusionary Housing allocation is set at 15% of the units being developed in the market rate project.

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<sup>2</sup> Over concentration is defined as more than 50 covenanted very low or low income units within ¼ mile, or more than 200 such units within ½ mile of the of the proposed affordable housing site.

- b. The income standard is set at the low income level. However, at the developer's sole discretion the requirement should be allowed to be fulfilled with very low income units.
- 5. Design, building quality and maintenance standards should be based on a defined standard such as the requirements imposed by the Tax Credit program.
- 6. The bedroom mix is not be required to match the unit mix provided in the market rate ownership housing or apartment project. However, the following standards should be imposed:
  - a. The percentage of studio units is capped at 15%;
  - b. At least 40% of the units must include two or more bedrooms; and
  - c. The remaining units must include one or more bedrooms.
- 7. Under the following circumstances the developer of the market rate project should be allowed to enter into an agreement with an affordable housing developer to construct, own and operate the affordable housing project:
  - a. The affordable housing developer must have recent relevant experience, and be approved by the City.
  - b. The affordable housing developer may not request any financial assistance from the City.
  - c. The developer may apply to use the California Government Code Section 65915 density bonus and the statutorily established number of incentives or concessions.
- 8. The affordable housing project must be constructed prior to or concurrently with the market rate project that triggered the Inclusionary Housing obligation. If the market rate project is proposed to be developed in phases, the affordable housing units should be required to be developed along with the first phase of the market rate project.

## In-Lieu Fee Payment Option

### In-Lieu Fee Payment Thresholds

Based on City Council and Planning Commission guidance, the City will establish objective criteria under which in-lieu fee payments are allowed. To assist the City in making these determinations, KMA offers the following recommendations:

1. An in-lieu fee payment option should be allowed for any fractional Inclusionary Unit requirement.
2. Ownership housing developments of any size should be provided with the option to pay an in-lieu fee.
3. The following options should be offered to proposed apartment projects:
  - a. Inclusionary Housing requirements have a disproportionate impact on smaller projects, because there are fewer market rate units available to spread the impact created by the income and affordability standards. KMA recommends that an in-lieu fee payment be allowed by right for apartment projects with 30 or fewer units.
  - b. As a baseline, apartment projects with more than 30 units should be required to produce the requisite number of Inclusionary Units. However, the City Council should be provided with the discretion to allow an in-lieu fee to be paid for apartment projects with more than 30 units if they are deemed to exhibit extreme hardship circumstances.

### In-Lieu Fee Schedules

It is KMA's opinion that an in-lieu fee measured against the square footages of the units corresponds more closely to the Affordability Gap than an in-lieu fee that is measured by the number of units. As such, KMA recommends that the in-lieu fee be based on the saleable area for ownership housing projects and the leasable area for apartment projects.

KMA recommends that the following in-lieu payment schedules be applied, in 2020 dollars, the first year following the adoption of the Inclusionary Housing Ordinance:

Recommended In-Lieu Fee Schedules				
Per Square Foot of Saleable Area or Leasable Area				
Units	Single Family Homes	Townhomes		Apartments
3	\$.41	\$.33		\$.33
4	\$.81	\$.66		\$.66
5	\$1.22	\$1.00		\$.99
6	\$1.63	\$1.33		\$1.31
7	\$2.04	\$1.66		\$1.64
8	\$2.44	\$1.99		\$1.97
9	\$2.85	\$2.33		\$2.30
10	\$3.26	\$2.66		\$2.63
11	\$3.66	\$2.99		\$2.96
12	\$4.07	\$3.32		\$3.29
13	\$4.48	\$3.65		\$3.61
14	\$4.89	\$3.99		\$3.94
15	\$5.29	\$4.32		\$4.27
16	\$5.70	\$4.65		\$4.60
17	\$6.11	\$4.98		\$4.93
18	\$6.51	\$5.31		\$5.26
19	\$6.92	\$5.65		\$5.59
20	\$7.33	\$5.98		\$5.91
21	\$7.74	\$6.31		\$6.24
22	\$8.14	\$6.64		\$6.57
23	\$8.55	\$6.98		\$6.90
24	\$8.96	\$7.31		\$7.23
25	\$9.36	\$7.64		\$7.56
26	\$9.77	\$7.97		\$7.89
27	\$10.18	\$8.30		\$8.21
28	\$10.59	\$8.64		\$8.54
29	\$10.99	\$8.97		\$8.87
30+	\$11.40	\$9.30		\$9.20

### In-Lieu Payment Timing

Developers should be required to pay the in-lieu fee when building permits are obtained for the project. However, for phased projects, the developer should be allowed to pay a pro rata share of the in-lieu fee concurrently with the issuance of building permits for each development phase.

### Land Dedications

The City Council should have the discretion, but not the requirement, to approve a developer's proposal to dedicate property in lieu of producing Inclusionary Units. KMA recommends that the following threshold requirements be imposed for any property put forth for City Council consideration:

1. The developer must be willing to convey the property to the City at no cost.
2. The developer must provide evidence of the following when the land dedication proposal is submitted:
  - a. The developer must have site control with lien-free title. Any encumbrances or easements that adversely impact the property's title must be disclosed and factored into the estimated value of the interests proposed to be conveyed to the City.
  - b. The property cannot contain any hazardous materials at the time the land dedication proposal is submitted:
    - i. The developer must disclose whether any hazardous materials were previously contained on the site; and
    - ii. If hazardous materials were previously remediated, the developer must provide evidence that the cleanup was performed in accordance with applicable law.
  - c. The property cannot have been improved with any residential use for at least five years prior to the submission of a land dedication proposal.

- d. Payment in full of all property taxes and special taxes must have been made when the proposal is submitted, and again prior to conveyance of the property to the City.
- 3. The Inclusionary Housing obligation should be set at 15% of the of the total units being developed in the market rate project. The income and affordability standard should be set at the very low income level.
- 4. The property must embody the following characteristics:
  - a. The property must be located within one-mile of the project that is subject to the Inclusionary Housing obligation.
  - b. The construction of Inclusionary Units on the property must not create an over concentration of very low income housing in any specific neighborhood.
  - c. The land dedication site must meet the following conditions:
    - i. The site's existing General Plan and zoning standards must allow for a residential use at a density sufficient to allow for the requisite number of Inclusionary Units to be developed.
    - ii. The site must be suitable in terms of size, configuration, and physical characteristics to allow for the requisite number of Inclusionary Units to be developed on a cost efficient basis.
  - d. The property must be fully served by the necessary infrastructure prior to conveyance to the City.
- 5. KMA recommends that the City only re-convey dedicated properties to developers with experience developing affordable apartment projects targeted to very low income households. To assist the City in evaluating land dedication proposals, the developer should be required to submit the following documents:
  - a. A conceptual site plan and narrative description of a project that could be developed on the property.

- b. A identification of the income and affordability restrictions proposed to be imposed.
- c. A pro forma analysis that quantifies any financial gap associated with the identified development scope, and describes how this financial gap will be filled.
- d. If a Section 65915 density bonus will be required, the terms of the requested density bonus; incentives and concessions; and development standards waivers must be identified.

Prior to submitting a proposal to the City Council for consideration, the City staff should independently evaluate the information submitted by the developer. Based on that review, the City should determine whether the proposal meets the defined threshold standards.

### Acquisition and Rehabilitation Projects

A primary purpose in establishing an Inclusionary Housing program is to assist the City in meeting its Regional Housing Needs Assessment (RHNA) targets. Under the requirements imposed by California Government Code Section 65583.1 (Section 65583.1) up to 25% of the City's RHNA obligation can be fulfilled with acquisition and rehabilitation units under the following circumstances:

- 1. The project(s) must be identified in the City's Housing Element;
- 2. An identified amount of financial assistance must be committed to the project;
- 3. Statutorily established relocation assistance must be provided to existing residents; and
- 4. The units must be provided to very low or low income households, at the Affordable Rent, over a 55-year covenant period.

Section 65583.1 also requires the project(s) to meet one of the following requirements:

- 1. The units are in imminent risk of loss to housing stock and the units having been found by the City or a court to be unfit for human habitation due to the existence of at least four violations of H&SC Section 17995.3 (a) – (g); or

2. The units are located in a market rate project that is being foreclosed upon, and upon acquisition the units will be converted to very low and low income units; or
3. The units are located in a project that is subject to existing income and affordability covenants that are due to expire during the eight-year Housing Element period. For this option, the following additional criteria must be met to qualify for RHNA credit:
  - a. The project must currently be defined as an “assisted housing development”;
  - b. The units must be in decent, safe and sanitary condition at the time of occupancy.
  - c. At the time the units are identified for preservation they must be available for very low or low income households.

For projects that meet these requirements, the City Council should have the discretion, but not the requirement, to approve a developer’s proposal to fulfill the Inclusionary Housing requirements for a market rate project with acquisition and rehabilitation units. The additional threshold requirements that should be imposed on acquisition and rehabilitation projects are:

1. The Inclusionary Housing requirement should be set at 20% of the units in the project that triggered the Inclusionary Housing obligation.
2. The affordability standard should be set at the very low income level.
3. The rents charged for the Inclusionary Units must be set at the lesser of the H&SC 50053 rents or an at least 10% discount from the achievable market rents for the rehabilitated units.
4. If there are more units in the acquisition and rehabilitation project than are required to fulfill the Inclusionary Housing requirement, those units may be rented at unrestricted market rate rents.

## IMPLEMENTATION RECOMMENDATIONS

As part of the implementation process for the Inclusionary Housing program KMA recommends that the City take the following actions:

### MARKETING REQUIREMENTS

The City wishes to focus the marketing effort in a manner that focuses on households that live and/or work in Pomona. To that end, the Inclusionary Housing regulations will require developers to prominently advertise the Inclusionary Units in local newspapers. In addition, information pertaining to Inclusionary Units that are being developed and marketed will be placed on the City's website.

### SECTION 65915 DENSITY BONUS

The City's Section 65915 density bonus ordinance does not currently include all of the amendments the State Legislature made between 2006 and 2020. Given that the Section 65915 density bonus is intended to reduce the financial impact created by the imposition of Inclusionary Housing requirements, KMA recommends that the City update Pomona Municipal Code Part III Section 520 to reflect the agreed upon requirements.

### AFFORDABLE HOUSING REGULATIONS

The following Inclusionary Housing Ordinance regulations documents should be created:

1. Affordable Ownership Housing Regulations: Developer Requirements;
2. Affordable Ownership Housing Regulations: Owner Requirements; and
3. Affordable Apartment Regulations.

### INCLUSIONARY HOUSING PROGRAM UPDATES

The Inclusionary Housing program should be updated at regular intervals:

1. The entire program should be re-evaluated at least every five years. Based on City Council guidance the first program re-evaluation will take place three years following the adoption of an Inclusionary Housing Ordinance.
2. To allow in-lieu fees to keep pace with changes in the market place during the intervening periods, the in-lieu fees should continue to be adjusted each year based on the percentage change in new home prices in Los Angeles County as published annually by the Real Estate Research Council (RERC).

## STAFFING PLAN

A staffing plan should be created for managing the development process and the ongoing monitoring of the Inclusionary Units once they are built.

## CASE STUDIES

### BACKGROUND

The following sections of this memorandum describe case studies for a hypothetical ownership housing project and a hypothetical apartment project. Both hypothetical projects include 100 units, but they are assumed to be developed at different densities and with different unit mixes.

The case studies identify each of the recommended options for fulfilling the Inclusionary Housing requirements. It is important to note that these case studies are based on the policy recommendations provided in this memorandum. If the City ultimately chooses to apply different requirements, these case studies will need to be modified accordingly.

### Fulfillment Options that Vary Between Ownership Housing and Apartments

The following Inclusionary Housing fulfillment options vary between ownership housing and apartment projects:

1. Production of the Inclusionary Units on site within the market rate project; and
2. A fee payment in lieu of producing affordable housing units.

The ownership housing and apartment project case studies are organized as follows:

1. The development scope assumptions are described.
2. The requirements associated with providing the Inclusionary Housing within the market rate projects are detailed.
3. An in-lieu fee payment estimate is provided for the hypothetical development.

### Standardized Fulfillment Options

The other three fulfillment options for Inclusionary Housing requirements carry the same responsibilities irrespective of the market rate project's tenure. The options are:

1. Production of the Inclusionary Units in an off-site location;
2. Dedication of land to the City in lieu of producing affordable housing units; and
3. Acquisition and rehabilitation of existing units.

The descriptions of these three other fulfillment options include the following information:

1. The development scope assumptions that guide the Inclusionary Housing requirements;
2. The affordability requirements associated with each option; and
3. The unit mix standards applied to each option.

### OWNERSHIP HOUSING PROJECT:

#### ON-SITE PRODUCTION AND IN-LIEU FEE OPTIONS

#### Development Scope Assumptions – Ownership Housing Project

The development scope used in the hypothetical ownership housing project are:

1. The project consists of 100 townhome units.

2. The development site consists of four acres, which equates to a density of 25 units per acre.
3. The project is developed in five phases.
4. The unit mix is detailed in the following table:

Unit Mix Hypothetical Ownership Housing Project		
Number of Bedrooms	Number of Units	Saleable Square Feet Per Unit
2	15	1,000
2	25	1,400
3	20	1,500
3	40	1,700
Total	100	148,000

### On-Site Production Options – Ownership Housing Project

As discussed previously in this memorandum, KMA recommends that developers be provided with two alternative methods for fulfilling the Inclusionary Housing requirements on site within a market rate project. Both of these options can be selected by developers by right, and they can be described as follows:

#### On-Site Production of Affordable Ownership Units

In this alternative, the Inclusionary Housing obligation is fulfilled with ownership housing units that are interspersed throughout the market rate project.

1. The Inclusionary Housing requirement is set at 11% of the total number of units to be constructed on the site. This equates to 11 units out of the 100 units included in the hypothetical townhome project.
2. The income and affordability restrictions are set at the moderate income level.

3. The 100 unit hypothetical townhome project consists of 40% two-bedroom units and 60% three-bedroom units. The Inclusionary Units are allocated on a pro rata basis to the smaller of the unit types in each bedroom category. For the hypothetical townhome project, the Inclusionary Units are distributed as follows:
  - a. Four two-bedroom units with 1,000 square feet of saleable area per unit; and
  - b. Seven three-bedroom units with 1,500 square feet of saleable area per unit.
4. The project is assumed to be developed in five phases. Assuming the 100 units are divided equally across the five phases, three Inclusionary Units must be constructed in the first phase, and two Inclusionary Units must be constructed in each subsequent phase.

#### On-Site Production of Affordable Apartment Units

In this alternative the developer will create a separate parcel to accommodate the required Inclusionary Units. To exercise this option, the developer must agree to fulfill the Inclusionary Housing requirement with affordable apartment units.

1. The Inclusionary Housing requirement is set at 15% of the total number of units to be constructed on the site. This equates to 15 affordable apartment units and 85 market rate home ownership units in the 100 unit hypothetical townhome project.
2. The income and affordability restrictions are set at the low income level.
3. The Inclusionary Units, which are developed on the separate parcel, are not required to match the unit mix provided in the market rate project. Instead, the following requirements are applied to the 15 unit Inclusionary Housing requirement in this hypothetical case study:
  - a. A maximum of two units (15%) can be studio units;<sup>3</sup>

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<sup>3</sup> The actual cap is 2.25 units. This was mathematically rounded down to two units.

- b. At least six units (40%) must include two or more bedrooms; and
  - c. The other seven units must include one or more bedrooms.
4. All 15 affordable apartment units must be constructed prior to or concurrently with the construction of the first phase of the market rate ownership housing project.

### In-Lieu Fee Payment Option

For the hypothetical 100 unit townhome project, the developer would be entitled to use the in-lieu fee option. Based on the in-lieu fee schedule being recommended by KMA, the project would generate the following in-lieu fee payment obligation:

- 1. The hypothetical project is a 100 unit market rate townhome project.
- 2. The total saleable area of the project is 148,000 square feet.
- 3. The in-lieu fee for projects that include 30 or more units is \$9.30 per square foot of saleable area.
- 4. The resulting total in-lieu fee is \$1.38 million, which equates to approximately \$13,800 per unit in the 100 unit market rate ownership housing project.

### APARTMENT PROJECT: ON-SITE PRODUCTION AND IN-LIEU FEE OPTIONS

The development scope used in the apartment project hypothetical are:

- 1. The 100 unit project is developed on a 1.43 acre-site. This represents a density of 70 units per acre.
- 2. The unit mix is presented in the following table:

Unit Mix Hypothetical Apartment Project		
Number of Bedrooms	Number of Units	Square Feet Per Unit
Studio	15	600
1	45	750
2	40	1,100
Total	100	86,750

### On-Site Production of Affordable Apartment Units

A developer may select the on-site production option by right. The requirements associated with this alternative are:

1. At an 11% Inclusionary Housing requirement, 11 Inclusionary Units must be provided.
2. The income and affordability restrictions are set at the moderate income level.
3. To match the distribution of the bedroom types included in the market rate apartment project, the Inclusionary Units must be provided in the following mix:

Inclusionary Unit Mix Hypothetical Apartment Project		
Number of Bedrooms	Number of Units	Percentage of Total
Studio	2 <sup>4</sup>	15%
1	5	45%
2	4 <sup>5</sup>	40%
Total	11	100%

<sup>4</sup> The actual cap is 1.65 units. This was mathematically rounded up to two units.

<sup>5</sup> The actual minimum is 4.4 units. This was mathematically rounded down to four units.

4. The Inclusionary Units must be dispersed throughout the market rate project and developed concurrently with the market rate project.

### In-Lieu Fee Payment Option

Under the recommended structure, a 100 unit apartment project would not be allowed to pay a fee to fulfill the Inclusionary Housing obligation. However, if the developer can prove a financial hardship, the City Council has the discretion to approve the payment of an in lieu fee.

Based on the in-lieu fee schedule being recommended by KMA, the hypothetical apartment project would generate the following in-lieu fee payment obligation:

1. The total leasable area of the 100 unit market rate project is 86,750 square feet.
2. The in-lieu fee for projects that include 30 or more units is \$9.20 per square foot of leasable area.
3. The resulting total in-lieu fee is \$798,100, which equates to \$7,981 per unit in the market rate project.

### OTHER INCLUSIONARY HOUSING OBLIGATION FULFILLMENT OPTIONS

Each of the three remaining Inclusionary Housing obligation fulfillment options applies to both ownership housing projects and apartment projects. These fulfillment options include the following common assumptions:

1. The hypothetical market rate project that triggered the Inclusionary Housing requirement includes 100 units; and
2. The Inclusionary Housing obligation must be fulfilled with apartment units.

### Off-Site Production Option

The City has approval rights over the following:

1. The development site proposed to be used; and

2. The affordable housing developer proposed to undertake the development of the Inclusionary Units.

The off-site production option includes the following additional requirements:

1. The Inclusionary Housing requirement is set at 15% of the units included in the market rate project. At 100 units, the market rate project generates a requirement for 15 Inclusionary Units.
2. The income and affordability requirements are set at the low income level.
3. The Inclusionary Units are not required to adhere to the bedroom mix included in the market rate project. The standards that are imposed on the Inclusionary Units in the off-site development option are:
  - a. No more than 15% of the units (two units) can be studio units;<sup>6</sup>
  - b. At least 40% of the units (six units) must include two or more bedrooms; and
  - c. The remaining seven units must include one or more bedrooms.
4. The Inclusionary Housing obligation must be fulfilled prior to or concurrently with the first phase of the market rate development.

### Land Dedication Option

The use of the land dedication option should be subject to City Council approval. Proposals must meet all the following requirements in order to be presented to the City Council for consideration.

1. The Inclusionary Housing obligation is set at 15% of the units being constructed in the market rate project, which equates to 15 units for the hypothetical 100 unit project.
2. The income and affordability standard is set at the very low income level.

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<sup>6</sup> The actual cap is 2.25 units. This was mathematically rounded down to two units.

3. At an assumed allowable density of 70 units per acre, the dedicated site must include at least 1.43 acres of land area.
4. The unit mix requirements are:
  - a. No more than 15% of the units (two units) can be studio units;<sup>7</sup>
  - b. At least 40% of the units (six units) must include two or more bedrooms; and
  - c. The remaining seven units must include one or more bedrooms.
5. The developer must submit a conceptual plan and a pro forma analysis to demonstrate that an apartment project that includes 15 very low income units will be feasible with no financial contribution from the City.

### Acquisition and Rehabilitation Option

The acquisition and rehabilitation option can only be exercised under very limited circumstances, and then only with City Council approval. Only projects that fulfill the following requirements will be presented to the City Council for consideration:

1. The Inclusionary Housing requirement is set at 20% of the units being constructed in the market rate project. To fulfill the affordable housing requirement for the 100 unit market rate project a developer would need to acquire and rehabilitate existing projects that include a total of at least 20 units.
2. The affordability standard is set at the very low income level.
3. The rehabilitation scope must have a value equal to at least 25% of the after rehabilitation value of the units, which includes the value of the land.<sup>8</sup>

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<sup>7</sup> The actual cap is 2.25 units. This was mathematically rounded down to two units.

<sup>8</sup> H&SC Section 33413 (2) (a) (iv).

## SUMMARY

The preceding memorandum presented KMA's policy recommendations related to creating an Inclusionary Housing program. The recommended affordable housing requirements are based on the results of the accompanying Financial Evaluation, and on an evaluation of the array of fulfillment options that can be made available to the developers of market rate residential projects.

It should be City's goal to create an Inclusionary Housing program that balances the interests of property owners and developers against the public benefits associated with increasing the inventory of affordable housing units in the community. To that end, KMA identified supportable Inclusionary Housing production requirements and provided a mix of alternative methods for fulfilling the requirements.